

CER Consultation Paper CER/14/455 Future of Gas Entry Tariff Regime

Vayu welcomes the opportunity to comment on the Commission for Energy Regulation's ("CER") consultation paper, which examines the initial modelling of the entry tariff regime into the future – CER/14/455 and other related material. We note that a change in the regime has been discussed at numerous meetings since the publication of the CER's decision paper (CER/12/087) on the entry tariff regime and that developments at an EU level have also prompted a radical overhaul of the regime.

Whilst we do not have a strong preference for one proposed methodology over another, we believe that forward looking concepts provide a better measure of an appropriate entry tariff.

We are open to discussing our views in more detail and our comments on specific questions follow:

Question 1 - Inputs

Bearing in mind that the CER is not at this time proposing one methodology as best suited to the Irish market; do stakeholders view the modelling of the three proposed methodologies as suitable? Please provide details where possible.

In our view modelling tariffs under the 3 methodologies is correct and that we agree in principle that a forward looking approach to setting tariffs is a more appropriate basis. However, we do not agree with the assumptions made.

The proxy capacity demand (kWh/day) falls when comparing scenario 1 to the scenarios 2 to 4. No rational explanation has been provided to support this as we would expect to see capacity actually increase, as shippers book additional entry capacity at Moffat as a back up to potential outages at the other entry points. At a minimum, assuming there are no structural issues at any of the entry points, we would at least expect to see capacity remain constant across all scenarios.

Vayu does not agree with the modelling of the Matrix approach incorporating Long Run Average Incremental Cost (LRAIC). This model has the impact of smearing costs specific to individual entry points across all entry points. At the workshop it was continually reiterated that the tariffs will aid parties in deciding where to construct a new entry point as it will highlight efficient points to construct. Under the Matrix LRAIC approach, any efficiency is removed as users of the Corrib and Inch entry points subsidise work required at Moffat and Shannon. If this work is required, the cost should be borne by those entry points alone meaning they are not an efficient point of entry.

Furthermore, we believe that the CER has been a bit premature in publishing its possible options for primary costs allocation methodologies. In the ENTSOG draft network code paper

which deals with the harmonised transmission structures for gas, another methodology called “Asset Allocation Methodology” was published. The CER refers to this option in the paper, but has not considered if it is suited to the Irish market. Our preference is that the CER should at least evaluate the option and should it decide to reject the option as a possibility, it should state the reasons for doing so.

Question 2 - Inputs

*Do stakeholders view the four Scenarios outlined above as appropriate for modelling purposes?
Are there other scenarios with different active Entry points that should be considered?*

Vayu agree with the modelling the four different scenario's, but not the assumptions made with respect to Shannon LNG in particular. In GB, the average daily total flow of gas from LNG terminals equates to 242 GWh per day. If the 4 smaller LNG terminals are removed from these figures, and assume their contribution is minimal, the daily flow from the 4 major LNG terminals (Isle of Grain 1 & 2, Dragon and South Hook) only equates to an average volume of 50 GWh per day per facility, making scenario 4, or at least the assumed flows unlikely.

The global market for LNG is competitive; entities bid for LNG cargoes on a commercial basis, which means that Ireland must compete with the UK to secure these volumes. The cost of shipping between Ireland and the UK is negligible when the likely origination of the LNG from the Middle East is considered. The IBP price will need to be higher than the NBP price for it to make commercial sense to export to Ireland. For shippers, the price of LNG at IBP must be less than that of gas from the NBP. If this is acknowledged, it is difficult to see how Moffat will be significantly displaced for LNG.

Question 3 - Inputs

Bearing in mind that ACER guidance suggests a 50:50 split between Entry and Exit for recovering allowed revenues what are stakeholders' views on the split?

Applying a principle of one molecule in, one molecule out seems logical; however the ACER network code is very clear on the other primary principles of cost reflectivity, transparency, non-discrimination and tariff stability.

Ireland has an unusual position in the EU energy market; we are heavily reliant on a single source for our gas. Furthermore, the gas network on the island is much different to many other countries in Europe. With Ireland being less densely populated, a lot of network assets were required to build it between the more densely populated areas of the country.

The CER's decision to absorb the interconnectors into the onshore network would suggest it would be difficult to justify recovering 50% of the regulated revenue from entry tariffs without keeping them artificially inflated.

It would be useful to roll the tariff calculations forward over more than one year to analyse if the preferred option gives rise to tariff volatility e.g. Corrib production profile is expected to drop off after 3-4 years.

Question 4 - Inputs

What are stakeholders' views on the expected merit order? If alternatives are proposed please provide supporting evidence.

We agree with the proposed merit order as we should be promoting indigenous supply above other sources.

Question 5 - Inputs

What are stakeholders' views on the expected capacity bookings? If alternatives are proposed please provide supporting evidence.

In our view the figures for expected entry capacity bookings are optimistic given the propensity of firm daily capacity bookings being made in the past 12 months and the level of firm annual capacity bookings expected in the 2014/15 winter period. This is in light of the decision of the SEM committee to allow the cost of transmission capacity bookings to bid into gas fired generators commercial offers.

Furthermore, we believe that the level of Moffat capacity bookings at c. 42-45 GWh is questionable. If this figure is based on technical information such as minimum flow requirements it should be disclosed.

Vayu agree with the modelling the four different scenario's, but not the assumptions made with respect to Shannon LNG in particular. In GB, the average daily total flow of gas from LNG terminals equates to 242 GWh per day. If the 4 smaller LNG terminals are removed from these figures, and assume their contribution is minimal, the daily flow from the 4 major LNG terminals (Isle of Grain 1 & 2, Dragon and South Hook) only equates to an average volume of 50 GWh per day per facility, making scenario 4, or at least the assumed capacity booking unlikely.

Question 6 - Inputs

What are stakeholders' views on the application of expansion constants to the system?

We agree with the principle of using an expansion constant and the fact that costly additions to the network should be more expensive to use. However, there is no empirical evidence provided with respect to the value assigned to the onshore segment, nor has any information been provided to justify a multiple of 3 for the subsea segments.

We note that the expansion constant in the paper is a blended cost of past projects, and therefore is questionable why past costs are used for incremental costs for the Virtual Point Variant A or the Matrix approach, which are both forward looking.

Question 7 - CWDA

Do stakeholders view the application of a historical approach such as the CWDA as appropriate to Ireland? Please provide reasons as to why the approach is suitable, or not to Ireland.

In our view this methodology would fairly represent the actual costs of the building the network to date including all related costs. However, we do not believe that it is the most appropriate methodology for Ireland as it is based on historic costs. In our response to the CER's consultation paper "The Regulatory Treatment of the BGE Interconnectors" – CER/12/013 we recognised that there are merits in moving away from a tariff regime based on historical costs. Ireland's gas network is still relatively young by international standards and is growing at a faster rate than most other European countries and a forward looking costs concepts. This would also be in keeping with the proposed EU network code on transmission tariff structures.

Question 8 - CWDA

Do stakeholders propose any modifications to the CWDA approach? If so, please provide reasons why.

The paper notes that expected capacity bookings have been used to calculate tariffs. No basis has been provided for the use of expected bookings. We believe that the calculations should be based on recent historic bookings, not a 3 or 5 year average as entry capacity bookings have radically changed in the last 12 – 18 months following the decision of the SEM committee to allow bidding in of capacity costs into generators commercial offers.

Question 9 - CWDA

Does the CWDA methodology promote tariffs that are stable and predictable? Please provide details.

Stability and predictability are primary components of the final tariff regime. Based on a one year review of the tariffs under each scenario it would appear that there is minimal fluctuation in the cost of each entry point once a new entry point is live on the system. However, we would also like to see the results from the scenarios if each was rolled forward as in a 5 year price control period to analyse if the tariffs were stable and predictable in each of these years.

Question 10 - CWDA

The CWDA methodology has the ability to incorporate either technical capacity or booked capacity. What are stakeholders' views on the merits of using either?

If it had to be a clear choice and a combination of both could not be used, booked capacity would provide a better basis for calculating the cost. Using technical capacity would have the impact of reducing some tariffs; however that entry point may not be used efficiently, with minimal capacity bookings in place. This would promote the use of Moffat above other entry points and would result in bookings elsewhere decreasing.

Question 11 - Virtual Point

Do stakeholders view the application of a forward looking Virtual Point based approach as appropriate to Ireland? Please provide reasons as to why the approach is suitable, or not to Ireland.

In our view a model that uses actual points on the system rather than a mathematically calculated virtual point would be more appropriate. The transportation system is a physical system and using actual nodes and points should produce more stable and predictable tariffs.

Question 12 - Virtual Point

Do stakeholders propose any modifications to the VP approach? If so, please provide reasons why.

No; however, we would like additional information on why the expansion constants can differ depending on the segment in the Irish system and also what different multiples are applied to the “dry” constant by virtue of either node 1 or node 2 being the dominant node.

Question 13 - Virtual Point

Does the Virtual Point Variant A promote tariffs that are stable and predictable? Please provide details.

No, the models produce tariffs that vary considerably in each scenario especially when compared with the other two possible methodologies.

Question 14 - Matrix

The draft Network Code on Tariffs indicates that NRAs have discretion as to the level of the negative expansion constant. Considering that the Matrix must take account of the flow direction what are stakeholder's views on the value of negative expansion that should be applied?

Applying a principle of non-discrimination, it would appear logical that a negative expansion constant should be used where the marginal unit is against the flow and also that the value of the negative expansion should be equal to the positive expansion constant i.e. 100%.

Question 15 - Matrix

Do stakeholders view the application of the Matrix approach as appropriate to Ireland? Please provide reasons as to why the approach is suitable, or not to Ireland.

Yes, in our view it promotes more efficient and indigenous sources of gas. It also takes into account the overall system and how far each entry point is from the exit zones reflecting true cost reflective shipping costs.

Question 16 - Matrix

Do stakeholders propose any modifications to the Matrix approach? If so please provide reasons why.

No.

Question 17 - Matrix

Does the Matrix approach promote tariffs that are stable and predictable? Please provide details.

Yes, the changes from scenario to scenario causes minimal fluctuation in the cost of each entry point once a new entry point is live on the system. The tariffs under the matrix approach also appear to be cost reflective and non-discriminatory.

Question 18 - Matrix

What are stakeholders' views on applying project based costs to the Matrix approach?

Vayu do not agree with the modelling of the Matrix incorporating the LRAIC. This model has the impact of smearing costs specific to individual entry points across all entry points. At the workshop it was continually reiterated that the tariffs will aid parties in deciding where to construct a new entry point as it will highlight efficient points to construct.

Under the Matrix LRAIC approach any efficiency is removed as users of the Corrib and Inch entry points subsidise work required at Moffat and Shannon. If this work is required, the cost should be borne by those entry points alone meaning they are not an efficient point of entry and also would not appear to be applying a cost-reflective tariff at the relevant entry points.

Question 19 - Matrix

Do stakeholders' view the application of a Matrix approach using Expansion Constants or a Matrix approach using project based costs as more suitable to Ireland?

Vayu believe that the application of a matrix approach using expansion constants would be more appropriate for Ireland. The use of the more expensive segments of the network should result in tariffs that are more expensive and conversely using cheaper segments to construct onshore entry points should result in lower tariffs.

Question 20 - Tariff Stability & Predictability

How can stability and predictability in tariffs be evaluated and quantified?

Stress testing at various levels of booked capacity rather than straightforward scenarios should be taken into account to assess tariff stability and predictability. Also the CER should be working closely with the operators of Corrib and Shannon to model the likely run rate of each. Corrib is expected to run at full production for a short number of years before production dramatically falls. Once this happens booked capacity will also fall. These scenarios should be modelled to take account of the highly probable scenario taking place and with capacity bookings shifting back to Moffat.

We also believe that a scenario which more closely resembles the capacity expected booked at Shannon should be modelled. This is in light of information that demonstrates the non-reliable erratic nature of LNG; one has only to review the delivery rate of LNG into the UK over the last 4 to 5 years. Events in other jurisdictions can impact the availability of LNG as was seen following by the Tsunami that struck Fukushima, Japan in 2011. This led to the majority of available LNG cargoes being directed to Japan as nuclear power stations were shut down.

Question 21 - Tariff Stability & Predictability

Apart from the publication of models behind tariffs what other factors do stakeholders view as necessary for tariff predictability and/or stability?

We believe the move by the CER to make the Price Control Review (“PCR”) models available should be continued in the future. This has aided stakeholders to gauge where tariffs were likely to be set over the course of the PCR.

Also, we believe that the formation of the tariff liaison group has been a positive step in stakeholder engagement. Furthermore, we believe that this group should continue to be a feature of the tariff regime and be re-convened at appropriate times if significant decisions are being considered to amend the regime in the future.

Question 22 - Storage

What are stakeholder’s views on the benefits that Storage can provide the transmission system?

Question 23 - General

Are there any other issues stakeholders would like to raise?