May 19th 2015

Mr. Colm Ó Gormáin
Commission for Energy Regulation
The Exchange
Belgard Square North
Dublin 24

Dear Colm,

Re: CER/15/057 Future of Gas Entry Tariff Regime

Bord Gáis Energy (BGE) welcomes this opportunity to respond to the Commission's (CER) Draft Decision on the future of the gas entry tariff regime. BGE recognises that a change from the current regime is necessary at this time in order to mitigate significant tariff increases for customers that would otherwise arise. We appreciate the CER's inclusive consultation approach with both industry and customers over the past number of months and years to find the optimal solution. However, despite the CER's Minded to Decision on the Matrix model, BGE is still concerned about the impact that this decision has on customer tariffs. The proposed Matrix model aims to reward "efficient new entry" by allocating an amount of money, which the CER has termed the "Diversity Premium", to the Producers of that new entry point. BGE's analysis estimates that this could increase customer tariffs by up to 2.4%. This impact is not evident in the CER's Draft Decision paper and a number of the assumptions made in the Paper's Impact Assessment require further analysis as we believe these assumptions have a higher customer impact should this Minded to Decision be implemented.

BGE believes that there is scope to reduce this impact on customers within the Matrix option currently preferred by the CER and we urge the CER to consider the proposals outlined below and provide a robust and transparent cost benefit analysis as part of its final Decision.

Arbitrary & unclear impact assessment analysis

While the impact assessment identifies the need for a regime change, the analysis carried out by the CER does not capture the true effect that the "Diversity Premium" will have on customer tariffs. The CER also makes arbitrary assumptions about the commercial contracts and customer portfolios held by suppliers. These assumptions, particularly around a supplier's flexibility to provide discounts, distorts the transparency of the CER's decision making process and does not accurately reflect the impact of the CER's decisions all other things remaining equal.

BGE conducted specific analysis on the impact of this decision on customers relative to the current cost allocation approach and tariffs. BGE estimates that the CER's Minded to Decision may have up to a 2.4% increase on residential customers and up to a 2% on SMEs, which will likely negate the falling wholesale costs currently being observed and remove any potential for any further price decreases being passed onto customers. The CER's Draft Decision Paper does not accurately represent this impact and uses arbitrary and some flawed assumptions to understate the effect of their decision. To the extent that commercial agreements or wholesale gas prices dampen the effect of the CER's decision, these factors are different for each supplier, are variable and whereby relevant to competition in the market, they should not be part of the regulatory impact assessment for this decision on how to allocate costs between entry points.

In the interests of transparency in the decision making process, BGE requests that the CER publish a focused assessment of the impact that this decision will have on customer tariffs and power generator costs (discussed below) and assess the merits of its decision on that basis alone. To the extent that the CER minimise the impact of the change on customers, they should only do that through the regulatory formula which they control and not by reference to market forces/ agreements which are variable and outside of the remit of the regulator. Recognising that the CER has worked closely with industry over the past number of months to find a solution which is in the interests of customers (both long term and short term), BGE believes there are further amendments to the Matrix option which could reduce the impact on customers further. These are discussed below.

Ability to further reduce customer impact

On the basis that the status quo would significantly increase customer costs, BGE accepts that the CER's Draft Decision to implement the Matrix model is the most suitable option for the Irish market at this time. Of all the options considered, it most appropriately achieves a balance between the criteria of equity, transparency and stability. However, BGE believes there are changes that could be made to this model in order to reduce the impact on customers further. Specifically, we believe that Opex and fuel costs should not be included in the Annuitisation Factor calculation and that the 90:10 capacity/ commodity split should be retained.

From a practical and equity perspective the proposal to include Opex and fuel costs in the Annuitisation Factor is unfair on customers in BGE's view as it essentially levies higher costs on customers related to a commodity cost (i.e. shrinkage) which is typically treated as a pass through cost only. From a theoretical perspective, given that the intent of the expansion constant – and the Annuitisation Factor by association – is to provide an efficient signal for investment in entry by reference to the cost of providing an extra unit of capacity, BGE does not believe that the price of operating that pipe and associated compressors and particularly the fuel costs related to the physical operation of those compressors, are relevant for the purposes of providing efficient entry signals for investors. The cost of the relevant capital investment is what is relevant for the purposes of providing LRMC entry signals.

To be clear, BGE is not suggesting that customers are paying twice towards shrinkage costs but customers at Moffat would be paying a higher price at Moffat by reference to the cost of shrinkage and its inclusion to the expansion constant.

A change to a 100% capacity charge would increase charges for low consuming customers who can currently manage a proportion of their costs through their commodity related charges. Therefore, in the interest of further reducing the customer impact, BGE believes that the 90:10 capacity/ commodity split should be retained.

Other items for consultation

Capacity/ Commodity Split
BGE does not believe that it is appropriate to move to a 100% capacity charge at this time. The change will have a disproportionate impact on low volume customers and will add unrecoverable costs for gas fired generators operating in the Single Electricity Market.

The analysis on the impact of the decision on gas fired generation needs further consideration. In the current SEM, generators bid in the cost of commodity to the market which is recoverable through the marginal price. Commodity throughput costs can currently be bid into the market as a SRMC while sunk capacity costs are typically not bid in by baseload or mid merit units given the market rules as provided for in the Bidding Code of Practice. As discussed bilaterally, the CER's proposed decision to move to a 100% capacity tariff will both increase costs for generators and remove their ability to recover those costs through the SEM. On that basis, and in the interests of supporting the sustainability of gas fired generators, BGE therefore suggests that the 90:10 capacity/commodity split is retained until the rules of the ISEM have been determined.

Bellanaboy Entry Tariff
BGE notes the CER's consultation on the recovery of the Linkline costs and therefore the entry tariff at Bellanaboy however we would like to take this opportunity to stress to the CER the importance of providing only one tariff for gas entering the Irish system from Corrib. In the interests of shippers using the Entry point, it is important that the arrangements are simple both operationally and administratively. BGE believes that this is best achieved through a single Entry tariff for the Bellanaboy Entry point which would incorporate both the costs to be recovered for the Linkline and costs for GNI's network. This is the same principle used for other similarly funded pipelines on the network with third party access.

Entry/ Exit Split
BGE maintains its position from the initial modelling consultation in supporting the Entry/ Exit split shift of revenue recoveries to 50:50.

Negative Expansion Constant
BGE believes that a multiplier for contra-flow segments of pipeline should not be implemented in the design of the Entry tariff regime. Doing so would require additional ex-ante forecasting which would result in greater uncertainty in revenue recoveries and therefore greater volatility in correction factors from year to year.

Treatment of Storage
In the interest of security of supply, BGE supports the treatment of Storage and allowing 100% Entry and Exit discounts. We believe storage is a valuable service on the island not just in terms of physical security of supply but also in managing pricing certainty for customers.

Summary and Conclusions

In summary, BGE accepts the CER's proposal to introduce a Matrix approach as the best alternative to the allocation of gas entry costs on the Irish system at this time. Notwithstanding that, BGE is concerned about the impact of the CER's Draft Decision on customers and the analysis undertaken by the CER supporting this position. BGE urges the CER to consider changes to the Matrix approach to minimise the magnitude of the tariff increase arising as a result of this change and to conduct a full and transparent impact assessment of its Decision. This Decision – its rationale and impact – must be clearly communicated such that all elements impacting customer tariffs can be reasonably assessed and understood.

I hope you find the above comments helpful and should you have any queries, please do not hesitate to contact me.

Sincere regards,

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Brian Larkin
Regulatory Affairs - Commercial
Bord Gáis Energy

{By email}