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Dear Sarah,

**Re- Informal Consultation for Changes to the Capacity Methodology Statements
issued 18th December 2014.**

Thank you for the opportunity to participate in this consultation. Here is the Eni UK Ltd (eni) response.

Executive Summary

1. Under the Licence change at Bacton the Interconnectors and their users are being granted their own dedicated ASEP, with Obligated Capacity sized precisely to match technical capacities, without a price signal or user commitment being given. Market economics have played no part.
2. In future, for unsold entry capacity to be moved away from the dedicated IP ASEP to another ASEP sufficient economic demand and commitment must be identified before substitution can be considered and potentially enacted.
3. Under CAM the long term entry capacity products offered at the IP ASEP differ from those offered at the UKCS ASEP, which makes a competitive price comparison impossible and serves to undermine the robustness of any substitution methodology.
4. The current informal consultation drafting of the Capacity Methodology Statements does not consistently allow substitution from the IP ASEP to be considered in the PARCA process, being dependent on the timing of when a PARCA is raised relative to the Annual Yearly auction process.



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5. Having gained ASEP rights over entry capacity without economic commitment, the Interconnectors and their users can prevent substitution by buying a low cost Retainer to secure an option over forward capacity.
6. Any proposed substitution is open to veto by Ofgem.
7. Thus, in combination, the economic allocation of entry capacity has been significantly disturbed by the Bacton split, both on the initial allocation of Obligated Capacity but also on an enduring basis through any substitution methodology. In recognition of this and depending on whether substitution of entry capacity away from the IP ASEP is to be properly allowed or prohibited, alternative UNC Modifications 501C or 501A respectively are the appropriate choices to restore value and competitive balance for current holders of long term capacity at the Bacton ASEP.

Response detail

eni has the following comments on the methodology as it applies to the two new Bacton ASEPs after implementation of UNC Modifications 0500 and 0501/0501A/0501B/0501C.

If entry capacity at the IP ASEP is not to be formally protected from substitution then significant issues remain.

- 1) **Entry Capacity products are different at the two Bacton ASEPs and so frustrate comparable economic signals for substitution consideration.** For substitution analysis to be properly undertaken it is difficult to see how an economic comparison can be made between bids for future capacity at the UKCS ASEP with those at the IP ASEP when the products offered in competing auctions or through the PARCA process are necessarily different. QSEC Auctions and PARCA at the UKCS ASEP allow bids for quarterly capacity over many future years whilst CAM compliant IP Auctions can only be for annual capacity for years beyond the year ahead and potentially are only for a bundled product. For example, if a PARCA application is made at the UKCS ASEP for winter quarters over a number of years ahead to support a potential storage project



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what price would then be appropriate in the IP Annual Auction to hold onto the annual strip of capacity whilst ensuring fair competition for entry capacity?

- 2) **A further protection from substitution for the IP ASEP?** Notwithstanding the above, Para 25 (v6.1) of The Entry Capacity Substitution Methodology Statement states that *'For the avoidance of doubt in the event that an incremental signal is received and substitution analysis is undertaken prior to the completion of the Annual Yearly auction for an IP ASEP, capacity at that IP ASEP will not be considered as available for substitution'*. This lack of certainty on timing and its effect on whether capacity is considered as available for substitution or not is unacceptable as a methodology. Increased clarity is required to ensure substitution is allowed from IP ASEPs or it is not. If it is to be allowed then the PARCA process will need to be consistent with the Annual Yearly auction process at the IP ASEP. This necessarily results in the PARCA substitution analysis becoming an annual process timed to coincide with the annual QSECs and Annual Yearly auctions, thereby making redundant the requirement to run ad-hoc QSECs.

Further considerations

- 3) Under the Licence change to split the Bacton ASEP, the Interconnector assets and their users have been assigned their own 'asset specific' ASEP, precisely sized to match the technical capacities of the Interconnectors without any price signal or revenue commitment being received. This is at odds with the User Commitment Framework and gives the Interconnector assets and their users little or no incentive to book long term entry capacity as the only threat to their precise capacity needs is the possibility of the thresholds for substitution being overcome in the medium term. The position is further strengthened through an ability to protect capacity from substitution through low cost capacity retention at the IP ASEP and the comfort that were the threat of a PARCA at a competing ASEP to be confirmed then there would be the opportunity to respond and secure capacity at the next auction before the threatened substitution could be effected. This fundamental change to the competitive



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landscape for entry capacity at Bacton undermines the value of the current long term entry product at the Bacton ASEP and prompted eni to raise alternative UNC Modification 0501C with the aim of delivering a balanced solution in response.

- 4) The competitive imbalance is further weighted towards the Interconnectors and their users as 20% of the new IP ASEP's Obligated Capacity is withheld from the potential substitutable capacity for offer in shorter term auctions under CAM, whereas the equivalent protection is only 10% at the UKCS ASEP. This relative difference in competitive threat and availability will drive relative capacity value differences and result in price signals for long term capacity at the two ASEPS that are not simply comparable in any substitution analysis.
- 5) Even after National Grid analysis suggests that substitution is the efficient solution, Ofgem holds a veto right. Given the importance of the Interconnectors to the UK's Security of Supply Strategy it is conceivable that DECC and Ofgem may choose to safeguard Interconnector capacity. Actually a possible ad-hoc veto right for Ofgem is already provided for in NGG's Entry Capacity Substitution Methodology Statement Submitted to Authority in the event that the application of the substitution "*may reasonably put National Grid in breach of its obligations with respect to EU Regulations (in particular the obligation to offer bundled capacity at Interconnection Points as required by the Capacity Allocation Mechanisms*" (Paragraph 89 of ECS v5.3 and v6.1).
- 6) Exit capacity at the IP ASEP is protected from substitution and therefore it would seem equitable that entry capacity should be treated similarly. In a country which is becoming ever more reliant on gas imports it does not seem appropriate nor sensible to construct a methodology which favours import capacity potential reduction in relation to export capacity. A reduced potential to import gas relative to export can only raise consumer prices above those levels they otherwise would be.



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We would encourage National Grid and Ofgem, together with industry, to debate these issues. A potential simple solution, justifiable from a security of supply and price standpoint, and for equal treatment with the Exit regime and for the proposed Transfer and Trade methodology, which explicitly prohibits capacity transfers to or from the IP ASEP, would be to stipulate that entry capacity cannot be substituted away from the IP ASEP. The challenges raised in this response are then resolved, the advantaged and secured positions of the Interconnectors, promoted by European CAM, are positively confirmed and the appropriate modification to effect the Bacton split becomes 0501A rather than 0501C, allowing industry to move forward simply, in full recognition of the new world for entry capacity at Bacton.

Yours sincerely,

Simon Witter

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