Final Modification Report

Code Modification A068:

'Balancing: EU Network Code Implementation'

31 July 2015

Issued to CER for Approval

Issued to Industry for Information

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Table No. 1: Supporting Information

Date	Reference
7 April 2015	Approved Interim Measures Report
20 April 2015	Modification Proposal Form
22 June 2015	Business Rules V1.0
22 June 2015	Initial Modification Report
31 July 2015	Business Rules V2.0

Table No. 2: Summary of timeline to date

ITEM	DATE
Code Modification A063 Consultations	Aug 2014 – Jan 2015
Interim Measures Consultation	Jan 2015 - April 2015
Modification Proposal Form Issued	20 April 2015
Code Modification Forum Meetings	22 April & 3 June 2015
Business Rules Consultation	22 June - 6 July 2015
Code Modification Forum Meeting	22 July 2015

1. Introduction

1.1. Background

Code Modification proposal A068 '*Balancing: EU Network Code Implementation*' is the Transporter's proposal regarding the implementation of the 'Balancing Network Code' (Regulation 312/2014) in the Irish gas market. The Regulation requires EU member states to implement the Regulation by 1 October 2015.

The proposed modification intends to incorporate those aspects of Regulation EU 312/2014 (Balancing Network Code) which relate to operational balancing (Chapter 3 of the Regulation), daily imbalance charges (Chapter 5 of the Regulation), and neutrality arrangements (disbursements account) (Chapter 7 of the Regulation). It also engages Chapter 10 of the Regulation 'Interim Measures'.

The items included in the scope of this modification A068 have been consulted on previously as part of Code Modification Proposal A063' Nominations, Imbalance Charges & Allocations: EU Network Code Implementation'. However, further to a review of the A063 business rules, Industry responses, and discussions with the CER, it was decided to amend the scope of the A063 business rules, such that those proposals relating directly to 'balancing' were removed. The other subject areas of modification A063, namely information provision, nominations, and allocations remained in the business rules, which were approved by the CER in March 2015.

Following the separation of balancing issues from the A063 modification process, the Transporter reviewed its initial proposals and proposed utilizing the provisions of Chapter 10 'Interim Measures' of Regulation 312/2014. Interim Measures allow for a gradual implementation of the Regulation over an interim period in circumstances where low levels of liquidity exist in a Member State's short term wholesale gas market. The Transporter published its 'Interim Measures Report' for consultation in March 2015, with CER approval of the Interim Measures Report following in April 2015. The purpose of the interim measures are to stimulate liquidity in the market through the amendment of tolerances and daily imbalance cash-out prices as the first step towards developing a potentially liquid short-term market over a longer period.

Code Modification A068 therefore sets out the proposals (based on the Interim Measures Report) which are to be implemented in the Gaslink Code of Operations for 1 October 2015.

1.2. Purpose of document

This Final Modification Report provides a summary of Industry responses to date, an indication of system impacts, and next steps towards implementation of this modification. The purpose of the document is to inform the CER regarding its decision as to whether it directs the Transporter to progress with the development of Code legal drafting on the basis of the Business Rules v1.0. Business Rules v1.0 represents the Transporter's final proposal, amended as appropriate in response to Industry consultation and discussions with the CER. In light of comments received we propose to make minor changes to the derivation of the Second Tier Imbalance Price and to introduce an entry tolerance at the Bellanaboy Entry Point.

The report is issued to Industry for information. There is no formal consultation period in respect of the Final Modification Report.

2. Summary of Consultation Responses

A summary of the written responses received to the consultation is provided in table no. 3:

Written Consultations	DATE
Consultation Period • Business Rules v1.0	22 June – 6 July 2015
5 Respondents: • Kinsale Energy • Tynagh • SSE • Vayu • Vermillion	

Table No. 3 Summary of Industry responses

Note that the summary of Industry comments which follows is not intended to be an exhaustive representation of comments received, but rather highlights those issues which appeared most prominent. For a complete view of all comments received, please see the individual response documents submitted by Shippers.

A range of comments were raised in response to the Business Rules v1.0. These can be broadly split into three areas:

- Comments on the specific proposals contained within the Business Rules;
- Requests for clarification on related issues within the Code of Operations and the balancing regime; and
- Observations on the general operation of the regime.

In this document we focus on the comments that were raised on the specifics of the Business Rules. Other items that were raised have been noted and clarification will be provided via the Code Mod Forum. The specific comments raised are summarised as follows:

- One shipper identified that the proposed amendment of the first tier imbalance price derivation would have a knock-on impact to the second tier imbalance price resulting in a wider spread between the marginal cashout prices.
- A respondent noted that the Bellanaboy Entry Point was not included within the revised definition of Shipper Portfolio Tolerance and requested that it should be added with a tolerance of 1.5%.
- A respondent commented on whether the obligation to balance contained within the Code of Operations should continue to be relevant in light of the commercial incentives that are contained within the Balancing Code.
- There were several comments regarding possible future changes to tolerances and second tier imbalance price derivations.

- There were a number of comments raised regarding the difficulties faced by power generators in responding to dispatch notifications received late in the Gas Day. Some shippers are seeking relief from imbalance and scheduling charges between 02:00am and 05:00am as a result of this.
- There were a number of requests for further information on the proposed changes to neutrality arrangements and the disbursements account.

The following table addresses the specific comments and the transporter response.

Shipper comment:
"Under the new regime, the First Tier Imbalance Price will be more punitive than present (currently UK SAP). Although the proposal in the modification is that the Second Tier Imbalance Price remains the same, it will also become more punitive because it is calculated as a compound of the First Tier Price. This compounding has not been adequately justified in the consultation paper. Shippers and suppliers will face significant increases in imbalance costs with a greater exposure to second tier imbalance given decreases in Shipper Portfolio Tolerance."
Transporter Response:
The intention of the proposal was not to introduce a greater spread between the Second Tier Imbalance buy and sell prices. We propose to amend the drafting contained within the Business Rules so that the Second Tier Imbalance Price is a function of the Euro equivalent of System Average Price which will maintain the current level of Second Tier Imbalance Price. The definition of Second Tier Imbalance Price will therefore be as follows: **1.1** For the purposes of calculating a Shipper's Daily Imbalance Charge, the Second Tier Imbalance Price shall be: (a) Where the Final Daily Imbalance Charge is positive, the lower of: i) The Euro equivalent of the **System Average Price** multiplied by 0.95 less the Imbalance Gas Transportation Costs; or ii) The Euro equivalent of the System Marginal Sell Price published by National Grid for the Day less the Imbalance Gas Transportation Costs. (b) Where the Final Daily Imbalance Price is negative, the higher of: i) The Euro equivalent of the **System Average Price** multiplied by 1.05 plus the Imbalance Gas Transportation Costs; or ii) The Euro equivalent of the System Marginal Buy Price published by National Grid for the Day plus the Imbalance Gas Transportation Costs.

Shipper comment:

In 3.1: Bellanaboy should be added. As Bellanaboy is a domestic entry point (not an IP), we suppose the entry tolerance would be 1.5% (same as for Inch).

Transporter Response:

The Transporter proposes to amend the definition of the Shipper Portfolio Tolerance to include the Bellanaboy Entry Point. The revision to the Business Rules shall be as follows:

> The Entry Tolerance percentage that will be applied to a Shipper's Final Entry Allocations for a Day is as follows:
>
> | Entry Point | Entry Tolerance % |
> |---|---|
> | Moffat | 0 |
> | Inch | 1.5 |
> | Bellanaboy | 1.5 |
>
> The Shipper Portfolio Tolerance for each Shipper for each Day shall be calculated in accordance with the following formula:
>
> SPT = ∑(3.5 % of LDM1All) + ∑(9 % of LDM2All) + ∑(19 % of LDM3All) + (30 %of DMAll) + (2.5 % of NDMAll) + (0% of MTAll[1]) + (1.5% of ITAll) + **<u>(1.5% of BTAll)</u> +** (1.5% of CSEPINCHAll) + ∑(3.5 % of I/COff1All) + ∑(9 % of I/COff2All) + ∑(19 % of I/COff3All)+ (0% of S/N IPAll[2])
>
> Where:
>
> BTAll = the Final Entry Allocation for a Shipper at the Bellanaboy Entry Point

The Business Rules have also been amended to clarify the application of the Entry Point Variance Tolerance at the Moffat Entry Point. On Days where the OBA at the Moffat Entry Point is not applicable then the Entry Point Variance Tolerance may apply in accordance with Code of Operations Section E 1.8. On Days where the OBA at the Moffat Entry Point does apply then the Entry Point Variance Tolerance shall not apply.

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1 On a Day where the OBA is not in effect at the Moffat Interconnection Point then the percentage used for the calculation of the Entry Tolerance at the Moffat Entry Point shall be 1.5%.

2 On a Day where the OBA is not in effect at the South/North Interconnection Point, then the percentage used for the calculation of the Exit Tolerance at the S/N IP shall be 1.5%.

Shipper comment:
….. we believe that the reduction in the tolerance levels of c. 25% across all sectors has been random at best. Much more analysis should have been presented in relation to the appropriate level of tolerance for each individual sector. ……shippers to Daily Metered (DM) sites do not have access to the real time consumption data and therefore have little or no control over what their portfolio of sites is consuming on any given day. We believe that dropping the tolerance level for this sector to 30% is disproportionate and firmly believe that the current tolerance levels for a shipper with an aggregate DM portfolio should be retained at 40%.
Transporter Response:
The Transporter carried out detailed analysis of tolerance reductions on an aggregate and shipper specific basis. This information has not been presented to the industry as it would be difficult to maintain confidentiality regarding specific shipper imbalance positions. Our analysis found that reductions in the region of 25% would not disadvantage any particular shipper or a category of shipper unduly. Whilst this would sharpen the incentives upon shippers to balance, this would not expose them to significantly increased risk of Second Tier Imbalance cashout. We would also highlight that the continued provision of After the Day Trades, allows shippers the option to trade out any imbalances after the end of the Gas Day when the Initial Imbalance position is known. The Balancing Code requires that tolerances are removed completely by the end of the interim period and we have proposed to do this on a gradual basis – making reductions each year. Maintaining the DM tolerance level at 40% would be counter to this and would not be compliant with the Balancing Code Interim Measures that have been approved by the CER. Taking this into account we do not propose to change the tolerance reductions set out in the Business Rules.

Shipper comment:
Article 50.4 (Tolerance) [of the Balancing Code] deals with the calculation of the maximum tolerance that should be bought or sold. It also crucially adds that this tolerance should be priced at a weighted average price. Any amounts in excess of the tolerance should be at a marginal sell or buy price. Applying a differential price to this 1st tier imbalance contravenes this Article and therefore the proposed structure should not be approved.
Transporter Response:
Art 50.4 of the Balancing Code states: *"tolerance level shall be the maximum quantity of gas to be bought or sold by each network user at a weighted average price. If there is a remaining quantity of gas that constitutes each network user's daily imbalance quantity which exceeds the tolerance level, it shall be bought or sold at marginal sell price or marginal buy price".* However, there is also the provision in the Balancing Code, Article 45.2 that states: *"The resort to an interim measure is without prejudice to the implementation of any other interim measure(s) as an alternative or additionally, provided that such measures aim at promoting competition and liquidity of the short term wholesale gas market and are consistent with the general principles set out in this Regulation."* During the negotiation of the Balancing Code, this flexibility was accepted by TSOs, ACER and stakeholders as it was foreseen that there might be helpful approaches that were not articulated in the Interim Measures section of the code. The proposed First Tier cashout differential within tolerance is a helpful transitional step that allows tolerances to continue for an interim period but with an appropriate and fair tightening of the cash-out incentive aimed to encourage the trading out of imbalance positions. It is certainly within the general principles of the Balancing Code to encourage and facilitate short term liquidity. Taking this into account, we do not propose any changes to the derivation of First Tier Imbalance prices within the Business Rules.

Shipper comment:
"General comment on balancing with reference to last Code Mod meeting, CER was adamant that while the obligation to ZIP (match nominations within an hour) was to be removed Shippers still had an obligation to be balanced. We don't believe there is an obligation to balance on a day, however the shipper will face the financial consequences of been out of balance. From this background there are now incentives (first tier imbalance prices) introduced to be in balance."
Transporter Response:
The Code of Operations Section E 1.1.1 states that ***"****Each Shipper shall use reasonable endeavours to ensure that, in respect of each Day, its Initial Inputs and Final Inputs are equal to its Initial Outputs and Final Outputs respectively."* This is generally referred to as the 'obligation to balance'. The Balancing Code contains the following relevant provisions - Paragraph 5 states: *"Network Users are to **bear the responsibility of balancing** their inputs against their offtakes, with the balancing rules designed to promote a short term wholesale gas market, with trading platforms established to better facilitate gas trade between network users and the transmission system operator. The transmission system operators carry out any residual balancing ….".* In addition, Article 4 – Balancing System General Principles, paragraph 1 states: *"The network user **shall be responsible to balance** their balancing portfolios in order **to minimise the need** for transmission system operators to undertake balancing actions as set out under this Regulation".* The Transporter's interpretation of these requirements is that the 'obligation' on shippers to balance on each Gas Day remains valid. This is clear in the Balancing Code. The transporter's role is reduced to one of a residual balancer. The removal of ZIP does not remove the obligation to balance, but does remove the requirement for each shipper to match its renomination within an hour. ZIP was initially introduced into the Code of Operations in order to ensure that shippers did not significantly change their balance position within-day for reasons of system security. Whilst the shipper has to balance over the Gas Day as a whole, it is not required to ensure that its nominations and/or renominations match exactly at every point throughout the Gas Day. This creates greater opportunities for the shipper to balance its inputs and offtakes at a trading point, in this case the IBP. This will encourage short-term trading and liquidity at the IBP – a key goal of the Balancing Code.

Shipper comment:
In relation to 2.3, Tynagh would like to reiterate it is unfair that imbalance charges may be incurred from 02:00-05:00 when a generator may be instructed to change its plant running, but is unable to renominate its gas position. Tynagh asks that the calculation of First and Second Tier Imbalance Quantities only considers the period of 05:00-02:00 of a Gas Day In relation to 5.3 and 5.4, Tynagh asks that the calculation of the Entry and Exit Scheduling Charge Quantities only considers the period of 05:00-02:00 of a Gas Day.
Transporter Response:
This issue has been recognised by the transporter and CER. The CER is currently undertaking a review of this issue including its magnitude and will report to the industry as soon as is practicable. The continued facilitation of After-the-Day Trades should help shippers to mitigate this issue.

Shipper comment:
SSE would suggest that if Shipper Portfolio Tolerances are to be reduced, then the reduction should not be set to zero but to no less than can be effectively measured taking account tolerances at meter installations. Shippers should be exposed to the manageable risk, but not the residual error at GNI meters. Given the reductions in Shipper Portfolio Tolerance we would like to highlight the importance of the accuracy and reliability of GNI metering (imbalance uses allocations not nominations) and NDM forecast data. Accuracy and reliability of metering is not something that shippers can either manage or improve – the balancing changes outlined in the modification should not remove the incentive for GNI to improve both. By entirely shifting this exposure to shippers, GNI lose one economic signal that should otherwise inform their performance.
Transporter Response:
The Interim Measures propose the gradual reduction of tolerances to zero by 2019 at the latest. The transporter is required to publish an annual Interim Measures Report that both assesses the performance of the interim measures and proposes future changes. Further reductions to the tolerance level shall be considered in future Interim Measures Reports and further reductions will be justified and proposed via a subsequent Modification Proposal. Under the Balancing Code provisions, the transporter will be required to publish a report on NDM forecasting accuracy at least every two years.

Shipper comment:
Section 4.4(b) states that the costs of balancing gas will be cashed out on a monthly basis. Will the annual reconciliation as outlined in Part E clause 1.4.16 to 1.4.19 still occur? It would be helpful to explain what is changing under section 4.4(b) and why the need to change.
Transporter Response:
The Balancing Code addresses Neutrality Arrangements in Chapter VII and is based on the assumption that settlement of balancing and imbalance charges is carried out on a monthly basis. The current arrangement within the Code of Operations contains an annual settlement of the Disbursements Account and therefore requires amendment. The Business Rules V2.0 have been amended to provide clarification of the future operation of the Disbursements Account from October 2016. Where receipts into the Disbursements Account are less than the payments from it then there will be a shortfall. This shortfall will be recovered by way of a neutrality charge to shippers based on their throughput in that month. However if the receipts into the Disbursements Account are greater than the payments from it then there will be an excess. This excess will be returned to shippers according to their throughput in that month. The neutrality charge could therefore either be positive (charge to shippers) or negative (credit to shippers) depending on whether there is a net shortfall or excess respectively. e.g. Monthly receipts into the Disbursements Account = 80 Monthly payment from the Disbursements Account = 100 Neutrality Charge = 100 – 80 = 20 20 is charged to Shippers pro rata to their throughput in the month Monthly receipts into the Disbursements Account = 100 Monthly payment from the Disbursements Account = 80 Neutrality Charge = 80 – 100 = -20 20 is returned to Shippers pro rata to their throughput in the month The systems changes required to implement the revised neutrality arrangements are significant and the transporter therefore proposes to schedule implementation of the monthly settlement for October 2016.

3. Estimated System Impacts & Costs

The amendments required to the Transporter's IT System (GTMS) in respect of the Daily Imbalance Cash-out Price, Shipper Portfolio Tolerance and Trade Notifications / IBP Nominations are relatively minor in nature and can be implemented with minimal effect on other functionality. The Transporter proposes that of these amendments be implemented on 1 October 2015.

However, in the case of the 'neutrality arrangements' (in particular the proposals relating to the monthly 'cash-out' of the disbursements account). The proposals present substantial change in terms of the operation of the disbursements account and the associated calculations. Such extensive changes require detailed IT design & build work and robust testing to ensure that the transportation billing cycle is not compromised as a result of the modifications. Accordingly, the Transporter does not believe that it is feasible to implement the proposed changes by 1 October 2015 and therefore propose that the existing annual cash-out process be retained for gas year 2015/16, with the new proposals detailed in Sections 4.3 & 4.4 of A068 Business Rules implemented by 1 October 2016. Additional information publication requirements in relation to balancing charges and neutrality charges are nonetheless included in the business rules for implementation by October 2015.

Costs

As per Decision Paper CER/14/140 of 27 August 2014 ('Decision on BGN Allowed Revenues and Gas Transmission Tariffs for 2014/15'), the projected costs associated with the implementation of the European Network Codes namely, Capacity Allocation Mechanisms (CAM), Congestion Management procedures (CMP), Balancing (BAL), Interoperability & Data Exchange (INT&DE), and Tariffs (TAR)) over a four year period up to Gas Year 2016/17 is €6,961,632 of which €5,000,000 is IT capital expenditure to be spent between 2014/15 and 2015/16. It is estimated that approximately 120 functions on GTMS will require amendment and that a further 80 new functions will be developed.

Implementation Dates

The implementation date in respect of Regulation EU No. 984/2013 (Balancing Network Code) is 1 October 2015.

Changes as a result of this modification relating to cashout prices and tolerances will be implemented from 1 October 2015.

Changes related to neutrality arrangements will be implemented from 1 October 2016.