EFET Gas Committee
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Use-it-or-lose-it Principles

In relation to gas pipeline capacity, the term 'use-it-or-lose-it' (UIOLI) is sometimes applied to two very different situations; a medium to long-term firm service and a short-term interruptible service. This has caused some confusion, which this note aims to dispel by explaining the purpose of UIOLI and the principles under which EFET believes UILOI should operate.

The purpose of UIOLI

The primary aim is to ensure that pipeline (or other) capacity is used efficiently and that a barrier to the development of effective competition does not arise through restricted or inadequate access to unused capacity. In particular UIOLI aims to ensure that all capacity that could be available to market participants (Users) is indeed made available for use by those who need it.

Firm UIOLI

The firm product relates to medium or long-term contracted capacity that is unused by the capacity holder. This can obviously only apply in such regimes that allow long term capacity booking, or where there are legacy, long-term capacity bookings. In such instances the unutilised capacity is generally determined through a retroactive review of flow patterns, often on an annual or seasonal basis. The unutilised capacity is subsequently released to alternative Users for their future use.

This form of UIOLI might be necessary where the primary capacity allocation mechanism is non-market based, capacity has been contracted for periods in excess of one year, demand for capacity exceeds supply and/or secondary trading of firm capacity is limited.

In practice, with a well-designed short-term (interruptible) UIOLI service the incentives to over-book or withhold long-term capacity and the problems of implementing firm UIOLI can generally be avoided, or at least diminished.

EFET believes that the interruptible form of the UIOLI service is vital to deter capacity hoarding and to provide short-term and reasonably priced access to networks. In turn this will encourage secondary trading in both capacity and the gas commodity.

Interruptible UIOLI

This short-term service tends to be provided on a daily basis and effectively allows the use of unutilised firm capacity held by network Users.

The amount of UIOLI capacity to be made available to the market can be determined in a number of ways. Most commonly, it is calculated by the (fully independent) TSO with reference to the difference between Total Booked Capacity and Total Nominations by the holders (Users) of that capacity.

The point of reference for determining the location of the available capacity is dependent upon the form of the tariff structure i.e. for an entry-exit or nodal system, capacity would be provided at the designated points of entry/exit or nodes, for a point-to-point system capacity would be released along each specified route.

Where TSO's are unable accurately to specify the amount of capacity that may be released in accordance with the above principle, it could be appropriate to forecast capacity utilisation, or pre-determine a fixed quantity to be released. It might also be appropriate to seasonalise the relevant quantity.

The sanctity of the firm contract is maintained, permitting the firm holder the right to increase utilisation of its contracted capacity during the relevant period. Those Users who have purchased interruptible rights are aware that their flows maybe interrupted at any time.

The fact that the capacity offered by the TSO is interruptible also provides comfort to the TSO in releasing the maximum possible amount of capacity.

The allocation process, irrespective of the balancing period used by the TSO, must ensure that Users are not interrupted on a retrospective basis.

The payments for UIOLI need to be consistent with the objectives of UIOLI.

- The basis for a possible interruption must be clearly set out, as the user who buys the interruptible product will still have to pay for it even during a period when the capacity is interrupted. This affects the value placed on the UIOLI product by the buyer and also acts as an incentive to book firm capacity when this is available.
- The revenues for the UIOLI service are <u>not</u> paid to the User who has temporarily 'lost' their unused capacity. Revenues are paid to the TSO where it is ring-fenced (usually for re-distribution to all Users across the whole network)

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This payment structure is a fundamental point. The original User could either have used the capacity or sold it on to another user, or sold it back to the TSO, but if they have chosen to do none of these things and simply decide to stop others having access to the capacity they should not be rewarded for such behaviour. Indeed the original User who is hoarding and, through UIOLI, temporarily finds that their unused capacity is used by another User, would not have gained any direct income from this unused capacity that they were withholding.

One final reminder is that the original user still retains firm capacity rights because the UILOI was interruptible. As shown in the following example, subject to the nomination regime the original User would be able to make use of the capacity through re-nominations if they were appropriate.

Example of interruptible UIOLI:

- A market is daily balanced, with minimum capacity contract durations of 1 day.
- Total capacity at point X is 240 units.
- The TSO assumes non-profiled delivery of flow i.e. 10 units of capacity allocated per hour.
- At the start of the Gas Day, 06.00 hrs, firm Users, in aggregate, nominate an end of day quantity for delivery at point X of 120 units.
- The TSO offers 120units of UIOLI interruptible capacity to the market (this would normally be discounted well below the firm price)
- If all UIOLI capacity is procured and there are no re-nominations by firm Users during the Gas Day then it is assumed that for each hour 5 units of capacity are allocated to firm capacity Users and for each hour 5 units to interruptible capacity Users.
- If, at 18.00 hrs the firm Users re-nominate the maximum available hourly rate to the end of the Gas Day, that being10units per hour, then interruptible Users would be fully interrupted from 18.00hrs onwards.
- The final allocations for the day would then be: firm Users 180 units, interruptible Users 60 units.