

**EFET¹ Response to ACER Public Consultation on the
Draft Framework Guidelines on Rules Regarding Harmonized Transmission
Tariff Structures for Gas
(PC 2013 G03)**

Cost Allocation Methodologies and Tariffs for Incremental Capacity

¹ The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org.

Cost allocation methodologies

Question 1: Do you agree with the current proposal on the information to be gathered regarding input assumptions to run the methodologies (as described in Section 3.2 of the Cost allocation and the determination of the reference price)

Yes but with refinements

ACER's description in Section 3.2 of the input assumptions to the methodology and the cost concepts used, which TSOs shall be required to publish, appears comprehensive. They may however overlap with information which is currently required to be published under Annex I Chapter 3 of the Gas Regulation, or with the information TSOs are required to publish under Section 2 of the Framework Guidelines. So ACER should rationalise the publication requirements described in Section 2 and this new Section 3.2.

The Framework Guidelines should require the Network Code to specify a list of the relevant input parameters for each methodology and to detail any criteria to be applied when determining each parameter. The Network Code should require TSOs to publish a working model of the methodology being used, along with a description of how it operates. This should be pre-loaded with the current network representation (including capacity and flow assumptions per segment) and input parameters, but should allow for parameters to be manually changed, thereby providing network users with the ability to effectively replicate and predict tariff evolution without having to build an equivalent model of their own.

Question 2: Do you agree with the current proposal on the determination of the entry/exit split? (as described in Section 3.3.2 of the Cost allocation and the determination of the reference price)

Yes

ACER's latest proposal allows NRAs to set the entry/exit split as an input parameter based on specific cost drivers to the extent this fulfils the objectives in the Framework Guidelines, otherwise a default 50%/50% split is applied. Alternatively, the entry/exit split may be an output of the chosen cost allocation methodology itself. Whilst this may represent a subtle change from ACER's original proposal to require a 50%/50% split unless a split which better fulfilled the objectives in the Framework Guidelines could be justified, the practical consequences are likely to be the same.

Bearing in mind the extensive list of objectives in the Framework Guidelines², which are not always consistent with each other, and the nebulous nature of cost drivers, this new approach still leaves NRAs with a lot of leeway to set disproportionately high or low entry/exit components. However, we would support ACER's approach as there may be cases where a

² Albeit ACER has singled out three which should be considered most relevant

significantly lower entry or higher exit component is justified, principally as a result of cost drivers but ultimately to serve a wider purpose than pure cost reflectivity³.

It is important therefore for details of the entry/exit split⁴, and its justification, to always be included as part of the wider consultation NRAs/TSOs are required to undertake on the cost allocation methodology they use to set reference prices at entry/exit points.

Circumstances

Question 3: Do you agree with the proposed level of harmonisation regarding the circumstances leading to choose a tariff methodology? (as described in Section 3.3.3 of the Cost allocation and the determination of the reference price)

Yes but with refinements

We agree that the Network Code should elaborate on the circumstances when to apply a particular primary methodology or secondary adjustments, along with the consequences these may have as regards the relevant objectives in the Framework Guidelines. In reality however, such elaboration is likely to be of a general nature and, bearing in mind the extensive list of objectives in the Framework Guidelines, which are not always consistent, it is questionable how effective this will be in influencing the choice of methodology.

The Framework Guidelines should also clearly state that choice of cost allocation methodology shall be publicly consulted upon with all relevant stakeholders and be subject to NRA approval, either directly or following a recommendation from the TSO.

Question 4: Do you agree with the identified circumstances? (as described in Section 3.3.3 of the Cost allocation and the determination of the reference price).

No

Whilst we would support specific rules being applied to the possible use of the postage stamp methodology, the 90% capacity thresholds currently proposed appear to be arbitrary. It is also hard to see how any threshold defined in the Network Code relating to the difference between the average distance travelled by domestic and transit flows could be anything other than arbitrary either.

As for the rest of the identified circumstances in Section 3.3.3, whilst these appear to be relevant factors that should be considered when deciding between cost methodologies, cost concepts and capacity assumptions, it is not always clear exactly what they mean. For example, it is not clear to us what is meant by “The Network Code shall define, in relation to unstable flow patterns what forecast quality cannot be used and provide appropriate proxies instead”. ACER should redraft this section to make those identified circumstances it thinks

³ We would not typically expect the entry component to ever exceed 50%

⁴ And the capacity/commodity split where relevant

appropriate more clear and specific. It should also provide for these to be expanded upon in the Network Code.

Primary Methodologies

Question 5: Do you agree with the 4 generic Methodologies and their level of harmonisation as a basis for the description and harmonisation of current European Tariff approaches? (as described in Section 3.4.1 of the Cost allocation and the determination of the reference price)

Yes but with refinements

We assume that the four generic methodologies described in the Framework Guidelines represent those which are currently in use throughout the EU. To this extent, the Framework Guidelines appear to do little to harmonise the methodologies used and Member States are likely to continue with the status quo.

Whilst we recognise that harmonising cost allocation methodologies across the EU is difficult, we are disappointed that ACER has not strived for a greater degree of harmonisation. As such, the potential for competition and cross-border gas flows to be distorted because of differing cost allocation methodologies applying in different market areas persists.

For example, ACER could at least have identified a default methodology against which all EU TSOs would be required to calculate tariffs for comparison purposes. TSOs would still then be able to choose an alternative approved methodology if it was more cost reflective or better fulfilled other tariff objectives. But such an approach would better highlight the differences between two methodologies in each Member State⁵ along with the impact on tariffs across the EU of using a single methodology⁶.

Question 6: Do you agree with the description of the “postage stamp” methodology? (as described in Section 3.4.1.1 of the Cost allocation and the determination of the reference price)

Yes

The postage stamp methodology represents a simple approach to tariff setting which generates a single price for all entry points and a single price for all exit points, so is likely to be relevant only in some TSO systems. This approach does not provide any locational signals and will invariably result in a degree of cross-subsidy. The conditions relevant to its potential use could be further developed in the Network Code.

Question 7: Do you agree with the description of the “capacity-weighted Distance” methodology? (as described in Section 3.4.1.2 of the Cost allocation and the determination of the reference price)

⁵ The Framework Guidelines currently require TSOs to publish all relevant information and the outcome of at least two separate methodologies, but could differ between Member States

⁶ Albeit the entry/exit split may differ between Member States

Yes

The capacity weighted distance methodology is an improvement on the postage stamp methodology as it uses a simplified matrix of distances between entry and exit points as a cost driver for determining reference prices. As such it provides a basic element of cost reflectivity and variant B appears to enhance its cost reflectivity further by taking account of the probable flows at peak, rather than simply assuming each exit point will be supplied by each entry point.

Its relative simplicity and non-reliance on pipeline costs make it a candidate for a potential default methodology against which all TSOs across the EU would be required to calculate tariffs for comparison purposes⁷. It is stable, easy to understand and should be able to be applied in a consistent manner across the EU. If used as a default methodology it may be preferable to rely only on variant B, as this appears to be most cost reflective and takes account of bi-directional IPs and entry/exit zones with multiple gas qualities⁸. Also the proportion of capacity used to weight the average distance should probably be based only on technical capacity, not booked capacity, as this is more reflective of pipe in the ground.

Question 8: Do you agree with the description of Variant A of the “virtual point based” methodology? (as described in Section 3.4.1.3 under the title Variant A of the Cost allocation and the determination of the reference price)

Yes

Variant A of the virtual point based methodology appears to be more cost reflective⁹ and economically efficient than the capacity weighted distance model. It includes pipeline costs and annuitisation factors and derives its reference prices based on the marginal cost of flowing an extra unit of gas at each entry and exit point. It has been used in the UK for many years and is generally recognised as giving strong locational signals. However, it is clearly more complicated than the capacity weighted distance methodology and can be particularly sensitive to the merit order of entry flows assumptions used to supply peak capacity, which can cause price volatility. It is also the methodology most likely to require rescaling as a secondary adjustment due to its use of marginal costs. By relying on incremental costs, it may be more appropriate for use in expanding networks rather than in networks with constant or decreasing consumption¹⁰.

Whilst it could potentially be a candidate for a default methodology for comparing tariffs across the EU, this would require TSOs to adopt a more coordinated and harmonised approach to gas flow assumptions across the EU, as different flow assumptions at the same point could lead to significantly different prices. It also may be too complex and deliver relatively small incremental benefits for smaller systems when compared to the capacity weighted distance approach.

⁷ See our response to Question 5

⁸ See presentation of Fluxys at the ACER Workshop on Gas Tariffs and Incremental Capacity on 3rd September 2013

⁹ Its cost reflectivity is largely theoretical as the merit order assumptions about where gas will enter the system on a peak day are unlikely to reflect actual flows on the peak day, let alone a non-peak day.

¹⁰ Where observed costs may be more appropriate

Question 9: Do you agree with the description of Variant B of the “virtual point based” methodology? (as described in Section 3.4.1.3 under the title Variant B of the Cost allocation and the determination of the reference price)

Yes but with refinements

Variant B of the virtual point based methodology has some similarities with the capacity weighted distance approach except that its distance assumptions are based on the cartographic distance between the geographic coordinates (longitude and latitude) of each entry/exit point and the virtual point, not on the distance of the actual pipelines connecting entry/exit points. It also takes no account of pipeline cost and so appears to be more abstract and less representative of real cost drivers than its variant A equivalent.

The methodology seems extremely complicated and we still do not fully understand the inter-relationship between the dominant node and the virtual point. As such, we are concerned that the methodology could be unduly sensitive to the dominant point selected, or to the entry/exit points selected as a reference for setting the ratio of tariffs for entry/exit points to equal the distance between entry/exit points and the virtual point¹¹.

That said, the methodology does have the advantage of determining the appropriate entry/exit split rather than having to determine this ex-ante as an input to the methodology. However, the elements of the methodology that calculate the entry/exit split could presumably be run ex-ante as a separate process and fed into a different methodology.

ACER should provide a more coherent explanation of how it works and an explanation of the incremental benefits it has over variant A or the capacity weighted distance methodology.

Question 10: Do you agree with description of the “matrix” methodology? (as described in Section 3.4.1.4 of the Cost allocation and the determination of the reference price)

Yes but with refinements

The matrix methodology appears to be an extension of the capacity weighted distance methodology as it relies on capacity and distance as cost drivers. However, it also appears to factor in economies of scale in relation to pipeline capacity, albeit entry-exit paths are sometimes virtual.

Due to its complexity and the ambiguity of its description we still do not fully understand how the methodology works. However, based on its description in ACER’s worked examples paper, it appears to be heavily reliant on arbitrary assumptions which may have a significant influence on the outcome, which doesn’t inspire confidence. It also appears not to guarantee a unique solution and offers a number of options for solving the optimisation algorithm.

ACER should provide a more coherent explanation of how it works and an explanation of the incremental benefits it has over the capacity weighted distance methodology.

¹¹ See section 5.2.v.a of Acer’s Tariff Methodologies: Example Paper dated 23rd July

Secondary adjustments

Question 11: Do you agree with the 3 proposed secondary adjustments and their level of harmonisation? (as described in Section 3.4.2 of the Cost allocation and the determination of the reference price)

Yes but with refinements

We recognise there may be occasions when it is appropriate to make secondary adjustments to the reference prices derived from the primary cost allocation methodology and agree that ACER should limit this to the three methods described. In principle, secondary adjustments should be applied sparingly and in all cases should be justified and consulted upon with stakeholders. The Network Code should also identify which secondary adjustments can be used in conjunction with which primary methodology as not all of them may be appropriate¹².

Question 12: Do you agree with the proposal regarding the “rescaling”? (as described in Section 3.4.2.1 of the Cost allocation and the determination of the reference price)

Yes

Rescaling should be used provided it does not fundamentally undermine the locational signals¹³ (if any) resulting from the primary methodology as it is consistent with the requirement in Section 4.1 of the Framework Guidelines that “the determination of reference prices shall seek to minimise any gaps between the revenues which the TSO is entitled to obtain on the basis of the applied regulatory regime and the revenue actually obtained by the TSO.”

Question 13: Do you agree with the proposal regarding the “equalisation”? (as described in Section 3.4.2.2 of the Cost allocation and the determination of the reference price)

Yes but with refinements

Allowing for equalisation to be applied subject to certain pre-defined criteria listed in the Network Code seems preferable to allowing the postage stamp methodology to be used as a primary cost allocation methodology. Tariffs could then still be equalised for homogenous sets of entry/exit points, where appropriate, rather than having to equalise all entry or exit points. That said, the reasons quoted in the Framework Guidelines for applying equalisation are vague¹⁴ and need to be described more prescriptively in the Network Code.

Also, it is not clear what purpose the final paragraph of the Section 3.4.2.2 serves. It could be considered somewhat contradictory as equalisation, by its very nature, diminishes cost reflectivity. As tariffs in general are required to satisfy a large number of diverse objectives

¹² For example, rescaling would not need to be used in conjunction with the capacity weighted distance methodology as allowed revenues are an integral part of tariff determination, whereas it would be in the case of the virtual point variant A methodology.

¹³ We are not sure what ACER means by the “economic signals “ expected from the chosen allocation methodology in the final paragraph of 3.4.2.1

¹⁴ It is not clear why or how “renewable energies”, for example, constitutes a reason for equalisation.

set out in Section 1.2 of the Framework Guidelines, we suggest ACER deletes this paragraph to avoid confusion. ACER should also make it clear that domestic exit points can be further sub-divided¹⁵ for the purpose of equalisation as this is not what is implied in footnote 12.

Question 14: Do you agree with the proposal regarding “benchmarking”? (as described in Section 3.4.2.3 of the Cost allocation and the determination of the reference price)

Yes but with refinements

Benchmarking of tariffs by NRAs is provided for in the Gas Regulation and so is an appropriate secondary adjustment mechanism. However, by its very nature, the form of benchmarking described in the Framework Guideline¹⁶ involves cross-subsidy between different network users as any reduction in tariffs as a result of a benchmarking exercise requires a rise in tariffs elsewhere. Benchmarking may also be hard to apply effectively on a purely national basis as pipelines within Member States are often parts of wider trans-European transit routes. Clearly NRAs need to be mindful of the risks that pan caking may make gas flows on certain pipeline routes uncompetitive. But excessive benchmarking implies that networks tariffs and flows will be assessed on a point to point basis, rather than an entry exit basis.

The Framework Guidelines should specifically require ACER to express an opinion in cases where benchmarking is applied, regardless of whether neighbouring NRAs agree on the validity of its application.

Test

Question 15: Do you agree with the proposed cost allocation test? (as described in Section 3.6 of the Cost allocation and the determination of the reference price)

Yes but with refinements

As previously stated, we see merits in the Network Code requiring TSOs to publish a comparative test of the revenues resulting from domestic and cross border network usage. However, the ratios will need to be carefully defined and the revenues and cost drivers will need to be consistently applied¹⁷. The test should be applied both on an ex-post basis using actual revenues (to highlight obvious cross-subsidies) and on an ex-ante basis (as part of the TSOs justification in support of its chosen primary methodology and any secondary adjustment mechanism).

The extent to which LNG entry points should be treated as a national or cross border points¹⁸ and the specific mathematical formulas for each of the two ratios should be defined

¹⁵ For example, DSO exit points and power stations

¹⁶ Benchmarking could also result in an overall adjustment of a TSO's allowed revenue

¹⁷ For example, the Network Code will need to specify how cost drivers are applied at entry/exit points or pipelines which have a shared domestic and cross-border use

¹⁸ At this stage we are not sure why LNG terminals should be treated as cross-border entry points for the purposes of the comparative test and are concerned that this could create false perceptions of potential cross-subsidy.

in the Network Code for each primary cost allocation methodology, and should reflect the cost drivers used in each methodology. Where secondary adjustments are applied, the comparative test should be applied both pre and post the application of these adjustments, so as to highlight their effects. There may also be merit in applying the comparative test on a separate entry and exit basis as any excessive cross-subsidy between domestic and cross-border flows at entry or exit could be hidden by applying the test on an aggregated entry and exit basis.

Implementation

Question 16: Do you agree with the proposed implementation measures? (as described in Section 3.7 of the Cost allocation and the determination of the reference price)

Yes but with refinements

We agree that NRAs should publicly consult on which of the permitted cost allocation methodologies they intend to use highlighting the impact these will have on the evolution of tariff levels. As regards the obligation on NRAs to publish relevant information and the results of the comparative test for at least two of the primary methodologies, using a default methodology as a comparator to any other methodology proposed seems most appropriate.

In any case, projected tariff evolution should always be shown at individual entry/exit point level so as to enable network users individually to understand exactly how they will be affected by each methodology.

Question 17: Do you agree that at least every 4 years the input assumptions, forecasts and choice of methodology shall be revised by the NRAs regardless to the applicable national revision cycles? (as described in Section 3.7 of the Cost allocation and the determination of the reference price)

Yes but with refinements

Input assumptions and forecasts which affect the determination of reference prices under the primary cost allocation methodology should always be published and updated prior to the tariff period for which prices are being calculated. Typically this will happen annually not at least every four years. Clearly tariffs should always be based on the most up to date input assumptions and forecasts.

As regards the primary methodology itself, we agree that NRAs should be required to periodically assess the appropriateness of their chosen primary methodology¹⁹ once the Network Code has been implemented. Requiring them to do this at least every four years seems sufficient but this becomes less of a concern if the number of primary methodologies they can choose from is more restrictive. Should an NRA decide to change the primary methodology post implementation, careful consideration will need to be given to the timing of

¹⁹ Including the entry/exit split and the capacity/commodity split (where relevant)

this. Mitigating measures, similar to those applying at implementation, may also be necessary.

Question 18: Do you agree with the proposed mitigating measures in case of a tariff increase (applying at a tariff increase of more than 25%)? (as described in Section 3.7 of the Cost allocation and the determination of the reference price)

No

It is not clear from the Framework Guidelines whether the mitigating measures described effectively amount to a 25% price cap or whether they could reduce a price increase greater than this to a level lower than 25%. Also, it is not clear whether the mitigating measures are intended to mitigate the effect of price increases only for the year following implementation of the Network Code or throughout the remaining regulatory period. Mitigating measures are also referred to in Section 1.4 of the Framework Guidelines but presumably the measures contained in Section 3.7 are intended to replace these.

In our view, mitigating measures will be necessary at all entry and exit points to address the impact arising from the possible consequences of moving to a different cost allocation methodology or entry/exit split. However, they will also be necessary to address the impact of year on year price changes at interconnection points resulting from ACER's decision to adopt a floating payable price.

Prior to the implementation of the Network Code TSOs and NRAs should highlight the effect any change to the cost allocation methodology or the entry/exit split will have on reference prices at individual entry and exit points. In the event the price at an entry or exit point increases by more than 10% as a result of these changes and this has a material impact on network users' transportation charges²⁰, TSOs and NRAs should either cap price the increase at 10% for the first year following implementation of the Network Code or spread the increase evenly over the remaining regulated period²¹. Thereafter, there should be a limit of +/- 10% for any annual change in the reference price at interconnection points published at least one month before the annual capacity auction. Any changes greater than +/- 10% should be published at least two months before the annual capacity auction and network users should have a right to terminate their existing annual capacity contracts if the reference price at any interconnection point increases by more than 10% in any year.

Further transparency measures

Question 19: ACER consults on the publication of the following data of the regulated assets on the following:

1. RAB per TSO

2. Depreciation period per asset category

²⁰ A reference price could rise by significantly more than 20% but not have a material impact on a network user's transportation charges if increases from a very low base.

²¹ So if the tariff increase was 33% and the remaining regulatory period was 3 years TSOs would apply an 11% increase in each of the 3 remaining years.

3. *Rate of return, as defined by the regulatory rules applicable*

4. *Variable costs of the system per TSO*

5. *Major investment costs per country*

Do you deem proportionate the proposed level of harmonisation regarding additional transparency?

Yes but with refinements

The data proposed is necessary for network users to better understand the price control framework within which TSOs operate and to gauge whether costs are efficiently incurred. The information should be incorporated into section 2 of the Framework Guidelines and included in the standardised format to be developed under the Network Code.

Major investment costs should be published not just in aggregate but with sufficient information to allow average unit investments costs to be determined and compared²². Variable costs should also be broken down into categories such as manpower, fuel gas costs etc.

Question 20: Do you agree with the level of detail on the proposed provisions on monitoring, as set in section 1.4 of the endorsed Framework Guidelines on rules regarding harmonised transmission tariff structures for gas of 16 April 2013?

Yes but with refinements

As stated in our previous response, we support ENTSOG having a monitoring role as this will help ACER to determine whether the goals of the Framework Guidelines are being achieved. Aspects of the information being monitored²³ will also be relevant to network users and so ACER should make this monitored information available to network users as well as NRAs.

Question 21: Do you see value in having a standard gas tariff year across the EU, either starting on 1 January or 1 October?

Yes

Standardising the gas tariff year across the EU will be a significant benefit to network users as the price of capacity they procure for cross-border trade will relate to the same consistent yearly period and change at the same time throughout the EU. Greater consistency will be factored into network users' trading, supply and budgetary activities and will help to reduce the risk of margins in commodity transactions being eroded by unforeseen changes in capacity prices.

²² For example, cost per compressor or cost per km/dia

²³ For example percentage changes in tariffs, under/over recovery

In future, cross-border capacity will be allocated by auction on a bundled basis subject to harmonised timescales and rules. As the definition of annual capacity and the timescales for auctioning it are based on the standard October-September gas year any standard tariff year should be consistent with this. In order to avoid the uncertainty and distortion arising from different elements of the capacity bundle changing price at different times, we think it is imperative for a standard tariff year to be applied at least in relation to interconnection points. This being the case, and in order to avoid potential distortion and discrimination at a national level, it would seem appropriate to apply the same tariff year to all national entry and exit tariffs too.

Question 22: Do you agree to the proposal to consider a 30 day minimum notice period for an NRA decision or TSO communication of changes in the reference prices as compared to entering into force of the tariffs?

Yes but with refinements

In our opinion the notice period provided for changes in reference prices should relate to the size of any change in price. In the event a price change at an individual entry or exit does not exceed 10% then one month is an acceptable notice period, otherwise a minimum two months notice is required.

In the case of cross border capacity (bundled and unbundled) at interconnection points, such notice periods should apply from the date of the annual capacity auction specified in the CAM Network Code.²⁴ This is because network users must have accurate and complete information about at the applicable reference prices, multipliers and seasonal factors that will apply during the forthcoming year in order to inform their bidding strategies.

Question 23: In the Framework Guidelines there are no specific measures included to take into account the nature of interconnectors which currently is dealt separately from the national TSO network. Do you find that further provisions for interconnectors are necessary?

Yes the following measures should be included

We are not sure we fully understand this question, but assume it relates to interconnector pipelines with single entry and exit points that do not form part of a national transmission network and whose sole purpose is to interconnect the market areas neighbouring Member States²⁵. The provisions contained in the Framework Guidelines have clearly been developed with national transmission systems in mind, each having multiple domestic and cross-border entry/exit points. It does therefore seem disproportionate to assume they should be applied equally to single pipeline interconnectors who have far less complicated cost drivers and only a very small number of entry/exit points solely dedicated to cross-border flows.

With this in mind, ACER should consider including a requirement in the Framework Guidelines for the Network Code to specify which obligations should apply to interconnectors

²⁴ The CAM Network Code requires annual capacity auctions to be held on the first Monday in March each year

²⁵ For example the merchant interconnectors connecting GB, Belgium and the Netherlands

and which should not, along with how any relevant obligations should be adapted to be more compatible for interconnectors.

Incremental capacity questions

*Question 24: Do you agree that the economic test for incremental capacity should be a financial validation comparing the present value of capacity volume commitments times the projected tariff, with the deemed investment cost to release the respective capacity times the fraction committed by shippers (as set out in the formula: $PV \geq DIC * f$)?*

Yes

We agree this formula is appropriate for an economic test for incremental capacity,

Question 25: Do you agree that the principles of the economic test should be harmonised on a European level?

Yes but with refinements

Yes the principles of the economic test as laid out in the formula should be harmonised on an EU level and applied to all incremental capacity, whether allocated by long-term capacity auction or open season.

That said, the f parameter and the nature and extent of positive externalities will not be the same throughout the EU, or for all incremental capacity. The deemed investment cost must also be based on an efficient investment cost, as if this is artificially high it will threaten the success of the incremental capacity process.

Network users who are required to make binding long-term commitments to underpin incremental capacity should have a full understanding of how the f parameter, the deemed investment cost and the monetised value of any externalities have been calculated beforehand. As such, TSOs should be required to regularly publish such information in advance and invite comments from network users prior to final approval of the economic test by NRAs. Such information should be accompanied by sufficient technical information regarding the investment²⁶ to allow network users to make reasonable assumptions regarding investment efficiency.

Network users should also have transparency over how any over or under spend is treated in the future value of the asset base.

Question 26: Do you agree with the principles of setting the f parameter, where f represents the fraction of investment underwritten by the shippers in the economic test?

Yes but with refinements

²⁶ For example, pipe length and diameter, power of compressor station etc

The principles listed²⁷ appear to be broadly relevant but may not be complete or accurate, so will need to be more clearly and comprehensively described. ACER should therefore publish complementary guidance on the factors which must be considered when calculating the f parameter. The guidance should also cover how the extent of any positive or negative externalities should be treated²⁸. TSOs must demonstrate they have followed such guidance when publishing details of the economic test ex-ante.

Question 27: When external effects influencing f are monetised should the used method be aligned with the CBA analysis of the (TEN-E) Regulation (EU) No. 347/2013 [1] according to its Annex V?

Yes

It would seem sensible to use a consistent methodology for monetising externalities across jurisdictions and for the methodology adopted for CBA analysis carried out under the Infrastructure Regulation to be applied for incremental capacity.

Question 28: Which option of tariff adjustment is appropriate for cases where the tariff for existing capacity does not suffice to validate the economic test?

Other options should also be considered

The reference price for incremental capacity should logically reflect the cost of providing that capacity. So in the event the reference price derived from the tariff methodology used in relation to existing capacity is insufficient, a reference price which reflects the cost of providing incremental capacity should be used in a parallel bid ladder. This could be achieved either by option 2 or option 3 and we suggest they should both be considered and developed further by ENTSOG during the CAM amendment process. Either option ensures a solution which is cost reflective and avoids cross subsidisation between existing users and new subscribers.

If a single reference price were to be applied in a single bidding ladder one way of protecting existing users from the impact of such unexpected changes would be to apply mitigating measures to year on year price changes at interconnection points. Network users would have the right to terminate their existing annual capacity contracts if the reference price at any interconnection point increases unexpectedly due to incremental capacity in any year. Alternatively, or in addition to such mitigating measures, any auction premium paid by network users for existing capacity could be reduced commensurate with any increase in the reference price resulting from incremental capacity.

Question 29: Do you agree that the NRA shall have powers to decide to use an alternative approach for payable price (fixed/ floating) exclusively for incremental capacity?

Yes but with refinements

²⁷ Delineation of incremental tariff issues document , section 2.2

²⁸ For example, positive externalities resulting from enhanced security of supply should be reflected in a lower f parameter and the monetised benefit could be trigger a compensating adjustment to the TSOs allowed exit revenues or to the entry/exit split.

Applying a different approach to payable price for incremental capacity compared to existing capacity introduces significant added complexity and risks creating distortion and undue discrimination between network users. It should also be recognised that network users are unlikely to be able to commit to levels of long term investment sufficient to pass an economic test without a reasonable degree of price certainty.

The merits of applying a fixed payable price for incremental capacity to provide network users with greater price certainty, thereby encouraging them to make the commitments necessary to pass the economic test, apply equally to existing capacity, where greater price certainty encourages long-term booking and helps underpin TSO allowed revenues.

ACER should review its approach to payable price in light of the concerns that a floating payable price may not give incremental and existing capacity users sufficient price certainty. In the event it decides a floating payable price is still appropriate, network users must be given sufficient notice of any price increase and mitigating measures must be introduced which allow network users to terminate their capacity contracts in the event reference prices increase beyond a set threshold, for example 10%.

Providing an option for shippers to fix the payable price should also be considered as part of the Network Code development process.

Question 30: Should users, who have previously committed to an auction premium on existing long term capacity (in the interim period until a European incremental capacity regime is in place), be compensated when incremental capacity for the year for which the premium was committed is released at a later stage at a lower price?

No

It is not yet clear when an EU incremental capacity regime will be in place. But conceivably this could be at the same time as the CAM Network Code comes into effect if the incremental regime is implemented via a change to the CAM Network Code. Provided network users are able to keep abreast of how the incremental regime will operate and when it is likely to take effect, they can factor this information into any bids they make for existing long term capacity beforehand. It does not seem appropriate therefore to compensate them if incremental capacity is released for a year where they paid an auction premium.

General part

Question 31: Additional comments on tariff and incremental issues ACER should consider

As a general observation, the revised chapter on cost allocation and determination of the reference prices is clumsily drafted and unclear in many areas. This will make it particularly difficult for ENTSOG to interpret and develop a Network Code which complies with the requirements of the Framework Guidelines. Prior to issuing final Framework Guidelines ACER should, in conjunction with its lawyers, review both the cost allocation chapter and the remaining parts of the Framework Guidelines to reduce the ambiguity of some of the requirements and to eliminate any superfluous or duplicating text.

It is also concerning that ACER has yet to publish its Impact Assessment on tariff harmonisation comparing its proposals with what currently exists across the EU. Without this assessment network users are unable to get any real sense of the impact of these proposals and the extent of the tariff distortion that currently exists across the EU. As such their judgements can only be made on anecdotal evidence and their familiarity with the tariff arrangements pertaining in their own countries, making them largely theoretical. As the Framework Guidelines set the ground rules for what ENTSOG are allowed and required to develop in the Network Code, there is a very real risk that the absence of robust analysis at this stage will lead to policy choices being developed which at best fail to address the current concerns and at worst increase the extent of tariff distortion.

Whilst we agree the Framework Guidelines should define cost allocation methodologies and tariff setting in sufficient detail to achieve the required level of harmonisation and to avoid distortions to trade, ACER should concentrate on setting out clear principles rather than prescribing too much detail. This will allow ENTSOG more scope to consider efficient solutions and develop detailed proposals during the Network Code development process, in conjunction with ACER and stakeholders.

With regard to storage tariffs, we agree that gas flowing in and out of storage facilities will have already been subject to entry charges and will in future be subject to exit charges. This needs to be considered by NRAs as part of the cost allocation methodology. However, it is not clear how NRAs should reflect the “need to promote efficient investment in networks” or the need to “minimise any adverse effect on cross-border flows” when setting storage tariffs and NRAs are unlikely to interpret these requirements consistently. As such we think these should be deleted from section 3.5.

Question 32: Please rank the three most important issues for your company, association.

EFET’s three most important issues relating to the Framework Guidelines as a whole are as follows:

1) Publication and notice period

Reserve prices, seasonal factors (if any) and multipliers (if any) relating to all auctioned capacity products in the relevant gas year (October – September) must be published in advance of the first annual auctions for that gas year.

There must be a minimum one month notice period for any change to any capacity reserve/reference price and if the change exceeds 10% a two month notice period is required. In the case of capacity which is auctioned, these notice periods shall apply from the date of the first annual auctions for that gas year²⁹.

2) Multipliers and seasonal factors

²⁹ The CAM Network Code specifies that auctions for annual bundled capacity at interconnection points should be held on the first Monday in March. So the reserve prices, seasonal factors and multipliers relating to all bundled capacity products auctioned in that gas year (annual, quarterly, monthly, daily) will have to be published either one month or two months before this date.

Quarterly and monthly products should always be set proportional to the annual reserve price not multiplied, either individually or on average over the year, within a range of 0.5 – 1.5.

Any day ahead or within day reserve price risks segmenting the market and limit opportunities for optimisation and efficient price arbitrage. When setting day-ahead and within day multipliers within a range of 0 - 1.5, NRAs on both sides of the border should collectively decide on a balanced solution for that interconnection point.

Multipliers should not be unduly prescriptive or complex and should not be linked solely to instances of congestion.³⁰ NRAs should also consider the effects on liquidity, balancing markets, cross-border trade, price spreads and the risk of under/over recovery when setting multipliers.

3) Payable price

ACER should consider whether floating payable prices remain appropriate in light of the concerns that a floating payable price may not give incremental and existing capacity users sufficient price certainty³¹. In the event it decides a floating payable price is still appropriate, network users must be given sufficient notice of any price increase and mitigating measures must be introduced which allow network users to terminate their capacity contracts in the event reference prices increase beyond a set threshold, for example 10%.

Providing an option for shippers to fix the payable price should also be considered as part of the Network Code development process.

EFET Gas Committee

17th September 2013

³⁰ As per the definition used to trigger firm day-ahead use-it-or-lose-it under the CMP Guidelines.

³¹ See our response to question 29