



Agency for the Cooperation of Energy Regulators  
Trg republike 3  
1000 Ljubljana  
SLOVENIA

5th November 2012

Dear Sir

**Gazprom Marketing & Trading Limited Response to Public Consultation on Tariff Harmonisation Framework Guideline.**

Gazprom Marketing and Trading Limited ("GM&T") welcomes the opportunity to respond to the consultation on the proposed Framework Guidelines for Tariff Harmonisation. GM&T is the UK registered wholly-owned subsidiary of Gazprom Group ("Gazprom"), responsible for the optimisation of Gazprom's energy commodity assets through GM&T's marketing and trading network. GM&T is an active gas trader at various hubs within Europe, as well as marketing gas to end users.

The key points of our response are as follows:

- The proposed implementation period of 12 months from entry into force for both existing and new contracts is unrealistic. Many shippers will have made long term capacity bookings in good faith based on known capacity costs. These capacity costs will have been reflected in the related supply contracts for gas. It is unreasonable to expect such shippers to change their supply contracts to reflect new capacity costs within 12 months. Therefore we propose that either the application to existing contracts should be dropped, or shippers have the right to step out of affected capacity contracts prior to implementation of the network code.
- Tariffs should aim to minimise the risk of under or over recovery of revenues by TSOs to avoid potential discrimination between types of shippers or distortion of competition. This can arise if, in order to recover lost revenue, TSOs increase capacity charges or add commodity charges; such charges are likely to mean that those who book and pay the full regulated price for capacity are likely to pay more for capacity than those who book short term capacity at a discount.

I hope you find our comments useful. I would be happy to discuss them in more detail at your convenience.

Yours faithfully

**Alex Barnes**

**Head of Regulatory Affairs.**

**Gazprom Marketing & Trading Limited**

20 Triton Street

London NW1 3BF

United Kingdom

T: +44 (0)20 7756 0301

M: +44 (0)774 775 6032

E: alex.barnes@gazprom-mt.com

[www.gazprom-mt.com](http://www.gazprom-mt.com)

## **Public Consultation Questions**

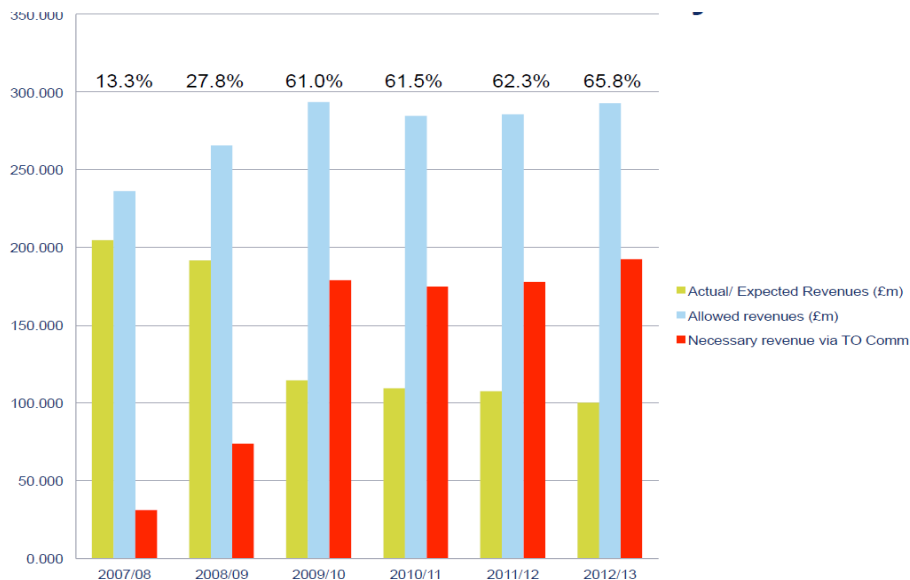
GM&T is responding in the capacity of a shipper and energy trading entity. Unless otherwise stated our answers are not confidential.

### **1. General provisions. Scope, application, definitions and implementation (Chapter 1 of the draft Framework Guideline)**

#### **1.1. Please explain whether any of the aspects of the application of the draft FG (NC) to existing contracts would cause disproportionate effects on gas business in relation to Third Package Objectives.**

Broadly speaking the FG establishes a good balance between the objectives set out in section 1.2. In the main the FG adopts a pragmatic 'no regret' formulation that avoids taking policy choices now where this might otherwise restrict future measures. In some areas, however we are concerned that the FG does not provide a clear enough policy steer to address actual and potential market distortions identified in the Brattle Report.

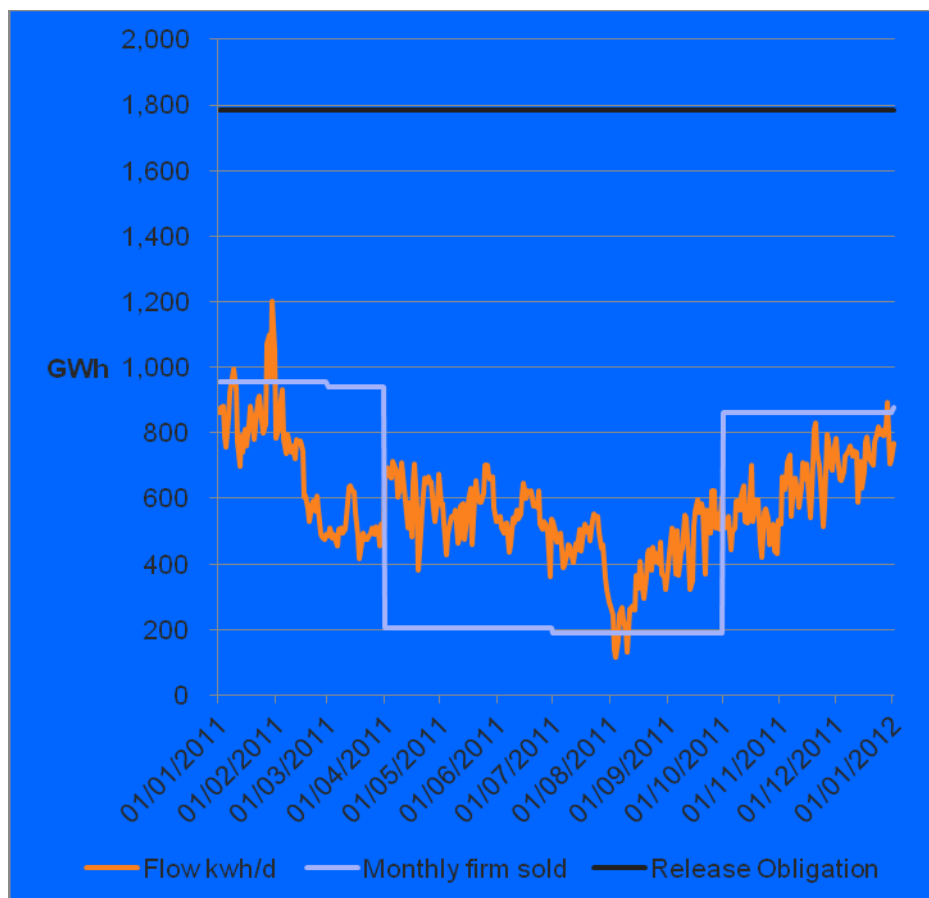
In particular the systemic under-recovery of revenue from entry capacity auctions found in the GB market illustrates the potential dangers of setting reference prices too low. In the GB market significant under-recovery of costs had been addressed through a substantial commodity charge which not only undermines cost reflectivity by dampening locational differentials but harms the interests of players that have committed to long-term capacity who end up with an artificially inflated transportation bill. The following chart shows how much of National Grid's allowed revenue for entry capacity is recovered from the commodity charge and how this has grown over time. The percentage for each year is the percentage of allowed revenue recovered from the commodity charge. As can be seen, although the intention is for revenue to be raised via capacity charges, the significant size of revenue under recovery means that a majority of the allowed revenue is now derived from the commodity charge.



This is caused by a combination of plentiful capacity available plus discounts for short term capacity. Essentially, in many cases for shippers, it is a very low risk option to buy capacity at short notice, and pay less for it. Although all shippers pay the commodity charge for the gas they flow, the shippers who have booked and paid capacity at the full regulated price

obviously pay more than those who have booked capacity at the discounted price, effectively subsidising those shippers.

The chart below illustrates the levels of capacity booked at Bacton, one of the main entry points into the GB market.



Monthly firm capacity sold indicates capacity sold at the regulated price, and as can be seen is less than flows in summer months in particular. This implies that those shippers flowing gas are buying discounted capacity (otherwise they would face scheduling charges).

Significant revenue over-recovery may be manageable in the GB context but applied to auctions of bundled capacity at cross border points across the EU risks placing a disproportionate cost burden on parties that have to secure long transit flow supply chains to get their gas to market. By indirectly impacting the competitiveness of particular classes of user, free movement of gas (e.g. gas storage flexibility) from one member state is affected. It is important that, in encouraging trading, NRAs and TSOs do not create distortions by enabling one group of shippers to pay less for their capacity, and the short fall in revenue to be made up by another group of shippers.

In our view, If NRAs in overseeing the tariff methodologies of relevant TSOs were more explicitly obliged to ensure year on year revenue stability, the prospect of reducing market distortions would be enhanced. Setting a maximum yearly target deviation for revenue under or over recovery would be one way of doing this, although we accept that setting an appropriate target would be difficult to establish initially. However, the NRAs through ACER could agree to set the target at a later date once the tariff code has been in place for a number of years, and data on actual TSO revenue recovery and evidence of market distortions is more widely available.

Equally important as the issue of revenue recovery is that of the implementation period for the new code of one year, and applying it to both new and existing capacity contracts. It is impossible to predict at this stage how shippers with existing capacity contracts will be affected by changes to the tariffs but a one year implementation period is too short a time for shippers to be able to adjust their related supply contracts to take account of new transportation costs. Therefore the FG should state that the new tariffs do not automatically apply to existing capacity contracts unless shippers agree to this or shippers have the option to walk away from their existing contracts and book capacity under the arrangements in the Capacity allocation Mechanisms Code ("CAM"). The implementation period for the Tariff Code should reflect the time that would be required for this to happen.

### **1.2 Please explain if any further definitions should be added for clarity of the FG (NC)?**

None identified at this stage.

### **1.3 Please suggest the top-5 core indicators for monitoring the future EU-wide implementation of the future tariff FG (NC)?** ACER and ENTSO-G both have legal obligations to monitor NC implementation (in accordance with Article 9 (1) and Article 8(8) of Regulation (EC) No 715/2009 respectively).

We suggest the following core indicators:

- Relative size of the over or under recovery of the Regulatory Account in a specific entry-exit zone in a given year/ relevant period. This would help gauge how effective the tariff design was in ensuring tariff stability. A related measure would be the volatility of tariff charge changes, as indicated by the degree of change between tariffs for different entry and exit points over different charging periods (e.g. year on year) (see below).
- A comparison of the revenue recovery from transit flows compared to domestic consumption in a specific entry-exit zone in a given year/relevant period expressed in unit terms (revenue/volume transported). This should be compared to the relevant costs of transporting gas between entry exit zones (transit flows) and those to end users.
- A comparison of the aggregate revenue collected from entry compared to the aggregate revenue collected for exit in a specific entry-exit zone in a given year/relevant period.
- A measure of the change of charges at each entry and exit point (or bundled entry-exit charges as appropriate) from one year/relevant period to another year/relevant year. There is no obvious right answer here, although an inappropriate degree of charge volatility (that is not driven the underlying costs in the tariffication model or changes in the value users place on cross-border capacity in the auctions) would be a cause for concern. If users find this charge volatility too difficult to predict market confidence is likely to be undermined, and this could lead to distorted capacity booking behaviour.

## **2. Cost allocation and determination of the reference price (Chapter 2 of the draft Framework Guideline)**

### **2.1 Transparency provisions**

#### **2.1.1 Do you agree with the level of harmonization proposed for the transparency in relation to tariffication methodologies?**

Broadly speaking, yes. We would like to see further obligations to ensure that market participants are able to fully understand the tariffication methodologies and any changes that are applied to those methodologies from time to time (see below).

#### **2.1.2 Would you support additional requirement(s) to ensure "reasonable and sufficiently" detailed tariff information? For example, one could consider including a provision such as:**

**“the transmission system operators or relevant national authorities shall provide additional information if a significant tariff fluctuation is expected on a specific or on all entry- and exit points”.**

Yes. Sufficient detail in our view should allow market participants to be able to replicate the results of the tariff calculations by the TSO. It should be possible for market participants to use the data provided (ideally using a model published by relevant TSO(s)) to derive the relevant tariffs/reference prices.

How TSOs publish data is important. As a minimum we would expect it published on the relevant TSO's website and it should be accompanied by an analysis of any changes with illustrative examples indicating the percentage changes in tariff levels and the expected impact on different classes of user.

In our view it should be possible to publish information including aggregate flow assumptions at entry and exit points used in any tariffication model. However data anonymity must be maintained so that exact patterns of use of individual users of the system are not identifiable.

It might be helpful to establish best practice guidelines to ensure that all TSOs aspire to the highest standards of transparency for tariffication methodologies.

## **2.2 Cost allocation and reference price setting methodology, general questions Do you agree with proposed level of harmonization for the reference price setting methodology, aiming for same methodology for all types of network users per one entry-exit zone?**

Yes but this is based on the important assumption that regulated capacity prices continue to apply to 'domestic' users within a given entry-exit zone. It is important to ensure that there remains scope for NRAs scope to treat different network users in an entry- exit zone differently provided such differences can be objectively justified. Indeed they should be obliged to consider such difference as failure to deal with relevant differences is in itself discriminatory.

If auction reference price arrangements were to ever apply to non interconnection points then more of these discrimination questions would arise. Therefore, in our view it is important to ensure that the FG does not oblige TSOs and NRAs to necessarily apply identical tariffication arrangements to all types of users under such circumstances.

For example large transmission connected users such as generators and storage operators may use the system differently, and they typically operate in a competitive environment compared to regulated price/revenue controlled distribution companies also connected to the system (the fundamental drivers in bidding for exit capacity in any auctions would be different). Certain parties, such as storage, may offer system support allowing TSOs to avoid some investment on their system – this is also an objective justification for different treatment.

We believe further clarity is required in the drafting of the FG to avoid inadvertently removing the scope to apply different tariffs (or discounts/adjustments) to accommodate objectively justified relevant differences between different types of network users within an entry-exit zone.

## **2.3 Cost allocation and the Reference price setting methodology, detailed questions.**

### **2.3.1 Do you agree with proposed option for setting reference prices for entry capacity i.e. to have methodology based on major cost driver (e.g. distance) unless use of equal tariffs can be justified?**

Yes but it is important to consider all the relevant cost drivers. Distance alone will not in our view provide genuinely cost reflective tariffs, indeed in meshed systems it will almost certainly provide the wrong pricing signal. It is important to model the patterns of flow within a given entry-exit zone and consider the incremental cost impact of accommodating changes in patterns on that system.

It is also important to consider how the use of different costs approaches for example historic costs versus Long Run Marginal Costs (LRMC) can impact cost recovery and the relative costs of transporting gas across different entry exit zones. The Brattle report demonstrates how the use of LRMC in one zone and historic costs in a parallel zone can lead to very different charges for those wishing to transit gas to zones further downstream. Naturally shippers will tend to book capacity via the cheaper route, so adjacent TSOs will need to take account of their tariff setting methodologies and their impact on neighbouring TSOs.

Furthermore the use of LRMC and historic costs can lead to different levels of revenue recovery which also need to be taken into account. For example if LRMC costs are lower than historic costs some form of scaling factor will be required to enable the TSO to recover its allowed revenue if the Regulated Asset Base is calculated on historic investment.

In light of the above further thought will need to be given to how to harmonise tariff setting to avoid unnecessary uncertainty for shippers and TSOs.

**2.3.2 Do you agree with proposed option for setting Reference prices for exit capacity i.e. to have methodology based on major cost driver (e.g. distance) unless use of equal tariffs can be justified?**

Yes – our comments set out in our response to 2.3.1 apply equally to exit.

**2.3.3. Do you agree with the cost allocation principle that revenue from entry points should equal 50% of revenue from all entry and exit points?**

Yes - equivalence of entry and exit revenue recovery is desirable so as not to erect artificial barriers to trade across borders. Higher weightings for entry charges may disadvantage parties in a neighbouring 'downstream' entry-exit zone preventing otherwise competitively priced gas (including storage flexibility, or demand side response) reaching such markets. Therefore a tariff model which aims to ensure a 50:50 split of revenue recovery between entry and exit, with minimal under recovery of revenue makes sense. However it should be recognised that any under recovery from entry capacity sales may be appropriately recovered by adding additional charges to exit, whether as an additional capacity charges or as a commodity charge as this is the most effective way to ensure that the full costs of gas transportation are borne by those who consume the gas. By recovering lost revenue via exit charges TSOs can ensure that costs are appropriately targeted on either consumers within the entry exit zone or those in downstream entry exit zones. By contrast targeting under recovery charges at entry points can have the affects of making Europe a less attractive market for outside suppliers.

**2.3.4 Do you agree with application of the proposed options for setting reference prices to all entry and exit points (without any separate mechanism for the domestic points, whilst ensuring no discrimination between domestic and cross-border network usage)?**

Yes. This is an essential prerequisite for removing distortions in tariffs applied to domestic and cross border flows. Ultimately it is about all EU citizens bearing a fair share of the transportation cost for delivery of their gas, which clearly relates to physical location of consumption but the overall pattern of use and flow across all EU transmissions systems. In this context it is not appropriate for member states to favour domestic flows, especially if the infrastructure investment has been secured on the back of transit flows.

This measure combined with equivalence in terms of entry and exit revenue recovery will help to remove the ‘pancaking’ of charges which inevitably leads to discrimination against long distance gas flows. This proposal offers a major step to placing all sources of supply irrespective of their origin on level footing.

**2.4. Pricing of entry- and exit capacity on the transmission network to and from gas storage facilities (see also questions under ‘9’ Locational signals).**

**2.4.1 Do you agree with proposed option to base tariffs for entry and exit capacity on the transmission network to and from gas storage facilities at an adequate discount to other entry and exit points on the TSO?**

Yes provided this can be objectively justified on the basis of benefits to relevant transmission systems, e.g. reducing the need for investment in pipeline infrastructure. It will be important to ensure discounts are not paid to users if gas is not delivered into or off taken from the system when required for system support.

**2.4.2. Do you agree with harmonization of such a discount across all storage points in the EU?**

No because the level of system support provided by storage (or indeed other classes of user) may vary depending on the configuration of a particular transmission system and the prevailing patterns of flow on that system.

It might be possible to mandate a minimum and or a maximum discount to be applied but that would appear to be arbitrary. In our view it would be better and inherently more cost reflective to determine an absolute value to be credited to individual storage facilities based on the benefits that the storage facility brings to system, but applicable only if actual network support has been provided.

**2.4.3 If you prefer harmonization for an ‘adequate’ discount, which level of such a discount applied to firm capacity level do you advocate?**

We do not advocate any particular level of discount. See our response to 2.4.2 above.

**2.4.4 What are your views on harmonization of tariff measures, leading to harmonization of transmission tariff levels across all storage points in the EU (instead of harmonizing a discount across all storage points in the EU)?**

The level of tariffs depends on the nature of and patterns of flows on the transmission system to which it is connected to, and the impact such facilities has on the interconnected transmission systems across the EU. Storage facilities and other forms of flexibility in one zone can provide system support across neighbouring zones for example.

In this context it is difficult to see what harmonisation of tariff levels across all storage points in the EU means in practice. Tariffs need to be considered on a case by case basis. Setting the same absolute levels of tariff would result in an inappropriate socialisation of costs, and would introduce a major market distortion.

**3. Revenue recovery (Chapter 3 of the draft Framework Guideline)**

**3.1 General – interdependency questions.**

**3.1.1. Do you agree that the current draft FG proposals on Reserve prices for short term products, on revenue recovery and on payable price are consistent together?**

The proposals are broadly consistent. The proposals provide sufficient scope for the TSOs and the relevant NRAs to establish tariffs to guard against significant revenue under-recovery, which would have otherwise been the case if TSOs were permitted to set multipliers at less than one.

**3.1.2 Are the current draft FG proposals on Reserve prices for short term products, on revenue recovery and on payable price properly addressing the ambition for the pricing of transmission capacity to strike the right balance between facilitating short-term gas trading on one hand and providing long-term signals for covering costs and promoting efficient investments on the other?**

In our view the right balance has been struck. Short-term trading will not be harmed and could well be enhanced as long-term capacity holders will be able to offer any unused capacity on the secondary market for a fairer price.

By ensuring there are appropriate signals to acquire long-term capacity the risk of revenue under-recovery is much reduced, but not eliminated altogether. Long term investment signals will be enhanced helping to ensure system integrity and improvement. It is also important that distortions and volatility of tariffs due to measures to recover lost revenue are also avoided by ensuring that the right level of revenue is raised in the first place.

A low multiplier regime leading to significant under-recovery would have in our view led to unfair and discriminatory tariffs that would hinder cross border trade and thus further market integration.

**3.2 Regulatory account**

**3.2.1. Do you agree with the principle to set reference prices to minimise the difference between allowed and collected revenues?**

Yes because it is important to ensure transportation costs are charged to users during the period in which the charges relate. Nevertheless, should there be significant revenue under or over-recovery it may be appropriate to smooth adjustments over a number of years.

In our view it is always better to seek to set reference prices at a level that is most likely to ensure a minimum difference between allowed and collected revenues in the first place. In our view this is more likely to require a multiplier closer to an average of 1.5, given users of short term capacity will necessarily profile their usage over the year.

ACER should recognise that there is no “cost free” way to compensate for revenue under recovery. Adjusting capacity tariffs means that only those who book capacity are likely to be affected by such charges. Inevitably this means those shippers who have either already booked capacity for future years or who will be booking capacity in future years. Those shippers, such as short term traders who only book capacity in the very short term to take account of price differentials between markets are less likely to book capacity in future years, as the increase in capacity costs will make the market price differentials less attractive and hence traders will not need to book capacity. Recovering lost revenue via capacity charges also increases the volatility of uncertainty of capacity charges making it less likely that all shippers will wish to book capacity long terms as they will not know what the price will be in future years.

A commodity charge will affect all shippers who flow gas and will therefore capture those who only book capacity short term, such as traders, as well. However the same problems of uncertain capacity tariffs occur. It also means that those shippers who booked capacity at the full regulated price or greater (as a result of any auction premium) will end up paying more again for their capacity via the commodity charge. Those who booked capacity at a discount or for nothing will only be paying that discounted price plus the commodity charge and therefore will benefit.

**3.2.2. Do you agree with proposed level of harmonization of using the regulatory account?**

It provides the right steer for TSOs and NRAs whilst at the same time providing some flexibility to find local solutions to manage the relevant regulatory account.



**3.2.3 Do you agree that NRAs should determine or approve how often and how fast the regulatory account has to be reconciled on a national level, whilst preserving balance between timely cost recovery and sudden adjustments to tariffs?**

We would prefer a common approach so that changes to tariffs are coordinated. In normal circumstances we would like to see adjustments in the year immediately following the year being reconciled. Up to three years could be allowed in the cases of significant over or under recovery, but this should be the exception rather than the rule. In some cases large and sudden adjustment may be unavoidable. The key point here however is to ensure complete transparency of regulatory accounts so that market participant can reasonably predict the likely changes.

However the problem remains that if an under recovery occurs in Year 1, and this shortfall is made up by increasing charges in Year 2, there is a risk that those shippers who caused the revenue shortfall in Year 1, may not be booking capacity in Year 2, and therefore will not be bearing their fair share of the costs of using the system. This is likely to be the case for traders who book capacity when market differentials make it worthwhile to do so, and will decrease their bookings as capacity costs rise relative to differences in market wholesale gas prices.

**3.2.4 What is your view on including the option to use the Regulatory Account (including the potential over-recoveries from auction premium) to contribute to solving congestion? How could this be done, especially in view of principles of non-discrimination and cost-reflectivity? Please give reasons for your answer, including any quantitative evidence, tables and examples.**

The problem with such an approach is that it can lead to one shipper paying the reference price for capacity plus an auction premium in Year 1, and another shipper paying only the reference price in a later year because the TSO has used the auction premium to create new capacity and therefore enabled supply and demand for capacity to match preventing the emergence of any auction premium. Essentially this acts as a cross subsidy from the first shipper to the second. It also raises the question of potential revenue over recovery by the TSO if the reference price paid by the second shipper equals the costs of the new capacity. If this is the case the auction premium revenue will mean the TSO will over recover.

However the use of auction premia could be used as part of an incentive mechanism for over selling and buy back of capacity. If such an incentive mechanism reduced costs to shippers then this would help justify the use of the auction premia in this way, although it would not necessarily directly compensate the first shipper who had paid the auction premium in the first place. Nevertheless we see little chance of there being a substantial pot of money available for this purpose as the bias in most entry-exit zones is still likely to be toward under rather than over-recovery.

Providing a mechanism to allow the TSO to pro-actively manage congestion where there are surplus congestion rents in a given entry exit zones seems appropriate. It would permit better optimisation and access to firm capacity that might not otherwise be available.

**3.3. Reconciliation of Regulatory accounts.**

**3.3.1 Which option for the reconciliation of regulatory accounts do you prefer?**

Please see our response to 3.2.1 on the different problems associated with the capacity and commodity approaches.

**3.3.2 In line with the interdependency discussion above in question 3.1, what are your views on recovering revenues by means of a separate charge set at the start of the gas year with the aim of minimising the amount that goes into the regulatory account?**

A separate one off charge at the start of the gas year would not be appropriate. It is important that any adjustments are reflected in the setting of ex ante charges typically applied in the following year. Passing-on charges to customers is difficult enough as it is but passing on a large one of ex post reconciliation charge is unreasonable.

**3.3.3 Do you agree with application of the option on reconciling regulatory account to all entry and exit points (both domestic and cross-border)?**

Yes. Seeking to target adjustments to particular entry or exit points may appear more cost reflective, but the knowledge of such a targeted charge would inevitably distort bidding behaviour in the first place. Given this there seems little option but to socialise the adjustments across all users in the relevant entry exit zone.

**3.3.4. Do you agree that the regulatory account should be recovered by splitting the total under- or over- recovery across all entry and exit points in the same proportion as set out in the cost allocation methodology?**

Please see our comments above that any under recovery of revenue should be targeted at exit charges as this is the most effective way of ensuring that the cost of transporting gas is borne by those who consume the gas.

**4. Reserve prices (Chapter 4 of the Framework Guideline)**

**4.1. General.**

**4.1.1. Do you consider it sufficient to have rules on firm, interruptible and non-physical backhaul capacity products or are you aware of other capacity products that should be addressed in the FG?**

Yes.

**4.2. Reserve prices (firm)**

**4.2.1. Do you agree with proposed level of harmonization?**

Yes.

**4.2.2. Do you agree with proposed option for the Reserve price for short-term products including the possibility that the national regulatory authority may decide to allow for higher short-term prices that may apply (via multiplier higher than one, but not higher than 1.5) if there is risk of *significant* under-recovery of allowed revenues?**

Yes. However, given the potentially damaging distortions arising from a significant under recovery of allowed revenue (described more fully in our responses above) we believe it would be more appropriate for the relevant NRA should require the TSO to apply a multiplier greater than one in such circumstances. It seems prudent to design in a reset possibility to amend the level of the maximum multiplier in the light of several years' operation of this mechanism. It would be most appropriate for ACER to do this at an EU wide level in conjunction with ENTSOG and all relevant stakeholders.

**4.2.3. Do you agree with application of the proposal on short-term Reserve prices to entry and exit points where the Network Code on CAM applies, i.e. interconnection points only?**

Yes the purpose of the arrangements is to facilitate cross border trade and market integration as defined in the Third Package, and not impinge of matters reserved for member states. Applying short term reserve prices beyond the interconnection points set out in CAM would seem to be out of scope at this stage.

**4.2.4. What criteria would you propose to set the Reserve price for short-term products that will be higher than the price of an annual product, to interconnection points?**

Clearly one would have to base and fine tune the level of reserve prices based on recover of revenue from short-term products in previous years. The scope for under-recovery is likely to vary with seasonal patterns of flow at particular interconnection points and it would seem reasonable to use the historical profile to identify which months or seasons require a reserve price higher than one.

**4.2.5 Would you agree with using Seasonality (or other criteria, which you may suggest) of the systems as criteria to set the Reserve price for short-term products that will be higher than the price of an annual product, to interconnection points?**

Yes – see above

**4.3. Reserve prices (interruptible)**

**4.3.1 Do you agree with proposed option to set Interruptible Reserve prices at a discount to firm capacity where the discount is based on the likelihood of interruption, and to recalculate once a year?**

In principle yes, but this is difficult to determine in practice. As a minimum charges for interruptible should cover at least the variable cost of providing such capacity.

**4.3.2. If you prefer a fixed discount, which level of such a discount applied to firm capacity level do you advocate?**

It would seem to appropriate to define the number of days of likely interruption per year, and base the saving on incremental investment avoided.

**4.3.3. Do you agree with application of the proposed option to entry and exit points where the Network Code on CAM applies, i.e. interconnection points only?**

**4.4. Reserve price (backhaul)**

**4.4.1. Do you agree with proposed level of harmonization?**

No. Backhaul is a function of the fact that infrastructure is built to reflect expected flow patterns at the time it was built; it will never precisely reflect the way in which the infrastructure is actually used. It is clear that over time, as more sources of supply are discovered and accommodated, be that indigenous supplies, imports of pipeline gas or LNG then the dynamics and costs of delivering the gas to customers will change. It must be considered that during periods when back-haul is significant then the impact on revenues could also be significant if discounts are applied. This leads to problems identified previously. We are uncomfortable with any proposition which may have revenue implications. One important consideration is which parties receive the revenue from backhaul services. As backhaul only exists as because of forward flows of shippers it is right that those shippers receive a share of the benefits of the backhaul capacity revenue via reductions in the charges. A 50:50 sharing between forward flow shippers and the relevant shippers seems reasonable in this regard.

ACER should also consider how backhaul differs from interruptible flows in an entry exit context. As backhaul is only possible whilst there is an opposite flow of gas (forward flow), the firmness of backhaul is therefore dependent on such forward flow. Therefore one solution would be to treat backhaul in the same way as interruptible i.e. if there was no chance of interruption because of the scale of the expected forward flow of gas, then backhaul should pay the same charges as forward flow. However the average tariff for shippers, both forward flow and backhaul, would be lower in this case to prevent revenue over recovery by the TSO.

**4.4.2 Do you agree with proposed option to set backhaul prices at a discount to firm capacity level so that Reserve prices reflect the level of actual marginal costs (= IT and administrative costs)?**

No – see response above.

**4.4.3 Do you agree with application of the proposed option on backhaul capacity pricing to entry and exit points where the Network Code on CAM applies i.e. interconnection points only?**

As noted above ACER should consider how backhaul differs from interruptible capacity given its dependence on forward flow of gas.

## **5. Virtual IPs**

**Do you support the proposed option for Reserve price in Virtual IPs as EU-wide standard? Please reason your answer, including any quantitative evidence, tables and examples on balance between cost-reflectivity and cross border trade stimulation.**

The merger and bring together of entry and exit points can lead to an inappropriate socialisation of tariffs, for example where there are very different costs associated with component entry-exit points of a virtual IP. More detailed consideration needs to be given to the issue of Virtual IPs before setting firm guidelines.

## **6. Bundled capacity products**

### **6.1. Reserve price (Bundled)**

#### **6.1.1. Do you agree with proposed level of harmonization?**

Yes – the degree of harmonisation seems appropriate. It will be important to ensure that the tariffication methodologies established in the entry-exit zones on each side of the interconnection point are similar in approach otherwise the reference prices on which the reserve prices are based may inadvertently result in an inappropriate allocation of revenues between TSOs in different member states.

#### **6.1.2 Do you agree with the proposed option that the sum of Reserve prices for unbundled capacity is used as bundled Reserve price?**

Yes - this seems a reasonable approach provided there is compatibility between charging methodologies on each side of the interconnection point.

#### **6.1.3. Do you agree with application of specified the proposal to entry and exit points where the Network Code on CAM applies i.e. interconnection points only?**

Yes.

**6.2. Do you support the proposed option for Reserve price (if unbundled) as the EU-wide standard? Please give reasons for your answer, including any quantitative evidence, tables and examples on balance between cost-reflectivity and cross border trade stimulation. We encourage you to specify if you support the Unbundled Reserve price being higher to support bundling of products.**

Yes.

**6.3. The Network Code on Tariffs shall specify that the revenues from Reserve price of bundled capacity products shall be attributed to the TSOs proportionally to the Reserve prices of their respective capacities in the Bundled Capacity. The revenues from the auction premium from bundled capacity above the Reserve price shall be split according to agreement between the relevant national regulatory authorities. Furthermore, the Network Code on Tariffs shall in the**

case that no agreement is concluded before the auction, specify that the revenues from the auction premium shall be split equally between the TSOs.

**6.3.1. Do you agree with proposed level of harmonization in that approach above?**

Yes - this seems a reasonable approach provided there is compatibility between the tariffication methodologies on each side of the interconnection point.

**6.3.2 Do you agree with proposed option for splitting auction revenues from bundled products to the relevant TSOs?**

Yes provided there is compatibility between the tariffication methodologies and the approach taken by TSOs on either side of the border is to, in good faith, seek to minimise the differences between allowed and collected revenues of their respective entry-exit zones. The setting of reserve prices for commercial gain i.e. seeking to capture an unwarranted greater share of revenues by one TSO compared to the other needs to be avoided. There will need to be full and active oversight by the respective NRAs and ACER of the tariffication methodologies used to set reference prices and the justification for setting multipliers at a level greater than one. There should be full transparency as to how auction revenues are split and such information should be published on an annual basis.

This transparency is important so as to ensure the right pressure is brought to bear on relevant TSOs and NRAs if there is an apparent unfair allocation of revenues between TSOs or between member states. This would help avoid the need for an (opaque and complex) inter TSO compensation mechanism along the lines of that established in electricity.

**6.3.3. Do you agree with application of the proposal to entry and exit points where the Network Code on CAM applies i.e. interconnection points only?**

Yes.

**7. Payable price**

**7.1.1. Do you agree with proposed level of harmonization?**

Yes – we agree that the approach for determining the payable price should be the same for all interconnection points. However we fundamentally disagree that price payable should change from the price envisaged at the time of auction, as this will discourage shippers from making any long term bookings of capacity.

**7.1.2 Do you agree with the proposed option to set payable price equal to the current Reserve price for year in which capacity is used plus any premium?**

No - a fundamental reason for purchasing long term capacity rights is to fix prices. Fixing prices is one positive incentive for purchasing long-term capacity (and is a feature of the GB entry capacity auctions). This proposal introduces substantial price uncertainty, not only from underlying changes in entry or exit costs but also from potential adjustments arising from revenue under-recovery.

There may be a logic in indexing the original auction prices to account for inflation but we do not believe adjustments to the payable price by uplifting the reserve price to account for revenue under-recovery is justified.

**7.1.3 Do you agree with the application of specified options regarding payable price to entry and exit points where the Network Code on CAM applies i.e. interconnection points only?**

Yes.

**8. Incremental capacity (no explicit chapter in draft FG, implications at least to chapters 2/3 foreseen).**

**8.1 Please provide evidence of concrete problems with the current arrangements for incremental capacities, whereas these problems affect tariff structures in EU. Any quantitative evidence, tables and examples (if necessary, subject to confidentiality) are welcomed.**

Lack of certainty of the price payable for capacity combined with the inability to modify the quantity of capacity to be booked, was a major problem in the Ruhrgas Open Season held in 2008.

**8.2. Please therefore consider if harmonization, or partial harmonization of any parameters in the “market test” is appropriate within Tariffication principles at EU-level?**

As noted in our response to the recent CEER consultation on market based mechanisms for new capacity, it is not possible to harmonise the market test parameters because of the need to take into account a variety of local factors.

**8.3 Are there any other elements required in the Network Code on transmission tariff structures, to accommodate incremental capacity offer (e.g. influence on regulatory accounts, regulatory periods length, requirement for a fixed for period of years tariffs).**

The key elements required to enable the offer of incremental capacity are as follows:

- Minimizing cross subsidies between those who book capacity long term and those who book capacity short term as a result of revenue under recovery
- Clarity of the calculation and evolution of capacity tariffs
- Certainty of capacity tariffs (for example by minimizing revenue under recovery).

**9. Usage of locational signals (no explicit chapter in FG, implications at least to chapters 2/3/4 foreseen).**

**9.1. Please provide evidence of concrete problems with the current arrangements for locational signals. Any quantitative evidence, tables and examples (if necessary, subject to confidentiality) are welcomed.**

**9.2 Are there any other elements required in the Network Code on transmission tariff structures to accommodate locational signals?**

Locational cost differentials should be used in the setting of entry and exit prices (both reference and regulated prices). The locational signals allow system users to take account of the respective costs of routing gas flows and making choices as to where they connect to the system. As such this approach offers significant benefits in promoting efficiency in the operation and development of transmission systems. Tariff methodologies that fail to provide the right locational signals or worse still simply socialise cost on a uniform basis will increase costs for EU citizens as a whole.

**9.3. Please consider whether the chapter on ‘Reference price’ should have more options added in regard to use of locational signals. Please consider specifically how tariff structures can be used to signal investment for e.g. gas-fired power plants, storages, LNG terminals, etc.**

Locational signals are appropriate in terms of the benefits particular users might bring to the system in terms of reducing operational costs and/or avoiding network investment (compressors and pipelines) that might otherwise be necessary. This is about ensuring the gas flow changes happen in the right place, in the right quantity at the right time.

**9.4. Shorthaul as a form of ‘locational signal’ in e/e systems.**

**9.4.1. Should the FG have a tariff structure in place to avoid the incentive for inefficient building of pipelines (to avoid the entry-exit system charges) described above?**

Yes – this is self-evidently the right thing to do and something that should be pursued. It is an essential measure that seeks to address a weakness inherent in all zone based charging approaches.

**9.4.2. How could this tariff structure be designed?**

Please refer to the details of the GB shorthaul tariff as an example of one suitable tariff design.

**9.4.3. Should there, in order to address risk of cross-subsidies and discrimination - be a limitation on the capacities that can be “shorthaul capacities”?**

We make no comment on the expert advice other than to say that provided there is unutilised capacity available to accommodate the additional load, setting charges at a level that ensures there is a contribution to fixed costs of the transmission system may be appropriate.

**9.5. Specific treatment of LNG (if any) considered, in view of considering specific storage treatment (see questions under 2.4).**

**9.5.1. Do you think that tariffs for entry and exit capacity from the LNG terminal could incorporate a discount relative to other entry and exit tariffs on the TSO, similar to the proposed option for underground gas storage?**

No – a LNG terminal is in essence no different to a standard pipeline entry terminal. Storage is very different as it provides the system with flexibility and can only serve a specific location. An LNG terminal competes with LNG terminals across the globe and it cannot be guaranteed that it will deliver gas into the network at peak times (noting that it is the supply of gas at peak times which will tend to determine capacity charges).

**10. Effects Entry-Exit Zone mergers & Virtual IPs (no explicit chapter in FG, implications at least to chapters 2/3 foreseen).**

**10.1 Please provide evidence of concrete problems with the current arrangements for mergers of entry-exit zones at national level.**

The recent merger of German entry exit zones led to TSOs restricting the quantity of firm capacity rights availability to shippers compared to their holdings at the old interconnection points between the non merged entry exit zones.

**10.2. Please advise, if there are alternatives or additional requirements within Tariffication setting harmonization steps, to accommodate ‘Effects Entry-Exit Zone mergers’ (once there). Please consider the Initial (draft) Impact assessment, when answering.**

We would welcome a specific workshop on this issue so that TSOs can explain the issues they face when entry exit zones are merged in relation to the problem identified in 10.1 above, and any other technical issues which arise from merging zones.

**11. What additional tariff structure measures do you envisage could improve the network code?**

Incentives rewarding TSOs for the overselling of capacity at interconnector points (the preferred solution set out in the CMP) are essential to ensuring the success of this approach, and to avoid the unnecessary restriction of re-nomination rights. TSOs should be permitted to keep a share of the additional revenue from the release of additional capacity over and above their normal allowed revenue. They may have to accept a share of any buy-

back costs but the majority of these balance costs would most likely have to be borne by the users of the interconnected entry exit zones.

**12. Please share below any further comments concerning the draft Framework Guideline.**

GM&T is very concerned in the way that ACER appeared to change its interpretation of the CAM FG at the very end of the Network Code drafting process; this in effect meant that certain measures which ACER wanted included in the CAM Network Code were not properly considered and discussed during the drafting process. Such last minute uncertainty should be avoided during the drafting of the Network Code for tariffs. In particular ACER should ensure that it is fully engaged at all times during the drafting process, and raises any concerns it may have as early as possible to ensure they can be properly discussed and evaluated.

**13. Please comment on any factual incorrectness of the attached Initial (draft) Impact Assessment, if possible with specific page references, including quantitative evidence, tables and examples from your experience in the gas market(s) (if necessary, subject to confidentiality).**