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European Union Agency for the Cooperation
of Energy Regulators

Agency Report

Analysis of the Consultation Document on the Gas Transmission Tariff Structure for Lithuania

NRA: Valstybinė energetikos reguliavimo
taryba (National Energy Regulatory
Council)

TSO: AB Amber Grid

16 April 2021

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1. ACER conclusion

- (1) The Lithuanian National Regulatory Authority ('NRA'), *Valstybinė energetikos reguliavimo taryba* ('VERT'), proposes a postage stamp reference price methodology ('RPM') with a 24-76 entry-exit split¹ for the regulatory period 2022-2023. VERT proposes to apply a discount of 75% to the entry at the Lithuanian LNG terminal. A commodity-based transmission tariff would be used to recover the TSO's variable costs mainly driven by flows (90-10 capacity-commodity split). VERT performs two kinds of asset cost splits: one for the regional networks² and another one for the transit from third country to third country³. Given this situation, VERT proposes several provisions modifying the usual postage stamp RPM:
 - The assets of the primary network and of the regional networks are identified and valued separately. The costs of the regional networks are exclusively allocated to domestic consumers.
 - The district of Kaliningrad would be supplied from Belarus by dedicated point-to-point products.
- (2) The Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR') foresees a cost allocation assessment ('CAA'⁴) to assess the impact of the RPM on cross-subsidisation. The results of the CAA without modifications is 116%, which is well beyond the 10% threshold foreseen in the Article 5 of the NC TAR. This deviation is caused by the asset-cost splits applied by VERT: The result of the CAA is 4.5% if the regional networks and the transit assets are excluded from the calculation.
- (3) The NC TAR also foresees a comparison of the proposed RPM with the capacity weighted distance ('CWD') methodology. In this comparison, VERT did not apply any asset-cost split or adjustment. As a result, the tariffs applied to the Klaipėda LNG entry and to the entry (Kotlovka) and exit (Šakiai) capacity products used for transit would be approximately three times as high, while the tariffs applied at domestic exits would be half the price compared to the tariffs proposed in the RPM. Except for the tariff at the LNG entry, the proposed RPM is more cost-reflective than the CWD methodology (thanks to the various asset-cost splits).
- (4) The consultation document published by VERT takes into account several recommendations issued by the Agency in its report on the previous Lithuanian consultation. VERT shared with the Agency useful information to substantiate the cost-reflectivity of its RPM.
- (5) The Agency, after having completed the analysis of the consultation document pursuant to Article 27(2) of Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR'), concludes that:
 - The consultation document contains all required information listed in Article 26(1) of the NC TAR;

¹ This entry-exit split is calculated taking into account all the adjustments and the asset-cost splits applied by VERT in the RPM. However, the initial entry-exit split, used as an input to the RPM, is 70-30.

² The Lithuanian TSO operates both a primary network and a regional network (high pressure distribution branches). This regional network is labelled as local or secondary network in VERT's public consultation document, to avoid any confusion with the regional market integration process involving Latvia, Estonia and Finland.

³ To transport gas from Belarus to the Kaliningrad district of the Russian Federation.

⁴ Throughout this document, 'CAA' is used to refer to the cost allocation assessment index described in Article 5(3)(c) of the NC TAR.

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- The simplified tariff model is in line with the requirements of Article 30(2)(b) of the NC TAR;
 - Network users would be able to reproduce and forecast the reference prices using the tariff model provided in the consultation document;
 - The risks of undue cross-subsidisations and the volume risks are efficiently mitigated by the asset-cost splits applied by VERT.
- (6) However, given the complexity of this RPM which is significant departure from a usual postage stamp RPM, clearer legal arguments would be necessary for the Agency to be able to confirm that the RPM is compliant with the requirements set out in Article 7 of the NC TAR, that the same RPM applies to all the points in the Lithuanian system and that there is no discrimination among domestic consumers.
- (7) The Agency was also unable to decide whether the mechanism used to compensate the discount granted to Klaipėda LNG is in line with the NC TAR due to the lack of a proper description and legal justification in the public consultation document.
- (8) The Agency recommends that, in its final decision, VERT take into consideration the following:
- Additional transparency (detailed break-down of the regulated asset base and of the allowed revenue) should be provided to demonstrate the cost-reflectivity of the tariffs of the cross-border capacities from Belarus to the Kaliningrad district and of the domestic exits on the regional networks (to the Achema plant and to the other domestic consumers).
 - VERT should provide a clearer legal base to demonstrate that singling out the Achema plant from the other domestic exit is not discriminatory. In particular, VERT should demonstrate that the unit costs of this specific exit stand out in comparison with the other regional branches to justify a specific tariff treatment. VERT should also clarify on what criteria it would base its decision if another consumer requested to be excluded from the equalisation.
 - VERT should explicitly describe in its tariff decision the mechanisms used to compensate the discount granted to Klaipėda LNG entry based on Article 9 of the NC TAR. The legal base for these mechanisms⁵ should as well be clarified. This could provide the necessary legal clarity the Agency misses at this point.

⁵ For instance a rescaling adjustment, as described in Article 6(4) of the NC TAR

2. Introduction

- (9) Commission Regulation (EU) 2017/460 of 16 March 2017 establishes a network code on harmonised transmission tariff structures for gas ('NC TAR').
- (10) Article 27 of the NC TAR requires the Agency to analyse the consultation documents on the reference price methodologies ('RPM') for all entry-exit systems⁶. This Report presents the analysis of the Agency for the transmission system of Lithuania.
- (11) On 17 December 2020, VERT forwarded a consultation document to the Agency proposing an RPM for the Lithuanian transmission system for the period 2022-2023. The consultation was launched on 16 December 2020 and remained open until 17 February 2021. On 10 March 2021, the consultation responses and their English summary were published. The Agency has taken these into consideration for this analysis. Within five months following the end of the final consultation, and pursuant to Article 27(4) of NC TAR, VERT shall take and publish a motivated decision on all the items set out in Article 26(1) of the NC TAR.
- (12) VERT had already carried out a public consultation based on the NC TAR and published a decision in 2019 for the period 2020-2023. The commissioning in 2022 of the Lithuania-Poland gas pipeline (GIPL) and the creation of a new interconnection point (Santaka IP) made necessary a new public consultation to update the previous decision. Besides including GIPL, the main evolutions proposed in the new public consultation document relate to a lower commodity charge and to the implementation of two categories of domestic exit tariffs.
- (13) This Report discusses both the RPM and the accompanying information published in the public consultation document, and the new information provided by VERT during bilateral discussions.

Reading guide

- (14) Chapter 3 describes and assesses the proposed reference price methodology. Chapter 4 presents the analysis on completeness, namely whether all the information referred to in Article 26(1) of the NC TAR has been published. Chapter 5 focusses on compliance, namely whether the RPM complies with the requirements set out in Article 7 of the NC TAR and whether the criteria for setting commodity-based transmission tariffs as set out in Article 5(2) are met. The document contains two annexes, respectively on the legal framework and a list of abbreviations.

⁶ With the exception of Article 10(2)(b), when different RPMs may be applied by the TSOs within an entry-exit zone.

3. Assessment of the proposed reference price methodology

3.1 Description of the proposed RPM

- (16) To design its RPM, VERT has to take into account several specificities of the Lithuanian transmission system:
- AB Amber Grid owns and operates both a primary transmission network⁷, connected to networks of other countries and to other major gas infrastructure such as the Klaipėda LNG terminal, and a regional transmission network⁸ solely dedicated to supply gas to Lithuanian consumers (called secondary or local in the consultation document to avoid any confusion with the on-going regional market integration process involving Latvia, Estonia and Finland) .
 - The primary transmission network is a gas ring allowing several flow patterns, as gas can enter Lithuania at the Kotlovka entry point from the East (from Russia through Belarus), at the Kiemėnai entry point from the North (Latvia), at the Klaipėda entry point from the West (connection with the LNG terminal), and at the Santaka entry point from the South (Poland). A major part of the current transmission network assets was built for diversification and security of supply purposes.
 - Due to its geographic position, a part of the Lithuanian transmission network is used both to supply Lithuanian consumers and to transit Russian gas from Belarus to the Kaliningrad district of the Russian Federation.
 - Latvian, Estonian and Finnish NRAs and TSOs are involved in the regional market integration process FINESTLAT⁹. Discussions are on-going between the relevant authorities to agree under what conditions Lithuania could join and VERT has already taken into account some elements of this regional integration process in its proposed RPM¹⁰.

⁷ 1476 km of pipes whose diameters range from 150 to 1200 mm

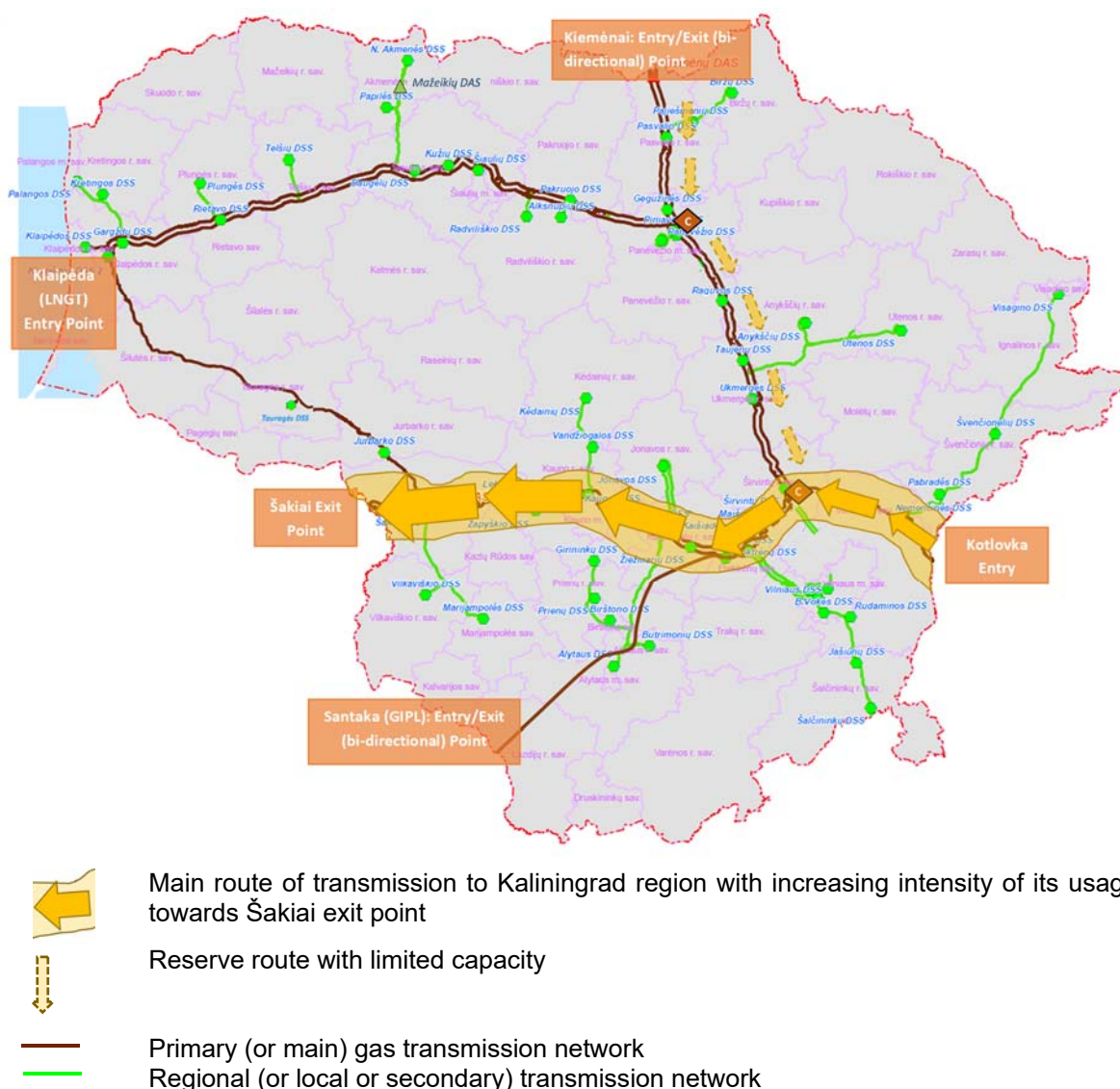
⁸ 802 km with 65 gas offtake points

⁹ The FINESTLAT market zone is established gradually: Latvia and Estonia implemented a common market zone in 2020. Finland plans to join the single market zone in 2022.

¹⁰ The tariff (the reference price applied to the firm capacity) applied to the Kotlovka entry point, connecting Lithuania to Russia through Belarus, is equal to the entry tariff applied to Russian gas in the FINESTLAT region. A discounted tariff is however applied at the same point to the "restricted" entry capacity used to flow gas to the Kaliningrad region.

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Figure 1: Map of the Lithuanian transmission system



- (17) These specificities lead VERT to propose a postage stamp reference price methodology with a 90-10 capacity-commodity split, and with a set of significant adjustments:
- While all the commodity revenue is collected at exits, a 70-30 entry-exit split is used as an input to allocate the capacity revenue. However, once all adjustments and asset-cost splits are applied, the proportions are reversed with an actual entry-exit split of 24-76.
 - VERT proposes to apply a 75% discount at the entry point from Klaipėda LNG terminal.
 - Two asset splits allow to isolate and to allocate to the relevant users the costs induced by, on the one hand, the regional network (i.e. high pressure distribution branches) and on the other hand, the transit flows towards the Russian district of Kaliningrad.

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Table 1: Breakdown of the Lithuanian TSO's expected allowed revenue in 2022.

M€	Estimated allowed revenue in 2022	Share of revenue for capacity based tariffs	Share of revenue for commodity based tariffs
Total TSO's allowed revenue	47.9	43.1	4.8
Primary network	31.4	26.6	4.8
• <i>Intra-EU transmission</i>	<i>21.0</i>	<i>18.5</i>	<i>2.4</i>
• <i>Cross-system use (transit to Kaliningrad)</i>	<i>10.4</i>	<i>8.1</i>	<i>2.3</i>
Regional network	16.5	16.5	0

3.2 Distinction between primary network and regional networks

- (18) In contrast to the current period, when the use of regional networks is classified as a non-transmission service, VERT proposes to reclassify their use as a transmission service. VERT identifies separately the costs of the primary network and of the regional network. VERT proposes to allocate the regional network costs entirely to the respective groups of regional network users.
- (19) VERT provided additional information during the bilateral exchanges with the Agency to substantiate the cost-reflectivity of the proposed RPM. In particular, VERT shared a detailed breakdown of their forecasted regulated asset base and allowed revenue in 2022, allowing the Agency to better understand the amounts published in VERT's simplified tariff model.
- (20) On a total forecasted regulated asset base (RAB) of 281.9 M€ in 2022, the values of the primary and regional networks will be 228.3 M€ (81%) and 53.6 M€ (19%).
- (21) The total allowed revenue of the TSO, amounting at 47.9 M€, is similarly divided with 31.4 M€ (66%) recovered from the primary network, and 16.5 M€ (34%) recovered from regional networks. Costs that are directly attributable to an asset (e.g. depreciation and remuneration) are allocated either to primary or to regional networks depending on the location of this particular asset in the system. Costs that are not directly attributable to an asset (mostly OPEX) are allocated in proportion to the length of each network category¹¹.

3.2.1 Primary networks, asset-cost split to isolate the costs related to the transit to Kaliningrad

- (22) VERT splits the transmission costs of the primary network between the costs related to the gas transmission within the European Union and the costs related to the transit of gas from Belarus to the Kaliningrad district of the Russian Federation.
- (23) Since the main transit route to the Kaliningrad region (from Kotlovka entry IP to the Šakiai exit IP, see Figure 1) is used both for transit and domestic purposes, the costs of the corresponding assets are split. The closer a section of pipeline is to the Šakiai cross-border exit (and the fewer domestic

¹¹ 1476 km for the primary network, 802 km for regional networks

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consumers connected downstream), the higher the percentage of its cost allocated to transit. More precisely, the split is done in the following way:

- The value of each existing asset on the transit route to Kaliningrad is split proportionally to the peak daily quantities¹² observed in the corresponding section of the route and flowed from this particular section to the Kaliningrad region or to domestic users, respectively;
- For new assets partly dedicated to transit, the split would be decided by VERT in its corresponding decision approving the new investment;
- Some other smaller costs are also partially allocated to the transit to the Kaliningrad region (e.g. a shares of maintenance and engineering costs, taxes and a minor share of the costs of a backup route, etc.).

- (24) According to VERT's calculation, the share of assets used to transit gas to the Kaliningrad region represents 20% (or 56.5 M€) of the total RAB and 22%¹³ (10.4 M€) of the total allowed revenue.
- (25) The tariffs applied to this transit (for the restricted capacity product¹⁴ at the Kotlovka entry point and for the Šakiai exit point) are based on this asset-cost split and on a point-to-point logic (on the basis of Article 7(d) on volume risk and Article 4(2) on conditional capacity of the TAR NC), and does not result from the application of the postage stamp RPM.

3.2.2 Regional networks, separate treatment for the Achema fertilizer plant

- (26) At the level of regional network, VERT differentiates between the main Lithuanian domestic consumer (which is the Achema fertilizer plant) and the other domestic consumers.
- (27) The Achema plant represents 44% of the booked domestic exit capacities, and about 60% of the domestic consumption. According to the documents shared by VERT with the Agency, the domestic exit tariffs applied to the plant are calculated to cover the costs of the regional network branch where the plant is connected (2.9 M€ in the RAB in 2022 inducing 0.6 M€ of allowed revenue)¹⁵.
- (28) Domestic exit tariffs applied to all other domestic consumers are equalised and cover the costs of the other regional network branches (50.7 M€ in the RAB in 2022 inducing 15.8 M€ of allowed revenue).
- (29) The Agency understands that, in practice, this differentiated tariffs applied to the Achema plant and to the other domestic consumers is equivalent to another asset-cost split within the regional assets (already treated separately from the primary network).
- (30) This issue is further assessed in the section 5.1.3.2 of this document.

¹² based on historical medium-term data

¹³ The two percentages differ slightly due to operational expenditures.

¹⁴ Conditional entry capacity which can only be used to flow gas from Kotlovka entry point to the Šakiai exit point

¹⁵ More precisely, 98.3% of the allowed revenue induced by the regional branch (49.3 km), where Achema is connected, are attributed to Achema's domestic exit (in proportion to Achema's share of the estimated annual peak consumption on this branch).

3.3 LNG discount and rescaling

- (31) In accordance with Article 9 of NC TAR, VERT proposes to apply a 75% discount at the entry point from Klaipėda LNG terminal¹⁶.
- (32) In order to compensate the missing revenue created by this discount, VERT rescales the tariffs applied at both domestic and cross-border exits (except the tariffs applied at the Šakiai exit IP to the Kaliningrad region, which is determined by the asset-cost split described in Section 3.2.1).
- (33) Thanks to the explanations provided by VERT, the Agency understands that this rescaling is performed in two steps:
- Ex-ante, the expected missing revenue in year Y+1 is reallocated to all exits in proportion to their respective expected capacity bookings¹⁷;
 - Ex-post, tariffs applied at all exits in year Y+1 are corrected to compensate the gap between the ex-ante rescaling based on the bookings for year Y-1 forecasted in year Y-2 and the correct rescaling based on bookings actually observed in year Y-1¹⁸.
- (34) The consultation document published by VERT does not provide a clear description of this rescaling mechanism (which can nonetheless be partially understood thanks to the simplified tariff model published jointly with the consultation document).
- (35) This complex rescaling mechanism (in particular its second step) explains why, despite applying a postage stamp RPM, the tariffs calculated by VERT differ from one exit of the primary network to another.
- (36) This particular mechanism is further assessed in the section 5.1.3.1 of this document.

3.4 Comparison with the CWD methodology

- (37) VERT provides a detailed comparison of the postage stamp reference prices with those from the counterfactual CWD methodology in Section 5.1.8 of the consultation document. The counterfactual CWD methodology with a 50-50 entry-exit split is applied without the adjustments and the asset-cost splits used by VERT in its proposed RPM.
- (38) This obviously leads to important differences with respect to the proposed RPM; in particular, the tariff at the Klaipėda LNG entry would be approximately three times as high in the CWD counterfactual. More interestingly, the total tariff to transport gas from the Kotlovka entry point (from Belarus) to the Šakiai exit point (to the Russian Kaliningrad district) would be 275% higher (approximately 204 €/MWh/d/y against 75 €/MWh/d/y) as well. The domestic exit tariff resulting from the CWD methodology would be half of the price than the one that is in the proposed RPM. This is

¹⁶ The Lithuanian TSO is also responsible for collecting a security of supply charge from domestic consumers which covers a part of the LNG terminal's costs, as explained in the Agency report "[The Internal Gas Market in Europe: The Role of Transmission Tariffs](#)" on page 44. This security of supply charge is not a part of transmission tariffs.

¹⁷ In 2022, this reallocation will add 55.62 €/MWh/d/y to the tariffs applied at the domestic exit points and at the cross-border exits to Latvia and Poland

¹⁸ In 2022, this ex-post correction leads to the reallocation of 623 k€ from the domestic exits to the Kiemėnai exit IP to Latvia because the LNG entries and the expected bookings at the Kiemėnai were underestimated in 2020 (of approximately 90%) when the ex-ante rescaling was performed. As a result, 46,81 €/MWh/d/y are added to the tariff at the Kiemėnai exit IP, while 6,52 €/MWh/d/y are deducted from the tariff at domestic exits.

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explained by two main factors: more costs would be allocated to the cross-border flows towards the Kaliningrad district, and no rescaling of the domestic exit tariffs is necessary to compensate for discounts granted to the Klaipėda LNG entry.

- (39) Overall, the comparison with the counterfactual CWD methodology is mainly useful for assessing the impacts of the special treatment of transit to the Kaliningrad district and of the 75% discount granted to the Klaipėda LNG entry. Except for this tariff at the LNG entry, the proposed RPM is more cost-reflective than the CWD methodology (thanks to the various asset-cost splits).

3.5 Cost allocation assessment

- (40) VERT calculates the CAA of its postage stamp RPM, using forecasted capacity bookings and flows as cost drivers. Two different results of the CAA are provided.
- (41) For the capacity-based tariffs, the calculation is done by both taking into account and by excluding the transmission to the Russian district of Kaliningrad and to the regional networks. This level of detail allows to assess the impacts of the significant adjustments applied to the postage stamp RPM:
- If the transmission to Kaliningrad and the regional networks are excluded, the result of the CAA is satisfying (4.5%);
 - If the transmission to Kaliningrad and the regional networks are taken into account, the result of the CAA amounts to 116.3%. This result, by far above the threshold of 10% mentioned in the NC TAR, is consistent with the comparison with the counterfactual CWD methodology. They demonstrate that the unit cost to ship gas from Belarus to the Russian district of Kaliningrad is significantly lower than the average unit cost of the primary network.
- (42) A CAA is also calculated for commodity-based tariffs and its result is within the 10% threshold laid out in Article 5 of the NC TAR (0% since the same commodity charge is applied at all exits).

3.6 Main evolutions and comparison with the tariffs for the prevailing tariff period

- (43) Quantitatively, the main differences between the proposed tariffs for 2022 and the currently applied tariffs are observed at domestic exits on regional networks. Indeed, the commodity charge will only be applied on the primary networks (covering 10% of the total allowed revenue). Currently, an additional commodity charge covers 50% of the regional networks costs. This additional charge will disappear in 2022, and will be compensated by an important increase of the capacity-based domestic exit tariffs.
- (44) The new consultation document published by VERT takes into account several recommendations issued by the Agency in its report on the previous Lithuanian consultation¹⁹:
- The same commodity charge is applied to all exits of the primary networks, covering 10 % of total allowed revenue (which is roughly the portion of the costs mainly driven by the quantity of

¹⁹ [Agency Report - Analysis of the Consultation Document on the Gas Transmission Tariff Structure for Lithuania, published on 04/07/2019](#)

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the gas flow). A commodity charge (depending on the size of consumers) is no longer applied on the regional networks;

- The use of regional networks is now considered as a transmission service;
- In addition, the domestic exits capacity-based tariffs do no longer depend on the size of the concerned domestic consumers, which was considered by the Agency as potentially discriminatory. A specific domestic exit point is created for the Achema plant. This setting allows to check that the corresponding exit tariffs reflects the costs induced by the regional branch where the Achema plant is connected (financially, the difference between the tariffs applied to the Achema plant and to other consumers remains however comparable to the current period);
- Formally, there is now a single reference price for the Kotlovka entry point. A discount is applied to the capacities booked to transit gas towards the Kaliningrad region (labeled as restricted capacity product).

(45) The new RPM proposed by VERT remains complex, with a set of specific adjustments applied to particular parts of the network. These adjustments make it difficult to judge whether it is the same RPM that applies to all entry and exit points of the system, as required by Article 6(3) of the NC TAR.

(46) The rescaling mechanism used to compensate the discount applied at the Klaipėda entry point (LNG Entry) would require a more extensive description.

4. Completeness

4.1 Has all the information referred to in Article 26(1) been published?

- (48) Article 27(2)(a) of the NC TAR requires the Agency to analyse whether all the information referred to in Article 26(1) of the NC TAR has been published.
- (49) Article 26(1) of the NC TAR requires that the consultation document be published in the English language, to the extent possible. The Agency confirms that the consultation document was published in English.
- (50) Overall, the information in Article 26(1) of the NC TAR has been properly published.

Table 2 Checklist information Article 26(1)

Article	Information	Published: Y/N/NA
26(1)(a)	the description of the proposed reference price methodology	Yes
26(1)(a)(i) 26(1)(a)(i)(1) 26(1)(a)(i)(2)	the indicative information set out in Article 30(1)(a), including: <ul style="list-style-type: none"> the justification of the parameters used that are related to the technical characteristics of the system the corresponding information on the respective values of such parameters and the assumptions applied 	Yes. However, the Agency considers that additional information should be published to substantiate the complex RPM proposed by VERT.
26(1)(a)(ii)	the value of the proposed adjustments for capacity-based transmission tariffs pursuant to Article 9	Yes
26(1)(a)(iii)	the indicative reference prices subject to consultation	Yes
26(1)(a)(iv)	the results, the components and the details of these components for the cost allocation assessments set out in Article 5	Yes
26(1)(a)(v)	the assessment of the proposed reference price methodology in accordance with Article 7	Yes
26(1)(a)(vi)	where the proposed reference price methodology is other than the capacity weighted distance reference price methodology detailed in Article 8, its comparison against the latter accompanied by the information set out in point (iii)	Yes
26(1)(b)	the indicative information set out in Article 30(1)(b)(i), (iv), (v)	Yes
26(1)(c)(i) 26(1)(c)(i)(1) 26(1)(c)(i)(2) 26(1)(c)(i)(3)	where commodity-based transmission tariffs referred to in Article 4(3) are proposed <ul style="list-style-type: none"> the manner in which they are set the share of the allowed or target revenue forecasted to be recovered from such tariffs the indicative commodity-based transmission tariffs 	Yes
26(1)(c)(ii) 26(1)(c)(ii)(1) 26(1)(c)(ii)(2)	where non-transmission services provided to network users are proposed: <ul style="list-style-type: none"> the non-transmission service tariff methodology therefor 	Not applicable

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<p>26(1)(c)(ii)(3) 26(1)(c)(ii)(4)</p>	<ul style="list-style-type: none"> • the share of the allowed or target revenue forecasted to be recovered from such tariffs • the manner in which the associated non-transmission services revenue is reconciled as referred to in Article 17(3) • the indicative non-transmission tariffs for non-transmission services provided to network users 	
<p>26(1)(d)</p>	<p>the indicative information set out in Article 30(2);</p>	<p>Yes</p>
<p>26(1)(e) 26(1)(e)(i) 26(1)(e)(ii) 26(1)(e)(iii) 26(1)(e)(iv)</p>	<p>where the fixed payable price approach referred to in Article 24(b) is considered to be offered under a price cap regime for existing capacity:</p> <ul style="list-style-type: none"> • the proposed index; • the proposed calculation and how the revenue derived from the risk premium is used • at which interconnection point(s) and for which tariff period(s) such approach is proposed • the process of offering capacity at an interconnection point where both fixed and floating payable price approaches referred to in Article 24 are proposed 	<p>Not applicable</p>

5. Compliance

5.1 Does the RPM comply with the requirements set out in Article 7?

- (51) Article 27(2)(b)(1) of the NC TAR requires the Agency to analyse whether the proposed reference price methodology complies with the requirements set out in Article 7 of the NC TAR. This article refers to Article 13 of Regulation (EC) 715/2009 and lists a number of requirements to take into account when setting the RPM. As the requirements overlap, in the remainder of this chapter, the Agency will take a closer look at the five elements listed in Article 7 of the NC TAR.
- (52) As the concepts of transparency, cost reflectivity, non-discrimination, cross-subsidisation and cross border trade are closely related²⁰ the Agency concludes with an overall assessment. Special attention is paid to the allocation of revenues between domestic and transit routes.

5.1.1 Transparency

- (53) **Article 7(a)** of the NC TAR requires that the RPM aim at ensuring that network users can reproduce the calculation of reference prices and their accurate forecast.
- (54) The consultation document published by VERT is transparent and provides all the information required by the NC TAR. Moreover, VERT shared with the Agency detailed calculations allowing a thorough analysis of the comparison between the chosen RPM and the CWD methodology, of the cost allocation assessment²¹ and of the main components of the allowed revenue. In particular, VERT provided to the Agency a detailed break-down²² of the TSO regulated asset base and of its allowed revenue. This was necessary to assess several specific settings of the RPM²³.
- (55) The Agency considers that the dataset and the simplified tariff model published by VERT allow network users to understand and reproduce the reference prices and their forecast from 2022 to 2023. In addition, network users can change the input variables and input their own assumptions.
- (56) The Agency finds the simplified tariff model in line with the requirements of Article 30(2)(b) of the NC TAR.
- (57) VERT published, on 10 March 2021, the responses to the public consultation and their summary in English. In addition, VERT published its evaluation of these responses, which is considered by the Agency as a best practice.

²⁰ The principle of cost-reflectivity is related to the principles of cross-subsidisation and non-distortion of cross-border trade. Tariffs that are fully cost-reflective do not result in any form of cross-subsidisation (and hence they do not distort cross-border trade), as they charge users for the exact costs they cause to the system. Following this reasoning, tariffs that are less cost-reflective may result in cross-subsidisation between users.

²¹ Throughout this document, 'CAA' is used to refer to the capacity cost allocation comparison index described in Article 5(3)(c) of NC TAR.

²² Forecasted amount for 2022

²³ split between primary and regional networks, costs related to the transit to the Kaliningrad region, costs related to the regional branch where the Achema plant is connected

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- (58) The Agency considers that, given the complexity of its RPM, VERT should publish additional information²⁴ (a break-down of the RAB and of the allowed revenue) to show the cost-reflectivity of the tariffs applied to the transit to the Kaliningrad Region, to the regional networks and to the Achema plant connection and to substantiate these specific settings.
- (59) The Agency considers that VERT should describe in detail in its tariff decision how the loss of revenue caused by the discount granted to the Klaipėda entry point (from the LNG terminal) is compensated by increasing the tariffs applied at exit points.

5.1.2 Cost-reflectivity

- (60) **Article 7(b)** of NC TAR requires the RPM to take into account the actual costs incurred for the provision of transmission services, considering the level of complexity of the transmission network.
- (61) As previously explained, specific asset-cost splits are proposed by VERT to properly reflect the costs induced by the use of the regional network and by the transit of gas from Belarus to the Kaliningrad district.
- (62) Given the information shared by VERT, the Agency considers these settings as cost-reflective.

5.1.3 Cross-subsidisation and discrimination

- (63) **Article 7(c)** of NC TAR requires the RPM to ensure non-discrimination and prevent undue cross-subsidisation.

5.1.3.1 Cross-subsidisation

- (64) For this analysis, the Agency defines 'cross-subsidisation' as a deviation from cost-reflectivity whereby users of the entry-exit system are charged tariffs that differ from the costs they cause to the system. One instrument to evaluate cross-subsidisation is the CAA.
- (65) In its previous report, the Agency requested VERT to explain the important differences between:
- the tariffs applied, on the one hand, to transport gas from Belarus to the Russian district of Kaliningrad and, on the other hand, to other uses of the primary network;
 - the tariffs applied to the Achema plant and to the other domestic consumers.
- (66) The additional information shared by VERT regarding the break-down of the TSO's RAB and allowed revenue satisfied this request.
- (67) Regarding the discount applied to the Klaipėda LNG entry, the Agency finds VERT's approach to be compliant with Article 9 of the NC TAR.
- (68) The first step of the complex rescaling mechanism used to compensate this discount (and described in section 3.3 of this document) is clearly in line with the rescaling adjustment described in Article 6(4)(c) of the NC TAR (since it adds the same amounts to each exit tariff).

²⁴ The Agency issued a [similar recommendation](#) to the Czech NRA, which also applies an asset-cost split in its RPM.

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- (69) However, the Agency could not decide whether the second step²⁵ of this mechanism is in line with the NC TAR because it lacks a proper explanation in the public consultation document. Besides a clear and detailed description, VERT should clarify in its tariff decision the legal base supporting this mechanism.
- (70) The Agency understands from the bilateral exchanges with VERT that the purpose of this second step is to correct undue cross-subsidies between domestic and cross-border users that erroneous capacity booking forecasts could cause (in particular due to the variability of LNG flows). The low level of cross-subsidies seems confirmed by the result of the CAA excluding the transmission to Kaliningrad and the regional networks (4,5%). This mechanism nevertheless increases the complexity of the proposed RPM and the volatility of the exit tariffs (while simplicity and stability are usually the strengths of a postage stamp RPM). VERT should explain how this trade-off is made.

5.1.3.2 Discrimination

- (71) For this analysis, the Agency defines 'discrimination' as 'applying different rules to comparable situations or the same rule to different situations'. The Agency highlights that the allocation of all transmission costs via a single RPM to all entry-exit points minimises the possibility of discrimination.
- (72) In comparison with its previous public consultation document, VERT introduced several changes to mitigate the risk of discrimination:
- A the Kotlovka entry point, the point-to-point product allowing to transport gas across Lithuania to the Russian district of Kaliningrad is now considered as a conditional capacity product and its tariff is set by applying a discount to the reference price;
 - The same commodity charge now applies to all exits.
- (73) The main remaining issue regarding discrimination relates to the exit tariffs applied to the Achema plant. While the information shared with VERT shows that these tariffs are cost-reflective, the legal base for singling out this domestic exit from all others is unclear (a postage-stamp RPM should in theory equalise all exit tariffs).
- (74) The NC TAR states in Art 6(4)(b) that "*equalisation by the transmission system operator(s) or the national regulatory authority, as decided by the national regulatory authority, whereby the same reference price is applied to some or all points within a homogeneous group of points*". It is therefore possible to exclude one domestic exit, like the connection to the Achema plant, from an equalisation.
- (75) Nonetheless, the Agency considers that VERT should substantiate its decision to single out the Achema plant connection and show that it is non-discriminatory. VERT should demonstrate that the unit costs of this specific exit stand out in comparison with the other regional branches to justify a specific tariff treatment. VERT should also clarify on what criteria it would base its decision if another consumer requested to be excluded from the equalisation. Therefore, the Agency recommends VERT's tariff decision to include:

²⁵ See section 3.3, tariffs applied at all exits in year Y+1 are corrected to compensate the gap between the ex-ante rescaling based on the bookings for year Y-1 forecasted in year Y-2 and the correct rescaling based on bookings actually observed in year Y-1.

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- a clearer legal base (the notion of cluster introduced by Article 3(19) of the NC TAR could possibly be useful),
- publishing a sufficiently detailed break-down of the TSO's costs.

5.1.4 Volume risk

- (76) **Article 7(d)** of NC TAR requires that the RPM ensure that significant volume risk related particularly to transports across an entry-exit system is not assigned to final customers within that entry-exit system.
- (77) According to Recital 6 of the NC TAR, it is legitimate to shelter domestic consumers from a cross-border volume risk where a TSO transports significantly more gas into other systems than for consumption into its own entry-exit system. In the Lithuanian case, the cross-border capacity booked to supply the Russian district of Kaliningrad (109 GWh/d in 2022) is indeed higher than the sum of all capacity bookings at other entries (91 GWh/d in 2022).
- (78) Therefore, the Agency agrees that a significant volume risk may theoretically be induced by the major role of cross-border flows in the Lithuanian transmission system.
- (79) Based on this reasoning, VERT proposed to shield the Lithuanian consumers from a potential cross-border volume risk by isolating the costs related to the pipeline route between Belarus and the Russian district of Kaliningrad. The asset-cost split proposed by VERT and the tariffs of the point-to-point capacity products proposed at the Kotlovka entry and at Šakiai exit deriving from this split are compatible with the principle of cost-reflectivity.
- (80) Once again, given the complexity of this calculation and the significant cross-border flows in the Lithuanian system, the Agency considers that VERT should publish the quantitative details of this calculation in an annex to its decision to prove that the principle of cost-reflectivity is respected (in particular the break-down of the regulated asset base and of the allowed revenue).

5.1.5 Cross-border trade

- (81) **Article 7(e)** of the NC TAR requires that the RPM ensure that the resulting reference prices do not distort cross-border trade.
- (82) The Agency considers that the proposed RPM does not unduly distort cross-border trade.

5.2 Are the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) met?

- (83) Article 27(2)(b)(2) of the NC TAR requires the Agency to analyse whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) of the NC TAR are met.
- (84) VERT proposes to apply commodity-based transmission tariffs on the Lithuanian primary network. The commodity-based transmission tariffs would provide 10% of the transmission services revenue. The Agency considers this an appropriate use of the commodity charge.
- (85) The NC TAR allows for two types of commodity-based transmission tariffs: a flow-based charge and a complementary revenue recovery charge. VERT proposes to apply a flow-based charge, to recover costs related to the quantity of gas flow (mostly compressor fuel costs). The flow-based

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charge is derived from forecasted flows. The same charge is applied at all exit points, including Šakiai exit point to the Russian district of Kaliningrad, while no charge is applied at the entries.

Annex 1: Legal framework

(86) Article 27 of NC TAR reads:

1. *Upon launching the final consultation pursuant to Article 26 prior to the decision referred to in Article 27(4), the national regulatory authority or the transmission system operator(s), as decided by the national regulatory authority, shall forward the consultation documents to the Agency.*

2. *The Agency shall analyse the following aspects of the consultation document:*

(a) whether all the information referred to in Article 26(1) has been published;

(b) whether the elements consulted on in accordance with Article 26 comply with the following requirements:

(1) whether the proposed reference price methodology complies with the requirements set out in Article 7;

(2) whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) are met;

(3) whether the criteria for setting non-transmission tariffs as set out in Article 4(4) are met.

3. *Within two months following the end of the consultation referred to in paragraph 1, the Agency shall publish and send to the national regulatory authority or transmission system operator, depending on which entity published the consultation document, and the Commission the conclusion of its analysis in accordance with paragraph 2 in English.*

The Agency shall preserve the confidentiality of any commercially sensitive information.

4. *Within five months following the end of the final consultation, the national regulatory authority, acting in accordance with Article 41(6)(a) of Directive 2009/73/EC, shall take and publish a motivated decision on all items set out in Article 26(1). Upon publication, the national regulatory authority shall send to the Agency and the Commission its decision.*

5. *The procedure consisting of the final consultation on the reference price methodology in accordance with Article 26, the decision by the national regulatory authority in accordance with paragraph 4, the calculation of tariffs on the basis of this decision, and the publication of the tariffs in accordance with Chapter VIII may be initiated as from the entry into force of this Regulation and shall be concluded no later than 31 May 2019. The requirements set out in Chapters II, III and IV shall be taken into account in this procedure. The tariffs applicable for the prevailing tariff period at 31 May 2019 will be applicable until the end thereof. This procedure shall be repeated at least every five years starting from 31 May 2019.*

(87) Article 26(1) of NC TAR reads:

1. *One or more consultations shall be carried out by the national regulatory authority or the transmission system operator(s), as decided by the national regulatory authority. To the extent possible and in order to render more effective the consultation process, the consultation document should be published in the English language. The final consultation prior to the decision referred to in Article 27(4) shall comply with the requirements set out in this Article and Article 27, and shall include the following information:*

(a) the description of the proposed reference price methodology as well as the following items:

(i) the indicative information set out in Article 30(1)(a), including:

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- (1) *the justification of the parameters used that are related to the technical characteristics of the system;*
 - (2) *the corresponding information on the respective values of such parameters and the assumptions applied.*
 - (ii) *the value of the proposed adjustments for capacity-based transmission tariffs pursuant to Article 9;*
 - (iii) *the indicative reference prices subject to consultation;*
 - (iv) *the results, the components and the details of these components for the cost allocation assessments set out in Article 5;*
 - (v) *the assessment of the proposed reference price methodology in accordance with Article 7;*
 - (vi) *where the proposed reference price methodology is other than the capacity weighted distance reference price methodology detailed in Article 8, its comparison against the latter accompanied by the information set out in point (iii);*
- (b) *the indicative information set out in Article 30(1)(b)(i), (iv), (v);*
- (c) *the following information on transmission and non-transmission tariffs:*
 - (i) *where commodity-based transmission tariffs referred to in Article 4(3) are proposed:*
 - (1) *the manner in which they are set;*
 - (2) *the share of the allowed or target revenue forecasted to be recovered from such tariffs;*
 - (3) *the indicative commodity-based transmission tariffs;*
 - (ii) *where non-transmission services provided to network users are proposed:*
 - (1) *the non-transmission service tariff methodology therefor;*
 - (2) *the share of the allowed or target revenue forecasted to be recovered from such tariffs;*
 - (3) *the manner in which the associated non-transmission services revenue is reconciled as referred to in Article 17(3);*
 - (4) *the indicative non-transmission tariffs for non-transmission services provided to network users;*
- (d) *the indicative information set out in Article 30(2);*
- (e) *where the fixed payable price approach referred to in Article 24(b) is considered to be offered under a price cap regime for existing capacity:*
 - (i) *the proposed index;*
 - (ii) *the proposed calculation and how the revenue derived from the risk premium is used;*
 - (iii) *at which interconnection point(s) and for which tariff period(s) such approach is proposed;*
 - (iv) *the process of offering capacity at an interconnection point where both fixed and floating payable price approaches referred to in Article 24 are proposed.*

(88) Article 7 of NC TAR reads:

The reference price methodology shall comply with Article 13 of Regulation (EC) No 715/2009 and with the following requirements. It shall aim at:

- a) *enabling network users to reproduce the calculation of reference prices and their accurate forecast;*
- b) *taking into account the actual costs incurred for the provision of transmission services considering the level of complexity of the transmission network;*
- c) *ensuring non-discrimination and prevent undue cross-subsidisation including by taking into account the cost allocation assessments set out in Article 5;*

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(d) ensuring that significant volume risk related particularly to transports across an entry-exit system is not assigned to final customers within that entry-exit system;

(e) ensuring that the resulting reference prices do not distort cross-border trade.

(89) Article 13 of Regulation (EC) No 715/2009 reads:

1. Tariffs, or the methodologies used to calculate them, applied by the transmission system operators and approved by the regulatory authorities pursuant to Article 41(6) of Directive 2009/73/EC, as well as tariffs published pursuant to Article 32(1) of that Directive, shall be transparent, take into account the need for system integrity and its improvement and reflect the actual costs incurred, insofar as such costs correspond to those of an efficient and structurally comparable network operator and are transparent, whilst including an appropriate return on investments, and, where appropriate, taking account of the benchmarking of tariffs by the regulatory authorities. Tariffs, or the methodologies used to calculate them, shall be applied in a nondiscriminatory manner.

Member States may decide that tariffs may also be determined through market-based arrangements, such as auctions, provided that such arrangements and the revenues arising therefrom are approved by the regulatory authority.

Tariffs, or the methodologies used to calculate them, shall facilitate efficient gas trade and competition, while at the same time avoiding cross-subsidies between network users and providing incentives for investment and maintaining or creating interoperability for transmission networks.

Tariffs for network users shall be non-discriminatory and set separately for every entry point into or exit point out of the transmission system. Cost-allocation mechanisms and rate setting methodology regarding entry points and exit points shall be approved by the national regulatory authorities. By 3 September 2011, the Member States shall ensure that, after a transitional period, network charges shall not be calculated on the basis of contract paths.

2. Tariffs for network access shall neither restrict market liquidity nor distort trade across borders of different transmission systems. Where differences in tariff structures or balancing mechanisms would hamper trade across transmission systems, and notwithstanding Article 41(6) of Directive 2009/73/EC, transmission system operators shall, in close cooperation with the relevant national authorities, actively pursue convergence of tariff structures and charging principles, including in relation to balancing.

(90) Article 4(3) of NC TAR reads:

3. The transmission services revenue shall be recovered by capacity-based transmission tariffs. As an exception, subject to the approval of the national regulatory authority, a part of the transmission services revenue may be recovered only by the following commodity-based transmission tariffs which are set separately from each other:

(a) a flow-based charge, which shall comply with all of the following criteria:

- (i) levied for the purpose of covering the costs mainly driven by the quantity of the gas flow;*
- (ii) calculated on the basis of forecasted or historical flows, or both, and set in such a way that it is the same at all entry points and the same at all exit points;*
- (iii) expressed in monetary terms or in kind.*

(b) a complementary revenue recovery charge, which shall comply with all of the following criteria:

- (i) levied for the purpose of managing revenue under- and over-recovery;*
- (ii) calculated on the basis of forecasted or historical capacity allocations and flows, or both;*

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(iii) applied at points other than interconnection points;

(iv) applied after the national regulatory authority has made an assessment of its cost-reflectivity and its impact on cross-subsidisation between interconnection points and points other than interconnection points.

(91) Article 4(4) of NC TAR reads:

4. The non-transmission services revenue shall be recovered by non-transmission tariffs applicable for a given non-transmission service. Such tariffs shall be as follows:

(a) cost-reflective, non-discriminatory, objective and transparent;

(b) charged to the beneficiaries of a given non-transmission service with the aim of minimising cross-subsidisation between network users within or outside a Member State, or both.

Where according to the national regulatory authority a given non-transmission service benefits all network users, the costs for such service shall be recovered from all network users.

Annex 2: List of abbreviations

Acronym	Definition
ACER	Agency for the Cooperation of Energy Regulators
CAA	Cost Allocation Assessment
VERT	The Lithuanian NRA, Valstybinė energetikos reguliavimo taryba
CWD	Capacity Weighted Distance
EC	European Commission
EU	European Union
IP	Interconnection Point
MS	Member State
NC TAR	Network code on harmonised transmission tariff structures for gas
NRA	National Regulatory Authority
RPM	Reference Price Methodology
TSO	Transmission System Operator



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