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Agency Report

Analysis of the Consultation Document on the Gas Transmission Tariff Structure for the Interconnector UK

NRA: Office of Gas and Electricity
Markets and Commissie voor de
Regulering van de Elektriciteit en het Gas/
Commission de Régulation de l'Électricité
et du Gaz

TSO: Interconnector (UK) Limited

21 December 2018

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1. ACER conclusion

- (1) Interconnector (UK) Limited ('IUK') proposes a charging methodology¹ in the final consultation according to Article 26 of the Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR').
- (2) The consultation document takes into account the derogation granted by the Office of Gas and Electricity Markets ('Ofgem') and the Commission for Electricity and Gas Regulation ('CREG') to IUK from certain articles of the NC TAR detailed in Chapter 3.
- (3) The Agency concludes, after having completed the analysis of the consultation documents pursuant to Article 27(2) of the NC TAR, that:
 - Overall, the information referred to in Article 26(1) of the NC TAR and not related to the aspects to which derogation applies, has been published. The consultation documents list principles, but do not provide specific information on the tariff structure, nor the reference prices;
 - Due to the derogation granted to IUK, the consultation documents do not allow the Agency to conclude that the proposed reference price methodology ('RPM') is compliant with the requirements set out in Article 7 of the NC TAR;
 - In line with the derogation granted to IUK, the absence of a compliance analysis in the consultation documents pursuant to Article 27(2)(b)(2) does not allow the Agency to conclude that the proposed RPM is compliant with the requirements for setting commodity-based transmission tariffs;
 - The compliance analysis pursuant to Articles 27(2)(b)(3) does not apply as non-transmission charges are not proposed.
- (4) The Agency considers the Initial Registration Fee and the Monthly Administration Fee that are referred to in the consultation document are related to services associated with 'access to the natural gas transmission networks'. Therefore these services should fall under the scope of Regulation (EC) 715/2009 and the NC TAR. Consequently the above-mentioned fees should be treated as fees for either transmission or non-transmission services.
- (5) The derogation granted to IUK is subject to the review of the Agency or the European Commission, based on Article 37(5) of the NC TAR.

¹ The proposed charging methodology is not based on the division of the allowed or target revenue by the forecasted bookings, as IUK has no allowed or target revenue. Instead, tariffs are calculated using a number of factors including costs, competitive forces and a range of market scenarios.

2. Introduction

- (6) Commission Regulation (EU) 2017/460 of 16 March 2017 establishes a Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR').
- (7) Article 27 of the NC TAR requires the Agency to analyse the consultation documents on the reference price methodologies for all entry-exit systems². This Report presents the analysis of the Agency for the transmission system of IUK.
- (8) On 4 October 2018, the Agency received the consultation document submitted by IUK³. The consultation was launched on 4 October 2018 and remained open until 3 November 2018.
- (9) Pursuant to Article 26 of the NC TAR, the initial public consultation must run for two months. Under a derogated framework, IUK ran the public consultation for one month. While under the general context of the NC TAR, the Agency has four months to assess the public consultation, in the context of the derogation granted to IUK, the Agency only had three months to do so.
- (10) On 30 November, the consultation responses and their 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 the NC TAR, CREG and Ofgem shall take and publish a motivated decision on all the items set out in Article 26(1).

Reading guide

- (11) Chapter 3 describes the derogation from a number of articles of the NC TAR granted to IUK by Ofgem and CREG. Chapter 4 presents an analysis on completeness, namely whether all the information in Article 26(1) has been published. Chapter 5 focusses on compliance, namely whether the RPM complies with the requirements set out in Article 7 of the Code, whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) are met, and whether the criteria for setting non-transmission tariffs as set out in Article 4(4) are met. Chapter 6 includes other comments. This document contains two annexes, respectively the legal framework and a list of abbreviations.

3. Derogation granted to IUK

- (12) On 5 December 2017, IUK submitted an application for derogation from a number of articles of the NC TAR to Ofgem and CREG for decision, pursuant to Article 37 of the NC TAR.
- (13) On 13 July 2018, pursuant to Article 37(4) of the NC TAR, Ofgem and CREG notified the Agency and the European Commission of their decisions granting IUK derogation from certain articles of the NC TAR⁴.

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

³ Details of the consultation are available at: <https://www.interconnector.com/media/126968/iuk-charging-methodology-consultation-letter.pdf>

⁴ See <https://www.creg.be/fr/publications/decision-b1783> and <https://www.ofgem.gov.uk/publications-and-updates/decision-derogate-iuk-certain-articles-eu-network-code-tariffs>

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- (14) Ofgem and CREG granted IUK derogation from the following articles:
- Articles perceived by IUK as restricting tariff flexibility and IUK's ability to compete in the market: Articles 12(3), 13, 28, 29(a), 29(b)(i), 31(2)(a);
 - Articles perceived by IUK as requiring the publication of information that is commercially sensitive for IUK as a merchant interconnector: Articles 7(a), 26(1)(a)(iii), 26(2), 30(1)(b)(ii), 30(1)(b)(iii)(2)(3)(5);
 - Articles perceived by IUK as relating to TSOs with a regulated asset base, captive customers and multiple network points and therefore not relevant to IUK as a merchant interconnector: Articles 5, 26(1)(a)(vi), 30(1)(a)(ii)(iii), 30(1)(b)(i)(ii), 30(1)(b)(iii)(1), 30(1)(b)(iv)(v), 30(2).
- (15) The Agency observes that the information published in the methodology proposal and analysed in detail in Chapters 4 and 5 is compliant with the publication requirements set by applying the derogation granted. The derogation granted to IUK is subject to a review by the Agency or the European Commission, based on Article 37(5) of the NC TAR.

4. Completeness

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

- (16) IUK was granted a derogation from Article 26(1)(a)(iii) and Article 26(1)(a)(vi), as well as the following articles, over which Article 26(1) sets a publication requirement: Article 5, Article 7, Article 30(1)(a), Article 30(1)(b)(i), (iv), (v), and Article 30(2).
- (17) Article 27(2)(a) of the NC TAR requires the Agency to analyse whether all the information items referred to in Article 26(1) of the NC TAR have been published.
- (18) Article 26(1) of the NC TAR requires that the consultation document is published in English, to the extent possible. The Agency confirms that the consultation document was published in English.
- (19) Overall, the information in Article 26(1) of the NC TAR which was not subject to derogation has been published, as detailed in Table 1 below. The methodology details the overarching principles. IUK states compliance on the requirements in Article 7 of the NC TAR, but does not demonstrate such compliance based on evidence (e.g. principles set in Article 7(b) to 7(e) of the NC TAR).

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Table 1 Checklist information Article 26(1) taking into account the derogation granted to IUK⁵.

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. Derogation from Article 30(1)(a)(ii) on forecasted technical capacity, and Article 30(1)(a)(iii) on the quantity and the direction of gas flows
26(1)(a)(ii)	the value of the proposed adjustments for capacity-based transmission tariffs pursuant to Article 9	Not applicable (discounts are not proposed)
26(1)(a)(iii)	the indicative reference prices subject to consultation	Derogation from Article 26(1)(a)(iii)
26(1)(a)(iv)	the results, the components and the details of these components for the cost allocation assessments set out in Article 5	Derogation from Article 26(1)(a)(iv)
26(1)(a)(v)	the assessment of the proposed reference price methodology in accordance with Article 7	Yes. Derogation from Article 7(a)
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)	Derogation from Article 26(1)(a)(vi)
26(1)(b)	the indicative information set out in Article 30(1)(b)(i), (iv), (v)	Derogation from Article 30(1)(b)(i) (iv)(v)
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. Article 26(i)(c)(i)(2) is not applicable as IUK has no allowed or target revenue.
26(1)(c)(ii) 26(1)(c)(ii)(1) 26(1)(c)(ii)(2) 26(1)(c)(ii)(3) 26(1)(c)(ii)(4)	where non-transmission services provided to network users are proposed: <ul style="list-style-type: none"> the non-transmission service tariff methodology 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 	Not applicable (non-transmission tariffs are not proposed)
26(1)(d)	the indicative information set out in Article 30(2);	Derogation from Article 30(2)
26(1)(e) 26(1)(e)(i) 26(1)(e)(ii) 26(1)(e)(iii)	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: <ul style="list-style-type: none"> the proposed index; 	Not applicable (fixed payable prices are not proposed)

⁵ See overview in Annex A of IUK's consultation letter : <https://www.interconnector.com/media/126968/iuk-charging-methodology-consultation-letter.pdf>

<p>26(1)(e)(iv)</p>	<ul style="list-style-type: none"> • 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 	
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5. Compliance

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

- (20) Article 27(2)(b)(1) of the NC TAR requires the Agency to analyse whether the proposed RPM complies with the requirements set out in Article 7 of the NC TAR. This article refers to Article 13 of Regulation (EC) No 715/2009 and lists a number of requirements to be taken into account when setting the RPM. As these 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.
- (21) Regarding the closely related⁶ concepts of transparency, cost-reflectivity, non-discrimination, cross-subsidisation and cross-border trade, the elements published by IUK are consistent with the derogation granted to IUK from this article and detailed in Chapter 3 above, and therefore insufficient to allow the Agency to reach a conclusion on any of those points.

5.1.1 Transparency

- (22) The derogation granted to IUK includes Article 7(a). Article 7(a) of the NC TAR requires that the RPM aim at enabling network users to reproduce the calculation of reference prices and their accurate forecast.
- (23) The Agency observes that, consistent with the derogation granted to IUK, the consultation documents do not allow such forecast.

5.1.2 Cost-reflectivity

- (24) Article 7(b) of the NC TAR requires that the RPM take into account the actual costs incurred for the provision of transmission services, considering the level of complexity of the transmission network.
- (25) The Agency cannot conclude that the RPM is compliant with the principle of cost-reflectivity as required by Article 7(b). The level of detail provided in the consultation documents is consistent with the derogation granted to IUK⁷. It does not allow the Agency to reach a conclusion

⁶ 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.

⁷ See Chapter 3 above.

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regarding the relevance of the chosen cost drivers and their respective contribution to the reference price⁸.

5.1.3 Cross-subsidisation

- (26) Article 7(c) of the NC TAR requires that the RPM ensure non-discrimination and prevent undue cross-subsidisation. One instrument to evaluate this is the CAA (Article 5 of the NC TAR).
- (27) Consistent with the derogation granted to IUK, which includes Article 5 of the NC TAR, the consultation documents do not detail the CAA. The consultation documents explain that the CAA is not relevant in the context of IUK, given that IUK has no intra-system network users. The consultation documents state, but do not demonstrate, that the RPM ensures non-discrimination and prevents undue cross-subsidisation. The Agency cannot reach a conclusion regarding these aspects of the RPM.

5.1.4 Volume risk

- (28) Article 7(d) of the 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. The consultation document explains that this aspect is not relevant in the context of IUK, given that IUK has no intra-system network users⁹.

5.1.5 Cross-border trade

- (29) Article 7(e) of the NC TAR requires that the RPM ensure that the resulting reference prices do not distort cross-border trade, hence that the RPM complies with the principles of cost-reflectivity, non-discrimination and preventing undue cross-subsidisation¹⁰.
- (30) Consistent with the derogation granted to IUK, the consultation documents do not demonstrate that the RPM complies with the principles of cost-reflectivity and non-discrimination, and that it does not result in undue cross-subsidisation as laid out in this Report. Therefore, the Agency also cannot conclude that reference prices are compliant with the principle of not distorting cross-border trade.

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

- (31) IUK proposes to apply commodity-based transmission tariffs. The consultation document does not provide sufficient details to allow the Agency to conclude that the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) are met. These criteria are laid out in Table 2 below. Nevertheless, principles set in the consultation document suggest that the commodity-based transmission tariff consists of a flow-based charge according to Article 4(3)(a) of the NC TAR¹¹.

⁸ The RPM is not based on the division of the allowed or target revenue by the forecasted bookings (see p. 6 of the consultation document), as IUK has no allowed or target revenue (see page 7 of the consultation document). Instead, tariffs are calculated using a number of factors including costs, competitive forces and a range of market scenarios (see page 4 of the consultation document).

⁹ See footnote 5 above.

¹⁰ See footnote 6 above.

¹¹ See IUK charging statement: <https://www.interconnector.com/access-services/iaa-contract/costs/>

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Table 2 Criteria for setting a flow-based charge pursuant to Article 4(3)(a)

Criteria	Y/N?
levied for the purpose of covering the costs mainly driven by the quantity of the gas flow	Yes
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	Yes
expressed in monetary terms or in kind	Yes

5.3 Are the criteria for setting non-transmission tariffs as set out in Article 4(4) met?

- (32) IUK proposes not to apply non-transmission tariffs. The criteria for setting non-transmission tariffs as set out in Article 4(4) are therefore not applicable.

6. Other comments

- (33) In the consultation document, IUK refers to two fees¹², namely i) an Initial Registration Fee and ii) a Monthly Administration Fee. These fees are not considered as associated with transmission or non-transmission services. In view of the Agency, both fees are related to services associated with 'access to the natural gas transmission networks' and should fall within the scope of the NC TAR. Consequently, the above-mentioned fees should be treated as fees for either transmission or non-transmission services.

¹² See p. 7 of the 'Charging Methodology related to the IUK Access Agreement and IUK Access Code. March 2018': <https://www.interconnector.com/media/119816/IUK%20Charging%20Methodology%20from%20March%202018.pdf>

Annex 1: Legal framework

Article 27 of the 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.*

Article 26(1) of the 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.*

Article 7 of the 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.*

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.

Article 4(3) of the 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.

Article 4(4) of the NC TAR reads:

4. The non-transmission services revenue shall be recovered by non-transmission tariffs applicable for a given nontransmission 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, the Agency	Agency for the Cooperation of Energy Regulators
CAA	Cost Allocation Assessment
CREG	Commission for Electricity and Gas Regulation
ENTSOG	European Network of Transmission System Operators for Gas
EU	European Union
IUK	Interconnector (UK) Limited
NC TAR	Network code on harmonised transmission tariff structures for gas
NRA	National Regulatory Authority
Ofgem	Office of Gas and Electricity Markets
RPM	Reference Price Methodology
TSO	Transmission System Operator



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