



European Union Agency for the Cooperation
of Energy Regulators

Agency Report

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

NRA: Sabiedrisko pakalpojumu
regulēšanas komisija
TSO: AS Conexus Baltic Grid

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1. ACER conclusion

- (1) The Latvian National Regulatory Authority ('NRA'), Sabiedrisko pakalpojumu regulēšanas komisija, carried out a consultation on the tariff structure applicable to Latvia for the period from 1 October 2023 to 30 September 2025. The proposed tariffs are derived from the broader scheme applicable to the Finish, Estonian and Latvian networks ('FINESTLAT') for the integration of their gas markets.
- (2) The tariff structure for the FINESTLAT market merger is the one that is already applicable, with no changes proposed in the current consultation. The NRA has informed ACER that the TSOs are reviewing the new market dynamics following the war in Ukraine and the prohibition of Russian gas imports to the three markets in addition to Lithuania¹. The main elements of the FINESTLAT market merger are:
 - A common entry tariff of 142.77 €/MWh/d/y set at all entry IPs to the FINESTLAT market zone (currently these are the LNG entry point in Finland, and the Latvian IP with Lithuania),
 - Zero tariffs at the IPs within the FINESTLAT zone,
 - An Inter-TSO compensation ('ITC') mechanism agreement by the concerned TSOs applied only to the revenue collected from entries. This mechanism is partial, as it does not provide an efficient compensation based on network costs. It redistributes TSO's revenue recovered from the FINESTLAT entry points proportionally to the consumption from each of the networks of the FINESTLAT market zone.
- (3) The NRA proposes to apply a postage stamp methodology to allocate the revenue not recovered through the ITC. This methodology allocates the remaining revenue separately to domestic exit points of the network and to the exit point to Lithuania. The proposed tariffs for domestic exits are 100% commodity based. In the 2018 tariff consultation, the NRA informed the Agency of a process to move towards capacity based tariffs, however, the NRA now stated its intention to maintain commodity based transmission tariffs. The Agency notes that the transmission network includes regional networks².
- (4) The tariff for the exit point to Lithuania is set separately from the tariffs applicable to the domestic exits.
- (5) The Agency notes that the application of 100% commodity tariffs leads to a different allocation of costs to network users based on their demand profiles compared to capacity-based tariffs. This is explained in paragraph (76) of this report. As a result, the proposed approach leads to a distortion of the cost reflectivity requirement. The application of pure commodity-based tariffs at domestic exit points suggests that, more than 10 years after its entry into force, the underlying implementation of an entry-exit model in the Latvian network is still on going. This is required by Article 13 of Regulation (EC) 715/2009, by the Network Code on Capacity Allocation Mechanisms in Gas Transmission Networks ('NC CAM') and by the Network Code on Gas Balancing of Transmission Networks ('NC BAL'), A proper implementation of the entry-exit model and of the standard capacity

¹ In discussions with the Agency, the NRA pointed this out and noted that the next step of the regional market integration including also Lithuania will take place no earlier than 1 October 2024

² The Latvian gas transmission system is divided in a gas transmission system network and a regional network as further discussed in Section 4.1 and shown in Figure 1 below.

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products is a prerequisite for the development of an reference price methodology (RPM) compliant with the Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR') requirements.

- (6) The methodology and the calculations proposed by the Latvian NRA to set tariffs do not fully comply with the NC TAR as they are based on multiple exceptions that may contradict the basic principles of the NC TAR. The Agency fails to recognise an RPM that is applied consistently to all points of the network in order to allocate the revenue of the TSO on the basis of capacity-based tariffs.
- (7) Concerning the use of the Incukalna underground gas storage (UGS) for the operation of the transmission network and its related costs, the NRA refers to two regulatory instruments used to inject gas in storage. The existing mechanism had been partially assessed by the Agency in the 2019 Report on the Tariff Consultation for Latvia ('2019 Agency Report'). In addition, a second instrument has been approved. The Agency finds that the information provided in the consultation is insufficient to assess these mechanisms. The Agency finds that the information provided in the consultation is insufficient to assess the costs and their allocation using the RPM. The NRA does not specify the extent to which these services are used nor the resulting costs.
- (8) The NC TAR foresees a cost allocation assessment ('CAA') and a comparison of the chosen RPM with the capacity-weighted distance ('CWD') methodology. The result of the CAA provided in the consultation is 173.36%, which is significantly above the 10% threshold laid out in Article 5(5) of the NC TAR and therefore requires a justification. The Agency notes that the NRA does not provide the details of the calculation, as required by the NC TAR. In addition, the Agency notes that the tariff structure of the FINESTLAT market zone does not make the CAA a useful tool, at least not in the absence of a thorough analysis, which is not provided in the consultation. The NRA also provides a comparison with the CWD methodology. The Agency notes that the assumptions used for the proposed postage stamp methodology and the CWD are not the same, so the calculation provided by the NRA is of limited use. The Agency finds that the consultation does not comply with the requirements of the NC TAR for neither the CAA nor the comparison with the CWD.
- (9) The Agency concludes, after having completed the analysis of the consultation document pursuant to Article 27(2) of the NC TAR, that:
 - The consultation document does not contain all the required information listed in Article 26(1), including the details of the CAA calculation, the assessment of the impact of the FINESTLAT tariff structure on cross-subsidisation, an explanation of the tariff changes throughout the tariff period and the methodology to forecast contracted capacity.
 - The proposed tariff structure used to calculate tariffs does not comply with the requirements on transparency, cost-reflectivity, cross-subsidisation and cross-border trade. The proposed tariff structure is compliant with the requirements on non-discrimination and volume risk.
 - The criteria for setting the commodity charge are not applicable. The Agency nevertheless expresses its concern about the application of commodity tariffs at domestic exits, as referred to in paragraph (3) and (5) above. Such an approach is non-compliant with Article 4(3) of the NC TAR.
 - The criteria for setting non-transmission tariffs are not applicable.

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- (10) While the Agency favours the regional integration of markets, it regrets that the chosen design of this integration leads to incompliance with the NC TAR. Some of the inconsistencies pointed out in its 2019 Agency Report were considered to be temporary, such as the application of commodity based tariffs. However, the current consultation proposes to extend the application of these features. The Agency provides in this Report several recommendations to be applied both regionally and nationally in Latvia to achieve compliance with the NC TAR.

Recommendations on the FINESTLAT or the further market integration with Lithuania (FinBalt)

- (11) On the proposed tariff structure for the FINESTLAT or the possible further market integration with Lithuania (FinBalt)³, the Agency provides the following recommendations, based on its previous reports.
- (12) First, the Agency recommends that the NRAs improve the process, including on the following elements:
- The governance should be based on the NRA obligations set out under Article 41(6) of Directive 2009/73/EC. The Agency notes that the agreements, and some elements of the implementation, have been led by the relevant TSOs.
 - The NRA should provide a clear timeline of the process towards the FinBalt market zone.
 - The NRAs of the FINESTLAT or the FinBalt market zone, as the case may be, should consult jointly on the proposed ITC mechanism⁴.
- (13) Second, the Agency recommends that the NRAs improve the compliance of the proposed FINESTLAT market zone with the NC TAR rules, which ultimately aim at ensuring cost-reflectivity, at preventing undue cross-subsidisation and at enabling transparency. For this purpose, the Agency recommends the following.
- The NRAs can set a common tariffs at entries to the FINESTLAT market zone (e.g. 142.77 €/MWh/d/y). However, this should be done based on the NC TAR rules⁵ and should maintain overall compliance with the rule to apply the RPM to all points of the network.
 - The NRAs should improve the design of the ITC with a view to fully meeting the two requirement set out in Article 10(3)(a) of the NC TAR, namely, preventing detrimental effects on the transmission services revenue of the TSOs, and avoiding cross-subsidisation between the networks involved in the market merger. For this purpose, the NRAs should establish a proper revenue redistribution mechanism to compensate for the effects described in paragraph (60) of this report, including the common entry points to the market zone and the applied zero tariffs at cross-border points. The costs of assets that are used across networks should be identified and allocated to the beneficiaries.
- (14) Third, the Agency further recommends that the consultation on the ITC should properly assess the potential cross-subsidisation, or its absence, resulting from the points made in paragraph (60) of this report. The consultation should compare the revenue that the networks would receive without

³ See Section 4.3.2 of this report.

⁴ See also paragraph (11), Section 4.1.1.2 and paragraph (49) of the 2019 Agency Report.

⁵ See also paragraph 13 and Section 4.1.2.1 of the 2019 Agency Report.

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the FINESTLAT market zone and as part of this market zone. This should enable stakeholders to assess the effectiveness and the potential improvements of the proposed ITC design.

Recommendations for the tariff structure specifically applicable to Latvia

- (15) On the proposed tariff structure applicable to Latvia, the Agency provides the following recommendations.
- (16) First, on the proposal to apply commodity tariffs to domestic exit points, the Agency remarks that the obligation to fully implement the Third Energy Package, including the entry-exit model, precedes the implementation of the NC TAR. The NC TAR assumes the prior implementation of an entry-exit system for capacity sales, for which the appropriate metering infrastructure should be in place.
- (17) Second, on the application of a separate tariff to the exit point to Lithuania, the Agency remarks that it is a requirement of the NC TAR to apply the same methodology to all exit points of the network. The NRA should derive the applicable tariff for the exit point to Lithuania based on the same methodology applied to the domestic exit points. For this purpose, the tariffs applicable to domestic exit points should be based on capacity.
- (18) Third, on the presence of regional networks, the Agency recommends to move this infrastructure to distribution networks. The Agency notes that this measure could potentially allow maintaining the commodity-based tariffs to domestic end users. In addition, the measure should facilitate an agreement on the regional market integration as it limits the potential cross-subsidisation between the involved networks.
- (19) Fourth, the Agency recommends to properly describe and assess the new storage filling mechanism, in addition to the links with and impact of this mechanism on the use of the existing regulatory instrument. The NRA should provide the costs and details of the costs to be allocated using the RPM. For this purpose, the Agency recommends that the NRA takes into account the recommendations provided in its 2019 Agency Report summarized in paragraph (88)⁶, provided in Chapter 6 of the ACER 2020 NC TAR Implementation Report⁷, and provided in Regulation (EU) 2022/1032 on national storage filling targets⁸.
- (20) Fifth, the Agency recommends to clarify the parameters of the simplified tariff model allowing to calculate the tariffs. Such model should include the required steps related to the ITC mechanism and to the split of revenues between all entries and all exits. The tariff model should enable the calculation of tariffs for all the tariff years of the regulatory period.
- (21) Sixth, the Agency recommends to publish the missing information that is required pursuant to Article 26(1). Table 1 below provides a list of this information. In addition, the Agency recommends that

⁶ While currently not used, the Agency notes that the existing storage filling regulatory instrument still exists.

⁷https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Publication/The%20internal%20gas%20market%20in%20Europe_The%20role%20of%20transmission%20tariffs.pdf

⁸ Regulation (EU) 2022/1032 of the European Parliament and of the Council of 29 June 2022 amending Regulations (EU) 2017/1938 and (EC) No 715/2009

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the NRA carefully reviews the English translation of the motivated decision to ensure that the arguments and justifications provided remain clear.

- (22) Eighth, the Agency recommends to provide the methodology to estimate the forecasted contracted capacity across all points of the network, including the assumptions used. This information is not included as part of the consultation and is a requirement pursuant to Article 26(1)(a)(i)(1) of the NC TAR. The Agency further recommends that the NRA compares the forecast with the neighbouring NRAs and justifies the differences where these exist. The current forecast for the exit point to Lithuania differs from the forecast provided in the Lithuanian consultation⁹ and is not provided for all years of the regulatory period.
- (23) Ninth, the Agency recommends to publish the full calculation of the CAA, including the assumption on capacity bookings, together with the simplified tariff model. The Agency further recommend that the NRA establishes several scenarios for the CAA calculation with the aim of reflecting, to the extent possible, the results of the ITC in the CAA calculation.
- (24) Tenth, the Agency recommends to provide a valid comparison between the proposed postage stamp methodology and the CWD methodology. The NRA should provide the parameters and the calculation used for the CWD methodology. The Agency further recommends to assess the effect referred to in paragraph (99) of this report as part of this comparison.
- (25) Finally, the Agency refers the NRA to the recently published report on *Future Regulatory Decisions on Natural Gas Networks: Repurposing, Decommissioning and Reinvestments*¹⁰. In particular, Chapter 2 provides guidance on decommissioning to assess the remuneration of the TSO in connection to unused infrastructure assets that were previously used to transport Russian gas.

⁹ <https://www.vert.lt/en/Pages/Updates/regarding-public-consultation-on-tariff-methodology-and-indicative-2024-2028-tariffs-of-lithuanian-tso-%e2%80%93-implementation-of.aspx>

¹⁰ <https://www.acer.europa.eu/events-and-engagement/news/acer-publishes-study-future-regulatory-decisions-natural-gas-networks>

2. Introduction

- (26) Commission Regulation (EU) 2017/460 of 16 March 2017 establishes a network code on harmonised transmission tariff structures for gas (NC TAR).
- (27) Article 27 of the NC TAR requires the Agency to analyse the consultation documents on the reference price methodologies for all entry-exit systems.¹¹ This Report presents the analysis of the Agency for the transmission system of Latvia.
- (28) On 18 January 2023, the Latvian National regulatory Authority ('NRA'), Sabiedrisko pakalpojumu regulēšanas komisija ('PUC'), forwarded the consultation documents to the Agency. The consultation was launched on 15 December 2022 and remained open until 17 February 2023. The consultation responses and their English summary were published on PUC's website. 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, PUC shall take and publish a motivated decision on all the items set out in Article 26(1).
- (29) PUC has already carried out a public consultation based on the NC TAR and published a decision in 2019 for the period 2020-2023; the Agency published its report including its recommendations related to this consultation.¹²
- (30) The Agency thanks the NRA for its availability to discuss the details of the consultation document and for the additional information provided to the Agency. Overall, the NRA has set an good example of cooperation with the Agency when carrying out the final consultation.

Reading guide

- (31) In Section 3, this document first presents an analysis on the completeness, namely if all the information in Article 26(1) has been published. Section 4 assesses the proposed tariff structure for the Latvian transmission network. Section 5 focusses on the compliance of the RPM, namely whether it is aligned 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. Section 6 includes other comments related to the treatment of the infrastructure used to transport Russian gas. This document contains two annexes, respectively the legal framework and a list of abbreviations.

3. Completeness

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

- (32) 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.

¹¹ With the exception of Article 10(2)(b), when different RPMs may be applied by the TSOs within an entry-exit zone.

¹² [Agency Report - analysis of the consultation document for Latvia.pdf \(europa.eu\)](#).

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- (33) Article 26(1) of the NC TAR requires that the consultation document should be published in the English language, to the extent possible. The Agency remarks that the consultation document has been published in English. The Agency nevertheless remarks that the argumentation provided is not always fully clear in the English version. The Agency recommends that the NRA carefully reviews the English translation of the motivated decision.
- (34) Overall, the Agency notes that the consultation is missing information that is required under Article 26(1) of the NC TAR. The Agency recommends that PUC includes in the motivated decision the missing elements referred to in Table 1 below.

Table 1 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 	Partial. The consultation includes limited information on the costs associated with the filling of the storage facility.
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	Partial
26(1)(a)(v)	the assessment of the proposed reference price methodology in accordance with Article 7	Partial. The consultation provides limited information on the impact of the FINESTLAT tariff structure, on the impact of the proposed commodity tariffs and on the storage filling obligation.
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)	Partial. The comparison is not based on the same assumptions, hence the comparability is limited.
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 	Non applicable
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 therefor • the share of the allowed or target revenue forecasted to be recovered from such tariffs 	Non applicable

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	<ul style="list-style-type: none"> 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 	
26(1)(d)	the indicative information set out in Article 30(2);	Yes
26(1)(e) 26(1)(e)(i) 26(1)(e)(ii) 26(1)(e)(iii) 26(1)(e)(iv)	<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 	Non applicable

4. Assessment of the proposed tariff structure

- (35) The following section assesses the proposed RPM, taking into account the input parameters of the methodology and the cost allocation assessment. It starts by describing the Lithuanian transmission network (Section 4.1), the changes compared to the 2108 consultation (section 4.2) and a description of the market integration FINESTLAT and the merger process between FINESTLAT and Lithuania (Section 4.3). Section 4.4 discusses the proposed RPM that is complementary to the FINESTLAT market zone tariff structure. Section 4.5 addresses the regional networks and Section 4.6 the treatment of the Incukalns UGS storage facility. The cost allocation assessment is addressed in Section 4.7 and the comparison with the capacity-weighted distance ('CWD') methodology in Section 4.8.

4.1 Description of the network

- (36) This section presents the network characteristics that are relevant for assessing the proposed tariff structure for the Latvian transmission network. It is supported by the map in Figure 1 below.
- (37) First, the Latvian gas transmission system¹³ is divided into a gas transmission system network and a regional network¹⁴ as shown in Figure 1 below. This point is further assessed under Section 4.5 of this report.

¹³ The total length of the Latvian transmission system is 1190 km.

¹⁴ In the public consultation document, the transmission system network is labelled as 'cross border transmission network' and the regional system network as 'national transmission system'.

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- The transmission system network consists of infrastructure connecting the entry points from and exit point to another country (being Kiemenaĩ to Lithuania and Luhamaa to Estonia) and to the natural gas storage facility Incukalns UGS¹⁵.
 - The regional networks consist of the part of the Latvian transmission system used to supply gas to domestic areas together with branches and gas regulation stations and nodes of the system operator¹⁶.
- (38) Second, the Incukalns UGS, with a total capacity of approximately 24 TWh compared to the total Latvian demand of 8-12 TWh¹⁷, plays a role ensuring pressure in the Latvian transmission network¹⁸. This point is further assessed in Section 4.6 of this report, as a new storage obligation will enter into force to ensure the storage of SoS volumes.
- (39) Third, the Estonia-Latvia interconnection enhancement project (Karksi) will allow for gas supply from Estonia to Latvia and increase the volume of gas flow from Latvia to Estonia¹⁹, allowing better access of the Incukalns UGS to users in Finland and Estonia. This is further supported by the construction of a bi-directional compressor station in Puiata, as part of the Baltic Connector project between Finland and Estonia.
- (40) Fourth, the Inkoo LNG terminal in Finland became operational in January 2023. This provides an alternative supply route to the FINESTLAT market zone in addition to the entry point to Latvia from the Lithuanian network.
- (41) Fifth, the GIPL pipeline connecting Poland and Lithuania entered into operation in May 2022.
- (42) Finally, the FINESTLAT system has two balancing zones: the common Estonian-Latvian balancing zone and the Finnish balancing zone. At the end of the transition period (not earlier than 2024), the merger of the two balancing zones will create a single FINESTLAT balancing zone.

¹⁵ The length of the gas pipelines is 577 km, the diameter is 700 mm and the working pressure therein is from 28 to 40 bars.

¹⁶ The length of the gas pipelines is 613 km, the diameter varies between 100 mm and 500 mm and the working pressure therein is up to 35 bar.

¹⁷ Historically, Latvian natural gas demand has stood at around 12 TWh. During 2022 it dropped to 8 TWh and the NRA expects it to stabilise around 10 TWh.

¹⁸ The aim of the Incukalns UGS enhancement project, which is planned to be completed by 2025, is to significantly reduce the dependency of the gas storage withdrawal capacity on the inventory level of gas in the gas storage. Making the withdrawal capacity less dependent on the inventory level of the gas stored, improves the reliability of gas supply and the operational efficiency of the storage facility which is, according to the consultation document, especially important for ensuring the efficient operation of one single Finnish Baltic gas market.

¹⁹ Up to 73,8 GWh/day.

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Figure 1: Map of the Baltic region including the Latvian transmission network



4.2 Changes compared to the 2018 consultation

- (43) The tariff structure proposed by the NRA is based on the proposal assessed by the Agency in its 2019 Agency Report. This includes the following key elements, which are described in greater detail in that report:
- Tariff structure for the FINESTLAT market zone,
 - RPM applied only to the domestic exit points of the Latvian network,
 - Tariffs applicable to domestic exit points are commodity based.
- (44) The 2022 consultation document refers to a number of changes that have an impact on the proposed tariff structure:
- Prohibition to source supply from Russian imports from 1 January 2023²⁰. This ban is also applicable to Finland, Estonia and Lithuania. Russian gas can only transit from third countries to third counties (i.e. from Russia or Belarus to the Kaliningrad district).
 - The NRA proposes 100% commodity based tariffs at Latvian domestic exit points, despite that during its 2018 consultation, the NRA communicated to ACER its intent to transition toward a capacity based system.
 - The NRA refers to the entry into force of a new storage obligation to store gas in the Incukalna UGS.

²⁰ Amendments to Article 106(4) of the Energy Law of July 14, 2022, which entered into force on 1 January 2023, stipulate that the supply of natural gas from the Russian Federation is prohibited.

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- The NRA proposes to allocate the costs associated with the storage filling obligation for the Incukalns UGS using the proposed RPM. In this manner, the costs are allocated to the end users of the Latvian network. Previously, a different service was used to keep gas in storage, which costs were allocated as a non-transmission service to end users of the Latvian network²¹.
- The Agency provides its views on regional networks, which had not been provided in its 2019 assessment.

4.3 FINESTLAT market merger

- (45) The proposed tariff structure for Latvia is determined by the regional market integration process (FINESTLAT²²) which includes the following elements:
- A common entry tariff of 142.77 €/MWh/d/y set to all external entry IPs of the FINESTLAT market zone. In the case of Latvia, this tariff applies only to the entry point from Lithuania.
 - Zero tariffs to the IPs within the FINESTLAT zone. In the case of Latvia, this applies only to the border with Estonia.
 - An ITC mechanism applied to the revenue collected from entry points to the FINESTLAT market zone. This mechanism is partial, as it does not provide an efficient compensation based on network costs.
- (46) The part of the revenue that is not recovered using the ITC is allocated to domestic exit points, using the proposed RPM, and to the exit point to Lithuania, which is based on the common FINESTLAT tariff.

4.3.1 Inter-TSO compensation mechanism

- (47) The basic principles for the ITC mechanism have been applied from the launch of the FINESTLAT system on 1 January 2020. The Agency regrets that this ITC mechanism was not properly consulted, as the settings of this mechanism were decided by an agreement between the concerned TSOs before the 2018 consultation of the Latvian RPM. The Agency refers to the additional details on the consultation requirements applicable to the ITC which are included under Section 4.1.1.2 of the 2019 Agency Report.
- (48) The main principles for the ITC include the following, as described in the consultation document:
- The revenue recovered from the tariffs of all entry points of the FINESTLAT market zone are gathered in a single revenue pool.
 - The pooled revenue is redistributed to each of the three networks based on the share of natural gas delivered through the transmission network for domestic consumption in each Member State.
 - A compensation for variable costs is possible following the validation of the relevant flow costs related to compression used for the purpose of flowing gas between Member States of the FINESTLAT market zone. The NRA communicated to the Agency that the validation process is agreed between the TSOs with no involvement from the NRAs.

²¹ See section 4.3 of the 2019 Agency Report

²² The FINESTLAT system started operating on 1 January 2020.

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- The calculation of ITC shares is performed by the elected Data Administrator, which is one of the TSOs of the three Member States, rotating annually.

- (49) In the current context, where Russian gas imports to the Baltic Member States have been halted, the partial ITC collects its revenues from the Latvian entry point from Lithuania and from the Inkoo LNG terminal in Finland. In the case of Latvia, the revenue received from the ITC is approximately 10% of the TSO revenue.
- (50) The Agency does not support the argumentation provided by the NRA in its consultation document concerning the compliance of the applicable ITC with the requirement on cost-reflectivity:

Taking into account the unforeseeable change of natural gas supply sources, it can be concluded that there is no natural gas transit in the FinEstLat system [...] Therefore, it is considered that the ITC procedure, which is based on the allocation of revenue between the natural gas transmission system operators, based on the domestic natural gas consumption of the given country, does not allow cross-subsidization between the intra-system and cross-system use of the network²³.

- (51) As clarified to the Agency, the NRA argues that not exporting gas to other networks outside the FINESTLAT market zone prevents cross-subsidisation from arising. However, in its analyses of the FINESTLAT market merger provided for Estonia, Finland and Latvia, the Agency has continuously emphasised the risk of cross-subsidies between these networks resulting from the applicable FINESTLAT tariff structure.
- (52) No such analysis is provided as part of the NRA consultation. As a result it is not possible to assess the potential cross-subsidisation resulting from the tariff structure of the FINESTLAT market zone.
- (53) The Agency notes that the proposed RPM is based on the redistribution of the entry revenue to the FINESTLAT market zone based on the domestic demand from each of the three networks. The Agency notes that while demand could potentially be an approximation of network utilisation, it does not have to be so necessarily. Capacity and distance, which are used as the cost drivers of the CWD methodology, in general provide better means of approximation. It is questionable whether redistributing costs between networks based on domestic demand alone allows to accurately identify the network costs associated with import and transport routes into and across the FINESTLAT market zone. Depending on the comparability of the involved networks in terms of capacity and distance, domestic demand may not be a sufficiently cost-reflective proxy to redistribute revenue. Using it can lead to cross-subsidies between end users of the FINESTLAT networks. The Agency already pointed this out in the Sections 4.1.2.2 and 4.1.2.3 of its 2019 Agency Report with specific examples where the ITC could lead to revenue compensation even when network costs had not been triggered.
- (54) The Agency concludes that the compliance of the FINESTLAT ITC agreement with the requirements of cost reflectivity and cross-subsidisation is not assessed in the current consultation.

²³ Page 23 of the consultation document.

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At the same time, the Agency identifies cases potentially leading to non-compliance with these requirements, implying that the analyses on cost-reflectivity shall not be omitted.

4.3.2 FinBalt merger process

- (55) The NRA indicated that the next step of the regional market integration by including also Lithuania ('FinBalt merger') will take place no earlier than 1 October 2024²⁴. As informed by the NRA, the relevant TSOs are requested to submit by 31 March 2023 to the relevant NRAs an ITC mechanism taking into account changes in infrastructure and gas flows and the need to ensure benefits to all participating countries. After their assessment, the NRAs will publicly consult the new proposal. As understood by the Agency, at this stage there is no concrete timeline for this process. NRAs will analyse the proposal submitted by TSOs and once it is considered as valid, it will be subject to a public consultation. The consultation on the broader FinBalt market zone will be followed by a consultation on the tariffs applicable in the individual Member States.

4.3.3 ACER recommendation

- (56) The Agency acknowledges that an ITC agreement is necessary to enable the FINESTLAT member countries and Lithuania to make progress towards a truly integrated regional gas market, especially if greater focus is put on keeping stable and predictable revenues, while implementing zero tariffs between their respective networks. It also acknowledges that developing a regional ITC mechanism is a complex task.
- (57) The Agency recommends that the NRAs improve the process, including on the following elements:
- First, the governance should be based on the NRA obligations set out under Article 41(6) of Directive 2009/73/EC. The Agency notes that the agreements, and some elements of the implementation, have been led by the relevant TSOs.
 - Second, the NRA should provide a clear timeline of the process towards the FinBalt market zone.
 - Third, NRAs of the FINESTLAT or the broader FinBalt market zone should consult jointly on the proposed ITC mechanism²⁵.
- (58) The Agency recommends that the NRAs improve the compliance of the FINESTLAT market zone with the NC TAR rules, which ultimately aims at ensuring cost-reflectivity, at preventing undue cross-subsidisation and at enabling transparency. For this purpose, the Agency recommends the following.
- (59) First, the NRAs can set a common tariffs at entries to the FINESTLAT market zone (e.g. 142.77 €/MWh/d/y). However, this should be done based on the NC TAR rules²⁶ and should maintain the overall compliance with the rule to apply the RPM to all points of the network. This rule is key to

²⁴ In discussions with the Agency, the NRA noted that the relevant TSOs were aware that the earlier prepared ITC mechanism was not corresponding to the new market conditions and clear benefits of the market merger for Lithuania were not identified yet.

²⁵ See paragraph (11), Section 4.1.1.2 and paragraph (49) of the 2019 Agency Report.

²⁶ See also paragraph 13 and Section 4.1.2.1 of the 2019 Agency Report.

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guarantee the application of other NC TAR rules and to guarantee transparency to stakeholders over the calculation of tariffs.

- (60) Second, the NRAs should improve the design of the ITC with a view to fully meeting the two requirements set out in Article 10(3)(a) of the NC TAR, namely, preventing detrimental effects on the transmission services revenue of the TSOs, and avoiding cross-subsidisation between the networks involved in the market merger. For this purpose, the NRAs should establish a proper revenue redistribution mechanism to compensate for the following effects:
- All the gas enters the FINESTLAT market zone from Latvia and Finland. As a result some networks will have a revenue over-recovery and others a revenue under-recovery.
 - Gas is transported across networks based on zero tariffs applicable at IPs within the FINESTLAT market zone.
 - There is infrastructure that is used across the market zone²⁷. These assets and its costs should be identified first, and second, they should be allocated to the beneficiaries when these are located outside the network where the relevant infrastructure is located.
- (61) The Agency remarks that the current ITC based on the redistribution of revenue according to the share of demand in each network has not been properly assessed and can lead to cross-subsidies between networks.
- (62) The Agency further recommends that the consultation on the ITC should properly assess the potential cross-subsidisation, or its absence, resulting from the points above in paragraph (60). The consultation should compare the revenue that the networks would receive outside the FINESTLAT market zone and as part of this market zone. This should enable stakeholders to fully assess the effectiveness and the potential improvements of the proposed ITC design.

4.4 Proposed reference price methodology

- (63) This section discusses the proposed RPM that is complementary to the FINESTLAT market zone tariff structure. The section looks at the scope of application of the RPM (Section 4.4.1), the tariff applicable to the exit point to Lithuania (Section 4.4.2), the capacity forecasts applied to the exit point to Lithuania (Section 4.4.3), the applicable commodity tariffs (Section 4.4.4) and the discounts for the connections with storage facilities (Section 4.4.5).

4.4.1 Scope of application of the proposed reference price methodology

- (64) Following the tariff structure applicable to the FINESTLAT market zone, the NRA proposes to apply a postage stamp RPM. This methodology is applied only to domestic exits, as there is a separate tariff applicable to the exit point to Lithuania (see Section 4.4.2) and discounts of 100% are proposed to entry points from and exit points to the Latvian storage facility.
- (65) It should be noted, that the proposed tariffs applicable to domestic exit points are based on commodity, not on capacity. As a result, the proposed RPM is not based on the application of capacity tariffs.

²⁷ See Section 5 of the 2019 Agency Report.

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- (66) The Agency notes that Article 6(3) of the NC TAR requires that the RPM is applied to all entry and exit points in a given entry-exit system subject to the exceptions set out in Articles 10 and 11.

4.4.2 Tariff applicable to the exit point to Lithuania

- (67) The Agency notes that the NRA proposes to apply the common FINESTLAT tariff to the exit point to Lithuania. As explained by the NRA, the revenue from this exit point is not part of the FINESTLAT agreement and is used to recover the allowed revenue of the Latvian TSO. The Agency notes that this tariff is not derived using the same postage stamp methodology that is applied to the domestic exit points of the Latvian network.
- (68) The ratio between the revenue allocated from cross-system use and intra-system use in the Latvian network can vary depending on the tariff set to the exit point to Lithuania which has an impact on cross-border flows.
- (69) The Agency remarks that it is a requirement according to Article 6(3) of the NC TAR to apply the same methodology to all exit points of the network. The NRA should derive the applicable tariff to the exit point to Lithuania based on the same methodology applied to the domestic exit points.

4.4.3 Capacity forecasts applied to the exit point to Lithuania

- (70) The NRA forecasts the contracted capacity for the exit point to Lithuania, as detailed in Table 2 below, which includes the forecasted contracted capacity.

Table 2: Forecasted booked capacity at the exit point to Lithuania (Kiemēnai). Source: 2023 tariff consultation for Latvia.

MWh/year	Gas year ²⁸ 2023-2024	Gas year 2024-2025
Capacity at exit point Kiemēnai (LV to LT)	2,999,517	0

- (71) The Agency notes that the forecast differs from the capacity forecast made recently in the Lithuanian consultation²⁹. This is shown in Table 3 below.

Table 3 Forecasted contracted capacity at the entry point from Latvia (Kiemēnai). Source: 2022 tariff consultation for Lithuania

Capacity: EUR/MWh/d/year	Tariff year 2023	Tariff year 2024-2028				
		2024	2025	2026	2027	2028
Kiemēnai	15.534	11.843	25.731	11.876	11.876	11.843

²⁸ Gas year last from 1 October to 30 September.

²⁹ The NRA notified to the Agency that from 1 October 2024, the capacity of the entry point Kiemēnai is set at 0 MWh/year, taking into account that on October 1, 2024 in the expectation that the FinBalt merger of the FinEstLat is already in place.

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- (72) The Agency recommends that the NRA provides the methodology to estimate the forecasted contracted capacity across all points of the network, including the assumptions used. This information is not included as part of the consultation and is a requirement pursuant to Article 26(1)(a)(i)(1) of the NC TAR. The Agency further recommends that the NRA compares the forecast with the neighbouring NRAs and justifies the differences where these exist. The capacity forecast should be provided for all years of the regulatory period.

4.4.4 Commodity tariffs applicable to domestic exit points

- (73) The proposed tariffs for domestic exit points are commodity based. The forecasted volume of gas supplied to gas using facilities connected to the Latvian regional and distribution networks is used to derive the domestic exit commodity tariff. The indicative tariff for the domestic exit points for the regulatory period from 1 October 2023 to 30 September 2025 increases by 74.7% compared to the current tariff.
- (74) For the analysis of the 2018 Tariff Consultation for Latvia, the NRA indicated to the Agency that the Latvian gas system is not yet technically ready to use a capacity charge at domestic exits, and that this solution will only be implemented at the beginning of the next regulatory period³⁰. In its 2019 Agency report the Agency welcomed the objective to implement a fully capacity-based transmission tariff at the beginning of the next regulatory period.
- (75) The Agency notes that the application of 100% commodity tariffs is not compliant with the NC TAR. The reference price derived using the RPM is the “*price for a capacity product for firm capacity with a duration of one year*”.³¹ According to Article 4(3) of the NC TAR, “*the transmission services revenue shall be recovered by capacity-based transmission tariffs*”. Article 4(3) of the NC TAR allows for the application of commodity charges, which can be the flow-based charge or the complementary revenue recovery charge. In both instances, the charges are applied “*as an exception*”.
- (76) The Agency notes that the application of 100% commodity tariffs leads to different costs for network users compared to capacity tariffs. Typically, users with a more stable demand can better profile the contracted capacity (e.g. industrial users), while users more exposed to more volatile and seasonal demand often need to book on the basis of peak capacity (e.g. space heating). Users with more stable demand will likely see their costs rise under commodity tariffs, while the reverse holds for users subject to seasonal demand. The Agency notes that this consideration is captured in the consultation response of the Association of Building Materials Manufacturers³². The Agency further notes that the requirement for tariffs to be cost-reflective is applicable on the basis of capacity tariffs, while the use of commodity based tariffs is foreseen as an exemption. The application of 100% commodity-based tariffs results in a distortion of the principle of cost-reflectivity.
- (77) The application of commodity-based tariffs at domestic exit points suggests that the underlying implementation of an entry-exit model in the Latvian network, as required by Article 13 of NC CAM

³⁰ This is mentioned in paragraph 51 of the 2019 Agency Report.

³¹ Article 1(3) of the NC TAR.

³² <https://www.sprk.gov.lv/sites/default/files/2023-03/Summary%20of%20responses.pdf>.

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and of the NC BAL, is still ongoing. A proper implementation of the entry-exit model and of the standard capacity products is a prerequisite for the development of an RPM compliant with the NC TAR requirements.

- (78) The Agency further notes that the proposed commodity tariffs are applicable at exit points located within regional networks. The Agency recommends to assess the recommendation of applying capacity based tariffs together with the recommendation made in section 4.5 below on regional networks.

4.4.5 Discount for the connections with storage facilities

- (79) PUC proposes to apply a 100% discount to entry points from and exit points to the Latvian storage facility. This is in line with Article 9 of the NC TAR.

4.5 Regional networks

- (80) As referred to in Section 4.1 above on the description of the Latvian network, the Agency points to the existence of regional networks as part of the Latvian transmission network.
- (81) The Agency remarks that the existence of regional networks when designing an RPM for the transmission network is a long-standing topic in the implementation of the NC TAR. The Agency provided guidance on this issue in the ACER 2020 NC TAR Implementation Report³³ which it has recently repeated in the 2023 ACER Reports on the Tariff Consultation for Italy and for Lithuania. The Agency recommends two options for the allocation of the cost associated with regional networks:
- First, in cases where regional networks are in place, these costs can be allocated using the RPM, should the proposed methodology prove capable of allocating the costs related to regional networks only to domestic users.
 - Second, should the allocation of the costs of regional networks to domestic end users not be possible under the proposed RPM, the Agency recommends to change the category of regional networks to distribution, allocating these costs outside the RPM.
- (82) This recommendation is based on the definitions of 'transmission' and 'distribution' in Directive 2009/73/EC³⁴.
- (83) In a number of Member States, the certification of the TSOs has resulted in these entities including regional networks as part of its transmission infrastructure. The Agency notes that the rules of the

³³https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Publication/The%20internal%20gas%20market%20in%20Europe_The%20role%20of%20transmission%20tariffs.pdf

³⁴ Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

'Transmission', as defined under Article 2(3) of the Directive 2009/73/EC, *mainly contains high-pressure pipelines, other than an upstream pipeline network and other than the part of high-pressure pipelines primarily used in the context of local distribution of natural gas, with a view to its delivery to customers, but not including supply,*

'Distribution', as defined in Article 2(5) of the Directive 2009/73/EC, *means the transport of natural gas through local or regional pipeline networks with a view to its delivery to customers, but not including supply*

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NC TAR are designed with the aim of allocating the costs of transmission networks, not of regional networks. The allocation of the latter together with transmission networks is likely to result in cross-subsidies between cross-system use and intra-system use.

- (84) The Agency notes that a postage stamp methodology cannot allocate the specific costs of regional networks only to the users of these networks. For this reason, the Agency recommends the NRA to change the category of regional networks to distribution, allocating these costs outside the RPM.
- (85) This recommendation should be read together with the recommendation on the tariffs applied to domestic exit points and together with the recommendation to apply the same tariff to domestic exit points and to the exit to Lithuania. The Agency notes that a 100% commodity based tariff could be applicable to regional networks once these become distribution assets, since these are then outside the scope of the NC TAR. The Agency invites the NRA to consider this option.

4.6 Treatment of the Incukalns UGS storage facility

- (86) The Incukalns UGS in Latvia is the only operating underground storage facility in the FINESTLAT system. The consultation document explains that compressor stations are used to ensure the necessary pressure in the transmission network. The document further refers to a risk assessment of the gas system of Estonia, Finland, Latvia and Lithuania developed in 2016 by the Joint Research Center of the European Commission³⁵ which states that the flexibility of the Incukalns UGS as an active pressure control facility depends on its inventory level and is a key component of the regional security of gas supply.
- (87) In the 2018 Tariff Consultation for Latvia, the NRA proposed to allocate a part of the costs associated with the Incukalns UGS using non-transmission tariffs. The Agency assessed this mechanism in its 2019 Agency Report under Section 4.3. The costs were expected to represent 4.9 M€ for two gas years out of the total 33.8 M€ allowed revenue of the TSO for one gas year during the 2020-2023 tariff period. The total costs are influenced by different aspects such as the price of gas.
- (88) In its 2019 Agency Report the Agency provided several recommendations³⁶, including on:
- the justification for the total amount of gas to be kept in storage,
 - the conditions to auction the gas and on the level of competition in these auctions,
 - the impact of the storage auctions on the market dynamics to ensure that the potential benefits provided by the UGS are not outweighed by the potential market distortions, and
 - on the ownership status of the UGS facility to ensure a separation between the users bidding to store gas and the UGS facility
- (89) The Agency notes that that the NRA refers to a new regulatory instrument to keep gas in the Incukalns UGS. The consultation document, however, does not sufficiently assess this new storage

³⁵ Joint Research Centre of European Commission. Joint Risk Assessment of the gas system of Estonia, Finland, Latvia and Lithuania, 2016.

³⁶ See Section 4.3 of the 2019 Agency Report.

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filling mechanism. As a result, the Agency has not been able to assess the mechanism. As explained by the NRA to the Agency, a new storage obligation has been put in place³⁷, serving to store gas for security of supply purposes. As a result of the stored gas, the pressure is kept in the UGS facility, which eliminates the need to actively use the previous storage filling instrument³⁸. The NRA informed the Agency that there are currently no costs foreseen for the previous storage filling instrument and that the TSO requested to remove this instrument from the legislation.

- (90) The NRA informed the Agency that the costs of the new storage obligation is financed with the Latvian State budget, and not with network tariffs. At the same time, the NRA informed that some operational costs related to the storage of the gas are allocated using the RPM. These costs are not provided in the consultation document. As communicated by the NRA to the Agency, these costs are marginal.
- (91) The Agency recommends that the NRA properly describe and assess the new storage filling mechanism, in addition to the links with and impact of this mechanism on the use of the existing regulatory instrument. The NRA should provide the costs and details of the costs to be allocated using the RPM. For this purpose, the Agency recommends that the NRA takes into account the recommendations provided in its 2019 Agency Report summarized in paragraph (88),³⁹ provided in Chapter 6 of the ACER 2020 NC TAR Implementation Report⁴⁰, and provided in Regulation (EU) 2022/1032 on national storage filling targets⁴¹.

4.7 Cost allocation assessment

- (92) PUC provides the results of the cost allocation assessment (CAA) for the proposed tariff structure. The result of the CAA for the tariffs applicable for two years is 173.36%.
- (93) The Agency notes that the result provided in the consultation document cannot be taken as indicative of potential cross-subsidisation resulting from the application of the RPM. In the proposed FINESTLAT tariff structure, the revenue that should be attributed to cross-system and intra-system use depends on the redistribution of revenue based on the ITC. In the case of the CAA calculation provided, the cross-system and intra-system revenue is based on the proposed tariffs. As a result, the proposed calculation does not reflect the actual revenue that should be attributed to cross-system and intra-system use.
- (94) In addition, the Agency notes that the data provided in the consultation document is not sufficient to interpret the result. The consultation document provides the general components of the calculation, but does not provide the details of these components, as required by Article 26(1)(a)(iv)

³⁷ Article 1(7) of the Energy Law.

³⁸ The required amount of gas to be stored in the UGS storage facility to assure sufficient pressure for the system is set at 0 MWh.

³⁹ While currently not used, the Agency notes that the existing storage filling regulatory instrument still exists.

⁴⁰ https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Publication/The%20internal%20gas%20market%20in%20Europe_The%20role%20of%20transmission%20tariffs.pdf

⁴¹ Regulation (EU) 2022/1032 of the European Parliament and of the Council of 29 June 2022 amending Regulations (EU) 2017/1938 and (EC) No 715/2009.

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of the NC TAR. As a result, the consultation is non-compliant with this requirement. Such level of detail is required to fully assess the proposed tariff structure.

- (95) The Agency remarks that it is a requirement of the NC TAR to publish the components and the details of these components for the cost allocation assessments. The Agency recommends that the NRA publishes the full calculation, including the assumptions on capacity bookings. The Agency further recommends that the NRA establishes several scenarios for the CAA calculation with the aim of reflecting, to the extent possible, the results of the ITC in the CAA calculation.
- (96) In addition, the Agency recommends that, for the purpose of assessing cross-subsidisation, the NRA compares the missing revenue resulting from the FINESTLAT tariff structure (i.e. resulting from the removal of tariffs at the exit point to Estonia) to the revenue resulting from the ITC. The NRA should assess whether end users of the Latvian network bear higher or lower costs associated with the cross-system use of the network as a result of the FINESTLAT tariff structure. For this analysis, the NRA should publish all the assumptions and parameters used, including the calculation.

4.8 Comparison with the CWD methodology

- (97) PUC provides a comparison between the proposed tariffs for entry and exit points based on the proposed postage stamp methodology and on the CWD methodology. The results are summarised in Table 4 below.

Table 4 Comparison of tariffs of entry and exit points determined by using postage stamp methodology and CWD methodology (Source: table 11 consultation document)

Entry / exit point	Indicative tariffs		
	Postage stamp methodology	CWD methodology	Comparison (Postage stamp -/- CWD)
Entry point Korneti	-	-	-
Entry point Karsi	-	-	-
Entry point Kiemėnai	0.14277	0.1131706	0.0295994
Entry point from storage facility	-	-	-
Exit point Korneti	-	-	-
Exit point Karsi	-	-	-
Exit point Kiemėnai	0.14277	1.4481347	-1.3053647
Exit point to storage facility	-	-	-
Exit point to domestic exit	0.0036101	0.469171	-0.4655609

- (98) The comparison does not include tariffs for the exit point to Estonia, and does not include the capacity and distance assumptions used for the CWD methodology. In addition, the tariffs calculated based on the postage stamp methodology apply the 142.77 €/MWh/d/y tariff to the exit point from Lithuania (which is not calculated using the postage stamp methodology). Both sets of tariffs are not comparable, as the presented postage stamp methodology is fully based on the FINESTLAT market merger, while the proposed CWD methodology is partially based on this tariff structure (e.g. removal of points within the market zone).

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- (99) The Agency recommends that the NRA compares both methodologies based on the same parameters. The NRA should provide the parameters and the calculation used for the CWD methodology. The Agency recommends that the NRA assesses the following two effects when comparing both methodologies:
- Impact of the ITC when calculating tariffs based on each of the methodologies.
 - Impact of revenue allocated to the exit to Lithuania and to domestic exits of the Latvian network resulting from the tariffs derived using each of the methodologies.

4.9 Interruptible virtual counter flow capacity products

- (100) In the consultation document, the NRA refers to a capacity product for interruptible virtual counter flow capacity. The Agency could not assess the compliance of the proposed tariff based on the information provided in the consultation.
- (101) The Agency recommends that the NRA assess the compliance of the tariff applicable to this product, in particular with Article 6(4) and 16 of the NC TAR.

5. Compliance

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

- (102) 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 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.
- (103) As the concepts of transparency, cost reflectivity, non-discrimination, cross-subsidisation and cross border trade are closely related the Agency concludes with an overall assessment. Special attention is paid to the allocation of revenues between domestic and cross-border routes.

5.1.1 Transparency

- (104) **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. In the context of the Latvian consultation, the tariffs are determined by the market integration setting, including the ITC mechanism and by the additional postage stamp methodology. The relative lack of clarity regarding the links between these elements limit compliance with the transparency requirements.
- (105) In particular, the consultation document does not provide clear explanations about the calculation of the revenue split between entries and exits. According to the consultation document, this split would be 50-50%, while the values change to 2-98% when taking into account the ITC.
- (106) The simplified tariff model further refers to a “revenue allocation coefficient” to allocate costs to domestic exit points and to the exit point to Lithuania. Such a factor is not compliant with the NC

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TAR. In addition, it is unclear how it would be applied in practice as the tariff for the exit point to Lithuania is set to the fixed value of 142.77 €/MWh/d/y.

- (107) The Agency recommends the NRA to clarify the parameters of the tariff model allowing to calculate tariffs. Such model should include the required steps related to the ITC mechanism and to the split of revenues between all entries and all exits. In the Latvian case, the revenues from the ITC mechanism should be considered as coming from an entry.

5.1.2 Cost-reflectivity

- (108) **Article 7(b)** of the 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.
- (109) The Agency notes that there are various elements of the proposed tariff structure that distort the cost-reflectivity of the proposed tariffs. The Agency cannot assess the degree to which cost-reflectivity is distorted as the relevant analyses are not provided by the NRA.
- (110) First, the proposed ITC for the FINESTLAT market zone can lead to cross-subsidies. As explained in paragraph (53), the compensation of the TSO revenue is carried out on the basis of demand, which does not necessarily reflect network utilisation.
- (111) Second, the proposed commodity based tariffs result in a distortion of the principle of cost-reflectivity compared to capacity based tariffs. The Agency notes that this distortion is not quantified in the consultation document.
- (112) Third, the tariff set at the exit point to Lithuania is not set based on the RPM and therefore does not reflect the underlying costs and network utilisation. These tariffs are not cost-reflective, since they should be calculated together with the tariffs applicable to the Latvian domestic exit points. This calculation should be based on contracted capacity across all points.
- (113) Based on this assessment, the Agency concludes that the proposed tariff structure is not compliant with the requirement on cost-reflectivity.

5.1.3 Cross-subsidisation

- (114) **Article 7(c)** of the NC TAR requires the RPM to ensure non-discrimination and prevent undue cross-subsidisation.
- (115) Based on the conclusion provided by the Agency on cost-reflectivity in paragraph (113) above, the Agency concludes that the proposed tariffs are not compliant with the requirement on cross-subsidisation.
- (116) Regarding the requirement of ensuring non-discrimination, the Agency has not identified any form of discrimination related to the proposed RPM. For this analysis, the Agency defines 'discrimination' as 'charging different prices to different network users for the identical gas transmission service'.

5.1.4 Volume risk

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- (117) **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.
- (118) Given the characteristics of the Latvian transmission system, such a risk seems unlikely.

5.1.5 Cross-border trade

- (119) **Article 7(e)** of the NC TAR requires that the RPM ensures that the resulting reference prices do not distort cross-border trade.
- (120) The Agency considers that the FINESTLAT market integration should favour cross-border trade within the region. At the same time, the proposed tariff for the exit to Lithuania is not set based on the RPM. The Agency concludes that the proposed tariff structure is not compliant with the requirement on cross-border trade.

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

- (121) 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) are met. The use of commodity based transmission tariffs is an exception. Only part of the transmission services revenue may be recovered by commodity based transmission tariffs.
- (122) Latvia proposes to apply commodity based transmission tariffs at its domestic exits for technical reasons. As already explained in this document, the Agency stresses the need to implement a fully capacity -based transmission tariff at the beginning of the next regulatory period.

6. Treatment of the infrastructure used to transport Russian gas

- (123) The Agency takes note of the response to the consultation provided by the Association of Buildings Material Manufacturers (BRA). In its response, the stakeholder argues that the segments used mainly for the transport of Russian gas should not receive the same remuneration as the rest of the network assets as these assets will no longer be used.
- (124) The Agency refers the NRA to the recently published report on *Future Regulatory Decisions on Natural Gas Networks: Repurposing, Decommissioning and Reinvestments*⁴². In particular, Chapter 2 provides guidance on decommissioning to assess the remuneration of the TSO in connection to unused infrastructure assets that were previously used to transport Russian gas.

⁴² <https://www.acer.europa.eu/events-and-engagement/news/acer-publishes-study-future-regulatory-decisions-natural-gas-networks>

Annex 1: Legal framework

(125) 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.*

(126) 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.*

(127) 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.

(128) 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.

(129) 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.

(130) 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	Agency for the Cooperation of Energy Regulators
ENTSOG	European Network of Transmission System Operators for Gas
NRA	National Regulatory Authority
TSO	Transmission System Operator
EC	European Commission
EU	European Union
MS	Member State
NC TAR	Network code on harmonised transmission tariff structures for gas
IP	Interconnection Point
VIP	Virtual Interconnection Point
RPM	Reference Price Methodology
CWD	Capacity Weighted Distance
CAA	Cost Allocation Assessment
RAB	Regulated Asset Base
OPEX	Operational Expenditures
CAPEX	Capital Expenditures