

MINUTES

Network Code on Harmonised Transmission Tariff Structures for Gas

ENTSOG Stakeholder Joint Working Session 1

11 February 2014 from 10:00 – to 17:00

At ENTSO-E Conference Centre, Av. de Cortenbergh 100, Brussels

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CEFIC & IFIEC	Dirk Jan Meuzelaar	Eurogas	Margot Loudon
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CRE	François Leveille	ExxonMobil / OGP	Kees Bouwens
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CREG	Johan Allonsius	Gas Connect Austria	Martin Bliem
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Gaslink	Denis Twomey	Net4Gas	Petr Molík
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GasTerra	Arco Hofman	ONTRAS	Niels Krap
Gastransport Nord	Jann Keller	Open Grid Europe	Stephanie Ruhland
Gasunie Deutschland	Ksenia Berezina	RWE Supply & Trading	Stephen Rose
Gazprom M & T	Alex Barnes	sec	Nigel Sisman
GDF SUEZ	Claude Mangin	Shell Energy Europe	Amrik Bal
GDF SUEZ Infrastructures	Sylvie Denoble-Mayer	Snam	Alessandro Gussetti
GIE	Philipp Daniel Palada	Snam	Lorenzo Nicolosi
GRTgaz Germany	Gregor Scholze	Snam	Marco Gazzola
Hungarian Gas Transit	Lajos Butosi	TIGF	Emmanuel Bouquillion
Interconnector UK	Pavanjit Dhesi	Vattenfall	Helga Norrby
Ministry of Industry and Trade	Michaela Niměřická	VCI / Cefic	Alexander Kronimus
National Grid	Colin Hamilton		

ENTSOG also provided a webcast facility for those unable to attend in person.

1. OPENING

> Welcome / Introduction; Process Update

Ms Ann-Marie Colbert welcomed the participants to the 1st TAR NC SJWS. An update of the TAR NC development process was provided. The 1st phase of the process was completed by the end of January which included the consultation on the draft Project Plan, the Kick-Off Meeting and the publication of the Launch Documentation and the final Project Plan. Based on the feedback received from the draft Project Plan consultation, two additional topics were included in the list of themes to be covered during the SJWSs, mitigating measures (at SJWS 2 on 27 February) and storage (at SJWS 3 on 14 March).

> Objectives

The objectives of SJWS 1 were indicated as follows: (i) to get an update from ACER on the Initial Impact Assessment (IIA); (ii) to discuss the topics listed in the Agenda of the Meeting and (iii) to encourage inputs and suggestions from the stakeholders.

2. ACER'S INITIAL IMPACT ASSESSMENT

2.1. Overview of the IIA

Mr Benoit Esnault provided an overview of different trade-offs and issues that ACER has been working on while preparing the IIA. Their approach included the identification of the problem, the identification of the different policy options and the assessment of the chosen policy option. While following this approach, ACER focussed on: (i) being in line with the issue of market integration; (ii) ascertaining how to determine what discrimination is; (iii) justifying the policy choices made. As for the reasons behind the cost allocation test, ACER noted that they chose the approach of avoiding cross-subsidies between the two categories of users –domestic and cross-border– since it was easier to work on the aggregated figures.

Mr Thomas Querrioux explained that an IA should correspond to the requirements of the EC IA Guidelines. ACER's IIA is not intended to represent a cost benefit analysis of all possible options; it focusses only on main policy options and does not address individual impacts. ACER specifically highlighted the following: (i) what they work on is only an initial IA that will be provided on a voluntary basis and will combine all the evidence ACER gathered; (ii) it was a hard task to produce numerical evaluations of the impacts since they don't have information gathering powers; (iii) they invite ENTSOG to work on this IA further and to provide more evidence in terms of the quantitative analysis. As for the timing, ACER's initial intent was to publish IIA by the beginning of 2014. The delay was caused by the additional requests from the EC in December 2013 and some late content input. The content of the IIA includes the evaluation of the cost allocation methodologies, the approach towards the reserve price, the revenue reconciliation mechanism and payable price. When evaluating a particular policy option, ACER used the criteria of effectiveness, feasibility and acceptability.

ACER welcomed 'evidence-based debates' and recommended to avoid 'opinion-based debates'. The latter are unlikely to trigger changes in ACER's position expressed in the TAR FG when they deliver the reasoned opinion on the future TAR NC. In particular, ACER welcomed such evidence on the topic of circumstances and methodology inputs. ACER also provided their reasoning behind the TAR FG provisions on mitigating measures, non-physical backhaul and payable price.

2.2. Discussion

Q: ACER indicated that they will not change their positions reflected in the TAR FG unless new evidence is provided but the way in which the policy options were evaluated is not clear. When is the IIA supposed to be published?

A: It will be published by the end of Q1/2014 since we are trying to give consideration to the additional requests of the EC. The choice was made after the assessment of the policy options against: (i) the objectives of the Gas Regulation; (ii) their effectiveness in terms of how they meet these objectives; (iii) the stakeholder opinion.

Q: The TAR FG foresees that a number of issues are subject to the NRA decision. Why is the same approach not foreseen for the payable price?

A: It was generally agreed that having different trajectories of tariffs in the MSs should be avoided. The idea is to have a consistent approach between the tariff dynamics in the EU.

Open choice can lead to some under-recovery and having a commodity charge in order to fill the gap between the allowed and the actual revenue.

Q: ACER asks for the provision of evidence for why they should change their view but they do not provide the evidence that they based their decision on – why is that?

A: The consultation questionnaire for the draft TAR FG was underpinned by the request for substantiated evidence. The decisions we made are based on the evidence we received.

Q: Some of the TAR FG provisions are very bad for TSOs in terms of revenue recovery, in particular the rules on the multipliers. Can the evidence change some TAR FG rules?

A: The TAR FG provisions on the revenue recovery are intended to be as balanced as possible. The treatment of multipliers is not designed to be detrimental to the TSOs' revenues. The choice is based on the level of congestion.

Q: Some of the TAR FG parts are clear on what is supposed to be elaborated in the TAR NC ('the Network Code shall specify' or 'ENTSOG shall elaborate') but some of them just indicate the necessity of the NRA decision. Does it mean that the TAR NC will only include the parts where the TAR FG gives an explicit mandate for elaboration by ENTSOG?

A: The requirement for the TAR NC is to be aligned with the TAR FG. Where the TAR FG says that something is to be elaborated in the TAR NC, we expect ENTSOG's input. We also anticipate some clarifications from ENTSOG, e.g. on the cost drivers – how to use capacity and distance in the different formulas.

Q: The TAR FG incentivises backhaul capacity since it can lower fixed and variable costs. Why do these arguments not apply for interruptible capacity, especially counter flow interruptible on bidirectional points?

A: There is an additional argument for backhaul capacity: it creates movement in the direction that does not exist whereas interruptible capacity is built on the top of firm.

Q: We understood that we are going to see a preliminary version of the IA earlier than the end of Q1/2014. Why has the partially completed document not been released?

A: Previously we were confident that the IIA can be published by the end of January. After ENTSOG Kick-Off Meeting of 15 January, we had some interactions with the stakeholders and realised that: (i) the idea that the stakeholders have about what an IA should be is wrong; (ii) additional work on some aspects of the IA is needed due to some belated inputs; (iii) the examples need to be fine-tuned.

Q: In terms of the language that was used in ACER presentation, what is exactly meant by 'discrimination', 'consistency of tariffs at IPs', 'cross-border and domestic'?

A: The concept of 'non-discrimination' may cover many potential realities, we have chosen to analyse non-discrimination between the categories of cross-border and domestic users. The key question was how to find a methodology that would allow determining which costs are to be attributed to each of those two categories. The starting point is to isolate the costs to be covered by domestic users; the remaining part of the costs should be dedicated to cross-border users. We expect ENTSOG to contribute to the determination of the methodologies so that in the end we have a proper split of costs.

Q: We provided you with some evidence on multipliers in Germany and what happens if zero day-ahead prices are introduced. It will be complicated for the TSOs to give more evidence than we have today. We are keen to see the justification for the multiplier of 1.5 in the IIA.

A: The provision of evidence is time- and resource-consuming. There are some grey zones in terms of understanding what 'non-discriminatory' is. In the end, what we are looking for is having tariff structures that are justified and that allow the network user crossing several MSs to compare the tariffs. As for the simulation of the network, we made an example in August which we then elaborated further. We can share with ENTSOG the excel file with the calculations.

3. COST ALLOCATION TASKS

3.1. Overview

> Transmission Services Definition; List of Dedicated Services / Infrastructure

Ms Ann-Marie Colbert presented the overview of the scope of the TAR NC. It was re-iterated that the setting of the total allowed/expected revenue is out of scope for the TAR NC. The revenue from the transmission services is used as an input to the cost allocation methodology. The output from the cost allocation methodology indicates the reference prices. The interactions between the various Chapters of the TAR FG were described. Further on, ENTSOG's initial proposal for the definition of transmission services and the list of dedicated services/infrastructure was presented. It was specifically noted that certain confusion arises from the fact that 'dedicated services' are mentioned in the TAR FG twice – in the definition of transmission service and in Section 3.1.1. ACER was invited to provide their views on the presented interactions between the definition of transmissions services, the cost allocation methodology and the cost allocation test.

> Distance, Average Distance & Network Representation; Forecasting Models; Unstable Flow Patterns

Mr Laurent De Wolf provided an overview of the inputs and outputs of different cost allocation methodologies stipulated in the TAR FG. It was noted that 'network representation' would also be an input to the Capacity Weighted Distance approach. Further on, ENTSOG's initial proposals for addressing several tasks from the TAR FG were presented. On the task of giving guidance for the network representation, the algorithm to be followed was presented. On the task of elaboration of the approaches for distance and average distance, it was indicated that the notion of distance can still be used in a fully decoupled entry-exit system. On the task of development of the forecasting models, it was noted that the TAR NC can only give some broad guidelines. On the task related to inputs criteria for unstable flow patterns, ENTSOG's initial proposal is to use technical or booked capacity.

3.2. Stakeholder Views

Mr Kees Bouwens presented some 'thought-provoking questions' to trigger discussion. In particular, the objective of the TAR NC was highlighted and its linkage with the requirements of Article 13 of the Gas Regulation which are to be complied with as of 3 March 2011. The

Gas Regulation provides for the possibility of developing the Guidelines on the tariff-related issues. It was reminded that the tariff arrangements covered in the CAM NC represented only a placeholder and hence need to be addressed in the TAR NC. It was noted that the entry tariff might hamper cross-border trade. The issue of whether the TAR NC scope can be extended to capture non-IPs due to the impact on the cross-border trade was also raised.

3.3. Discussion

Q: You referred to a lot of simplifications needed for the tariff methodology, e.g. regarding the fact that large pipelines are cheaper than the smaller ones. Is it possible to have a reduction factor for large pipelines?

A: Not taking into account the sizes of the pipelines may result in the cross-subsidies. The distance might not be the only cost driver.

Q: In the 'virtual' world, distance and flows are not important. Why is the entry tariff detrimental for cross-border trade?

A: This statement was made specifically to IPs. Evidence shows that the end-consumers will pay for these entry charges whereas it seems to be more transparent to pay for the exit. Entry tariff at the border represents something like an import tax.

Q: The TAR FG does not fully reflect the situation of all MSs and creates the risks of discrimination of transit countries. The Czech Republic has repeatedly indicated to ACER the necessity of introducing the 5th cost allocation methodology and the possibility of having more than one regulatory account. We ask ENTSOG to consider the situation of the transit countries in the TAR NC development process.

A: This point has not been raised in any MS meeting so far. Hence, the EC asked for this statement to be sent to them so that it can be considered. ACER indicated that they did consider the 5th cost allocation methodology proposed by Net4Gas and they found that it already fits with the methodologies set out in the TAR FG. The proposed methodology is similar to the one applied in Portugal – using the matrix approach after splitting the costs.

Q: As for the two approaches for calculating the distance, is it possible for this group to decide on which one of those is the best to be followed?

A: The TAR FG asks ENTSOG to define the possible approaches but not to choose only one of them. ENTSOG has indicated two approaches and welcomes any other ones.

Q: Price difference between adjacent hubs does not reflect the price of the capacity. Apart from lowering the entry tariffs, another solution would be to make sure that the price difference between the adjacent hubs reflects the price at the IPs. What is the internal energy model that is pursued?

A: The EC wants a liquid market and to provide a level playing field for market participants. We do not decide on any top-down approach.

Q: Why did ACER rule out the commodity top-up charge approach, i.e. the possibility of applying a commodity charge in addition to the capacity charge? This top-up charge represents an adjustment that ensures revenue recovery by the TSOs.

A: We prioritised the approach of capacity charges with a view to ensuring tariff stability and visibility. The commodity charge is distorting the cross-border trade in some cases. The TAR

FG is based on the assumption that the majority of the costs are driven by capacity. Technically, the commodity charge is not excluded for non-IPs and can be used as a primary mechanism for the purpose of the revenue recovery on those points.

Also, the following comments were raised within the session:

- GIE: If we define the rules for cross-border points, the domestic points are automatically affected. In relation to the distance, there is a risk of losing locational signals which may have the impact on the investments of the TSO at a specific point. On the note of 'cross-border vs. domestic' it was indicated that the price at the VTP is not related to the costs but is determined by the market. The lower entry tariff is not automatically transferred to the customer.
- OGP: In the process of the consultation there were two separate questions: capacity charge vs. commodity charge and fixed price vs. floating price. The combination of those was not considered.
- ACER: In the past, transit was viewed as a separate activity with a possibility to have dedicated infrastructure for that. Now we should stick to the definition of 'transmission' from the Third Package and not to treat differently regional transmission, local transmission and transit.
- ENTSOG: We welcome the written inputs, comments and suggestions on the discussed issues and we will share them with the ENTSOG TAR WG.

4. INTERRUPTIBLE CAPACITY & NON-PHYSICAL BACKHAUL

4.1. Overview

> Interruptible Capacity Methodology

Mr Brendan O'Riordan presented ENTSOG's initial view on the methodology for determining the reserve prices for interruptible capacity. Three alternatives for offering the discount were indicated: (i) ex-ante discount; (ii) ex-post discount; (iii) the combination of both. The difference of the wording in the Gas Regulation and in the TAR FG was noted: whereas the Gas Regulation states that it is the probability of interruption that must be reflected in the price of interruptible capacity, the TAR FG stipulates that it is 'the risk (likelihood and duration)'. The two alternatives for reflecting the risk were presented. It was suggested that at the same time as the tariffs are published, the report on the assessment of the risk of interruptions may be published.

> Non-Physical Backhaul

Ms Violeta Bescos presented ENTSOG's initial view on the pricing of uni-directional interruptible capacity / non-physical backhaul capacity. Non-physical backhaul is very similar to interruptible capacity at bidirectional points since it can only be provided if there is a nomination for the gas flow in the opposite direction. The main difference with interruptible capacity is the reason for the interruption: for interruptible capacity it is too many nominations, whereas for non-physical backhaul capacity – lack of nominations in the opposite direction. Marginal pricing of non-physical backhaul capacity can create the risk of under-recovery for some TSOs and potential cross-subsidisation especially when competing

TSOs offer forward products and non-physical backhaul products in parallel at different IPs connecting the same systems. It was noted that ENTSOG welcomes stakeholder input on the topic discussed.

4.2. Stakeholder Views

Mr Stephen Rose provided his views as a Prime Mover. The risk of interruption at IPs is to be considered in conjunction with the requirements of the CMP Guidelines and of the CAM NC. It was noted that the network users can evaluate themselves the risk of interruption on the basis of information that the TSOs are obliged to publish per Gas Regulation (nominations, flows and system imbalances). Non-physical backhaul capacity should be priced the same as interruptible capacity.

4.3. Discussion

Q: The SOS Regulation requires offering physical backhaul at the IPs. In this respect, will non-physical backhaul capacity still be offered at many IPs?

A: A TSO may ask for an exemption from the SOS Regulation. CAM NC also includes minimum requirements for the offer of this product at uni-directional IPs; whether it is offered or not will depend on the level of demand of each point.

Q: The Gas Regulation states that the pricing of interruptible capacity is to reflect the probability of interruption and the TAR FG appears to be in clear contradiction to this since it foresees different prices for different sorts of interruptible capacity.

A: The EC have not considered the TAR FG to be against the Gas Regulation but this point will be re-checked by the EC.

Q: Regarding the advantage of non-physical backhaul, it was said that it reduces system operation costs, in particular the compressor usage. Why not price the backhaul capacity negatively because of its advantages?

A: If the non-physical backhaul capacity has the same drivers towards what might be interrupted on a particular day then its treatment should be the same as that of the interruptible capacity.

Q: Interruptible capacity should be discounted upfront, the alternative of the ex-post discount is not viable.

A: The suggested alternative is a different pricing mechanism and is one of the options for stakeholder consideration.

Q: Is the assessment report of the risk of interruption foreseen point by point or system by system? Do you foresee a discount point by point?

A: It is up to the TSO to decide if the assessment is done for each IP or for a group of IPs (if their risk of interruption is similar).

Also, the following comments were raised within the session:

- E.On: It should be priced at negative tariffs because it saves costs for the network.
- GIE: The benefits of the use of non-physical backhaul could be shared amongst shippers. Forward flow shippers should also benefit from its use, as they are the ones making it possible.

- Eurogas: There are no additional costs for non-physical backhaul capacity. How would the price for it be set? Why does the TAR FG foresee that it is priced at marginal costs?
- DNV KEMA: In order to avoid cross-subsidies, non-physical backhaul capacity is to be priced at least at incremental cost. Marginal cost pricing should be the minimum but for equity reasons it could be priced higher.
- ENTSOG: Interruptible capacity could be offered even if firm is not sold out. This is indeed the status quo in some systems across EU. Moreover, in many systems forecasted interruptible capacity bookings are taken into account when calculating the tariffs, TSOs have in this case target revenue to meet for firm and interruptible capacity.
- Ontras: Due to the rule on the sequence of interruptions foreseen in the CAM NC, if more than daily interruptible capacity is offered then it will lead to having different risks of interruption at the same point. Hence, ex-post discounts are a practical tool to approach this.
- ACER: We did not foresee an ex-post discount approach but an ex-ante one. However, it may have some merits which could be investigated. Marginal pricing of non-physical backhaul capacity was selected to promote the use of the product, but should not be priced below zero.

5. CAM-RELATED TOPICS

5.1. Overview

Ms Irina Oshchepkova provided the overview of the CAM NC-related topics to be discussed during the session. The difference in the scope of the TAR FG Chapters was shown.

> Payable Price

Mr Pavanjit Dhesi presented ENTSOG's initial view on the topic of payable price. It was noted that the approaches towards the payable price other than envisaged by the TAR FG should be given due consideration, in particular having three options: fixed price, floating price or their combination. The pros and cons of having fixed or floating prices were indicated. The TSOs need effective revenue recovery mechanisms and the diversity of the options will ensure that the best one is found for the relevant market.

> Bundled Capacity

Ms Irina Oshchepkova presented ENTSOG's consideration of the topic of bundled capacity pricing. The specific attention was given to the comparison of the TAR FG provisions and the current requirements of the CAM NC.

> Virtual Interconnection Points

Mr Jann Keller presented ENTSOG's initial view on the topic of VIPs. The algorithm of how to calculate the VIP tariff for each TSO in correlation with the applicable cost allocation methodology was shown. If a cost allocation methodology does not allow 'merging' of the physical IPs into a VIP then it may be necessary to calculate the weighted average of the individual IP tariffs.

5.2. Stakeholder Views

Mr Alex Barnes provided views on the topic of payable price. The three possible components of the payable price are: (i) variable reserve price; (ii) auction premium; (iii) top-up commodity charge. It was noted that the interactions with the revenue recovery mechanism should be given due consideration. The difference between the commodity charge on top of the fixed capacity charge vs. just the floating capacity charge lays in the risks taken when booking the capacity for more than one year ahead. With the latter approach the risk of variability is higher. Another point was made with regard to the timing of the tariff publication vs. the timing of the annual capacity booking.

5.3. Discussion

Q: The concept of commodity charge applied in the GB system was only to minimise the gap between the allowed revenue and the actual revenue. As stipulated in the TAR FG, it is the task of the NRA to decide on how often and how fast the regulatory account is to be reconciled with a view to avoiding sharp tariff adjustments. ENTSOG should not re-write the TAR FG and re-open the closed down debates.

A: The GB example showed what happens when the long-term bookings are dis-incentivised. In the process of the TAR NC development, all options should be considered and evaluated by the stakeholders. We need to make the best decision now since the NC amendment process takes too long.

Q: The best way to assure tariff stability and predictability is to have long-term contracts. They are also needed for investment signals. Without the possibility of having multipliers higher than 1.5 there is no incentive to book long-term capacity.

A: The network users need to get out of the long-term contracts, to be able to react to demand. 'Long-term' is defined under the Gas Regulation as more than a year and it does not seem enough for what the TSOs need.

Q: To be able to set a booking strategy, before March we need to know the annual price, the multiplier and the seasonal factor at least for the first year. Will it be addressed at the next SJWS 2?

A: Yes, under the topic of 'Tariff setting year – impact assessment'.

Q: The compromise solution could be to use the auction premium to minimise any price escalation of capacity at the time of its use.

A: From an ACER perspective, this option seems to be workable.

Q: What will happen in cases of a tariff increase due to the calculation of an average tariff at a VIP? Are the mitigating measures applicable?

A: The mitigating measures are possible to apply regardless of the reasons for the tariff increase.

Q: How many VIPs do you expect to be eligible in the EU?

A: The number of potential VIPs can be calculated. We should not mix the notions of VIP and VTP. The VIP is to be created between the adjacent entry-exit systems and intends to provide flexibility to the TSO in terms of which route to flow the gas through.

Also, the following comments were raised within the session:

- IUK: Having an option of fixed price for interconnector TSOs is particularly of importance due to the absence of captive demand.
- RWE: ENTSOG's presentation included suggestion that the auction premium can be escalated in line with the inflation. This can be done for the reserve price as well. There might be more options between the two extremes of fixed and floating payable price.
- Gasterra: Why not provide users with a choice of whether the price should be fixed or floating? In case of a fixed price, the TSO may have a premium which ensures more certainty and more investments.

6. CONCLUSIONS

> Information about the topics to be discussed at TAR NC SJWS 2

Ms Ann-Marie Colbert indicated the topics to be discussed at SJWS 2: (i) cost allocation tasks – circumstances/criteria and cost allocation test; (ii) mitigating measures; (iii) multipliers and seasonal factors; (iv) tariff setting year IA; (v) transparency.

> Summing Up; Closing Remarks

Ms Ann-Marie Colbert thanked the participants for their contribution to the discussions. The draft slides for the next SJWS will be uploaded onto ENTSOG website a couple of days the meeting. The participants were invited to register for TAR NC SJWS 2 once they receive the respective invitation.

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Next TAR NC stakeholder meeting (SJWS 2): **27 February 2014**

ALL DOCUMENTS RELATING TO THIS MEETING CAN BE FOUND ON THE ENTSOG WEBSITE AT
<http://www.entsog.eu/events/tariff>