ACER
Agency for the Cooperation of Energy Regulators

Briefing on recent developments on the Agency's work

ACER South South-East Gas
Stakeholders Group meeting (SSE GRI, 25th SH)

Belgrade, 7 May 2019

Agenda

1. Recent matters regarding the Agency *(5 min)*
2. GRI Coordination Group and regional meetings *(5 min)*
3. NC TAR implementation – Agency's national consultations' review *(15 min)*
4. Agency's decision on HUAT incremental capacity *(15 min)*
5. Agency's report on conditional capacities *(15 min)*

1. Recent matters regarding the Agency

The BoR and AGWG chairs

- New colleagues in some of the Agency's key roles:
  - » New BoR chair: Ms Clara Poletti (ARERA, Italy)
  - » New BoR vice chair: Mr Rolands Irlkis (PUC, Latvia)
  - » New AGWG chair: Mr Paulo Verdelho (ERSE, Portugal)

Possible new Gas Package

- The Agency is inputting in the new gas package proposal:
  - » ACER consultation paper by the summer on:
    - Targeted regulation
    - Cross-border tariffs
    - New gases/products
    - Infrastructure planning
- Coordinated at BoR level, inputs from ACER Gas Department and AGWG
- Complementary to CEER paper
- Let your inputs reach the Agency by end of May via the AGWG/BoR

2. GRI Coordination Group and regional meetings

GRI Coordination Group (CG)

Last meeting (43rd) held on 21 January 2019 via telco

Updates on:

- **South GRI activity**
- **SSE GRI activity**
- **Baltic Gas Regional Cooperation:** updates on market integration and other regional developments

Next GRI CG meeting: 25 or 27 June 2019 (physical+telco - tbc)

Baltic Gas Regional Cooperation

- Presented at the GRI CG (21 January 2019) and ACER (18 February 2019) meetings
- **LV, EE and FI NRAs** tried to agree on the single entry-exit system framework (**FINESTLAT)**
- **LT:** is consulting **2 tariff proposals** for 2020:
  1. A separate, national entry-exit zone
  2. Entry-exit **zone with FINESTLAT**
- ACER meetings with FI, EE, LV, and LT are planned

South GRI (FR, ES, PT)

Last meeting (24th Stakeholders Group) on 21 March 2019

Accomplishments of the South GRI Work Program 2017-2018

- **Target 1**. Use of interconnections in the Region
  - » Report published in October 2017
- **Target 2.** Gas balancing in the Region
  - » Report published in October 2018
- **Target 3**. Analysis of market integration in the Region
  - » **VIP Iberico** - the inclusion of the PT in MIBGAS and the implicit allocation mechanism.
  - » **VIP Pirineos** - the evolution of price spreads and the potential impact of the market areas merger in FR on VIP Pirineos.
- **Target 4.** Assessment of the infrastructure investment plans
  - » discussion about the TYNDP, PCI list, and GRIP process
- **Target 5.** Implementation of OSBB mechanism
  - » Completed on 1 April 2018

South GRI: work plan 2019-20

- SGRI **Work Plan 2019-2020**

1. **Infrastructures** → Update of the report on the use of infrastructures

2. **Market integration** → Analyses focusing on the inclusion of PT in MIBGAS and price spreads between the different market places.

3. **Contribution of gases to decarbonisation** → exchange experiences and coordinate the implementation of a balanced energy mix.

3. NC TAR implementation – Agency's national consultations' review

TAR consultation timeline

2018												2019									ACER
~~Jan~~	~~Feb~~	~~Mar~~	~~Apr~~	~~May~~	~~Jun~~	~~Jul~~	~~Aug~~	~~Sep~~	~~Oct~~	~~Nov~~	~~Dec~~	~~Jan~~	~~Feb~~	~~Mar~~	~~Apr~~	May	Jun	Jul	Aug	Sept	Analysis
		NL: 12 Mar - 28 May																			√
				SE: 30 Apr - 30 Jul																	√
				RO: 9 Jun - 14 Sept																	√
						NI: 30 Jun - 30 Aug															√
							DK: 15 Aug - 16 Nov														√
							PT: 17 Aug - 17 Oct														√
								PL: 28 Aug - 31 Oct													√
								PL Yamal: 28 Aug - 31 O													√
								SI: 31 Aug - 31 Oct													√
									IUK: 4 Oct - 3 Nov												√
									BE: 8 Oct - 7 Dec												√
									IT: 16 Oct - 17 dec												√
									DE: 17 Oct - 17 Dec												√
									CZ: 1 Oct - 31 Dec												√
									EL: 10 Oct - 31 Jan												√
										HU: 31 Oct - 15 Jan											√
	NRA									SK: 6 Nov -6 Jan											√
	TSO										IE: 11 Dec - 11 Feb										√
	IC										HR: 18 Dec - 18 Feb										√
												AT: 31 Jan - 31 Mar									
												BBL: 25 Feb - 25 Mar									
													LT: 5 Mar- 6 May								
													FI: derogated								
																BG: tbc					
																EE: tbc					
																LV: tbc					
																	FR: tbc				
																	ES: tbc				
																	GB: tbc				

Deadline for publishing the NRA motivated decision

Consultation information available at ACER's website link

RPM compliance with Article 7

- Transparency
  - » Publication and justification of the RPM
  - » Reproduce and forecast transmission tariffs
- Cost reflectivity
  - » Transmission tariffs shall take into account the actual costs incurred for the provision of transmission services, considering the level of complexity of the transmission network
- Avoiding undue cross-subsidisation, non-discrimination
- Non-distortion of cross-border trade
- Volume risk
  - » Safeguard domestic customers from the risk associated with significant transit flows

Differences between EU systems

- Combination of very different national gas systems
  - Small vs. big demand: from 1bcm/y to more than 80bcm/year
  - LNG dependent vs. pipeline dependent countries
  - Single supplier vs. very diversified supply structure
  - Various structures of demand and consumption seasonality

- Different positions along the gas value chain
  - Upstream countries: producers
  - Midstream countries: transit countries
  - Downstream countries: consumers

RO tariffs consultation analysis

- ANRE reopened the consultation to include non-transmission services and a simplified tariff model.
- Easy to understand and the cost allocation assessment does not show a high degree of cross-subsidies
- RPM justification is insufficient to comply with the requirement to take a motivated decision.
- ACER recommendations to include in the final decision
  - An analysis of the relevance of distance as a cost driver.
  - The requirements listed in Article 7 of the NC TAR.
  - The conclusions of the comparison with the CWD methodology.
  - Indicate the manner in which non-transmission tariffs are reconciled.
- Additional ACER recommendations to include in the final decisions:
  - How the costs of transit pipelines are taken into account.
  - How the RPM is applied to points related to the transit pipelines.

PL tariffs consultation analysis

- No sufficient details to justify the choice of the RPM (meshed network/investment)
- Lack of transparency on the duration of the regulatory period and variable entry-exit split → forecast of reference prices is uncertain
- Lack of pre- and post-adjusted tariffs in the counterfactual CWD → consistent comparison is difficult
- Lacks of consistent evaluation of the proposed RPM against Article 7 criteria
- Yet, based on its own analysis, the Agency was able to conclude that the RPM complies with the requirements laid out in Article 7.

PL - Yamal analysis

- A modified CWD is proposed, not clearly described and are likely to be incompliant.
  - » role of the cost drivers unclear
  - » Agency could not easily assess cost-reflectivity, cross-subsidisation and effects on cross-border trade.
- If modifications are incompliant → the Agency recommends to adopt a simpler and more transparent distance-based RPM.
- Lack of transparency on the duration of the regulatory period and variable entry-exit split → forecast of reference prices is uncertain
- The simplified tariff model is not point specific

SI tariffs consultation analysis

- Costs drivers defined on the basis of geographical areas
  - » Complex and not transparent
  - » Leaves discretion when defining the areas
  - » Justification is insufficient
- The RPM is not cost-reflective and does not prevent undue cross-subsidisation.
  - » the RPM might aim at incentivising cross-border flows by lowering tariffs at IPs
- Not compliant use of adjustments (to differentiate domestic exits)
- ACER recommends considering benchmarking to:
  - » Simplify the RPM
  - » Address competitiveness of IPs
  - » Ensure transparency.

IT tariffs consultation analysis

- The proposed RPM is compliant with the requirements in Art 7 of cost-reflectivity, cross-subsidisation and cross-border trade.
- The RPM is not compliant with the transparency requirement as it does not allow users to reproduce and forecast tariffs accurately. This results from:
  - The proposed capacity reshuffling mechanism
  - The calculation of distances as an input to the CWD methodology
- The simplified tariff model does not cover commodity charges nor allows estimating the evolution of tariffs beyond the first tariff period.
- Discounts to domestic exits located within 15km of the national transmission network are not compliant with the NC TAR.
- The TSO charges several services that are not assessed in the consultation (e.g. storage charges). The Agency recommends ARERA to assess whether they are 'access services' and therefore fall under the scope of the NC TAR.

CZ tariffs consultation analysis

- Two distinct regulatory regimes proposed to mitigate volume risk. To clarify:
  - » Cross-system and intra-system costs split
  - » Details on risk premium for cross-system infrastructure
- Other incompliances:
  - » Tariff stability mechanism that averages tariffs over consecutive regulatory periods
  - » Fixed payable prices (not allowed under revenue cap regime)
- ACER could not conclude that the methodology is cost-reflective (information available was insufficient).
- The RPM seems to be compliant with the requirement of preventing undue cross-subsidisation.

SK tariffs consultation analysis

- Neither the public consultation nor the proposed RPM are compliant with the NC TAR.
- The RPM is not based on a target revenue established by the NRA, which should be the starting point for applying the RPM.
- The propose RPM is marginal and non-transparent and cannot be considered as the methodology used for setting tariffs.
  - » 75% of the capacity is booked on the basis of fixed price contracts.
  - » The RPM is not used to set reference prices at domestic points.
  - » The RPM is not used to set reference prices at points with third countries.
- The Agency recommends that:
  - » URSO reviews Eustream's costs and establishes the target revenue, or the methodology to set it, based on efficiently incurred costs of the TSO.
  - » A new TAR consultation process is started

HU tariffs consultation analysis

- The assessment against the requirements in Art 7 is incomplete and insufficient.
- Cost-reflectivity, avoidance of undue cross-subsidisation, and non- distortion of cross-border trade are not met
- Storage discounts are not taken into account in the cost-allocation assessment nor in other ratios
- Application of rescaling (aims at tariff stability, but leads to an under-recovery).
- Invalid comparison with CWD as the two methodologies lead to different levels of revenue recovery.

- The Agency recommends MEKH to:
  - » Provide a detailed justification of the proposed RPM against the criteria set out in Art 7 together with the rest of calculations required in Art. 26(1).
  - » Align compliance on specific elements (storage discounts, rescaling, revenue recovery).

EL tariffs consultation analysis

- RAE proposes a postage stamp RPM. The choice to disregard distance as a cost driver is not sufficiently motivated.
- LNG socialisation: 75% of the allowed revenue of the LNG terminal is recovered via transmission charges (RPM). The Agency recommends to:
  - » Not use the RPM to allocate this revenue.
  - » Allocate as non-transmission instead to make these revenues subject to the requirements of Article 4(4) of the NC TAR.
- Large negative regulatory account accumulated over 16 years. To be reconciled using a commodity charge.
  - » ACER recommends, based on Art. 17, to minimize over-/under-recovery, recover revenues timely and avoid significant differences of tariffs between tariff periods.

HR tariffs consultation analysis

- The Agency considered that HERA consultation is broadly in line with the requirements of the NC TAR.
- The decision to build the Krk LNG terminal (2021) impacts the RPM.
  - » Croatia (currently both a producing and an importing country) might export gas in the future ➔ important decrease of cross-border exit fees and end of the commodity charge
- Some services provided by the TSO were neither considered by HERA as transmission nor as non-transmission services.
  - » The Agency recommended to reassess this classification.

Best practices: policy learnings

- The choice of RPM should be sufficiently justified in relation to:
  - The structure of the network
  - Art. 7 principles (cost-reflectivity, cross-subsidisation, cross-border trade, volume risk and transparency)
  - National policy goals in relation to the RPM (explicit)
- All services that are provided by the TSO to enable network users to gain '*access to the natural gas transmission networks*' should be included in the consultation.
  - Transparency about all tariffs charged by the TSO (even for charges not related to TSO activities).
  - In case of doubt, ACER looks at '*access to networks*' in a broad sense to decide if a service falls under the scope of the TAR NC
- Simplified models should allow reproducing/forecasting tariffs accurately
- Provide CAA pre- and post- adjustments.

4. Agency's decision on the HUAT incremental capacity project proposal for the IP Mosonmagyaróvár

Incremental capacity process
CAM Network Code, recital 11

- *A streamlined and harmonised Union-wide process for the **offer of incremental capacity** is necessary to react to possible market demand for such capacity. Such a process should*
  - *consist of regular demand assessments*
  - *followed by a structured phase of design and allocation,*
  - *based on effective cooperation between TSOs and NRAs across Union borders.*
- *Any investment decision to be taken further to the assessment of market demand for capacity should be **subject to an economic test to determine the economic viability**.*
- *This economic test should in turn ensure that **network users demanding capacity assume the corresponding risks associated with their demand** to avoid captive customers from being exposed to the risk of such investments*

Decision HUAT Incremental Project

- The Agency published the Decision based on Article 8(1) of Regulation (EU) 713/2009.
- The Agency consulted concerned NRAs, TSOs and third parties
- The Agency facilitated the process to reach the binding phase.
- Importantly,
  - *No cost would be socialised and the captive users in the Hungarian network would not be impacted. The f-factor would ensure that stakeholders interested in the project bear the costs. In Austria, socialisation is approved in line with the NRA view on the project.*
  - *Once the binding round takes place, stakeholders will decide to pay or not for the development of HUAT.*

The decision: principles

Aim: approving terms and conditions to proceed to next step in incremental capacity process (annual auction -binding capacity commitments- and economic test)

- The economic test compares the present value (PV) of revenues from the auction of incremental capacities to the present value of the estimated increase of the allowed revenues due to the incremental project.
- The f-factor sets the share of allowed revenues to be covered directly from incremental capacity bookings (1 = all costs must be carried by network users bidding for incremental capacity)
- **Economic test is positive if:**
  - $PV_{(capacity\ booking\ revenues)} \geq f\text{-}factor \times PV_{(estimated\ increase\ allowed\ revenues)}$
  - If the economic test is positive, the project shall be implemented; if not, the incremental project is terminated.

The HUAT incremental capacity project

- Increase of capacity at Mosonmagyaróvár interconnection point, direction from Hungary to Austria

- Two technical projects considered based on non-binding market demand
  - » Smaller project offers 5,740,470 kWh/h/a firm yearly capacity
  - » Larger project offers 10,007,100 kWh/h/a firm yearly capacity
  - » In both cases, 10% technical capacity set aside for shorter term products

- Binding commitments to be requested in annual yearly capacity auction in July 2019 in order to carry out the economic test

Main parameters economic test

Parameter	AT	HU
Discount factor	5.188% **(NRA approved WACC)**	8.47% **(NRA suggested WACC for HUAT project)**
Depreciation period	15 years **(as proposed)**	15 years **(as proposed)**
F-factor (0 to 1)	0.5 (offer level I)/ 0.75 (offer level II) **(as proposed)**	1 **(as proposed)**
Reference price	0.77 EUR/kWh/h/a **(as proposed)**	631.25 HUF/kWh/h/a **(as proposed)**
Minimum premium that makes economic test positive for set capacity booking threshold (NC TAR)	1.40 EUR/kWh/h/a for threshold 1,913,490 kWh/h/a (around 33% offer level I) **(as proposed)** 1.27 EUR/kWh/h/a for threshold 6,714,000 kWh/h/a (around 67% offer level II) **(as proposed)**	3,441.41 HUF/kWh/h/a for threshold 4,305,353 kWh/h/a (around 75% offer level I) **(set according to TAR NC)** 2,421.74 HUF/kWh/h/a for threshold 7,505,325 kWh/h/a (around 75% offer level II) **(set according to TAR NC)**
Interpretation positive economic test	**In case of positive economic test, 50% / 75% of project costs (smaller or larger technical project) are recovered from bidding network users within 15 years; remainder is socialised according to f-factor***	**In case of positive economic test, full project costs are recovered after 15 years from bidding network users*. No cost are socialised**

* Disregarding potential revenues from bookings in excess of threshold level, from bookings of capacity set-aside for shorter term bookings, revenues beyond 15 years of initially offered capacity

5. Agency's report on conditional capacities

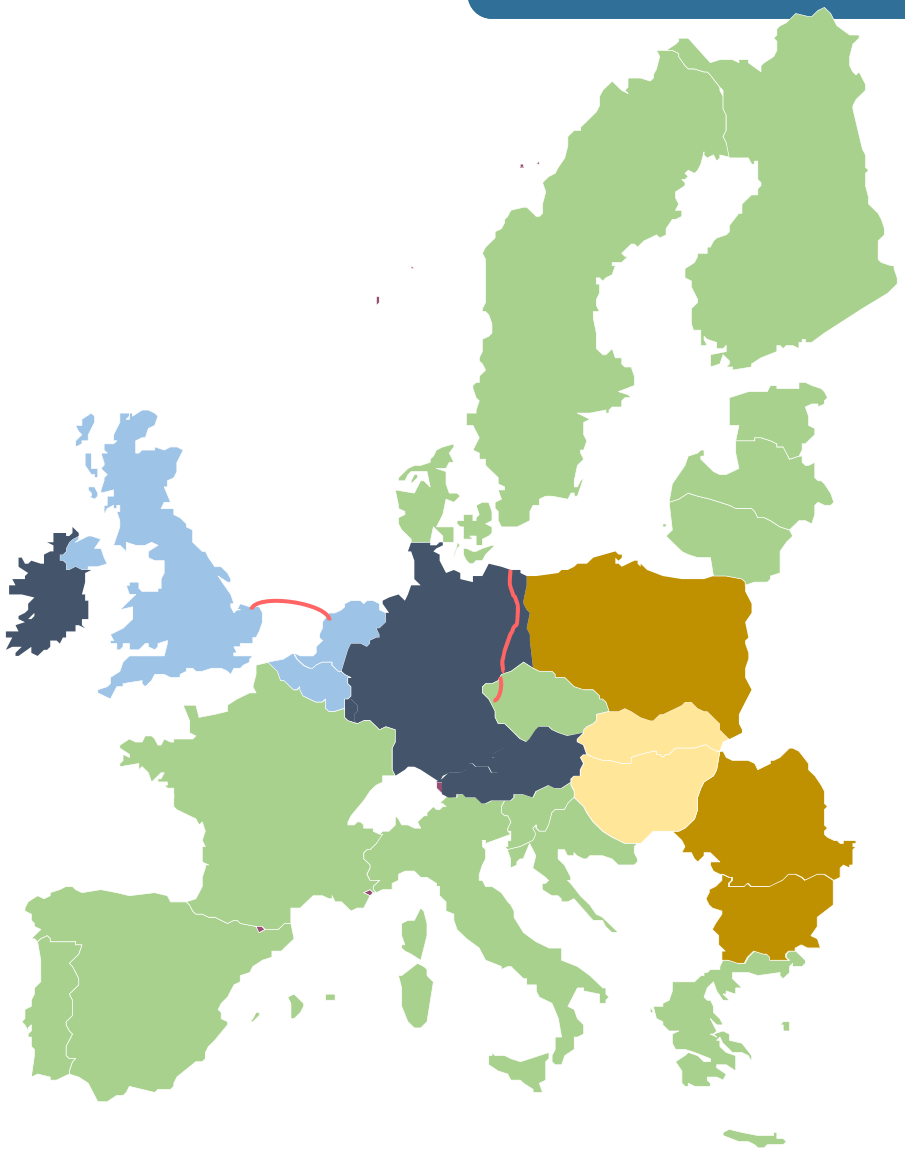
What is the study about?

- **Agency's legal obligation → CAM NC, Art 38.4**
  - » reporting on the conditionalities stipulated in contracts for standard capacity products for firm capacity, having regard to their effect on efficient network use and the integration of the Union gas markets

- **Background: the entry-exit system → Gas Directive and Regulation**
  - » non-discriminatory network access
  - » freedom to book entry and exit capacity independently
  - » network charges shall not be calculated on the basis of contractual path

The Report assess the existence, extent, and application of conditions on firm capacity that limit the functioning of the full entry-exit systems

Where are conditionalities?



Conditional products: restriction to firmness and/or allocability of firm capacity (e.g. bFZK, BZK, DZK)

Non-firm services: modifying the standard conditions of firm capacities (e.g. wheeling, OCUC, short-haul) to designate balanced flows from specific entry to exit points

Dedicated transit pipelines: infrastructure used for transit with partial or no connection to the rest of the transmission system, and designated point-to-point flows on the basis of legacy transit contracts

Legacy transit contracts: long-term transit contracts through which capacity is booked at IPs of the transmission system

No conditionalities

Pipelines with TPA exemption, granted by the pertinent authorities, in accordance with the provisions of Directive 2009/73/EC

Dedicated transit pipelines and transit contracts

Dedicated transit pipelines

Romania

Two transit systems:

- T1 Pipeline: no historic contract in place, but the pipeline is not yet connected with the Romanian transmission system (undergoing).
- T2&3 Pipeline: historic contracts reserve 100% of the capacity until 2023.

Bulgaria

The interconnection point between national and a transit network cannot accommodate free flows.
On the transit network 99% of capacity is booked through a long-term transit contract until 2030

Poland

A historical contract reserving part of the capacity is in place on the TGPS pipeline.
The rest is marketed by GAZ-SYSTEM ISO.
Information on the historical contract (expiry, capacity) is confidential.

Long-term transit contracts

Hungary

50-60% of capacity to Serbia is allocated through a long-term transit contract. The rest is available through auctions. Transit concerns IPs with third countries (no NC CAM procedures needed). Network users show limited interest to contract remaining capacity

Slovakia

Long-term transit contracts are still in place, as network users were not interested to convert them to entry-exit ones.
Booked capacity of transit contracts corresponds to just 13.5% of overall booked capacity at entry and exit points

Removing conditionalities

- Simulations show:
  - » Higher impacts when conditionalities are widely used and the market is short
  - » Effects to interconnected areas
  - » Price reduction
  - » higher liquidity of the market
  - » increase in market integration when upgrading capacities

- …But this analysis does not take into account the costs of capacity upgrading

Conclusion on conditionalities

- Status
  - » Not fully in line with current regulatory framework
  - » Broadly used, in different forms, in different MSs
  - » Legacy from the past (pre entry-exit system)…
  - » …but possibly expanding in the future
    - DE (market merger)
    - EL (accommodating TAP pipe)
    - HU (serving power plants)

- Effects
  - » Lower liquidity (or at least liquidity transfer)
  - » Missing level playing field (some MSs invested to remove conditionalities)
  - » Lower transparency & harmonisation
  - » Possibly improved cost-efficiency, at least locally

Recommendations

- Create a EU catalogue of allowed, standardized conditionalities
- Increase transparency (products specifications, volumes, prices, etc.)
- Adopt a case-by-case approach for upgrading or removing conditionalities
- Gradually blend-in transit routes
- Verify pricing rules (conditional vs. interruptible products)
- Investigate the implications for the tariffs methodologies
- Legislative review (new Gas Package)
  - » Define the entry-exit model, allowed deviations (and their rationale)
  - » Give clear directions on the two options:

Complete the e-e system and address:
- Related high tariffs increase
- End of LT non-standard contracts

Only selectively remove conditionalities:
- Standardise what remains
- Deal with a reduced tariffs increase