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Principles on Calculating Tariffs for Access to Transmission Networks – An ERGEG Public Consultation Paper

Thank you for the opportunity to comment on this consultation. The European Federation of Energy Traders (EFET) considers that getting the tariff equations right is a key part of the work to ensure that system access and investment can occur efficiently. EFET agrees that a common set of principles will help to harmonize calculations and procedures.

EFET considers that there is little to argue about with the general principles for calculating transmission revenues for regulated businesses. The detail of how those revenues are translated into user tariffs is often more contentious, particularly when considering objectives of non-discrimination between comparable network users and reducing cross subsidization.

We have specific comments on different sections of the consultation.

Section 4 Issues

It would be desirable for the overall tariff design to be consistent with the framework for capacity release and allocation, and also consistent with creating a level playing field where shippers can compete. It should be possible to avoid situations that distort the capacity buying decision in favour of short or long term capacity contracts, but rather allow shippers to manage portfolio needs through a variety of properly priced capacity contracts.

Specifically, it is necessary to consider how network expansions should be priced, and how short term prices should be calculated.

- It is insufficient to use past prices as a guide to the future under an expansion scenario. Expansion costs may be higher or lower per unit. Seeking to protect the capacity value of previous long term capacity buyers by keeping tariff levels at historic prices does not have a rational economic basis, and will result in a cost and revenue mismatch.

- Similarly short term tariffs should more properly reflect the supply-demand balance. EFET does not understand the risks mentioned in section 4.4 and we do not believe that short term contracts are any more risky for TSOs when they are part of a properly construction range of capacity auctions. Overall risks are better managed by giving shippers the ability to obtain a variety of contracts and hence the ability to shape needs in line with business requirements.

At a detailed level, the introduction of measures such as entry-exit tariffs also raises questions about the appropriate tariff split, and how to deal with under and over recovery of revenues necessary to fulfill agreed price control returns. Guidance on these issues may prove useful in order to avoid a large variety of approaches and the risk of cross subsidization. An example of this would be where auctions are used for entry capacity and this results in an over recovery of the required revenue. The TSO must find a way to use this revenue that creates the least distortion.

For interruptible tariffs, the basic principle in the consultation is sound, but this must be assessed against the way in which a TSO seeks to manage its risk. EFET has concerns about situations where a significant amount of interruptible capacity is sold at near firm prices for a sustained period. This would seem to indicate that the TSO is forcing too much risk back on shippers by holding a cheap or free option on interruption.

A better solution is where the maximum possible firm capacity is offered to the market. When this is coupled with an efficient secondary market that increases the utilisation of the sold capacity, this should leave only a residual amount of interruptible capacity for sale. The chance of interruption for this residual capacity would naturally be higher, and it may simply make more sense to offer this to the market on a zero reserve auction basis so that shippers can assess their own risks.

In terms of transparency, we welcome the proposals on the historical flows, and believe that the value of this information would be enhanced by a better understanding of the underlying available capacity.

EFET agrees that more work is required on balancing charges. We support the concept of market based pricing rather than the use of penalties which are detrimental to competition.

Efficient balancing would also be enhanced by having well structured Operational Balancing Agreements between TSOs. These may provide a logical first step toward harmonization and regional balancing.

For the use of revenues, EFET agrees that revenue should be returned when this is above the regulated returns, and indeed mechanisms may also be needed to deal with the under recovery of revenue. In any case, care is needed to ensure that such revenue flows are not unduly discriminatory noting that different parties will occupy different parts of the supply chain. For example, it may not be appropriate to reallocate entry revenues to the distribution level. In addition, consideration should be given to investment remedies where the over recovery of revenue is significant and persistent as this could indicate ongoing congestion.

Section 5 Issues

EFET broadly agrees that infrastructure investment incentives should be considered in some circumstances. We would encourage the development of a broader discussion on this point, which may include:

- consideration of the appropriate balance of risks between shippers, network operators and consumers;
- the development of pragmatic economic tests for investment decisions in order to provide greater certainty for shippers on outcomes, and TSOs on the treatment of the investment in the asset base;
- clarity on measuring strategic benefits at least on a regional level; and
- consideration of how to allocate costs across interconnecting systems which would help to ensure that investment occurs in the most efficient location.

Section 6 Issues

We believe that the stated criteria to assess effective pipe to pipe competition follows general economic principles, and it is important to have clarity on how any assessment would be made.

However, EFET considers that Europe is unlikely to have any significant pipe on pipe competition. The history of the development of national grid systems and specific transit pipes places the overall network in a position as a natural monopoly rather than competing pipes.

Thank you again for the opportunity to comment on the consultation. If you have any questions on this response we will be pleased to follow up any points.

Yours sincerely,

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EFET Gas Committee