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IMPLEMENTATION OF THE NETWORK CODE ON HARMONISED TRANSMISSION TARIFF STRUCTURES FOR GAS

Discussion of comments received

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1 SUMMARY OF RESPONSES RECEIVED

On 17 August 2018, ERSE launched a public consultation process, entitled "Implementation of the Network Code on Harmonised Transmission Tariff Structures for Gas". The consultation process, which took place between 17 August 2018 and 17 October 2018, resulted in the participation of 13 entities that submitted comments.

The list of entities participating in the public consultation is summarized in the table below.

Official ERSE Councils	▪ Advisory Council ▪ Tariff Council
Spanish Sector Regulator	▪ Comisión Nacional de los Mercados y la Competencia (CNMC)
Transmission system operators	▪ Portugal: REN ▪ Spain: ENAGAS
Suppliers	▪ EDP Comercial[1] ▪ Endesa ▪ Galp Gás Natural ▪ Iberdrola
Other entities in the natural gas sector	▪ Naturgy Group (Naturgy) ▪ EDP S.A. (EDP) ▪ Portuguese Association of Natural Gas Companies (AGN) ▪ European Federation of Energy Traders (EFET)

In summary, the main comments[2] received are as follows:

- ERSE should ensure coordination with CNMC, the body responsible for regulating natural gas in Spain. It should be noted that at the launch date of the public consultation by ERSE, the timetable set by Spain for the analogue consultation process was unknown.
- The majority of the comments approve the proposal for the reference price methodology, in particular because it is simpler and more transparent than the tariff methodology currently in force.

[1] The comments and suggestions of this supplier are reflected in the document submitted by EDP S.A.

[2] This synthesis of comments made by ERSE brings together, on the one hand, the most frequent comments and, on the other hand, the comments considered more relevant to the discussion (even if less frequent).

- Some comments consider it inappropriate to differentiate prices between the entry point from the VIP and from the LNG terminal, namely to avoid a higher price at the VIP.
- The new entry-exit split proposed by ERSE should be introduced gradually, in coordination with Spain and should be accompanied by an impact assessment.
- The change in the entry-exit split should lead ERSE to reassess the communication of the tariff impacts, since in the case of an increase in the proportion of revenues to be recovered at entry points, final consumers perceive a reduction in the transmission tariff paid although it will be offset by an increase in the transmission tariff at points of entry paid by market agents and passed on to the cost of energy for consumers.
- Zero capacity prices at exit points to the VIP, to the LNG terminal and to the underground storage are considered adequate by the transmission system operator in Portugal. However, the transmission system operator in Spain (ENAGAS) questions the rationale for the application of zero capacity prices at the exit point to the VIP.
- A number of participants point to the relevance of the 'tariff pancaking' problem[3], where a lack of coordination between Portugal and Spain can exacerbate this problem.

The exhaustive list of the comments received, as well as their discussion by ERSE, is provided in the following chapter.

[3] 'Tariff pancaking' refers to the accumulation of transmission tariffs paid by cross-border flows of natural gas: since natural gas must pay transmission tariffs at entry and exit points each time it crosses a transmission network, a cross-border flow has to support the transmission tariffs of the various transmission networks it crosses. Several market players consider this accumulation of transmission tariffs excessive.

2 DISCUSSION OF RESPONSES RECEIVED

Although the public consultation comprehended a set of eleven questions, due to the structure of the responses received it is more convenient to present the set of responses received according to the topics addressed.

Topic	Response received	Observation by ERSE
New regulatory period	With a view to the new regulatory period 2019-2022, tariff stability should be preserved and excessive rigidity in the parameters for the next regulatory period should be avoided. In addition, a time schedule was requested for the implementation of the network code and an evaluation of the changes introduced. **(Advisory Council, Tariff Council, Galp Gás Natural, AGN)**	ERSE underlines that the regulatory changes required under the network code will still be discussed within the regulatory review process which will precede the next regulatory period. The changes to be proposed in the regulatory review will take into account the comments received to this public consultation, and in addition the results of the analysis by the Agency for the Cooperation of Energy Regulators (ACER). ERSE takes note of the need to present the timing of the changes, to be introduced in a phased manner, and to monitor the impacts caused.

Topic	Response received	Observation by ERSE
Coordination with Spain	It is important to ensure coordination with the only country with which Portugal has a physical border. This coordination should include the definition of the parameters that determine the transmission tariffs, namely the entry-exit split. The coordination should involve ERSE, CNMC and other stakeholders of MIBGAS, which will allow to improve the functioning of MIBGAS. REN considers it a good idea to continue working with CNMC to harmonize the regulatory framework (for example in terms of tariffs), since a substantial part of the gas consumed in Portugal uses Spanish infrastructures (in 2017, around 43% of natural gas entering Portugal used the interconnection points). **(Advisory Council, Tariff Council, REN, Endesa, Galp Gás Natural, EDP, AGN, EFET)**	ERSE recognizes the importance of articulation with Spain, and in particular with CNMC. This coordination has been pursued under the South Gas Regional Initiative (South GRI). The present consultation included a consultation with CNMC which stated that it had no further comments.
Modified CWD methodology	ERSE's proposal to change the current method of calculating the reference price (matrix method) towards the modified capacity-weighted distance (modified CWD) methodology was evaluated positively by all the participants that commented on it. The comments acknowledge that the new methodology is simpler, allowing a better understanding by the stakeholders. Galp Gás Natural referred to the need for ERSE to monitor the effectiveness of this change. **(Advisory Council, Tariff Council, REN, ENDESA, Galp Gás Natural, AGN, EDP)**	ERSE takes note of the favorable comments on the modified CWD methodology and will monitor the impact that the adoption of the new methodology may have on the market.

Topic	Response received	Observation by ERSE
Requirements for the reference price methodology	Naturgy considers that the proposed methodology does not meet the requirements of Article 7(c) and 7(e) of the tariff network code. The company claims that Article 7(c) is not met due to the differentiation in transmission tariffs at the entry point from the VIP when compared to the entry point from the LNG terminal, since in the new methodology prices are different, resulting in a discrimination. The company believes that prices should be the same, in line with the current tariff situation. As regards Article 7(e), which provides that there should be no distortion in cross-border trade, the company claims that the discrimination between entry point prices from the VIP and from the LNG terminal does not allow this requirement to be met. **(Naturgy)**	With regard to Article 7(c), the lack of price equalization between the entry points from the VIP and from the LNG terminal cannot be classified as a situation of discrimination or undue cross-subsidization. The different prices resulting from the methodology result from the analysis of the three allocation factors used, namely capacity, distance and unit cost. Since the unit cost applicable to entry points from the VIP and from the LNG terminal are identical, the difference in prices results exclusively from the use that these two points make of the transmission network in terms of capacity and distance (compared to the other points in the network). In addition, the tariff network code limits the possibility of price equalization after the application of the reference price methodology to some or all points within a homogeneous group of points [Article 6(4)(b)]. According to the definition of "homogeneous group of points" in Article 3(10), interconnection points and LNG facilities do not belong to a homogeneous group of points, being impossible the equalization of prices under these terms. With regard to Article 7(e), ERSE stresses that a price difference does not necessarily imply price discrimination under the aforementioned article (and is consequently not a distortion in cross-border trade). The reference price methodology proposed by ERSE objectively determines reference prices based on the abovementioned allocation factors, without discriminating the prices of capacity products specifically for cross-border flows.

Topic	Response received	Observation by ERSE
Zero capacity prices at the exit to the VIP	ENAGAS stresses that the application of zero reserve prices at the exit point to the VIP does not result from the application of the methodology, but rather from an 'ad hoc' decision by ERSE. Although recognizing that the predominant flow in the Iberian VIP is in the ES->PT direction, physical flows can also occur in the opposite direction. Additionally, if the use of the LNG terminal in Sines continues to increase, the likelihood of reverse flows will increase. ENAGAS also adds that the interconnection point at Valença do Minho was initially designed to be unidirectional towards PT->ES to supply Galicia in the North of Spain (GME project, which was later adapted to have a bidirectional connection). REN agrees with the rationale presented by ERSE in the public consultation justifying zero capacity prices at the exit points to the VIP, to the LNG terminal and to the underground storage. **(REN, ENAGAS)**	ERSE stresses that regarding the physical flows with commercial origin, the exit point to the VIP has been used only in the direction ES->PT. The result can be confirmed on the ENTSOG transparency platform (https://transparency.entsog.eu/#/), for example for the period between October 2015 and September 2018. Additionally, from the point of view of the need to increase interconnection capacity in the near future, in particular at the interconnection point in Campo Maior, whose annual utilization was around 70% in 2017, the contracted capacity in the opposite direction to the dominant flow can avoid or postpone the need to reinforce the interconnection. This reality will be monitored by ERSE.
Capacity prices at the entry points	Iberdrola states that the new methodology has a negative impact on industry competition since it attributes a higher entry price to the VIP compared to the entry price for the LNG terminal (the LNG terminal is only used by one or two companies, while smaller suppliers use the VIP). In addition, due to the existence of a significant south-north transit, the more natural gas is injected from the south (from the LNG terminal), the greater the need for future investments. Therefore, even if the methodology leads to higher entry prices at the VIP, the tariff approval should ensure that entry prices for the VIP are not higher than the entry prices for the LNG terminal (since 2010 ERSE equalizes entry prices for the VIP and for the LNG terminal). **(Iberdrola)** The existence of different prices at entry points from the VIP and from the LNG terminal increases the risk of tariff deviations due to the price relationship between natural gas and LNG, particularly with an entry-exit split that allocates a higher proportion of revenues to the entry points. **(REN)**	Effectively the new methodology results in a higher entry price for the VIP than for the LNG terminal. This was already happening with the matrix methodology, with ERSE equalizing prices ex-post. However, the tariff network code limits the price equalization after the application of the reference price methodology to some or all points within a homogeneous group of points [Article 6(4)(b)]. According to the definition of "homogeneous group of points" in Article 3(10), points of interconnection and LNG facilities do not belong to a homogeneous group of points, being impossible the equalization of prices under these terms. Regarding the risk of increased tariff deviations, this situation will be evaluated and monitored during implementation, as suggested by REN. ERSE has taken note of the comments and will assess the possibility of accommodating concerns under the tariff network code.

Topic	Response received	Observation by ERSE
Entry-exit split	The responses consider that a change in the entry-exit split of its current value of 27%-73% to the new value proposed by ERSE of 40%-60% should be carried out gradually, for example over the regulatory period. The implementation of the new entry-exit split should still be subject to re-evaluation, avoiding a rigidity of these parameters. This will make it possible to adapt this parameter to external conditions, such as the consultation process in Spain, a possible solution to eliminate 'tariff pancaking' between Portugal and Spain or the reaction of market players to the new entry-exit split. REN and Naturgy agree with the economic rationale that led to the entry-exit split (although Naturgy underlines that insufficient information on the structure of transmission system assets was provided to assess the resulting breakdown). Endesa pointed out that the new entry-exit split proposed by ERSE is closer to the value proposed by Regulation (EU) 2017/460. Naturgy considers that the tariff variations resulting from the new entry-exit split do not meet the requirement in Article 17(1)(c) of the tariff network code as they are significant. **(Advisory Council, Tariff Council, REN, Endesa, Galp Gás Natural, Naturgy, AGN)** Some comments have stressed that the current split has proved adequate. In particular, EFET and EDP consider that the current entry-exit split should be maintained until there is a joint Iberian proposal (to avoid an increase in the cost of interconnection, by the 'tariff pancaking' effect). **(GGN, AGN, EDP, EFET)** EDP notes that the transfer of costs from the exits to the entries will contribute to an increase in the cost of production of the gas power plants (due to the intermittent production), implying an increase in the price of electricity for the final consumer. **(EDP)**	ERSE agrees with the comments received that the change to a markedly different entry-exit split in the course of a single year creates significant tariff variances. In the final decision to be taken by ERSE, if this change proves to be significant, it will be reflected gradually and desirably articulated with the Spanish regulator. In addition, ERSE recognizes the need to monitor whether the change in the entry-exit split does not result in adverse consequences for the functioning of the market. Regarding Naturgy's comment about insufficient information, ERSE provided information on this matter in the 'E-X Split' worksheet of the "TransmissionTariffs.xlsx" file. The entry-exit split of the final transmission tariffs depends on several factors, namely: the entry-exit split of the pre-adjustment prices and the reconciliation process with the level of allowed revenues. In the proposal presented the entry-exit split was preserved in the reconciliation process. In the final decision, taking into account the comments presented, ERSE will reevaluate this theme. Moreover, ERSE considers that EDP's argument regarding the impact on electricity consumers due to the consequences for gas power plants lacks information in order to be assessed by ERSE.

Topic	Response received	Observation by ERSE
Volatility of transmission tariffs	The transmission system operator alerts to the risk of increased volatility in transmission charges. In the short term, the new entry-exit split will reduce prices at the exit points by increasing the price of energy (by incorporating the higher price at entry points). In the medium/long term there may be significant variations if a decision is taken towards the reduction or elimination of transmission tariffs at the interconnection points with Spain as an approach to correct the 'tariff pancaking' problem. **(REN)**	ERSE takes note of the concerns expressed by REN. In line with the comments made in the previous point, ERSE intends to re-evaluate this matter.
Multipliers for non-yearly capacity products	Maintenance of the multipliers is evaluated positively and reflects the importance of tariff stability. Endesa stressed the importance of reducing the value of the multipliers as the level of infrastructure utilization increases. **(Advisory Council, Endesa, Galp Gás Natural, AGN)**	ERSE confirms that it intends to maintain the value of the multipliers. In abstract, ERSE agrees that the multipliers should be decreasing with the degree of utilization of the infrastructures.

Topic	Response received	Observation by ERSE
Discounts to be applied at entry points from and exit points to storage facilities under Article 9	REN considers that the discount to be applied at interface points with the underground storage should be 100% and states that several countries are proposing to apply discounts above the minimum value (Sweden and Denmark are proposing discounts of 100%). With respect to the LNG terminal, REN agrees with the application of a zero discount at the entry point, namely in view of the current competitive position of the terminal, which ensures the security of supply function. However, REN recommends that the price ratio at the entry from VIP/LNG terminal should be monitored by ERSE. **(REN)** Naturgy, recognizing the importance of underground storage as an element of flexibility for various agents, in particular smaller market agents, considers that the 95% discount at entry points is excessive and overvalued, since only 4% of entries into the transmission network between January and August 2018 occurred from underground storage. A lower discount would mean lower transmission charges at the other entry and exit points. The company also disputes the lack of discounts under Article 9(2), in particular the absence of a discount applied to the entry point from the VIP in the case it is considered as being developed with the purpose of ending the isolation of Member States. In the last year the VIP had an average use of 70% of the nominal capacity, representing 39% of the gas entries into the transmission system. **(Naturgy)**	The reference price methodology results in prices that allow the correct allocation of costs to the various entry and exit points. These are the prices that transmit the signals for an efficient use of the infrastructures. Thus, the application of discounts should be used under exceptional circumstances. Underground storage is an important infrastructure in terms of offering flexibility to market agents, facilitating the management of the consumption portfolio by the gas suppliers and consequently mitigating the situations of imbalance. This issue is particularly relevant for smaller agents, facilitating their entry into the market. Applying a discount on this interface does not result in a significant loss of revenue as the capacity bookings at this point are negligible in relation to the remaining points. Therefore, ERSE considers it appropriate to apply a discount of more than 50% in accordance with Article 9(1). The consideration of lower prices at the entry from the VIP will be an issue to be addressed in the integration of the Spanish and Portuguese gas systems, with the goal of developing MIBGAS. In the framework of the South Gas Regional Initiative, studies and public consultations on this matter were carried out by the regulatory authorities.

Topic	Response received	Observation by ERSE
Discounts applied to standard capacity products for interruptible capacity	REN and Endesa approve the application of the 'ex-post' discount to standard capacity products for interruptible capacity (in particular the interruptible capacities to be offered in daily and within-day products at interconnection points). In REN's position, this option is justified by the absence of historical information in order to apply an 'ex-ante' discount. REN believes that, for longer-term products, the 'ex-ante' discount may be more appropriate in economic terms [: "For longer horizons (monthly, quarterly or annual maturity), if interruptible capacity products are offered by transmission system operators in the future, the discount to be applied shall take into account the cost to the system of an ex-post discount, according to the model established in the tariff network code, given the price difference for longer term products in relation to daily products and the increased risk of interruption associated with these products." [translation by ERSE from Portuguese to English] **(REN, Endesa)**	ERSE considers that the coexistence of 'ex-post' and 'ex-ante' discounts is not compatible with the tariff network code.
Commodity charge	REN does not object to the amount of allowed revenues to be recovered by a commodity charge but considers it necessary to clarify the specific costs to be recovered with this charge. **(REN)**	ERSE takes note of the comment and will clarify the nature of the costs to be recovered with the commodity charge in its final decision.
Communication of changes in transmission tariffs	The change in the entry-exit split should lead ERSE to reconsider the communication of the tariff impacts, since in the case of an increase in the proportion of revenues to be recovered at entry points, final consumers perceive a reduction in the tranmission tariff paid at the exit points although it is offset by the increase in the transmission tariff at entry points paid by market suppliers and passed on to end-consumers through the cost of gas. Emphasis should be given to the evolution of allowed revenues in transmission. **(Advisory Council, Tariff Council, Galp Gás Natural, Iberdrola, EDP)**	ERSE recognizes the importance of adequately communicating changes in transmission tariffs, particularly in a context where the entry-exit split is altered, causing changes in the level of network access tariffs offset by changes in the opposite direction in transmission tariffs at entry points (the effect of which is reflected in consumers' energy costs).

Topic	Response received	Observation by ERSE
Other considerations - tariff period	REN suggests synchronizing the tariff period of regulated tariffs for natural gas (currently from July to June) with the gas year (October to September), resulting in greater simplicity and predictability of tariffs for traders and in more comparable offers for consumers. **(REN)**	ERSE has in the past committed to discuss the synchronization of the tariff period of regulated tariffs for natural gas with the gas year. This discussion will be conducted in the context of the regulatory review for the new regulatory period.
Other considerations - 'tariff pancaking'	REN believes that a correct allocation of transmission costs in Portugal and Spain can mitigate the problem of tariff pancaking. The definition of zero prices at the interconnection points would only redistribute the costs to other points, for example to the exit points. As Portugal is an importing country, it is logical that the cost for domestic consumers should reflect the prices applied for the usage of infrastructures in other countries, namely in Spain. EDP believes that changing the entry-exit split (by increasing the proportion recovered at entry points), without coordination with the Spanish regulator, will increase the problem of tariff pancaking. **(REN, EDP)**	The tariff pancaking problem associated with the VIP is an important issue to address in the context of the integration of the Spanish and Portuguese natural gas systems, with the goal of developing MIBGAS. Under the South Gas Regional Initiative, studies and public consultations on this matter were carried out by the regulatory authorities (http://www.erse.pt/eng/naturalgas/mibgas/Paginas/default.aspx). Tariff pancaking has been singled out as one of the obstacles to market integration. The study "Quo Vadis EU gas regulatory framework", requested by the European Commission in the context of the construction of an integrated energy market, presents alternatives to transmission tariffs at interconnection points between Member States. Additional studies are also expected for 2019 on this subject.

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