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EFET response to the CNMC consultation on gas tariffs (TAR NC) - *Circular de Peajes Gas*

EFET response – 30 September 2019

The European Federation of Energy Traders (EFET)[1] welcomes the opportunity to provide comments on the CNMC consultation on gas tariffs and the implementation of EU regulation 2017/460 (TAR NC).

We appreciate the fact that the CNMC published in English such consultation to the largest extent possible, according to European legislation. We also thank the CNMC for the meeting on the 24th of September. We think that such good initiatives should be open to all stakeholders for the next regulatory period and on every other important aspect that has cross-border implications. Workshops are key for better understanding the implications of relevant regulation and to share knowledge.

In general, we found some potential miscalculations in the consultation. We recognise that such issue might arise from different assumptions or different statistical models. However, it is important to note that we consider that there is not enough information to fully assess the proposed methodology and its impact on the market. This is mainly due to the lack of certainty in relation to allowed costs and by the future charges set by the government.

Below you will find our detailed comments.

1. Quantitative dispersion of Entry-Exit Tariffs

EFET acknowledges that CNMC has followed the Capacity Weighted Distance (CWD) mechanism foreseen in the European Regulation to calculate the applicable tariffs to the entry and exits points of the Spanish system. However, the resulting quantitative figures proposed show a significant range of values for each VIP (as per Sheet "Final Tariff" of the Excel file "*Propuesta Circular*"). The wide range of values warrants revaluation and adoption of some mitigation measures considering the impact on neighbouring markets and the incentives on market participants.

Of particular relevance, we note the difference in the tariffs for the "pipeline points": whereas the VIP figures have differences of more than 20% to the average entry tariff (with the VIP Pirineos particularly advantageous), the "*Conexiones Internacionales*" (Tarifa and Almeria) are closer to that average.

[1] The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org

We suggest that a critical assessment including a sensitivity analysis and a comparative study with other EU countries of the calculated figures should be performed, which could avoid the creation of preferred entry points. As contributions to justifying this reanalysis, we note the approval of entry tariffs so markedly different may potentially lead to congestion in the entry points with lower tariffs, and that does not seem to be justified considering the existing surplus capacity in the Spanish market.

Noting that the European TAR NC regulation admits variations to CWD (for instance the Modified CWD as applied by ERSE in Portugal), a less unequal VIP tariff level could be considered at least for the initial transition years as considered by TAR, even if during the regulatory period a convergence mechanism was established that would allow the full application of pure CWD methodology by the end of the period.

As a potential alternative to reduce the difference between the VIPs' entry/exit tariffs, a 33/66 instead of 50/50 entry/exit cost split could be applied, as in have done neighbouring countries such as France.

2. Differences between tariffs resulting from the application of the *Circular* and current tariffs and evolution of the tariffs during the Regulatory Period (RP)

From the sheet "Final Tariff", we consider that the proposal of establishing an initial high level for the entry transmission tariffs, with a strong decrease during the regulatory period (close to 50% reduction) could be reassessed. In fact, with the profile proposed, the market would not have the desirable tariff stability, being especially faced with high prices in the beginning of the RP.

For example, a rough comparison between the tariff currently applied at European IPs for entry to PVB (equal to 130,18 €/(MWh/day)/year) and the corresponding ones resulting from the *Circular* (202,01 €/(MWh/day)/year for VIP Pirineos and 334,41 €/(MWh/day)/year for VIP Ibérico before escalation as per paragraphs VIII.1.2, VIII.1.3 and VIII.1.4 of the *Memoria*) shows an increase respectively of 55% and of 157%[2].

Given the magnitude of said increases, while acknowledging that since the methodology for the calculation of current tariffs is not public and since current tariffs include both transmission and distribution activities a thorough analysis of said differences cannot be done, we would have appreciated at least a qualitative explanation of the reasons thereof.

In order to avoid such important increases[3] followed by decreases in the following years in the entry tariffs, we would propose to apply the entry tariff calculated according to the methodology for October 2024- September 2025 from October 2020 on, with the under recovery recovered through a transitory transport access tariff. Since the capacity

[2] The actual global increases are even higher, since on top of the mentioned increase of the capacity charges the proposed introduction of a commodity charge has to be considered.

[3] We note e.g., that in the frame of the implementation of the TAR NC and specifically in accordance with Article 6.4 thereof, E-Control Austria has proposed to set a limit of 10% for the tariff increases "*in order to safeguard existing contracts and tariff stability as well as to avoid market distortion*" (relevant Consultation document at this linkhttps://www.e-control.at/documents/1785851/1811597/2019-01-31+Consultation+document+TAR+NC+ECA_EN.PDF/bdc09cb9-f2b3-284e-5d0d-57288d3f52dd?t=1548930369725)

reservation is expected to be stable throughout the RP this methodology would not be detrimental to the recovery of the allowed revenues but would create a scenario of predictability and stability that we deem beneficial for the market.

3. Proposal on Multipliers

We believe that intraday multipliers should be simpler, and we do not understand the reasoning behind having twenty-four separate multipliers which differ for transmission entry and exit points and LNG services. Our understanding is that the intraday multipliers proposed in Tables 11 and 81 of the consultation represent coefficients, from which the twenty-four separate intraday multipliers are derived. If our understanding is correct, this results in intraday multipliers at transmission entry points which individually and on average do not exceed the typical limit of three specified in Article 13.1(b) of the TAR NC. However, in the case of multipliers at transmission exit points and LNG services (albeit multipliers for these are not covered by the TAR NC) the intraday multipliers are, in some case individually and on average, greater than three.

Intraday multipliers should be the same for transmission entry and exit points and for LNG services and should apply at a constant rate, regardless of the number of hours within the day that the capacity/service is booked for. Shippers would therefore be charged the same intraday hourly tariff (determined by multiplying the yearly tariff calculated on an hourly basis by a single intraday multiplier) regardless of whether they book two hours of capacity or twenty. Unless specifically justified, this single intraday multiplier should be less than or equal to three.

Given the global nature of the LNG market, where significant activity takes place in the short-term, once a cargo is directed to Europe Spain mainly competes on price with other European terminals. Therefore, having comparatively higher tariffs to deliver in Spanish terminals decreases the country infrastructure's attractiveness.

4. Proposal on gas tariffs

The *Circular* proposes an allocation of costs between the fixed and variable terms which is heavier on the former. From a solely cost recovery perspective we understand why this rationale is appealing, however it may have impacts on the wholesale gas market (including LNG). The proposed tariff structure may make new participants face a higher cost to acquire capacity regardless of the utilisation of capacity.

In relation to the proposed LNG tariff methodology, we propose:

1. Demand for LNG services should include forecast usage – The forecast demand is proposed to be based on 2019 utilization rates. We consider that for LNG this should be revised in order to take into account forecast global market conditions and its relative position in the LNG markets merit order in Europe, due to the global nature of the market and the regional competition between markets and the Spanish LNG market

reform to be introduced in early 2020, with one of the expected impacts of the reform being higher infrastructure utilization. Overall, we consider that the conditions for higher LNG activity in Spain are likely to be in place for 2020 and 2021.

2. Dealing with historic over investment –

   The fact that the "*otros costes de regasificación*" (i.e. costs associated with the investment on Musel, improvement to LNG terminals and the cost of the incentive of continuity of supply through regasification) will not be charged to LNG terminal users but directly to the final customers (we guess through an ad-hoc price component) is proved in our opinion not only by the response that the CNMC gave to our specific question during the meeting of last week, but also by the numbers in the tables on page 126 of the *Memoria*: the values in row *Peaje transitorio otros costes de regasificación* of the table *Retribución variable* are the result of the multiplication of the *Término variable* of 0,261065 €/MWh (as stated in *Cuadro* 82 on page 124) by the *Volumen* in the last row of table 3.*Previsión de las variables de facturación* (corresponding to the global gas demand in Spain), not by the *Volumen* in the row *Regasificación* of the same table 3.

3. Security of supply – We suggest considering the positive impact that LNG terminals have on security of supply, and how that is valued by final consumers.

5. Impacts on the power market

We suggest, for short-term products and most significantly intraday capacities to consider the impact on the gas-powered electricity stations. The impact which multipliers have on the costs of dispatch of the marginal technology leads to higher costs for final electricity consumers. The most extreme example where no consideration to the interaction between the markets appears to have been considered is over the six-hour misalignment period between the gas and power days. The two main impacts are:

1. Contestability of the power market – Independent gas-power generators are likely to be priced-out of the power market due to the high-costs of short-term capacity. Independent gas-power generators tend to acquire short-term capacity in order to generate where the price is at or above their marginal costs. However, if the tariffs and intraday multipliers increase their costs, they will be less competitive. This is concerning, where less efficient generators operate because of the distortion caused by tariffs. This is most likely to be the case if the less efficient generator is part of a large gas portfolio which allows them to better optimize.

2. Higher wholesale power prices – Following from the point above, on a plausible scenario where a gas-power station must acquire intraday regasification and transportation capacity the extra cost will be translated to the power market.

6. Other remarks

In relation to interruptible capacity, we consider that an ex-ante discount provides a more valuable commercial incentive as it simplifies simple pricing in commercial operations. However, an ex-post discount has to be priced-in as a probability of interruption and the probability of interruption is very low.

The draft *Circular* proposes a new structure of tariffs for the exit of the local networks to customers. The current structure is based on pressure and consumption levels. Also, the draft *Circular* establishes that customers should be relocated every year in the appropriate consumption level (and that all customers should be re-invoiced the whole year considering the consumption of last year). This re-invoicing is not a novelty but with the new wider structure the volatility of the prices will be wider as well (a customer can go from level D.11 to level D.1 in one year) which may cause uncertainty, specially to combined cycle power plants whose consumption every year is uncertain.

We finally request a clear implementation road map and an entry into force of the new tariffs from the 1st October 2020 as several contracts have already been concluded and the proposed *Circular* will have extensive commercial impacts on market players[4].

[4] In this regard, we note that Article 29 of the TAR NC requires that "*the reserve prices applicable until at least the end of the gas year beginning after the annual yearly capacity auction*" "*shall be published before the annual yearly capacity auction*"; this means that the tariffs applicable in the GY20 have to be published beginning of July 2020.