

Supporting Document for Public Consultation on the Draft Incremental Proposal

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1. Introduction

This consultation supporting document accompanies the Draft Incremental Proposal, Ref. INC00164-14 (hereinafter the Draft Incremental Proposal). The Draft Incremental Proposal consists of two parts:

The first part is an amendment to the Network Code on Capacity Allocation Mechanisms (CAM NC) and will cover the issues of when to offer, co-ordination requirements, information provision, auction procedures and open season procedures. The second part is a chapter of the network code on Harmonised Transmission Tariffs Structures for Gas (TAR NC) that relates to sections 2.4.1 and 3.5 of the Framework Guidelines for TAR NC and will cover the economic test and tariff issues related to incremental capacity and the relevant information provision.

This supporting material was developed for the purpose of the public consultation pursuant to Article 10 of the Regulation (EC) 715/2009¹ (hereinafter the 'Regulation') and Article 28 of ENTSG Rules of Procedure².

Pursuant to Article 7 in the Regulation the Agency for the Cooperation of Energy Regulators (ACER) shall assess amendment proposals and be able to recommend them to the European Commission (EC) for adoption. For the case of including the offer of incremental and new capacity in the CAM NC, the EC invited ENTSG to draft an Incremental Proposal based on the ACER Guidance to ENTSG on the development of amendment proposals to the CAM NC on the matter of incremental and new capacity (ACER Guidance).

In this context, ENTSG has produced this supporting document to record how it arrived at a formulation comprising the Draft Incremental Proposal with input from ENTSG members via its Incremental Advisory Kernel Group and from external stakeholders at the **stakeholder joint working sessions (SJWSs) held regularly between February 2014 and April 2014**. **The materials from the SJWS are referenced throughout this supporting document and should be read in conjunction with it** [see the "Kick off Meeting - SJWS - Workshops" and "Business Rules" sections on <http://www.entsog.eu/publications/incremental-capacity#All>]

ENTSG stresses that the Draft Incremental Proposal and the supporting document do not contain any commitment or representation of any nature from ENTSG as to the content of the final Incremental Proposal.

¹ Regulation (EC) No 715/2009 of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005, Official Journal, L211/36, 14.08.2009.

² ENTSG, Rules of Procedure of the International Non-Profit Association (AISBL) European Network of Transmission System Operators for Gas," established 1 December 2009.

This supporting document also serves as an **ENTSOG consultation document**, as it invites respondents to provide views on issues raised throughout the document as part of the consultation on the Draft Incremental Proposal.

For the avoidance of doubt, the Supporting Document for Public Consultation should not be construed as part of the Incremental Proposal to be delivered to ACER in December 2014.

The Supporting Document for Consultation is publicly disclosed to the market here for consultation purposes only and without any commitment whatsoever from ENTSOG, as already mentioned, as to the final content of the Incremental Proposal. Any and all interested parties, in their capacity as professional stakeholder, shall be responsible for seeking to obtain the accurate and relevant information needed for their own assessment and decision to respond to the consultation.

Additionally, the content of the Draft Incremental Proposal and the Supporting Document for Public Consultation should not be considered to give rise to any specific right or obligation whatsoever to ENTSOG or any of its members as to any stakeholder.

ENTSOG has sought to produce a supporting document which is both useful and relevant for respondents to the consultations and observers of the policy-making process. The structure and layout has been developed to facilitate reading and reference.

ENTSOG welcomes responses to this public consultation on the Draft Incremental Proposal and will consider all views submitted. Please see the following section for response submission details.

2. How to respond to this consultation

ENTSOG welcomes all comments on the Draft incremental Proposal -- in particular, replies to the specific questions which are raised throughout this document (see Annex 1 for a summary list).

To enable ENTSOG to consider responses as fully as possible, we would be grateful if respondents could:

- consider fully this document, the Draft Incremental Proposal (Ref. INC00164-14), the Draft Amendment Proposal to the CAM NC (Ref. INC00168-14), the Draft TAR NC and the materials from the SJWS;
- provide responses that are as focused and succinct as possible; and
- provide full reasoning and supporting quantitative and/or qualitative evidence (where available) for responses.

If you wish any part of your response submission to be treated as confidential, please mark these sections of your document clearly. Please note, however, that ENTSOG's approach to developing the

Draft Incremental Proposal relies heavily on transparent exchange of views across market participants. We would encourage you to allow your full response to be made public.

Please use the Consultation Response Form (in Survey-Monkey format) provided on the incremental site on the ENTSOG website <http://www.entsog.eu/publications/incremental-capacity>. Respondents are not required, though, to reply to all questions within the supporting document.

Respondents will also have the opportunity to seek clarification on these documents at a consultation workshop to be held in Brussels on 24 June 2014. Initial views from respondents could also be expressed at the workshop.

3. Procedural background and prior consultation with stakeholders

3.1 Organisation and timing

The Draft Incremental Proposal and this supporting document have been prepared by ENTSOG, an organisation currently comprising 43 gas transmission system operators and 3 associated partners from 26 European countries, in line with the association's purpose to promote the completion and functioning of the internal market. The rules for the amendment of a Network Code are defined in Article 7 of the Regulation, which states that ACER shall assess amendments proposals and be able to recommend them to the Commission for adoption. For the case of including the offer of incremental and new capacity in the CAM NC, the European Commission (EC) invited ENTSOG to draft an Incremental Proposal based on the guidance provided by ACER. As mentioned in the introduction, pursuant to the invitation letter received by ENTSOG, the Incremental Proposal must be delivered to ACER by 31 December 2014.

3.2 Consultation and expertise

ENTSOG's obligation to conduct an extensive consultation process during the preparation of a network code is stipulated in Article 10(1) of the Regulation, which is equally valid for the preparation of an amendment to a network code. In line with its internal process and in compliance with the Regulation, ENTSOG has encouraged full stakeholder involvement and has engaged extensively with market participants both on process and content.

In the project plan consultation all market participants were invited to register to participate in the process of developing the Draft Incremental Proposal. Stakeholders, representing all levels of the gas value chain including producers, traders, network users and end users, expressed strong support for ENTSOG's proposed process as described in the final project plan for the Incremental Proposal³.

³ <http://www.entsog.eu/publications/incremental-capacity#1-LAUNCH-DOCUMENTATION-AND-PROJECT-PLAN-FOR-THE-INCREMENTAL-PROPOSAL>

Stakeholders have actively participated in the development process and the SJWS: The Kick Off Meeting (14 January 2014), SJWS 1 (10th of February 2014) SJWS2 (26th February 2014) SJWS3 (13th March 2014) SJWS 4 (25th March 2014) and SJWS 5 (8 April 2014).

3.3 Stakeholder views

In accordance with the Regulation and ENTSOG's statutes, stakeholders' views and the discussions at the SJWS have been integral to the decisions made during the development of the Incremental Proposal and as such are described throughout this document when describing the rationale for the options selected. The minutes of the SJWS including stakeholder discussions on the relevant topics can be consulted on the ENTSOG website.⁴

3.4 Planning and next steps

Responses to this consultation will help to determine the approach to be taken by ENTSOG when formulating a revised Incremental Proposal. ENTSOG will stage a consultation workshop on 24 June where stakeholders will present their views and gather the responses until the consultation deadline on 30 July. After the deadline end of July, ENTSOG will develop the text for a refined Incremental Proposal. A refinement workshop will be held on 23 September and a stakeholder support process (SSP) will be held from 7 November until 21 November. The final Incremental Proposal will be delivered to ACER on 31 December 2014. Key dates for the finalisation of the Incremental Proposal can be found in the table below.

Table 1: Key dates in the process to finalise the Draft Incremental Proposal⁵

30 May 2014	Public consultation on the Draft Incremental Proposal launched
24 June 2014	Consultation workshop
30 July 2014	Deadline for responses to the public consultation
23 September 2014	Refinement workshop
7-21 November 2014	Stakeholder Support process (SSP)
31 December 2014	Final ENTSOG-drafted Incremental Proposal submitted to ACER

⁴ <http://www.entso-g.eu/publications/incremental-capacity#2-KICK-OFF-MEETING---SJWS---WORKSHOPS>

⁵ The dates of the workshops associated with the public consultation were changed from the original work plan from 24 April to 9 May and 31 July to 26 July.

4. Policy context for development of the Incremental Proposal

The CAM NC⁶ focuses on capacity allocation for already existing capacity at interconnection points (IPs) in gas transmission systems. The XXII Madrid Forum of October 2012 has recommended that processes are established by which capacity demand beyond the offer of existing capacity can be satisfied in a market-based manner.⁷ ACER has therefore been requested to elaborate procedures for market-based identification and allocation of incremental capacity at existing IPs and new capacity. These procedures are captured in the 'ACER guidance to ENTSG on the development of amendment proposals to the CAM NC on the matter of incremental and new capacity' (ACER Guidance).⁸

5. Topics of the Draft Incremental Proposal

For each section of the Draft Incremental Proposal, we provide:

- A: the corresponding extracts from the ACER Guidance to which the chapter is aligned;
- B: "Background to Draft Incremental Proposal formulation" comprising where relevant: an interpretation of the FGs; options and approaches considered and analysed; the rationale for preferred options included in the Draft Incremental Proposal; and any open issues and questions for public consultation;
- C: Options for topics raised during the SJWS.

Within the Supporting Document the reader will also find boxes, framed in green, with illustrations of relevance for the chapter in question. At the end of each chapter stakeholders are invited to respond to a set of questions with regards to the chapter in question.

The terms and definitions applied within the Draft Incremental Proposal, referenced in this supporting document, are those in the Regulation and the Directive 2009/73/EC⁹.

5.1 Articles 1 – 3 of CAM NC – Subject matter, Scope and Definitions

Articles 1 – 3 of CAM NC consist of the first chapter on general provisions, including the subject matter, the scope and the applicable definitions. These general provisions of the CAM NC were developed in order to set the framework for capacity allocation mechanisms of existing technical capacity at interconnection points. In the context of the Incremental Proposal, an extension of this

⁶ Commission Regulation (EU) No 984/2013 of 14 October 2013 establishing a Network Code on Capacity Allocation Mechanisms in Gas Transmission Systems and supplementing Regulation (EC) No 715/2009 of the European Parliament and of the Council // OJ L 273, 15.10.2013, p. 5.

⁷ http://ec.europa.eu/energy/gas_electricity/gas/forum_gas_madrid_en.htm

⁸ Published on ACER website on 2 December 2013:

[http://www.acer.europa.eu/Gas/Framework%20guidelines_and_network%20codes/Documents/ACER%20Guidance%20on%20NC%20CAM%20Amendments%20\(final\).pdf](http://www.acer.europa.eu/Gas/Framework%20guidelines_and_network%20codes/Documents/ACER%20Guidance%20on%20NC%20CAM%20Amendments%20(final).pdf)

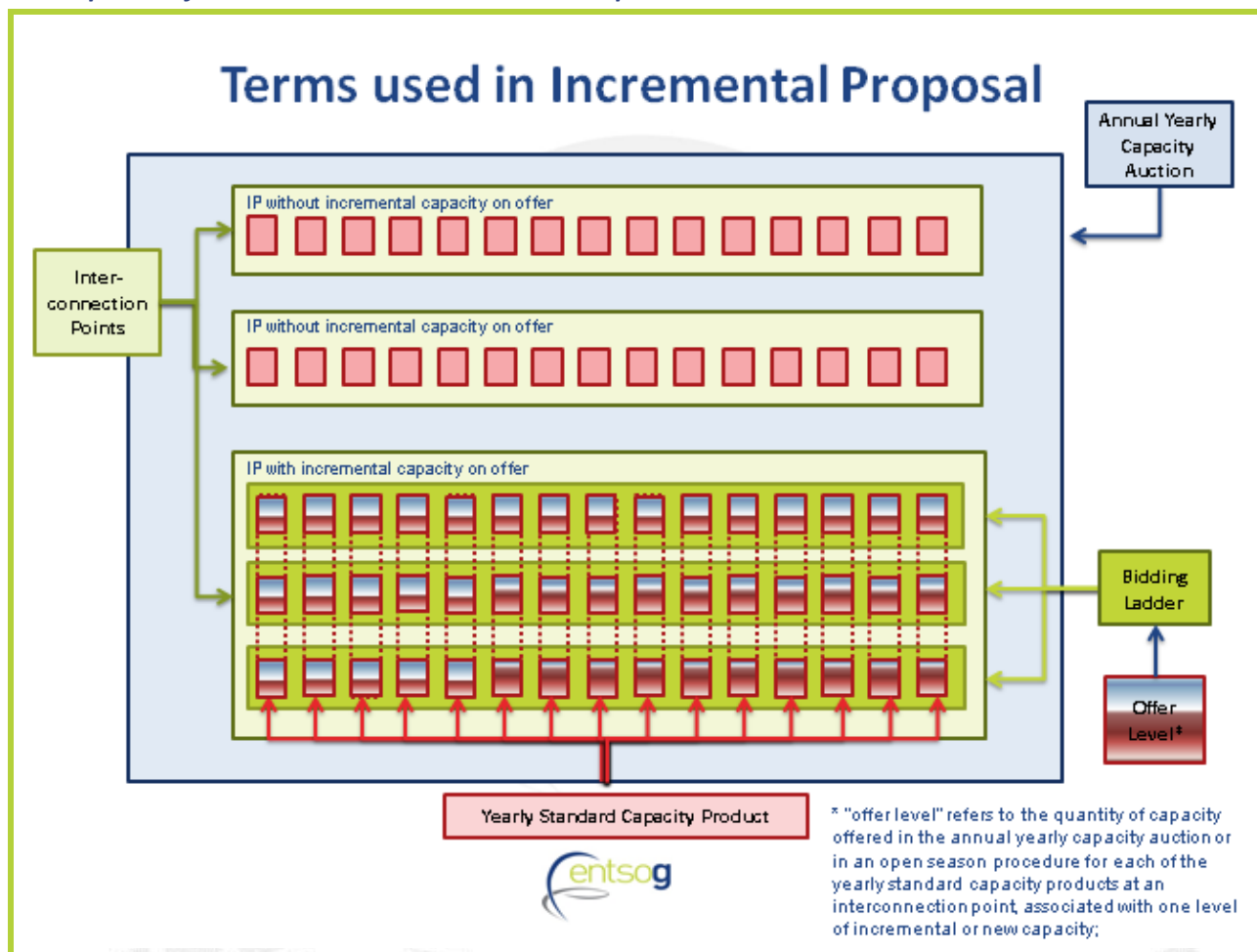
⁹ Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, *Official Journal*, L211/94, 14.8.2009.

framework is necessary in order to include the allocation mechanisms for incremental and new capacity.

ENTSO-G is therefore proposing amendments and additions to Articles 2 (Scope) and 3 (Definitions). In particular, the scope of the CAM NC shall apply to incremental and new capacity when identified and allocated via market based procedures, meaning in cases where an investment or a capacity optimisation is based on commitments of network users. Furthermore, ENTSOG proposes to reduce the exemptions for incremental and new capacity that were originally defined in Article 2(3) and to limit exemptions to Articles 19(2) and 27 (provisions on booking platforms) for cases of Open Season Procedures subject to a decision by the National Regulatory Authority (NRA).

The definitions set in Article 3 shall be extended in order also to cover terms that are being used in the context of the Incremental Proposal. In particular, the terms requiring a definition that are being used in the amendment of the CAM NC are 'bidding ladder', 'economic test', 'incremental capacity', 'new capacity', 'offer level' and 'Open Season Procedures'. In addition to this, some definitions of other and future regulations, especially the Draft Tariff NC, are relevant for the amendment of the CAM NC. The following illustration aims at clarifying the definitions of the terms above:

Example I: Definitions used in the Incremental Proposal



The annual yearly capacity auction is a single yearly process that combines the offer of all yearly standard capacity products for all Interconnection points (IP) of a Transmission System Operator (TSO). For each IP, the TSO can offer no more than the next 15 gas years, therefore at a maximum 15 yearly standard capacity products can be offered per IP in the annual auction. In the example above, the TSO is offering capacity at 3 IPs. In case no incremental or new capacity would be on offer, the TSO could offer at a maximum 45 yearly standard capacity products.

The example is however illustrating a case in which incremental capacity is on offer at one of the IPs. For this offer, the TSO has designed 3 offer levels, one offering only the existing capacity and two offering the existing capacity and a respective level of incremental capacity. The offer level refers to the quantities of capacity offered in the annual yearly capacity auction or in an Open Season Procedures, associated with one level of incremental or new capacity at an interconnection point. Each offer level is associated with one bidding ladder, which is the combination of all yearly standard capacity products for one interconnection point in the annual yearly capacity auction belonging to one specific offer level.

Question 1: *Do you agree with the additional definitions proposed in Article 3 (CAM NC)? If not, please elaborate.*

5.2 Articles 4 – 20 and 21 - 28 of CAM NC

Besides the general provisions in chapter I and the core of the Incremental Proposal in Articles 20a to 20h of CAM NC, some amendments and additions to existing articles of CAM NC are proposed by ENTSG in order to cover specifics of incremental and new capacity in all parts of the CAM NC. Nonetheless, ENTSG proposes to change only those existing articles of CAM NC that are needed for the offer of incremental and new capacity.

In particular, these amendments mainly refer to the allocation methodology in Article 8, the principle of the annual yearly capacity auctions in Article 11 and the ascending clock algorithm in Article 17. It is important to highlight that ENTSG is not proposing any changes to processes applicable in the CAM NC referring to existing capacity and that amendments to these articles solely refer to specific treatments of incremental and new capacity, in cases where this is necessary.

Question 2: *Do you agree with the proposed amendments and changes to Articles 4-20 and 21 to 28 (CAM NC)? If not, please elaborate.*

5.3 Article 20a of CAM NC: Co-ordination requirements

A: Corresponding extracts from the ACER Guidance

CAM NC amendment should require TSOs and NRAs to closely co-operate and co-ordinate across borders in order to enable offers of incremental or new capacity as bundled products according to the existing NC CAM. The CAM NC amendment should outline the overall process and which coordination results should be reached at what stage.

In the course of this co-ordination, agreement should at least be reached on:

- *Co-ordinated timelines for the project;*
- *How delays in the provision of capacity are dealt with contractually;*
- *How effects of delays on other systems can be mitigated;*
- *The capacity volumes and characteristics of bundled yearly products for which demand can be tested;*
- *The common procedure to be used for securing network users' binding commitments, taking into account the selection criteria defined in section 2.e) and 2.f);*
- *The way in which the requirements for triggering the investment decision in each regulatory system can be combined in a single economic test, and when the test would be satisfied;*
- *Simultaneous or common information provision and a coordinated or single point of contact for network users.*

In addition, the CAM NC amendment should define whether additional (and if so which) specific coordination requirements need to be fulfilled in the situation where an investment project spans across more than one interconnection point.

B: Background to Draft Incremental Proposal formulation

Article 20a of the amendment proposal for the CAM NC covers provisions on general co-ordination requirements in incremental and new capacity projects. These provisions are based on the framework provided by ACER in the ACER Guidance. ENTSOG is of the opinion that intensive co-ordination and co-operation among TSOs involved in an incremental or new capacity project and the relevant NRAs is essential for the success of such projects.

For this reason, ENTSOG is suggesting clear provisions in the amendment of the CAM NC that oblige TSOs and NRAs to co-ordinate their activities. Furthermore, an obligation for NRAs to co-ordinate and align their decision-making and approval processes is required, as investment projects at interconnection points mostly affect two different NRAs and therefore require consistent decisions of these entities.

Besides this, ENTSOG has followed the ACER Guidance by proposing provisions that oblige TSOs to offer incremental and new capacity as bundled capacity according to Article 19 of CAM NC and that offer levels shall be designed in a way that result in harmonised capacity levels at both sides of an IP. Furthermore, TSOs shall agree on the features of a project, including joint offer and commissioning timeframes and consistent mitigating measures in case of delays.

C: Topics and policy choices

General coordination requirements

Paragraph 5 of Article 20a is following the principles of the ACER Guidance by defining that the allocation of incremental and new capacity shall as a default rule be conducted via standardised auctions, in specific being the ascending clock auction algorithm in the context of the annual yearly capacity auction. Open Season Procedures can be applied instead of auctions for incremental and new capacity, however this application is subject to approval of the involved NRAs and is linked to certain circumstances that are defined in Article 20g(2).

During the SJWSs, a few stakeholders suggested defining auctions and Open Season Procedures on an equal level and that the application of the one or the other should only be linked to clear circumstances. In particular, it was proposed to clearly define that a new capacity project, especially where several IPs and entry-exit-zones are involved, should as a default rule be conducted via Open Season Procedures. ENTSOG has decided to take these considerations into account by including it as an example of when an Open Season Procedures could be initiated as described in article 20g.

Question 3: Do you agree with the level of co-ordination between TSOs and NRAs involved in an incremental or new capacity project as foreseen in Article 20a (CAM NC)? If not, please elaborate.

Question 4: Do you agree with the auction default and the alternative open season procedure as

defined in Article 20a (5) (CAM NC)? If not, please elaborate.

Question 5: Do you have any additional remarks to the provisions in Article 20a (CAM NC)?

5.4 Article 20b of CAM NC: Information provision

A: Corresponding extracts from the ACER Guidance

For each considered capacity expansion, TSOs should provide to the other TSOs involved or affected and to each relevant NRA at least the following information on a provisional basis as early as possible:

For each considered capacity expansion at the relevant IP, the volume of annual yearly standard bundled capacity products offered and the contractual details and terms and conditions of the capacity contracts;

- *The detailed rules used for securing network users' binding commitments, i.e. the specific allocation design, in line with the provisions of section 2.e) and 2.f);*
- *Detailed information on what level of network user commitment is necessary to enable the investment from an economic perspective (economic test);*
- *A reference to the applicable tariff and methodology as published by the TSOs;*
- *The timeline of the full process, including of the publication of economic test results and final capacity allocations, and possible approval procedures by national authorities.*

This information should be provided to the NRAs for approval, with a sufficient lead time before an offer of incremental or new capacity is made for binding commitments. Moreover, the CAM NC amendment should outline the process steps and which information should be provided at each step. After NRA approval, TSOs should publicly provide at least this information with a sufficient lead time, before an offer of incremental or new capacity is made for binding commitments. The CAM NC amendment can list any other pertinent information that is to be exchanged or published in order to ensure a user-friendly and non-discriminatory process. The CAM NC amendment should also outline principles on post-allocation reporting and the type of information TSOs should publish by a specified date.

B: Background to Draft Incremental Proposal formulation

The ACER guidance emphasises the cooperation between TSOs and NRAs across borders in order to ensure an efficient process and to assure that market needs are being addressed. The bundling of capacity products implies coordinated levels of incremental or new capacity and project timelines. Furthermore, information provision is necessary for network users to allow them to be able to make informed bids.

ENTSOG is proposing principles on information provision in Article 20b of the amendment of the CAM NC. In particular, Article 20b is defining the type of information that must be submitted by TSOs involved in an incremental or new capacity project to their respective NRAs for approval and when such information is to be provided to network users in preparation for an auction or open season.

It is important to highlight that the principles on information provision proposed in the context of the CAM amendment do interact with the publication requirements on the economic test parameters as defined in Article 45 of the Tariff NC. Namely, the term 'parameters of the economic test' in

paragraph 2 lit. (c) of Article 20b of CAM NC refer to the parameters defined in Article 45 (1) of the TAR NC.

C: Topics and policy choices

Process steps

During the SJWS, stakeholders discussed the timing of process steps and the availability of information to the market. With regards to information that is provided to the respective NRAs for approval before an offer of incremental and new capacity, ENTSOG proposes a two-step process which is also interacting with the provisions in 20a (Co-ordination requirements) and 20c (When to offer incremental and new capacity).

Demand assessment

The first information that is to be provided to the respective NRA for approval is a demand assessment based on the 'when to offer' criteria defined in Article 20c. This demand assessment shall be the start of each incremental or new capacity project and shall be the basis for conducting technical studies. It is important to highlight that an aggregated demand assessment as proposed by ENTSOG shall not prevent the possibility that one single 'when to offer' condition can launch the process of offering incremental or new capacity.

The demand assessment shall however make sure that once the process is triggered; all other factors that possibly give information on the actual demand of all network users for incremental or new capacity are taken into account. Furthermore, the level of demand identified in this assessment shall be used by the TSOs to develop offer levels for incremental or new capacity at reasonable levels.

Once the demand assessment is approved by the relevant NRA, TSOs shall start modelling the project including the required offer levels, the indicative project timelines and the parameters that are relevant to establish an economic test. These factors shall be submitted to the NRA after the technical studies are finalised as the second part of the process that shall include the argument for conducting an open season including the respective proposed features.

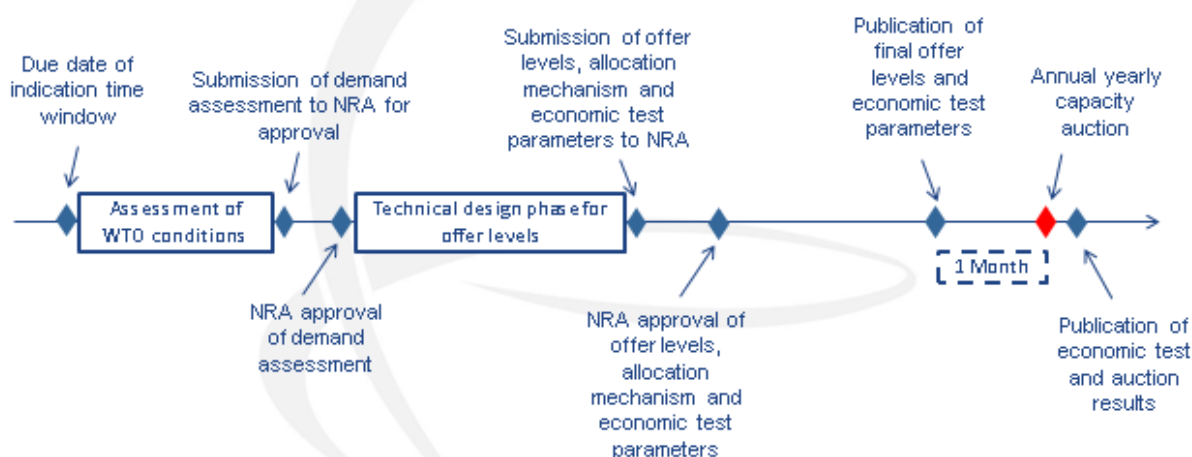
As soon as these concrete parameters, as also defined in Article 20b (2) are approved by the NRA, the actual offer of incremental or new capacity can be conducted. For the publication of these parameters to be available for the market, ENTSOG proposes a lead-time of at least 1 month before the auction or the binding phase of the Open Season Procedure.

The following two diagrams illustrate process steps for auctions and Open Season Procedures on how these process steps could interact:

Example II: Process steps: Auctions

Process steps: auctions

The following timeline shows the main process steps in case an auction is chosen as allocation mechanism:

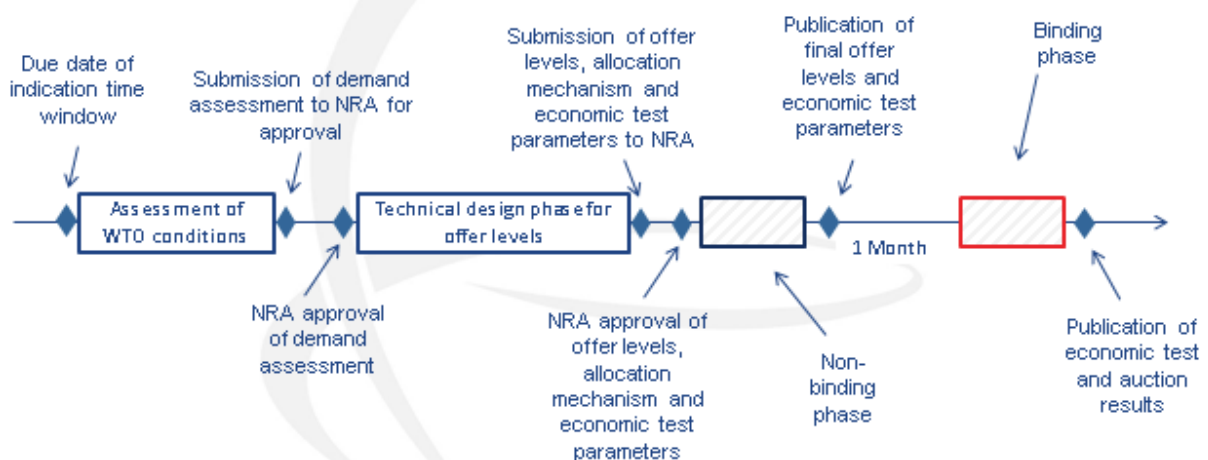


Please note: The timeframes in this diagram are only indicative and are not necessarily in the correct ratio to each other

Example III: Process steps: Open Season Procedure

Process steps: open season procedure

The following timeline shows the main process steps in case an open season procedure is chosen as allocation mechanism:



Please note: The timeframes in this diagram are only indicative and are not necessarily in the correct ratio to each other

Question 6: Do you agree with ENTSG's proposal of a demand assessment to be the basis for conducting technical studies and subsequently designing offer levels? If not, please elaborate.

Question 7: Do you agree with the scope of information to be provided to the NRA and to be published by TSOs involved in an incremental or new capacity process as foreseen in article 20b(2) (CAM NC)? If not, please elaborate.

Question 8: Do you agree with the lead-time foreseen for the publication of information relevant to an incremental or new capacity project and especially the economic test as described in article 20b (3) (CAM NC)? If not, please elaborate.

Question 9: Are there any other issues that you wish to address regarding information provision as foreseen in article 20b? If so, please elaborate.

5.5 Article 20c of CAM NC: When to offer

A: Corresponding extracts from the ACER Guidance

The CAM NC amendment should, as a minimum requirement, require a formal offer of incremental or new capacity, where there is likely to be significant unsatisfied demand for capacity. An offer of incremental or new capacity should be made by the existing TSOs or new entities certifiable as TSOs when at least one of the following conditions is met. This does not preclude more frequent or regular testing of demand.

- *The ENTSOG Ten Year Network Development Plan (TYNDP) identifies a physical capacity gap in the sense that an area is undersupplied in a reasonable peak demand scenario and incremental or new capacity at the IP in question would be able to close the gap; or a national network development plan identifies a concrete and sustained physical transport requirement;*
- *No yearly capacity product based on existing capacity will be on offer (as the yearly product is fully booked) in the year when incremental capacity could be offered first and in the three subsequent years (capacity set aside for the short term is considered not offered). In the case of several IPs between two entry-exit systems the requirement refers to all IPs between these entry-exit systems taken together.*
- *Network users indicate in a non-binding manner to TSOs their need for and their willingness to underwrite incremental or new capacity for a sustained number of years and this transport need leads to physical constraints after exhausting all other mechanisms to maximise the availability of existing capacity.*

ENTSOG should propose draft provisions for NC CAM for a cost efficient, transparent, European process, for instance on the allocation platform(s), including a time window in each year when such interest can be expressed. The CAM NC amendment should require TSOs to individually make public what information they require within this process. The minimum data required for an indicative capacity request should be well-founded and should include the location, an indication of the amount of capacity required and an indication of the number of years for which a network user considers a binding offer or bid. When specifying their needs, network users should have the possibility to indicate whether they would be interested in buying incremental or new capacity at several IPs along a 'hub-to-hub' route. TSOs should report to affected NRAs whether or not they have received expressions of interest. If they have received any, TSOs should indicate whether these are sufficient for a formal offer of incremental or new capacity and propose coordinated solutions for addressing these indicative requests.

A failure to test market demand for incremental or new capacity, when indicative demand is identified as above, is deemed to be in breach of the TSOs' existing obligation to assess market demand for investment, enshrined in Regulation (EC) 715/2009, e.g. in Article 16 (5).

B: Background to Draft Incremental Proposal formulation

The Incremental Proposal includes the three criteria, which indicate a possible demand in incremental capacity as required in the ACER Guidance. This approach takes into account relevant indicators trying to identify significant unsatisfied demand for capacity. The conditions for when to offer incremental and new capacity are described in article 20c in the Draft Incremental Proposal.

C: Topics and policy choices

Criteria for when to offer

Initially, ENTSOG presumed that all three criteria must be matched and that the fulfilment of only one of these criteria would not be sufficient to initiate an incremental process. The original intention of the ACER Guidance was to address situations where only one criteria was provided (e.g. a non-binding indication for a new transportation route to connect to a new supply source). The debates at the final SJWS equally indicated that the preferred approach would be to allow all criteria individually or in combination to trigger an incremental or new capacity process.

ENTSOG therefore included this into the section of “when to offer” in the current version of the Draft Incremental Proposal. The text also provides the flexibility to assess all conditions in combination when designing potential offer levels to ensure efficient design of capacity projects. It should be noted, that the three criteria are not necessarily independent of each other and further studies could therefore provide a more correct assessment before initiating an incremental process.

Time window

The time window for submitting non-binding indications was also discussed during the SJWS. A two month time window could be considered to be too restrictive and lead to immature indications if network users need to submit their indications at a specific point in time. However, it was highlighted that a standardised time window would be more transparent and thus possibly be more beneficial for all network users.

Initially, it was suggested that the best starting date to submit non-binding indications was the last day of the yearly auction, but the stakeholder discussions clarified that there could be a risk that a network user would participate for existing capacity and submit non-binding indications. As illustrated in example IV below, the start date is therefore 10 days after the start date of annual long term auctions and initially the suggested end date would be 2 months after the start date.

The majority of stakeholders present at the SJWS supported the idea to provide more time flexibility for network users for non-binding indication submission. ENTSOG took into account this feedback which is now reflected in the Draft Incremental Proposal allowing for network users to be able to submit non-binding indications throughout the whole year. This helps to avoid the problem of immature requests caused by a short time window for their submission. This also makes it possible for TSOs to start the necessary preparations during the year in case a mature non-binding request arrives that could be considered on a stand-alone basis. TSOs will still have the possibility to define a due date which will be a starting point for the aggregated demand assessment and other subsequent steps of the incremental process. The Draft Incremental Proposal also states that the period between the two subsequent due dates shall not exceed 24 months.

Example IV: Timeline for submitting non-binding indications

Period for submitting non-binding indications

Two approaches are still under discussion:

1 Time window approach

- Specified time window after the annual long-term auctions
- Indications received in time window will be considered for next possible auction or open season procedure



2 Due-date approach

- Specified due date (potentially after long-term auctions)
- TSOs will fully assess and report based on indications received
- If indications are sufficient, TSOs have the possibility to shorten the process and to launch the offer process before the due date



Fees for technical studies

The ACER Guidance requires ENTSG to propose provisions for a cost efficient European incremental capacity process. Since demand indications which can be submitted by network users are non-binding, there is a risk that the amount of incoming non-binding indications is such that it might exceed the network planning capacities of the respective TSO. The assessment whether a non-binding indication is well founded or not is not insignificant. However, technical studies and network modelling resulting from these demand indications bring substantial costs for the TSOs and do not necessarily result in a capacity project from which revenues could be generated to cover such costs.

The SJWS discussions lead to the proposal to include an option for TSOs to charge such fees in cases where the regulatory framework does not allow an alternative mechanism for the recovery of costs. But in this case the function of such fees as a filter for immature/exaggerated non-binding requests would be lost. This was therefore included in the Draft Incremental Proposal.

Question 10: Do you agree with the conditions that shall lead to the offer of incremental and new capacity as defined in Article 20c (1), (6), and (7) (CAM NC)? If not, please elaborate.

Question 11: Do you agree that the due date approach is preferable to the time window approach as foreseen in article 20c (3) (CAM NC)? If not, please elaborate.

Question 12: Are there any other issues that you wish to address regarding conditions of when to offer incremental and new capacity as foreseen in article 20c (CAM NC)? If so, please elaborate.

5.6 Article 20b of CAM NC: Auction mechanisms

A: Corresponding extracts from the ACER Guidance

The CAM NC amendment should stipulate the integration of incremental and new capacity into the annual yearly capacity auctions of the NC CAM for existing capacity. This should apply at least in the case where a capacity expansion between two adjacent market areas is considered.

ENTSO-G is requested to develop, test and consult a detailed amendment to the NC CAM's allocation procedure for existing capacity, keeping the integrity of the ascending clock algorithm. The amendment should enable the integrated offer, testing, and allocation of bundled new and incremental capacity to take place together with existing unsold yearly capacity. The same service for the same period will have the same value for network users if acquired at the same time.

ENTSO-G should apply at least the following principles for the development of the methodology:

- offer and allocate bundled incremental and new capacity in a cost effective, nondiscriminatory, transparent procedure that enables taking into account willingness-to-pay, on the booking platform that promotes competition;
 - ensure efficient allocation of existing capacity, irrespective of the outcome of the economic test for the incremental and new capacity under consideration;
 - the possibility to accommodate different reserve prices if a tariff adjustment is justified;
- and
- the possibility to test network users' differentiated willingness to pay for more than one level of incremental and new capacity in an auction, e.g. no increment (allocate existing capacity only because the economic test is not passed), small increment (allocate incremental and existing capacity), large increment, very large increment, etc....

ENTSO-G is requested to consider:

- the possibility for network users to revise their bids if the economic test fails for incremental and new capacity;

ENTSO-G should focus in its proposal on providing a recommended technical approach of integrated bidding for existing and incremental capacity (drawing on the model of parallel bidding ladders).

B: Background to Draft Incremental Proposal formulation

The CAM NC provisions on the long term offer of capacity need to be amended, when accommodating the offer of incremental/new capacity at an interconnection point together with

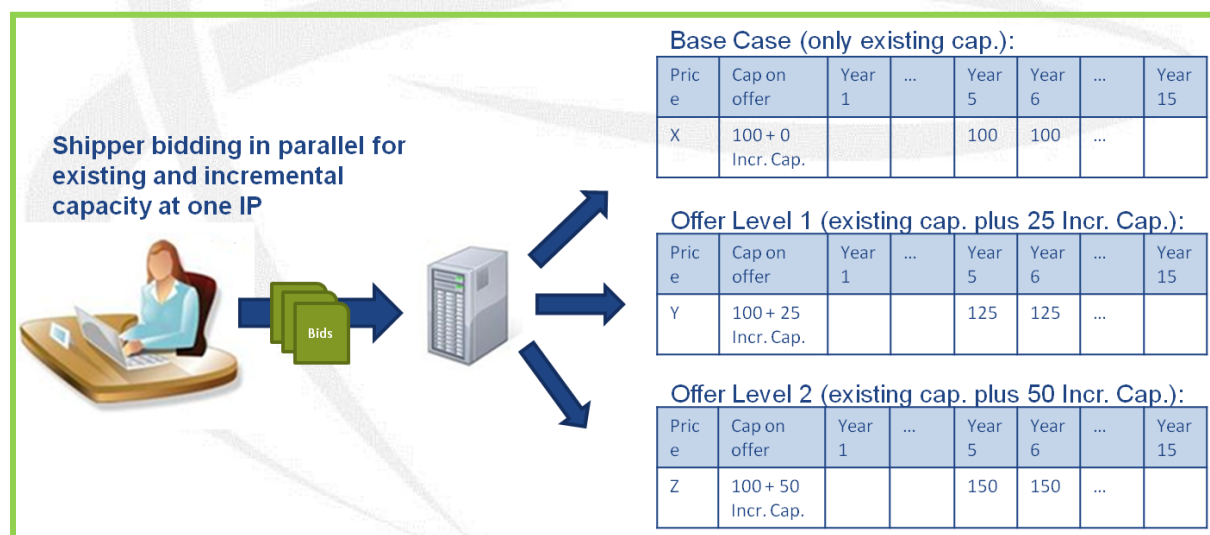
existing capacity. However, via the implementation of a “parallel bidding ladder approach” ENTSOG is maintaining the ascending clock algorithm defined in CAM NC as a basis for the auction procedure as requested by ACER. In addition, the ACER Guidance asks ENTSOG to consider the possibility for network users to revise their bids if the economic test fails for incremental and new capacity which may have caused by how TSOs designed the offer levels. The provisions for auctions mechanisms are described in article 20d in the Draft Incremental Proposal.

C: Topics and policy choices

Parallel bidding ladders

Within the framework of a parallel bidding ladders approach, the shipper will have to place bids for bundled capacity for each year and offer level in parallel. Whereas the offer level(s) include the base with only the existing capacity, the number and magnitude of the remaining offer level may vary from project to project. In practise, bidders have to place bids in a number of parallel “regular” ascending clock auctions according to CAM NC at one and the same interconnection point. As an example, for an incremental auction including ten years of incremental or new capacity with three offer levels (base case, level 1, level 2) three parallel bidding ladders will be opened, each containing ten auctions.

Example V: Bidding for bundled capacity with incremental capacity on offer



The parallel bidding ladders approach provides:

- a high degree transparency and flexibility for the users;
- the possibility to auction existing capacity only and incremental capacity in conjunction with existing capacity in the same time window;

- the possibility to accommodate different reserve prices;
- the possibility for network users to differentiate their willingness to pay as a function of different offer levels.

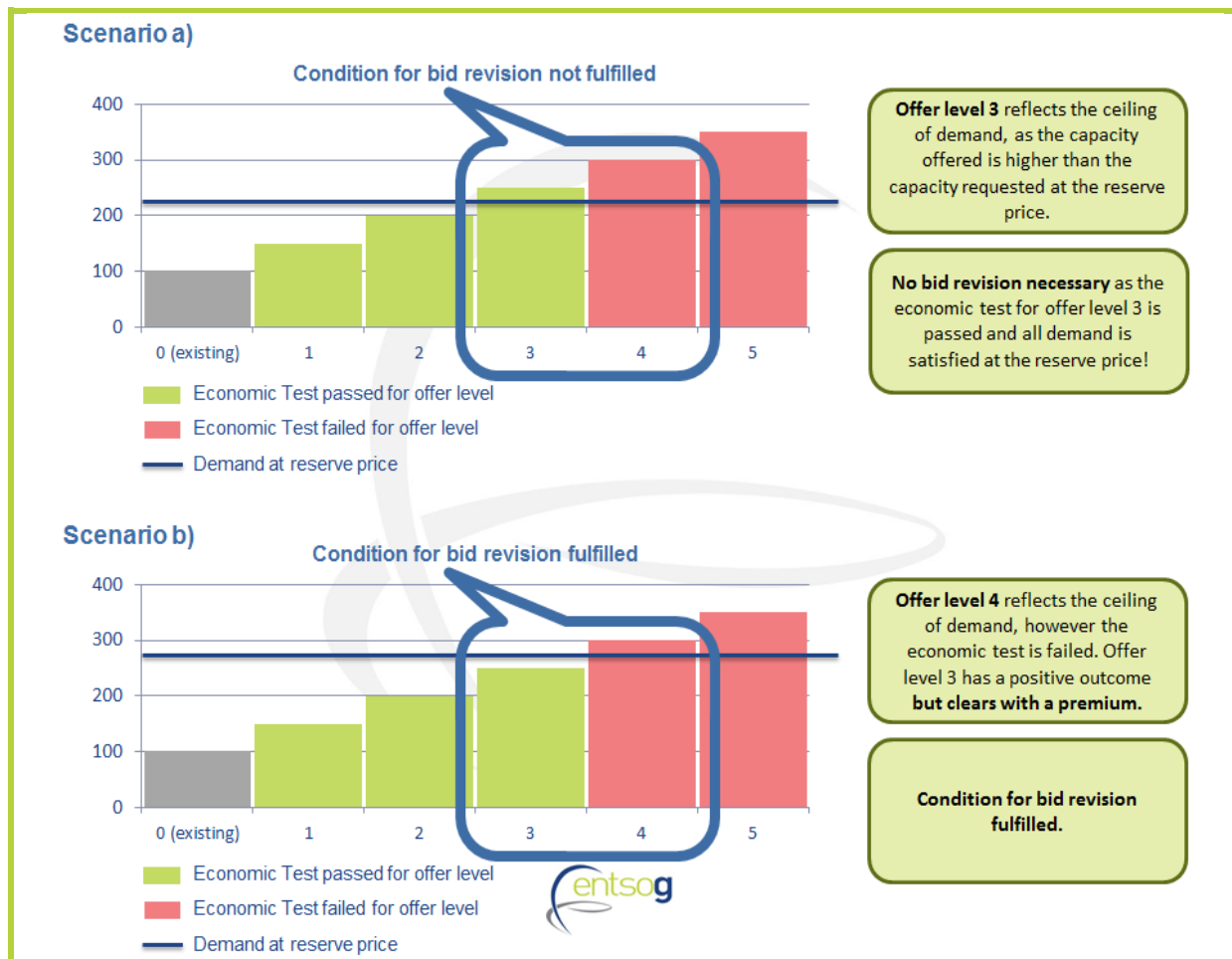
Revision of bids

During the SJWS, ACER requested ENTSG to look closer into the possibility of allowing bid revision in the auction mechanisms. The parallel bidding ladder based auctions sometimes may result in suboptimal outcomes due to the design of the offer levels being tested in incremental capacity auctions. Network users should be given the chance to re-assess their bidding behaviour after an auction ended in order to improve such (perceived) suboptimal auction outcomes.

If bid revision is deemed necessary, ENTSG is of the view that clear conditions for its application should be defined. Bid revision should therefore only be applicable in those cases where a well-defined “suboptimal auction result” actually materialises and the complexity of auction processes should not be unduly increased by the application of bid revision. A well-structured bid revision procedure would allow network users to appropriately follow such auction processes and to ensure the comprehensibility of the respective auction results.

Given the application of the parallel bidding ladder approach, ENTSG proposes to define an auction result as being suboptimal in case the highest offer level which results in a positive economic test clears at a premium. The reason for this definition is that incremental auctions as such have the inherent objective to avoid auction premiums for congestion and that for network users a higher offer level at the reserve price might be preferable to the successful lower offer level at a premium.

Example VI: Bid revision



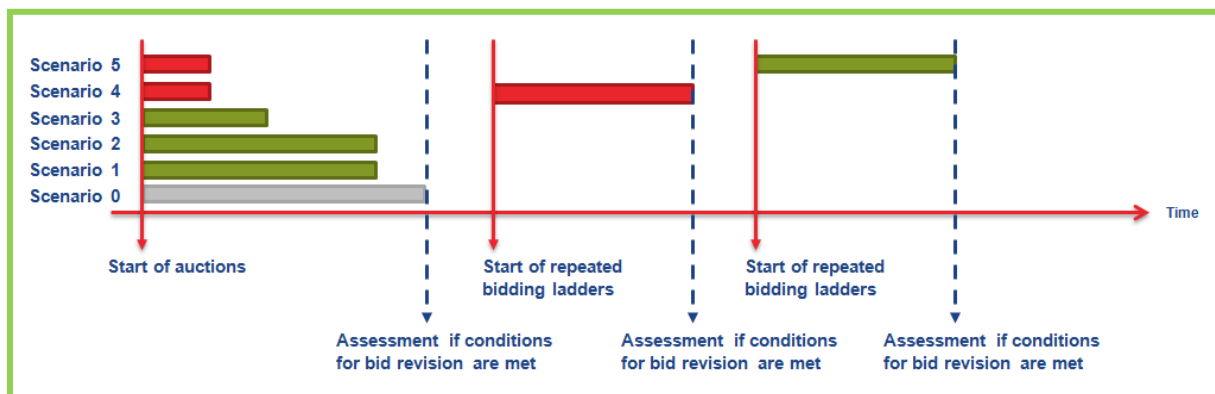
Technical design of bid revision

Once the auctions for all offer levels have cleared, the TSOs will assess whether the conditions for bid revision are met (highest offer level resulting in a positive economic test cleared at a premium). As can be seen in the example VI above, this is the case in Scenario b) where offer level 3 (which represents the highest offer level resulting in a positive economic test) clears with a premium on the starting price of the auction. In such a case (also illustrated in example VII below) the TSOs will repeat the bidding ladder for at least the next highest offer which allows network users – both new ones as well as those having placed bid in the initial bidding ladder – to place new (revised) bids as if a completely new auction starts.

ENTSOG is convinced that such a repetition of a bidding ladder is the clearest and most comprehensible solution for bid revision and additionally would require least effort in terms of

technical implementation for those TSOs and booking platforms which have already implemented CAM NC algorithms.

Example VII: Technical design of bid revision



It is important to note that bids in bidding ladders which won't be repeated remain binding (e.g. in bidding ladders 0 to 3 in the picture above) as long as the repeated auction has not yet ended. Only in cases where the repeated auction results in an improved outcome (lower costs per unit of capacity while meeting the economic test and a higher amount of incremental or new capacity) compared to the initial result, the offer scenario of the respective bidding ladder represents the project the TSOs should consider for further steps in the incremental process.

ENTSOG believes, that given the assumption that bid revision will improve the efficiency of parallel bidding ladder based auctions, the concept described above should be applied consistently also in repeated auctions. When the conditions for bid revision are fulfilled in a repeated bidding ladder (e.g. in bidding ladder 4), the next higher bidding ladder (e.g. bidding ladder 5) should be repeated as well (and so forth). The number of repeated bidding ladders is limited by the number of higher offer levels.

Question 13: Do you agree with the concept of parallel bidding ladders to auction incremental and new capacity as foreseen in article 20d (CAM NC)? If not, please elaborate.

Question 14: Do you agree with ENTSOG's opinion that repeating the identified bidding ladder(s) represents the clearest way to allow for bid revision as foreseen in article 20d (3) (CAM NC)? If not, please elaborate.

Question 15: Do you prefer: 1) a continuous approach for bid revision as proposed by ENTSOG in article 20d (3) (4); or 2) an approach according to which bid revision is only applied once? Please elaborate.

Question 16: Are there any other issues that you wish to address regarding auction mechanisms as foreseen in article 20d? (CAM NC) If yes, please elaborate.

5.7 Articles 20e, 20f, 20g of CAM NC: Open season procedures

A: Corresponding extracts from the ACER Guidance

The CAM NC amendment should limit the use of open season procedures for incremental and new capacity to those cases where the likely capacity demand, as identified in section 2.b) or in any informal or non-binding assessment phase:

i) extends across more than two market areas; or

ii) requires an investment project of such size and complexity (e.g. where the investment decision for incremental and new capacity is predicated on associated simultaneous investment decisions in respect of related projects) that the procedure described in section 2.e) could appear not to be a robust approach.

ENTSO-G is requested to elaborate on provision (ii) in terms of when this is the case.

The decision whether the criteria are met and an open season can be used is subject to NRAs approval. The terms of the open season and in particular the design of the binding commitment phase of the open season should be approved by all NRAs affected. The terms should comply with the following principles, in addition to the coordination and information provision requirements in 2.c) and d):

It should offer non-discriminatory opportunities to make commitments for capacity products.

- The capacity expansion should aim at satisfying all commitments, as far as this is overall efficient and economically feasible; where satisfying all commitments would not be economically feasible, or not efficient in the broader geographical context, an allocation rule based on willingness-to-pay should be used in priority. This may lead to using an algorithm modelled on the CAM auction algorithm, for example as described in section e).

- Pro-rating is the only other fall-back allocation rule that should be allowed in order to arrive at an efficient investment size that maximises the degree to which user requests are fulfilled. Its usage should be conditional on the demonstration that the (sole) use of willingness-to-pay would be impractical (e.g. pro-rata needed in combination with willingness-to-pay when demand curves are used or when flat bookings are obtained from network users which cannot be economically met simultaneously).

For binding commitments in any open season procedure, all relevant provisions of the NC CAM on capacity products should hold, particularly with respect to capacity product design, bundling and the capacity set aside for short term allocation. Only the following deviations from the NC CAM are admissible:

- Network user commitments for capacity can be obtained for 15 years as of the capacity becoming useable. Beyond that, commitments for an additional period of up to 5 years can be obtained³. The requirement of additional commitments has to be shown to and assessed by the concerned NRAs.

- If existing capacity is still available at an IP for the years for which binding bids for new capacity are invited, these capacity products can be included in the offer of incremental and new capacity.

- Conditional commitments, for instance across a number of years requested, including or excluding bids at

other IPs, or for a minimum amount of capacity required (fill-or-kill) can be obtained in open season procedures.

B: Background to Draft Incremental Proposal formulation

The ACER Guidance limits the use of Open Season Procedures to circumstances when the capacity demand is extended over more than two market areas or if the investment project is of such complexity that only Open Season Procedures would be able to accommodate such a project. The SJWS revealed a significant interest in the conduct, the guiding principles and the allocation mechanism in Open Season Procedures. The ERGEG Guidelines for Good Practice on Open Season Procedures (GGPOS) proved to be still relevant and were cited by stakeholders throughout the process. The provisions for Open Season Procedures are described in articles 20e, 20f and 20g in the Draft Incremental Proposal.

C: Topics and policy choices

When to use of Open Season Procedures instead of auctions

During the SJWS, ENTSG was requested by the European Commission to be more prescriptive on when to use Open Season Procedures focusing on how and when decisions will be taken. Consistent with the requirements in the ACER Guidance, ENTSG developed a number of examples of when to use Open Season Procedures instead of Auctions. The Incremental Proposal therefore highlights a number of examples that illustrate when Open Season Procedures are more suitable than auctions. These examples were the following:

1. When an investment project for incremental or new capacity stretches over more than one interconnection point, more than two market areas, or when an auction cannot accommodate all the market scenarios or when the development of new or incremental capacity is linked to or influenced by the realisation of an exempted infrastructure. In such circumstances, the prospective network users are likely to be interested by a link between allocation of capacity in the considered project and allocation of capacity of the exempted infrastructure. This is very similar to conditional bidding as shown in example 3 below.
2. When the required offer levels cannot be efficiently derived from the demand assessment, since shippers have different capacity requests and auction cannot satisfy the diversity in their request. In such situations, the range of potential projects is too wide to be directly handled via an auction. A single interconnection point may need a small amount of capacity for some shippers for a short duration as well as big volumes for other shippers, all reflecting different requirements. Open season procedures enable iterative exchanges between network users and TSOs. Through the Open Season Procedures TSOs will be able to compare, refine and select the options that will best fit to market possibilities.
3. Allowing for conditional bidding can be desirable, because it is expected to improve the likelihood of passing an economic test. The condition may be such as “fill-or-kill”, a request to book for a certain period or a request to book capacity along the entire gas route:

- a) The fill-or-kill condition allows for a shipper to cancel a bid if his entire capacity request is not obtained.
 - b) The request to book for a certain period allows for a shipper to abandon the bid in case the bid cannot be honoured for the whole period.
 - c) The request to book capacity along the entire gas route allows for a shipper to cancel a bid if it is not possible to book capacity along the entire gas route.
4. When the horizon of user commitments that is necessary to pass the Economic Test at reference price is longer than the 15 years horizon provided in the auctions as stated in the CAM NC (article 11 in the Regulation (EU) No 984/2013). This deviation from CAM NC may improve the financial viability of the project because it allows for an additional number of years for booking of capacity. This option could be a decisive incentive for shipper interest and thus for the viability of the project itself.
 5. When an iterative approach with regard to potential cost sharing agreements is selected as foreseen in article 44 in the TAR NC showing a mechanism for possible redistribution of revenues. The one-off performance of an auction would limit the chances of successfully redistribute potential revenue across the border.

Principles for the use of Open Season Procedures

ENTSOG developed a number of processes and procedures that must be taken into account when conducting an Open Season Procedures. Many of these principles are inspired by the ERGEG Guidelines for Good Practice on Open Season Procedures (GGPOS).

The aspect of transparency and non-discriminatory access for all market participants was subject to extensive debate throughout the SJWS where some stakeholders expressed their concern regarding the transparency, fairness and openness of Open Season Procedures. This section of the Incremental Proposal obliges TSOs to publish a notice that describes the different steps in the Open Season Procedures outlining all relevant process information such as start and end dates for making non-binding offers, procedures and timetables and the date on which capacity allocations will be directed or assigned to open season participants.

Allocation of incremental and new capacity in Open Season Procedures

Some stakeholders at the SJWS focused on long term bookings in order to ensure the financial viability of the investment whereas others prioritised the development of competition and assuring equal market access for all market participants. ENTSG emphasised throughout the SJWS that the Open Season Procedures should aim to satisfy all expressed demand for capacity. In cases when such demand could not be satisfied, an allocation rule needs to be applied. This allocation rule should take into account the interest of all groups.

In line with the ACER Guidance, ENTSOG has written an allocation rule that aims at prioritising the capacity requests of network users for each year according to the price of per unit of capacity they are willing to pay. This mechanism could be modelled upon the CAM NC auction algorithms. Some stakeholders thought that this allocation rule provides a prerogative for short term capacity booking at the expense of long term capacity booking. This could be detrimental when passing the economic test of the project and potentially endanger the financial viability of the project. Therefore, the Incremental Proposal includes an alternative allocation rule, that should be applied if the default rule does not allow for the economic test to be passed, taking into account the higher contribution of long term capacity requests for the financing of incremental or new capacity.

The stakeholder discussions illustrated the difficulty in providing ex-ante an alternative allocation rule that fits all the possible cases. The Draft Incremental Proposal limits the alternative allocation rule to situations where willingness to pay per year has not lead to the development of incremental or new capacity, with safeguards in matter of transparency (the rule must have been ex-ante disclosed in the notice). The rule makes it clear that the overall contribution of a network user can be part of the allocation mechanism. When there is a choice between increased competition due to incremental capacity or no incremental capacity the policy objective can then be to assure the realisation of an incremental capacity project.

Question 17: *Do you agree with the provisions that shall lead to conducting an Open Season Procedure instead of auctions for incremental and new capacity as foreseen in article 20e (2) (CAM NC)? If not, please elaborate.*

Question 18: *Do you see any other conditional capacity commitments in Open Season Procedures than the issues raised in the Draft Incremental Proposal article 20f (3) (CAM NC)? If yes, please elaborate.*

Question 19: *Do you agree that the proposed Open Season Procedures notice contains sufficient information as foreseen in 20f (8) (CAM NC)? If not, please elaborate.*

Question 20: *Do you agree with the default allocation rule foreseen for Open Season Procedures, being willingness to pay per unit and year as foreseen in article 20g (3) and the alternative allocation rule subject to NRA approval as foreseen in article 20g (4) (CAM NC)? If not, please elaborate.*

Question 21: *Are there any other issues that you wish to address regarding Open Season Procedures as foreseen in article 20e, article 20f and article 20g (CAM NC)? If yes, please elaborate.*

5.8 Article 42 of TAR NC: Economic test principles

A: Corresponding extracts from the Framework Guidelines for harmonised Tariff Structures for Gas

2.4.1 Incremental and new capacity

After NRA approval, TSOs shall publicly provide at least the following information with a sufficient lead time, before an offer of incremental or new capacity is made for binding commitments:

- PV_{AR} , the present value of the estimated potential increase of the TSOs' allowed revenue in each year during the economic life of the new asset, which is attributable to the investment (outgoing cash flows);
- The fraction (" f ") of the PV_{AR} , which refers to the estimated increase in allowed revenues attributable to the investment that needs to be underwritten by user commitments to pass the economic test (incoming cash flows), including the factors that have influenced the determination of f , which should be quantified, where possible and relevant;
- An estimated projection of tariffs for the bundled yearly capacity products of the capacity expansion(s) considered and an explanation of how it is calculated.

3.5. Incremental and new capacity

Section 3.5 applies to all incremental and new capacity at entry and exit points under the scope of the Network Code on CAM, where the decision to invest is market-based, i.e. based on binding user commitments made during a CAM auction or open season.

In such situations the decision to invest will be conditional on the validation of an economic test showing that the project is financially viable considering network users' binding commitments to purchase the incremental or new capacity.

3.5.1. Economic test

3.5.1.1. Economic test formula

The Network Code on Tariffs shall specify that network users' binding commitments in respect of an incremental or new capacity project shall be deemed sufficient to justify the investment, when a financial test is passed: the value of expected future payments from network users' commitments shall be equal to or exceed an appropriate proportion of the estimated increase in allowed revenues of the TSO.

The test is formulated as follows and is passed if:

$$PV_{UC} \geq f \cdot PV_{AR}$$

Where:

PV_{UC} is the Present Value of expected network users' commitments (incoming cash flow), which is the auction or allocation clearing price multiplied by the capacity volume commitment for each year where such commitment is obtained, discounted with the cost of capital to its present value.

PV_{AR} refers to the present value of the estimated potential increase of the TSOs' (yearly) allowed revenue, which is attributable to the investment, during the economic life of the new asset. The Network Code on Tariffs shall require TSOs to make their best efforts to provide a reliable estimate.

f is the fraction of PV_{AR} that needs to be underwritten by user commitments to pass the test³⁴.

³⁴

The economic test is intended as an ex-ante tool (ahead of the investment decision) to evaluate the

financial viability of a project on the basis of the best information available at the time of the investment decision. The proportion of PV_{AR} (including, subject to any regulatory efficiency assessment, any PV_{AR} cost over runs) not covered by expected future payments from network users' commitments would be recovered, either by future bookings at the point, or from all network users via the revenue recovery mechanism.

3.5.1.2. Criteria to be considered when setting the "f" parameter

The "f" parameter can be determined on an individual project basis, but shall be subject to approval at a Member State level by relevant NRAs. When setting the "f" parameter, the following criteria shall be taken into account:

Duration of network users' commitment period compared to the economic life of the asset; (The longer the commitment period relative to the asset life is, the more can be underwritten by investors, which may justify a higher "f" parameter);

② Capacity set aside for short term bookings, which is at least 10% according to the Network Code on Capacity Allocation Mechanisms; (This may result in a lower "f" parameter, considering that the 10% or part of it will be booked only short term.);

② Positive externalities which may justify a lower "f" (e.g. improvement of competition, improvement of security of supply, investment useful for other points in the network and not just the one where it creates capacity).

3.5.1.3. Single economic test

The Network Code on Tariffs shall specify that a single economic test shall be published, incorporating the aggregate investment requirements of all involved TSOs and NRAs relating to a given capacity project. Only those investment costs directly relating to the incremental capacity should be included. Where NRAs involved determine different "f" factor values, NRAs shall cooperate to determine an aggregate "f" factor value.

If the distribution of PV_{AR} and the PV_{UC} between the TSOs does not allow one of them to meet its specific investment requirement (based on its assessment of "f"), while the single test is passed, TSOs and NRAs may decide to modify the distribution of revenues between the TSOs (by a cost sharing agreement or a different split of the bundle reserve price).

In case of external financial support (e.g. subsidies from the EU), the PV_{AR} should be lowered according to the amount received.

B: Background to Draft Incremental Proposal formulation

The economic test as described in the Tariff Framework Guidelines is essential for the process of offering incremental and new capacity under market demand circumstances irrespective whether this will be done via auction or Open Season Procedures. The economic test checks whether the market is willing to underwrite the investment via upfront commitments. During the SJWS, especially determination of f-factor, the calculation of Present Value of Regulated Revenues as well as User Commitments and the combination into a single economic test were discussed. The provisions for Economic test principles are described in articles 42-45 in the Draft Tariff Network Code.

C: Topic and policy choices

Change of 'PVAR' to 'PVRR'

The concept of Present Value of Allowed Revenues (PVAR) was thoroughly discussed at the stakeholder discussions. PVAR represents the present value of increase in allowed revenues related to the respective capacity expansion. However, in price cap regulatory regimes, no maximum level of revenues is set or approved by the NRA, therefore 'Allowed Revenues' as a term do not exist. The formula that is used for the Draft Incremental Proposal is therefore PVRR (Present Value of Regulated Revenues) which are either the allowed revenues in revenue cap regimes or the target revenues in price cap regimes. The general principle of the formula, however, remains unchanged by this.

The 'f-factor'

The f-factor was also debated by the stakeholders. Some stakeholders argued that the 'f-factor' should be high ensuring the market-based character of investments underpinned by up-front user commitment. Whereas a high f reduces the chance of a positive economic test, it also reduces the risk of cross-subsidies. The task of the TSO and NRA is to find the right balance when defining f. Therefore, the criteria written down in the Draft Incremental Proposal and derived from the Framework Guidelines for developing a network code for tariffs must be taken into account. The 1-f part must also be guaranteed and recovered through a number of means as mentioned in the Draft Incremental Proposal:

- Future bookings of the incremental/new capacity (being demand continuation or capacity reserved for short term offer)
- Tariffs paid at any other point(s) via socialisation
- Any other financing through appropriate payment guarantee mechanisms established by NRAs or Member States
- If none of the above can be ensured, the costs associated with 1-f needs to be decreased either by increasing f or by decreasing PVRR through e.g. EU subsidies

Single economic test and redistribution of revenues

The Draft Incremental Proposal states that TSOs shall combine the underlying economic test into one single economic test. It also states that the aggregated single test is only passed, if the level of user commitment is such that both underlying individual economic tests are passed. This effectively means that the minimum level of network user commitment to pass the test on both sides (450 in example VIII below) is the basis of the mathematical exercise to determine the parameters of the single economic test.

Example VIII: Passing of single economic test

Level UC	0	150	250	350	450	550
TSO A	no	no	yes	yes	yes	yes
TSO B	no	no	no	no	yes	yes
Single Test	no	no	no	no	yes	yes

Red = test is not passed, Green = test is passed

In the example, a range of possible network user commitments exist at which the economic test is passed only on one side of the border but not on the other (the range between 250 and 450). In order to decrease this range, involved NRAs might agree to modify the distribution of revenues between TSOs. This could be done in a number of ways: NRAs may decide on a cost sharing agreement or a different split of the bundled reserve price. The relevant TSOs and NRAs will decide on a case by case basis, bringing different regulatory regimes and technical realities together and take into account the uniqueness of each cross-border investment project. The relative sizes of the investment to the existing systems and the distribution of costs across the border distinguishes every case different from the previous.

The Draft incremental proposal contains three approaches to structure the discussion process on a potential redistribution of revenues:

- An ex-ante agreement, where TSOs and NRAs assess a potential redistribution of revenues once the parameters of the individual economic tests are agreed upon on both sides of the border before the economic test is held.
- An ex-post agreement, where TSOs and NRAs assess a potential redistribution of revenues after the single economic was not passed based on a minimum level of network user commitment that is required on both sides of the border. This could mean that if the actual level of network user commitment in an auction or Open Season is not sufficient to pass the single economic test but to theoretically pass the individual economic test on one side of the border, the TSOs and NRAs involved could discuss on how to adjust the test parameters afterwards in order to pass the economic test.
- Integrated agreements where TSOs and NRAs agree on a redistribution of revenues into an allocation procedure which is only offered in Open Season Procedures. The redistribution of costs or revenues would then be based on the binding user commitments.

Redistribution can help to align the level of needed user commitments in term of booked capacities. ENTSOG is of the opinion that no general rule regarding the redistribution can exist since all

forthcoming projects are different in their characteristics. NRAs may therefore decide to redistribute revenues before, after or during the binding phase in the case of Open Season Procedures. The single economic test can only be positive if all underlying economic tests are positive when taking into account a possible redistribution of revenues.

Question 22: Do you agree with the structure of the economic test in the Incremental Proposal as foreseen in article 42 (TAR NC)? If not, please elaborate.

Question 23: Do you agree with the factors that shall be taken into account when defining the f -factor as foreseen in article 43 (TAR NC)? If not, please elaborate.

Question 24: Do you agree with the structure of the recovery mechanisms for the share of $1-f$ as foreseen in article 43 (2) (TAR NC)? If not, please elaborate.

Question 25: Do you agree with the way the single economic test is aggregated as foreseen in article 44 (TAR NC)? If not please elaborate.

Question 26: Do you agree with the three approaches for a potential redistribution of revenues as described in article 44 (4) (TAR NC)? If not, please elaborate.

Question 27: Are there any other issues that you wish to address regarding economic test as foreseen in articles 42-45 (TAR NC)? If yes, please elaborate.

5.9 Article 46 of TAR NC: Tariff principles

A: Corresponding extracts from the Framework Guidelines for harmonised Tariff Structures for Gas

3.5.2. Determination of the price at which users can request incremental or new capacity

The Network Code on Tariffs shall specify that, when determining the minimum price at which network users can request incremental capacity, the reference price as determined by the cost allocation methodology shall apply.

In the specific case, and only in the case, where selling all the incremental or new capacity offered at the reference price would not generate sufficient revenues to pass the economic test with the value of the " f " parameter defined on the basis of the criteria set out in section 3.5.1.2, NRAs may decide to adjust the minimum price at which participants can request capacity. This adjustment shall ensure that the economic test is passed if all the incremental or new capacity offered is subscribed.

The Network Code on Tariffs shall define how this adjustment shall be implemented, taking account of the following principles:

1. Preserving the financial integrity of the economic test;
2. Avoiding cross subsidy between network users;
3. Compatibility with the cost allocation methodology;

4. Avoiding fragmentation of reserve prices at the same entry or exit point.

Applying a premium to the tariff paid by those users booking capacity in the first auction in which incremental capacity is offered (those users triggering the investment) would be consistent with these principles and should be the default option. In determining the Network Code on Tariffs, ENTSOG shall consider alternative approaches, in addition to the default option. Where such alternatives are consistent with the principles above, ENTSOG shall include them in the Network Code on Tariffs. Where any alternative approaches result in the application of a premium to the reserve price paid by users other than those triggering the investment during the first auction of incremental capacity i.e. by other future users at later auctions, NRAs shall determine a maximum number of yearly auctions for which the minimum premium should apply.

B: Background to Draft Incremental Proposal formulation

This section in the ACER Tariff Framework Guidelines specifies that when a minimum price is determined at which network users can request incremental capacity, the reference price as determined by the cost allocation methodology shall apply. The tariff principles for incremental and new capacity are described in article 47 in the Draft Incremental Proposal.

C: Topic and policy choices

Fixed versus floating tariffs

Stakeholders raised this issue due to concern that this could have implications for the economic viability of a project. This issue is also raised within the TAR NC work stream. In article 41 of the draft TAR NC, the option of a fixed tariff has been included, since it could facilitate the realisation of incremental and new capacity. This possibility is particularly relevant for incremental and new capacity. In fact, fixed prices could represent a necessary condition for incentivising shippers' long-term bookings through the predictability and stability they provide. In other terms, fixed prices can represent a good solution to get clear market commitments backing infrastructure commissioning. The application of either fixed or floating tariffs will be decided by the NRA.

Tariffs to be used to calculate PVUC

The issue regarding calculation of PVUC regarding reference prices was also presented at the SJWS. This resulted in a provision in the Draft Incremental Proposal stating that reference prices, to which incremental and new capacity will be offered, have to be estimated on the basis of the relevant assumptions. The reference prices have to be used only for the purpose of calculating the Present Value of User Commitments, constituting mere indicative estimations of the projection of future tariffs.

Mechanisms for tariff adjustment

The economic test is designed to establish whether the level of user commitment is sufficient to cover a predefined share (f-factor) of the PVRR. This means that depending on the choice of f-factor a range of PVRR will be covered by up-front commitments of network users. Cases where future

bookings are not fully covering the costs of the remaining share require the guarantee from NRAs that the resulting revenue shortfall shall be recovered via a payment guarantee mechanism.

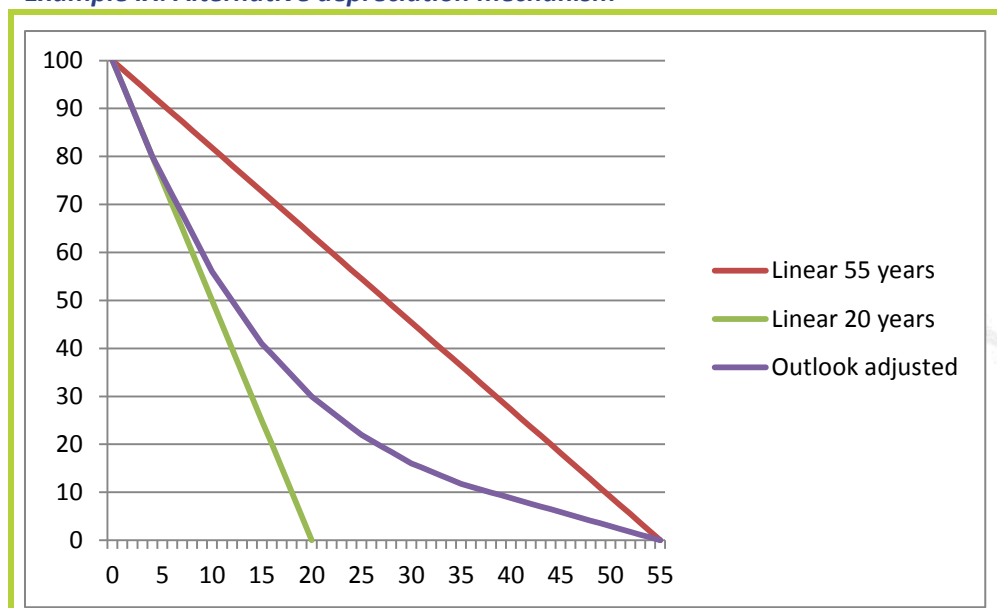
While this guarantee might suffice for many systems, price-cap regimes, and merchant pipelines or interconnectors, systems with a high level of transit or a relatively small captive domestic customer base and systems involved in pipe-to-pipe competition risk that a share of the investment will be unrecoverable. During the SJWS ACER invited ENTSG to suggest possibilities to address this issue. The obvious way to do this is to enable the f-factor to be relatively high, meaning close to 1. Since the reservation for short term offer is fixed at min. 10%, the other element pressing the value of f down is the assumed economic lifetime of the asset. Together with many stakeholders, ENTSG concludes that an adjusted depreciation rate, thereby improving the alignment of the technical and the economic lifetime of the respective investment, would be the most logical solution to this problem.

Adjustment of the depreciation rate

During the SJWSs, ENTSG and stakeholders concluded that as an option limited to incremental and new capacity only and to be decided by the NRA on a case by case basis, an adjustment of depreciation rates would be a useful tool enabling the economic test to be passed. At SJWS 5, an adjustable depreciation mechanism was presented and debated among the stakeholders. This outlook adjusted depreciation mechanism reconciles a faster recovery of an investment without a formal change in the depreciation period under the regulatory contract for future or existing assets. The fact that it is being used in upstream project means it is a proven concept for projects with a more dynamic horizon. Under this outlook adjusted depreciation mechanism a new asset would start to be depreciated in over period of for instance 20 years.

In principle after the first year of operation there is again an outlook for the next period of e.g. 20 years on the benefits from the infrastructure. If the outlook has not deteriorated in comparison with the previous outlook there is again a viable period of 20 years of use of the asset. This results in depreciating the remaining 19/20 of the asset again over a period of 20 years, in the second year the depreciation would then be 19/20/20. One would continue this process within the normal regulatory lifetime of 50+ years. Of course if the outlook does deteriorate one would stay with the original 20 year period. The outlook adjustment curve (purple color) is presented in example IX below:

Example IX: Alternative depreciation mechanism



This solution would lead to a quicker depreciation at the start of a new asset without losing the current depreciation period. The higher PVUC would increase the chance of passing the economic test and hence making the incremental and new capacity possible. The alignment of depreciation period and booking horizon leads to higher PVRR during the booking horizon and hence to higher reference prices at the start and lower prices further on.

Adjustment of tariffs

In line with the ACER Guidance, four mechanisms for tariff adjustment have been elaborated and presented as illustrated in example X:

Example X: Advantages and disadvantages of mechanisms of tariff adjustment

Approach	Advantage	Disadvantage
Minimum premium for those participating to incremental process	➤ User that booked long-term capacity before investment was triggered are protected from tariff increases through investment	➤ Reduces willingness for long-term commitment as future offers will be cheaper
Adjusting reference price for all users at the IP, except for those that have booked before initial offer	➤ User that booked long-term capacity before investment was triggered are protected from tariff increases through investment	➤ Complexity due to at least two different reference prices for the same product
Adjusting reference price for all users at the IP	➤ Clear and simple process (one reference price for all users)	➤ Affects users that booked long-term capacity before investment was triggered
Downward adjustment for those participating to incremental process	➤ User that booked long-term capacity before investment was triggered are rewarded for allowing the investment to proceed	➤ Users with existing capacity have a relative disadvantage

Based on SJWS discussions, the minimum premium has been included as a default tariff adjustment in addition to the shorter depreciation period. The other possible adjustments of tariffs as seen in example X above are not excluded by the incremental proposal.

Question 28: Do you agree with the default mechanism foreseen to adjust tariffs if required as covered in article 46 (TAR NC)? If not, please elaborate.

Question 29: Do you agree that in order to raise the level of commitment a downward tariff adjustment rewarding long-term booking can be included as foreseen in article 46 (TAR NC)? If not, please elaborate.

Question 30: Do you agree with including a possibility to adjust depreciation rates as a mechanism to avoid socialisation of costs as foreseen in article 46 (TAR NC)? If not, please elaborate.

Question 31: How do different tariff options impact on the markets' willingness to commit long term in order to pass the economic test? Please elaborate.

Question 32: Are there any other issues that you wish to address regarding tariff related issues as foreseen in article 46 (TAR NC)? If yes, please elaborate.

6. General issues on the process and approach

6.1 Level of detail in the Draft Incremental Proposal

Question 33: Do you consider that the level of detail in the Draft Incremental Proposal is appropriate for EU legislation? If not, please elaborate.

Question 34: After reviewing and/or replying to the topic-related questions in Chapter 5 of this supporting document, do you find that there are other material issues that ENTSG should consider as it develops the Incremental Proposal?

Question 35: Do you find that this supporting document for the public consultation was 'respondent-friendly' in terms of its readability, style, etc.? If not, please explain how ENTSG could improve future consultation documents.

Annex 1 – Summary of topic questions

Articles 1 – 3 of CAM NC – Subject matter, Scope and Definitions

Question 1: Do you agree with the additional definitions proposed in Article 3 (CAM NC)? If not, please elaborate.

Articles 4 – 20 and 21 - 28 of CAM NC

Question 2: Do you agree with the proposed amendments and changes to Articles 4-20 and 21 to 28 (CAM NC)? If not, please elaborate.

Article 20a of CAM NC: Co-ordination requirements

Question 3: Do you agree with the level of co-ordination between TSOs and NRAs involved in an incremental or new capacity project as foreseen in Article 20a (CAM NC)? If not, please elaborate.

Question 4: Do you agree with the auction default and the alternative open season procedure as defined in Article 20a (5) (CAM NC)? If not, please elaborate.

Question 5: Do you have any additional remarks to the provisions in Article 20a (CAM NC)?

Article 20b of CAM NC: Information provision

Question 6: Do you agree with ENTSG's proposal of a demand assessment to be the basis for conducting technical studies and subsequently designing offer levels? If no, please elaborate.

Question 7: Do you agree with the scope of information to be provided to the NRA and to be published by TSOs involved in an incremental or new capacity process as foreseen in article 20b(2) (CAM NC)? If not, please elaborate.

Question 8: Do you agree with the lead-time foreseen for the publication of information relevant to an incremental or new capacity project and especially the economic test as described in article 20b (3) (CAM NC)? If not, please elaborate.

Question 9: Are there any other issues that you wish to address regarding information provision as foreseen in article 20b? If yes, please elaborate.

Article 20c of CAM NC: When to offer

Question 10: Do you agree with the conditions that shall lead to the offer of incremental and new capacity as defined in Article 20c (1), (6), and (7) (CAM NC)? If not, please elaborate.

Question 11: Do you agree that the due date approach is preferable to the time window approach as foreseen in article 20c (3) (CAM NC)? If not, please elaborate.

Question 12: Are there any other issues that you wish to address regarding conditions of when to offer incremental and new capacity as foreseen in article 20c (CAM NC)? If so, please elaborate.

Article 20d of CAM NC: Auction mechanisms

Question 13: Do you agree with the concept of parallel bidding ladders to auction incremental and new capacity as foreseen in article 20d (CAM NC)? If not, please elaborate.

Question 14: Do you agree with ENTSG's opinion that repeating the identified bidding ladder(s) represents the clearest way to allow for bid revision as foreseen in article 20d (3) (CAM NC)? If not, please elaborate.

Question 15: Do you prefer: 1) a continuous approach for bid revision as proposed by ENTSG in article 20d (3) (4); or 2) an approach according to which bid revision is only applied once? Please elaborate.

Question 16: Are there any other issues that you wish to address regarding auction mechanisms as foreseen in article 20d? (CAM NC) If yes, please elaborate.

Articles 20e, 20f, 20g of CAM NC: Open season procedures

Question 17: Do you agree with the provisions that shall lead to conducting an Open Season Procedure instead of auctions for incremental and new capacity as foreseen in article 20e (2) (CAM NC)? If not, please elaborate.

Question 18: Do you see any other conditional capacity commitments in Open Season Procedures than the issues raised in the Draft Incremental Proposal article 20f (3) (CAM NC)? If yes, please elaborate.

Question 19: Do you agree that the proposed Open Season Procedures notice contains sufficient information as foreseen in 20f (8) (CAM NC)? If not, please elaborate.

Question 20: Do you agree with the default allocation rule foreseen for Open Season Procedures, being willingness to pay per unit and year as foreseen in article 20g (3) and the alternative allocation rule subject to NRA approval as foreseen in article 20g (4) (CAM NC)? If not, please elaborate.

Question 21: Are there any other issues that you wish to address regarding Open Season Procedures

as foreseen in article 20e, article 20f and article 20g (CAM NC)? If yes, please elaborate.

Articles 42-45 of TAR NC: Economic test principles

Question 22: *Do you agree with the structure of the economic test in the Incremental Proposal as foreseen in article 42 (TAR NC)? If not, please elaborate.*

Question 23: *Do you agree with the factors that shall be taken into account when defining the f-factor as foreseen in article 43 (TAR NC)? If not, please elaborate.*

Question 24: *Do you agree with the structure of the recovery mechanisms for the share of 1-f as foreseen in article 43 (2) (TAR NC)? If not, please elaborate.*

Question 25: *Do you agree with the way the single economic test is aggregated as foreseen in article 44 (TAR NC)? If not please elaborate.*

Question 26: *Do you agree with the three approaches for a potential redistribution of revenues as described in article 44 (4) (TAR NC)? If not, please elaborate.*

Question 27: *Are there any other issues that you wish to address regarding economic test as foreseen in articles 42-45 (TAR NC)? If yes, please elaborate.*

Article 46 of TAR NC: Tariff principles

Question 28: *Do you agree with the default mechanism foreseen to adjust tariffs if required as covered in article 46 (TAR NC)? If not, please elaborate.*

Question 29: *Do you agree that in order to raise the level of commitment a downward tariff adjustment rewarding long-term booking can be included as foreseen in article 46 (TAR NC)? If not, please elaborate.*

Question 30: *Do you agree with including a possibility to adjust depreciation rates as a mechanism to avoid socialisation of costs as foreseen in article 46 (TAR NC)? If not, please elaborate.*

Question 31: *How do different tariff options impact on the markets' willingness to commit long term in order to pass the economic test? Please elaborate.*

Question 32: *Are there any other issues that you wish to address regarding tariff related issues as foreseen in article 46 (TAR NC)? If yes, please elaborate.*

Annex 2 – External stakeholders

In December 2013 organisations and companies expressed their interest in participating in the Incremental Proposal development process. Please find below a working list of stakeholders based on those expressions of interest and on actual SJWS participation.

Prime movers

<u>First name</u>	<u>Last name</u>	<u>Organisation</u>
Kees	Bouwens	OGP
Davide	Rubini	OGP
Phillip	Palada	GIE
Alex	Barnes	EFET/Gazprom Marketing
Andrey	Konoplyanik	Gazprom
Dirk Jan	Meuzelaar	IFIEC/CEFIC

Participants at SJWS and via Webcast

<u>First name</u>	<u>Last name</u>	<u>Organisation</u>
Aidan	Hogan	Gaslink
Akos	Heiter	Hungarian Energy and Public Utility Regulatory Authority
Aleksandar	Savic	Gas Connect Austria
Alessandro	Gussetti	Snam
Alex	Barnes	Gazprom Marketing & Trading Ltd.
Alexander	Kronimus	VCI/Cefic
Alexander	Yankovskiy	Gazprom
Amroze	Adjuward	EDF
Ana	Barrera	CNMC
Anais	Rossi	eni
Andrew	Pearce	BP Gas Marketing
Andrey	Konoplyanik	Gazprom export LLC; Russian State Gubkin Oil & Gas University
Andrzej	Robaszewski	Gaz-System S.A.
Angeliki	Mourtzikou	Regulatory Authority for Energy
Annick	Cable	Ofgem
Antoine	GUILLOU	CRE
Antonijo	Bolanca	CROATIAN ENERGY MARKET OPERATOR Ltd.

Antonio	Daniele	Snam
Arco	Hofman	GasTerra
Benjamin	Scholz	GASCADE Gastransport GmbH
Borek	Kubatzky	Net4Gas
Carole	Mathieu	CRE
Chris	Cuijpers	CREG
Claude	Mangin	GDF SUEZ
Colin	Hamilton	National Grid
Cor	Tuinman	Alliander N.V.
Cristiano	Francese	Trans-Adriatic Pipeline
Csilla	Bartok	ACER
Davide	Rubini	Statoil
Debra	Hawkin	Independent
Dirk Jan	Meuzelaar	CEFIC/IFIEC
Elena	Bezrodnaya	Open Grid Europe GmbH
Elisa	Kahl	ACM
Elisa	Rondella	edison spa
Emmanuel	BOUQUILLION	TIGF
Fabrice	Desjardin	GRTgaz
François	LEVEILLE	CRE
Frederick	Bernthaler	Central European Gas Hub AG
GORAN	BABIC	CROATIAN ENERGY REGULATORY AGENCY
Hein-Bert	Schurink	Energie-Nederland
Henrik	Schultz-Brunn	Thyssengas GmbH
Hilde	Vinck	Synergrid
Hugues	de Peufelhoux	GRTgaz
Ivo	Van Isterdael	Creg
Jacques	van de Worp	IFIEC Europe
Jan	Wagebach	PRISMA European Capacity Platform GmbH
JanWillem	van Dijk	Gasunie Transport Services
Jeff	Chandler	SSE
Jindrich	Mühlhofer	Ministry of Industry and Trade
Johannes	Heidelberger	BNetzA

Joppe	Onna	Stockholm University
Juan	Lopez-Vaquero	ACER
Juan	Carbayo	cepsa g.c.
Judit	Zegnal	Bruxinfo - Hungarian news agency
Kees	Bouwens	ExxonMobil / OGP
Lajos	Butosi	Magyar Gáz Tranzit ZRt.
Lauren	Skillen-Baine	Mutual Energy Limited
Laurent	Percebois	GDF Suez Infrastructures
Laurent	De Wolf	Fluxys
Lewis	Hodgart	ACER
Luca	Melis	Regas Italia
Marco	Gazzola	Snam
Margot	Loudon	Eurogas
Markus	Krug	E-Control
MAXIM	EMELIN	individual
Mirella	Subotić	Plinacro Ltd.
Monica	Immovilli	Edison SpA
Nabil	Mezlef	EDF
Niels	Krap	ONTRAS Gastransport GmbH
Nigel	Sisman	sisman energy consultancy ltd
NIKOLA	VISTICA	CROATIAN ENERGY REGULATORY AGENCY
Paloma	Izquierdo Fernández	ENAGÁS
Philipp Daniel	Palada	GIE
Renata	Drzymala	Gaz-System S.A.
Riccardo	Galletta	Florence School of Regulation
Robert	Feher	FGSZ
Robert Jan	Maaskant	TAQA Energy
Sebastian Borek	Kubatzky	NET4GAS
Simone	Rossi	eni
Stefan	Ratschko	Gasunie Deutschland Transport Services GmbH
Stephen	Rose	RWE Supply & Trading GmbH
Stephen	English	Premier Transmission Limited
Stephen	Rose	RWE Supply & Trading GmbH

Sue	Ellwood	Ellwoods Limited
Sylvie	Denoble-Mayer	GDF SUEZ Infrastructures
Thomas	Hölzer	ACER
Thomas	Querrioux	ACER
Valentin	Höhn	IFIEC Europe
Valter	Diniz	REN
Vinko	Nedelko	Energy Agency of the Republic of Slovenia
Warner	ten Kate	GasTerra B.V.
Werner	Luyts	Fluxys
Zsolt	Éles	Hungarian Gas Storage Ltd.

Annex 3: Relation to the previously published Business Rules

As an intermediate step in the development of the Draft incremental Proposal a set of Business Rules (INC00148-14) were developed and published. The Draft Incremental Proposal is a further refinement of these Business Rules. When merging the Draft Incremental Proposal with the existing CAM NC, the numbering of topics/subject in the business Rules had to be adjusted accordingly. The table below explains the correspondence between the chapters of the Draft Incremental Proposal and the chapters of the Business rules:

Content	Business rules	Draft Incremental Proposal
Scope and definitions	III	Art. 2
General Co-Ordination Requirements	Chapter IV, BR 1.1 -1.6.	Art. 20a CAM NC
Information Provision	Chapter IV, BR 2.1. - 2.8.	Art. 20b CAM NC
Conditions for when to offer incremental and or new capacity	Chapter IV, BR 3.1. - 3.7.	Art. 20c CAM NC
Auction mechanisms	Chapter IV, BR 4.1-4.4.	Art. 20d CAM NC
Open Season Procedures	Chapter IV, BR 5.1 – 8.6	Art. 20e-g CAM NC
Economic Test principles	Chapter IV, BR 9.1 – 12.3.	Art. 42-45 TAR NC
Tariff issues	Chapter IV, BR 13.1- 13.6.	Art. 46 TAR NC