ENTSOG: 1st Stakeholder Joint Working Session for the Incremental Proposal
10 February 2014

1st SJWS for the Incremental Proposal

10 February 2014

Mark Wiekens

Advisor, Market Area

Welcome - Objectives

- Welcome to the 1st SJWS for the Incremental Proposal
- Objectives for today
  - Exploration of the first group of topics: Cross-Border and Information Provision, Economic Test & Tariff-related issues
- Build on Kick Off Meeting 14 January
  - ACER presentation on Guidance
  - EC provided the broader context for the Incremental Proposal
  - Stakeholders provided views on the various topics
  - Engaged discussions, constructive dialogue – in overall, a good basis for the upcoming SJWS and beyond

Agenda for today

Nr	Session	Time
	Welcome Coffee	10:00-10:30
1	ENTSOG opening and introduction	10:30-10:40
2	Results of project plan consultation	10:40-11:00
3	ACER outline of expectations ➢ Cross-border co-ordination and information provision ➢ Economic test and tariff issues	11:00-11:20
4	Cross-Border co-ordination and information provision ➢ ENTSOG outline of concepts ➢ View of stakeholders /open discussion	11:20-12:30
	Lunch Break	12:30-13:30
5	Economic test ➢ ENTSOG outline of concepts ➢ View of stakeholders /open discussion	13:30-15:00
	Coffee Break	15:00-15:15
6	Tariff issues ➢ ENTSOG outline of concepts ➢ View of stakeholders /open discussion	15:15-16:30
7	Conclusions of SJWS 1	16:30-16:45

Housekeeping – general information

- Fire escape
- Attention to the wires
- Webcast – questions via mail possible before and during the webcast
- The SJWS discussions (including webcast) are reserved for the stakeholders, but notes and presentations will be available for the press and the public shortly after the meeting

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Conclusions of the Project Plan for the Incremental Proposal

10 February 2014

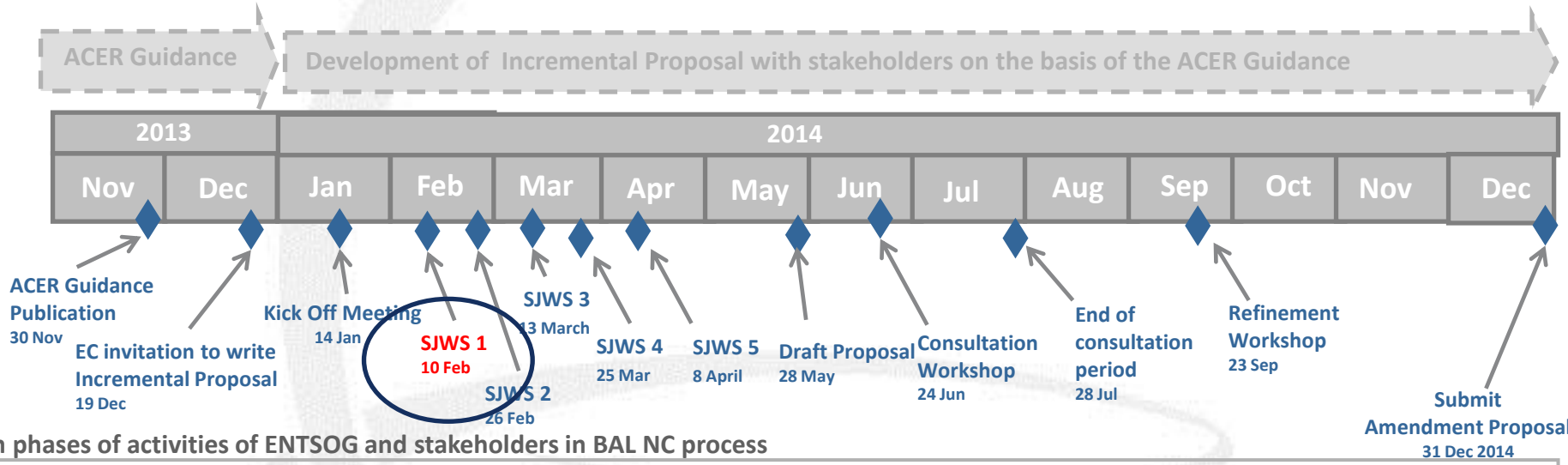
Frederik Thure

Market Area

Agenda

- ENTSOG timeline overview – state of play
- Respondents
- Project plan conclusions
- Participation by level
- Themes to be developed in the Incremental Proposal

Timeline for incremental proposal Development and consultation overview



Main phases of activities of ENTSOG and stakeholders in BAL NC process

ENTSOG	Development of launch documentation and Project Plan		Development of draft Incremental Proposal in cooperation with stakeholders						Refinement of Incremental Proposal based on the feedback by stakeholders				
Stakeholders		Kick-off Meeting	SJWS 1	SJWS 2	SJWS 3	SJWS 4	SJWS 5	Consultation period			Refinement Workshop		SSP

SJWS 1
- Coordination Requirements
- Information Provision
- Economic Test
- Tariff-relaed issues

SJWS 2
- When to Offer
- Auctions
- Open Seasons Procedures

SJWS 3
- Coordination Requirements
- Information Provision
- Economic Test
- Tariff-relaed issues

SJWS 4
- When to Offer
- Auctions
- Open Seasons Procedures

SJWS 5
- Content to be confirmed

Incremental proposal development – from identification to draft text

- Topic identified from Guidance
- Topic introduced in "Launch Documentation" and at Kick Off Meeting

- Topic presentation at SJWS 1 & 2
- No policy options ruled out at this step
- Stakeholder input

- Business rules formulated based on stakeholder feedback on SJWS 3 & 4
- No policy options ruled out at this step
- Stakeholder input received

- Topic revisited at future SJWS
- Business rules refined

- Business rules transposed into draft Incremental Proposal text

- Texts consolidated into draft Incremental Proposal for consultation

Main conclusions from Project Plan

- Participation from a wide range of the industry
- Broad agreement on the identified topics, but..
- …also suggestions recieved on how to optimise the process
- Total stakeholder participation
  - 23 respondents for the draft PP
- Prime mover:
  - 5 prime movers for the Incremental Proposal

Prime movers: 5

Participant	Organisation and/or company	Name(s)
1	OGP	Kees Bouwens
2	OGP	Davide Rubini
3	Gas Infrastructure Europe (GIE)	Philipp Palada
4	EFET/Gazprom Marketing and Trading	Alex Barnes
5	Ifiec / Cefic	Dirk Jan Meuzelaar

Active SJWS participants: 13

Participant	Organisation and/or company	Name(s)
1	Gazprom Export	Andrey Konoplyanik (Co-chair of GAC WS 2, Prime Mover for New Capacity issues)
2	EDF	Amroze Adjuward
3	Eni	Simone Rossi
4	Centrica	Helen Stack
5	Eurogas	Margot Loudon
6	BP Gas Marketing	Andrew Pierce
7	Edison SpA	Elisa Rondella
8	GDF SUEZ	Jean-Louis Martinaud
9	Trans-Adriatic Pipeline	Cristiano Francese
10	GDF SUEZ Infrastructures	Sylvie Denoble-Mayer
11	German Chemical Industry Association	Alexander Kronimus
12	IFIEC Europe	Valentin Höhn
13	EFET	Maria Popova

Consultation respondents / observers

Participant	Organisation and/or company	Name(s)
1	Eurelectric	Sébastien Doligé
2	GasTerra B.V.	Ivelina Boneva
3	Gazprom Marketing & Trading	Francisco Goncalves
4	AGGM Austrian Gas Grid Management AG	Eric Gilhaus
5	EDF Trading	Andrea Bonzanni
6	RWE Supply & Trading GmbH	Steve Rose (observer)

Project plan for the Incremental Proposal

Question 2 : In your opinion, does the draft project plan for the development of an Incremental Proposal contained in this document provide sufficient basis for quality stakeholder involvement given the timelines within which this project must be delivered? If the response is no, please propose some improvements for consideration.	
Yes	22
No	0
No answer	1

- Broad support for the project plan

" […] the project plan provides a reasonably good basis for a quality stakeholder involvement."

"We appreciate ENTSOG's efforts to develop a project plan that allows stakeholders to be fully involved in the process of elaboration of the incremental proposal."

Timeline for Incremental Proposal

Question 3: What do you think of the proposed timeline, including frequency and number of meetings? Are any changes needed?	
Yes	22
No	0
No answer	1

- Broad support for the proposed timeline

" […] We would like to underline the importance of giving to stakeholders enough time to respond to written consultations; this is really necessary for associations with a large membership. Workshops and meetings are as important as written answers."

" The timeline is tight, but should be achievable. The number of meetings seems appropriate."

Topics and suggestions

Question 4: What do you think of the proposed topics for the Incremental Proposal? What other topics might be included (Qualitative answer)

- Agreement on the topics proposed – but some suggestions to how ENTSOG should run the process:

" […] We believe the list of topics is fine. We would like to ask ENTSOG to ***publish well in advance the preparatory documents*** *that need to be read before the workshops take place."*

"Special focus should be done on the ***"f factor"*** *(f & 1-f) and the determination of its parameters, because of its major importance in the economic test."*

" […] would like a clear discussion and assessment about the different options for auctions and open seasons that have been proposed in ***CEER's Blueprint for Incremental Capacity****."*

"During the process it is important to provide ***concrete simulations and examples*** *on how the incremental mechanisms work."*

" We agree with the proposed topics, provided that they are looked at in the context of the ***Gas Target Model*** *and the implementation of the various* ***Network Codes****."*

Stakeholder process requests

" […]publish well in advance the preparatory documents"	ENTSOG will update its external website with the pre-reading material in due time
"Special focus should be done on the "f factor "	The "f factor" will be adressed in the topic Economic Test (SJWS1 10 Feb & SJWS 3 13 March)
"[…]provide concrete simulations and examples on how the incremental mechanisms work."	An auction simulation is planned for SJWS 4 (Tue 25 March)
"[…] ENTSOG might consider requiring parties to register for the streaming sessions […]"	All webcast participants are registered
"[…] the importance of giving to stakeholders enough time to respond to written consultations"	Consultation period equal to full network code process

Topics identified

Issues to consider in the SJWS according to some respondents

Gas Target Model

CEER blueprint for inc. capacity

Impact Assessment by Frontier (Requested by ACER)

Implementation of Network Codes

Issue/topic areas

ACER GUIDANCE

Open Season

Crossborder co-ordination

Information provision

Auctions

When to offer

Tariff-related issues

Economic Test

INCREMENTAL PROPOSAL

Deliverables

Amendment proposal → **CAM Network Code**

ET & Tariff-related issues → **TAR Network Code**

Webcast

Question 5 (a+b): Do you think it would be a good idea to establish livestreaming of the SJWS?	
Yes	22
No	0
No answer	1

- Overwhelming support for webcast
- But more viewers are sought for.. Please spread the word that SJWS are being webstreamed in high quality by a professional team
- Preference to register on the day itself, but registration on the day itself is possible
- Questions regarding webcast, please contact Alexandra at alexandra.kiss@entsog.eu

Any questions or comments?

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ACER
Agency for the Cooperation of Energy Regulators

ACER Guidance on Incremental

Cross-border coordination and information provision

Economic test and tariff issues

Carole MATHIEU – CRE
François LEVEILLE – CRE

ENTSOG workshop
11 February 2014

ACER Guidance – rationale

- ACER guidance on incremental and new capacity aims at developing harmonized approaches to market-based procedures
- Objective: spelling out general obligations from Reg 715/2009 and Dir 2009/73 for market testing and investment; addressing cross-border co-ordination issues
- Thereby striking the balance between network user requirements and economic feasibility, while minimising stranded asset risk

Cross-border coordination and information provision

- Background:
  - Previous monitoring exercises showing that the **GGPOS principles** on coordination and transparency had often been neglected;
  - Requirement of the CAM network code to offer incremental/new capacity in the form of **bundled products.**

  ➔ Need to develop **binding rules** on these aspects

- ENTSOG's tasks:
  - outline the overall process and **which coordination results** should be reached **at what stage ;**
  - define the **information provisions** that should be exchanged between involved parties (TSOs, NRAs, network users)

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List of issues on which adjacent TSOs and NRAs need to agree

Issues	Objectives
Timelines for the project	Same commissioning dates
Delays	Anticipate how delays would be dealt with / their effects could be mitigated
Capacity offer	Consistent volumes and characteristics of the bundled product components
Procedure for securing network users' binding commitments	Single procedure enabling the offer of bundled products
Combination of the investment requirements in a single economic test	Decision-making process made clearer to network users
Interaction with network users / point of contact	TSOs to provide simultaneous/common information provision

Cross-border coordination for projects along a route

- ACER sees a potential need for additional coordination requirements for TSOs/NRAs involved in projects spanning across several IPs

- ENTSOG invited to assess further this question and eventually come up with a proposal

Information provision

- ACER provided a **non-exhaustive list of information items** to be exchanged by TSOs/NRAs involved
  - Capacity volume and terms and conditions
  - Design of the allocation mechanism
  - Investment requirement (level of NUs' commitments required)
  - Applicable tariff and methodology
  - Envisaged timeline of the process

- Once approved by the NRAs, **information to be published** by the TSOs with a sufficient lead time

  ➔ Network users able to make **informed bids**

Tariff issues

- Background:
  - Feedback from previous capacity developments showing that investment decision processes across EU were too diverse and not transparent enough;
  - This situation was generating uncertainty for the stakeholders.
  - ➔ **A harmonized decision tool** was needed for the NRAs to decide whether or not an investment decision is relevant.

- This decision tool is the economic test:
  - Testing a theoretical financial viability of a project looked at in isolation even though, in any case, the investment would be incorporated in the TSOs' RAB at the end of the process

Tariff issues, general principles

- In market based capacity development, investment is validated when user commitments (i.e. long term bookings) allow to cover the costs
  - **Principle**: determine a financial threshold to trigger investment decisions
  - **Objective**: showing that the investment project is financially viable considering network users' binding commitments
- Principle of an "economic test":
  - Bookings*tariffs are compared to the costs
  - Main variables: offered capacity (volume and duration) and tariff level

Economic Test for Investment decision

- A **harmonised test based on a financial evaluation** comparing:
  - **PV_{UC}** which is the present value of expected users' commitments and
  - **PV_{AR}** which is the present value of the estimated potential increase in allowed revenue;
  - **f:** single cost coverage level.
- PV_{UC} shall reach a certain fraction f of the PV_{AR} ;
- The formula:

$$\boldsymbol{PV_{UC} \geq f \bullet PV_{AR}}, \; f \leq 1$$

The level of cost coverage ('f')

- The minimum level of cost coverage (f) shall take into account:
  - Duration of users' commitments compared to the economic life of the asset;
  - Capacity set aside for short term bookings;
  - Externalities (improvement of competition, security of supply, etc.)
- Cost sharing agreements and external financial support should be included in the economic test (modification of expected cash flows, reduction of PV_{AR}).

Interaction between the economic test and tariffs (1/2)

- By default, the reference (annual) price resulting from the application of the **cost allocation methodology** applies to incremental capacity.

- In the specific case **where selling all the incremental capacity at this price would not generate sufficient revenues** to pass the economic test, NRAs may adjust the reserve price.

- This tariff adjustment shall :
  - preserve the **integrity of the economic test**
  - **avoid cross-subsidy** between network users
  - be **compatible with the cost allocation** methodology
  - **avoid fragmentation** of reserve prices at the same point

Interaction between the economic test and tariffs (2/2)

- Considering those principles, **the default adjustment mechanism should be to apply a minimum mandatory premium** in the first auction in which incremental capacity is offered (i.e. only to the bookings triggering the investment).

- Consistently with the same principles, **ENTSOG shall consider alternatives approaches** where users who did not commit in the first place but benefit from the investment would also bear a part of the costs.

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Thank you for your attention!

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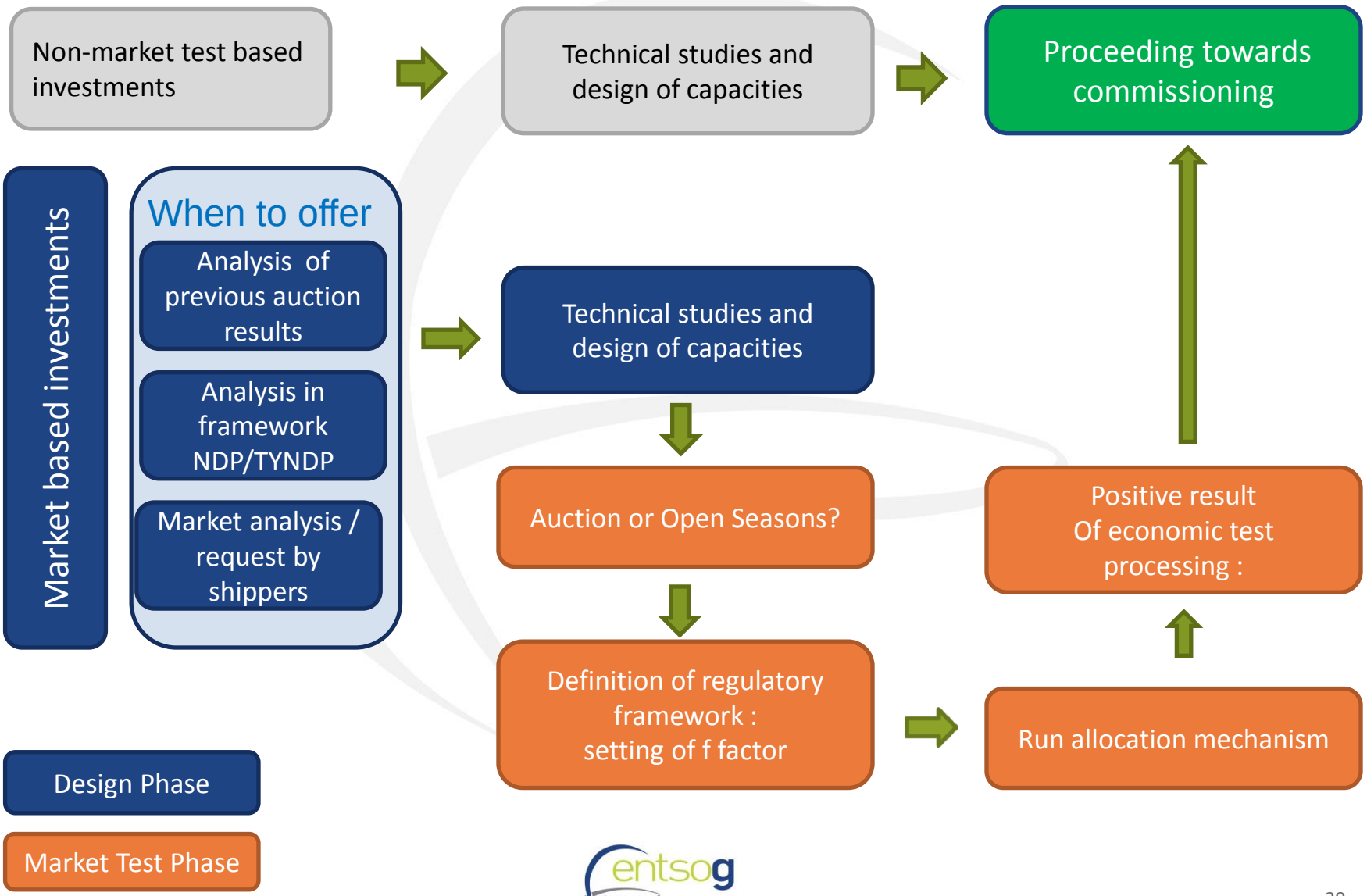
1st SJWS Incremental Proposal

Cross Border Co-Ordination and Information Provision

Agenda

1. **High level process description**
2. Cross-Border Co-Ordination requirements
3. Information Provision requirements

High level process diagram



Agenda

1. High level process description
2. **Cross-Border Co-Ordination requirements**
3. Information Provision requirements

Co-ordination requirements

- Intensive co-operation and co-ordination among TSOs and with the respective NRAs is necessary to enable offer of incremental/new capacity
- Minimum co-ordination requirements shall be included in the amended NC CAM to be undertaken in all incremental/new capacity projects
- ACER Guidance is requesting an integrated offer of incremental/new capacity together with existing capacity as **bundled products** according to the existing NC CAM
- Bundling of incremental/new capacity products ensures high degree of co-ordination in terms of:
  - Commissioning dates
  - Level of increment
  - Commitment horizons
  - Etc…

Design Phase

Objective

- Assessing technical details and capacity design of incremental/new capacity project

Milestones

- Starting with the assessment of the ‘When to offer’ conditions and the decision on whether to offer incremental/new capacity
- In case of positive decision by TSOs and NRAs, co-ordinated project planning for incremental/new capacity project including different offer levels is undertaken by involved TSOs
- Planning for each scenario includes estimation of respective costs, timeframes for construction, legal and administrative processes

Time requirement

- Usually one year or more, depending on the scale and complexity of a project
- Interaction with yearly auctions and development of TYNDP/NDP influences starting point and time requirements for design phase

Interaction with conditions for when to offer

- Design phase starts when non-binding indication, TYNDP/NDP and auctions in combination identify a sustained demand for incremental/new capacity
- Along the process, some TSOs may be obliged to include investment projects in their national NDPs before an investment decision is taken
- In order to give more certainty to network users on the economic test result, there must be consistency between the incremental process and NDP/TYNDP processes

Market test phase

Objective

- Preparing and holding the economic test for an investment project

Milestones

- Decision on allocation mechanism (auction or OSP) once design phase of offer scenarios is completed
- Agreement on economic test parameters (f-factor, tariff, PVAR, guarantee for 1-f,…) with respective NRA and combination into single economic test
- Holding of auction or binding phase of OSP and run of the economic test

Time requirement

- Discussions with NRAs and TSOs involved on economic test parameters and possibly a redistribution of revenues can be long lasting
- Time required for market test phase dependent on characteristics of project (based on TSO experiences 6 months is a minimum time frame)

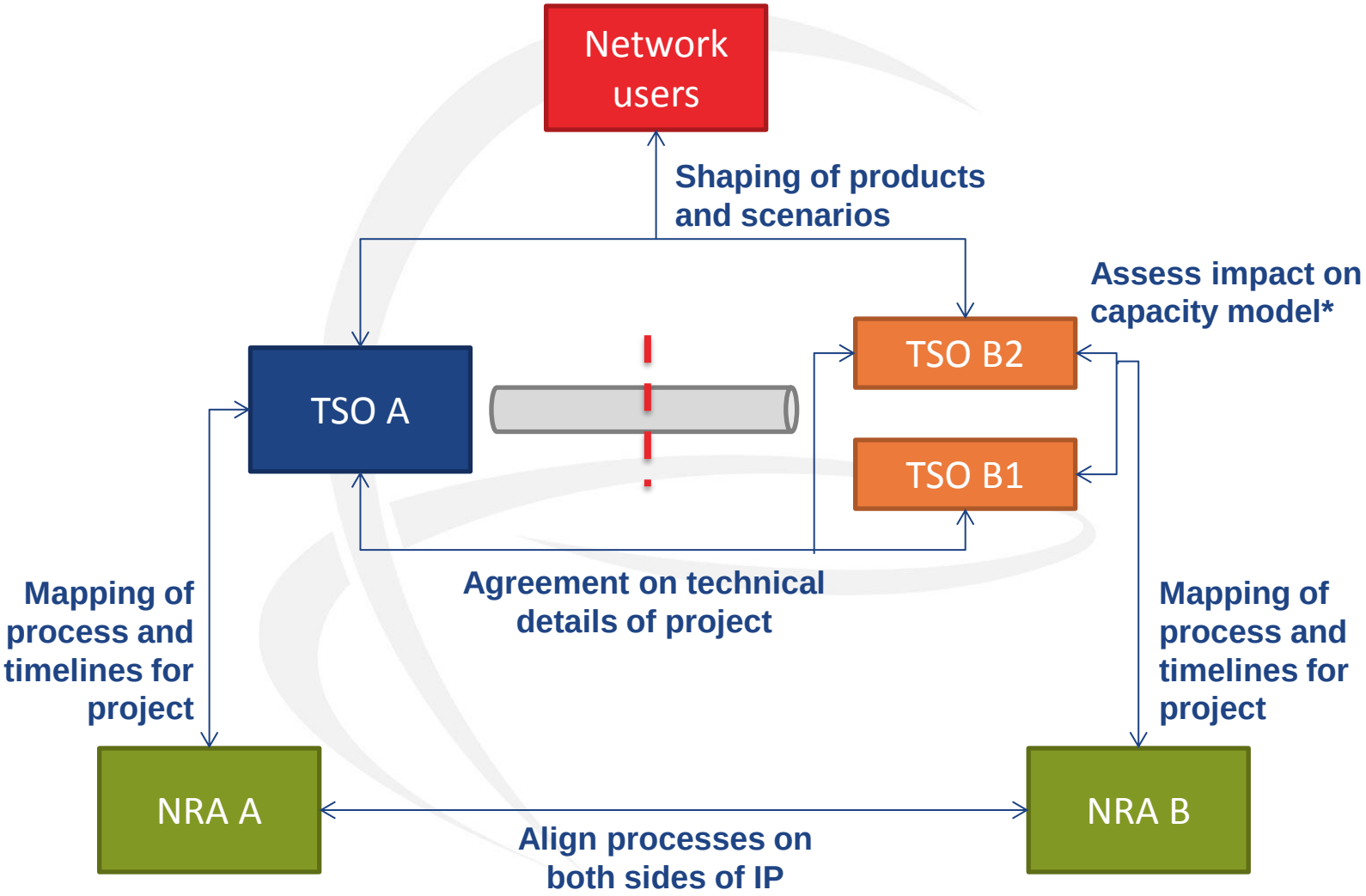
Co-ordination : additional take-aways

- The breakdown into design phase and market test phase is not a plain line
  - There may be some overlap between the two phases
  - In case of iterative exchanges, looping can happen, with way back to elements of design phase
- The marketing of bundled capacity at CAM IPs guarantees network user full coordination is reached
  - Bundled capacity implies automaticaly full commercial coordination
  - No possible mismatch in volumes across the border
  - No possible concerns due to discrepancy in commissioning of capacity

Agenda

1. High level process description
2. Cross-Border Co-Ordination requirements
3. **Information Provision requirements**

Overview of goals in design phase



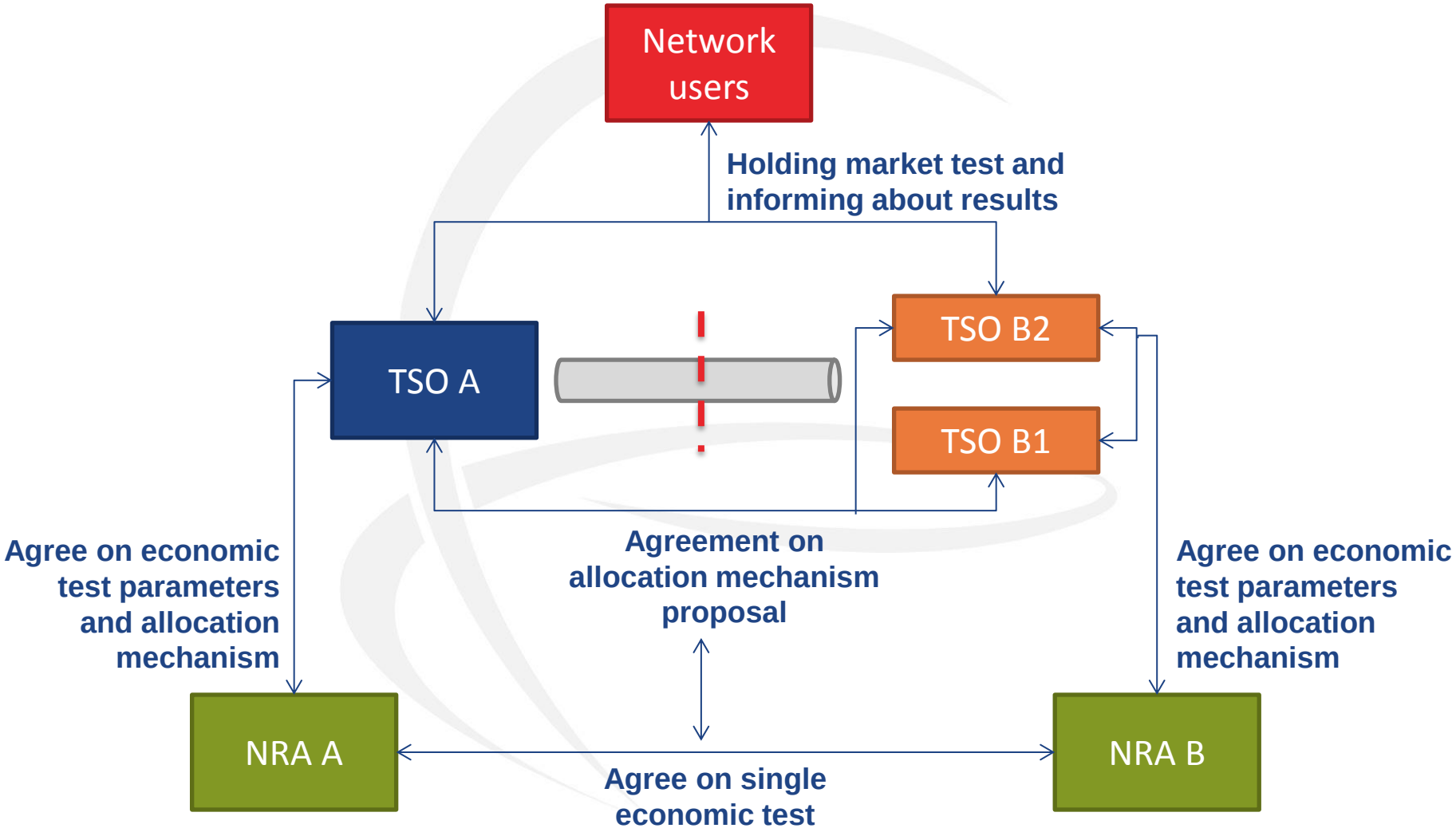
Information exchange in design phase 1/2

Provider	Recipient	Information	Goal
Network Users	TSO	➢ Potentially non-binding indication for demand starting the process	**Start process for offering incremental/new capacity**
TSO	Adjacent TSO (across IP)	➢ Information exchange embedded in ongoing co-ordination between TSOs involved for designed a project ➢ Individual plans for technical parameters, timelines, mitigation procedures and bundling procedures	**Adjustment of parameters towards a common project**
TSO	TSOs in the same market area (if any)	➢ Parameters of project that have an impact on the market area (e.g. on the capacity calculation model) ➢ If IP is shared on one side of the border, mutual agreements on investment project have to be found	**Assess impact on capacity model in market area (if relevant)**

Information exchange in design phase 2/2

Provider	Recipient	Information	Goal
TSO	NRA (and possibly other authorities)	➢ Details of incremental/new capacity scenarios as assessed by TSO (costs, timeframes, etc.) ➢ Initiating of national approval process for investment	**Mapping of process, timelines and procedures for construction from a regulatory perspective**
NRA (and possibly other authorities)	TSO	➢ Cost recognition for investment project ➢ Early assessment of tariff and revenue allowance due to investment project	
NRA	NRA responsible across IP	➢ Alignment of timelines, rules and possibly initial discussions on cross IP or cross TSO cost compensation, if relevant ➢ Assessment of externalities	**Align processes at both sides of the border**
TSO	Network Users	➢ Preliminary information on levels of incremental/new capacity offer scenarios and specific on capacity products (quality, firmness, bundling, etc.) ➢ Indicative timelines for realisation of investment project ➢ Information exchange could also beintegrated into market test phase (provision of economic test parameters)	**Shape products and quantity based on market needs**

Overview of goals in market test phase



Information exchange in market test phase 1/2

Provider	Recipient	Information	Goal
TSO	TSO across IP	➢ Agreement on allocation mechanism ➢ Agreement on common points of project	**Agree on allocation mechanism proposal**
TSO	NRA	➢ Proposal for economic test parameters ➢ Proposal for allocation mechanism to be used ➢ Proposal for contractual framework for bundling	**Agreement on (single) economic test**
NRA	NRA (across IP)	➢ Agreement on single economic test ➢ Agreement on possible redistribution of revenues	
NRA	TSO	➢ Approval of economic test parameters ➢ Approval of allocation mechanism ➢ Approval of contractual framework for bundling	
TSO	Network Users	➢ Capacity allocation mechanism used and timing for incremental/new capacity project ➢ Parameters of the economic test and basis for calculation ➢ After allocation: results of economic test and capacity allocated to individual network user	**Inform about economic test parameters and results**
Network Users	TSO	➢ Commitment to incremental/new capacity project (via auction or OSP)	**Commit for the investment**

Information exchange in market test phase 2/2

Information about economic test and allocation results:

- Network users should be informed **as early as possible** about their individual results of the allocation procedure
- For **auctions**, aggregated information about the allocation procedure results shall be published **no later than 24 hours** after informing network users about their individual results
- For **OSP**, aggregated information about the allocation procedure results shall be published **as soon as possible** after informing network users about their individual results
- Aggregated information to be published are:
  - Accepted bid price per year (in an auction)
  - Aggregated volume allocated per year
  - Number of network users participating successfully in auction or OSP
  - Number of network users participating unsuccessfully in auction or OSP

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Economic Test

January 2014

Agenda

1. **Economic Test formula**
2. Setting of f-factor
3. Coverage of 1-f
4. Publication requirements
5. Single Economic Test

Economic Test formula

PVUC ≥ f * PVAR

Present Value of User Commitment

$$= \sum_{y=x}^{y=z} \frac{(Tariff_y + Premium_y) * UC_y}{(1+d)^y}$$

Tariff(y)	Tariff per year
Premium(y)	Premium per year, if any*
UC(y)	Level of User Commitment
d	Discount rate for future cash flows
x	First year of incremental capacity on offer
z	Last year of booking horizon

*The offer scenarios for incremental/new capacity should be designed in a way to avoid scarcity and thus premiums in the auctions.

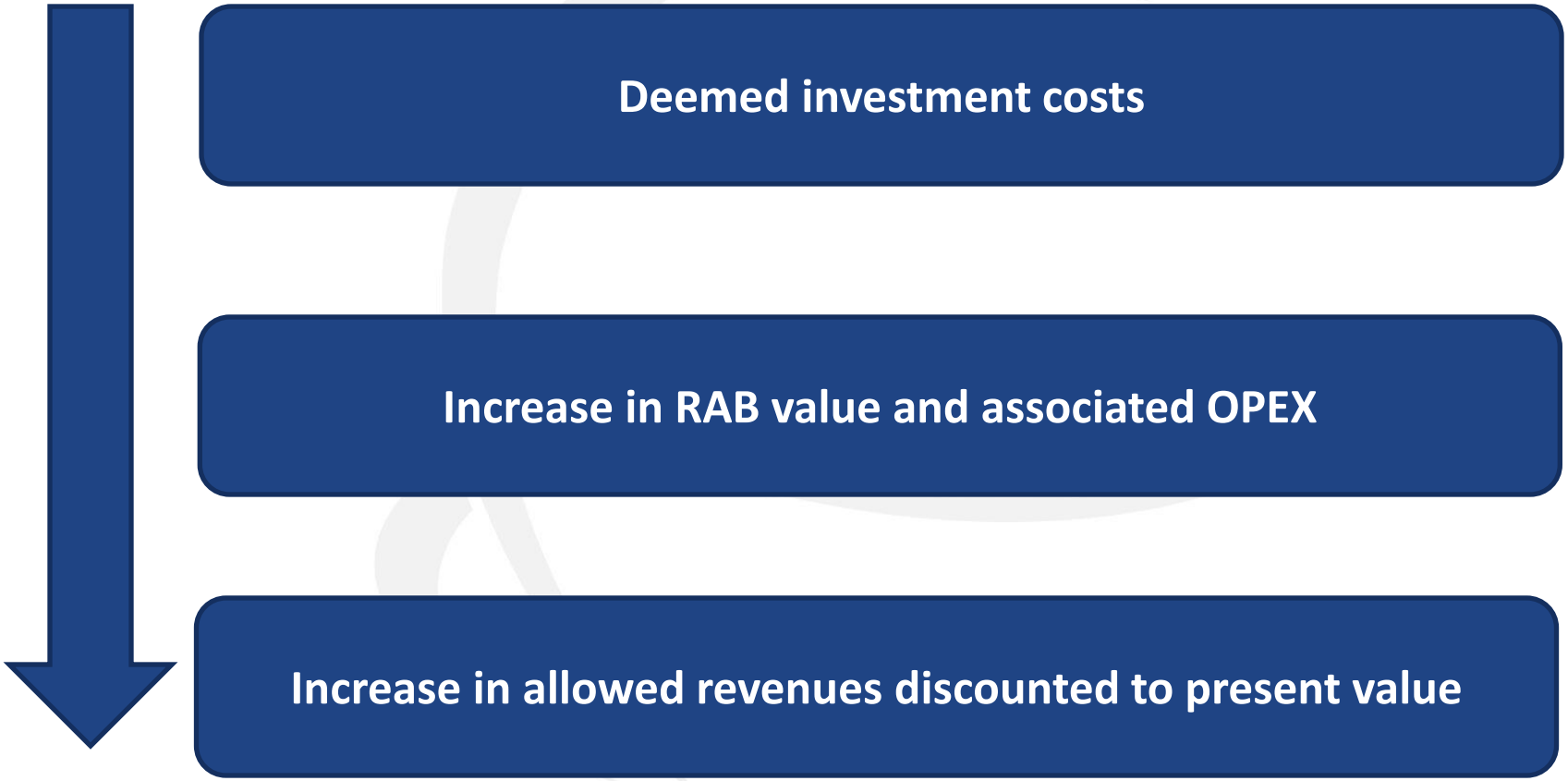
Present Value of Allowed Revenues*

$$= \sum_{y=o}^{y=l} \frac{RAB_y * RoR_y + Dep_y + OPEX_y}{(1+d)^y}$$

RAB(y)	Increase in regulated asset base
RoR(y)	Regulated rate of return on investment
Dep(y)	Depreciation of investment
OPEX(y)	Operational expenditures induced by investment
d	Discount rate for future cash flows
l	Economic lifetime of investment

*PV of allowed revenues could be replaced by PV of regulated revenues

From DIC to PVAR



Agenda

1. Economic Test formula
2. **Setting of f-factor**
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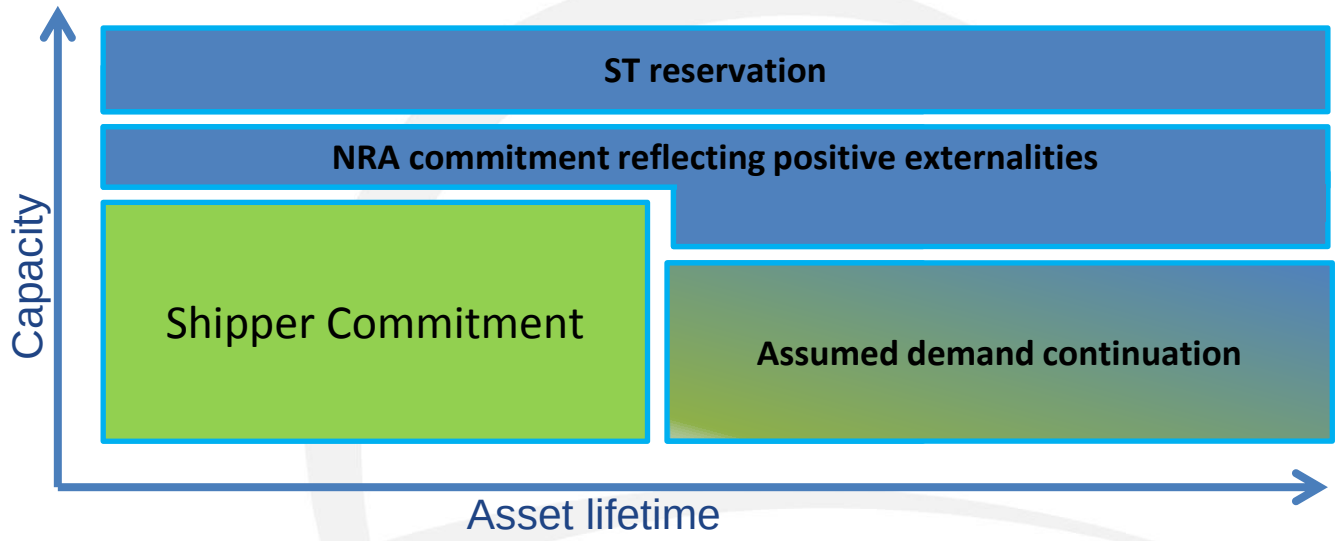
Factors influencing level of f-factor 1/2



Market underwritten part of investment for which investment recovery is guaranteed by market

Regulatory underwritten part of investment for which investment recovery is guaranteed by NRA

Factors influencing level of f-factor 2/2

Factor	Description	Effect on Economic Test
Short-term reservation quota	In case ST reservation quotas must be applied to incremental/new capacity as well, a lower amount of capacity on offer in long-term auction has to cover the defined share of PVAR.	Potentially an obstacle to passing the economic test, e.g. in transit countries or price cap regimes.
Positive externalities induced by investment	Comparison of current costs of network users and future costs of network users induced by an investment, aside of the incremental/new capacity itself. E.g. effects on wholesale prices due to a new or increased connection to an adjacent market.	Beneficiary of positive externalities (e.g. the market as such) is not necessarily the sponsor of an investment – flow of revenue therefore unclear.
Assumed demand continuation	Assessment of continuation of demand for incremental/new capacity based on long-term forecast of gas flows	Reliability of assessment influences share of PVAR that needs to be covered upfront.

Agenda

1. Economic Test formula
2. Setting of f-factor
3. **Coverage of 1-f**
4. Publication requirements
5. Single Economic Test

Present Value of Non-User Commitments

PVAR = f * PVAR + (1-f) * PVAR

Covered by User Commitments

Guaranteed by NRA

Share of PVAR, that is not covered by upfront User Commitments (PVNC)

The proportion of PVAR (including, subject to any regulatory efficiency assessment, any PVAR 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.

Revenue-Cap Regulatory Regimes	Price-Cap Regulatory Regimes
As PVNC is included in the regulatory asset base of the TSO, revenues on investment are guaranteed through regulatory system. Costs of investments will therefore be covered by future user payments at all points of the system.	Revenues on an investment are not sufficiently guaranteed in price cap regimes as revenue recovery is depending on future bookings of incremental/new capacity. Other mechanisms have to be found.

Agenda

1. Economic Test formula
2. Setting of f-factor
3. Coverage of 1-f
4. **Publication requirements**
5. Single Economic Test

Publication requirements

Economic test parameters to be published beforehand:

1. PVAR:
Present value of estimated increase in allowed revenues of a TSO during economic lifetime of new asset.

2. f-Factor (and calculation basis):
The share of PVAR that needs to be underwritten by network user commitments in order to pass the economic test.

3. Estimated tariffs (and calculation basis):
Estimation of projective tariff at respective IP(s) and information on the calculation model used to make the estimation.

ENTSOG proposes a lead-time for publication of **one month** before the capacity allocation procedure

Agenda

1. Economic Test formula
2. Setting of f-factor
3. Coverage of 1-f
4. Publication requirements
5. **Single Economic Test**

General principle of single economic test

- Principally, investment projects should be designed in a way that each investment party is able to cover its costs individually;
- A single economic test thus needs to reflect the requirements of all involved parties;
- For a bundled product, the minimum level of user commitment to pass the single economic test is therefore the lowest minimum level of user commitment to pass the individual economic tests on both sides;
- The f-factor of the single economic test is only a mathematical calculation based on combined PVAR, bundled tariff split and the minimum level of user commitment. It has no meaning in itself;
- If all involved parties agree, a redistribution of revenues can be explored to decrease the minimum level of user commitment needed to pass the single economic test.

Single Economic Test

Single Economic Test needs to reflect a **minimum level of user commitment** that allows all involved TSOs to cover the share of their PVAR associated with their investment.

Investment at TSO A	
Level of Increment	100 capacity units
PVAR	300 EUR
f Factor	0.5
Tariff	2.50 EUR
Required level of UC	**60 capacity units**

Investment at TSO B	
Level of Increment	100 capacity units
PVAR	375 EUR
f Factor	0.75
Tariff	4 EUR
Required level of UC	**70 capacity units**

Minimum level of UC to pass Single Economic Test is therefore 70 capacity units

Aggregated f-factor as a mathematical calculation based on combined PVAR, Tariffs and minimum level of UC

Single Economic Test for A and B	
Required level of UC	70 capacity units
Tariff	6.50 EUR
f Factor	**0.677**

f-Factor is only a mathematical calculation and can theoretically be higher than the two individual f-factors

Minimum level of User Commitment

The Single Economic Test identifies three different sections of user commitment levels:

Economic Test Result	10	20	30	40	50	60	70	80	90	100
TSO A										
TSO B										
Single Economic Test										

1. A section where the individual Economic Tests at both sides of the IP are not passed (level <60 in the example);
2. A section where the individual Economic Test is passed at one side of the IP but not on the other side of the IP (level 60-70 in the example);
3. A section where the individual Economic Tests are passed on both sides of the IP, and therefore also the Single Economic Test is passed (level >70).

Section 3 – the only section where the Single Economic Test is passed – can potentially be increased by a redistribution of revenues for the investment…

Considerations for redistribution of revenues

A redistribution of revenues for an investment can potentially increase the chances of passing the economic test.

Two possible mechanisms to be considered are:

1. A cost-sharing agreement between the TSOs (or other sponsors) involved in the project to credit one of the parties;

2. A different split of the reserve price to be charged at the respective IP for bundled capacity products.

ENTSOG position:

- The default procedure should be that investment projects are designed in a way that allows all involved parties to cover their costs individually, without the need for cost-sharing;

- The decision on when to consider a redistribution of revenues and which mechanism to use should be left to the respective TSOs and NRAs involved based on a case by case assessment.

Considerations for redistribution of revenues

ENTSOG provides three different approaches for structuring the process of agreeing on a potential redistribution of revenues – for discussion with stakeholders:

Approach	Description	Advantage	Disadvantage
Ex-ante approach	Assessment of potential redistribution of revenues once the individual economic tests are defined but before parameters of single economic test are published	➢ More certainty for network users on parameters of the economic test	➢ Potentially unnecessary delays due to long-lasting revenue discussions
Ex-post approach	Assessment of potential redistribution of revenues only once a single economic test based on the highest minimum level of user commitment is negative	➢ Resources and time for assessment only used if really necessary	➢ Final outcome of economic test could be delayed due to assessment
Integrated and iterative approach	Assessment of potential redistribution of revenues integrated into the design and the binding phase of an open season, thus open season could be chosen in case redistribution of revenues is expected to be necessary	➢ Efficient combination in which recourses and time are used rationally	➢ Requires full immersion of network users throughout the whole process ➢ Transparent for insiders, but less for outsides

1st SJWS for Incremental Proposal

Tariff Issues

January 2014

Agenda

1. **Tariff calculation for incremental/new capacity**
2. Tariff adjustment

Tariff for incremental/new capacity

How to calculate the tariff at which network users can request incremental/new capacity?

Tariff FG: "…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."

Which tariff to use for the calculation of PVUC in the economic test?

Tariff FG: "…An estimated projection of tariffs for the bundled yearly capacity products of the capacity expansion(s) considered…"

Due to floating tariffs, no tariff is specified in an auction or in the binding phase of an open season. The tariff used for the calculation of the economic test can be different from the tariff invoiced at the time of usage.

How to determine tariff used to calculate PVUC?

- Due to floating tariffs, the tariff used for the initial allocation of incremental /new capacity will be different to the tariff used in future years, when incremental/new capacity will be commissioned.

- For the calculation of PVUC, two approaches are proposed for discussion by ENTSOG:

Approach for tariff to use for calculation of PVUC	Considerations of approaches
1. To define a standardised approach for tariff projection in a network code applicable to all incremental/new projects	➢ Clear and predictable process ➢ Potentially low quality of projection due to lack of flexibility for specific circumstances ➢ Under-recovery in case of lower actual tariffs at time of usage (included in 1-f)
2. Case by case process for the estimation of future tariffs to be applied by the individual TSOs subject to NRA approval	➢ More flexibility but less defined process ➢ NRA approval implicitly guarantees under-recovery in case of lower actual tariffs

Approaches for tariff determination in incremental/new capacity process

Possible approaches for determining a tariff for the calculation of PVUC are:

Approach	Description
Assumption of stable reference price	To apply the reference price for the respective IP at the time of the initial offer of incremental capacity for all years of the booking horizon assuming a stable tariff
Assumption of "as-if" reference price	To calculate a reference price for the respective IP based on the framework of the year of the initial offer of incremental capacity under the assumption that the investment (and associated increase in RAB and OPEX) is already in place for that year and assuming a stable tariff
Estimation of reference price development	To calculate reference prices for each year of the booking horizon based on the estimated cost and revenue structure, taking into account the cash flows associated with an investment in the respective years

Which approach is most appropriate depends among others on size and complexity of a project! Therefore prescription of a harmonised approach might not be constructive

Considerations for alternatives

Fixed tariffs for incremental/new capacity in order to avoid differences in tariff application and a potential under-recovery for an investment

Consequences could be:

- Higher willingness of network users to commit for a long period of time thus increasing the chances of passing an economic test
- Cross-subsidisation with other points if investment costs increase and no other mechanism for revenue recovery is available
- Application of different tariffs for the same product at the same IP
- Way of allocating incremental/new capacity together with existing capacity at different tariffs needs further elaboration

Stakeholder views?

Agenda

1. Tariff calculation for incremental/new capacity

2. **Tariff adjustment**

Precondition for tariff adjustment

An adjustment of tariffs for incremental/new capacity should be considered when selling all incremental/new capacity would not generate sufficient revenue to pass the economic test

- Each economic test scenario should be designed in a way that the test can be passed if all incremental/new capacity on offer is allocated
- Default option (as stated in TAR FG) should be the application of a premium in the first year incremental/new capacity is on offer
- Alternative approaches are to be developed by ENTSOG

ENTSOG position:

A default option should not be defined at this point of the process but all approaches should be assessed on an equal basis!

Tariff adjustment mechanisms

Next to applying a premium in the first year of offer, the following alternatives could be considered for adjusting tariffs to give the economic test a chance to be passed:

- Adjusting the reference price for all users at the respective IP
- Adjusting the reference price for all users at the respective IP, except for those that have booked capacity at the respective IP before the first offer of incremental capacity
- Introducing a minimum premium only for those network users that are participating in the incremental process
- Introducing a discount for those network users that are participating in the incremental process in order to incentivise them to increase their volume bids

Additional approaches?

Considerations of alternatives

Approach	Advantage	Disadvantage
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
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
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
Discount for those participating to the incremental process	➢ Rewarding for network users committing long-term and thus underpinning the investment	➢ Disadvantage for users holding existing capacity

SJWS 1 for the Incremental Proposal

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Concluding remarks

Mark Wiekens

Adviser, Market Area

10 February 2014 – ENTSO-E
Conference Center

See you at the next event:

SJWS 2 for the Incremental Proposal

Wednesday 26 February 2014
ENTSOG 2nd floor
Avenue Cortenbergh 100

10 February 2014 – ENTSO-E
Conference Center