


**Interconnector (UK) Limited**8<sup>th</sup> floor, 61 Aldwych  
London WC2B 4AE

Switchboard: +44 (0)20 7092 6500

Central Fax: +44 (0)20 7092 6501

Website: [www.interconnector.com](http://www.interconnector.com) @IUK\_Ltd

Andy Burgess  
Associate Partner  
Transmission and Distribution Policy  
Office of Gas and Electricity Markets  
9 Millbank  
London  
SW1P 3GE

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Dear Andy,

**RE: GAS TRANSMISSION CHARGING REVIEW – CALL FOR EVIDENCE**

Thank you for the opportunity to respond to this consultation. We welcome the launch of this review, especially as a number of tariff issues need to be determined as early as 2015 to facilitate the launch of bundled products at interconnection points.

There are five key issues that IUK would like to highlight:

1) Short term capacity products should not be discounted

By allowing short term reserve prices to be discounted, we have seen shippers in GB and other Member States incentivised to book short term capacity rather than long term. For this reason National Grid has experienced huge levels of under-recovery. The resulting high and volatile commodity charges, to address the under recovery, have created serious distortions to cross border flows and discriminated against those shippers who had already prudently committed to long term capacity bookings.

The incentives to book short term and long term capacity must be balanced fairly. Long term bookings, after all, provide benefits in terms of network planning, security of supply, and some element of revenue certainty for TSOs. We therefore believe that short term capacity should not be discounted unless there is an over recovery situation.

This is a particularly sensitive issue for TSOs like interconnectors who do not have a captive demand. If short term discounts lead to an under recovery situation, National Grid can at least raise commodity charges on its captive demand. What mechanisms will interconnectors without captive demand have?

2) Discrimination between domestic and interconnection points needs to be avoided

We believe that domestic GB points must be considered in the scope when considering changes required by the new European tariff rules. The charging regime for domestic and interconnection points needs to be as consistent as possible. This is needed to ensure a level playing field and to ensure that one user group or type of asset is not given an unfair advantage which distorts competition, impacts cross border flows, and creates an inefficient use of the system. For example the different treatment of entry points from Norway or UK production facilities versus gas entering from continental Europe or the different treatment of LNG and Storage compared to interconnector connections has the potential to discriminate and distort flows.

3) The short haul tariff should continue

Short haul tariffs are cost reflective and avoid inefficient by-pass of the NTS system. Short haul is a positive option for shippers and should continue in the future. At Bacton (and Zeebrugge) such tariffs play an important role in providing shippers with the flexibility to respond to market demand by wheeling gas from the various sub terminals. They play an important role in promoting cross border trade. We understand that short haul tariffs are not forbidden under the new European tariff rules. It is important therefore that such tariffs are permitted going forward.

4) Provide shippers with certainty about what they will pay

A key objective of Ofgem's review is to ensure shippers face stable prices. We are concerned that the Tariff Network Code, by mandating floating prices at interconnection points, will lead to unstable prices for shippers. Shippers have already said at a number of DECC/Ofgem stakeholder meetings that if they are unsure about the future price of capacity they are likely to purchase only short term products for which they will have price certainty.

Without long term bookings, interconnectors face a significant risk of not being able to recover their allowed revenues. Under ACER's current Tariff Framework Guidelines, interconnectors would be permitted only to increase capacity charges to address an under recovery. Given that interconnectors do not have captive demand, this may serve only to exacerbate the problem.

Some mechanisms are therefore needed to provide shippers with a degree of certainty around the floating price and this will help to encourage long term bookings. One suggestion at a recent DECC/Ofgem stakeholder meeting was to consider introducing a cap and floor around the floating price. We think that there is merit in Ofgem's Review exploring such an option in detail. It would help to give shippers a degree of certainty about the maximum extent to which their liability could change.

5) The review should acknowledge the interface with neighbouring systems

We do not believe that it is sensible to consider National Grid's future charging regime in isolation from the regime which will be applied to the interconnectors and its impact on them. Interconnector operators should be involved in the review from an early stage. This is for two principle reasons:

- a) The European Tariff Network Code will need to be implemented by the interconnectors as well as National Grid. Any principles developed by Ofgem in respect to National Grid could have a bearing on interconnector charging. The establishment of a new charging regime for each interconnector (in IUK's case applying to post 2018 capacity) will need to address some fundamental issues and some key decisions will need to be made relatively soon.
- b) The charging regime of one TSO can influence the behaviour of users on adjacent systems. This has already been shown in GB where the use of zero reserve prices impacts cross border flows on the interconnectors. A bundled capacity world will make the influence even greater. Any proposed change should therefore take into account the impact on adjacent systems.

The charging arrangements applying to interconnectors should not however form part of the scope of this review. This is for three reasons. First, other NRAs as well as Ofgem may have jurisdiction over the interconnectors. Inclusion of interconnector tariffs in the scope would undermine Ofgem's ability to make final decisions without reference to other NRAs. Secondly some of the most pressing issues for interconnectors are not shared with NGG (such as how to achieve effective under-recovery). And finally, the principle of proportionality suggests a much lighter touch approach should apply to interconnectors. Nonetheless there are some clear linkages and interactions, which need to be understood and taken into account when examining National Grid's tariffs, through the involvement of the interconnector operators. IUK will be discussing the charging arrangements to apply to its post 2018 capacity within a timeframe that allows it to meet its European Network Code obligations.

If you wish to clarify anything outlined in this letter please do not hesitate to contact me.

Yours sincerely

**Robert Sale**

Business Development and Regulation Director