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Dear Pavanjit

Authority decision to approve proposed modifications to Interconnector (UK)'s charging methodology

Summary

On the 11 December 2018, Interconnector (UK) ('IUK') proposed modifications to its charging methodology to the Authority for approval, pursuant to Standard Licence Condition ('SLC') 10 of the Gas Interconnector Licence ('the Licence'). This decision and attached direction sets out our approval of IUK's proposal.

IUK's Charging Methodology proposal

Following an annual review of its charging methodology, IUK are proposing the following changes:

- Simplification and consistency changes necessary to recognise the cessation of IUK's long term contracts which ended on 30 September 2018. IUK is proposing to remove the distinction between long term and standard contract shippers.
- Changes to increase the scope of booking incentives to include combination booking incentives for forward and reverse flow. As with long term booking incentives, the applicable incentives will be published in IUK's monthly charging statement ahead of the relevant auction.

IUK consulted on the proposed changes to its charging methodology. The public consultation opened on 4 October 2018 and closed after the mandatory 28 day consultation period on 3 November 2018.

There were four responses to the consultation, one of which was supportive of the proposals. The other respondents expressed concerns around the incentives and their publication:

- One respondent was supportive of the proposed charging methodology in general but noted that incentives offered should be set out fully in the charging methodology (rather than the charging statement), and that it should not result in capacity being sold at a lower level than what has already been assigned to users.

- One respondent suggested that the booking incentive should be varied on a quarterly basis rather than monthly.
- A further respondent also noted that details of incentives should be notified to network users at the earliest opportunity.

Ofgem Views

Ofgem's analysis of the modified charging methodology has been set out below against the four licence objectives.[1]

Transparency, Objectivity and Non-discriminatory

It is clear from IUK's consultation that some network users would prefer that incentives are published in advance of the monthly charging statement, either on a quarterly basis or within the charging methodology itself. The process of publishing the applicable incentives in the charging statement is an established principle approved by Ofgem in previous charging methodology submissions by IUK.

Consistent with our views in our previous approval of IUK's charging methodology,[2] IUK is a merchant asset that competes with alternative providers of flexible gas supply (and demand). Competition and prevailing market conditions mean the risk of IUK being able to exert market power is limited. Therefore, in our view it is appropriate that IUK be able to vary prices (and incentives) in the short-term consistent with the price flexibility afforded under the proposed charging methodology.

With regards to the comment about capacity being sold at a lower level than what has already been assigned to users, we consider it is for IUK as a merchant asset to set appropriate incentives that are within the limits allowed under the proposed charging methodology.

In addition we consider that the simplification and consistency changes are necessary to reflect IUK's current circumstances and therefore we consider the changes are in line with the charging methodology objectives.

Compliance with EU Law

We also consider that the new incentives proposed are compliant with EU law. The combination incentive is published in advance of a given auction and allows IUK to maintain the tariff setting principles required by EU Network Code on Gas Tariffs[3] that we approved within its charging methodology on the 28 February 2018. We also note that the offer of these incentives do not prevent IUK from offering capacity sequentially as required by the EU Network Code on Capacity Allocation Mechanisms.[4]

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[1] SLC10A(4) states that the charging methodology shall be transparent, objective, non-discriminatory and compliant with the Regulation and any relevant legally binding decision of the European Commission and/or Agency (collectively 'the relevant charging methodology objectives')

[2] https://www.ofgem.gov.uk/publications-and-updates/decision-proposed-modifications-interconnector-uk-s-charging-methodology

[3] Commission Regulation 2017/460 establishing a network code on harmonised transmission tariff structures for gas: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32017R0460

[4] Commission Regulation 2017/459 establishing a network code on capacity allocation mechanisms in gas: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A32017R0459

Decision on the proposed charging methodology

Upon review of the documents submitted on 11 December 2018 to Ofgem for approval with the main features as summarised above, the Authority considers the proposed modified charging methodology to be transparent, non-discriminatory, objective and compliant with any relevant legally binding decision of the European Commission and/or Agency.

Directions issued in accordance with SLC 10(14) of the licence to this effect can be found in the annex of this letter.

If you have any questions relating to this decision, please contact Robin.Dunne@Ofgem.gov.uk.

Yours sincerely
David Hall
European Markets

ANNEX – Charging Methodology

Direction issued to Interconnector (UK) Ltd pursuant to Standard Licence Condition 10 (Charging Methodology to apply to third party access to the licensee's interconnector) paragraph 14 of its Gas Interconnector Licence

1. This Direction is issued by the Gas and Electricity Markets Authority (the "Authority") pursuant to Standard Licence Condition 10 ("SLC 10") paragraph 14 of the gas interconnector licence ("the Licence") granted or treated as granted under section 7ZA of the Gas Act 1986 ("the Act") to Interconnector (UK) Ltd ("IUK" or "the licensee").

2. SLC 10 paragraph 9 requires the Licensee to review its Charging Methodology at least once in each calendar year and make such modifications to the Charging Methodology as may be requisite for the purpose of ensuring that the Charging Methodology better achieves the relevant Charging Methodology objectives. Following such a review and in accordance with SLC10 paragraph 11, on 11 December 2018, IUK submitted its proposed modified Charging Methodology to the Authority for approval.

3. SLC 10 paragraph 4 requires that the charges and application of the underlying Charging Methodology be objective, transparent, non-discriminatory and compliant with the Regulation (Regulation (EC) No 715/2009 on conditions for access to the national gas transmission networks) and any relevant legally binding decision of the European Commission and/or Agency (collectively the 'relevant Charging Methodology objectives').

4. Having regard to the relevant Charging Methodology objectives set out in SLC 10 paragraph 4, and to our principal objective and statutory duties, the Authority considers that IUK's proposed modified Charging Methodology meets the relevant Charging Methodology objectives.

5. The Authority hereby directs, pursuant to SLC 10 paragraph 14, that IUK's proposed modified Charging Methodology is approved.

6. This Direction shall come into effect at the beginning of the Gas Day on 12 March 2019, at which point the proposed Charging Methodology will replace the existing Charging Methodology. This Direction shall remain in effect until the Authority revokes or varies the Direction in writing upon reasonable notice.

7. This direction constitutes notice of the Authority's reasons for the decision pursuant to section 38A of the Act.

Dated: 11 March 2019
David Hall
European Markets
Duly authorised on behalf of the Authority