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Date: 19 March 2019

Dear Marcel,

Approval of modified charging methodology for the BBL interconnector pursuant to Standard Licence Condition 10 of the gas interconnector licence

Summary

On 19 December 2018, BBL Company (BBL) 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 BBL's proposal.

Background

The EU network code on gas tariffs (TAR)¹ aims to increase the transparency of transmission tariffs by introducing a number of requirements on transmission system operators (TSOs). In particular, it sets out how TSOs must design reference price methodologies² and how corresponding reserve prices are calculated.

In order to facilitate compliance with TAR, BBL is proposing changes to its charging methodology as a part of its annual review pursuant to SLC10(9) of the Licence. This proposal follows our recent decision³ to derogate BBL from certain articles of TAR that if applied would have a negative impact on BBL as a merchant interconnector.

BBL are also proposing changes to reflect the availability of physical reverse flow on the BBL interconnector this year and some other minor clerical and consistency changes.

BBL's proposal

Changes necessary to comply with EU Network Code on Gas Tariffs

BBL are proposing the following modifications necessary to facilitate compliance with TAR:

¹Commission Regulation (EU) 2017/460, establishing a network code on harmonised tariff structures for gas <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R0460&from=EN>

² TAR defines reference price methodology as the methodology applied to the part of the transmission services revenue to be recovered from capacity-based transmission tariffs with the aim of deriving reference prices.

³ <https://www.ofgem.gov.uk/publications-and-updates/decision-derogate-bbl-certain-articles-eu-network-code-tariffs>

- Reserve prices for yearly capacity products (for gas years 1 to 15) and maximum possible reserve prices for non-yearly capacity products will be published at least thirty days before the annual yearly capacity auction.
 - The applicable reserve prices for non-yearly capacity products will be calculated by applying a multiplier to the maximum non-yearly reserve prices. The charging methodology sets out an upper and lower range for the multipliers, as well as minimum notice periods⁴ for their publication.
- BBL's 'competitive forces factor', applied to the reserve price calculation to reflect competitive market circumstances, is superseded by the application of multipliers and is therefore removed from the reserve price calculation.
- For interruptible capacity, BBL have removed the possibility of a discount after the interruption has occurred and will retain the discount applied in advance of a possible interruption, as TAR does not allow both discounts to be applied.

Booking incentives

BBL proposed in the consultation to include two new booking incentives on capacity products. However, in its submission report to Ofgem it decided to remove these incentives from its submission.

Other Changes

BBL have also proposed several other minor and clarification changes to the CM. These include:

- Changes to reflect that physical reverse flow will be available on the interconnector from 1 July 2019.
- Changes to annual indexation levels.
- Clarifying that auction steps will be published on BBL's website in advance of a given auction.
- Details of interruptible capacity charges in the event additional firm capacity is released.
- Other minor clerical changes.

Industry Consultation

BBL consulted on the proposed changes to its charging methodology. The public consultation opened on 23 July 2018 and closed after the mandatory 28 day consultation period on 22 August 2018.

There were three responses to the consultation, all of which were broadly supportive of the proposals. Two respondents noted that the minimum notice period proposed should align with Interconnector UK (IUK). BBL consequently amended its minimum notice periods to reflect this.

One respondent also noted that there was a risk that, over time, BBL could use the multipliers proposed in the Charging Methodology to accrue excess profit, and that this behaviour should be monitored.

There were no comments in respect to the other changes in BBL's modification proposal.

⁴ The minimum notice period is two weeks before the auctions for monthly capacity, 6 hours for day ahead capacity and 1 hour for within day capacity.

Ofgem Views

Ofgem's analysis of the modified charging methodology has been set out below against the four licence objectives.⁵

Compliance with EU Law

The main changes proposed by BBL are changes intended to ensure compliance with TAR. We note that pursuant to Article 4 of TAR, BBL in its charging methodology use a reference price methodology to arrive at a reference price for yearly capacity. Consistent with chapter III of TAR, BBL calculates non-yearly reserve prices through applying seasonal factors and multipliers to the reference price. In line with TAR, the charging methodology requires publication of reference prices one month ahead of the annual auction.

In addition, BBL intends to use a fixed payable price approach to auction clearing, consistent with Chapter VI of TAR.

We consider that these modifications, coupled with the recently granted derogations, facilitate compliance with TAR.

Transparency/non-discriminatory/objectivity

In our recent derogation decision we derogated BBL from the requirement to set multipliers within a given range set out in Chapter III of TAR. As mentioned in that decision it is our view that given the competitive environment, it is appropriate for BBL, as a merchant interconnector operator, to have more tariff setting flexibility than allowed for under TAR. In its proposal BBL have proposed an absolute upper limit on these multipliers which restricts the possible prices for short-term capacity to a known range when BBL publishes annual capacity prices ahead of the annual capacity auction each year. The current charging methodology does not contain restrictions on multipliers.

With regards to the consultation response recommending monitoring of BBL, we will continue to monitor to ensure that BBL's arrangements remain appropriate and compliant.

It is also our view that the other clarification changes are consistent with the charging methodology objectives.

The authority's decision

Upon review of the documents submitted on 19 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.

Publication of BBL's charging statement

In accordance with SLC10(15) of the Licence, BBL is required to publish a charging statement detailing the prevailing charges 28 days prior to it coming into effect unless the Authority directs otherwise.

Consistent with BBL's proposal of minimum notice periods for monthly, within day and day ahead reserve prices (and their multipliers), we consider it appropriate that BBL publish these provisions in line with the minimum notice periods set out in its proposal.

⁵ 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')

The Authority has therefore decided to direct that monthly, within day and day ahead reserve prices (and their multipliers) be published no later than the minimum notice periods set out within the charging methodology. All other provisions of the charging statement shall be published 28 days prior to coming into effect.

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

Yours Sincerely

David Hall
Head of European Markets

ANNEX 1 – Charging Methodology

Direction issued to BBL Company 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 BBL Company (“BBL” 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 19 December 2018, BBL 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 BBL’s proposed modified Charging Methodology meets the relevant Charging Methodology objectives.
5. The Authority hereby directs, pursuant to SLC 10 paragraph 14, that BBL’s proposed modified Charging Methodology is approved.
6. Pursuant to SLC 10 paragraph 15, the authority directs that monthly reserve prices and their multipliers shall be published no later than two weeks prior to coming into effect, day ahead reserve prices and their multipliers shall be published no later than 6 hours before coming into effect and within-day reserve prices and their multipliers shall be published no later than 1 hour before coming into effect. All other provisions of the charging statement shall be published 28 days before coming into effect.
7. This direction constitutes notice of the Authority’s reasons for the decision pursuant to section 38A of the Act.

Dated: 19 March 2019
David Hall
Head of European Markets
Duly authorised on behalf of the Authority