ANNEX B: Key proposed changes to IUK's Charging Methodology (marked version[1]

2 Capacity ~~Reserve~~ Price

2.1 General Principle

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Entry and Exit Capacity will be made available by IUK for sale under an IAA by means of auctions, ~~or~~ subscription processes, or other process subject to relevant NRA approval. In any given auction or subscription process - the same terms and conditions apply to all Shippers.

~~IAA Capacity for use before 1 November 2015 will be advertised and sold on ISIS via an auction conducted on the day ahead of the intended day of use. This capacity will be sold in a pay-as-bid auction subject to a reserve price. IAA Capacity for use from 1 November 2015 will be sold via a subscription process subject to relevant NRA approval or via auction on PRISMA. Entry and Exit Capacity charges will be payable when capacity is purchased irrespective of whether or not the capacity is utilised.~~

~~2.1 Reserve price for Capacity for use during the period to 1 October 2018~~

~~The reserve price for Entry and Exit Capacity will be set by IUK to ensure objective and non-discriminatory treatment across all shippers. STA Shippers have underwritten the investment and operational costs of the Interconnector by committing to ship or pay payments, based on cost related tariffs, for the 20 year term of the STA. Without these long term commitments the infrastructure would not have been built. IAA Shippers who purchase IAA Capacity will be able to access Entry and Exit Capacity on an as required, day-ahead basis, without undertaking a long term commitment.~~

~~The tariff paid by STA Shippers under the STA, is based on two elements: the construction cost of the Interconnector pipeline and its Bacton and Zeebrugge terminals, and the operating costs. The base value of the reserve price for IAA Capacity is calculated from the average cost of capacity for STA Shippers derived from IUK's Financial Statement for year ending 30th September 2013, as follows:~~

~~Stated values (page 17 of 2013 statement) -~~

- ~~Tariff payments based on construction costs = £142,883,000~~
- ~~Tariff payments to recover operating costs = £34,901,000~~
- ~~Total Capacity (kWh/h) = 59,731,735 (equivalent to 45.5 bcm/yr)~~

~~Therefore, the average cost of capacity in the gas year 2012/2013 (p/(kWh/h)/day)~~

~~= (£142,883,000 + £34,901,000)*100/(365*59,731,735) = 0.8154 p/(kWh/h)/day~~

[1] Apart from the key content changes highlighted in this Annex, some changes to other sections of the Charging Methodology have also been necessary to make it more enduring e.g. removing references to the period pre-CAM up to 31 October 2015 and some actual price information that is outlined and updated in IUK's Charging Methodology Statements. Annex C provides a full clean version of the proposed methodology.

~~An escalation factor is used to calculate the total reserve price for IAA Capacity for subsequent years. This is similar to the way the STA tariff is escalated each Gas Year. For illustration, the reserve price for daily capacity for Gas Year 2014/15 is calculated as follows:~~

- ~~Escalation Factor = ratio based upon the Producer Price Index (PPI) = PPIr/PPIo (see Appendix 1 for PPI reference numbers).~~
- ~~PPIr = the average value of the PPI for the twelve month period ending on 30 June immediately prior to the commencement of the Gas Year which ends on 30 September in year r in respect of which the price is calculated~~
- ~~PPIo = average PPI for twelve months ending 30 June 2012 = 106.1083~~
- ~~PPIr for 2014/15 = 108.6583~~
- ~~Escalation to 2014/15 = 108.6583/106.1083 = 1.0240~~

~~TOTAL RESERVE PRICE FOR OS CAPACITY FOR GAS YEAR 2014/2015 (p/(kWh/h)/day)~~
~~= 0.8154 * 1.0240~~
~~= 0.8350 p/(kWh/h)/day~~[PSD1]

~~The total price above will be split 50:50 into daily Entry Capacity Reserve Price (0.4175 p/(kWh/h)/day) and daily Exit Capacity Reserve Price (0.4175 p/(kWh/h)/day). If longer term capacity becomes available (principally through surrender or LTUIOLI), then the reserve price will be set in the relevant auction based on the capacity duration e.g. for monthly capacity it would be p/(kWh/h) per month.~~

~~2.2 Reserve price for Capacity for use from 1 October 2018 onwards~~

~~2.2.1~~ General Principle

The ~~reserve~~ prices for capacity sales for Entry and Exit Capacity ~~for use from 1 October 2018~~ will be set by IUK to ensure objective and non-discriminatory treatment across shippers taking part in the capacity sales.

The key factors determining the reserve prices are:

- Competitive forces and the prices of competing and complementary services;
- Operating costs for operating and maintaining the company and its assets;
- Capital expenditures required to maintain the service;
- Projected customer demand for IUK capacity and the forecast volume of both long term and short term sales under a range of market scenarios.
- Ensuring no cross subsidy from STA shippers in the period to 1 October 2018.

IUK will set ~~reserve tariffs~~prices which are competitive and responsive to market forces. The ~~tariffs~~ prices will not be mechanistically determined by a formula. The ~~reserve~~ prices will be attractive to shippers, and will reflect the value of the services. Appendix 1 provides more information regarding the prices for the period till 1 October 2018 to ensure no cross-subsidy from the STA shippers.

For any given auction, t~~T~~he price paid for Entry Capacity and Exit Capacity will be the reserve price plus any premium bid at the time of the allocation process.~~-~~. This means the capacity price would be fixed at the time of allocation (but subject to future indexation) providing price certainty to IAA Shippers.

For ascending clock auctions held on PRISMA, the determination of the large price step shall seek to minimise as far as reasonably possible, the length of the auction process. The determination of the small price step shall seek to minimise, as far as reasonably possible, the level of unsold capacity where the auction closes at a price higher than the reserve price.

2.2 Short term prices

The same principles as outlined in 2.1. will be used to determine the level of the price multiplier for each entry and exit product less than a year in duration relative to the annual price. This includes, but is not limited to, the reserve price multiplier for standard capacity products

[2]. The multipliers can differ for different entry and exit points, types of capacity, durations and time periods to reflect the different underlying market and cost conditions.

2.3 Publication of the capacity price

The relevant price will be published at least:

- Twenty eight days ahead of any capacity product sale with a capacity duration equal to, or greater than one year
- Fourteen days ahead of any capacity product sale with a duration equal to, or greater than, a quarter.
- A day ahead of any capacity product sale with a duration greater than one day and less than a quarter.
- An hour ahead of any daily and within day capacity product sale.

~~2.2.2~~2.4 Principles for price structure of ~~2015~~ any Subscription Process ~~(valid for any Subscription Process held before 1 November 2015)~~

~~The capacity offered in 2015 will be long term capacity booked well in advance of delivery. It is important for IUK to know in 2015 that some capacity has been booked post 2018, to allow for more efficient and effective capacity planning of IUK's future business model. To reflect this fact, v~~Various incentives ~~were~~ could be included in ~~the 2015~~any subscription process to encourage long term booking subject to NRA approval.

For example, t~~T~~he main principles for the price structure of ~~the 2015~~any -subscription process may include, but are not limited to, the following~~are outlined below~~:

- ~~The price paid for Entry Capacity and Exit Capacity will be the reserve price plus any premium bid at the time of the allocation process.~~ The price paid for Entry and Exit capacity ~~This means~~

[2] Transmission system operators are required to offer standard capacity products as specified in Article 9 of Commission Regulation (EU) No 984/2013. These standard capacity products are yearly, quarterly, monthly, daily and within day capacity products.

~~the capacity price is~~ will be fixed at the time of allocation (but subject to future indexation) providing price certainty to IAA Shippers.

- A booking incentive on the ~~reserve~~ price ~~will be offered for bookings~~ for Annual Capacity Products that are longer in duration (i.e. booking incentive 10% for bookings of 5-7 Gas Years, 15% for bookings of 8-9 Gas Years and 20% for bookings of 10 Gas Years or longer).

- ~~IUK will also offer t~~The option of booking Quarterly Capacity Products for shippers who book Annual Capacity Products for a Capacity Period of 5 successive Gas Years or more. Quarterly Capacity Products for two quarters or three quarters of entry and exit will be available in addition to the Annual Capacity Products. The 2 Quarter Capacity Product will be made available at a premium of 50% to the price of Annual Capacity Products corresponding to the same duration (i.e. the reserve price after any booking incentives are applied) and the 3 Quarter Capacity Product will be made available at a premium of 20%.

- A Capacity Transaction for a Firm Annual Capacity Product for 5 or more successive Gas Years benefits from a "lowest price guarantee" in that the Capacity Charge is the lower of: (i) the sum of the reserve price and the premium; and (ii) the lowest price for which such Firm Annual Capacity Product is allocated in a PRISMA auction for that Gas Year or if there is no allocation for that Gas Year, the lowest IUK reserve price for that Firm Annual Capacity Product for that Gas Year. ~~In addition, the IAA Shipper is protected from increases to such charge and from additional charges being imposed as provided in the form of Confirmation in paragraph 5 of Annex B-3 to Section B of the IAC.~~

~~2.2.3~~2.5 Indexation

When calculating the ~~entry~~ Entry or ~~exit~~ Exit capacity charges to apply in a future year, the ~~reserve~~ price ~~element for an Annual Capacity Product~~ will be subject to ~~annual~~ indexation as provided for in ~~Section F paragraph 5.3 of~~ the IAC. ~~Any auction premium will remain fixed.~~