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Sent by email to: consultation@interconnector.com

7 September 2017

Dear Danielle, Pavanjit,

Gazprom Marketing & Trading Limited (GM&T) feedback on IUK proposals to amend the IUK access rules and seek changes to the application of the CAM and TAR NCs

Thank you for the opportunity to respond to your consultations. In this response we include feedback on the proposals published in each of the following documents:

- Consultation on IUK's Implicit Allocation Mechanism
- Consultation on IUK's Access Terms
- Consultation on IUK's Charging Methodology (CM) for capacity sales from January 2018
- Consultation on Interconnector (UK) Limited's request under Article 37 of Commission Regulation (EU) 2017/460 establishing a network code on harmonised transmission tariff structures for gas for a derogation from the application of one or more Articles of this Commission Regulation

Although these consultations are presented separately, we see them as interlinked and prefer to respond to the whole package of proposals in one letter.

We would like to request that, in future, where 4 lengthy consultations are launched simultaneously the deadline for providing feedback be extended from the usual 4 weeks to allow shippers more time to review the proposals.



Given IUK's unique circumstances, GM&T supports IUK having appropriate flexibility to offer innovative products beyond the standard products set out in CAM, e.g. non-standard durations or access to inventory. This would be useful for shippers and a complementary tool for a merchant operator competing with other flexibility assets who do not have the same restrictions on the products they offer.

We agree that a key advantage of the implicit allocation service is that it allows the market "to buy capacity when a shift in price spreads creates an economic rationale to do so" whereas the CAM auction timetable "limits shippers ability to purchase IUK capacity whenever they see market value" (page 2 of the implicit allocation consultation). As per page 6 of the consultation, we agree that the proposals will increase market efficiency and allow shippers to react promptly to market events and pricing, but only to the extent that the pricing of Interconnector capacity is made available on a transparent basis with plenty of notice.

We are however of the opinion that IUK is seeking excessive flexibility in its TAR NC derogation application and that their Charging Methodology is not nearly detailed enough for GM&T to be able to support IUK's proposals to introduce implicit allocation as an additional means to acquire capacity. The lack of transparency and foresight on pricing decreases the attractiveness of the product and increases the risk for shippers - both those with existing bookings and those looking to acquire capacity in the future.

(a) Implicit Allocation Mechanism

In relation to implicit allocation, we would like to make the following comments on IUK's proposals:

- **Application of CAM:** We understand that CAM NC Article 2.5 allows that: "Where implicit capacity allocation methods are applied, national regulatory authorities may decide not to apply Articles 8 to 37." i.e. it is not necessary to dis-apply Articles 8 to 37 of the CAM NC simply because implicit capacity allocation is being introduced. The treatment of Articles 8 to 37 is crucial. In this particular case, we do not think that it is appropriate to dis-apply these articles. In the original consultation document IUK stated that it was "seeking Implicit Allocation to be implemented without Articles 8 to 37 having effect. IUK intends [but would no longer be obliged] to continue offering its post-2018 capacity through auctions on the PRISMA platform, under Articles 8 to 37, in addition to Implicit Allocation", "IUK intends to implement Implicit Allocation with Articles 8 to 37 of the CAM NC dis-applied". We welcome the clarification letter that IUK published on 1 September which states that "IUK will continue to offer its capacity through the CAM NC auctions via PRISMA" and "IUK will only seek to dis-apply Articles 8-37 for the capacity while it is offered through the Implicit Allocation Mechanism" and we agree that this approach is appropriate.
- **Capacity release:** On page 3 of the consultation document, IUK states that "in accordance with the CAM NC, 20% of technical capacity will be set aside and not offered in the annual yearly

auctions beyond 5 years out" and that half of that will only be offered 1 year ahead, as per the CAM NC. We agree that this is appropriate.

- **Capacity conversion:** On page 4 of the consultation document, IUK references the capacity conversion service mandated under Article 21(3) of the CAM NC. We strongly support their proposals to offer this service for daily firm products in addition to longer-term products, going above and beyond the obligations in the CAM NC to the benefit of shippers. It is particularly important to implement this if implicit allocation (where unbundled capacity is offered) is implemented.
- **Timings and limitations (2.2.2):**
 - We understand the timings and limitations set out in the first paragraph of section 2.2.2 of the consultation document and think it is very sensible to impose restrictions. Whilst we support the additional flexibility from introducing implicit allocation, we think that the PRISMA auctions should continue to be the main, prioritised route for capacity release. We would therefore prefer that capacity be offered via implicit allocation only once it has already been offered in a PRISMA auction, to ensure that the amount of capacity offered via PRISMA is maximised. We think that another way to limit possible gaming would be to have implicit allocation linked to basis trading only, rather than to any gas trade.
 - We note that IUK proposes to limit the quantity of capacity made available via implicit allocation ahead of the CAM NC annual auctions to 40%. We think it is appropriate to maximise the offer on PRISMA but suggest this is achieved by offering capacity via implicit allocation only once it has already been offered in a PRISMA auction.
 - We do not think that it is appropriate for some capacity to be available under implicit allocation at all times, as this will lead to a reduction in the capacity offering on PRISMA. PRISMA should remain the main way of marketing capacity, with implicit allocation used as an additional, not an alternative, way of marketing capacity.
 - We agree that for day-ahead and within-day the PRISMA auctions are better suited than implicit allocation, "as the timescales to pick up capacity from neighbouring TSOs are limited".
- **Allocation rules:** In the "Consultation on IUK's Access Terms", there is an "example of how the Implicit Allocation Rules may look. These will be fully developed before capacity is offered through Implicit Allocation and published on [IUK's] website." We query why these rules are not already developed and a core part of the consultation on Implicit Allocation. The document, when signed, "is binding on the IAA Shipper and cannot be withdrawn or changed", so it is an important part of the implicit allocation process that should be subject to thorough legal review

from both IUK's side and shippers'. The wording in the table of products could be clearer and there are some vague phrases used, e.g. "around the same time as" on page 3.

(b) Pricing

General

One of IUK's consultation documents states that prices will be published "sufficiently in advance of offering capacity" and IUK "commits to making available a pricing publishing timetable on IUK's website. The timetable will set out how far in advance prices are published before the relevant allocation mechanism... [IUK is] currently thinking, as a minimum, that prices will be published in line with the current timetable established under PRISMA auction rules, e.g. for the annual CAM auction, a month in advance". In another of the documents IUK states that it will "publish the price in advance for any potential product offered" and in another it states that "IUK is committed to publishing indicative prices for its standard CAM products for the coming gas year no later than thirty days before the annual capacity auction". We note that IUK is "currently preparing the tariff structure for Implicit Allocation and will aim to provide these tariffs to the market by the end of 2017" for implementation 1 January 2018.

We have several concerns:

- We do not think it is acceptable for a TSO to "aim" to provide tariffs for 1 January 2018 by the end of 2017.
- It is not sufficient to say what IUK is "currently thinking".
- The timetable referred to above is exactly what shippers needed to see as part of this consultation process in order to be able to judge whether it is appropriate or not. A reference to its future existence is not sufficient.
- It is not sufficient to say that IUK "will publish the price in advance for any potential price offered" and there appears to be conflicting messages even within this suite of documents on what "sufficiently in advance" means. More notice and more certainty is needed. IUK's proposed approach to setting prices, particularly in relation to daily and within-day products, amounts to introducing a variable tariff with no inherent stability or predictability. The proposals allow IUK to assess the spread between markets, on a very short-term basis, and set the price of capacity based on this. This puts IUK in a similar position to shippers, assessing market spreads and determining the arbitrage opportunities available. We question whether this is appropriate for a TSO and note that, if implemented, market dynamics are likely to change. We think that the auction premiums allowed for under the PRISMA auctions gives IUK additional revenue on days where market events increase the value of capacity, and this is preferable because it's transparent and market-driven.

- Because of the numerous references to the Network Codes, shippers are left not knowing when prices for implicitly allocated capacity will be published, only when prices for standard CAM products might be published. IUK undertakes to "publish how the pricing of standard products sold through the IAM will relate to the pricing of the equivalent product durations offered on PRISMA". But this is not a sufficiently detailed proposal. In conjunction with the proposals under the TAR derogation consultation, the implication is that shippers will have very little notice of prices and that any information published comparing the pricing of IAM capacity vs PRISMA capacity will either not be published in time for shippers to make an informed judgment or will be indicative and therefore subject to change.
- Regardless of initial publication date/notice of prices, IUK is seeking the ability to be able to change the reference price, multipliers and seasonal factors at any time during the year (which makes both the indicative prices and actual/confirmed prices of very little value to shippers). This will create an unacceptable level of uncertainty and could hinder liquidity and security of supply.

Long-term bookings

We note that in previous consultations IUK has stated its intention to market post-2018 short-term capacity at a multiple "significantly greater" than the annual reserve price to incentivise long term bookings and we support this approach.

If IUK wishes to promote long-term capacity bookings, as it has previously stated, we would suggest guaranteeing the economic advantages of booking longer-term capacity over allowing multipliers of less than 1 to be applied to short-term products. In discussions relating to the development of the TAR NC, IUK has previously stated its opposition to short-term multipliers of less than 1; we are surprised this is not reflected in the proposed Charging Methodology.

Additionally, we would like to stress that in order for a shipper to be able to make a decision to buy a capacity product it has to know the respective prices of all of the various capacity products available. The multipliers for all capacity products must be published in a transparent manner well in advance of the start of the year. The flexibility that IUK is seeking could stop shippers booking IUK capacity, damaging cross-border trade and security of supply if used to the full extent. Whilst we have been assured by IUK verbally that it does not intend to seek to use all of the flexibility that it is seeking in these consultations, (a) we question why they are seeking this flexibility if that is the case and (b) once the restrictions are dis-applied it is entirely at IUK's discretion to change its mind about the extent to which it prices flexibly. Shippers need the reassurance of regulatory restrictions.

Shippers who trade gas at the key hubs in NW Europe need to be able to factor IUK's transportation costs into their trading decisions.

On page 7 under heading 2.3.3 "Shaped capacity purchases", IUK implies that one aim of introducing implicit allocation is to "reduce the risk to shippers of making a longer-term booking". We would like to emphasise that the risk to shippers in making a longer-term booking lies in having no foresight of the capacity prices. Currently shippers do not have enough information about the pricing of IUK capacity to be able to price-up longer-term capacity against shorter-term capacity. In the same sentence IUK refers to "typical utilisation patterns", something that the TAR NC derogation consultation denies exists and uses as justification for IUK having flexibility to change prices frequently and not consult on them or publish them in good time. This will actively discourage shippers from booking long-term capacity.

On page 7 under 2.3.5 "Unbundled Capacity", IUK claims that it "seeks to incentivise longer term bookings whereas the National Grid Gas ("NGG") pricing regime seeks to incentivise short term capacity bookings" and overleaf notes that "a Shipper who wanted to lock in longer term IUK capacity would have to commit to long term NGG capacity under an unknown future charging regime [if they bought bundled capacity]. Offering unbundled capacity via Implicit Allocation allows a Shipper to mitigate their risk". IUK should be aware that it is uncertainty over IUK's own pricing regime that creates risk for shippers purchasing longer-term capacity. NGG's pricing regime and any changes to that regime are subject to stakeholder consultation and appropriate notice periods, and the charging-related information that NGG provides is very detailed. NGG plans to apply the TAR NC in its entirety.

(c) TAR NC Derogation

Whilst we agree that certain articles of the TAR NC should not be applied to IUK, e.g. Article 5 on cost allocation because IUK has no domestic points, IUK's request goes far beyond what we were expecting or think is reasonable.

Across IUK's various consultation documents the following points are made, to which we would like to respond:

- "IUK would not be able to respond to changing market conditions, unlike competing flexibility assets" "IUK would not be able to respond to changing market and competitive conditions"

We do not think that it is appropriate for a TSO to respond to changing market conditions in the manner described by IUK; it is the role of shippers to respond to changing market conditions. Furthermore, we question how this would be achieved on a day-to-day basis – IUK would need to analyse the "changing market conditions" in order to be able to "respond" to them, but no explanation is given about what this would involve.

- "...harm competition in the flexibility market as it would reveal commercially sensitive information to IUK's competitors (e.g. via consulting on prices and outlining other charges)." "IUK also needs a less restrictive framework when it comes to publication and transparency obligations to avoid having to share commercially sensitive information with competing flexibility assets." "not appropriate from a competition point of view to consult/publish this

information given that IUK competes with other flexibility assets that are not under the same obligation”

Whilst we understand IUK’s concerns about revealing sensitive commercial information, we would like to reiterate that shippers will be reluctant to use the Interconnector if they have no information or certainty about prices and if transparency is poor.

- “it is not possible for IUK to accurately predict flows” “Flows and capacity bookings... will be highly difficult to predict” “it is not possible for IUK to accurately predict flows/bookings and therefore to lock in a “correct” tariff structure effectively over a year” “Historically, IUK has seen intermediate to low average annual utilisation with occasional periods of high utilisation. This type of utilisation pattern is expected to continue after October 2018”

We understand that it is difficult to predict flows through the Interconnector, however the level of bookings will decrease substantially if transparency is poor and if there is no certainty on prices.

- “Price spreads do not reflect the wider economic benefits that IUK provides”

We agree that price spreads do not reflect the wider economic benefits that IUK provides. We do not think that this is justification for the level of flexibility in price-setting that IUK is seeking.

We cannot support IUK’s request for derogations from the following articles of the TAR NC:

- Para 1 Art 6
- Para (a) Art 7
- Para 3 Art 12
- Art 13 - We feel strongly that if IUK thinks the TAR NC multiplier caps are not appropriate for its asset then it should propose alternative caps or ranges to be applied, not request complete discretion. These caps or ranges needed to be shared as part of this consultation, and should not have been left to a later date to determine.
- Art 26
- Art 27 – We understand that the 2 months period for the ACER assessment and 5 months for the NRAs may be excessive in IUK’s case, however that does not justify dis-applying the entire article; a middle-ground should be sought.
- Art 28
- Art 29
- Sub-paragraphs (a)(ii) and (b)(iii)(2) of para 1 Art 30
- Art 31

We query the rationale behind requesting a derogation from paragraph 4 of Article 16. The paragraph reads: "As an alternative to applying *ex-ante* discounts in accordance with paragraph 1, the national regulatory authority may decide to apply an *ex-post* discounts." It goes on to explain that *ex-post* discounts are only allowable under restricted circumstances. We are therefore confused as to why IUK is seeking a derogation from this paragraph. It appears that no derogation is required to implement *ex-ante* discounts for interruptible instead of *ex-post*.

(d) Specific comments on Charging Methodology tracked changes version

- General comments: the document has not been reviewed thoroughly for typos, and in some instances, e.g. at the bottom of page 2 of the tracked changes version, a sentence is shown as a new addition but is then shown as deleted from the previous version of the document later (half way down page 3) so that it is difficult to work out which provisions are changed.
- Section heading: 1. Introduction
 - The description of the TAR NC refers only to two aspects of the TAR NC, it does not reflect what the TAR NC is. If a description is going to be included then it needs to be improved.
 - "Any available capacity will be offered as products with standard durations in auctions on the PRISMA platform in accordance with Regulation (EU) 2017/459 ("CAM Code")." – this is inconsistent with the consultation that IUK has published on implicit allocation where the PRISMA-related sections of the CAM NC are proposed to be dis-applied.
 - The sentence "The IAA and IAC are NRA approved" has been added. Several changes like this have been made to the document and it is not clear to the reader why this is the case. Please provide an explanation.
 - Under 1.1 "Units", why has "Charges are expressed and will be billed as follows" been replaced by "Charges and prices are expressed as follows"? Is there a change to the definition of 'prices' and 'charges' to warrant this or a change in the invoicing process?
 - Under the same heading, the "Electricity Charges – Euros" bullet point has been deleted, yet below that we are told that invoiced amounts will be in either sterling or Euros. We think "or Euros" needs to be deleted.
- Section heading: 2. Capacity Prices
 - "Prices will be published on IUK's website (and other platforms) in advance of the relevant Allocation Mechanism. A pricing publication timetable will be available on IUK's website." This is not specific enough. The publication timetable is what we need to see included in the Charging Methodology, not a reference to it.

- "Capacity for use for the period to 1 October 2018... is made available under the IAA and offered under the relevant PRISMA auction." This states that implicit allocation won't be applicable for capacity pre-October 2018, so is being implemented from 1 January 2018 with a 10 month delay in when capacity can be purchase, but if that is the case then it is not clear from the other consultation documents. Can you please clarify?
- We would like additional information about the proposal to introduce a "risk premium". There is no information in the consultation about what a risk premium is or is designed to achieve, and the impact on prices if it is set to a non-zero value – the implication is that this will only affect the pricing of non-annual products but it is not clear. (There is a typo at the bottom of page 5 of the Charging Methodology on this point.)
- "The tariffs will not be mechanistically determined by a formula" (top of page 6) is deleted. We would like to know why this is.
- "The prices will be attractive to shippers" (top of page 6) should be deleted as it is subjective and not appropriate for inclusion in a Charging Methodology.
- Section 2.3.3 "Price for capacity products with a duration less than one year" has insufficient detail. There is no indication as to whether multipliers for short-term capacity will be greater than or less than 1. A table showing the ranges of multiplier levels for each product or capacity duration could be included here.
- Under 2.3.4, "The price structure of any Allocation Mechanism [sic] may include, but not be limited to, the following:" – the use of "may" is not appropriate for a charging methodology document. Particularly when immediately followed by a statement that "price paid... will be fixed at the time of allocation". We do not think that IUK should state that it "may do: x, y and will do z" as it is not clear whether the "may" or "will" takes precedent in applying to z.
- Under the same heading, and prefixed with "may", is also a statement about 'lowest price guarantees'. It says that the guarantee calculation will include a reference to "the premium" despite this being in section 2.3.4 on the price structure for non-PRISMA allocation mechanisms, so we think that the reference to premium should be removed – or the paragraph be made clearer.
- Section heading: 3. Buy-back Prices
 - In future IUK proposes that Buy-backs be communicate to shippers via the IUK Shippers Information System, not the Bulletin Board. We would prefer to see the requirement posted on the Bulletin Board where it is open for everyone to see rather than just IUK shippers, given that if a Buy-back event takes place it implies there has been quite a



significant change in the market within-day and creates REMIT concerns for involved parties.

We would like IUK to clarify whether ACER will have oversight of the TAR NC derogation process, and whether they are able to review on the proposals to ensure that a derogation would not undermine the Network Codes.

(e) More generally

Capacity right-sizing

We note from the CM that the reserve price and multipliers will be set with reference to certain key principles including costs incurred by IUK to operate and maintain the facilities. No further information is provided. We understood from IUK's Information Memorandum and other publications relating to the 2015 sales processes, that IUK intends to respond to the markets' demand for capacity by right-sizing the asset, to minimise unnecessary costs. GM&T would like to seek clarity from IUK on when it will make a decision about the appropriate level of capacity to continue operating and maintaining, given the potential impact on costs and therefore capacity prices.

Regulatory treatment of interconnectors

The consultation raises fundamental questions about the treatment of interconnectors by regulators. The IUK and BBL interconnectors link three of the most liquid markets in Europe and we are keen to see appropriate regulatory treatment of these assets to ensure the continued success of these key markets.

Although categorised as a TSO and required to implement the EU Network Codes, IUK highlights that it is not supported by an allowed revenue or under-recovery mechanism, and argues it ought to be granted the right to set prices flexibly to compete with other assets not subject to the same stringent regulatory requirements. However GM&T believes the flexibility sought by IUK in these proposals is potentially damaging to the market.

We believe that if IUK were not subject to such challenging market conditions without appropriate regulatory treatment and potentially the support of an under-recovery mechanism, IUK may be able to offer more reasonable provisions for price-setting.

We would like Ofgem and CREG, as part of their assessment/approval process for this series of consultations, to provide the market with their view of the future of IUK from a regulatory perspective, taking into account the impact on liquidity, competition and security of supply if the Interconnector is unable to continue operating due to the lack of appropriate regulatory treatment.



Yours sincerely,

A handwritten signature in blue ink, appearing to read "Gavin Steyn". The signature is fluid and cursive, with a long horizontal stroke at the end.

Gavin Steyn

Head of Commercial Operations