



All Stakeholders

8th August 2017

Dear Stakeholder,

Consultation on IUK's Charging Methodology (CM) for capacity sales from January 2018

Interconnector (UK) Limited ("IUK") would like to hear stakeholders' views on its proposed Charging Methodology ("CM") for capacity purchased from January 2018. IUK's CM outlines the principles for setting its prices. The proposed changes are outlined in Annex A (marked version compared to the current approved CM) and Annex B (clean version).

1. Background

Article 15/5bis, § 15 of the Belgium Gas Act and Condition 10 of IUK's GB interconnector licence require IUK to prepare and submit for the respective National Regulatory Authority ("NRA") approval, a CM for access to the interconnector. Regulation (EU) 2017/460 which establishes a network code on harmonised transmission tariff structures for gas ("TAR Code") also outlines rules on the application of a reference price methodology as well as the calculation of reserve prices for standard capacity products.

IUK's CM is approved by both Ofgem (the GB NRA) and CREG (the Belgian NRA). The CM takes into account and recognises that IUK, given its specific circumstances, needs to be able to set competitive, market-based tariffs which both reflect market conditions and allow for cost recovery. The CM has been reviewed annually, as required by the governing rules, since its original approval in June 2015.

2. Proposed changes to the CM

On 30 September 2018 IUK's original long term contracts end and more than 90% of its capacity will become available including products on a shorter term basis. This capacity will be offered as CAM standard products and also, subject to NRA approval, via other allocation mechanisms.

As part of this year's review, IUK is therefore taking the opportunity to propose changes to the CM to ensure that it is appropriate for the sale of all types of capacity durations from 2018 as well as enabling the sale of capacity via other allocation mechanisms. The CM also reflects relevant requirements of the TAR Code which recently came into force.

The specific changes can be seen marked up in Annex A.

Summary of the proposed changes to the CM

References to the amended Belgium Gas Act and TAR Code

The introduction now notes that the CM is prepared as required under Article 15/5bis, § 15 of the Belgium Gas Act which was amended in January 2017 to require interconnector operators to prepare a CM and submit it for approval to CREG. The introduction also notes that the TAR Code, which came into force in April 2017, outlines rules for the application of a reference price methodology and reserve prices for standard capacity products at interconnection points.

Introducing the term “Allocation mechanism”

In addition to the CM covering sales via PRISMA, IUK proposes to introduce (in sections 1 and 2) text to allow the CM to be used for sales of capacity via other “Allocation Mechanism(s)” subject to NRA approval (and described in the relevant access rules). This is in order to enable the CM to be used for the pricing of all capacity offered by IUK via any other mechanism approved by NRAs - for example via Implicit Allocation.

Reference to the proposed Belgian IUK financial control

CREG is currently consulting on a proposed IUK financial control¹. This control establishes a safeguard against excess profit. We are therefore proposing to amend section 2.3.1 of the CM on General Principles to note that there is an additional element governing IUK’s finances.

Relevant CM elements of the Tariff Network Code

IUK believes that the approach set out in the current CM remains appropriate for the reference price methodology, taking into account IUK’s full market exposure, the unpredictability of its flows, and the fact that IUK faces direct competition from a range of flexibility assets.

The price payable for IUK capacity will continue to be fixed at the time of purchase and subsequently will change only in line with inflation provisions. This provides price certainty for Shippers. IUK is proposing to introduce a “risk premium” in the list of key factors determining the fixed price. This is a factor required under Article 24 of the TAR Code if a Transmission System Operator offers fixed payable prices. As IUK is generally seeking to incentivise longer capacity bookings it does not, in practice, normally expect a value higher than zero for the risk premium parameter.

Furthermore, a new section 2.3.3 has been added to the CM to commit IUK to using the same principles as outlined in 2.3.1 of the CM to determine the level of multipliers for products less than a year in duration.

Pricing transparency

In section 2.1, IUK commits to publishing prices sufficiently in advance of offering capacity through the relevant allocation mechanism. IUK confirms prices will be published on IUK’s website (and other relevant platforms) and commits to making available a pricing publishing timetable on IUK’s website. This timetable will set out how far in advance prices are published before the relevant allocation mechanism.

¹ The CREG consultation is open from 8th August 2017 until the 5th September 2017. For further details please see: www.creg.be/fr/consultations

For standard CAM product auctions we are currently thinking, as a minimum, that prices will be published in line with the current timetable established under PRISMA auctions rules e.g. for the annual CAM auction, a month in advance. The appropriate pricing publication will be considered further for other allocation mechanisms.

Differential pricing

IUK has introduced text to say that, whilst ensuring no undue discrimination, it will have the ability to set different prices at different entry/exit points, for different flow directions, and for different products (under section 2.3.1). IUK believes it is important, as a physically bi-directional interconnector with a typically seasonal profile, to be able to reflect and adjust to changing market conditions and respond to competitive circumstances.

Simplification of the commodity charging

The section on fuel charges has been simplified to outline how IUK will recover charges to flow gas. IUK will estimate the consumption of gas and electricity based to transport a unit of gas through the transportation system and convert these into a suitable commodity charge. The elements of the commodity charge will be set out in IUK's Charging Statement.

Simplification/ consistency changes

Some changes have been proposed for consistency. For example:

- Amendments to how prices are represented in section 2.2 to $p/(kWh/h)/h$ reflect how prices are invoiced;
- The principles for any Allocation Mechanism pricing structure have also been amended to be generic rather than refer to the November 2015 Subscription Process which has now passed; and
- There is also some simplification on the background text explaining how to access capacity.

3. Your feedback

We are interested in hearing your views on our proposed changes to our Charging Methodology.

We would appreciate comments from all interested parties. In particular we would welcome your response to these specific questions:

- Do you agree that the CM, for the sale of capacity from January 2018, is appropriate?
- Do you agree that the proposals are appropriate for an interconnector with full market exposure?
- Do you have any other feedback on the proposed changes?

Please send your response to consultation@interconnector.com by 17:30 UKT on 7th September 2017.

Please ensure that a "read receipt" is requested to confirm that your response has been received. Please note that any responses not marked confidential may be published on IUK's website. Confidential responses may be shared with Ofgem and CREG at their request.

Additionally, if any party would like a more detailed explanation of our prevailing regulatory framework, and how the proposal is consistent with that framework, we would be happy to arrange a bilateral meeting to discuss this.

If you wish to clarify any aspect in relation to this letter, or have any questions, please contact Pavanjit Dhesi on +44 (0) 78 666 20 832 or Pavanjit.dhesi@interconnector.com

Yours faithfully

PDHESI

PAVANJIT DHESI
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ANNEX A: Proposed changes to IUK's Charging Methodology (marked version compared to current methodology)

ANNEX B: Proposed changes to IUK's Charging Methodology (clean version)