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from:

VERENIGING LNG SHIPPERS NEDERLAND

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Case Number: ACM/14/023224

ACM consultation on NC TAR implementation

Dear Madam / Sir,

28.5.2018

VERENIGING LNG SHIPPERS NEDERLAND, welcomes the opportunity to consult on the implementation of the Commission Regulation (EU) 2017/460 of 16 March 2017, establishing a network code on harmonized tariff structures for gas (NC TAR) into the Dutch tariff code regulation. Individually, OMV, Uniper and Orsted have been active in the implementation discussions that have taken place over the last year.

In December 2007, the final investment decision was taken to construct and operate a LNG terminal in the Netherlands. Since then GATE has received support from key political stakeholders and has always been perceived to be an integrated element of the future Dutch and continental Europe gas market.

The terminal's construction was, and remains fully in line with both Dutch and European energy policies, built on the pillars of strategic diversification of LNG supplies, safety and environmental awareness. Production of natural gas in northwest Europe, including the Netherlands, is declining and more gas will have to be imported via pipeline gas or as liquefied natural gas (LNG) in the future.

The recently established LNG association VERENIGING LNG SHIPPERS NEDERLAND with its above-mentioned founder companies share a common interest as long-term shippers and investors in the GATE LNG terminal.

As you are aware, these companies have been active for a long time in the Dutch gas and energy market supplying natural gas to the TTF, the most liquid hub in Europe. Over the years we have made significant long-term investments in infrastructure and have made long term transport capacity commitments as required

by GTS at that time. Our annual gas transport commitments are in the order of several million Euro's per company and the current ACM proposal of how to allocate the transportation costs will lead to a significantly higher exposure. As materially impacted parties, we therefore have a strong interest in the outcome of the current ACM proposal.

The implementation of NC TAR and the setting of tariffs is based on a number of principles as laid down in the EU Regulation 715/2009. These include cost reflectivity, providing incentives for investment, facilitating efficient trade and competition, transparency, interoperability, non-distortion of cross border trading, benchmarking and promotion of gas market liquidity. Furthermore, under Dutch administrative law a number of general principles of good administration are laid down and shall be considered when making any such a major decision. These principles are partly codified in the General Administrative Act (Awb), including the principle of careful preparation (section 3:2 Awb), the principle of proportionality (section 3:4 Awb), and the principle of proper reason (section 3:46 Awb). Whilst we are supportive of some of the changes proposed by ACM, such as the decision to apply a postage stamp mechanism, we have two significant disagreements.

Firstly, we disagree with the proposal to apply an Entry/Exit split of 50/50. We found that GTS's in-depth analyses and arguments for a 0/100 split (as opposed to current 35/65) well reflected the particular needs of the Dutch gas market. In our view, this 0/100 split would safeguard Dutch security of supply, maintain TTF liquidity, safeguard its fundamental role as price reference point for Europe's gas markets and would help maintain high transit flows. Moreover, the external analysis conducted by Brattle showed that this Entry/Exit split would also lower the overall cost for Dutch end consumers, which we are sure you will agree is a key issue to consider. The Brattle study was conducted before the unfortunate earth quakes in early 2018 and the subsequent ministerial decree to further reduce Groningen production and finally to cut it to zero until 2030. In the light of this recent decision and the need to secure Dutch gas supplies into the future, we assume that the outcome of the Brattle study would be even more supportive of a 0/100 Entry/Exit split.

VERENIGING LNG SHIPPERS NEDERLAND supports GTS's views and position on the need for a 0/100 Entry/Exit split. By not only rejecting this proposal, but also moving in the opposite direction from the current split and therefore further unduly increasing the GATE tariffs compared to today, the draft ACM decision significantly weakens the competitive position of the GATE LNG terminal. We are concerned that this will make trade less efficient, less competitive and ultimately reduce Dutch gas market liquidity.

Secondly, we disagree with ACM's view that at present there is no reason to initiate a tariff benchmark pursuant to Article 6 (4) a of TAR NC. We will set out the reason for our disagreement in a separate section of this letter below.

In terms of benchmarking, we also disagree with ACM's decision not to consider an LNG discount pursuant to Article 9 (2) of TAR NC since we are of the opinion that GATE LNG does promote Security of Supply for the Netherlands as well as for neighboring countries.

Security of Supply as well as the impact on competition are critical issues when making a tariff decision for a 5-year period. We have already expressed our more detailed view on both aspects earlier in the NC TAR implementation process, as set out in our individual letters to ACM and GTS in June 2017.

In order not to harm competition in the Dutch LNG market and to ensure Security of Supply as a function of competitiveness, we request that ACM applies benchmarking principles for determining the Entry tariff at Gate pursuant to Article 6 (4) a of TAR NC. Entry tariffs should be benchmarked with competing LNG Terminals such as Zeebrugge LNG. Our points of view are further elaborated in the following sections.

Under NC TAR, we would like to make it clear that there is no obligation to apply a 50/50 split for a postage stamp methodology, only for the counterfactual. EU Regulations stipulate a range of principles (cf. article 13 of Regulation 715/2009) that should be considered, including:

1.) Cost reflectivity

This principle requires a clear view and analysis on how costs are built up and how they should be divided. ACM did not provide any analysis supporting their proposal. ACM assumes that Entry/Exit costs are divided 50/50. However, the following analysis clearly demonstrates that a cost reflective Entry/Exit split is not met by a 50/50 split.

Cost reflectivity can be based on several criteria, for instance the overall capacity split between Entry and Exit or the total number of Entry and Exit points. This will lead to an Entry/Exit split different to the proposed split. This is demonstrated by the following calculation:

If we refrain from making the above considerations on the actual configuration of the system and only look at the costs, we can consider how the costs of the high pressure transmission network (hogedruk transportnet, HTL-network) and the "regional" transmission network (regionale transportnet – RTL-network) should be divided. When calculating an appropriate Entry/Exit split, we considered the ratio of costs in the GTS HTL system and the RTL system. As the RTL system is designed for distribution use (only 2 entry points and 415 Exit points) and gas cannot move from the RTL to the HTL system, it seems fair to assume that costs related to the RTL system should be allocated to the Exits. Even though the number of Exit points and overall capacity in the HTL system is larger for Exit than for Entry, we assume that the HTL system is split 50/50 between Entry and Exit.

GTS has reported the costs for the HTL and RTL system separately in the annual reports of 2016 and 2017 for GTS (HTL) and GGS (RTL), as detailed on the GTS website. The value of the asset base is published on the balance sheet and the depreciation costs are published on the profit and loss account. The annual Capex cost can be calculated by applying the relevant WACC. OPEX is published on the profit and loss account under "Other operating expenses". By adding the OPEX to the CAPEX we can find the total costs for GTS and GGS. We then assign the GTS costs to both Entry and Exit, whereas the GGS costs are fully assigned to Exit. From this, an Entry/Exit split can be determined as illustrated in the Table 1 below (2017 numbers).

Table 1: Cost of the HTL & RTL system (million € - WACC of 4% – without storage discount)

	HTL System (50/50 Entry/Exit)	RTL system (100% Exit)	Entry %	Exit %
Capex	390	80		
Opex	560	169		
Total	949	249	39%	61%

The above example shows that even when only applying the principle of cost reflectivity, the Entry/exit split should be a maximum of 39/61%.

The decision to change to a 50/50 Entry/Exit split will have significant negative economic consequences for the Dutch LNG shippers, and without any substantive reasons not only violates Article 13 of Regulation 715/2009 and section 12f of the Dutch Gas Act, but the principles in the Dutch Administrative Act, including the principle that a decision must be based on proper reasons, careful preparation and proportionality.

2.) Benchmarking

The GATE LNG Entry tariff:

GATE is of key importance for gas supply to the Netherlands and to the wider North West European market. LNG represents one of the main alternatives for global gas supply to the Netherlands that can be used to offset the significant reductions in indigenous production. Furthermore, GATE connects the Dutch gas market with LNG sources worldwide, providing cover for potential shortages if pipeline imports are disrupted. The

GATE LNG terminal helps facilitate the intended role of the Netherlands as the “gas roundabout” of North West Europe (a policy based on Security of Supply arguments).

The supply of LNG to GATE is, however, dependent on cost exposure and due to its flexibility even more so than pipeline supplies. It competes strongly with other LNG facilities in Europe. Looking across the West and South European region the entry-exit split looks more favorable compared to the entry tariff in Netherlands (see Figure 1). In Belgium and France, the split is around 30-70 and according to the DNV-GL study no plans are known on further adjustments. In addition, France are likely to maintain the discount for the LNG terminals of 5% and the absolute entry tariff for the Zeebrugge LNG terminal is much lower than the entry tariff for the GATE terminal (see Figure 2).

Figure 1: Entry-exit split in six EU countries (Source: DNV-GL Study on the implementation status of NC TAR, 2017)

	Belgium	Denmark	France	Germany	Ireland	United Kingdom
Expected PRM	Similar as current methodology as it resembles the CWD methodology	Move to postage stamp model	CWD methodology is currently implemented. No changes are expected	Move to postage stamp model	No changes are foreseen to recently (2015) introduced matrix methodology, but this still subject to consultations.	Move to CWD methodology. Current LRMC method seen as too volatile, unpredictable and unstable.
Entry-exit split	30-70 split No plans to adjust this split.	Not predefined	35-65 split to stay in place	Not predefined	33-67 split was motivated during the previous tariff reform. No indications this will change with implementing TAR NC.	No changes expected. Current target is 50-50

Figure 2: Tariffs for transmission services of Fluxys (Source: http://www.fluxys.com/belgium/en/Services/Transmission/TransmissionTariffs/~media/Files/Services/Transmission/Tariffs/2018/tariff_sheet_2018_transmission_ENv2.ashx)

Tariffs for transmission services of Fluxys Belgium SA (*)

For year 2018 (*)

Tariffs for yearly capacity reservation

<u>Entry Interconnection Point</u>	Capacity tariff in €/kWh/year		
	Firm	Interruptible	Backhaul
Alveringem	0,732	0,586	
Dunkirk LNG Terminal	0,732	0,586	
Eynatten 1	0,732	0,586	
Eynatten 2	0,732	0,586	
IZT	0,732	0,586	
Loenhout	0,732	0,586	
Hilvarenbeek L	0,845	0,676	
's Gravenvoeren	0,732	0,586	
Virtualys	0,732	0,586	0,586
Zandvliet H	0,732	0,586	
Zeebrugge	0,732	0,586	
Zeebrugge LNG Terminal	0,732	0,586	
Zelzate 1	0,732	0,586	
ZPT	0,732	0,586	
Blaregnies L			0,676
Blaregnies Segeo / Blaregnies Troll	0,732		0,586
Zelzate 2			0,586

In the UK, the current proposal of the TSO (National Grid) foresees the special treatment of all existing long-term entry capacity bookings. This is to maintain the current “price protection” of existing Entry capacity bookings, in accordance with Article 35 of NC TAR. The final transportation tariff arrangements are still

under discussion but if, as expected, the Regulator approves the price protection for existing Entry capacity bookings, with the potential for a zero-top-up charge for these historical contracts, all of the UK LNG terminals will have much more favorable entry conditions than GATE. Therefore, in our opinion the GATE shippers are facing an uneven playing field compared to neighboring countries.

Since NC TAR furthermore states that "in order to promote security of supply, the granting of discounts should be considered for entry points from LNG facilities", we strongly believe that postponing such benchmarking (and postponing the possible application of a discount for LNG entry points) to a later stage is, based on the current facts and circumstances known to ACM and based on the comparative table above, not only in violation of NC TAR, but is also contrary to the aforementioned general principles of proper administration.

3.) Tariffs shall provide incentives for investments in gas transmission

EU Regulation 715/2009 stipulates that the tariff system shall provide incentives for new investments and interoperability. GTS is responsible for making the investments, but GTS has required that market participants underwrite the investments via long term commitments (entry bookings) and consequently are forced to accept the full risk for changes in the cost of the system. For such a system to work efficiently, it is imperative that market participants can rely on a stable and predictable regulatory environment where changes are only made after careful consideration and must be well justified. If changes are made, they should be proportionate and non-discriminatory and based on fair and transparent principles. If not, such changes can increase regulatory uncertainty, undermining investor confidence and potentially leading to a hiatus in investment – either in existing or new infrastructure. Shippers would be unlikely to make such long-term commitments in the first place, if there is a high level of uncertainty over future cost exposures.

For GATE shippers, the Entry cost has already increased more than 30% since 2012 and with the proposed ACM decision, the cost will have almost doubled by 2020. This is clearly not in line with the objective of providing incentives for investments in future gas transmission, if shippers cannot rely on a stable and predictable regulatory regime. Furthermore, we believe that this decision is contrary to the principles of the General Administrative Act (proportionality) to implement the shift in Entry/Exit split, without properly considering the impact on long-term investments made via capacity bookings.

Conclusion

VERENIGING LNG SHIPPERS NEDERLAND asks ACM to take due account of the above considerations in drafting their final decision implementing the NC TAR and lower the proposed Entry/Exit split of 50/50. By considering in more detail the issues cost-reflectivity in terms of Entry/Exit costs, transparency and employing benchmark regulation to LNG Entry points, we believe that a more appropriate Entry/Exit split can be found which better meets the unique needs of the Dutch Gas Market.

We are at your disposal for any clarifications and we look forward to participating in the process also after 28 May 2018.

Signed on behalf of VERENIGING LNG SHIPPERS NEDERLAND:

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