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OMV GAS

Subject: ACM/14/023224

ACM consultation on NC TAR implementation

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Dear Madam / Sir

OMV Gas Marketing & Trading GmbH (OMV Gas) is an active player on the Dutch gas market and has been invited to comment on the draft decision under case number ACM/14/023224. Besides the effort to publish the draft decision, we appreciate ACM's approach to soundly explain its thoughts behind said decision.

Before discussing the decision and its - in our view - largely negative consequences on the currently functioning TTF market area, we would like to express our appreciation for ACM and also GTS to have market participants on board in this process from a very early stage (starting with April 2017). However, we believe that the ACM agrees that the series of workshops in 2017 did not meet the requirements for a consultation in accordance with Article 26 of Commission Regulation 2017/460 (NC TAR) but rather provided market stakeholders with insights as well as with the basis to develop a common understanding on the objectives and requirements of the NC TAR and the subsequent implementation in the Dutch tariff code.

The concept of a 0/100 split was discussed in the presence of the ACM over a period of several months. Shippers and other market stakeholder invested time and efforts to evaluate the impact of such concept, before the ACM expressed its present view on the future tariff structure. Considering, that key elements of the ACM's current draft decision significantly deviate from the majority of market participants' (including GTS') expressed in the course of these informal sessions and the official hearing in May 2018, **we expect the ACM to use the opportunity provided by NC TAR to hold at least one additional consultation round.**
Firstly, the final document, subject to consultation of a matter which is of such significant importance to business cases should widely reflect the opinions of interested market stakeholders. This is not the case. Secondly, for transparency reasons this consultation round has to include figures on forecasted capacity bookings (aggregated "Rekenvolumina" on entry and exit level) until 2024 instead of the currently provided available forecast until 2021.

[redacted]

Those Rekenvolumina can be and should be published by the ACM as described in the explanatory notes (point 70) for the entire 2020-2024 period. Despite not knowing the allowed revenues after 2021, market participants need all information to the extent possible for the entire period under subject in order to be able to assess the impact resulting from the tariff decision and for making their ultimate statements in a final consultation phase.
Thirdly, because of the early start of the process, there is still sufficient time to conduct a further carefully prepared consultation round.

Regardless of uncertainties concerning the formality and currently missing information as mentioned above, OMV Gas has assessed the draft decision and came to the following conclusions:

1) **Reference Price Methodology (RPM):**

OMV Gas generally supports the ACM in its preference to opt for a **postage stamp** RPM and sees broad compliance with the objectives coming from NC TAR Article 7. We see advantages over a CWD approach, particularly in the area of reproducibility and predictability and also simplification (no tariff difference between different categories of entry or exit points). However, the ACM's application of the postage stamp RPM fails to meet several requirements from Article 7 NC TAR because of the following two main reasons:

a) ***Entry/Exit Split***

The impact of the RPM on reserve prices is to the largest extent influenced by the **entry/exit revenue split** considered. ACM proposes to apply a 50/50 entry-exit split which received largely negative feedback in the hearing on May 14th 2018.

Applying a 50/50 split as proposed would lead to a 53/47 tariff ratio [%] in the Netherlands, meaning that in fact the costs to import gas into TTF from any IP import point other than storage is by 6 percentage points higher compared to the GTS Exit costs.
We have compared this result from the envisaged 50/50 split with the actual Entry/Exit tariff ratio in other European countries, namely Germany, Belgium, France, Spain, Czech Republic, Italy and Austria. (Rem: We are happy to share the details and structure of our own analyes with ACM following your request).
The average Entry/Exit ratio based on the reserve price of cross-border points in these countries equals to ~33%/67% which is by 20% (!) lower compared to the Entry/Exit tariff ratio resulting from ACMs draft decision.
We believe that this proposed tariff structure is a strong signal to the market and would become a clear disadvantage for pipeline and LNG imports into the Netherlands. [redacted]

- OMV Gas does not support the ACM's proposed 50/50 split for the following reasons:

    - Preamble 10 of NC TAR requires tariff structures to avoid downstream market foreclosure. Though it is clearly not the intention of ACM to substantially limit imports into the Netherlands in the long-run, it is beyond doubt, that artificially and excessively high entry tariffs would lead to a lower number of companies being able or willing to supply the TTF market area and its customers.
    - The ACM has provided no analysis why it has chosen a 50/50 split nor has substantiated its view why TTF or the Dutch gas market in its entirety will have the highest benefit from a 50/50 split compared to other revenue allocation splits.
    - The ACM has brought forward that a 50/50 split represents an equal and balanced distribution of costs and hence results in the most accurate cost-reflectivity. However, this assumption is not backed by any assessment nor cost analyses and hence ACM missed in our view to demonstrate that this split meets the requirements and targets of TAR NC best.
    - As a consequence of the scenario that TTF becomes an isolated market served by only a few suppliers due to entry barriers set by regulation, liquidity could move to adjacent markets where access conditions are commercially more attractive.
    - Inappropriately high Entry tariffs not just put market liquidity at risk but also tend to harm Security of Supply ("SoS").

- OMV Gas has from an early stage supported the proposed 0/100 split suggested by GTS for the following reasons:

    - The Brattle study clearly demonstrated that zero entry fees have a lowering effect on end-consumer prices, which we believe should be in the interest of the ACM and the Dutch end-consumers.
    - Additional analysis by GTS provided evidence that low or zero entry tariffs – at the expense of exit tariffs – result in low transit costs. Article 7 (e) of NC TAR requires an RPM which does not distort cross-border trading. Keeping overall transit fees as low as possible ideally complies with this provision. In addition, EC 2009/715 Article 13 (2) requires that tariffs "shall neither restrict market liquidity nor distort cross-border trade". The former requirement is logically met by zero or very low entry tariffs, while the latter is, in line with GTS' analysis, provided by the lowest possible transit costs.
    - The ACM has stated in its explanatory notes to the draft decision (note 68) that "attracting gas flows to the Netherlands cannot be regarded as being in the general public interest". Supported by supply/demand forecasts which predict the Dutch market to become soon a significant net importer, we believe –

contrary to ACM – that attracting gas flows to the Netherlands will be of utmost public interest.

- Zero or low entry fees are essential to protect liquidity on TTF. Linear modelling as provided by ACM (workshop from Nov 27 2017) wrongly assumes that the split of the overall cost of entering and exiting the market has no impact. We believe a cheap or even free possibility to enter the GTS grid without being exposed to upfront costs motivates traders to use TTF as the gateway to either supplying end-consumers or supplying adjacent market areas. Domestic customers will directly benefit from liquidity and GTS will face no risk in recovering allowed revenues from exit capacity bookings.

- Furthermore many wholesale companies supplying end-consumers face limitations to actively source gas from abroad and therefore continue to rely on ample and liquid supplies available directly on the TTF hub.

b) Transmission vs Non-Transmission Services

The key parameters to establish a robust RPM are derived from the separation between **transmission vs. non-transmission services**. ACM's treatment of non-transmission services as transmission services is unfortunately arbitrary.

- OMV Gas opts for **quality conversion** (QC) to be treated as non-transmission service with a perfectly cost-reflective and objective distribution on only L-gas exit capacity in order to minimize undue cross-subsidization.
- Different to the view of the ACM presented in the current draft decision, we think that the task of QC must not be regarded as transmission service because:
  - It results in substantial lack of cost-reflectivity
  - It would in no way fulfil the provision from Article 7 (b) of NC TAR to "Consider the level of complexity while taking into account the actual costs incurred". This aim can only be met if the cost for quality conversion is imposed exclusively on L-Gas Exits. Quality Conversion may as well be covered with a usage (=commodity) based fee on L-Gas exits if it provides a more cost-reflective approach compared to a capacity based fee. However, the aim of predictability favors in our view the socialization of a capacity-based fee for QC over a commodity based charge on L-Gas exits.
  - The ACM draft decision provides no predictability for a period beyond the next calendar year in regards to QC. Especially H-Gas Open Season contracts concluded over ten, twenty or more years will continue to be unduly affected because of ongoing and upcoming investments related to the L-Gas shortage. Such investments, like the planned Zuidbroek [redacted]

nitrogen plant, will increasingly impact the asset base as a result of the intention to reduce Groningen-Gas production to zero and thus boost physical conversion demand from L-Gas shippers. This high degree of non-predictability shall be limited to those network users which are triggering conversion-related investment. This consequently should result in a distribution of quality conversion costs solely across network users booking L-Gas (exit) capacity.

- In the explanatory notes (note 31) to the draft decision the ACM explains its non-consideration of **WQA as a transmission service**. While the principle of QC and the WQA-service is the same (in both cases nitrogen is injected to lower the Wobbe-index), from a legal point of view WQA-service does currently not qualify as transmission service nor non-transmission. service because it does not fulfill the precondition under Article 4 (1b) NC TAR. Gate LNG importers currently pay for the non-regulated WQA service as well as for the socialised QC as part of the LNG Entry tariff. QC is a socialized fee since 2009 and has been introduced after the investment decision in WQA. In order to repair this undue and overdue structural impairment on the accounts of LNG importers, OMV Gas asks the ACM to consult on WQA in accordance with the last sentence of Article 4 (1) NC TAR in order to determine whether WQA should be included in the set of transmission or non-transmission services. This would consequently authorize the ACM to regard it as transmission service based on the last sentence of Article 4 NC TAR.

- In the explanatory notes (note 31) to the draft decision the ACM explains its non-consideration of WQA as a transmission service. Gate LNG importers currently pay for the non-regulated WQA service as well as for the socialised QC as part of the LNG Entry tariff. QC is a socialized fee since 2009 and has been introduced after the investment decision in WQA, which is why LNG importer face an undue and overdue structural impairment.
  While the principle of QC and the WQA-service is the same (in both cases nitrogen is injected to lower the Wobbe-index), from a legal point of view WQA is treated as an individual service and hence does not qualify or can be regarded as transmission service. WQA does at the moment not fulfill the precondition under Article 4 (1b) NC TAR and OMV Gas therefore asks the ACM to consult on WQA in accordance with the last sentence of Article 4 (1) NC TAR in order to determine whether WQA should be included in the set of transmission or non-transmission services. This would consequently authorize the ACM to regard is as transmission service based on the last sentence of Article 4 NC TAR, and thus WQA could be treated equally to how ACM currently regards QC. [redacted]

- The allocation of **balancing costs** to transmission services in the highly complex GTS grid is in our view not sufficiently and transparently cost-reflective but it may provide for practical reasons a sufficient solution to allocate the costs for that service via capacity-based transmission tariffs.

Overall OMV Gas welcomes the application of the postage stamp RPM but the underlying factors and parameters – mainly the entry/exit split and a misconceptional consideration of transmission services – lead to results neither desired by NC TAR nor by Regulation 2009/715.

OMV Gas has identified other weaknesses in the draft decision which we will explain in the following and ask the ACM for re-assessment and clarification.

2) Adjustments according to Article 6 (4) NC TAR

- Article 6 (4) of NC TAR provides reasonable tools to combine the reference price methodology and harmonized calculation principles for transmission tariffs with the specific national requirements to meet market characteristics. In our view **benchmarking** needs to be employed to adjust reserve prices at network points where the RPM results in obviously non-competitive reserve prices. The ACM argues that there is no need for benchmarking without having substantiated its decision.
- The Dutch market as a future net importer provides for such specific characteristics and therefore benchmarking shall be applied to major import points connecting non-EU countries as well as to LNG Entry. Different to the opinion of the ACM as expressed in point 68 of the explanatory notes, we think that attracting gas flows to the Netherlands is of utmost public interest. We believe that the TTF market entries (widely independent from the final Entry/Exit split but in any case when applying the envisaged RPM with a 50/50 split) require necessary corrections through benchmarking so that especially the major sources from outside the European Union are being directed towards TTF.

3) Adjustments of Tariffs according to Article 9 (2) NC TAR

- OMV Gas partly shares the ACM's general view not to aim for importing gas at the expense of other European transmission systems (explanatory notes 68). We therefore assume that the ACM regards the LNG discount in accordance with Article 9 (2) NC TAR as a European instrument to strengthen overall SoS across the internal energy market. LNG cargoes contributing to European SoS have to tackle the hurdle to comply with higher quality specifications compared to many other destinations. We therefore suggest that a discount should consequently be granted to all European LNG entries in order to compete with LNG importers outside the European Union with the aim of increasing SoS on a European scale. We ask the ACM to consider this approach and take the leading role in introducing a discount in accordance with Article 9 (2) NC TAR. [redacted]

4) Discount on Interruptible Capacity

- OMV Gas - in line with many other market players - is of the opinion that interruptible capacity has a different value than firm capacity and therefore asks the ACM to apply **an ex-ante discount**. It is up to market players to assess whether the discount reflects the commercial risk coming from the lower quality of the capacity product before deciding whether to book it or not.
- The ex-ante discount needs to be combined with the unconditional marketing of interruptible capacity on a day-ahead basis in order to enhance TSOs' capacity sales and shippers' flexibility. This is in line with Art 32 (1) of NC CAM (2017/459) and common practice in other European markets, for instance Germany or Austria.
- The ex-post discount as proposed by ACM does not reflect the value of interruptible capacity. The remuneration for factual interruptions does not cover the commercial losses (imbalances etc.) on both affected markets in case of an interruption.

5) Short-term factors & Seasonality factors

- OMV Gas believes that the **short-term multipliers** proposed by ACM are too high.
    - We believe that the short-term factors proposed by the ACM and especially the 2.5 daily multiplier are in no means reflecting the actual cost of shorter-term capacity but significantly impede the short-term trading activities on TTF and even neighboring trading points.
    - The NC CAM auction calendar only offers limited possibilities for network users to book capacity products with duration longer than one day. We see a significant risk of an overall reduction in bookings as a result of high short-term multipliers since a majority of market participants is booking capacity only on short-term basis to cover their flexibility demand.
      While trading opportunities may be limited by high short-term tariffs, suppliers may abuse the national transmission system to balance their sales related offtake portfolio instead of sourcing the flexibility in adjacent markets or from storage assets.
    - OMV Gas does expect a negative impact from high short-term factors, since trading volumes and liquidity will likely be shifted to markets where short-term multipliers are at more reasonable levels.

- OMV Gas does not see a necessity for **seasonal factors** at all.
    - It has been observed for years that the utilization of the high pressure gas grids, including the one of GTS, does not just depend on the seasonal supply and demand profile but is often even more influenced by market prices, different trading strategies and the dynamics and volatility of the global energy [redacted]

markets. The combination of the daily short-term multiplier [2.5] with the season winter factor [e.g. January = 1.83] results in a daily Entry tariff of 0.92 EUR/MWh(!). Just as an example, the same products costs 0.595 EUR/MWh with the neigbouring German TSO Open Grid Europe.

Once more and by using this example of excessively high short-term entry (and exit) costs, we want to create awareness that the tariff structure as proposed by ACM will significantly distort cross-border trading and negatively influence Europe's currently most liquid and reference gas market TTF.

To conclude our analysis of the ACM's draft decision, we would like to state that the decision largely complies with NC TAR but significantly fails to meet the targets and objectives desired from NC TAR and regulation 2009/715.
We strongly urge the ACM to modify the draft decision concerning the following components:

- Adjust the entry/exit split: In the absence of fundamental evidence provided to support the ACM's 50/50 approach, OMV Gas opts for a significant shift of the entry/exit split towards cheap entry capacity fees.
- Eliminate the undue socialization of quality conversion across H-Gas network points
- Apply benchmarking in accordance with NC TAR Article 6 (4) for major import points such as GATE LNG
- Reconsider the pricing of shorter-term and interruptible products.

Being a long-term capacity holder and having made significant contributions to Dutch SoS, market liquidity and investments in infrastructure, OMV Gas expects a tariff system that provides stability, fairness, cost-reflectivity and predictibility. OMV Gas also expects a tariff structure which does not harm the leading role of TTF compared to other European hubs. The implementation of NC TAR in the Netherlands will lead to drastic changes but must not result in undue discrimination of long-term capacity holders. If the ACM's final tariff decision leads to significant negative economic consequences for long-term contract holders, we expect a mechanism that grants shippers the right to terminate existing long-term capacity contracts.

OMV Gas is happy to remain at your disposal regarding the further development on this process. In case you have further questions or comments please contact Mr. [redacted] ([redacted]@omv.com; +43 (0) [redacted])

With best regards

OMV Gas

[redacted]