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## Agency Report

# Analysis of the Consultation Document on the Gas Transmission Tariff Structure for Lithuania

NRA: Valstybinė kainų ir energetikos  
kontrolės komisija (National Commission  
for Energy Control and Prices)

TSO: AB Amber Grid

3 July 2019

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## 1. ACER conclusion

- (1) The Lithuanian National Regulatory Authority ('NRA'), Valstybinė kainų ir energetikos kontrolės komisija ('VKEKK'), proposes a postage stamp reference price methodology ('RPM') with a 70/30 entry-exit split<sup>1</sup> for the regulatory period 2020-2023. VKEKK proposes to apply a discount of 75% to entry at the Lithuanian LNG terminal. VKEKK performs two kinds of asset cost splits: one for high pressure distribution branches<sup>2</sup> and another one for the transit from third country to third country<sup>3</sup>. Given this situation, VKEKK proposes several provisions modifying the usual postage stamp RPM:
  - The assets of the primary network and of the local network are identified and valued separately. The capacities of the primary network would be offered as transmission services, while the capacities of the local network would be offered as non-transmission services.
  - The district of Kaliningrad would be supplied from Belarus by dedicated point-to-point products.
  - A commodity-based transmission tariff would be used to recover the TSO's variable costs.
- (2) VKEKK proposes in its consultation two different tariff setting scenarios. In the first scenario, the Lithuanian transmission tariff is designed without taking into account the regional integration process. In the second scenario, VKEKK proposes to adjust its RPM to promote regional integration (notably with a zero tariff between Lithuania and Latvia).
- (3) The Agency, after having completed the analysis of the consultation document pursuant to Article 27(2) of Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a Network Code on Harmonised Transmission Tariff Structures for Gas ('NC TAR'), concludes that:
  - The consultation document contains the required information listed in Article 26(1) of the NC TAR;
  - The choice of the postage stamp methodology as the proposed RPM might overall be compliant with the requirements set out in Article 7 of the NC TAR, but some additional information would be necessary for the Agency to be able to confirm that the proposed tariffs are cost-reflective;
  - The results of the cost allocation assessment ('CAA') and of the comparison with the counterfactual Capacity Weighted Distance ('CWD') methodology show the unit costs applied to determine tariffs of the cross-border capacities from Belarus to the Kaliningrad district are significantly lower than the average unit cost of the domestic transmission system;
  - The proposals to promote regional integration (Scenario 2) seem acceptable on a provisional basis. Nevertheless, the Agency considers that, in the long term, a cost-benefit analysis is necessary to establish a sustainable and fair inter-TSO compensation ('ITC') mechanism between the countries of the region.

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<sup>1</sup> This entry-exit split is used as an input in the RPM. The actual entry-exit split, resulting from various adjustments to the RPM, is approximately 46/54.

<sup>2</sup> The Lithuanian TSO operates both a primary network and a local network (high pressure distribution branches)

<sup>3</sup> To transport gas from Belarus to the Kaliningrad district of the Russian Federation.

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- The simplified tariff model is in line with the requirements of Article 30(2)(b) of the NC TAR;
  - Network users would be able to reproduce and forecast the reference prices using the tariff model provided in the consultation document;
  - While the non-transmission tariffs applied to the local network seems cost-reflective, these services should be rather classified as transmission or as distribution services, based on Article 2(5) of Directive 2009/73/EC<sup>4</sup>. In both cases, these services should be priced in a non-discriminatory manner, regardless of the network users' size or consumption.
- (4) The Agency recommends that, in its final decision, VKEKK take into consideration the following:
- Additional transparency (age of assets, level of depreciation...) should be provided to justify the lower unit cost applied to determine the tariffs of the cross-border capacities from Belarus to the Kaliningrad district.
  - Only one reference price should be applicable at the Kotlovka entry from Belarus. The point-to-point product allowing to transport gas across Lithuania to the Russian district of Kaliningrad should be considered as a conditional capacity product and its tariff should be set by applying a discount to the reference price (calculated by the RPM for the firm, freely allocable, yearly capacity product).
  - The use of the local transmission network should be either considered as a transmission service or reclassified as a distribution service if the RPM cannot properly allocate the costs of the regional branches to the relevant network users. The application of different tariffs, depending on the size of the consumers, would be considered discriminatory.
  - The choice between the two tariff proposals (Scenarios 1 and 2) presented in the public consultation must be justified. While the Scenario 2 does not strictly comply with the NC TAR at a national scale, it is clearly a positive step towards regional market integration.
  - In this perspective, the Agency recommends that VKEKK and the FINESTLAT NRAs set a deadline for the implementation of a regional transmission tariff in line with the NC TAR. The ITC mechanism and possibly, at a later stage, a common RPM should be based on a cost-benefit analysis to allocate the costs and the benefits of the regional gas infrastructure in a homogenous and effective manner.

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<sup>4</sup> Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, OJEU L-211 of 14 August 2009.

## 2. Introduction

- (5) Commission Regulation (EU) 2017/460 of 16 March 2017 establishes a network code on harmonised transmission tariff structures for gas ('NC TAR').
- (6) Article 27 of the NC TAR requires the Agency to analyse the consultation documents on the reference price methodologies for all entry-exit systems<sup>5</sup>. This Report presents the analysis of the Agency for the transmission system of Lithuania.
- (7) On 5 March 2019, VKEKK forwarded a consultation document to the Agency proposing a RPM for the Lithuanian transmission system for the period 2020-2023. The consultation was launched on the same day and remained open until 6 May 2019. On 3 June 2019, the consultation responses and their summary were published. The Agency has taken these into consideration for this analysis. Within five months following the end of the final consultation, and pursuant to Article 27(4) of NC TAR, VKEKK shall take and publish a motivated decision on all the items set out in Article 26(1) of the NC TAR.
- (8) The VKEKK consultation includes two alternative tariff proposals, to take into consideration recent regional developments, in particular the expected creation of the adjacent market zone comprising Finland, Estonia and Latvia ('FINESTLAT')<sup>6</sup>. In the first proposal, the postage stamp RPM is established independently of the neighbouring systems. In the second proposal, the RPM is adjusted by setting zero tariffs at Kiemėnai IP between Lithuania and Latvia. This Report assesses both tariff proposals, namely Scenarios 1 and 2.
- (9) For their part, the Finish, Estonian and Latvian authorities plan to base their integration project on several tariff adjustments, but do not intend to harmonise their respective RPM:
  - they would set zero tariffs at IPs within the FINESTLAT region,
  - they would equalise the tariff at their respective entries at external border points of their market zone,
  - they would implement an ITC mechanism to allocate the revenues from these entries proportionally to the consumption of each country of the region.
- (10) A number of bilateral exchanges to collect additional information took place between the Lithuanian NRA and the Agency. VKEKK provided clarifications in a timely manner following the requests of the Agency. The Agency appreciates the interactions with VKEKK during this process.
- (11) This Report discusses both the RPM and the accompanying information published in the public consultation document, and the new information provided by VKEKK during bilateral discussions.

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<sup>5</sup> With the exception of Article 10(2)(b), when different RPMs may be applied by the TSOs within an entry-exit zone.

<sup>6</sup> More information about this process of regional integration is available on VKEKK's website: <https://www.regula.lt/en/Pages/Updates/Results-of-the-regional-study-on-calculating-natural-gas-transmission-service-tariffs-presented.aspx>. In particular, the NRAs of Finland, Latvia, Estonia and Lithuania agreed to appoint Baringa Partners LLP to undertake a study on the best RPM for calculating the transmission tariffs across the region: <https://www.regula.lt/SiteAssets/naujienu-medziaga/2018/2018-gruodis/Tariff%20model%20for%20the%20natural%20gas%20entry-exit%20system%20for%20the%20common%20Baltic-Finnish%20market%20Baringa%20Phase%202%20Report%20Final%20V3%201.pdf>.

The public consultation on the transmission tariffs launched by the Estonian NRA also refers to this regional integration process: <https://www.konkurentsiamet.ee/index.php?id=18309>

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### Reading guide

- (12) Chapter 3 presents the analysis on completeness, namely whether all the information referred to in Article 26(1) of the NC TAR has been published. Chapter 4 focusses on compliance, namely whether the RPM complies with the requirements set out in Article 7 of the NC TAR, whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) are met, whether the criteria for setting non-transmission tariffs as set out in Article 4(4) are met and whether the criteria for setting fixed payable prices as set out in Article 25 are met. Chapter 5 includes recommendations to progress the tariff setting at the regional level. The document contains two annexes, respectively on the legal framework and a list of abbreviations.

## 3. Completeness

### 3.1 Has all the information referred to in Article 26(1) been published?

- (13) Article 27(2)(a) of the NC TAR requires the Agency to analyse whether all the information referred to in Article 26(1) of the NC TAR has been published.
- (14) Article 26(1) of the NC TAR requires that the consultation document be published in the English language, to the extent possible. The Agency confirms that the consultation document was published in English.
- (15) Overall, the information in Article 26(1) of the NC TAR has been properly published.

Table 1 Checklist information Article 26(1)

Article	Information	Published: Y/N/NA
<b>26(1)(a)</b>	the description of the proposed reference price methodology	Yes
<b>26(1)(a)(i)</b> <b>26(1)(a)(i)(1)</b> <b>26(1)(a)(i)(2)</b>	the indicative information set out in Article 30(1)(a), including: <ul style="list-style-type: none"> <li>the justification of the parameters used that are related to the technical characteristics of the system</li> <li>the corresponding information on the respective values of such parameters and the assumptions applied</li> </ul>	Yes
<b>26(1)(a)(ii)</b>	the value of the proposed adjustments for capacity-based transmission tariffs pursuant to Article 9	Yes
<b>26(1)(a)(iii)</b>	the indicative reference prices subject to consultation	Yes
<b>26(1)(a)(iv)</b>	the results, the components and the details of these components for the cost allocation assessments set out in Article 5	Yes
<b>26(1)(a)(v)</b>	the assessment of the proposed reference price methodology in accordance with Article 7	Yes
<b>26(1)(a)(vi)</b>	where the proposed reference price methodology is other than the capacity weighted distance reference price methodology detailed in Article 8, its comparison against the latter accompanied by the information set out in point (iii)	Yes
<b>26(1)(b)</b>	the indicative information set out in Article 30(1)(b)(i), (iv), (v)	Yes
<b>26(1)(c)(i)</b> <b>26(1)(c)(i)(1)</b>	where commodity-based transmission tariffs referred to in Article 4(3) are proposed	Yes

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<p><b>26(1)(c)(i)(2)</b></p> <p><b>26(1)(c)(i)(3)</b></p>	<ul style="list-style-type: none"> <li>• the manner in which they are set</li> <li>• the share of the allowed or target revenue forecasted to be recovered from such tariffs</li> <li>• the indicative commodity-based transmission tariffs</li> </ul>	
<p><b>26(1)(c)(ii)</b></p> <p><b>26(1)(c)(ii)(1)</b></p> <p><b>26(1)(c)(ii)(2)</b></p> <p><b>26(1)(c)(ii)(3)</b></p> <p><b>26(1)(c)(ii)(4)</b></p>	<p>where non-transmission services provided to network users are proposed:</p> <ul style="list-style-type: none"> <li>• the non-transmission service tariff methodology therefor</li> <li>• the share of the allowed or target revenue forecasted to be recovered from such tariffs</li> <li>• the manner in which the associated non-transmission services revenue is reconciled as referred to in Article 17(3)</li> <li>• the indicative non-transmission tariffs for non-transmission services provided to network users</li> </ul>	<p>Yes. However, the Agency disagrees with the classification of local networks as non-transmission services (see section 4.3).</p>
<p><b>26(1)(d)</b></p>	<p>the indicative information set out in Article 30(2);</p>	<p>Yes</p>
<p><b>26(1)(e)</b></p> <p><b>26(1)(e)(i)</b></p> <p><b>26(1)(e)(ii)</b></p> <p><b>26(1)(e)(iii)</b></p> <p><b>26(1)(e)(iv)</b></p>	<p>where the fixed payable price approach referred to in Article 24(b) is considered to be offered under a price cap regime for existing capacity:</p> <ul style="list-style-type: none"> <li>• the proposed index;</li> <li>• the proposed calculation and how the revenue derived from the risk premium is used</li> <li>• at which interconnection point(s) and for which tariff period(s) such approach is proposed</li> <li>• the process of offering capacity at an interconnection point where both fixed and floating payable price approaches referred to in Article 24 are proposed</li> </ul>	<p>Not applicable</p>

## 4. Compliance

### 4.1 Does the RPM comply with the requirements set out in Article 7?

- (16) Article 27(2)(b)(1) of the NC TAR requires the Agency to analyse whether the proposed reference price methodology complies with the requirements set out in Article 7 of the NC TAR. This article refers to Article 13 of Regulation (EC) No 715/2009 and lists a number of requirements to be taken into account when setting the RPM. As these overlap, in the remainder of this chapter, the Agency will take a closer look at the five elements listed in Article 7 of the NC TAR.
- (17) As the concepts of transparency, cost reflectivity, non-discrimination, cross-subsidisation and cross border trade are closely related<sup>7</sup>, the Agency concludes with an overall assessment. Special attention is paid to the allocation of revenues between domestic and transit routes.
- (18) While respecting the principles of Article 7 of the NC TAR, VKEKK has to take into account several specificities of the Lithuanian transmission system:

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<sup>7</sup> The principle of cost-reflectivity is related to the principles of cross-subsidisation and non-distortion of cross-border trade. Tariffs that are fully cost-reflective do not result in any form of cross-subsidisation (and hence they do not distort cross-border trade), as they charge users for the exact costs they cause to the system. Following this reasoning, tariffs that are less cost-reflective may result in cross-subsidisation between users.



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- AB Amber Grid owns and operates both a primary transmission network, connected to networks of other countries and to other major gas infrastructure such as the Klaipėda LNG terminal, and a secondary (or local) network solely dedicated to supply gas to Lithuanian consumers.
  - Moreover, due to its geographic position, a part of the Lithuanian transmission network is used both to supply Lithuanian consumers and to transit Russian gas from Belarus to the Kaliningrad district of the Russian Federation.
  - Lastly, VKEKK has to consider the recent regional developments. On the one hand, new gas infrastructures, like the Klaipėda LNG terminal and the future GIPL pipeline connecting Lithuania and Poland, are gradually ending the Baltic states' isolation from the other European gas markets. On the other hand, Finland, Estonia and Latvia are planning to integrate their respective markets into a more liquid, better functioning single market zone, called FINESTLAT<sup>8</sup>. Discussions are on-going between the relevant authorities to agree under what conditions Lithuania could join.
- (19) A postage stamp RPM has been proposed to meet these objectives. In its consultation document, VKEKK justifies this choice because of:
- the topology of the Lithuanian transmission network, which is a gas ring allowing several flow patterns,
  - the variety of possible alternative flow patterns, as gas can enter Lithuania at the Kotlovka entry point from the East (from Russia through Belarus), at the Kiemėnai entry point from the North (Latvia), at the Klaipėda entry point from the West (connection with the LNG terminal), and from 2022<sup>9</sup>, from the South with the commissioning of the GIPL pipeline connecting Lithuania with Poland.
  - a major part of the current transmission network assets was built for diversification and security of supply purposes.
- (20) In the light of the above, VKEKK applies significant additions to the standard postage stamp RPM to take into account the specificities of the Lithuanian transmission network:
- VKEKK identifies separately the costs of the primary network and of the local network. VKEKK proposes to allocate the local network costs entirely to the respective groups of local network users. To allow this deviation from the regular postage stamp RPM, VKEKK designates the use of the local network as a non-transmission service (giving a broad reading to Article 4 of NC TAR).
  - VKEKK splits the transmission costs of the primary network between the costs related to the gas transmission within the European Union and the costs related to the transit of gas from Belarus to the Kaliningrad district of the Russian Federation. The tariff applied to this transit is based on an asset-cost split and on a point-to-point logic (on the basis of Articles 7(d) of the TAR NC on volume risk and 4(2) of the TAR NC on conditional capacity), and does not result from the application of the postage stamp RPM.

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<sup>8</sup> The FINESTLAT market zone will be established gradually: Latvia and Estonia will implement a common market zone in 2020. Finland plans to join the single market zone in 2022 at the earliest.

<sup>9</sup> Expected timeline

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- VKEKK proposes two scenarios in its consultation. In the first scenario (hereafter Scenario 1), VKEKK applies the postage stamp RPM without taking into account the current regional developments. VKEKK presents the second scenario (hereafter Scenario 2) as an intermediate step, aiming at integrating the Lithuanian system into the new regional market, before the regional integration with FINESTLAT. In this scenario, the postage stamp RPM is adjusted by setting zero tariffs at the Kiemėnai IP between Lithuania and Latvia and by equalising entry tariffs with those applied in FINESTLAT.

Table 2: Breakdown of the Lithuanian TSO's allowed revenue.

M€	Estimated allowed revenue in 2020	Share of revenue for capacity based tariffs	Share of revenue for commodity based tariffs
<b>Total TSO's allowed revenue</b>	<b>45.5</b>		
Transmission revenue (primary network)	28.6	25.7	2.9
• <i>Intra-EU transmission</i>		17.6	1.2
• <i>Cross-system use (transit to Kaliningrad)</i>		8.1 to 8.2	1.6
Non-transmission revenue (local network)	16.9	8.4	8.4

### 4.1.1 Transparency

- (21) **Article 7(a)** of the NC TAR requires that the RPM aim at ensuring that network users can reproduce the calculation of reference prices and their accurate forecast.
- (22) The consultation document published by VKEKK is transparent and provides all the information required by the NC TAR. Moreover, VKEKK shared with the Agency detailed calculations allowing a thorough analysis of the comparison between the chosen RPM and the CWD methodology, of the cost allocation assessment<sup>10</sup> and of the main components of the allowed revenue. In particular, VKEKK provided detailed calculations for each of the two scenarios and made it possible to isolate the effect of the specific tariff applied to the transit to the Kaliningrad district.
- (23) The Agency considers that the dataset and the simplified tariff model published by VKEKK allow network users to understand and reproduce the reference prices and their forecast from 2020 to 2023. In addition, network users can change the input variables and input their own assumptions. When issuing its final tariff decision, VKEKK should however publish an updated set of data and a new version of the simplified tariff model, taking into account the latest data available regarding the

<sup>10</sup> Throughout this document, 'CAA' is used to refer to the capacity cost allocation comparison index described in Article 5(3)(c) of NC TAR.

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applicable transmission tariffs in FINESTLAT<sup>11</sup>. More generally, all the information required in Article 30 of the NC TAR will have to be published<sup>12</sup> and the level of detail provided should be consistent with the level of complexity of the RPM and along the diversified treatment of the assets in the RPM.

- (24) The Agency finds the simplified tariff model in line with the requirements of Article 30(2)(b) of the NC TAR.
- (25) VKEKK published, on 3 June 2019, the responses to the public consultation and their summary in English. In addition, VKEKK published its evaluation of these responses, which is considered by the Agency as a best practice.
- (26) The Agency considers the RPM proposed by VKEKK to be complex and the responses to the public consultation corroborate this assessment. According to VKEKK, this complexity responds to the particularities of the Lithuanian situation, as described in paragraph 19. The Agency warns that this complexity may constitute a barrier to entry into the Lithuanian market. Although this is not a transparency issue *per se*, the Agency encourages VKEKK to simplify its RPM and to limit the number of changes from one regulatory period to another.
- (27) The Agency recommends that VKEKK publish, in a user-friendly-manner, information regarding the other charges collected by the Lithuanian TSO that do not contribute towards its allowed revenue (in particular the security of the supply fee recovered on behalf of the LNG terminal operator).

### 4.1.2 Cost-reflectivity

- (28) **Article 7(b)** of NC TAR requires the RPM to take into account the actual costs incurred for the provision of transmission services, considering the level of complexity of the transmission network.
- (29) As previously explained, the use of the local network is considered by VKEKK as a non-transmission service. This topic will be discussed separately, in Section 4.3 of this Report.
- (30) Similarly, VKEKK applies a special treatment to the transit of gas from Belarus to the Kaliningrad district. This issue is discussed in detail in Sections 4.1.3 and 4.1.4 of this Report.
- (31) VKEKK proposes to use a postage stamp RPM, which would actually only apply to the parts of the primary transmission network used to ship gas within the European Union. This RPM uses, as an input parameter, entry-exit splits of 70-30 and 68-32 in Scenarios 1 and 2, respectively. These initial entry-exit splits are, nonetheless, modified by several adjustments of the RPM (see Section 4.1.2.2).
- (32) VKEKK proposes to implement commodity-based transmission tariffs during the next regulatory period. The capacity-commodity split would be 90-10.

#### 4.1.2.1 Description of the network

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<sup>11</sup> In particular tariffs at the Kiemėnai IP between Lithuania and Latvia and at all entries from Russia.

<sup>12</sup> Some additional information might be needed to back the complexities of the RPM (e.g. values in the regulated asset base of the local networks, of the assets dedicated to transit gas to the Kaliningrad district and of the other assets of the primary network, WACC, depreciation period and depreciation level for each category of asset...)

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- (33) The primary transmission system network in Lithuania is a ring allowing several flow patterns. It is 1311 km long and consists of 2 cross-border metering stations and pipes with diameters ranging from 150 to 1200 mm.
- (34) The local network, whose aggregate length is 802 km, consists of several regional distribution branches that allow to deliver high-pressure gas to 68 offtake points.
- (35) The Lithuanian transmission network is currently connected to only one Member State, Latvia, through the bi-directional Kiemėnai IP. An additional cross-border IP will be created with Poland once the GIPL pipeline will be commissioned (expected in 2022).
- (36) The transmission network is connected to an LNG terminal at Klaipėda entry point.
- (37) Finally, the Lithuanian network is connected to two third countries at the Kotlovka entry point (from Belarus) and at the Šakiai exit point (to the Kaliningrad district of the Russian Federation).

### 4.1.2.2 Calculation of the tariffs and adjustments to the application of the RPM

- (38) For the primary network, the proposed postage stamp RPM only uses forecasted booked capacities as a cost driver.
- (39) VKEKK proposes to apply a discount of 75% to the Klaipėda entry from the LNG terminal.
- (40) In Scenario 2, the postage stamp RPM is adjusted by setting zero tariffs at Kiemėnai IP between Lithuania and Latvia and by equalising entry tariffs with those applied in FINESTLAT.
- (41) All these adjustments will lead to under-recovery. To allow the TSO to obtain its allowed revenue, VKEKK applies rescaling tariffs at Lithuanian domestic exit points, thereby altering the initial entry-exit split. The actual entry-exit split depends on the relative level of bookings at Klaipėda entry from the LNG terminal in comparison with bookings at the other entries. Moreover, in Scenario 2, entry tariffs would remain fixed over the regulatory period in order to preserve their equalisation with the tariffs applied in FINESTLAT. The expected increase of the allowed revenue would therefore be only recovered from the exit points<sup>13</sup>. According to VKEKK assumptions, the actual entry-exit split would be roughly 45-55 in Scenario 1, while it would evolve from 45-55 to 35-65 over the regulatory period in Scenario 2.
- (42) The Agency understands that most of the responses to the public consultation relate to the integration of the Lithuanian system into the future regional market. While most respondents acknowledge the benefit of Lithuania joining the FINESTLAT project, Finish, Estonian and Latvian NRAs consider that the Lithuanian proposal of setting zero tariffs at Kiemėnai IP between Lithuania and Latvia (Scenario 2) should be completed by the inclusion of all the Lithuanian entry points in the ITC agreement, signed by their own TSOs. Other stakeholders complain about the 75% discount at the Klaipėda LNG entry (and about subsidies granted directly to the LNG terminal), because it might distort the competition between gas sources in the region.
- (43) Regarding the discount applied to the Klaipėda LNG entry, the Agency finds VKEKK's approach to be compliant with Article 9 of the NC TAR. Moreover, the Agency considers, especially in the case of isolated markets with a dominant gas supplier, that the fixed costs related to marginal alternative gas sources (LNG in this case) could be discounted in the transmission tariff. This minimisation of

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<sup>13</sup> The Lithuanian domestic exit points and the future cross-border IP with Poland.

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the fixed costs allocated to the additional piece of infrastructure that transports these marginal sources would force the dominant supplier to reduce its margins and compete on a level playing field (which would benefit final consumers on the condition that competition functions properly at the retail market level). The discounts should however be limited to fixed costs; variable costs should be properly reflected by the tariff to preserve the economic efficiency of the transmission system. The same reasoning could apply to the future IP between Lithuania and Poland once the GIPL pipeline is commissioned.

- (44) The Agency considers that the Scenario 2 proposed by VKEKK is formally incompliant with the NC TAR. Indeed, adjustments of the RPM like setting zero tariffs at Kiemėnai IP between Lithuania and Latvia and equalising Lithuanian entry tariffs at Kotlovka IP with those applied in FINESTLAT cannot be justified at a national level. However, provided it is only temporary, this Scenario 2 is a pragmatic stepping stone towards regional market integration between the Lithuanian system and FINESTLAT. In the long term, such cross-border tariff adjustments would only make sense if a harmonised approach is applied at a regional level. Ideally, the goal of a common RPM applied jointly by all NRAs within the market zone should be strived for and, building on the flexibility provided by Article 11 of the NC TAR (regarding the rules applicable to entry-exit systems covering more than one Member State), this goal could be achieved progressively.
- (45) To the best of the Agency's knowledge, the NRAs of FINESTLAT propose to set up an ITC mechanism that would be limited to pooling revenue from their entries and then redistributing it in proportion to each country's consumption. The Agency can understand that this mechanism allows to maintain each TSO's revenue from the entries<sup>14</sup>. Ensuring TSOs' financial sustainability is legitimate, but is only one objective among others in a market merger project. The Agency considers that it would be preferable to apply the more complete and consistent principles of Article 10 of the NC TAR, and an ITC mechanism which should both prevent detrimental effects on the TSOs' revenue and avoid cross-subsidisation between intra-system and cross-system network uses.
- (46) This notion of cross-subsidisation is key and the Agency considers that the concerned NRAs should take into account both the costs and the benefits of the regional integration and make sure that users pay for the infrastructure in neighbouring countries if they use them. Therefore the cost-benefit analysis would allow to allocate the costs and the benefits of the merger in a homogenous manner and can form a solid basis for a future joint RPM. This RPM would have to preserve the logic of the previous major investment decisions which ended the isolation of these markets and made possible this regional integration, namely the Klaipėda LNG terminal, the Baltic Connector and the various projects of common interest approved in the region based on cross-border cost allocation agreements (e.g. the GIPL pipeline, the enhancement of Klaipėda - Kiemėnai pipeline...). The joint RPM would have to be consistent with the cost allocation decisions (in particular, concerning asset lifetimes, assets values and costs) to make sure that the infrastructure is effectively priced.
- (47) Additional considerations regarding the implementation of a joint RPM at the scale of the market zone are further elaborated in Section 5.

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<sup>14</sup> After the creation of the FINESTLAT region, with zero tariffs between Finland, Estonia and Latvia, the incentive to use each entry of this 3 countries to supply their respective markets will disappear. The ITC mechanism allows to neutralise the risk of one IP concentrating the majority of income in the future, by sharing this income.

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### 4.1.2.3 Comparison with capacity weighted distance methodology

- (48) For its primary network, VKEKK provides a detailed comparison of the postage stamp reference prices with those from the counterfactual CWD methodology in Section 5.1.8 of the consultation document and in the full tariff model. More accurately, two comparisons are provided, for Scenarios 1 and 2, respectively. The counterfactual CWD methodology with a 50-50 entry-exit split is applied without the adjustments used by VKEKK in its proposed RPM.
- (49) This obviously leads to important differences with respect to the proposed RPM; in particular, the tariff at the Klaipėda LNG entry would be approximately twice as high. More interestingly, the total tariff to transport gas from the Kotlovka entry point (from Belarus) to the Šakiai exit point (to the Russian Kaliningrad district) would be almost twice as high (approximately 136 €/MWh/d/y against 75 €/MWh/d/y in both scenarios). This specific issue of the applied tariff to the cross-border capacities from Belarus to the Kaliningrad district is discussed latter in this Report (see Sections 4.1.3 and 4.1.4). The domestic exit tariff resulting from the CWD methodology would be half of those in the proposed RPM (52 €/MWh/d/y against approximately 100 €/MWh/d/y in Scenarios 1 and 2). This is explained by two main factors: more costs would be allocated to the cross-border flows towards the Kaliningrad district, and no rescaling of the domestic exit tariffs is necessary to compensate for discounts granted to the Klaipėda LNG entry or to the Kiemėnai IP with Latvia.
- (50) Overall, the comparison with the counterfactual CWD methodology is mainly useful for assessing the impact of the special treatment of transit to the Kaliningrad district. This point is discussed in depth in Sections 4.1.3 and 4.1.4 of this Report. On the other hand, the application of the counterfactual CWD methodology is limited to the primary network. It therefore does not provide any information on the proposed tariffs for local networks considered as non-transmission services by VKEKK.

### 4.1.2.4 Comparison between the tariffs for the prevailing tariff period and the tariffs for the first tariff period for which tariffs are proposed

- (51) VKEKK proposes in its consultation document a significantly different RPM in comparison with the one applied in 2019. On its primary network, the entry-exit split changes from 20-80 in 2019 to approximately 45-55 in 2020, while the capacity-commodity split is modified from 71-29 in 2019 to 90-10 in 2020, both in Scenarios 1 and 2. The adjustments applied to promote regional integration contribute to these differences (equalisation of the Kotlovka entry with FINESTLAT's entries from Russia and the zero tariff at the Kiemėnai IP with Latvia in Scenario 2).
- (52) In VKEKK's proposal, the tariffs that would apply to the local network are also significantly different from the current tariff structure. In its consultation document, VKEKK accentuates the difference in treatment between users consuming more than 10.4 TWh per year and users consuming smaller quantities.
- (53) The Agency considers that both the complexity of the proposed RPM and the extent of the differences with the current regulatory period could create difficulties for stakeholders. Some of the proposed evolutions are direct consequences of the application of the NC TAR (e.g. the new capacity-commodity split) or of the on-going regional integration project (e.g. the new entry-exit

split). On the contrary, the tariff settings on the local network are mainly the result of the VKEKK's choices<sup>15</sup>

- (54) The Agency recommends that VKEKK, as far as circumstances allow, promote the stability of its RPM in the next years and reduce the complexity of the rules applied.

#### 4.1.3 Cross-subsidisation and discrimination

- (55) **Article 7(c)** of NC TAR requires the RPM to ensure non-discrimination and prevent undue cross-subsidisation.

##### 4.1.3.1 Cross-subsidisation

- (56) For this analysis, the Agency defines 'cross-subsidisation' as a deviation from cost-reflectivity whereby users of the entry-exit system are charged tariffs that differ from the costs they cause to the system. One instrument to evaluate cross-subsidisation is the CAA.
- (57) VKEKK calculates the CAA of its postage stamp RPM for its primary network, using forecasted capacity bookings as the only cost driver. Five different results of the CAA are provided: for Scenarios 1 and 2, the calculation is done both taking into account and excluding the transmission to the Russian district of Kaliningrad. For the counterfactual CWD methodology, the calculation is done taking into account the transit to Kaliningrad. This level of detail is a good practice and is particularly useful in this case, since the results vary significantly:
- If the transmission to Kaliningrad is neglected in Scenario 1, the result of the CAA is satisfying (2.19%) while it amounts to 75.07% in Scenario 2 (above the threshold of 10% mentioned in NC TAR). This result is neither surprising nor concerning, since setting a zero tariff at the Kiemėnai IP with Latvia automatically distorts the CAA. This Scenario 2 is a transitory step towards a regional market integration. In this case, the result of the CAA at the scale of the region would be more meaningful, especially with a joint RPM implemented in each country.
  - If the transmission to Kaliningrad is taken into account, the results of the CAA in both scenarios exceed 86%. These results, by far above the threshold of 10% mentioned in the NC TAR, are consistent with the comparison with the counterfactual CWD methodology. They demonstrate that the unit cost to ship gas from Belarus to the Russian district of Kaliningrad is significantly lower than the average unit cost of the primary network.
- (58) The Agency considers that this important difference between the unit costs applied, on the first hand, to transport gas from Belarus to the Russian district of Kaliningrad and, on the other hand, to other uses of the primary network will have to be clearly justified in VKEKK's decision. Given the results of the CAA, VKEKK should explain why the proposed RPM does not lead to undue cross-subsidisation between categories of users and why the cost-reflectivity principle is fulfilled. The justification currently provided in VKEKK's consultation is analysed in Section 4.1.4 of this Report.

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<sup>15</sup> e.g. a different capacity-commodity split (50-50) is applied on the local network. Moreover, this split is only an average. Different capacity and commodity charges are proposed for big consumers (more than 10,4 TWh/y) and for smaller consumers.



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### 4.1.3.2 Discrimination

- (59) For this analysis, the Agency defines 'discrimination' as 'applying different rules to comparable situations or the same rule to different situations'. Based on the information provided in the consultation document, it appears that two different capacity products would be offered at two different tariffs at the Kotlovka entry. In both scenarios, the tariff to enter into the Lithuanian entry-exit zone would range between 142 and 145 €/MWh/d/y, while the tariff to transport gas in a point-to-point manner to the Šakiai exit (to the Russian district of Kaliningrad) would only range between 32 and 35 €/MWh/d/y. Without a proper justification, this difference of treatment might be considered discriminatory. Moreover, point-to-point capacity products do not comply with the entry-exit model established by the Third Energy Package, and the NC TAR does not allow two reference prices to coexist at the same interconnection.
- (60) The Agency acknowledges that a gas pipeline starting from a third country (Belarus) and crossing a Member State finally to supply another third country (Russia) is a unique case in Europe. The aim of the Third Energy Package and the entry-exit model is to enable the emergence of liquid and efficient gas markets at regional level and to initiate their integration within the European Union. The point-to-point capacity product offered to transport gas across Lithuania to the Russian district of Kaliningrad does not fully comply with the European regulatory framework, but, in practice, it does not jeopardise its objectives, since the integration the Kaliningrad district into the European gas market has never been considered.
- (61) Regarding the issue of a possible discrimination between the two kinds of capacity products proposed at the Kotlovka entry, the Agency considers that VKEKK should clearly demonstrate in its decision that the legitimacy of the tariff difference is supported by two distinct rationales:
- From a cost-based perspective, it should comply with the cost-reflectivity principle (as already underlined in the previous section and more extensively analysed in the Section 4.1.4);
  - From a market value perspective, the product with a point-to-point constraint, which does not allow to deliver or to trade gas in Lithuania, would justify a discount in comparison with the tariff of the regular firm entry capacity that can be dispatched unrestricted in the concerned market zone.
- (62) The Agency considers that only one reference price should be applicable at the Kotlovka entry point. According to the NC TAR, this reference price is the price for a product for firm capacity with a duration of one year. In the case of the Kotlovka entry, only the capacity product allowing full access to the Lithuanian entry-exit zone should be considered as firm, and its tariff should be considered as the reference price. The point-to-point product allowing to transport gas across Lithuania to the Russian district of Kaliningrad should be considered as a conditional capacity product and its tariff should be set by applying a discount to the reference price. VKEKK could base the calculation of this discount on the reasoning detailed in the next Section 4.1.4 (paragraph 67), which allows to identify the costs related to the pipeline route between Belarus and the Russian district of Kaliningrad.

### 4.1.4 Volume risk



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- (63) **Article 7(d)** of NC TAR requires that the RPM ensure that significant volume risk related particularly to transports across an entry-exit system is not assigned to final customers within that entry-exit system.
- (64) According to Recital 6 of the NC TAR, it is legitimate to shelter the domestic consumers from a cross-border volume risk where a TSO transports significantly more gas into other systems than for consumption into its own entry-exit system. In the Lithuanian case, the cross-border capacity booked to supply the Russian district of Kaliningrad (109 GWh/d in 2020) is indeed higher than the sum of all capacity bookings at other entries (85 GWh/d in 2020).
- (65) Therefore, the Agency agrees that a significant volume risk may theoretically be induced by the major role of cross-border flows in the Lithuanian transmission system.
- (66) Based on this reasoning, VKEKK proposed to shield the Lithuanian consumers from a potential cross-border volume risk by isolating the costs related to the pipeline route between Belarus and the Russian district of Kaliningrad. A split<sup>16</sup> is proposed by VKEKK and the tariffs of the point-to-point capacity products proposed at the Kotlovka entry and at Šakiai exit derive from this split. In 2020, 34% of the allowed revenue related to the Lithuanian TSO's primary network would be allocated to cross-system route from Belarus to the Russian district of Kaliningrad, representing €9.8 million. According to VKEKK's consultation document, the risk of under-recovery on this cross-system route is fully borne by the TSO.
- (67) As explained in the previous Sections 4.1.2 and 4.1.3, the tariff applied to point-to-point products is approximately 75% lower (depending on the years and the scenarios) than the tariff for capacity to access the Lithuanian market. In addition, the CAA and the comparison with the counterfactual CWD methodology show that the unit cost of shipping gas to Kaliningrad was lower than the average unit cost of the Lithuanian network. This situation seems paradoxical at first sight because the riskiest assets (inducing a volume risk) are generally over-priced to compensate the risk.
- (68) For this reason, it is crucial to demonstrate that the split setting apart the costs of the transit to Kaliningrad respects the cost-reflectivity principle. VKEKK details the methodology used to establish the split (mostly in Section 5.2.2 of its consultation document). In a nutshell, the assets of the transmission route to the Kaliningrad district (Kotlovka entry point – Šakiai exit point) and their related costs are identified. VKEKK argues that the sections of pipeline closest to the Šakiai exit point are more dedicated to the cross-system service, whereas the sections of pipeline closer to the Kotlovka entry point are used as well for domestic purposes. VKEKK proposes to split the costs of each pipeline sections by gradually increasing the portion of costs allocated to the cross-system service, as they get closer to the Šakiai exit point<sup>17</sup>.
- (69) VKEKK's reasoning seems compatible with the principle of cost reflectivity. Nevertheless, the numerical calculation used to establish the Intra-System / Cross-System split is not published. Given the complexity of this calculation and the significant cross-border flows in the Lithuanian system, the Agency considers that VKEKK should publish the quantitative details of this calculation in an annex to its decision to prove that the principle of cost reflectivity is respected.

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<sup>16</sup> This split sets apart the costs relating to transit to Kaliningrad from the other costs of the primary network (relating to gas transmission within the European Union). See VKEKK's consultation, section 5.2.2, table 13, p 31.

<sup>17</sup> To do this calculation, VKEKK uses, as cost driver, the peak daily gas quantity (based on historical medium-term data) in the specific section of the pipeline used both for the provision of transmission for the EU network users and transmission to Kaliningrad region services.

#### 4.1.5 Cross-border trade

- (70) **Article 7(e)** of the NC TAR requires that the RPM ensure that the resulting reference prices do not distort cross-border trade.
- (71) In Scenario 2 proposed by VKEKK, the postage stamp RPM is adjusted by setting zero tariffs at Kiemėnai IP between Lithuania and Latvia. This adjustment, by nature, would distort cross-border trade. However, Scenario 2 is proposed as an intermediate step, aiming at integrating the Lithuanian system into the new regional market, before its full integration with FINESTLAT. In this particular context, the temporary distortion would only be a transitory measure with no detrimental impact on the European gas market as a whole.
- (72) The Agency considers that the proposed RPM does not unduly distort cross-border trade.

#### 4.2 Are the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) met?

- (73) Article 27(2)(b)(2) of the NC TAR requires the Agency to analyse whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) of the NC TAR are met.
- (74) VKEKK proposes to apply commodity-based transmission tariffs on the Lithuanian primary network. The commodity-based transmission tariffs would provide 10% of the transmission services revenue. The Agency considers this an appropriate use of the commodity charge.
- (75) The NC TAR allows for two types of commodity-based transmission tariffs: a flow-based charge and a complementary revenue recovery charge. VKEKK proposes to apply a flow-based charge, to recover costs related to the quantity of gas flow (mostly compressor fuel costs). The flow-based charge is derived from forecasted flows. The same charge is applied at all exit points, including Šakiai exit point to the Russian district of Kaliningrad, while no charge is applied at the entries.
- (76) The commodity CAA index is zero in both Scenarios 1 and 2.

#### 4.3 Are the criteria for setting non-transmission tariffs as set out in Article 4(4) met?

- (77) Article 27(2)(b)(3) of the NC TAR requires the Agency to analyse whether the criteria for setting non-transmission tariffs as set out in Article 4(4) of the NC TAR are met.
- (78) As explained in Section 4.1 of this Report, VKEKK considers that the use of the local transmission network as a non-transmission service. VKEKK's aim is to allocate all costs relating to the regional branches to the users of these branches only.
- (79) The Agency considers this objective to be sound and in line with the cost-reflectivity principle. The identification of regional branches and their related costs is a best practice.
- (80) Nonetheless, the Agency is concerned about the complexity of the solution proposed by VKEKK. In its consultation document, VKEKK proposed tariffs based both on capacity and commodity charges, deriving from an average 50-50 capacity-commodity split for this part of the network. In

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addition, the capacity and commodity charges applied to a particular network user would depend on its yearly quantity of gas transported in the network.

Table 3: Proposed tariffs for the use of the Lithuanian local network (classified as a non-transmission service).

NON-TRANSMISSION SERVICES (Local network)	Unit	2020 (indicative tariffs)
Tariff for Consumption capacity for Group with annual Q ≤ 10.4 TWh	EUR/MWh/day/year	73.68
Tariff for Consumption capacity for Group with annual Q > 10.4 TWh		9.39
Flow-based charge for Group with annual Q ≤ 10.4 TWh	EUR/MWh	1.00
Flow-based charge for Group with annual Q > 10.4 TWh	EUR/MWh	0.03

- (81) This kind of tariff settings, dependent on the consumption of each consumer, is unusual. Based on bilateral discussions with VKEKK and with the Lithuanian TSO, the Agency understands that only one industrial consumer in Lithuania exceeds the 10.4 TWh. This consumer is connected to a branch more depreciated than the other parts of the local network. The proposed non-transmission tariffs reflect these differences of depreciation<sup>18</sup>. At a transmission level, the Agency would consider it discriminatory, since different conditions would be applied to network users to access the market, depending on their size.
- (82) From a legal perspective, the Agency disagrees with the classification of the local network use as a non-transmission service. According the Article 4(1) of NC TAR, “A given service shall be considered a transmission services where both of the following criteria are met:
- a. the costs of such service are caused by the cost drivers of both technical or forecasted contracted capacity and distance;
  - b. the costs of such service are related to the investment in and operation of the infrastructure which is part of the regulated asset base for the provision of transmission services.”
- (83) The Agency considers that the cost drivers of the local networks<sup>19</sup> do not differ from the cost drivers of the primary network, which are capacity and distance. On the one hand, the cost drivers do not justify, by themselves, different approaches to the primary network and the local network. On the other hand, the topology of the local network (unmeshed branches) brings it closer to distribution networks.
- (84) Therefore, the Agency considers that, in the current regulatory framework, the use of the local transmission network should be either considered as a transmission service or reclassified as a distribution service, if the RPM cannot properly allocate the costs of the regional branches to the relevant network users<sup>20</sup>. If VKEKK chooses to reclassify the use of the local network as a

<sup>18</sup> Another parameter is the rate of use of this delivery capacity which is higher than the average rate of use of domestic delivery capacities in Lithuania according to VKEKK.

<sup>19</sup> Diameter (which is equivalent to the capacity) and length of the local branches.

<sup>20</sup> Article 2(1)(1) of Regulation (EC) No 715/2009 does not recognise any distinction between regional and national transmission, while only proposing a definition for ‘transmission’. However, Article 2(5) of Directive 2009/73/EC proposes the inclusion of regional networks in ‘distribution’ under the supervision of the Member State. It is not for the Agency to judge the alignment with these articles.

transmission service, the same RPM should apply to all part of the transmission network, in particular with only one capacity-commodity split. This approach is encouraged by Article 2(3) and (5) of Directive 2009/73/EC.

#### **4.4 Conclusions regarding the overall compliance and the level of complexity of the proposed RPM**

- (85) VKEKK proposes, in its consultation document, a complex methodology, which raises several concerns. The VKEKK tariff proposal is based on two asset splits, allowing to isolate and to allocate to the relevant users the costs induced by, on the one hand, the local network (i.e. high pressure distribution branches), and on the other hand, the transit flows towards the Russian district of Kaliningrad. In addition, the regional market integration project led by Finland, Estonia and Latvia induces other adjustments of the Lithuanian RPM.
- (86) First, VKEKK should either reclassify the use of the local network as a distribution service or as a transmission service. In both alternatives, VKEKK should implement a single RPM with a single capacity-commodity split to the transmission system, irrespective of whether the local network is included in the scope of transmission or in the scope of distribution. At the transmission level, the same conditions should apply to all network users, regardless of its size or consumption.
- (87) The results of the CAA and of the comparison with the counterfactual CWD methodology show important differences between the unit costs applied, on the one hand, to ship gas across the Lithuanian system and, on the other hand, within Lithuania. These results are explained by two specificities:
- In Scenario 2, VKEKK proposes a zero tariff at the Kiemėnai IP between Lithuania and Latvia<sup>21</sup>;
  - Dedicated point-to-point capacity products are proposed at a cheaper price to transit gas from Belarus to the Russian district of Kaliningrad<sup>22</sup>.
- (88) While the complexity and the discrepancy induced by the regional integration in Scenario 2 should only be temporary, the transit across Lithuania to the Kaliningrad district will remain. VKEKK should both:
- clarify why a specific treatment is necessary for this transit route (e.g. significantly different level of depreciation in comparison with the other transmission assets, physical constraints justifying a conditional point-to-point product);
  - simplify as much as possible the RPM, in particular by proposing only one reference price for the regular firm entry capacity at the Kotlovka entry point from Belarus. The reserve price of the point-to-point product at this entry should be set by applying a discount to this reference price;

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<sup>21</sup> Without taking into account the cross-system route towards the Kaliningrad district, the result of the CAA is 2,19% in scenario 1 while it amounts to 75,07% in scenario 2.

<sup>22</sup> In scenario 1, the result of the CAA is 2,19% without taking into account the cross-system route towards the Kaliningrad district, while it amounts to 86,02% once it is included in the calculation.

- finally, consider reclassifying the use of the local network either as a transmission service or as a distribution service. The same RPM should apply to all part of the transmission network, in particular with only one capacity-commodity split, as mentioned above.

## 5. Others

- (89) The regional integration project formally goes beyond the scope of this Report. However, the responses to VKEKK's public consultation show the relevance of the regional market project for the Lithuanian transmission tariffs.
- (90) The Agency should therefore study the modalities for the creation of a regional market area and consider the application of the tariff code in this particular context.
- (91) As explained in Section 4.1.2.2, the NRAs of FINESTLAT plan to implement an ITC mechanism to support the equalisation of their entry tariffs at the external borders of their tariff zone, pooling the revenues from these entries and then redistributing it in proportion to each country's gas consumption. They do not plan to build a joint RPM, which would be feasible based on Article 11 of the NC TAR. Each country intends to keep its own RPM and allowed revenue parameters (e.g. chosen cost drivers, WACC, depreciation period...), and the proposed ITC mechanism can be considered as a limited (10%) and *ex-post* adjustment to these national methodologies.
- (92) The Agency suggests to conduct an analysis in the opposite direction, from the regional to the national level. The first step would be to determine what should be the ideal RPM at the scale of the regional market zone, covering:
- what the regional entry-exit split should be;
  - what the entry tariffs into the new regional zone should be; and
  - specifically, to which piece of infrastructure could discounted tariffs apply. As already explained, the Agency considers that the fixed costs related to marginal alternative gas sources (LNG, Storage, pipeline ending the isolation...) could be socialised in the transmission tariffs, in particular in the case of isolated markets with a dominant gas supplier. This minimisation of the fixed costs allocated to the piece of infrastructure that transports these marginal sources would force the dominant supplier to reduce margins and compete.
- (93) Once the tariffs at the external borders of the new regional zone are determined in order to maximise the benefits for all consumers in the region (in terms of access to alternative gas sources, competition, security of supply, etc.), the Agency would consider meaningful the following steps to elaborate an ITC mechanism:
- First, the transmission assets jointly used within the regional market zone and their associated costs should be identified to ensure an acceptable level of cost-reflectivity at a regional level. These costs should be logged into the ITC mechanism.
  - Ideally, the ITC mechanism should aim at allocating these costs in a manner that would be in line with the distribution of the benefits of the merger. A similar kind of reasoning is already used to allocate the costs of Projects of Common Interest, with Cross-Border Cost Allocation decisions (CBCA) based on cost-benefit analysis. In this way, the ITC mechanism would be sustainable as it could be used both for existing costs and for new

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investments. In addition, the cost-reflectivity principle promoted by the NC TAR would be safeguarded, since this kind mechanism would allow to allocate efficient costs (and exclude sunk costs of over-dimensioned infrastructures) to their beneficiaries.

- The last step would be to adjust the domestic exits of each TSOs within the regional market, to allow them to recover their allowed revenue and to contribute to the ITC mechanism.

## Annex 1: Legal framework

(94) Article 27 of NC TAR reads:

1. *Upon launching the final consultation pursuant to Article 26 prior to the decision referred to in Article 27(4), the national regulatory authority or the transmission system operator(s), as decided by the national regulatory authority, shall forward the consultation documents to the Agency.*

2. *The Agency shall analyse the following aspects of the consultation document:*

*(a) whether all the information referred to in Article 26(1) has been published;*

*(b) whether the elements consulted on in accordance with Article 26 comply with the following requirements:*

*(1) whether the proposed reference price methodology complies with the requirements set out in Article 7;*

*(2) whether the criteria for setting commodity-based transmission tariffs as set out in Article 4(3) are met;*

*(3) whether the criteria for setting non-transmission tariffs as set out in Article 4(4) are met.*

3. *Within two months following the end of the consultation referred to in paragraph 1, the Agency shall publish and send to the national regulatory authority or transmission system operator, depending on which entity published the consultation document, and the Commission the conclusion of its analysis in accordance with paragraph 2 in English.*

*The Agency shall preserve the confidentiality of any commercially sensitive information.*

4. *Within five months following the end of the final consultation, the national regulatory authority, acting in accordance with Article 41(6)(a) of Directive 2009/73/EC, shall take and publish a motivated decision on all items set out in Article 26(1). Upon publication, the national regulatory authority shall send to the Agency and the Commission its decision.*

5. *The procedure consisting of the final consultation on the reference price methodology in accordance with Article 26, the decision by the national regulatory authority in accordance with paragraph 4, the calculation of tariffs on the basis of this decision, and the publication of the tariffs in accordance with Chapter VIII may be initiated as from the entry into force of this Regulation and shall be concluded no later than 31 May 2019. The requirements set out in Chapters II, III and IV shall be taken into account in this procedure. The tariffs applicable for the prevailing tariff period at 31 May 2019 will be applicable until the end thereof. This procedure shall be repeated at least every five years starting from 31 May 2019.*

(95) Article 26(1) of NC TAR reads:

1. *One or more consultations shall be carried out by the national regulatory authority or the transmission system operator(s), as decided by the national regulatory authority. To the extent possible and in order to render more effective the consultation process, the consultation document should be published in the English language. The final consultation prior to the decision referred to in Article 27(4) shall comply with the requirements set out in this Article and Article 27, and shall include the following information:*

*(a) the description of the proposed reference price methodology as well as the following items:*

*(i) the indicative information set out in Article 30(1)(a), including:*



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- (1) *the justification of the parameters used that are related to the technical characteristics of the system;*
    - (2) *the corresponding information on the respective values of such parameters and the assumptions applied.*
  - (ii) *the value of the proposed adjustments for capacity-based transmission tariffs pursuant to Article 9;*
  - (iii) *the indicative reference prices subject to consultation;*
  - (iv) *the results, the components and the details of these components for the cost allocation assessments set out in Article 5;*
  - (v) *the assessment of the proposed reference price methodology in accordance with Article 7;*
  - (vi) *where the proposed reference price methodology is other than the capacity weighted distance reference price methodology detailed in Article 8, its comparison against the latter accompanied by the information set out in point (iii);*
- (b) *the indicative information set out in Article 30(1)(b)(i), (iv), (v);*
- (c) *the following information on transmission and non-transmission tariffs:*
  - (i) *where commodity-based transmission tariffs referred to in Article 4(3) are proposed:*
    - (1) *the manner in which they are set;*
    - (2) *the share of the allowed or target revenue forecasted to be recovered from such tariffs;*
    - (3) *the indicative commodity-based transmission tariffs;*
  - (ii) *where non-transmission services provided to network users are proposed:*
    - (1) *the non-transmission service tariff methodology therefor;*
    - (2) *the share of the allowed or target revenue forecasted to be recovered from such tariffs;*
    - (3) *the manner in which the associated non-transmission services revenue is reconciled as referred to in Article 17(3);*
    - (4) *the indicative non-transmission tariffs for non-transmission services provided to network users;*
- (d) *the indicative information set out in Article 30(2);*
- (e) *where the fixed payable price approach referred to in Article 24(b) is considered to be offered under a price cap regime for existing capacity:*
  - (i) *the proposed index;*
  - (ii) *the proposed calculation and how the revenue derived from the risk premium is used;*
  - (iii) *at which interconnection point(s) and for which tariff period(s) such approach is proposed;*
  - (iv) *the process of offering capacity at an interconnection point where both fixed and floating payable price approaches referred to in Article 24 are proposed.*

(96) Article 7 of NC TAR reads:

*The reference price methodology shall comply with Article 13 of Regulation (EC) No 715/2009 and with the following requirements. It shall aim at:*

- a) *enabling network users to reproduce the calculation of reference prices and their accurate forecast;*
- b) *taking into account the actual costs incurred for the provision of transmission services considering the level of complexity of the transmission network;*
- c) *ensuring non-discrimination and prevent undue cross-subsidisation including by taking into account the cost allocation assessments set out in Article 5;*



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*(d) ensuring that significant volume risk related particularly to transports across an entry-exit system is not assigned to final customers within that entry-exit system;*

*(e) ensuring that the resulting reference prices do not distort cross-border trade.*

(97) Article 13 of Regulation (EC) No 715/2009 reads:

*1. Tariffs, or the methodologies used to calculate them, applied by the transmission system operators and approved by the regulatory authorities pursuant to Article 41(6) of Directive 2009/73/EC, as well as tariffs published pursuant to Article 32(1) of that Directive, shall be transparent, take into account the need for system integrity and its improvement and reflect the actual costs incurred, insofar as such costs correspond to those of an efficient and structurally comparable network operator and are transparent, whilst including an appropriate return on investments, and, where appropriate, taking account of the benchmarking of tariffs by the regulatory authorities. Tariffs, or the methodologies used to calculate them, shall be applied in a nondiscriminatory manner.*

*Member States may decide that tariffs may also be determined through market-based arrangements, such as auctions, provided that such arrangements and the revenues arising therefrom are approved by the regulatory authority.*

*Tariffs, or the methodologies used to calculate them, shall facilitate efficient gas trade and competition, while at the same time avoiding cross-subsidies between network users and providing incentives for investment and maintaining or creating interoperability for transmission networks.*

*Tariffs for network users shall be non-discriminatory and set separately for every entry point into or exit point out of the transmission system. Cost-allocation mechanisms and rate setting methodology regarding entry points and exit points shall be approved by the national regulatory authorities. By 3 September 2011, the Member States shall ensure that, after a transitional period, network charges shall not be calculated on the basis of contract paths.*

*2. Tariffs for network access shall neither restrict market liquidity nor distort trade across borders of different transmission systems. Where differences in tariff structures or balancing mechanisms would hamper trade across transmission systems, and notwithstanding Article 41(6) of Directive 2009/73/EC, transmission system operators shall, in close cooperation with the relevant national authorities, actively pursue convergence of tariff structures and charging principles, including in relation to balancing.*

(98) Article 4(3) of NC TAR reads:

*3. The transmission services revenue shall be recovered by capacity-based transmission tariffs. As an exception, subject to the approval of the national regulatory authority, a part of the transmission services revenue may be recovered only by the following commodity-based transmission tariffs which are set separately from each other:*

*(a) a flow-based charge, which shall comply with all of the following criteria:*

- (i) levied for the purpose of covering the costs mainly driven by the quantity of the gas flow;*
- (ii) calculated on the basis of forecasted or historical flows, or both, and set in such a way that it is the same at all entry points and the same at all exit points;*
- (iii) expressed in monetary terms or in kind.*

*(b) a complementary revenue recovery charge, which shall comply with all of the following criteria:*

- (i) levied for the purpose of managing revenue under- and over-recovery;*
- (ii) calculated on the basis of forecasted or historical capacity allocations and flows, or both;*

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*(iii) applied at points other than interconnection points;*

*(iv) applied after the national regulatory authority has made an assessment of its cost-reflectivity and its impact on cross-subsidisation between interconnection points and points other than interconnection points.*

(99) Article 4(4) of NC TAR reads:

*4. The non-transmission services revenue shall be recovered by non-transmission tariffs applicable for a given non-transmission service. Such tariffs shall be as follows:*

*(a) cost-reflective, non-discriminatory, objective and transparent;*

*(b) charged to the beneficiaries of a given non-transmission service with the aim of minimising cross-subsidisation between network users within or outside a Member State, or both.*

*Where according to the national regulatory authority a given non-transmission service benefits all network users, the costs for such service shall be recovered from all network users.*

## Annex 2: List of abbreviations

Acronym	Definition
<b>ACER</b>	Agency for the Cooperation of Energy Regulators
<b>CAA</b>	Cost Allocation Assessment
<b>VKEKK</b>	The Lithuanian NRA, Valstybinė kainų ir energetikos kontrolės komisija
<b>CWD</b>	Capacity Weighted Distance
<b>EC</b>	European Commission
<b>EU</b>	European Union
<b>IP</b>	Interconnection Point
<b>MS</b>	Member State
<b>NC TAR</b>	Network code on harmonised transmission tariff structures for gas
<b>NRA</b>	National Regulatory Authority
<b>RPM</b>	Reference Price Methodology
<b>TSO</b>	Transmission System Operator



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