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Subject:

Implementation of the network code on harmonised transmission tariff structures (COMMISSION REGULATION (EU) 2017/460)

Dear Sir/Madam,

As you know in the last few years Shell has systematically engaged in the debate on the Austrian gas transmission system charges. Our participation to the discussion has always aimed at ensuring:

- Cost reflectivity;

- Efficient use of infrastructure;
- Reasonable cost levels for all.

In our mind, pursuing these objectives meant contributing to a well-functioning market with high liquidity and high competition and to increased overall welfare.

Recently, we have also shared with your office a quantitative analysis on the financial situation of Trans Austria Gasleitung GmbH performed by the renowned consultant Frontier Economics (www.frontier-economics.com) which we attach again for your convenience.

While at the beginning of the current regulatory period we have applauded some improvements, mainly directed at eliminating elements of cross-subsidies between the transit routes and the Austrian domestic system, as in the context of the previous TAR consultation, we remain concerned about several material aspects, namely:

1. No transparency on several items listed in article 26 of the TAR Code and other TAR transparency requirements;
2. Limited transparency on the definition of TSOs' allowed revenues and high transmission costs when compared to other EU TSOs;
3. Limited explanations backing the forecasted booking levels used as input for the tariff methodology;
4. Suboptimal consultation process;
5. Setting of multipliers;
6. No-introduction of commodity charge.

1. <u>No transparency on several items listed in article 26 of the TAR Code and other transparency requirements</u>

This is the list of Article 26 items of TAR Code that are not covered in the consultation document:

- The components and the details of technical characteristics of the system used for the cost allocation assessments set out in Article 5;
- The indicative information set out in Article 30(1)(b)(i), (iv), (iv);
- The indicative information set out in Article 30(2), i.e. the tariff model does not allow to identify separately operational costs (e.g. fuel gas) or to identify how tariff would have changed without the 10% cap for tariff increase (please see Section 2 of this letter). Specifically on fuel gas and considering current price dynamics, we have doubts on the reflectivity of the cost of gas assumed for the tariff calculation.

With respect to the last point we note that according to Article 30.2.b the tariff model should allow network users to calculate the transmission tariffs applicable for the prevailing tariff period and to estimate their possible evolution beyond such tariff period. More in general, Article 7(a) states that the reference price methodology shall aim at enabling network users to reproduce the calculation of reference prices and their accurate forecast. Unfortunately, the information provided and the model published do not have the above characteristics.

On this basis we must conclude that the published document does not qualify as a TAR compliant consultation. The situation is further aggravated by what we describe in Section 2 of this letter and by the fact that this is already the second TAR Code consultation held in 2019.

2. <u>Limited transparency on the definition of TSOs' allowed and high transmission costs when compared to any other EU TSOs</u>

While we understand that the definition of TSOs' Regulated Asset Base (RAB) and the related allowed revenues is not part of the ongoing consultation, these aspects are at the core of the criticism that Shell and other network users have brought to the attention of E-Control in the past.

Unfortunately, as per the Austrian Gas Act the underlying process for setting the above values is not subject to the opinion of network users, not even with respect to the purely methodological aspects, and leaves very little room to the opinion of end users. Hence, we take this opportunity to send the old message once again, hoping that our concerns will be finally heard.

The problem is clear: Austrian TSOs are among the most expensive gas transport service providers in Europe and unchallengedly so and until E-Control does not engage in a thorough transparency exercise bringing the Austrian gas market to a level of transparency comparable to other best in class EU Member States, consumers – both in Austria and in neighbouring countries – will continue to grant excessive profit to Austrian TSOs with no special advantage in return.

As we did in the past, we note that without access to the details of the underlying regulated assets or their depreciation levels and without the publication of the rationale supporting the remuneration levels, it is difficult to carry out any fully accurate assessment or benchmark exercise.

All we can say in this regard is that we have evidence that Austrian TSOs continue to be compensated more than other comparable European TSOs.

The Frontier study attached to this response further demonstrates this point. It also highlights that strong revenues are driven by:

- High allowed rate of return on equity, supposedly to compensate for a volume risk which was and is immaterial up until at least 2022;
- High levels of new investments, partially reflected in the regulated asset base before investments happen;
- Short asset depreciation periods when benchmarked with other countries and actual lifetime of assets, which may also point at old TAG assets being already fully depreciated;
- Lack of clarity with respect to the management of the revenues accumulated through the years, including post-2017, as a result of the volume risk premium.

On the basis of the above we question the compatibility of the Austrian rules on setting tariffs and TSOs' allowed revenues with article 13 of Regulation 715/2009 which states that "tariffs, or the methodologies used to calculate them, applied by the transmission system operators and approved by the regulatory authorities […] 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".

As side note to this matter, we believe that the proposed 10% cap on tariff increase from one regulatory period to the next at each system points represents a very mild regulatory risk mitigation feature, a full capacity reset right being the only way to protect network users from price spikes comparable to the indicative tariffs published with this consultation. Also, while the measure might in theory protect from excessive tariff increase, its application does not allow market participants to understand how tariffs would have changed had the cap not been applied, adding to the limited transparency of the overall proposal.

3. Limited explanations backing the forecasted booking levels used as input for the tariff methodology

We understand that missing the introduction of a new reference price methodology, in a period characterised by low interest rates and low cost of capital, and with gas prices that are lower than in the past and have on average progressively decreased during the past four years, the only driver behind the massive cost increase represented by the indicative tariff can be the forecasted contracted capacity or the presence of excessive, and possibly unjustified, new investment.

However, we see nowhere the signs that booking may go dramatically down during the next regulatory period, even considering the possible conclusion of existing long-term transportation agreements.

To corroborate this view, we would like to emphasise the ongoing restriction of the TENP pipeline causing the reduction of flows to Italy via Germany/Switzerland to the advantage of the Austrian route to the south. However, this opportunity may materialize only if the Austrian route remains more attractive than LNG deliveries and/or deliveries from TAP. In other words, the risk of lower utilization of the Austrian system, if existing at all, it is primarily self-inflicted.

4. Suboptimal consultation processes

We note that E-Control, differently from other National Regulators, has not engaged in any discussion on the broader principles informing the selected tariff methodology, neither it has presented alternative scenarios, de facto limiting the opportunity for market participants to objectively gage the selected option against others that could have been equally defendable.

Unfortunately, once this process is concluded there will be no further formal opportunity to challenge the approved tariff methodology for four years and, given the transparency deficit discussed above, the risk of numerous legal challenges initiated by market participants may increase leading to high regulatory instability.

We also note that the indicative tariffs published in the consultation document are based of the current level of allowed revenues and are therefore subject to further adjustment. While we understand that any such change would happen in the form of a rebate, which we welcome, we note that it is unfortunate to have a consultation run on values that may materially differ from the final tariffs published by May 2020.

All the above is particularly unfortunate considering that this is already the second TAR consultation run by E-Control in 2019.

Therefore, we would appreciate having an additional month for stakeholders to respond and as well as having the consultation document revised as to bring it in line with the required level of transparency.

5. Setting of multipliers, seasonal factors, clustering of system points, interruptible capacity

The choice made with respect to multipliers does not rely on a thorough quantitative justification. This leaves market participants with the only possibility to comment based on their vested interest, rather than with an eye to contributing to a well-functioning market.

Against this background we suspend our judgement in hope of receiving additional explanatory information and we limit ourselves to noting that short term multipliers, are generally higher than multipliers used in other Member States and this seems at odds with the preoccupation to ensure a continued utilisation of transit pipelines.

With respect to the discount for interruptible capacity we note that no justification is provided to back the choice to differentiate among different system points and we recommend using the ex-ante discount methodology across the system to avoid forms of discrimination.

6. No-introduction of commodity charge

In some bilateral discussions with E-Control we could appreciate the expressed intention to introduce a commodity charge in the tariff structure aimed at covering fuel costs. The proposal – perfectly in line with the provisions of the Austrian Gas Act and with the TAR Network Code – would have allowed a higher level of cost reflectivity and higher level of transparency.

Having a commodity charge reflecting operational costs linked to actual gas flows would have put shippers, particularly those that have invested in long-term, in a position to better control the costs related to the service they receive.

Unfortunately, E-Control chose to disregard the idea without sharing the rationale behind their decision, preventing yet again the possibility to have an informed discussion towards selecting the best solution for all market participants.

In conclusion, the sum and the complexity of the issues addressed in the comments above are such that engaging in further discussions could be beneficial to ensure our position is fully understood.

We are therefore available for a bilateral meeting to further substantiate our position if necessary or required.

Sincerely,

Davide Rubini

Regulatory Affairs & Commercial Manager - South and East Europe

Shell Energy - Europe and Environmental Products