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**Sabiedrisko pakalpojumu  
regulēšanas komisijai**  
Ūnijas ielā 45, Rīgā, LV-1039  
Latvija

**Regarding a consultation document  
"Main Principles of Entry-Exit Tariffs"**

On June 21, 2017 Joint Stock Company "Conexus Baltic Grid" (hereafter – Conexus Baltic Grid) received a draft document "Main Principles of Entry-Exit Tariffs" (hereafter – the Consultation Document) prepared by the national regulatory authorities (hereafter – NRAs) of Estonia, Latvia, Lithuania and Finland. Conexus Baltic Grid hereby submits the following comments on the Consultation Document:

1. The Consultation Document provides for two solutions – Interim solution and Long-term solution. Both solutions assume full merger of entry-exit zones from the very beginning, as well as the need to create inter-TSO Compensation Mechanism (hereafter – ITC mechanism). As the balancing regimes differ in all the countries of the envisaged single tariff zone, complete elimination of national entry-exit zones and interconnection points between them is not possible before full harmonisation of the balancing regimes.

In order to harmonize the balancing regimes, at least the TPA rules of all TSOs in the region have to be changed in that regard. Conexus Baltic Grid would like to suggest for the interim solution setting maximally low, above zero, entry/exit tariffs at the interconnection points (hereafter – IPs) between the transmission systems. Such solution will remove cost burden from the IPs, while maintaining the national regime for capacity booking, nomination, allocation and balancing regimes, thus allowing developing an efficiently functioning solution for the single balancing zone for the fully merged entry/exit zone for the long-term solution.

Conexus Baltic Grid does not support setting zero entry/exit tariffs at the IPs between the transmission systems for Interim solution, as it will require the changes of TPA rules of all involved TSOs in order to introduce stricter measures for limiting of capacity hoarding and congestion management rules.

2. Article 2(2) of the 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 (hereafter – Gas Directive) provides the definition of gas transmission. According to it, upstream networks and, more important in the context of the Consultation Document, high-pressure pipelines primarily used in the context of local distribution of natural gas are not considered being involved in gas transmission. In Conexus Baltic Grid view, the Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a network code on harmonised transmission tariff structures for gas (hereafter – NC TAR) makes clear distinction between two types of services and differentiates the tariff setting regimes for transmission and non-transmission services, by defining them in Article 3 (12) and (15), and providing criteria for differentiation in Article 4 respectively.

Taking into account Article 4 of the NC TAR that specifies the source of revenue for transmission and non-transmission services and emphasising the necessity to minimize cross-

subsidies between transmission and non-transmission services, the costs shall be split and attributed to transmission and non-transmission services before application of reference price methodology. Furthermore, NC TAR is very clear in requiring the choice to be made for reference price methodology for tariff calculation and the setting of the default reference price methodology (Article 7 and 8) for **transmission services** only. As concerns the costs representing allowed revenue from the non-transmission services, no entry/exit split and no ITC mechanism should be applied. Thus, the bias of non-transmission related costs (i.e. costs of the TSO not related to ensuring technical cross-border capacities among the countries forming single entry/exit zone) will be avoided before application of the Article 8(1e) of NC TAR.

In Conexus Baltic Grid view, the approach foreseen by the NC TAR is easy to use as a long term solution as it removes the burden of decision making on non-transmission related costs from the regional market agenda and leaves it up to the national tariff setting procedure, which shall follow the set of requirements foreseen for non-transmission tariffs in Article 4(4) of the NC TAR.

3. Conexus Baltic Grid would like point out that the discount to the transmission system interconnection point with Inčukalns underground gas storage (hereafter – UGS) is identified as the interim solution, while the long-term solution foresees special treatment only for biogas entry point, which contradicts with the Article 9(1) of the NC TAR. The Consultation Document does not provide any justification, why such solution was chosen by the NRAs, and which should at least include an analysis whether and to what extent IP at UGS will have to compete with a standard IP. Conexus Baltic Grid draws the attention of NRAs to the policy document prepared for the European Commission “Quo Vadis EU gas market regulatory framework – Study on a Gas Market Design for Europe” that suggests setting of zero tariffs for IPs with UGS, thus benefiting the market with more flexibility at lower cost.

4. Conexus Baltic Grid would like point out that the short-term capacity products are already defined and regulated by the provisions of Article 2(15) and Article 14 of the Regulation (EC) No 715/2009 of the European Parliament and of the Council on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005 (hereafter – Gas Regulation). In Conexus Baltic Grid view, the principles of tariff setting have to be harmonized for both – long-term and short-term services, applying the general rule “single tariff for all entry points”, and applying the same principle also to the choice of short-term multipliers and/or seasonal factors, if any.

5. In order to introduce a single entry/exit zone or some intermediary solution, the tariff approval process must be streamlined and coordinated among countries to ensure synchronized changes. It can be achieved by introducing the same rules of entry into force of the approved tariffs, providing reasonable timeframe for approval of tariffs or allowing the TSOs to calculate the tariffs according to the established methodologies, like in other EU member states, and ensuring the regulatory overview over determination of allowed revenue being a parallel process, with the correction mechanisms to be applied during the tariff review process and not as the starting point for the tariff review.

6. Regarding the proposed ITC mechanism Conexus Baltic Grid would like to point out as follows:

6.1. the compensation calculation and settlement for hosting of flows needs to be done on monthly basis due to the following reasons:

6.1.1. until the specific responsibilities of the TSOs for operation of the Korneti/Misso entry/exit point in the new conditions are not set, Conexus Baltic Grid will operate as an isolated entry/exit system with no revenue from entry/exit tariffs (assuming zero tariffs also for IP with UGS) or remuneration for hosting of flows, currently represented by entry/exit tariffs at the IPs with Estonia and Lithuania;

6.1.2. seasonality and variability of the flows in the region, especially taking into account the changes brought in by gas market opening in Latvia;

6.1.3. expectations for more cross-border (hosted) flows in the system of Conexus Baltic Grid destined for the consumers in Estonia and Lithuania than during previous few years;

6.1.4. hosting of flows in gas business is more material than in the case of electricity, which seems to be taken as a basis for proposed calculation in the Section 3 of the Interim solution;

6.1.5. taking into account the opportunities, brought in by the UGS, conveniently located in the middle of the common Baltic gas transportation system, and assuming zero tariffs for IP with UGS, Conexus Baltic Grid expects the use of the UGS for Baltic TSOs technical needs in order to enhance the commercial services offered to the market participants. For example, TSOs could ensure larger commercial gas flows by re-dispatching the gas from technical reserve in UGS, replenishing it afterwards by injection of the gas or acquisition of it from the reserves held by market participants;

6.2. the same principle regarding the excess/shortfall revenues should apply equally to short-term and long-term solution. Currently the last sentence of Long-term solution Section 3 (ITC) mentions only excess revenue;

6.3. in Conexus Baltic Grid view, it must be clearly set in the regulatory framework that the ITC payments are legitimate expenses or income of the TSO with appropriate inclusion of them into allowed revenue calculations.

7. Conexus Baltic Grid would like to draw the NRAs attention to a need to consider the proposed solutions also in the light of reduction of burden on the business environment and tax administration. In this perspective, none of the solutions reduces the burden of taxes. In Conexus Baltic Grid view, if one of the objectives of the concept of regional single tariff zone is to simplify procedures for the users of gas transmission networks, the proposed solutions make the tax administration of services more complicated for network users.

Conexus Baltic Grid carried out case study analysis of tax rules. Situation A – a shipper registered in Latvia buys gas in Lithuania for own consumption or re-sale from a shipper registered in Lithuania and books necessary capacity of transmission system at Latvia-Lithuania IP. Situation B – a shipper registered in Latvia sells gas to Lithuania and books necessary capacity of transmission system at Latvia-Lithuania IP. Assumptions: the shipper in Latvia and the shipper in Lithuania both are registered as value added tax (hereafter – VAT) payers in their countries of residence. The shipper from Latvia does not have its permanent office in Lithuania. Gas is transported through gas transmission system.

Tax legislation (Law on Income Tax, VAT Law, Law on Excise) does not differentiate wholesale or retail activities and does not provide definition of wholesale and retail. The EU Directive on VAT determines that the point of delivery, if it is done using gas transmission system within the EU countries, is the country of business activity of the taxpayer or the country of residence of its permanent office or country of permanent residence, if both criteria are apply:

- a) Shipper's business activity of taxpayer is re-sale of gas;
- b) Shipper's own consumption of gas is negligible.

If both conditions are false, the address of consumption of gas is the address of physical delivery. The shipper in Latvia will have to prove its re-seller (trader) status to the shipper in Lithuania or provide with the address of physical consumption (if bought for own consumption). If no such information is provided, the shipper in Lithuania will have to apply the Latvia's VAT provisions to the value of the contract.

Amber Grid will apply the reverse VAT for the transmission and balancing services provided to the shipper from Latvia in the Lithuanian gas transmission system (the shipper from Latvia

will calculate 21% VAT for the services provided within the EU and pay to the Latvian tax authorities). Conexus Baltic Grid will apply standard VAT rate 21% for the services provided to the shipper from Latvia for transmission in the system of Conexus Baltic Grid.

The excise tax must be declared and paid in Latvia (for the volume sold to final consumers and self-consumption). If the gas is not imported into the EU (any of the member states) for the free circulation, the shipper from Latvia is responsible for the customs procedures.

For the situation B - for the transmission of gas to Lithuania Conexus Baltic Grid will apply standard VAT rate 21% for the services provided to the shipper from Latvia through the gas transmission system of Conexus Baltic Grid. Amber Grid will apply the reverse VAT for the transmission and balancing services provided to a shipper from Latvia in Lithuania.

The shipper from Latvia will determine the point of delivery according to the criteria mentioned in situation A. The shipper has to determine:

- a) whether it has to register as VAT payer in Lithuania according to the VAT law of Lithuania, and
- b) whether the threshold of registration is reached (in Lithuania is 45 000 EUR; source: <http://www.vmi.lt/cms/en/pridetines-vertes-mokestis-pvm->).

If the shipper from Latvia sells gas to a person not subject to registration as VAT payer, such obligation will certainly arise.

Overall tax regimes, if a company wishes to perform business activity selling products or offer services in other countries:

- a) Income tax: the laws on other countries set the obligation of registration and payment of tax. If the convention for avoiding of double-taxation and evasion between the countries is signed, (hereafter – Convention), the obligation of registration exists in the cases corresponding the ones set by Convention. The Conventions are in force with both Lithuania and Estonia.
- b) Excise tax: the specific law in the country of consumption have to be followed.
- c) VAT: Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax sets general rules for application of VAT, but the transposition into national laws may differ. In general, the rate of 0% is used for deliveries of goods between EU VAT subjects of the reverse VAT payment scheme is applied for services provided within EU (the important exceptions exist). If the goods are delivered or services provided to the EU subjects with no VAT responsibilities reaching the nationally set threshold (35 to 100 thousand EUR), the originator is obliged to register and pay VAT in specific country. Standard rates are: Estonia 20%, Lithuania 21% (source: [http://europa.eu/youreurope/business/vat-customs/buy-sell/vat-rates/index\\_lv.htm](http://europa.eu/youreurope/business/vat-customs/buy-sell/vat-rates/index_lv.htm)).
- d) Customs: the delivery of goods is not taxed, but the customs status of the goods has to be checked. If the goods are not cleared for free circulation, the customs declarations has to be provided by one of the parties. Natural gas as the product has no import tax, but customs procedures exist. VAT directive suggests application of 0% rate for the import of natural gas, but national specifics may exist.

Member of the Management Board



Zane Kotāne