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ERGEG public consultation on "Capacity Allocation Mechanisms and Congestion Management Procedures"

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Dear Mrs. Geitona,

We appreciate the opportunity to give our opinion on the ERGEG consultation paper "Capacity Allocation Mechanisms and Congestion Management Procedures".

Before entering into a more detailed discussion on the consultation document, we would like to point out basic principles on which any capacity allocation mechanisms and congestions management procedures should be based:

- Capacity is calculated efficiently
- Maximum of capacity is allocated to the market
- Capacity allocation is market-based and non-discriminatory
- Market participants use their rights efficiently
- There is the necessary level of coordination between TSOs and regulatory authorities
- Information about flows and capacities in networks are transparent and openly accessible in real-time[1], provided that the confidentiality of commercially sensitive information can be preserved

EnBW also believes that these principles and the following positions – although they may be deemed necessary for a non-discriminatory access of market players to essential facilities such as pipelines – they are not necessarily applicable to other infrastructures such as storage facilities, where other technical and commercial parameters may exist.

[1] The ERGEG consultation document talks about „potentially contractually congested cross-border interconnection points" (p. 9). We do not understand this notion – by offering transparent information about flows and available capacities TSOs should be able to undoubtebly show if an interconnection point is physically and/or contractually congested or not.

2. The scope of ERGEG's principles and of the derived proposals covers bringing capacity to the market where there is currently contractual congestion. Do you agree with this approach?

EnBW agrees with the general approach of proposing measures by which unused capacity currently held contractually is made accessible to the market and by which TSOs are encouraged to offer capacity which is not yet available, however we reject the approach as proposed pursuant to G2.2.1. According to this concept a reasonable proportion of the available capacity should be set aside for short-term capacity products to be offered on a firm basis, unless the primary and secondary market and the UIOLI procedures provide shippers with satisfactory access to capacity. This approach implies the opportunity for regulators to deprive long-term shippers of their capacity rights even if the contracted capacities are fully utilised. EnBW believes that the market position should not have a decisive impact on the regulation of capacities.

Furthermore it is the intention of the aforementioned approach to restrict the market position of dominant players. Yet we would like to stress the fact that a European approach is de facto impossible since a common understanding of dominant players does not exist; the definition may vary between Member States.

EnBW instead believes that capacities should only be made accessible to market players on the basis of transparent and non-discriminatory secondary market mechanisms – as conceived in the Third Energy Package.

We also see it as problematic for a shipper to lose its capacity rights completely for the whole term as pursuant to G4.2.3.

3. In principle, European regulators consider FCFS allocation potentially discriminatory. Do you share this view? What do you think about the proposed mechanisms (OSP with subsequent pro-rata allocation or auctioning)?

EnBW agrees that FCFS allocation is a potentially discriminatory approach, particularly where it applies to physically congested points. Allocation procedures should be based on auctions as it is done in the power sector.

4. In your view, what is the future importance of the proposed capacity products (firm, interruptible, and bundled) and of the proposed contract duration (intra-day up to multi-annual)?

EnBW agrees that there is a need for multiple capacity products with different terms ranging from multi-yearly to intraday products. The market needs indeed a variety of capacity products. The focus should be on a capacity allocation primarily on the longer term (yearly and multi-yearly products) which then allow the holders of capacity to slice and dice the capacity in shorter term products (e.g. quarterly, monthly, daily). As supply contracts are usually fixed on an annual or multi-annual basis, capacity products need to have the same set-up in order to allow for a sensible hedging of the shipping risk.

5. What is the role of secondary capacity trading?

Secondary trading offers the possibility to optimise trading portfolios. In order to guarantee optimal market efficiency, market participants not already holding capacities can use secondary capacity products to avoid carrying imbalance positions or the risk of not being able to deliver on contracts. On the other, market participants holding primary capacities can use secondary capacity trading to slice and dice their products and make unused products available to the market, i.e. splitting up a longer term capacity product into more shorter term products (example: a yearly product is split up in quarterly or monthly products).

We therefore see secondary capacity trading most of all as an optimisation tool to make use of a maximum of capacity. TSOs should provide a central register for capacity rights holdings, yet we do not necessarily share ERGEG´s view that TSOs should also run the actual secondary capacity trading platforms.

6. and 7. How do you assess the proposed measures to enhance the availability of firm capacity and to improve short-term and long-term congestion management? What are your views on the proposals? Do they address the problems? Will they lead to more effective capacity allocation methods being developed?

EnBW welcomes the following measures and sees them essential for the development of a liquid European gas market:

- Close cooperation between TSOs by sharing grid information to increase the available capacity by using dynamic capacity calculations – we see coordinated capacity calculation methods as an important step towards more capacity
- Close cooperation between regulators by e.g. deciding on common regional approaches
- Close cooperation between regulators and TSOs in order to allow the implementation of the same procedures and standards on all borders and allow the same incentive schemes and the same rules for revenues of TSOs
- Offering capacities in a transparent and non-discriminatory manner as firm and interruptible capacities in multiple terms
- Application of user consultations for any capacity offer developed by TSOs
- TSOs shall maximise firm capacity under consultation of the relevant market players on a regional level to assess how much infrastructure/capacities it needs.

On the other hand, we see problems with examples of other proposals in the ERGEG consultation document:

- A proportion of the available capacity shall be set aside for short-term capacity products (see p. 15, 2.3.2) – **our view**: the allocation of capacity should preferably be allocated in the longer term, the market should then decide how to "slice and dice" the products. Short-term products are then the outcome of the unused capacity from long term products

- Allocation of existing capacity: "the CAM utilised should be either pro-rata or auctions" (p. 18, 2.4.2) – **our view**: pro-rata methods are from our point of view not market-based, we therefore call for auctions in any case
- Allocation on pro-rata basis (p. 19, G3.1.1) – **our view**: as mentioned above, pro-rata methods should not be part of any allocation mechanism
- Booking platforms: all capacity is to be allocated via this TSO platform (p. 20, G 3.3) – **our view**: TSOs are natural holders of capacity rights and they should hence be responsible for capacity administration, though especially when it comes to secondary capacity trading we see no obligation to run the actual trading procedures through a central TSO platform. TSOs should in this case provide for a central registry on which any kind of trading platform could connect to. Not the TSOs should seek to reduce the number of platforms but the market will.
- "Short-term flexibility is a basic requirement for the development of competitive markets." (p. 22, 2.5.3) – **our view**: there is no doubt that the market also need short-term flexibilities, these can either be offered by short-term capacity rights or by storage products. EnBW is however against a focus on the short-term alone and against a reservation of capacity for short-term products. We advocate for a focus on longer term products that can be sliced and diced to shorter term products.
- UIOLI procedures (pp. 21) – **our view**: EnBW rather calls for an UIOSI[2] approach as it is used in cross-border trading in power.

8. Are the needs of shippers performing supply activities properly taken into account?

We see absolutely no need in dividing shippers up into different classes (performing and not performing supply activities) and therefore cannot give an answer to this question. Each shipper must be treated equally in terms of capacity allocation regardless of his motivation "via transparent, fair and non-discriminatory allocation procedures" (p. 9 of the consultation document).

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[2] No matter which methodology is applied we agree that anti-hoarding provisions are required to ensure the efficient usage of capacity and to protect against capacity holdings being used to limit competition in the underlying product market. Our argumentation goes further than the UIOLI approach taken in the ERGEG consultation paper. Capacity holders must have the opportunity to receive the benefits of the rights they have purchased. In the UIOLI approach we understand that the unused capacity falls back to the TSO in the day-ahead timeframe who then markets it on the secondary market. The compensation paid would be on the basis of the primary contract. The Use-it-or-sell-it approach (UIOSI) is a more refined version giving the capacity holder the right to decide how to market the unused capacity (himself or through TSOs/OTC) while receiving the actual value on a day-ahead basis (this value can be 0 as well; we envisage a day-ahead trading scheme similar to schemes used in the power sector where capacities have to be nominated until a certain gate closure time. After this GCT the unused capacity will be sold on the secondary market.)

9. Are the proposed measures suitable to facilitate development of liquid gas markets?

The proposed measures are in part suitable to facilitate the development of liquid gas markets - they are necessary but not sufficient. We see that the major problem in the ERGEG consultation is the fact that renomination rights would change mostly for those market participants already holding large quantities of capacity. Therefore some ideas like the principle addressed in the 2plus2-rule could be a way forward. However, these measures do not resolve the problem of renomination rights. One important question is therefore how to get those market participants to give up their opposition to such changes before changing the existing rights by regulatory measures.

Interlocking of different measures is from our point of view the key for the establishment of liquid gas markets, every stakeholder has a responsibility: market participants willing to change the quality of renomination rights, TSOs to cooperate closely and to calculate their grids dynamically and regulators developing regional approaches and cooperation.

Whatever the approach to be taken, it must be market based and non-discriminatory with the aim of maximising firm capacity available to the market.

10. In your view, how important are compatible booking and operational procedures between adjacent systems?

The improvement of coordination pursuant to G2.4 and establishing of compatible booking and operational procedures between adjacent systems according to G2.3. are important prerequisites for more efficiency and liquidity in European gas markets. Bundled standard products and the relating booking platforms have to include all relevant common rules and mechanisms for nominations, balancing, auctions etc. on either side of the border are an essential feature to minimize costs for trading cross-border. However, the availability of compatible procedures necessitates a high degree of cooperation between adjacent TSO systems and between TSOs and their respective regulators. A clearly regional mindset is needed to attain workable solutions for market participants. Offering these procedures however is from our point of view only one aspect on a micro level. The even more important aspect on a macro level is the question of how a European pipeline system can be optimised.
However pipeline congestions are not solely limited to contractual conditions. Only where contracted capacity is regularly used and congestions are highly likely to occur additional capacities should be physically extended through further investments. However this issue is not explicitly covered in the proposed principles. Without consideration of physical congestion and their elimination the issue of bottlenecks cannot be adequately mentioned. We therefore emphasise, that physical congestion shall be additionally addressed. In this context we would like to refer to the growing investment requirements resulting out of the changing of gas flows due to new infrastructure projects (e.g. LNG import terminals). Despite common GGPOS there is a lack of coordination between TSO's particularly at cross border points.

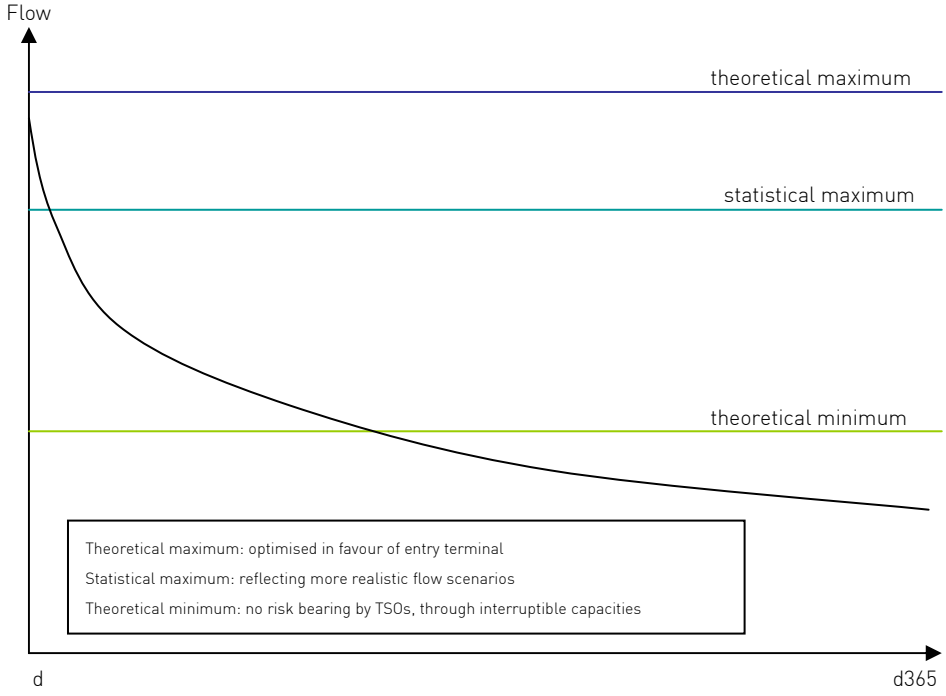
In order to improve the required investment climate, it is necessary to grant same incentives for affected TSO's resulting from similar regulatory regimes and therefore better collaboration among regulators. Open seasons have been initiated only sporadically so far. This prevents shippers from entering into binding commitments and reversely hampers needed investments. In order to avoid these disadvantages new capacity or physical capacity enhancement should remain possible on a bilateral basis between shippers and TSO's.

Therefore quick wins to get compatible procedures are highly desirable but this can only be one step ahead with more following.

11. Do the proposed measures increase the efficient use of the system? What aspects would you support and like to see further developed?

With its initiative, ERGEG seems to focus on enhancing the availability of short term firm capacity rather than long term. Whereas EnBW believes that the integration of European markets does require the release of additional – short and long term – transmission capacity, EnBW also believes that there is a huge potential in maximizing available capacity through improved methods of capacity calculation, in particular the implementation of dynamic modelling by TSOs.

Capacity calculation approaches



When calculating technical system capacity, TSOs currently use a scenario approach that ensures smooth operation of nominated flows even under hostile circumstances, e.g. sudden drop in temperature, unplanned outage of production

field or storage. It is basically because of this approach that interruptible capacity still plays a major role in continental gas transport: it releases – probably – unused capacity to the market without putting TSOs at risk of having to compensate capacity holders in the unlikely – although possible – case of usage. But as this "probability" can be statistically calculated by TSOs, there is a realistic possibility to allocate this risk fairly and maximizing the available technical (i.e. firm) capacity to the market.

Therefore, TSOs should move to a **maximum technical capacity** approach that takes into account a certain risk of not being able to deliver all the sold capacity. TSOs should be entitled and obliged to buy back capacity at a market price in the – unlikely– event, that they cannot fulfill their obligations (capacity buy back mechanism). Certainly, this approach requires that revenue regulation of TSOs is adjusted accordingly in order to allow for symmetric risks and chances, regulators should ensure that TSOs have appropriate compensation and incentives to improve their modeling capabilities as an immediate priority.

One element shortly mentioned in the consultation document is the question of incentivisation of TSOs in order to guarantee more capacities are available to the market. Though in principle one task of a TSO is to make a maximum of capacities available to the market, we see that additional incentivisation may make TSOs willing to free more capacities if the possible extra financial risk is convered by extra revenue. We therefore agree that a simple incentive could be an effective replacement of complex rules. If, for example, a TSO introduces measures to make more capacity freely available to the market at a certain point it could be rewarded for this by allowing a certain extra revenue for a limited time. In another case, if a TSO defines a congestion as a clear physical one and arranges building new capacity that will be freely available to the market, the TSO could then also be rewarded by an extra revenue.

Last but surely not least, EnBW would like to see further measures and commitments to ensure the coordination of regulatory decisions across borders in the area of CAM and CMP as being the key prerequisite of further market development and integration. We agree that current national approaches are "a source of capacity mismatches at many interconnection points and, hence, sub-optimal use of infrastructure, which is an obstacle to cross-border gas trading" (p. 6 of the consultation document).

Yours sincerely

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