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Dear Sirs

**ERGEG principles: Capacity allocation and congestion management in natural gas transmission networks**

Thank you for the opportunity to comment on the above consultation document. As a shipper across several Interconnection Points, BP wishes to make the following comments. These comments are not confidential.

Given the levels of contractual congestion at interconnection points between gas transportation systems, and given that most transportation capacity is held under long term contract by (current or former) supply affiliates of the TSOs, then only a very small proportion of capacity is available to traders and alternative suppliers on a primary basis. Any proposals that look to address this issue are to be welcomed.

Any final proposals need to include harmonization of issues such as measurement units and parameters, temperature and pressure, the timing of the start and finish of the gas day, booking and notice periods, the inclusion of tolerance services as well as the means of trading the product on the secondary market.

Information transparency is vital on certain aspects of system operation such as system capacity, capacity sold, capacity still available and the utilisation rates.

On the specific questions within the document our comments are as follows.

**1. Do you agree with the problems that ERGEG has identified with capacity allocation and congestion management? Are there other aspects that should be taken into account?**

We agree with the problems identified and are supportive of measures to rectify these issues. The need to incentivise the TSO to release all available capacity and the need to encourage the active trading of capacity on the secondary market are both essential to the success of any solution proposed. Having efficient UIOLI rules in place will add to the efficient use of the pipeline system and will encourage greater utilisation rates

In addition to the issues addressed, we would suggest ERGEG consider the importance of transparency in tariff setting – especially when TSOs are seeking to underwrite a considerable investment program; the revenue setting mechanism for TSOs, which currently allows TSOs to recover their revenue entirely from capacity bookings, with no incentive to encourage efficient throughput; the value of a bottom-up process, where regulators are empowered to address cross border issues in their own jurisdiction as they occur, rather than impose a top-down model that may be geared towards problems in some member states while at the same time causing difficulties in others.

**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?**

Many of the principles proposed in the paper will help achieve a more harmonised capacity regime at cross-border interconnection points. In particular we support: obligations on cooperation between TSOs; alignment of codes, contracts and procedures; maximisation of capacity availability; appropriate incentives; and a range of firm and interruptible capacity products.

Nevertheless, we have concerns about three areas of the approach:

- How actual and potential contractually congested points will be identified and defined. A single point may be physically congested in winter but only contractually congested in summer; it is not always possible in advance to determine when each will be the case. Sales of interruptible capacity will confuse this further. For this to be successful a comprehensible, objective means of identifying actual (and with more difficulty, potential) congestion.
- Firm day-ahead UIOLI will undermine the value of primary capacity holdings. This is especially dangerous to investors in cross-border flexibility, who would need to hold two capacity products in place of one in order to exercise their flexibility – a product that is exercisable up to the day ahead, and one that is exercisable within day. This will create significant difficulty in the establishment of regional balancing markets. Additionally, it is unclear how holders of primary capacity will be compensated for the reduction in option value, particularly where their bookings have been used to underwrite open season investments. Finally, the interaction with interruptible services and balancing aggregation is unclear, particularly where regional products or services are involved. We would not support this proposal in its current form.
- Long-term UIOLI / withdrawal of unutilised capacity does not address the additional risks conferred on an investor, if a shipper has underwritten the investment with a long term capacity contract which is prematurely terminated.. Equally, it suggests that an unusually mild winter could lead to the termination of certain rights that might prevent a supplier fulfilling

commitments in the following winter under a return to seasonally normal conditions.

**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)?**

In a constrained market, the First Come/Committed First Served (FCFS) booking service does not allow for efficient allocations of capacity, as a buyer with slower communication links can be prioritized lower in spite of placing a higher value on the available capacity. In particular, there is a concern that affiliates of TSOs may have information or communications advantages in terms of hearing of capacity availability and registering interest. This can be resolved in part by allowing all requests in an initial period to be treated as if received at the same time. For constrained markets, auctions or open seasons are, however, preferred.

With regard to allocation mechanisms, it is important to distinguish between new capacity that has not yet been constructed, and existing capacity. For new capacity, Open Subscription Windows are one method, though auctions are also possible. In neither case does this resolve issues such as what proportion of the new capacity should be underwritten. An economic test that is compatible across all market areas needs to be implemented for this purpose.

The Last Committed, First Interrupted principle should not be seen as an effective constraint management tool and should not be used for this purpose.

For existing capacity, other techniques may be more suitable, depending on circumstances.

**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)?**

Shippers require a variety of products to monetise their gas. Bundled products must not discriminate against those who choose to only hold capacity on one side of an interconnection point. As an alternative to a bundled product, unbundled products could be offered on a linked basis or under conditional bidding. This would allow parties who hold capacity on one side to match this up with capacity in the connected system on the other side of the interconnection point. Where auctions are not coordinated, it may be possible to include conditions precedent on success in the related auction or capacity could be handed back to the relevant TSO by the shipper. These unbundled products should also be offered as the same product type either firm or interruptible, but not a mix as this renders the whole booking interruptible regardless of any firm product offering.

Reserving part of the capacity on offer for short term bookings could encourage new entrants to the market. Although we would prefer to see the duration of this capacity being two years or less rather than the one year or less as proposed in the consultation document.

**5. What is the role of secondary capacity trading?**

Secondary capacity trading is crucial in promoting open access to transportation capacity. As the current model stands once the capacity is sold the TSO has absolutely no incentive to facilitate the workings of the secondary market. There is also the problem of national legislation that needs to be addressed in certain countries to enable a fully functioning secondary market.

One possible solution to facilitate better access to capacity would be to split the revenues that TSOs receive into Capacity/Commodity elements. (i.e. only a proportion of the allowable revenue is derived from capacity sales and a significant part depends on levels of throughput; therefore the TSO is encouraged to ensure that capacity is made accessible to parties who will use it, and they are less inclined to build capacity that will not be used.) If that were the case TSOs would be incentivised to increase throughput. They would therefore be incentivised to facilitate the efficient workings of a secondary market by putting the necessary trading platforms in place. This could be seen as one way to encourage greater liquidity in the market.

Having an effective UIOLI process in place should also help to facilitate an active secondary market. Where the majority of capacity is held by incumbents, measures that prevent the hoarding of capacity must be encouraged.

**6. How do you assess the proposed measures to enhance the availability of firm capacity and to improve short-term and long-term congestion management?**

See the response to Q2 above for our views on short term firm UIOLI and Long-term UIOLI

In addition to the concerns already expressed, we would add that the example of short term firm UIOLI that is set out in the consultation would not work in all member states. For example if this were to be introduced into the GB market it would cause a problem rather than solve a problem, by restricting the ability of holders of storage and other forms of capacity from responding to market events. To restrict renomination rights in this way is going to harm the value of capacity on the secondary market and could severely curtail that market.

Offering capacity to the market via auctions or open seasons should be the preferred solution. But it is important to have a transparent economic test that regulators approve to allow capacity build. TSOs should publish clear methodologies detailing how they decide to invest in new capacity. This should include mechanisms for how shippers can trigger investment in new capacity and how regulators will interact with the TSO in developing an economic investment model. All these factors need to be considered to facilitate a functioning market.

**7. What are your views on the proposals? Do they address the problems? Will they lead to more effective capacity allocation methods being developed?**

BP welcomes the majority of the proposals within the document but is mindful that without greater transparency and active secondary markets these initiatives will not evolve in to anything of substance.

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

There should be no distinction between shippers with supply activities and shippers that are mainly carrying out trading.

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

An improvement in the liquidity of the wholesale market occurs when there is an increase in:-

- The number of players active on the market
- Price transparency
- Number of trades taking place.

Better access to transportation capacity, including better access to capacity for new entrants should increase the amount of players active in the market. Short term auctions for congestion management will improve price transparency and it will also encourage the optimal allocation of gas to where it is valued the most. Any improvement in interconnection capacity should encourage shippers to trade more at the hubs as they can arbitrage between countries (however, this is not the only thing that needs to be changed to improve liquidity at the hub).

Most of the proposals in the document will facilitate competition in the wholesale market, however, we are concerned with the limitations on the renomination time and the effect this could have on the value of capacity be it primary or secondary. There must also be a question over whether this aspect of the proposal could be seen as discriminatory.

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

Very important, without cooperation between Interconnection Points it will be almost impossible to implement. TSO's must be encouraged to coordinate the release of similar capacity products. They should also agree to the release of some bundled (or linked) products across IPs. But as stated above these proposals must not disadvantage those shippers that wish to only hold capacity on one side of an IP.

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

The proposed measures if implemented may see an increase in the efficient use of the system where a constraint exists. For these proposals to work the TSO must be incentivised to take greater risks where the release of firm capacity is concerned. TSOs should be encouraged to release more capacity than the system could physically take. If nominated flows are greater than physical capacity the TSO could use buy-backs as a constraint management tool. This could also solve the historical problem of incumbents holding all the available capacity for security of supply reasons by making more capacity available on the short term market.

It is important that incumbents that are holding capacity for historical security of supply purposes should be encouraged to develop products that can release this "stranded" capacity back to the market when it is not required for SoS activities.

TSOs should publish baseline capacities at interconnection points. These baselines should be open to regulatory scrutiny.

We hope that you find these comments helpful. If you wish to discuss further please don't hesitate to contact me on the number above.

Yours sincerely

**Andrew Pearce**  
**Regulatory Affairs**