Response GasTerra to Public Consultation: ERGEG principles for CAM & CMP

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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?

ERGEG paper:

ERGEG page 2: Regulatory and contractual obstacles to cross-border gas flows remain a major barrier to market integration at a European level.
ERGEG page 3: underdeveloped network access for new entrants is identified as a barrier to entry…capacity is fully booked on a long term basis, hindering the development of competition.
ERGEG page 4: the difficulty of new entrants in obtaining capacity. This is due to the lack of available capacity at many cross-border points and to some discriminatory aspects of allocation mechanisms. This situation contributes to an inefficient use of existing capacity (short term and long term) an a lack of liquidity on most European markets.

GasTerra:

Regulatory and contractual obstacles to cross-border gas flows are part of the problems which market integration is facing and solutions to this problem can indeed contribute to a better functioning of the market. At the same time all aspects of the market situation should be taken into account, including the fact that stability and flexibility of access is paramount to shippers and for the guarantee of security of supply.

ERGEG paper:

ERGEG page 4/5: The contracts allow the historic capacity holder to re-nominate, typically until two hours before the relevant gas flows are to commence. Thus capacity not used by such historic capacity holders is either not released on the secondary market or, if it is, it is only released on a very short-term and interruptible basis. Therefore, congestion management measures need to be implemented more effectively to achieve the goal of functioning third party access and competitive gas markets.

GasTerra:

Re-nomination rights are needed for the market to work (e.g. balancing) and also because a lot of the obligations in commercial contracts are based on the transport capacity rights held. Some examples are given below:

1. There are a lot of commercial gas delivery contracts in which parties have agreed to deliver the gas on the border. This means that the seller has booked transport capacity on one site of the border (exit capacity) and the buyer has booked transport capacity on the other site of the border (entry capacity). Furthermore, suppose the parties have agreed in the contractual arrangement that the buyer of the gas has the ability to decide until 2 hours before the hour that the gas flows how much they want to flow. This sort of contractual arrangements are based on the existence of renomination rights. In case

renomination rights are restricted the selling party can get into contractual problems if during the day the buying party decides that they want to flow more gas than previously anticipated. There will be costs associated with this (contractual penalties). So, if renomination rights are restricted the shipper in the described situation wants to make sure that he gets enough value for the part of the renomination rights that he had to give up to pay the eventual contractual penalties.

2. There are shippers that have access to flexibility on one site of the border and sell this flexibility on the other site of the border. Suppose in this case that the shipper has transport capacity on both sites of the border (exit and entry capacity). Especially on the short term this flexibility has value, because parties have to balance their portfolio's. If renomination rights are restricted, part of this value is taken away. In this case the shipper wants to make sure that he gets the same value for the part of the renomination rights that he had to give up as what he expected to get in the market. In this situation it could be that the flexibility is used to balance his own portfolio (alternative is buy flexibility on the other site of the border or pay penalties to the TSO) or sell it to someone else. The valuation of the renomination rights depend on the situation the shipper is in.
3. There are X-border points where parties do not have to nominate, but where one party is balancing shipper. This means that there can be contractual arrangements where the selling party is delivering exactly the amount of gas that the buying party takes, where in the Dutch system the offtake at time t must be in balance with the delivery at time t+2. Suppose in this case also the situation as described under 1.) applies. This means that the selling party does not know (until two hours before the gas has to flow) how much exactly must be delivered. The whole system of restricting renomination rights does not work in this situation.

In the above cases 1.) and 2.) shippers might want to give up part of their renomination rights as long as they are sure that they get the right value in return to either pay penalties due to possible breaking contractual agreements or the value that they expected to get by using the rights for short term delivery of flexibility. In the above case 3.) nomination rights are not applicable.

ERGEG paper:

ERGEG page 5: in an efficient market, all technically available capacity would be used and demand for additional capacity would signal the need for investment.

GasTerra:

In practice not all technical available capacity is used all the time, but all the technical capacity IS needed on some peak hours. The same holds for long-term capacity that is needed for a commodity long-term contract; the capacity is not used all the time, but it IS needed on some (unpredictable) peak hours.

ERGEG paper:

ERGEG page 6: One existing barrier may be that some of the current capacity allocation methods do not create pricing signals that would encourage shippers to sell on exces capacity. A market-based approach to capacity allocation through auctions may create such incentives.

GasTerra:

Auctions are a good way to allocate capacity as long as they take place on a regular basis (such that transport capacity can be purchased when opportunities on the commodity market occur).

ERGEG paper:

ERGEG page 6: …where the congestion is physical, then investment should be considered.

GasTerra:

Where capacity is long term fully booked and the booked capacity is needed and there is a demand for more capacity, investments should be considered.

ERGEG paper:

ERGEG page 8: If shippers are to have an incentive not to hoard extra capacity for peak periods, they must know that they can buy capacity for shorter durations on a regular basis.

GasTerra:

Shippers have bought capacity in the past, because it is needed for commodity contracts. If shippers would sell this needed capacity and rely on a short term market for transport capacity they introduce a price risk or if they can not purchase the needed transport capacity on a short term market they introduce the risk of penalties for not being able to deliver commodity.

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?

GasTerra:

The availability of capacity on cross-border points should be such that it supports the creation of a NW-European market. On side of the coin is resolving the contractual congestion. Available, unneeded and new capacity must be shared among market participants on a level playing field. On the other hand, in order to promote competition on commodity and to create one integrated (NW) European market, and most importantly: in order to guarantees security of supply, a certain overcapacity on infrastructure is needed. Where such overcapacity is not available (physical congestion), CMP may not always be enough. A regulatory environment promoting investment should be created, even if that is outside of the scope of ERGEG's principles, in practice both approaches (CMP and regulatory environment promoting investment) complement each other.

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)?

GasTerra:

The most important criterion for allocation of capacity is that market participants can obtain it in a level playing field and that it supports the creation of a commodity market. This means that when opportunities on the commodity market occur, all market participants must be equally able to purchase additional transport capacity.

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)?

GasTerra:

A variety of capacity products should be available, such that all sorts of commodity deals are supported.

5. What is the role of secondary capacity trading?

GasTerra:

Secondary capacity trading is the preferred method of re-allocating unneeded capacity on the short term (day ahead). The secondary capacity market is not a basis on which market participants will make long term commodity deals.

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?

GasTerra:

There are a number of mechanisms proposed that try to free up some of the transport capacity such that it becomes available to the market on a day ahead basis. Some mechanisms imply that shippers (voluntary or obligatory) put some of their transport rights back on the market. An important base principle in these mechanisms is whether a shipper can decide on the price he wants for his rights or that the market or others decide this for him. We want to stress the base principle that if a shipper (has to) deliver part of it's transportation rights back to the market than that shipper must be able to decide what price he wants in return.

ERGEG paper:

ERGEG 1.2.1 page 5: Guarantees should also be given that, if not used, capacity will be brought back to the market. UIOLI mechanisms achieve this aim by maximizing the use of pipelines, while also at communication the willingness of the regulators' and transporters' to deter capacity hoarding when capacity is fully allocated under long term contracts. Other mechanisms such as capacity release could also help to provide new entrants with firm capacity in case of market domination by incumbents.

GasTerra:

A much more preferable mechanism is UIOSI where market participants are encouraged to sell unneeded capacity on the secondary market. The main challenge is to interconnect commodity traders, operating in a non regulated market, within the regulated facility networks. Networks should provide to commodity traders enough facilities in such a way that the market is liquid and functioning: security of supply and competitions to end-consumers. In such a challenge Europe experienced that 'over' capacity is needed in order to provide enough market mechanisms. In this setting the UIOSI is a much better tool, challenging the bridge between commodity traders and regulated facilities.

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

GasTerra:

See other answers.

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

GasTerra:

In the past, supplying shippers have bought transport capacity that is needed for supply contracts. Taking away the needed transport rights will introduce financial risks for the supplying shippers.

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

GasTerra:

See answers before on the disadvantages of some proposed measures.

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

GasTerra:

Essential, but for an efficient commodity market not only the transport capacity bookings and procedures should be compatible between adjacent systems, but they should also be compatible with all sorts of commodity deals.

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

GasTerra:

Not if parties risk the loss of needed capacity.