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taking care of the essentials

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To Nathalie Burton
ERGEG
Via Email

11 November 2004

Dear Nathalie -

ERGEG Public Consultation on Guidelines for Good Third Party Access Practice for Storage System Operators (GGPSSO) [Dated 6 October 2004]

Centrica Storage Limited (CSL) offers the following comments on ERGEG's two papers - the Position Paper and the proposed Guidelines.

These comments are non-confidential.

Copies of this response are being sent to Ofgem, as the relevant UK regulator, and to the UK's Department of Trade and Industry.

Key Issues –

- Principles, Timescales and Implementation

CSL is the major provider of third-party storage capacity in the UK - it and its predecessors have been providing Third-Party Access (TPA) to our capacity for 10 years. We are also a user of TPA capacity, secured from one of our competitors. Drawing on our experience, we are firmly of the view that effective third-party access to gas storage is a key element of liberalisation of European gas markets and is vital in ensuring the development of real competition.

Hence we are strongly supportive of ERGEG's desire to provide guidelines on good practice in providing third-party access to gas storage throughout Europe.

However, CSL believes that effective TPA to gas storage facilities requires three main conditions. Clearly a good storage contract is necessary, which of course is addressed by many of the GGPSSO proposals. But in addition there must be a transportation (or network) code which facilitates the use of storage services for balancing a shipper's or supplier's gas requirements, which gives clear and commensurate incentives to achieve such a balance and which provides practicable means of moving gas between the storage facility and any relevant balancing or demand point. Also, there must be a relevant gas market or means of forecasting forward imbalance exposures, so that storage users can see any prospective difference in value between gas injected and withdrawn.

CSL therefore questions whether early implementation of any GGPSSO proposals is likely to be worthwhile for storage facilities where the local transportation arrangements and/or market access arrangements fall short of the appropriate standards and where there are no PSO obligations that would alternatively generate demand for storage services. In our view, GGPSSO will simply be ineffective if or while there are other barriers to competition.

In addition, although there are many experienced users of storage capacity anxious to spread their presence and activities into new markets, CSL believes that there will normally tend to be a "maturing" phase for most storage services – as new players become familiar with the access rules for the services and how they can best be used in particular local environments. Hence CSL recommends that the relevant regulatory authorities should be prepared to be flexible in the required implementation plans for the various markets. We believe that the aim should be to introduce basic TPA as quickly as possible, comprising for example, standard bundled units of capacity and support for secondary trading of unbundled capacity elements, with operating rules which are as flexible as the facility and the transportation system can accommodate. We naturally would recommend that existing TPA practices which have proved attractive to users are considered as possible models.

However, we further believe that it is likely to be impractical to seek to insist on storage operators (or in some cases their users and potential users) moving immediately to very complex arrangements where there may be no urgent need. We strongly urge that any adopted GGPSSO document should admit timescales which are practical taking into account the current position in a market and the aspirations of potential storage users.

This may mean that a more flexible approach to deadlines than in the current draft papers is appropriate.

- Storage Revenue Risks

A further major issue in such immature markets centres on the risk that a SSO offering TPA may find that demand for such services is low at prices needed to cover the SSO's costs.

Where rTPA applies, the regulator should take into account the SSO's potential sales and income levels in assessing the likely outcome of any pricing proposals. Ideally, the SSO should receive an appropriate rate of return on investment taking into account the predicted storage utilisation.

However, care needs to be taken to try to avoid the risk that prices are set which would cover the SSO's costs if all (or nearly all) the storage capacity is sold but which might result in insufficient capacity being sold. In this event, the SSO might fail to get enough revenue to justify retention of the storage facility but, especially where this is a result of distortions during a transition to a competitive market, the regulator might conclude that closure of the storage facility is not in the long-term interests of the relevant market.

Increasing the tariffs would clearly not be likely to solve the problem, so the regulator would need to consider how a SSO in such a situation should be remunerated for keeping the storage facility operational, and how the resultant cost should be funded.

We believe in general that a major issue for regulators and for European Storage Operators should be how pricing issues are best addressed where "market forces" might result in insufficient costs to justify ongoing retention of storage facilities, despite the widely-expressed concerns over future security of supplies and the possible need of marginal storage facilities to assist with future PSOs; and we think the ERGEG paper should recognise this though it may not strictly be a "GGP" matter.

Indeed, it seems very desirable that regulators contemplating pressing for storage TPA where other arrangements may currently exist should consider whether the change may risk a loss of storage capacity which might jeopardise security in the short- or long-term.

ERGEG Position Paper

- The Choice between negotiated and regulated access to storage services

CSL would observe that the Paper refers to "negotiated and/or regulated access" as if these are substantially distinct and mutually-exclusive approaches. As is widely known, the UK has facilities where some aspects of the storage services are regulated and other aspects are negotiated, as well as some facilities that are exempt from the requirement to provide third-party access. For example, general contract and access terms may be subject to regulation while prices for services can be negotiated (subject to non-discrimination requirements). We suggest that the two papers should make clear that a flexible approach to regulation such as this is relevant and desirable.

- Transparency requirements

In our view, the general comments about the desirability of publishing "on-line" information covering "commercial and operational" areas have failed to take account of a potential severe and discriminatory commercial exposure for some SSOs.

CSL supports the on-line publication of substantial commercial and operational information, and indeed has a web-based system that provides a wide range of information, some password protected.

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However, the ERGEG comments appear to have been taken by some parties to embrace publication of "real-time" information on gas flows and gas holdings (based on the references to "real time" information in paragraphs 6.1 and 6.6 of the Draft Guidelines), and this would pose several significant issues.

First, this type of information is expensive to provide, and arguably the cost is rarely justifiable.

Second, any proposal that a SSO must provide "real-time" information to cover gas flows and gas holdings would be discriminatory unless at least all other major system entry points serving any relevant market are also required to provide similar information: storage services can provide a valuable source of flexibility but usually are alternatives to other forms of flexibility – having such information from one type of source published, while comparable information about other types of flexibility is not, will generally reduce the perceived value of storage services and thereby disadvantage affected storage operators.

Third, and most importantly, if storage operators are providing a "nominations whole" service as envisaged by paragraph 3.4 of the Guidelines paper, then the SSO is normally compelled to buy or sell gas to meet the differences between physical flows and aggregate net nominated flows. If the physical flow data is published "in real time", then the market participants will be able to see if flows into the storage facility alter – in particular, they will be able to see if there were a failure and flows reduce suddenly. This would leave the SSO exposed to selling gas (if the failure were on injection) or buying (for a withdrawal failure). The SSO would be a "distressed" seller or buyer, and the market would be aware of his position and exposure. This would be blatantly discriminatory, unless comparable real-time data would be available for all other entry points and for major exit points.

Simply, the principle of "holding whole" is incompatible with the publication of real-time gas flows.

In this context CSL believes that the principle of having "nominations whole" (where practicable in the light of the local balancing regime) is more important and valuable to customers than any form of real-time information on gas flows.

On the other hand, if customers' gas flow allocations into or out of storage facilities are based on actual flows, then clearly prompt information on changes in flow rates are very valuable to those customers, and the value may generally justify the costs of providing such information. CSL therefore concludes and recommends that publication of real-time flow information may be appropriate where customers' flow allocations will normally be determined or affected by actual gas flows in or out of a facility but that such publication cannot be appropriate where storage customers' nominations will usually be "allocated whole".

CSL considers that this should be made clear in Section 6 of both papers.

CSL provides other detailed comments in the later discussion on Section 6 of the Guidelines.

CSL also recommends more clarity regarding circumstances where publication of aggregate nominations or inventory levels might provide information about an individual customer's activities. Specifically CSL suggests that any related obligation might be waived either if 85% of the operational space capacity in a facility is held by two or less customers. This aspect is amplified in our later comments on Confidentiality Requirements.

GGPSSO Proposals

- **General Comments**

By way of background, CSL is firmly in support of steps to ensure that effective TPA to storage services is available throughout Europe and also firmly supports the agreement of Guidelines for Good Practice (GGP) for Storage Operators (SSOs) which could cover the provision of TPA and also the interactions with the adjacent transporter (TSO).

Overall, we support the intention of producing a "minimum set of requirements" for SSOs offering TPA. However we remain of the view that the ERGEG paper is in some cases over-prescriptive and includes in our view material that goes beyond the realistic "minimum" - specific examples are quoted later in this response.

CSL also offers in this response a number of recommendations intended to clarify some aspects which could be interpreted in more than one way.

On the whole, CSL would not be seriously affected by the ERGEG proposals: they largely reflect what CSL and its customers do except in respect of publication of capacity and operational information. However CSL is keen to ensure that any accepted guidelines reflect what is reasonable, fair and appropriate as "Europe-wide" norms and that the proposals for implementation do not create inappropriate pressures given the likely short-term benefits achievable.

- Timescales

At present the paper includes comments on implementation by 1 April 2005 in paragraphs 3.8 (provision of TPA services) and 6.10 (publication of information). Although CSL supports the effective availability of TPA as soon as is practicable, we think the suggested timescale is over-ambitious in a Europe-wide context and (as noted earlier) we consider that where inadequate related infrastructure and systems are not in place early implementation may provide insufficient benefits to justify the costs.

In general we believe that the issues of timescales justify a more flexible treatment, and we recommend the following approach would be more appropriate, and best inserted at the end of the introductory section - "As soon as possible, SSOs and National Authorities should agree timescales for implementing the agreed guidelines. The timescales should reflect the needs of the potential storage users in relevant markets and the pace of developments in the individual markets while avoiding undue discrimination between SSOs and avoiding conflict with ongoing contractual commitments unless these are to be terminated."

CSL further considers the national regulators should be able to allow exemptions from any proposed timescales where they consider these to be in a national interest, particularly where markets may not be mature or competitive in non-storage respects.

- Section 1 - Roles and responsibilities of Storage System Operators

In respect of paragraph 1.2b, we recommend deletion of the words "and transparent". TPA should be non-discriminatory, but "transparency" of the TPA services available at "nTPA" sites seems inappropriate as this could discriminate against the interests of the SSO and certain customers for no good reason.

In addition we support the view expressed by EFET that the SSO should provide a financially firm service and avoid exposing users to undue risks beyond the user's control – we would not oppose such a comment in Section 1.

In the light of comments at the Brussels meeting in June, it may be useful if the paper stresses that a SSO's responsibility for delivering (or accepting gas) is limited to the connection point with the adjacent TSO's system. SSOs cannot provide support or flexibility elsewhere: users will need (or have to procure) transportation capacity rights to move gas between transportation zones or to other exit points. This is not an issue that SSOs can address or an issue for a storage GGP - rather it is a transportation GGP matter.

- Section 2 - Role of Storage Users

In 2.1a, we recommend that a more accurate wording would be that Storage users shall be responsible "…. for providing gas for injection into and accepting gas on withdrawal from storage facilities ….".

We recommend the inclusion of a comment that "A Network Code may require storage users to be prepared to provide gas and/or storage capacity for security of supply or network balancing purposes."

- Section 3 - Necessary TPA services

CSL does not oppose the proposal (paragraph 3.4) that subject to the availability of an appropriate balancing regime the SSO should offer at least a guaranteed firm service with nominations kept whole. However, this means that in the event of operational failures storage operators may have to buy or sell gas, and this needs to be considered alongside any obligation to publish physical flow data in "real time" as could be construed from paragraphs 6.5 and 6.6. The underlying issue is as summarised earlier and is further discussed below.

CSL notes that the phrase "subject to Force Majeure" has been omitted from paragraph 3.4 since the 6 September draft. We do not oppose the deletion of the phrase, as it could have been taken to imply that where such agreements exist the only exemption from the "nominations whole" principle would be in the case of Force Majeure. Reflecting custom and practice, there should be a number of circumstances where the customers' nominations would not be held whole, although the circumstances should occur rarely: the arrangements would naturally form part of non-discriminatory contract terms, and where such terms are regulated would obviously be agreed with the regulatory authority.

Conversely, CSL is surprised by the deletion of "including use-it-or-lose-it arrangements" from paragraph 3.3c - despite the reference to discouraging hoarding in 4.3, we consider this to be an important "anti-hoarding" principle, which could be a fundamental aspect of any GGP.

More broadly, we consider that the wording in Paragraph 3.3 may understate the importance of "Standard Bundled Units" as the basic "building block" for capacity holdings. As was discussed at the recent GTE-Eurogas workshop, it is convenient both for users and for SSOs if SBUs based of the operating parameters of the storage facility form the nucleus of normal capacity holdings; but it is also very desirable that customers

can restructure such holdings as easily as possible, and this is likely to be best addressed by the SSO offering user-friendly means of trading unbundled capacity.

It may be that demand for storage services at some locations is such that some capacity should be "partitioned" for initial sale as unbundled capacity, but a similar effect can be achieved if the SSO is prepared to be a counter-party in sales of unbundled capacity, for example by quoting prices at which they are prepared to buy back some unbundled capacity which would be offered for re-sale.

We also consider that the phrase "down to a minimum period of one day" is unhelpful – a more useful approach would be to emphasise that services should be available both day-ahead and within-day when possible.

CSL therefore suggests the following alternative text for paragraph 3.3 -

"3.3 ... a menu of services, including the following:

a) capacity will be substantially sold as bundled services (SBUs) comprising injectability, space and deliverability, with ratios determined by the facility's technical parameters,

b) the above will be complemented by unbundled services where commercially & economically viable and where requested by storage users,

c) an appropriate range of both long-term (> 1 year) and short term firm services (< 1 year) will be offered,

d) short term interruptible storage contracts and services will be offered through the release of unutilised injectability, space and deliverability (Use-It-Or-Lose-It).

The primary aim is to ensure that SSOs provide flexible primary services, where commercially & economically viable, such that storage users are able to shape the storage service required through the SSO releasing bundled, unbundled and interruptible services as appropriate. In addition, the users will be able to restructure capacity holdings by means of secondary trading of unbundled capacity, and should be able to acquire capacity day-ahead and within-day wherever this is practicable."

We observed earlier that the comment (para 3.8) that all storage operators should provide all the TPA facilities by April 2005 seems very ambitious: we would expect national regulators to want to set suitable and realistic deadlines for all facilities in a country and to do so consistently and fairly, but not necessarily using the same date for all sizes or types of facilities.

Section 5 – Confidentiality Requirements

CSL recommends that this section is expanded to address circumstances where publication of aggregate nominations or inventory levels might provide information about an individual customer's activities. Specifically CSL suggests that any obligation to publish information on flows or inventories might be waived if 85% of the operational space capacity in a facility is held by two or less customers. Our later comment on paragraph 6.5 addresses this too.

Section 6 - Transparency requirements

CSL believes that any information publication obligations should be non-discriminatory, and that requirements should apply even-handedly to similar or competing storage facilities, particularly of course where publication may be seen as commercially sensitive by the SSO or by the SSO's customers.

In general CSL would expect regulators not to require information to be published in respect of storage facilities when reasonably comparable information is not being required in respect of competing sources of flexibility, which may include offshore or onshore production facilities. But we favour regulators having the ability to seek additional information "as needed", and that such information may be published where there is a need and its publication is not likely to be commercially harmful to the SSO or the SSO's customers.

A further general point is that we recommend the paper should distinguish between information to be released into the public domain and information which would be released to "customers" (which would include companies who have signed all the SSO's documentation but who might have no capacity holdings at certain periods). The prompt publication in the public domain of failure/outage information may harm the SSO's customers if they have to re-balance for the duration of an outage.

However, care is needed to identify realistic and fair "minimum" publication requirements. The information obligations adopted should reflect market needs and avoid unnecessary costs.

Generally we do not consider that that the costs of providing “real-time” information to customers or the public are worthwhile. CSL provides its customers with on-line hourly information on their injection and withdrawal allocations and predictions, and this has proved sufficient for users’ needs. We therefore believe that the proposal that “information should be provided on a real-time basis if required by system users” is fundamentally unsound.

We accept that prompt knowledge of a facility failure may be of market value. However, as discussed earlier, unless similar “real time” information is to be made available for all sources of gas to a relevant market any SSO providing a “nominations whole” service would be seriously disadvantaged by the publication (as may storage customers), and we do not consider that such SSOs can reasonably be required to provide such information.

In addition, the phrase “if required by storage users” (in respect of real-time information, paragraph 6.1) is impracticable. It introduces issues of how best to consult with users on this area and how to deal with conflicting opinions. If necessary, the relevant regulator should determine whether publication is appropriate.

Publication of information relating to planned maintenance (to paragraph 6.7) is reasonable, but the issue of publishing information on unplanned maintenance, or flow rates which would reveal this, must be affected by what rights the storage operator has to fail to honour the customers' nominations - if customers' nominations are held whole for some or all of an unplanned/unforeseen outage (or capacity reduction) the publication of such information will generally expose the storage operator to additional cost as any affected market reacts to the information on flow restriction, and will do so in a discriminatory way unless comparable failure information is provided for all other sources of gas and flexibility. The SSO would become a “distressed” buyer or seller of gas, and as no other comparable organisation would be in this position the proposal must be unduly discriminatory.

Obviously several of the areas envisaged by Paragraphs 6.5 can be argued to be commercially sensitive for storage operators with active competitors in a relevant market unless those competitors can be obliged to publish similar information.

Specifically we believe that the publication of “real-time” “storage level”, “working gas”, “technical capacity” and aggregated inflows and outflows” data, as envisaged in paragraphs 6.4/5, exposes the storage operator to unreasonable risk when linked to holding nominations whole.

Hence CSL considers that the GGPSSO proposals should discriminate carefully between information that would be provided promptly or “real-time” and information that would be provided retrospectively.

However, CSL generally favours publication of information by “on-line” means. CSL supports publication on-line of standard contractual terms and with providing customers with on-line access to information relating to their own activities including nominations, capacity holdings, secondary market activity and likely charges. To the extent that methodologies and retrospective data are to be published they too can be made available on-line.

CSL does not consider that “[the] method of determining available storage capacity and the operational parameters including transparency on the rules of ownership and use of working gas” (6.4c) are really “commercial terms” that should be published, and believes that whether or not such information should be published should be a matter for the SSO’s discretion.

In passing, the text relating to “flexibility tolerances” (6.4b) is unclear. CSL recommends that the text can be simplified, without material impact, to “services offered, the storage code (if applicable) and/or the main standard conditions for each service outlining the rights and responsibilities for all users (including rights for counter-flow injection and withdrawal nominations), rules relating to transfer of capacity and gas in store, and any PSO rules relating to enforced transfer of storage capacity rights linked to movements of end-users between suppliers.” (This would thus address 6.5e too).

In respect of paragraph 6.5, CSL recommends that the information covered in 6.5c, d and e should for convenience be listed in paragraph 6.4.

As regards operational data, CSL would in principle support the publication of –

- aggregated customer nominations (“daily aggregated inflow and outflows”, 6.5b), occasionally during a day, but promptly
- aggregate inventory levels (“storage level, including working gas”, 6.5a) weekly or monthly, in arrears

CSL supports publishing maximum practicable annual capacity levels on-line at all times. However publishing the proportion of nominal capacity that has been sold could sometimes jeopardise seriously the SSO’s

commercial interests, and the decision whether or when to publish such information should therefore be for the SSO's discretion.

CSL therefore recommends the following text in lieu of the existing paragraphs 6.4-6 -

"6.4 The following information should be provided on-line:

a in rTPA, the tariffs for each service offered shall be published ex ante with the derivation criteria attached (i.e. the underlying technical and economic reasons for establishing them). In nTPA, the main commercial conditions including the prices for core standard services must be published and updated whenever the SSO changes them; prices and underlying criteria should be made available to the national regulatory authorities at least in case of disputes;

b services offered (including maximum nominal capacities available), the storage code (if applicable) and/or the main standard conditions for each service outlining the rights and responsibilities for all users (including rights for counter-flow injection and withdrawal nominations), rules relating to transfer of capacity and gas in store, and any PSO rules relating to enforced transfer of storage capacity rights linked to movements of end-users between suppliers

c storage capacity allocation, congestion management and anti-hoarding and re-utilization provisions, including auction terms where applicable

d rules and charges applicable to storage penalties payable by storage users and compensation payments payable by the SSO to storage users

e user-friendly instruments for calculating charges for a specific service (e.g. tariff calculator) and for verifying online the level of available capacity, including net and available firm and interruptible capacities

f information on historical utilisation

g maps indicating the location of their storage facilities and the connecting points of the storage facilities to the relevant network

6.5 The following operational information shall be published online (in energy units, according to interoperability criteria) to system users:

a aggregated customer nominations, on a number of occasions during a day as agreed with the Regulatory Authority

b aggregate inventory levels weekly or monthly

However the above obligation should be waived either if a facility has three or less active customers or if 85% of the operational space capacity in a facility is held by two or less customers."

Also, CSL recommends that the last sentence on daily maintenance logs (in 6.6) is deleted, as the proposal would create effort which would rarely be justified. Instead, such information could be made available to the national regulatory authorities "on request", but this does not warrant inclusion in GGPSSO.

Concerning paragraph 6.9, CSL supports views that SSOs should be entitled, but not required, to make charges in respect of support and systems to facilitate secondary-market trading of storage capacity and gas in store. This relates to paragraph 9.2 too.

In any event, CSL believes that a number of SSOs would have difficulty in implementing suitable information systems by 1 April 2005; however we accept that the scope for reference "to the relevant national authority" for possible temporary exemption should give reasonable comfort in such cases.

Section 7 - Tariff structure and derivation

As explained earlier, CSL recommends that a very important issue is that the regulator should take into account the SSO's potential sales and income levels in assessing the likely outcome of any pricing proposals. Ideally, where rTPA applies the SSO should receive an appropriate rate of return on investment taking into account the predicted storage utilisation, and care needs to be taken to try to avoid the risk that prices are set which would cover the SSO's costs if all (or nearly all) the storage capacity is sold but which might result in some capacity being unsold. Increasing any storage tariffs would clearly not be likely to solve the problem.

Regulators should generally be alert to risks that an SSO might fail to get enough revenue to justify retention of the storage facility: especially where this is a result of distortions during a transition to a competitive market, the regulator might conclude that closure of the storage facility is not in the long-term interests of the relevant

market. In such cases the regulator would need to consider how the SSO should be remunerated for keeping the storage facility operational, and how the resultant cost should be funded.

We thus consider that a major issue for regulators and for European Storage Operators should be how pricing issues are best addressed where “market forces” might result in insufficient costs to justify ongoing retention of storage facilities, despite the widely-expressed concerns over future security of supplies and the possible need of marginal storage facilities to assist with future PSOs; and we think the ERGEG paper should recognise this though it may not strictly be a “GGP” matter.

Section 8 - Storage penalties and settlement processes

It is important to distinguish between the charges for use of interruptible capacity (including in the case of UIOLI) and over-run charges where a customer exceeds the flows the SSO intends and yet has gas allocated to them. CSL interprets the “storage penalties” text in paragraphs 8.2b and 8.3 as intended to apply in the latter case.

In CSL’s view the only circumstances where re-distribution of "storage penalties" (as envisaged in paragraph 8.3d) could be appropriate would under rTPA or if storage users had initially been obligated to buy capacity irrespective of their economics and the benefits foreseen. Otherwise, there is no justification for users getting what would effectively be rebates on negotiated prices.

Yours sincerely

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