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**“CEER Vision Paper for a conceptual model for the European gas market:
Call for Evidence”**

- EDP Gás and Naturgás Energia Comercializadora Comments -

1. What are in your view the main goals to be aimed at by the gas target model beneath the high-level policy goals set out by the 3rd Package?

EDP Gás and Naturgás Energia Comercializadora, being part of EDP Group, the electricity incumbent in Portugal and with a relevant presence in the electricity and gas markets in the Iberian Peninsula, envisages a gas target model that may deliver:

- Secure, competitive and flexible gas supplies
- Liquid and transparent wholesale markets
- Guidance and coordination to further regional level integration

through:

- Cross border market integration
- Efficient capacity allocation
- Efficient use of pipeline capacity
- Security of supply
- Effective competition and efficient functioning of the internal gas market
- Adequate flexibility to accommodate CCGTs needs

In order to get these goals, we think that regulation has to encourage:

- Non-discrimination
- Harmonization
- Transmission System Operators real coordination in technical, operational, investment planning and administrative areas (e.g., capacity requests to be dealt by one TSO in coordination with the others that may be involved)
- Transparency on Third Party Access
- Appropriate and feasible level of cross-border gas interconnection capacity
- Information transparency

2. What are in your view the major developments and anticipated changes in the European gas market (on national and international level) and where would a target model bring added value? Including:

a. the role of long term capacity contracts in the future European gas markets;

In our point of view, while in the past most of the capacity contracts were long term contracts, related to gas long term contracts or investment in facilities, this contractual structure is changing.

In this way, we believe that in a context defined by:

- Liquid secondary market for capacity
- Efficient capacity allocation or congestion management
- UIOLI, oversubscription, etc., mechanisms

the weight of long term contract is going to be reduced. In this process it will be very important how those mechanisms are defined because they should be coherent with shippers needs and ensure flexibilities.

On the other hand, the reduction of long term contracts weight is going to be limited by the need to ensure investments with long term compromises.

Related to this issue, EDP Gás/Naturgás have already commented on a previous ERGEG consultation that:

“We realize that the existing long term contracts may decrease the efficiency of the guidelines proposed, nonetheless stakeholders need consistent rules in order to optimize its business decisions.

Moreover, in our opinion, the effective control on the use of booked capacity is more important than modifying existing contracts and its positive impact is higher in order to maximize cross border capacity utilization. So in this way, we also believe that there are other mechanisms (ej. UIOLI, liquid secondary markets, anti-hoarding measures) that can encourage the effective use of the capacity by all agents, without implying the adaptation of existing contracts.

EDP Gas could face significant challenges in amending existing contract arrangements in line with these Framework Guidelines in 6 months. As mentioned by Eurelectric, It will only be possible to change the relevant clauses of existing contracts on a case-by-case basis if they are in contradiction with the new legally binding rules”.

To sum up, we think that this will be a natural process that should not be regulatory imposed and in neither case without a real transition period, where shippers change their contract portfolio to adapt to this new reality.

b. the role of hubs / gas exchanges.

We believe that gas hubs can have a very important role in the attainment of a competitive European single gas market.

Regarding this goal, in our opinion, regulation could establish those basic issues that are necessary to create a hub or wholesale gas market but on the other hand, we think that gas hubs should be allowed to develop naturally, based on a few regulatory basic principles as balancing zones and on market demand, and participation by shippers should not be mandatory. In fact, gas hubs should be considered as another source of flexibility offered to the market.

Finally, in order to achieve a real hub it is necessary that enough interconnection capacity is ensured and be available for shippers, to consider the specific characteristics of each system and that the price of the hub reflects all these issues. If the hub does not consider these characteristics, it would not work correctly and it could cause distortions in the market.

This issue is especially important in cases such as the one of the Iberian Countries, Spain and Portugal, because, even with a hub in place, without enough interconnection capacity it will remain an “energetic island”.

Furthermore, if adequate interconnection capacity is developed, along with the implementation of a hub, the Iberian Peninsula can increase significantly the security of supply of the European gas market, due to its relevant connections to the gas supply countries in the north of Africa.

3. What are in your view the key elements of a conceptual model for the European gas market to contribute to non-discrimination, effective competition, and the efficient functioning of the internal gas market?

Please include views on the key aspects of market design such as, capacity allocation and congestion management procedures, network tariff arrangements, wholesale market pricing, balancing arrangements and, gas quality specifications? Please consider the interaction of these arrangements.

In its previous responses to the public consultations organised by ERGEG, namely on the Pilot Framework Guideline on Capacity Allocation and the Pilot Framework Guideline on Gas Balancing, EDP Group has already taken some views on the target models proposed there. The following section builds on those responses and also gives some preliminary views on other issues such as tariff arrangements and transparency:

- Third Party Access (TPA): In order to get those goals, it is essential to get a transparent TPA system.

Nowadays around Europe, two TPA models are applied: regulated and negotiated. In the second type of access, in our opinion the grade of transparency and regulatory control should be higher.

- Harmonization: It is necessary to get a minimum harmonization level in key matters (CAM, CMP...). Moreover, we think that it should define a specific timetable for the harmonization stages in order to avoid “different speeds” between system which generate inconsistencies and inefficiencies that distort the way to get goals set out by the 3rd package.

Finally, as we say, we support that it is essential to get a minimum level of harmonization but we believe that it should not suppose a reduction of shippers’ flexibilities (e.g. types of products), too.

- Information transparency: EDP Group stresses the importance of information transparency in shaping and boosting the development of functioning, efficient and liquid energy markets. Fundamental data about supply and demand drives price formation and it is crucial for market efficiency and liquidity that such information is made consistently available to all market participants so as to create a level playing field.
- Capacity Allocation: A clear, well-known, easy Capacity Allocation Mechanism (CAM) is basic in order to avoid any discrimination.

Regarding this mechanism, we believe that, when capacity is scarce, auctions are the best way to ensure that firm capacity is allocated to those parties that value it most.

However, we suggest that ERGEG balances the administrative costs and complexity subject to auctions in order to combine auctions with other capacity allocation mechanisms (such as first come, first served) in the short-run, when there aren't congestion problems. In fact, in our opinion, FCFS method could be a good allocation procedure in some specific situations, for example in interconnection points with excess capacity.

On the other hand, it should also be said that the application of the same allocation procedure across the European interconnection points will ensure that shippers become familiar with the operational process and will avoid distortions between different systems.

Finally, we support that it is essential to get a minimum level of harmonization but we believe that it should not suppose a reduction of shippers' flexibilities (e.g. types of products) , too.

- Congestion Management: A transparent, well-known, easy, market based Congestion Management Procedure (CMP) is necessary in order to avoid any discrimination and to get an effective competition and efficient functioning of the internal gas market.

On the one hand, in our opinion, it is essential to guarantee a dynamic capacity calculation to maximise the offer of capacity to the market, just as using tools as:

- Oversubscription and capacity buyback to make available an extra amount of firm capacity to the market.
- Surrendering of capacity back to the TSO
- Interruptible capacity offer

On the other hand, congestion management procedures would not suppose a reduction of flexibilities for shippers. In this way, for example, we believe that existing re-nomination rights should not be limited.

Furthermore, we would like to stress that CAM and CMP rules to be defined in the European gas target model should evolve in order to accommodate a more flexible use of the gas system. Otherwise, strict rules will have a direct impact on energy costs for final consumers of gas and electricity. A higher

degree of flexibility should be achieved in markets where a large percentage of the electricity production is guaranteed with gas fired plants, such as in the case of both Portugal and Spain.

- Network tariff: we believe that network tariffs have to be cost reflective, based in a transparent and well-known methodology.

Moreover, it is also important that regulators cooperate when assessing methodologies and network access tariffs to be implemented, to ensure that the approach taken in one Member State does not negatively affect activities in neighbouring gas markets

Regarding the tariff methodology, it should consider the following requirement:

- Pricing of very short-term capacity products to facilitate efficient gas trade and competition.
 - Avoiding perverse effects of potential competition between short and long term bookings.
 - Avoid cross-subsidies between cross-border and domestic network usage.
 - Providing incentives for efficient investments.
- Interconnection Capacity: In order to get a European gas single market, it necessary to reach an appropriate and feasible level of cross-border gas interconnections capacity. Mainly working in two ways:
 - Maximising existing interconnection capacity.
 - Taking coordinated investment decision in order to build new capacity.

Finally, we have to say that this issue is especially important in cases such as the one in Spain/Portugal because without enough capacity would be an “energetic island” and would be very difficult to get a real European single market.

- Wholesale market pricing

In a European context, cross border market integration, increase of interconnection capacity, harmonization of operational rules and a competitive market are issues which are going to “produce” or give us a real European wholesale market price.

Nowadays, in a fragmented European gas market, each regional or national market has its own wholesale market price. Only the NBP index is being considered by the market as a global reference for gas price.

We believe that gas hubs have a very important role to get a competitive European single gas market and in the determination of a transparent wholesale market price. In this way, regarding hubs, in our opinion, regulation could establish necessary bases to create a hub or liquid wholesale gas market but on the other hand, we think that gas hubs should be allowed to develop naturally, based on initial balancing zones and market demand.

To sum up, in our opinion, a real wholesale market and a representative wholesale market price will be a natural consequence of the mentioned measures as cross border integration, efficient use of pipeline capacity or standard harmonization.

- Balancing Arrangements: As we said in the context of the public consultation about “Gas Balancing Rules on European Gas Transmission Networks”, we believe that balancing activities should be taken primarily by market users, with the TSO being responsible for the supervision of the system’s integrity and for making available to market players adequate levels of flexibility (especially when CCGTs and LNG terminals are in place) such as tolerance ranges provided by TSOs.

Moreover, in our opinion cross border market integration has to progress at the same time together with the harmonization of balancing rules because without these condition this development could be distorted.

- Gas quality specifications: In our point of view the goal should be to define standards that are as wide as possible within reasonable costs. So in this way, a range of gas quality to:
 - Enhance security of supply.
 - Minimise investment in appliances and equipment, maximise energy output.
 - Allow access of biogas to the natural gas transmission system.
 - Have flexibility to meet changing sources over time
- Transmission System Operators’ real coordination in technical, operational, investment planning and administrative areas (e.g., capacity requests, ...)
- Short Term Capacity Products: In order to increase markets liquidity and competitive offers to final customers, TSOs should develop short term capacity products based on capacity availability in periods of lower demand that could be used by shippers for spot business, refill gas storages, etc.

4. What level of detail, e.g. level of harmonisation, do you expect from the CEER vision paper on a conceptual model for the European gas market? For example:

In opinion of EDP Group level of detail should be high enough to avoid inconsistencies between the future network codes and to allow for regional market specificities.

a. Do we need a definition of an EU-wide gas day? If yes, what should this definition be?

A EU-wide gas day definition can be useful, especially for cross border operations. Nevertheless, the definition of a specific gas day for all European countries should be preceded by a careful analysis of each market specificities since in some countries, like Spain and Portugal, the gas day timetable is linked to the “electricity day”.

In this way, in our point of view, it is important to keep this link between “electricity day” and “natural gas day”, at least in those cases where CCGTs have a relevant participation in the electricity generation (e.g. Spain and Portugal).

b. How deep should the "reach" of the EU gas market model be, i.e. should it encompass DSOs? Is there a trade-off between vertical depth (i.e. including all levels of national gas markets) and horizontal depth (i.e. integrating balancing zones cross border)?

The role of DSOs is very important for the daily operations of any gas market. Activities like data collection and transmission, measurement, allocation of standard load profiles (on non-metered customers), capacity allocation and network development on DSO level. Thus, we consider that DSOs activities should also be analysed.

In our opinion, considering the importance of LNG terminals and entry or exit points to or from gas storage facilities, and their role in the introduction of liquidity and efficiency to the market, we believe that a complete model to be developed for the European gas market should also be applied to these infra-structures.

5. Which areas or aspects of the gas market should be affected by the target model and what are the constraints for such a model?

In opinion of EDP Group, the gas target model should affect those aspects specified in the 3rd Package where ACER and ENTSOG are required to develop Framework Guidelines and Network Codes. This principally applies to: capacity allocation and congestion management, balancing, harmonisation of tariff structures, transparency and interoperability.

6. Which areas or aspects of the gas market should be excluded from the target model description and left to national/regional decision making

In order to avoid discrimination, it is necessary to get a common grade of harmonization convergence in key elements, as those aspects specified in the 3rd Package where ACER and ENTSOG are required to develop Framework Guidelines and Network Codes. In this way, it is not compatible with national decision-making. As Gas Directive establish (art. 7) is basic a close cooperation between ACER, NRA, TSOs, DSOs and stakeholders.

7. What are the options for integrating the currently fragmented European markets?

We consider that balancing zones should be organised in a systemic point of view and not constrained by national borders. Thus, we also agree that TSO's should be encouraged to cooperate in order to develop cross-border balancing zones with common rules.

In this way, European gas market should change from a fragmented situation to a limited number of consolidated EU market areas (e.g. Iberian gas market). In our opinion, this should do:

- reflecting the efficient limits of balancing zones
- encompassing different networks within and across Member States
- entry/exit capacity pricing principles around a virtual hub
- freedom to ship gas within the market area unhindered by quality or capacity constraints
- ability to buy and sell gas within the market area at a virtual point

Are there any existing models you would like to recommend? In case your answer is yes, we would be interested to learn about the features of this model and if there are also any draw-backs in this model in your view.

a. Should we merge balancing zones to create cross border or regional balancing zones or market areas? How many balancing zones does Europe need and how big should they be?

Consolidation of market areas can only take place to the limit of efficient balancing zones. Regarding this issue, in our opinion the most important requirements would be:

- common balancing arrangements to be applied
- non discriminatory access to consolidated system linepack along with storage and flexible gas
- Common gas quality parameters within market areas with TSOs resolving any quality differences by blending/treatment
- Standard renomination lead times at interconnectors
- common methodology to be applied:
 - to calculate entry/exit capacity and commodity tariffs within consolidated zone
 - to apportion costs associated with quality conversion
- TSOs could be incentivised to facilitate consolidation and efficient balancing
- Information transparency

b. Is the coupling of market areas as it is being developed in European electricity markets appropriate for gas?

As mentioned by Eurelectric, in our opinion, market coupling of day-ahead electricity wholesale markets is seen in the power sector as the most efficient tool to optimise available capacity, thereby increasing the number of trades between the market coupled areas and achieving an optimal level of price convergence. It cannot be automatically assumed that the same benefits will arise in the gas markets where price convergence has progressed through other means and the lead times for trading gas are much longer.

We believe that a thorough assessment should be carried out to identify the pro's and con's of introducing market coupling in the gas markets and how and if it is the best way to forge larger and more liquid gas wholesale markets. In the meantime, work should continue on the development of Framework Guidelines and Network Codes in line with Madrid Forum discussions and as set out in the 3rd Package.