DRAFT GUIDELINES OF GOOD PRACTICE ON OPEN SEASON PROCEDURES (GGPOS)

Centrica response to the EGEG Public Consultation Paper

Centrica is a long-standing holder of gas transportation capacity in the IUK pipeline and across Belgium, a material part of which was originally obtained as a result of open season processes. We regularly participate in national transmission system entry capacity auctions in Great Britain and are also holders of Grain 2 LNG re-gasification capacity rights. Recently, we have participated in further open season processes with a view to securing additional long term gas transportation capacity in North West Europe.

We therefore have considerable experience of gas sector open season processes operating in a number of different contexts and jurisdictions. Centrica is keen to see fully appropriate, transparent and non-discriminatory open season processes play a key role in securing significant gas infrastructure investment to meet growing market demands and support closer EU market integration across national borders, including expanded gas trading at and between hubs.

We therefore welcome this ERGEG Public Consultation Paper ("PCP") and appreciate the opportunity to provide further input and comments based on our own experience of open season procedures in practice.

Our comments below are presented according to the structure of the PCP – i.e. first on the scope of application of the GGPOS and then on each major section of the GGPOS itself.

Application

Although para (1) of the PCP refers specifically to the 2005 Gas Transmission Regulation, we note and generally support the wider application of the GGPOS as set out in para (13) of the PCP.

We do, however, have two specific comments on the scope of application, as follows:

- We doubt whether classic open season procedures can be applied successfully to most gas distribution investments, though some aspects might be relevant for significant grid extensions (e.g. to previously non-connected communities and/or major new housing developments). In mature gas distribution systems such as those in N/NW Europe, most distribution investments will typically be subject to a more general network development obligation on the distribution network operator, against a regulated rate of return.
- The application of the Guidelines to infrastructure which is exempt from Regulated Third Party Access is not entirely clear from PCP para (14). This may be important as regards many new LNG terminals and some interconnector pipelines. Given the importance

of cross-border consistency in approach, together with the inter-related nature of regulated and exempt facilities – and noting that the GGPOS are not in any event proposed to be legally binding, as set out in PCP para (15) – we take the view that all new gas transmission, storage and LNG facilities should also be subject to (most of) the Guidelines. In the case of exempt facilities, however, the applicable Guidelines should exclude those paragraphs relating to regulatory intervention from which the potential investment has been exempted.

Guidelines on Open Season Procedures

Para (17): We understand and agree with the general two-step OS schema set out in this para. In some cases, however, it may be appropriate to include more than one "round" in the assessment of market demand. This is particularly so where the applicable tariff is materially dependent on the scale of the investment to be made. This is implicit in para (20), the 14th bullet point, which requires the sponsor to indicate the variation in tariff against the allocation of incremental capacities to network users. In circumstances where an initial indication of market demand allows the sponsor to narrow down the range of indicative tariffs, it would be reasonable to allow market participants the possibility of varying their demand indications in the light of that. What we wish to avoid is a situation – experienced in the past – in which the applicable tariffs are varied significantly at a point where market participants have no option but to maintain the level of their demand, or else drop out of the OS process altogether.

Secondly, the GGPOS should make clear that the proposed basis for Capacity Allocation must be specified at the outset of the Open Season process, to allow market participants to bid appropriately. In the past, we have experienced OS processes which have been initiated without adequate clarification of the basis on which capacity would eventually be delivered and allocated among market participants – and other cases in which the basis for capacity allocation has appeared to change during the course of the process.

First Step: proposal to shippers

Para (18): It would be normal for a sponsor to have made an initial evaluation of economic and technical constraints before consulting system users – though this initial evaluation can and often will be refined in parallel with the OS as it proceeds.

Para (19): We consider this a most important step and we would add that the regulatory authority should express any material concerns with the OS process at this early stage. In our experience, it is all too common for the position of national regulators on fundamental points to remain unclear towards the very end of the OS process – even after binding (but conditional) contracts have been entered into. This has the effect of increasing risk unduly and militates against the high level of user commitments required to underpin much-needed investment decisions.

A second comment on this para is that it should recognise the need for national colleagues to consult where necessary with their peers in neighbouring jurisdictions – especially in the case of interconnectors or parallel OS processes for pipeline investment on either side of a national border. There may also be a helpful co-ordinating role for ERGEG in this respect.

Third, we consider that the regulators could play a useful and more pro-active role in subsequent phases of the OS process. For example, the opportunity for market participants to comment on and influence the drafting of relevant legal agreements has often been unsatisfactory in the past. In particular, we think it would be useful to convene an "industry forum" in which participants in the OS process could raise and debate comments on the legal documentation in the presence of the national energy regulator, as well as the sponsor. This would increase openness and transparency, allow OS processes to avoid a "take it or leave it" approach to contracts and would have the additional benefit of enabling the regulator to take a more informed view of any regulatory issues around the OS process.

Para (20): This is, in our view, a good and thorough list of key requirements. The effectiveness of OS processes would, in our view, be materially enhanced if these requirements were adhered to. We would nevertheless like to make a small number of comments, as follows:

- In bullet point 10, relating to capacities upstream and downstream of the project, it is desirable to address both existing and potentially available capacities, so as to cover the case of parallel OS processes on either side of a national border (of which several recent examples can be cited). In our view, the GGPOS should be seen as an excellent opportunity to improve the level of cross-border co-ordination – especially as this has evidently been less than satisfactory in the past.
- Given the general desirability of harmonising, as far as economically and technically feasible, the (H gas) quality specifications applicable to cross-border gas transmission, we suggest that bullet point 11 (quality specifications) should encompass, where relevant, the relationship to gas quality specifications applicable immediately upstream and downstream of the project. We are aware at least one recent case in which parallel OS processes running either side of a national border involved inconsistent gas quality specifications at the same delivery/redelivery point. Such situations should clearly be brought to the attention of both market participants and national regulators at the earliest possible opportunity in the process.
- We would add two further bullet points to the list:
  - First, the sponsor should indicate to market participants the consequences for the sponsor and market participants if (for reasons of genuine *force majeure* or otherwise) the capacity finally subject to binding user commitments is not in fact made available, or is not made available on time. This issue is later

addressed in PCP para (29), but it is a material element of the contract package which should be made transparent to potential system users at an early stage.
    - Second, the sponsor should indicate the process and timescale according to which final regulatory approvals are expected to be secured.
- It is also important for sponsors to provide market participants initial drafts of the relevant legal documentation (e.g. agreements for transportation or LNG regasification capacity) at an early stage in the OS process.

Para (21): In terms of the feedback to be provided by interested parties, there is a specific issue which arises in relation to parallel OS processes taking place in respect of incremental transportation capacity on either side of a national border. The interest of some transit shippers in one OS process may well be contingent on the satisfactory progress of the parallel process towards a commensurate investment in new capacity. In such cases, we consider that there should be scope for market participants to indicate the contingent nature of their interest, with a view to triggering a greater and more open level of inter-TSO co-ordination. This also raises issues of cross-border regulatory co-ordination, in relation to which ERGEG has recently launched a separate public consultation.

More generally, we do not agree that market participants should have to identify their source of gas/supplier (as opposed to the relevant upstream or downstream gas transportation system they will rely on). There are three main reasons for this:

- Most importantly, it is not necessary for the system operator (SO) to know the supplier's identity.
- The identity of existing suppliers may be confidential and the communication of this gives rise to unnecessary "information ring fencing" issues in the case of any SOs which are not yet fully unbundled.
- In fact there may not be any existing supplier and this in itself may be confidential information.

As regards the nominated upstream/downstream transmission system, we recognise that there may be genuine network engineering reasons for the SO to require this information in some cases. However, we consider that market participants should not be restricted in this sense any earlier, or to any greater extent, than is strictly necessary.

Para (23): In our view, this para should also address the circumstances envisaged in the last sentence of PCP para (9) – i.e. where the SO is unable or unwilling to invest but outside investors are prepared (and should be permitted) to do so. We agree that this is a desirable fallback position, but note that it is not currently permitted or facilitated in a number of Member States. Para 23 should also require the SO to facilitate a "second round" of market demand assessment as mentioned in our comments on PCP para

(17), i.e. where there is a material change to initially indicated tariffs or a significant clarification of the likely tariff range.

Second Step: Capacity Allocation following Open Season

The current draft GGPOS appears to proceed directly to capacity allocation as the second step in the process. In some cases, this will be appropriate – e.g. where the capacity to be made available is restricted for technical, regulatory/planning or other reasons and there is excess market demand at the indicated tariff (or first round auction price) level. In other cases, however, it may not be. Unless there are *bona fide* reasons otherwise, the SO should generally be obliged to invest (at least) on a scale necessary to meet firm user commitments at the indicated viable level of tariffs – taking into account any other legal obligations bearing on capacity development by the SO. Only if this is not possible should there be recourse to the allocation of constrained incremental capacity, whether by auction or pro rata. This conclusion is implied by PCP para (26), but even so the "build obligation" element of the OS process is not fully recognised in the GGPOS as it stands.

Para (25): The non-binding letter of intent stage will often be appropriate, but not universally so. For example, it is likely to be unnecessary in the case of regular capacity auctions (such as those for transmission entry capacity in Great Britain) against a well-understood set of auction rules and network access conditions.

Para (29): This para addressed the important issue of tariffs, which we addressed in our comments on para (17). In terms of para (29), the onus should be on the sponsor and the relevant national regulator to ensure that the finally approved tariff (or at least the approved and tariff methodology) is clearly and transparently set out prior to the conclusion of binding agreements with market participants.

Results of the open season and transparency

Para (30): We do not agree that the names of prospective shippers, and (in particular) the percentage of total capacity gained by each of them, should necessarily be made public without their consent. In the case of facilities subject to regulated TPA, we can understand that the national regulator may need access to this information, but the capacity secured by an individual network user would normally be regarded as commercially confidential information.

Para (31): In the case of bilateral contracts (as opposed to a network code or other multi-party agreement), the regulator has a key role to play in ensuring that terms are fully non-discriminatory – see PCP para (19) - and providing market participants with appropriate assurance to that effect. Typically, confidentiality agreements entered into with the sponsor at an early stage of the OS process prevent market participants from verifying this for themselves.

Co-ordination with adjacent system operators

Para (34): this is in our view a critically important provision, since is has been an area of serious weakness with OS processes in the past. Unfortunately, the wording of the para does not make it clear whose responsibility it is to ensure that these conditions are fulfilled. We assume that the responsibility should lie with the adjacent SOs and (in default) with the relevant national regulators. It may also be appropriate to consider whether this would require a Regional Co-ordination responsibility to be placed upon National Regulators, working through ERGEG.

Please see also our response to PCP para (21). If there is scope for interested parties to indicate any inter-dependencies between parallel OS processes in their initial response to the sponsor, then this would provide one useful signal of the need for co-ordination between adjacent SOs – and indeed between National Regulators.