

# **CEER Vision Paper for a conceptual model for the European gas market**

## **Call for Evidence**

### **Comments by WINGAS GmbH & Co. KG on some selected issues**

#### **Question for stakeholders**

##### **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 3<sup>rd</sup> Package?**

The most important goal is to reach as fast as possible a level playing field in all European gas markets and for suppliers from all countries.

An effective target model in our view therefore would start by taking into consideration today's realities. It then would describe necessary actions to accomplish fair competition. In detail a target model should encompass a precise roadmap what the least liberalized country has to do in order to reach the level of the upper (as measured by the status of liberalization) 20% of countries.

In order to keep the complexity of the many parallel initiatives (3<sup>rd</sup> package, framework guideline, network code, regional initiatives etc.) manageable, the gas target model should describe its position and goals in contrast to them. Before going beyond the ideas of these initiatives a common understanding should prevail within CEER.

The proposed actions of the target model should focus especially on issues of access to the grid, capacity allocation and balancing rules. Nonetheless, regulators should take a holistic view on gas markets. They therefore have to take into account security of supply considerations (which are more pertinent compared to electricity since gas is mainly produced outside the EU). As an overarching consideration, a gas target model should promote (or at least not avert) a sound investment climate. This adverts in particular to investments in pipeline infrastructure as insufficient border connections pose the main obstacle towards international trade.

##### **2. What are in your views 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:**

We wish to underline that long term contracts – concerning both supply and capacity – are important both for market liquidity and investment decisions. A matter of special importance is the protection of existing capacity contracts. First of all, long-term contracts guarantee the availability of gas from a diverse field of suppliers. They are hence the most important prerequisite for new suppliers to actually enter the gas market. In general, we expect (and speak up for) an effective harmonization of access regimes (implementation of entry/exit systems) that facilitate cross border market integration, capacity allocation via auctions etc. We subscribe to ERGEG's vision of a target model promoting a "set of entry/exit market zones with their own virtual hubs connected through a limited number of bundled capacity products identical all over the EU and allocated via auctions."

In the following, we comment in greater detail some selected issues that, from our point of view, deserve special consideration:

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

A matter of special importance is the protection of existing long-term capacity contracts. Those contracts are the driving force for TSOs to build capacities since they give the long time security that capacities are indeed needed and paid for. Moreover, long term contracts allow the hedging of market risk in trading and are thus the base of building up long-term portfolio strategies in Europe.

Of particular importance is that long term capacity bookings are indispensable both for the contracting / operating of long term import agreements which ensure security of European supply and the assurance of export capacity, which is equally important since shippers have to be able to deliver the contracted volumes of gas to their customers.

**b. the role of hubs / gas exchanges.**

We favor a market-driven evolution towards a Hub-to-Hub model, based on initial balancing zones and market demand. We believe that such a competition between gas hubs is the most effective way to develop European gas markets. We expect the deployment of a “Cross Border Trade model” (with separate places of price formation, separate balancing accounts, strengthened CA/CM arrangements). After all, it is important that such a model guarantees liquidity (ability to buy and sell at market prices, from exchanges and long term contracts) and enables gas to effectively cross borders. In contrast, merging balancing zones bears the disadvantage of destroying valuable transport capacities. In addition, it must be possible to reserve long term capacity (via coordinated open season and / or other investment processes).

**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 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.**

We would like to focus our remarks on the question of capacity allocation:

In our view, it is important to bring to fruition the contents of the 19<sup>th</sup> recital of the preamble to Regulation 715/2009, which points out that it is “vital that gas can be traded independently of its location in the system”, and that the only way to do this “is to give network users the freedom to book entry and exit capacity independently, thereby creating gas transport through zones instead of along contractual paths”. The same recital stresses that tariffs should not be dependent on transport routes.

Of special importance is the abolition of what is known as “transit systems” – which hinder competition e.g. in Belgium or Austria. That abolition is of special urgency in order to speed up gas-to-gas competition in Europe. The definition of “transmission” enshrined, e.g., by Article 2 | 1 of Regulation 715/2009, does not allow any differentiation between transit and (other) transport.

WINGAS explicitly supports measures aiming at the stepwise harmonization of the rules on capacity allocation across Europe. Indeed, we share the view that available capacities have to be increased and that fair, transparent and non-discriminatory access conditions are of utmost importance for the further development of gas-to-gas-competition. However, the aim to enhance competition has to be in balance with the equally important aim to guarantee security of supply.

WINGAS judges the further development of a secondary capacity market and of secondary capacity products as an important step towards making unused capacity available to the market. While to us hoarding of capacities is totally unacceptable, we are convinced that “Use-it-or-sell-it” incentives and requirements should take priority over measures of constraint (like UIOLI). There are however two crucial points concerning secondary capacity pricing. First, the secondary market’s potential to free capacities will only materialize if prices of secondary capacity can start below the price of primary capacity. Second, in order to discourage speculation, there should be a price cap for secondary capacity. Nevertheless the market should be designed so that supply shortfalls are clearly signaled.

We are in favor of a European harmonization of capacity products since this is an important precondition for competition. Of specific importance are identical cross-border rules.

We share the view that cross border products will facilitate the exchange of gas between virtual hubs of adjacent markets. However, this does not mean that the possibility to trade gas at the border should be prohibited. Particularly, the commercial value of existing contracts that specify gas delivery at the border has to be protected.

We welcome the establishment of bundled products as a means to increase liquidity on gas markets since such products allow TSOs to optimize their operation modes. Again, the protection of existing cross-border supply contracts with delivery at a flange is important for sustaining the commercial value of these contracts (especially with respect to import contracts). It should be accentuated that there are certain prerequisites for bundled products, i.e. the implementation of entry-exit and trading hubs with standardized operating rules & products in all markets, the joint maximization of offered capacity at all interconnection points, as well as the harmonization of booking and allocation procedures.

In general, we support the view that auctions should be the standard mechanism to allocate firm capacity. However, we would like to direct the attention to some inherent dangers of auction processes, which consist mainly in strongly volatile or increasing prices at some points. A clear auction design, with fixed auction dates and deadlines that are in line with gate closure times of the respective gas exchanges, is of utmost importance. Available capacities should be published in advance. In order to offer the long time perspective needed for many projects in the gas industry, it should be possible to use long term contracts in form of open seasons and other capacity contracts.

## Gas quality

We support the view that standards should be as wide as possible (as long as the costs are acceptable). Such a wide range of gas quality offers the advantage of minimizing investment in appliances and equipment while maximizing energy output. In addition, a reasonable range of gas quality provides flexibility to meet changing sources over time and thus enhances security of supply.

### Balancing:

TSOs should offer a daily balancing system. But we believe that there should be incentives to reduce the imbalances of the system and to sustain its stability. For example, if a shipper can contribute to a diminution of such imbalances, he should have the option – boosted by suitable incentives – to structure his gas supplies throughout the day since this helps the system to prevent imbalances.

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

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

**b. How deep should the “reach” of the EU gas market model be, i.e. should it encompass DSO’s? 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 across borders)?**

The vision can and should be a consistent paper that takes into account this survey and today’s reality characterized by substantial differences among European countries respective the state of liberalization. In our view, a conceptual model for the European gas market constitutes a top-down set of principles that tackle the core problem of a different state of liberalization among the EU-member states. In general, it is of utmost importance to avoid over-regulation and to trust in market-driven processes (e. g. with respect to the definition of capacity products, reliance on open-season procedures).

However, with respect to some aspects, a harmonization and standardized definitions are essential. This is particularly true for the definition of an EU-wide gas day. We strongly support the introduction of an EU-wide gas day. In an integrated European gas market, there is a need for a consistent definition both of time and of energy units. As daily balancing is almost universally accepted, the day could be defined e.g. CET 06.00 to 06.00, while the energy unit should be kWh (instead of bcm).

**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?**

The gas market model description should focus on basic principles respective genuine regulatory issues, e.g. entry-exit zones, market-based balancing, congestion management, capacity allocation, framework for investments, transparency and tariff structure.

Of particular importance is to avoid discrimination across Europe with respect to the rules governing the bundling of capacity. With respect to some aspects like e.g. the design of auctions, a patchwork of rules varying from one MS to the other would harm the development of competition.

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

Since the gas market model description should focus on basic principles respective genuine regulatory issues (entry-exit zones; market-based balancing; congestion management; capacity allocation; framework for investments; transparency; tariff structure), it should not entail rules on matters related to trade issues (like wholesale pricing).

**7. What are the options for integrating the currently fragmented European markets? Are there any existing models you would like to recommend? In case your answer is yes, we would be interested to learn 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?**

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

While the merging of balancing zones in general enhances liquidity, the downside is that valuable transport capacities are extracted from the market (which might necessitate compensation measures by transmission system operators that are disproportionately expensive). That trade-off demands a thorough inquiry whether alternative solutions like the coupling of several market areas or regional cooperation are in particular cases preferable. The further reduction of balancing zones thus has to be meaningful from an economic perspective. For these reasons, a specific number of balancing zones suitable for Europe cannot be designated in advance.