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CEER Call for Evidence on the Vision Paper for a conceptual model for the European gas market (# C10-GWG-70-03)

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Dear Ladies and Gentlemen, dear Mrs. Geitona,

EnBW welcomes the opportunity to comment on CEER's call for evidence on its "Vision Paper for a conceptual model for the European gas market".

Before concentrating on answering the proposed questions, we would like to describe how we deal with the call for evidence and the development of the gas market target model for 2015.

In this exercise we see the need to take a look at characteristics and prerequisites of a possible target model. The next step is to concentrate on the essential content of the target model. In our answers we then come up with principles we think should be embedded in a target model.

We are curious how all the stakeholders' input and the results of the study by Florence School of Regulation and the Clingendael Institute will be combined in a number of options as foreshadowed at the CEER workshop on December 3rd 2010 in Vienna. Therefore it will be interesting to see how the options will look like and how and if they can be the basis for further, more detailed work and consideration.

Before we can talk about content we have to step back for a moment and consider essential characteristics of a possible target model:

- The target model must be pragmatic yet ambitious at the same time
- It revolves around the idea that all maturities of contracts for buying and selling wholesale gas on forward, day-ahead, intra-day and balancing markets are available in all EU gas markets
- It builds upon recent discussions of FG on CAM, CMP, Balancing and takes into account upcoming outcomes of the tariffication issue
- It sets out principles that are accepted as a common reference point

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- It gives guidance on how to encompass necessary differences in national energy policies (where they are needed)
- It is in so far prescriptive in areas which endanger a single European Gas Market to evolve
- It identifies the challenges for achieving the goals of the target model and tries to foreshadow issues that may not be resolved by 2015

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?

The Third Energy Package sets up the corner stones of a conceptional model for the European gas market. And although the Gas Directive and Gas Regulation still leave much leeway during the transition process for each Member State, the new European act of law at the same time sets the stage for a new bottom-up approach. In this new unprecedented procedure network operational rules will be standardized on a European level by the development of framework guidelines and network codes.

The purpose of the target model should be to define what a single European gas market should look like and at the same time ensure compatibility of the subsequently developed guidelines (e.g. congestion management procedures should be compatible with capacity allocation mechanisms).

The target model should therefore focus on those areas that are subject to harmonization according to Art. 8 of Regulation 715/2009 and not those that cannot be standardized through the new framework guideline/guidelines procedure according to Art. 6 of Regulation 715/2009.

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

Long-term capacity contracts are one way to reduce a portfolio's risk. They will continue to play an important role. The target model must ensure that long-term capacity contracts become available for all market participants through market-based allocation (see CMP considerations below).

Hubs should become the only place at which gas is traded (through bundled products) – this aim, already clearly stated in the current Draft Framework Guideline on CAM (“five year sunset clause”), shall be included in the target model. This implies that the future lies in hub-to-hub trading only – this will then heavily facilitate cross-border trade.

EnBW supports bundled products. Simplified hub-to-hub trading will surely foster market development, liquidity and allow a maximum of players entering the market. The implementation of bundled products however is a very complex matter which cannot be done, if certain prerequisites are not fulfilled:

- National regulatory regimes allow a closer cooperation of TSOs and make capacity allocation for shippers independent of single TSOs (physical points belonging to different TSOs can become one single “virtual” border point); incentives should be introduced by NRAs for fostering TSO cooperation
- TSOs have a common understanding of capacity calculation and strongly cooperate to calculate capacities relative to the situation in adjacent systems
- TSOs are willing to offer a one-stop-shop to shippers
- A new tariff regime offers lower transactional costs than the ones for current flange trading – flange trading currently is an additional flexibility tool to manage the portfolio without bearing the costs of both the entry and exit capacity
- It is clear what happens with capacities (either a physical entry or exit capacity) held by market participants at only one side of the border
- Standard hub trading processes
- Standard nomination procedures to trade between hubs
- Harmonisation of balancing systems
- Standard trading conditions throughout Europe or at least those markets linked by hub-to-hub trading (no national barriers for trade at hubs, no specific hub regimes in some countries)

If the target model acknowledges the need for hub-to-hub trading and hence the introduction of bundled capacity products as the only way of cross-border gas exchange, there also needs to be a clear understanding that hub-to-hub trading requires changes in current contractual arrangements which must be allowed for.

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.

Non-discriminatory access to (cross-border) primary capacity products is one of the most essential features for the European gas market in 2015. However, capacity issues require a holistic view including the way capacities are calculated and allocated, the existence of efficient congestion management and its link with the way investment decisions for new infrastructure are taken. EnBW therefore proposes the target model shall include principles on...

- ...how TSOs calculate available capacities
- ...how TSOs cooperate cross-border
- ...how TSOs allocate capacities
- ...how the market can trigger new investments to happen
- ...how market participants are incentivised to book according to their needs and return unused capacities to the market

TSOs enabling cross-border competition through harmonised capacity products and processes should therefore be a key object in a target model. From an EnBW point of view TSOs should develop a cross-border i.e. common understanding of their grids in order to maximise the available capacity in all time horizons and calculate capacities jointly. We also see the need to create one-stop-shops for primary capacity allocation, e.g. on a regional basis (example: CASC CWE in power). Allocation should only be possible through auctions.

Since TSOs have a natural monopoly, it is crucial that their function allows for changing needs of the market. Even if effective CMP comes into force, investment in new infrastructure must be possible and regulators have to ensure that they cooperate in a way that prevents lengthy planning and decision procedures. The target model has to include ideas on how cross-border investments are financed to facilitate the regulators' work. The market-based primary capacity allocation procedures should be designed in a way that they give investment signals to the TSOs - if needed additional efficient investment trigger signals should be mentioned. Investment in new infrastructure should however be the last resort after all necessary congestion management procedures have been taken.

This brings us to a closer look on CMP. After having mentioned responsibilities of TSOs and regulators, CMP takes market participants and their booking behaviour into focus. We are convinced that efficient and non-discriminatory CMP principles will prevent over-investment and therefore must be an integral part of the target model. It must ensure that all capacity contracts are treated equally in terms of CMP, no matter when they were signed - this will lead to changes in existing contracts (affecting those contracts of the pre-competition market phase; the competition market phase starts once market-based capacity allocation is in place).

Furthermore, the target model has to set out principles on the reset of legacy contracts including an incentivisation to do so on the market participant side, which goes further than the current CMP discussion. We encourage the EU Commission and the regulators to boldly give a clear commitment that a market-based reset is an option. This reset does not mean building up the market from scratch, but to put the market on a fair basis, which currently does not exist. Neither does a reset of legacy capacity contracts endanger security of supply. It would strengthen the market as to offer the gas needed in the market on a truly competitive basis. We see that such a market-based reset paves the way for fair price building in market-based capacity allocation and for the access to long-term ca-

capacity contracts for all market participants. We are happy to discuss this idea further in the range of one of the market model options.

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:

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 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)?

In order to develop a target model for a single European gas market, we have to assume a couple of prerequisites, which should already be implemented as foundation stones of the competitive market model:

- The market must agree on characteristics of a target model
- The EU Commission must make clear how and when it ensures existing but unfulfilled requirements will be fulfilled (e.g. implementation of entry-/exit-systems)
- A target model can only be accepted if transparency in every step of its development is guaranteed – explanations why some ideas are included and not others are needed
- All stakeholders must commit to the target model process
- kWh is the only valid measurement unit relevant for the wholesale market (trade and capacity-wise)
- Every balancing zone has a virtual trading point
- Definition of a standard gas day (no time differences due to time zones; e.g. 6:00-6:00h CET)
- A set of standard primary capacity products must be specified

Although we think a gas day like proposed above is a pragmatic goal for 2015, we also see the need for further investigation and impact assessment on if and how the electricity and the gas day could be aligned (see below).

Aside from the fact that DSOs may be indirectly affected by the harmonization of rules regarding e.g. balancing, data exchange or capacity management, we do not see the necessity to have the gas target model encompass DSOs.

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 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?

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

The design of balancing systems plays a crucial role in order to enable market and balancing zone integration. EnBW sees the need for the target model to set out principles of market-based balancing as discussed in the scope of the FG on balancing.

A number of balancing zones will then be naturally enabled to merge, yet we do not think that a specific target number of balancing zones is helpful. Merging balancing zones is a complex matter and has upsides (making trade easier) that may come with major downsides (e.g. reduce cross-border capacities). We support the idea to create balancing zones in regional rather than in just national boundaries.

We are fully convinced that market coupling is one important element of electricity market design. Its definite upsides known from the electricity perspective should be explored in gas as well as being one of the tools to optimise the use of capacity between neighbouring balancing zones in the day-ahead time-frame. Thus we see the need to develop a common understanding on what market coupling in gas is and how it should work.

Complementary areas or aspects to be discussed

We see the target model discussion as a good opportunity to assess certain questions further in the coming months. One of those issues is the possibility of a harmonised "energy day" (electricity and gas). Others are the necessity to reflect the influence of renewable energy sources on the gas market and the standardisation of gas quality (i.e. odorisation of gas in a TSO system in one country is a major barrier for cross-border trade).

Conceptual gas market model design in 2011 for 2015 and then?

We think CEER should not only focus on the content as such, but also consider its implications. As an example it should be clear how long the target model is applicable, i.e. the target model influences down-to-earth discussion, but outcomes of these discussions must be reflected again in a possible revision. Therefore an alignment process is needed once the current FG/NC processes in gas on balancing, CAM, CMP and tariffication have been worked through. It is also important that, once a target model is actually a widely accepted one by stakeholders, no parallel exercises are done. It is therefore crucial to have TSOs, the EU Commission and market stakeholders all on board.



EnBW will actively take part in the discussion on the upcoming options and we hope that our comments so far contribute to CEER's work on designing a limited number of those options for a gas market target model for 2015.,

We remain at your disposal should you have any further enquiries.

Kind regards.

Yours sincerely

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