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Position Paper

ERGEG Pilot Framework Guideline on gas balancing rules

Berlin, 28. Oktober 2010

General Remarks

The German Association of Energy and Water Industries (BDEW) represents 1,800 members of the electricity, gas and water industry. In the energy sector, we represent companies active in generation, trading, transmission, distribution and retail.

We welcome the opportunity to comment on the ERGEG Consultation Paper.

BDEW believes that a harmonised European balancing system should lead towards:

- Market based procurement of physical energy (by Network Operator)
- Market based settlement of individual imbalances of shippers on a daily basis, whereas within-day-balance or restrictions for groups of customers may be possible
- Minimisation of costs from balancing actions
- System users to absorb consequences of own actions (avoid unjustified cost socialisation)
- Development of liquid market places
- Reduction of market role of TSOs, i.e. shippers should balance their portfolios through transactions at a liquid market within the respective balancing period.

A market design should be fair and transparent and discourage market abuse.

The rules for participation in the balancing market shall ensure that as many market participants as possible, under technical and economical restrictions, can participate to maximise liquidity.

The relation of any balancing regulation to measures stipulated under related regulations such as framework guidelines for CAM & CMP and the EU Security of Supply Regulation must be clear and overlap must be avoided.

Sanctity of contract should also be considered and honoured as part of any transition to a harmonized balancing regime across the EU.

Questions for stakeholders

Problem identification, scope, definitions, purpose, policy objectives and compliance

(1) Do you agree that the problems identified in the problem identification chapter are the main ones? Are there additional problems that should be addressed within the gas balancing pilot framework guideline?

We believe the consultation outlines the main issues but note that in some circumstances the issues raised (access to storage and capacity) are expected to be addressed outside of the pilot framework guidelines on balancing. In these cases, coordination between the parallel developments of pilot framework guidelines is called for. In addition it is unclear how these guidelines would apply in relation to emergency response mechanisms/security of supply regulation.

We like to point out that current national balancing provisions have been developed according to system needs. Further, the physical networks have evolved over time in order to comply with the structure of the demand for natural gas and the wholesale gas market. Therefore, the problem identification should take into account that there are physical differences among entry-exit systems that must be considered in the design of a harmonized balancing regime.

(2) Do you agree with the scope (section 1) and objectives (section 3) of this pilot framework guideline? Are there policy issues that should, but are not currently addressed by the draft document?

The main objective of the framework guideline should be to achieve a level of harmonisation of balancing systems across EU transmission networks that supports the development of competitive gas markets and benefits consumers, whilst at the same time safeguarding security of supply and the safe operation of the network.

To help achieve this, the framework guideline should provide a framework for the creation of balancing systems that are non-discriminatory, avoid any undue barriers to entry and complexity, are transparent, easy to communicate and understand, market based, cost-reflective and that to the extent possible avoid cross-subsidization between users.

The primary objective of the framework guidelines is to set out clear and objective principles guiding the development of the Network Code. A target model in itself does not provide these principles, a target model is welcomed as useful in addition to clear principles as an explanation on how the principles could be applied and what the impact of them would be.

(3) In your view, should the European network code for gas balancing lead to an amendment of national balancing rules? If so, how detailed should the European target model be?

Naturally the European network code has to result in modifications of today's national system designs. The European target model should be as detailed as possible. It should allow for national deviations when these are justified for obvious commercial or technical reasons.

National balancing rules should be amended where there is significant misalignment with the European target model but only to the extent this misalignment hinders the development and liquidity of the market.

Regarding the strong ongoing progress in the German gas market, for Germany remain only smaller amendments to achieve the European target model. Therefore we appreciate amendments of national balancing rules for one European target model.

Unless one set of national balancing rule is adopted for Europe, amendments will be inevitable. At the present stage it is difficult to anticipate which aspects of national balancing rules will have to be amended. However, the level of details should allow enough flexibility to develop an efficient balancing regime that both complies with the system needs (See

Question 1) and facilitates cross-border gas trade where current balancing regimes constitute the main obstacle.

(4) Do you agree with the approach of defining a target model for the network code and allowing interim steps subject to NRA approval?

The framework guideline on gas balancing should be striving for a single target model for balancing regimes in all European gas markets.

Physical specifics in the different member states – particularly network design and available flexibility – will in some cases require interim steps. This is to be acknowledged in case there is a clear timetable for transition to the target model. After implementing the interim steps the European networks should be able to meet the principles of the proposed target model.

(5) What timescale is needed to implement the provisions in the target model outlined in Part II after the network code is adopted? Is 12 months (as in section 10) appropriate or should it be shorter or longer?

IT development periods and the establishment of interfaces between the TSOs, DSOs and the shippers will be a key element in determining the required implementation period.

Taking into account the experiences gained from the implementation of the current German balancing system (GABi Gas), a reasonable implementation period should be considered to avoid unnecessary discomfort for all stakeholders involved.

While physical investments may have to follow an approval process with the NRA and programming and implementing of new IT systems or of new measurement systems certainly do require more than 12 months, other measures, e.g. commercial procedures or calculation of market-based reference prices, can be implemented in a short term. Therefore, we recommend to not impose a uniform time limit but rather to respect costs and technical feasibility. Defining deadlines should be reserved to until it is clear which measures are to be taken and to which measures they will refer.

(6) Should the pilot framework guideline be more specific regarding the purpose and policy objectives for network codes (section 3), in particular areas including nomination procedures?

The pilot framework guideline should outline the policy objectives with the detail behind these objectives worked by ENTSO-G as part of the network code development process. ENTSO-G should then closely consult with stakeholders during the network code development process.

Consistency with other network codes and the outcome of other comitology processes is essential for a proper operation of gas networks.

(7) With reference to section 3 (proposed policy objectives), do you have comments on how Article 21 of the Gas Regulation 715/2009 should be reflected in the gas balancing network code?

Please refer to our responses above.

The role of network users and TSOs

(8) Is it necessary to have a harmonised approach to the network user and TSO roles regarding gas balancing?

BDEW believes that a harmonized approach between the TSO and network users according to their individual market role responsibility will lead to a more efficient system, where networks users have primary responsibility for balancing their positions via a trading point / liquid market and the TSO has its primary responsibility to residually balance the system. Clearly this assumes a liquid market and availability of timely information as outlined in Article 21(2) and Annex I chapter 3 of Regulation (EC) No 715/2009.

We welcome the proposition on roles as set out in Sections 5.1 and 5.5 of the proposed framework guidelines. However, the framework guidelines should target for a clear definition. This would facilitate the development of and ensure consistency in the network codes.

(9) What are your views on the proposals for the target model to be reducing the need for TSOs to undertake balancing activities?

The target model should lead towards a stepwise reduction of market role of TSOs and thereby simultaneously ensure that TSOs are enabled to efficiently access liquid markets for flexibility products.

The framework guideline seeks to define a common but optimal target model for Europe. Implementation in each system may therefore give rise to some variation. The framework guideline should be explicit about the criteria to be used to define when markets (i.e. access to wholesale markets) rather than mechanisms (TSO use of balancing platforms) should be sought.

We welcome the introduction of possible intermediate steps towards the target solutions. However, FG proposal involve a fundamental change for many network users and TSOs. It is therefore required to establish confidence in market: a single transition step towards the target model might therefore not be sufficient. A stepwise approach may be required.

(10) Is it appropriate for the target model to impose within-day constraints on network users? If so, should such constraints be imposed on all network users or only on certain groups of network users? If within-day constraints should only be imposed on certain groups of network users, which ones are these? How could this be justified?

A proper assessment of system needs is essential to identify the scope for each market role. Whereas system users underlie the standards of a simple commoditized daily balancing regime and TSOs are in charge of system management requirements there is a need for an optimized split of the responsibility for locational and temporal requirements.

Within-Day constraints can be necessary measure in an interim step to ensure system stability.

Any within day constraints should be justified and applied in a non discriminatory way across all network users, once all other measurers available to TSOs to remove those constraints have been utilised. In the German balancing regime (GABi Gas) within day constrains are used for single network user groups with important impact on the network stability (e.g. power plants).

The target model should use the daily balancing.

(11) Is balancing against a pre-determined off-take profile a useful interim step?

BDEW supports the balancing against a pre-determined off-take profile. The pre-determined off-take profile should reflect the real off take profile as exactly as possible. .

The German system GABi Gas has established the Day-ahead allocation of non-daily metered customers. All customers have to be allocated through the DSO every day until 12 o'clock for the next day. This system has the major advantage that all network users know in advance the amount of gas they have to deliver on the next day. This leads to a strong increase of suppliers on this market segment.

(12) Should TSOs have the option to sell flexibility provided by the gas transmission pipelines system (linepack) subject to the NRAs' approval? If so, should this be mandatory?

Linepack is an essential instrument for balance fluctuations within-day or for longer term. While some networks may have excessive linepack available, others may rely on additional external flexibility products. Therefore, offering linepack on a market is an option that may be profitable and that may facilitate access to flexibility products in adjacent networks. However, offering this instrument on a market would possibly preclude a network operator from his only instrument that is solely controlled by himself on a short term basis to ensure system integrity and shall therefore not be mandatory in any case.

If TSOs have excessive linepack available first of all the TSO should use this linepack to optimize the entry-exit systems and to eliminate capacity bottlenecks. After having optimized

the grid capacities, TSO should have the option to sell flexibility from the linepack at the wholesale market, if they use the additional revenues for reducing fees or charges for all network users. As a result all network users, not only the trigger one for balancing activities, will have a benefit.

The TSO should ensure network users are provided with non-discriminatory and cost reflective access to flexibility services to aid network users to balance their position to the extent technically possible, within the capabilities of the transmission system. For the avoidance of doubt the above comments relate to flexibility services owned/operated by the TSO and should not be interpreted as forcing availability of commercially owned flexibility assets to market participants at cost.

(13) Should the target model enable TSOs to provide tolerances to market participants for free or should this be an interim step?

Tolerances mainly serve as an instrument to distribute the cost for balancing services among network users. Offering tolerances to one group of network users implies that the costs have to borne by other users. A cost sharing rule shall reflect in a fair way the extent to which a group of users contributes to the balancing needs and costs. When a market-based balancing regime properly reflects and allocates the costs, tolerances may be unnecessary.

Tolerance levels should reflect the actual technical capabilities of the transmission system and capabilities of network users to balance their positions. Any charges for providing tolerances in a daily balancing regime should be cost reflective. Last but not least tolerances make the balancing procedures more complex and least transparent.

TSO obligations on information provision.

(14) Are there any additional information requirements that you believe should be included? In particular, should the pilot framework guideline oblige TSOs to provide information beyond the requirements set out in the revised Article 21 and Chapter 3 of Annex 1 to Regulation (EC) No 715/2009 (as recently approved through comitology)? If so, please provide details?

The Network Code shall ensure that all necessary information to comply with the balancing regime and to properly react to incentives are provided to the market. This shall reflect the needs created when implementing an efficient market-based balancing regime. Further, the information provision requirements shall enable both TSOs and network users to take proper measures to keep the system within operational limits. Costly investments which, in the end, would be borne by final consumers should be subject to a thorough cost-benefit analysis and NRA approval. In any case, transparency provisions are to be observed. Interactions with transparency guidelines are to be considered.

In order to be able to manage their balance position efficiently e.g. in making decisions on how to re-nominate within day, shippers need user friendly timely (in some cases) online access to information on:

- Their own detailed balancing status (including metering and allocation data etc.).
- It has to be ensured that TSOs and DSOs cooperate in order to provide shippers with the information they need. For this reason it is important to clear possible inconsistencies between the framework guidelines for TSOs and the national network codes that are relevant for DSOs. As DSOs do not have a formal role in the development process of the network codes they have to be integrated in the above mentioned clearing process in a balanced way.
- As additionally, all information the TSO is already obliged to provide under Regulation 715/2009 and its annexes.
- As soon as possible after the close of the balancing period, the TSO must provide each individual shipper with a detailed breakdown of the imbalance costs that shipper has incurred.
- Information on the volumes and prices for TSO balancing transactions at the end of the balancing period.

(15) What are the benefits and disadvantages of TSOs providing network users with system information?

It has to be ensured that full system transparency in combination with a model like the one which will be used in the Netherlands does not lead to technical system instabilities caused by shippers simultaneously trying to "help the system" by optimizing their imbalance status.

The benefits for network users are transparent information about the system status. Publishing close-to-real-time information to all network user could be helpful to optimize the own trading strategy. However providing real-time information regarding prices and volumes of TSO activities for balancing could support arbitrage trading against TSO and should be avoided.

From a TSO perspective, shippers taking actions to balance their portfolios are very much appreciated. Detailed system information should not lead to a possibility to misuse the respective information (e.g. for any arbitrage activity) against the balancing system.

(16) What are the costs of TSOs providing network users with system information? How do compare against the benefits and/ or disadvantages?

A through cost-benefit analysis would be an appropriate instrument to answer these questions. Physical investments and amendments of the IT and measurement systems would certainly be necessary for TSOs and DSOs but, at the present stage, any guess would not rely on proper information and would be misleading.

The TSOs and the DSOs need to be able to recover any (efficiently incurred) costs.

Balancing periods

(17) What are your views on our assessment of the policy options?

We believe the main policy options have been considered.

(18) Are there relevant additional policy options on balancing periods which have not been considered in this section? Should these be considered going forward?

We believe the main policy options have been considered.

(19) Is it necessary to harmonise balancing periods? If so, what are the benefits of a regional or pan-European harmonised balancing period? If not, why is it not necessary? Please explain your answer.

Yes, the target model must provide for a harmonized balancing regime on a daily basis including the harmonization of the gas day. The balancing period is an essential characteristic of the balancing system, and different periods would lead to substantially different market designs. This would surely not facilitate cross border trading. Also within daily balancing restrictions or within daily balancing obligations for some customer groups must not be contradictory to a sufficient compatibility of balancing systems.

(20) If you agree with a harmonised balancing period, what do you consider is the appropriate length of the balancing period?

Throughout Europe BDEW supports a daily balancing period. Within day constraint for some customer groups must be possible. (See also question 19)

(21) Do you agree with the target model? Please explain your answer.

We agree with the target model proposal of daily balancing as this regime affords network users sufficient time and flexibility to balance their position and optimizes their portfolio, thus facilitating liquidity within the market.

However, the target model should not include strict within-day restrictions. Restrictions may eliminate to some extent the efficient and flexible access and usage of the networks. Furthermore, strict restrictions may not be suitable to comply with locational and temporal needs of flexibility products. Therefore, proper market-based within-day incentives constitute a more favourable instrument in order to efficiently operate and balance a network.

(22) What would be the costs of implementing the target model in (and beyond) your Member State or balancing zones(s) (as the case may be)?

The costs for implementing the target model depend on various assumptions (e.g. implementing the necessary IT Infrastructure). Therefore an assumption of the concrete costs is difficult.

If an inappropriate target model should be implemented, possibly because of an insufficient assessment of all benefits, consequences, and, especially, alternatives, the forgone efficiency gains have to be borne by network users who cannot pass-on additional costs to final consumers.

TSO buying and selling of flexible gas and balancing services

(23) Do you agree with our assessment of the policy options?

BDEW likes to point out that there are two different requirements on balancing:

Portfolio balancing for System users to balance their portfolio based on sales/ purchases of flexible supplies (including intraday trades at virtual points) and physical system balancing for TSO to ensure physical system integrity based on sales/ purchases of flexible supplies (typically location specific).

For the purpose of portfolio balancing it should be noted that:

- Shippers must be enabled to balance portfolio imbalances during the balancing period at a trading point.
- Remaining imbalances must be settled by TSOs.

For the purpose of physical system balancing through system control energy should be noted that:

- Use of liquid trading points to an extent as large as physically possible (some need for locational products will persist in networks with internal congestion)
- Availability of standardised Balance-of-Day/Within- Day product[1]
- The Network Code shall foresee appropriate alternative instruments in case that the aforementioned availability of flexibility products and liquid markets are not existent.
- No reservation of transport capacities for balancing purposes

[1] The initial impact assessment presumes that offering short term flexibility products, e.g. within-day gas, is in the interest of the active market participants, either on the wholesale market or on a stand-alone balancing platform. By designing a daily balancing regime with highest flexibility, the shortest product that serves the trade purpose will be a day-ahead product. Consequently, within-day products, which may be essential for balancing purposes, define a separate relevant market, for which no liquidity will be generated. The TSOs cannot take measures to increase the liquidity on their own. The mere need of the TSO who is in charge of the residual balancing of a network would not be enabled to ensure that a market for flexibility products emerges.

- No reservation of storage capacities for balancing purposes through the TSO. Traders could offer gas, based on market prices, from own flexibilities (also storage flexibilities) to the TSO.

TSOs welcome that balancing services, including the procurement of flexible gas is considered as a complementary service to the physical infrastructure, and that these services shall be cost neutral to the TSOs.

We suggest the framework guidelines to impose on the Network Code to foresee instruments, rules and measures that facilitate the creation of liquid markets for flexibility products.

(24) Do you agree with the target model? (Please give reasons). If so, what do you consider are the benefits and disadvantages of the target model?

A transition towards the target model must be preceded by an assessment on both the availability of all required products and facilities on liquid markets and on the economic consequences of such a transition.

The target model considers a balancing platform in the case of insufficient liquidity, however we believe the target model should focus on achieving a fully liquid market, and the use of a balancing platform as an interim measure whilst market liquidity is addressed.

(25) What are the costs of implementing the target model in your Member State?

Member states to provide a response.

(26) What interim steps, if any, may be needed in your Member State or balancing zone(s)?

Member states to provide a response.

(27) Is it appropriate for balancing platforms to be part of the target model subject to NRA approval, even where markets are sufficiently liquid to enable TSO procurement on wholesale markets?

Balancing platforms may be necessary to allow for procurement of locational and temporal products, as there may be situations where network topography and the distribution of flexibility sources hamper the balancing of physical imbalances by energy procured at the virtual trading point. However, the use of locational products has to be limited to the extent that is necessary for a proper system management.

(28) Is it appropriate for TSOs to procure balancing services on the wholesale market and/or or is appropriate for these to be procured on the balancing platform? Should TSOs be permitted to reserve long-term contracts for flexible gas and/ or associated capacity for this purpose?

Where the normal commodity market provides all products which are necessary to manage the network system properly and the market is sufficiently liquid to ensure full supply of all balancing energy needed, special balancing platforms should be redundant. Wherever these requirements are not in place, platforms should be implemented as an intermediate step.

(29) In your view is it possible in your market to reduce TSOs' reliance on long-term products? If so, how may this be best achieved?

We believe it should be possible to reduce TSOs reliance on long term products where sufficient liquidity and competition exists in the market.

Whether long-term products are suitable will highly depend on how they are designed, e.g. they may have to provide conditional access to physical injection or outflow, and on their availability.

Imbalance Charges

(30) Do you agree with our assessment of the policy options?

We believe the main policy options have been considered.

Imbalance Charges in Europe need to be based on objective criteria meeting the standards of fairness and non-discrimination. Imbalance charges should reflect the costs of TSOs undertaking balancing actions. In case of market-based procurement of balancing energy the imbalance charges thus approach the market price. At the same time the charges must provide for adequate incentives for shippers to balance inputs and offtakes and facilitate the participation of new market entrants.

(31) Do you agree that methods for calculating imbalance charges should be harmonised? If so please explain what the benefits may be. If not, please explain why not.

We agree it would be beneficial to harmonise the calculation of imbalance charges on a pan European basis, as this would help facilitate better integration and liquidity across Europe. However we believe some flexibility is required during the interim period to recognize the current differences and time required to address those differences.

The network code shall ensure that calculating methods meet the system needs.

(32) What are your views of the target model? In particular, please provide your views on:

- **Whether an imbalance charge should be applied when TSOs do not take balancing actions;**
- **What the imbalance charge should be based on, if it is applied when the TSO has not taken a balancing action, whether imbalance charges should be dual or single priced;**
- **Whether imbalance charges should be based on the marginal price.**

We agree with the target model using the TSO marginal price as basis for imbalance charges. If there has been no TSO balancing action then we believe a charge is still payable and could be based on the daily system average price i.e. a reasonable estimate of what the TSO might have bought/sold at on that day if action had been taken.

(33) What would be the costs and benefits of implementing your preferred options in your Member State?

Member states to provide a response.

(34) What are your views on the interim steps in the document?

We agree with the interim steps to use a proxy based price in the absence of a liquid wholesale market or balancing platform, as long as the charge does not deter new market entry and is approved by the relevant national regulatory authority.

Cross-border cooperation

(35) Are there any other relevant policy options on cross-border cooperation that should have been included in this section?

BDEW suggests that the framework guideline should reflect potential future developments of the market e.g. implicit auctions for short-term allocations, according to Art. 12(2) of the European Network Access Regulation 715/2009.

In order to set out clear and objective principles according to Art. 6(2) of Regulation 715/2009 there should be identified when markets are considered to be integrated. A potential merger of balancing zone shall be preceded by a thorough impact assessment which shall identify whether the incremental benefits compared to implicit auctions outweigh the costs of merging of balancing zones.

(36) Do you agree with our assessment of the policy options in this section?

BDEW supports thorough assessment of the costs and benefits of harmonisation of cross border cooperation as much as possible. Transmission system operators may elaborate on how to harmonise balancing regimes and streamline structures (in particular the balancing period and the basis for calculating balancing charges, but also the calculation of line-pack and time, frequency and format of information provision) in order to facilitate cross border gas trade.

The description of the issues that cross-border cooperation shall cope with requires additional clarification. In particular it is not clear to what extent the multiplicity of balancing zone is considered as an issue or the existence of several market areas. Consequently, we express severe doubts that a merging of balancing zones is key to tackle the issues mentioned.

One Priority should be to introduce market based balancing concepts that allow market players to deliver flexibility cross-border to converge prices and that way better integrate markets. The TSOs assert that the framework guideline put too much emphasis on merger of balancing zones. We note the risk that although larger zones might increase liquidity, this may detract from physical system operational efficiency and prevent market based solutions on handling situations of physical congestion. Merging zones is a heavy tool, that has serious consequences and that could even be counter productive in achieving a transparent internal market for energy. Balancing zones shall be designed such that the balancing regime creates incentives to keep the network in balance. However, a merge of balancing zones can create obstacles to ensure system integrity by the TSO and increase opacity on physical congestion. Usually, balancing gas may be needed (or excessive) within a particular network. By creating a large balancing area that covers several networks, the provision of balancing gas cannot be targeted to the location where is needed – unless the market for balancing services introduces a locational dimension to the marketed products. This, in turn, would create submarkets within a balancing zone without efficiency gain. Further, on the cost side, costs would be averaged and allocated to users in the entire balancing zone rather than targeted to the users who are causing the need for balancing services.

The underlying intuition of the framework guideline is that the market will balance more efficiently than a single monopoly agent. We propose that the primary focus should be to ensure access to capacity and balancing roles that enable the market to deploy cross-border flexibility as much as possible. A further need is to consider the roles market players under very different system designs that exist for good reasons, throughout Europe. Merging of balancing zones might then come later once the wider implications (particularly tariff) are better understood.

(37) Are Operational Balancing Accounts (OBAs) useful to deal with steering differences? Should the network code make it mandatory on TSOs to put in place OBAs?

BDEW supports transparent mechanisms that facility better cross border trade and improve regional cooperation. OBAs seem to be a useful tool to deal with steering differences and are therefore already facilitated at different IPs.

OBAs constitute agreements between TSOs which are designed to cope with steering differences. They mainly have an operational dimension. Therefore they are only of limited use for balancing purposes where network users are involved. Rather their benefit is to reduce the complexity of settlements among TSOs and to facilitate the equivalence of nominated and allocated quantity of network users. OBAs are put in place when network operators agree that they are necessary to operate an interconnection point. Thus, we suggest the framework guideline to support OBAs according to system needs without a legal obligation.

ERGEG may envisage including OBAs in the upcoming framework guidelines for interoperability.

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