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Draft Pilot Framework Guideline on Capacity Allocation on European Gas Transmission Networks (E09-GNM-10-05 and E09-PC-46)

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Dear Ladies and Gentlemen, dear Mrs. Geitona,

we welcome the opportunity to provide our input to the Draft Pilot Framework Guideline on Capacity Allocation on European Gas Transmission Networks, in particular in reply to the questions put forward in the consultation documentation.

General

What are your main views of the proposed measures? Do you think network codes based on these guidelines can achieve non-discriminatory and transparent capacity allocation and the fulfilment of the capacity allocation principles set out in the Third Package of Energy legislation?

Overall, we very much welcome ERGEG's ambitious approach towards more integrated markets. But we also have to state that there is no simple answer to the question if network codes can achieve non-discriminatory and transparent capacity allocation – there is not necessarily a direct link between the network code and the wished-for positive effects.

Marked-based CAM depends on a whole set of prerequisites. The issue of CAM is subject of this consultation but cannot be seen separate from CMP. We believe that one crucial element for achieving non-discriminatory and transparent allocation is the implementation of effective CMP regime that creates a true level-playing field and gives all market participants the same chances. Ideally, CMP will resolve the problem of contractual congestions and reveal the really, physically contracted interconnections. This will lead to fair prices for capacity products for all market participants.

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In setting up its target model, ERGEG has rightly compiled principles that deal with both capacity allocation mechanisms and capacity congestion management procedures, hence ensuring a compatibility between both processes. Then the development of the guidelines for congestion management and allocation mechanism were separated. While CMP guidelines will be adopted via Comitology Procedure the Draft Pilot Framework Guideline on CAM is open for public consultation. In the consequence of the different procedures of development of these guidelines, the new CMP rules will come into effect with a legally binding character before the new CAM guidelines / network codes. Taking into account that effective CMP is a crucial prerequisite for a well functioning CAM EnBW welcomes this proceeding but at the same time points out that the responsible institutions (e.g. ERGEG / ACER, ENTSOG) have to ensure the compatibility of CMP and CAM rules in the future.

Another important prerequisite for a new CAM approach is the implementation of entry-exit-systems throughout the EU and a common understanding of technical terms such as a gas day. The network code has to ensure that such a common understanding is reached.

Another essential prerequisite for a non-discriminatory and transparent capacity allocation is the network code definition process and the level by which all stakeholders and especially those willing to expand their business opportunities are consulted by ENTSOG and the degree by which their input is taken into account when writing the network code. ERGEG/ACER, ENTSOG and the EU Commission are those bodies defined by the Third Energy Package that play a part in the Framework Guideline and network code process. A successful completion of their work is only guaranteed by thorough consultation of the stakeholders.

As much as we see the amount of work done and time spent by ERGEG on CAM we miss a more thorough impact assessment focussing on the economic effects of the measures proposed. We therefore encourage ERGEG to add more detailed cost-analyses to future impact assessments of Framework Guidelines.

What are your views of the implications of each for the measures for sector in which you operate? In particular, we are interested to understand the nature of the implications in a qualitative way (and, if available, any quantitative evidence on costs and benefits would be extremely welcome).

TSOs would be responsible for implementing the measures proposed by ERGEG. Measures - in particular the implementation of standardised communication procedures and the establishment and application of auctions - result in additional efforts and costs for TSOs. Hence the acknowledgement and the allocation of expenses are of crucial importance for TSOs. In our view the efforts and expenses for implementing these measures should be accompanied by incentives given by NRAs to TSOs.

From a market perspective effective CAM and CMP will create a fair framework in which all market participants will act on the same level-playing field. Market-based CAM will allow easy access to capacities for new market entrants by giving

a fair value to capacities. Depending on the speed of integration of markets this will enhance the liquidity of adjacent markets / hubs and not only facilitate competition on the level of commodity trading but furthermore allow for more opportunities for competition in the retail business (downstream). Easy access to capacities will hence create competitive ways for sourcing in the downstream business (B2B and B2C). As much as new market entrants will profit from fairly priced capacities so will customers – they will have access to a larger number of suppliers.

Scope of the Arrangements

Do you support the scope of the draft framework guidelines proposed?

EnBW supports the scope of the Framework Guideline on CAM proposed. We would like to stress the role Regional Initiatives can play in the implementation process of this Framework Guideline. Although there shall be a clear target model in place we think that the implementation of the Framework Guideline is not necessarily a synchronised process at all European interconnection points at the same time, there maybe the need to implement harmonised capacity allocation mechanisms faster in those regions with already liquid and competitive markets. This lead will then create the necessary push for other markets to speed up the creation of market-based and non-discriminatory frameworks.

Existing contracts

What are in your views of the challenges that existing contractual arrangements create with regard to capacity allocation? What would be the possible ways to overcome those challenges?

A big challenge for applying a new CAM regime on existing contracts is getting the message through to those affected by the contract changes that putting long-term contracts on a new basis is an essential means to create a European gas market. Fortunately we can already see moves into that direction by some market participants as a new CMP and CAM regime will not only result in business opportunities for new but also for historic market players. The verve of ERGEG's work will eventually change historic business models where they do not comply with competitive and fair market rules. However, to ensure smooth transition the details for those changes have to be set out.

Adapting relevant clauses of contracts to comply with the new regulatory CAM framework will put all contracts on the same standard and will e.g. allow that secondary products cut out of legacy capacity contract portfolios will be compatible with primary capacity products allocated through new CAM.

Should relevant clauses in existing contracts be amended if they contradict the new legally binding set of rules (which will be based on the framework guideline) in order to create a level playing field for all shippers?

It is essential to create a level-playing field on the way to more integrated gas markets in Europe. In that respect it is necessary that the same rules apply to all market participants irrespective of their size and role in the market and irrespective of which products they are currently holding (primary and secondary capacity products, underlying supply-contracts). Any clause contradicting market-based, non-discriminatory and non-transparent principles must be subject to amendment. This applies to all aspects of capacity allocation management as it does to the strongly connected congestion management procedures. Only if the same rules are applied to current primary capacity products then these products can feed in the secondary capacity market in order to foster more liquidity.

Experts have discussed if existing / legacy contracts should be questioned if certain conditions are met, in order to free up capacity, which would then be reallocated. Do you consider such a proposal appropriate?

This question touches upon the core of congestion management procedures. CMP was part of the initial ERGEG consultation on CAM and CMP but is not part of the Framework Guideline on CAM. However, by mentioning this issue in the CAM discussion we understand that ERGEG still sees the strong connection between CAM and CMP. We also understand that without effective, non-discriminatory and transparent CMP the implementation of CAM will never be able to create a level-playing field, e.g. without implementing effective anti-hoarding measures by UIOLI there will be no significant amounts of capacities available for allocation. Examples from the power side show that by adapting legacy contracts major progress can be made towards more market integration. Since the first ERGEG CAM and CMP discussion we have also seen some movement of historically important market participants offering part of their capacity portfolios back to the market.

TSO cooperation

Is the scope of the identified areas for TSO cooperation appropriate to ensure efficient allocation of cross-border capacity in order to foster cross-border trade and efficient network access?

We support further cooperation of TSOs. The cooperation of adjacent TSOs must be accompanied by closer cooperation of the relevant NRAs and the abolishment of inconsistent national regulations. Currently differences and considerable ambiguity regarding CAM and capacity products exist not only between the different Member States but also within one Member State. Thus the creation of a common and harmonised set of provisions and rules is indispensable for fostering TSO cooperation. Furthermore, cross-border harmonised tariff regulation must set the right incentives for closer cooperation of TSOs.

Contracts, codes and communication procedures

Should a European network code on capacity allocation define a harmonised content of transportation contracts and conditions of access to capacity?

When having harmonised products and standardised allocation mechanisms, communication procedures and processes the market eventually needs a harmonised content of transportation contracts and conditions of access to capacity. Nonetheless they should be technically feasible and economically reasonable.

Should a European network code on capacity allocation standardise communication procedures that are applied by transmission system operators to exchange information between themselves and with their users?

Standard processes are a key to foster market integration. We believe that the standardisation of communication procedures applied by TSOs is without alternative. If TSOs are to maximise the amount of available firm capacity they need to harmonise and standardise their calculation methodologies – hence standard communication procedures are the underlying prerequisite. We acknowledge that the standardisation can be rather long as can be seen in the electricity market but once first steps are taken in this regard the added value becomes visible quickly.

Capacity products

What are your views of our proposals regarding capacity products?

Generally speaking we share the view that there is a need to reserve capacity for short-term firm capacity products. The question however is how much is a reasonable amount to ensure more competition. We propose that ENTSOG enters into this discussion with stakeholders when defining the network code. The focus on short-term products (one year and less) should not hinder the allocation of longer-term products to a broad scale of shippers. We see interruptible capacities as a product coming into play once all firm capacity products are allocated.

ENTSOG and ERGEG must ensure that by setting up a new CAM framework capacity marketing should become possible in both directions (as a trading product) of an interconnection point irrespective of the actual physical flow in the physical network.

Do you agree with the idea of defining a small set of standardised capacity products that do not overlap?

Limiting the number of capacity products is a sensible approach however it must be ensured that the limited number of capacity products reflects the need of the market. Furthermore primary capacity products must be designed in a way that

they can easily be traded on the secondary market or be combined with secondary capacity products. All capacity products shall be subject to slicing and dicing by the owner of the capacity right, i.e. long-term products can be split up and short-term products can be combined to longer-term products. We would like to add that harmonising capacity products (e.g. day-ahead capacity) requires harmonisation of market design in adjacent systems (e.g. definition of a gas day).

Should TSOs offer day-ahead and within-day capacity products?

TSOs shall be enabled to offer day-ahead and within-day capacity products. We think however that the focus should be on the development of the day-ahead time horizon. The question of a within-day cross-border capacity market is strongly connected with the development of a within-day cross-border commodity market – one cannot be done without the other. We think that further discussions are necessary on the specific issue of within-day trading as first results of the implementation of the new CAM and CMP rules become visible.

Should European TSOs offer the same capacity products at every interconnection point across Europe?

As we have already seen on the power market standardisation is crucial for further market integration. Even if allocation procedures and capacity calculation methods may not be standardised all over Europe right from the start the standardisation of products is one of the easier exercises. The market needs a set of capacity products (e.g. yearly, monthly and daily products) which can be sliced and diced (this must include the possibility to combine primary and secondary capacity products). A prerequisite for harmonised firm capacity products however is the common understanding of what a gas day is, how market based balancing works and how the products are priced (tariff regime). We see once more how much the different Framework Guidelines are interlinked.

Should TSOs offer interruptible capacity also in cases where sufficient firm capacity is available?

We agree with ERGEG that TSOs must concentrate on the maximisation of firm capacities. In cases without any congestion we do not see the need to offer interruptible capacity products. The network code shall include clear definitions, e.g. of congestion, capacity products (firm and interruptible) and market-based procedures followed in case of curtailment.

Breakdown and offer of capacity products

Should a reasonable percentage of the available capacity be set aside for firm short term capacity products?

The idea of setting aside a reasonable percentage of the available capacity for firm short-term products makes sense to boost market development. However, once effective CAM and more so CMP are in place we believe that there will no longer be a need for such a reservation. We therefore propose a revision of this clause at a later stage.

Cross-border products

Do you support full bundling of cross-border capacity into one single capacity product, including a limitation of the possibility to trade at the border so that gas is traded at virtual hubs only in order to boost their liquidity?

EnBW supports bundled products as the long-term target model. 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 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 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

Do you consider combined products to be an appropriate interim step towards bundled products?

EnBW sees a longer interim period for combined products. We see significant efforts to be taken by TSOs in order to implement combined products at all inter-connection points. The current tariff regime in selected countries favours com-

bined products more than bundled ones. Currently trading is possible at physical points (flange trading) – the use of entry capacities only in order to conclude the deals keeps the transactional costs low as the exit capacity of the other system does not need to be purchased.

Should capacity at two or more points connecting the two same adjacent entry-exit systems be integrated into one single capacity product representing one single contractual interconnection point?

We support the idea of creating a one-stop-shop for shippers. Shippers will be less interested in booking capacities at a specific physical interconnection in the future but more interested in getting capacity to ship gas from one side of the border to the other (in the sense of capacity management facilitating commodity trading). In that respect combining points between the same adjacent entry-exit-systems is the optimal step for further market integration. As we are also an active market participant in the electricity market we see the clear benefits such an approach brings for the market as a whole in our everyday business. Nonetheless the proposed measures should be technically feasible and economically reasonable for TSOs.

Capacity allocation

Should auctions be the standard mechanism to allocate firm capacity products?

Definitely yes, an auction is the most flexible and market-based allocation mechanism which can be adapted to different market designs still in place. We fear that offering different allocation mechanisms will hinder market integration. Even the slightest discussion between adjacent systems whether allocation at interconnection points shall be done on the basis of pro-rata or auctions is time which should be better focused on an actual push towards common allocation procedures. We think that offering options in this respect is counterproductive and not consistent with a target model. TSOs shall not discuss two allocation approaches in the course of network code development but concentrate on one target model.

The price of the capacity in an auction depends on supply and demand. Once again we refer to the need of effective CMP measures in place before implementing new CAM measures in order to prevent synthetic situations of scarcity of capacity caused by contractual congestions. Once contractual congestions are resolved, only auctions reflect the fair price of the capacity.

Another important point to raise in this respect is the strong link between tariffs and allocation procedures. Choosing auctions as the only allocation method also implies that they are used in case of no congestion. In this case there has to be a follow-up discussion on the question of the reserve price. From a pure demand-and-supply-logic the reserve price would than be at 0 (not only on a day-ahead basis but for all capacity products). Yet current tariff regimes set the reserve price above Zero to ensure that TSO costs are covered. We therefore urge all formal

bodies of the formal policy process to consider both aspects (demand-and-supply as well as TSO view) when working on a new cross-border tariff regime.

What would be the implications of using auctions for capacity allocation in the markets in which you operate? Is there any way in which auctions can be designed to overcome potential issues resulting from their introduction in those markets?

We do not share the scepticism of ERGEG in respect of auctions. Auctions, i.e. having fair, transparent and market-based allocation of capacities, can be designed according to the current market design – at the same time they will contribute to move market designs in Europe towards an overall more market-based approach.

Do you support pro rata allocation as an interim step? If yes, should pro rata allocation only be used in given situations or market conditions?

An auction is the optimal and market-based allocation method. EnBW welcomes the idea of a target model of one allocation method for the integrated European gas market. Implementing different allocation methods bears the risk that the integration will eventually take longer than necessary. By mentioning two allocation methods in the Framework Guidelines the network codes will have to deal with the definition of both methods. We are not convinced that pro-rata allocation is a suitable alternative on the way to more integrated markets. We do not follow the argument that in some cases pro-rata allocation will deliver “fairer” results than well-designed auctions taking into account the specific market maturity. Auctions are a means of promoting a more competitive market design.

Re-Marketing Booked Capacity

Should the network code define harmonised firm secondary capacity products and anonymous procedures for offer and allocation of secondary capacity products in line with those on the underlying primary capacity market?

The network code shall define harmonised firm capacity products traded through standard trading platforms. It must be ensured that secondary capacity products can be combined with primary capacity products to manage a portfolio. However, EnBW does not support the idea mentioned in the Draft Framework Guideline that secondary capacity trading shall only be possible through TSO platforms. The Framework Guideline shall not hinder OTC trading. Besides the exchange of standard products, OTC trading shall be allowed for the exchange of non-standard products as agreed by the counterparts. OTC products must of course be designed in the way that they comply with nomination and booking procedures of TSOs. TSOs must be informed in all events of a title transfer.

Booking platforms

Do you think that all capacity connecting systems of two adjacent transmission system operators should be allocated via a joint, anonymous, web-based platform?

We support any means by which primary capacity allocation is facilitated for shippers. The aim must be the creation of a one-stop-shop for shippers to acquire capacity from market area A to market area B. Eventually shippers do not care about booking capacity at certain physical interconnection points. The interest is to get from one side to the other. In order to achieve such a sophisticated capacity allocation TSOs will have to work closely together: capacity products must be harmonised, communication procedures and capacity calculation have to be standardised. Network codes must lead the way into this direction.

The introduction of such web-based platforms requires close cooperation between TSOs which is one of the targets of the Third Legislative Package. Thus we agree with close TSO cooperation in order to establish well-functioning and cost-effective platforms. However expenses for the introduction and operation of such web-based platforms e.g. technical support of the IT systems and equipment, human resources, communication, branding and premises shall not be burdened to TSOs without compensation.

Do you agree that joint allocation of primary and secondary capacity products on these platforms would strengthen capacity markets?

EnBW agrees that a limited number of platforms will concentrate liquidity and may strengthen the capacity markets as a whole. However, strengthening the market also implies giving choice to the market, i.e. allowing OTC trading of capacity rights alongside of platforms. It is essential to find the right balance of standardisation and flexibility which can be achieved by a minimum of primary and secondary capacity platforms (e.g. one on a regional level such as CASC-CWE in the power sector).

EnBW hopes that its comments contribute to answer ERGEG's specific questions in the context of consulting on the Draft Pilot Framework Guideline on Capacity Allocation on European Gas Transmission Networks.

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

Yours sincerely

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