

Mrs Fay Geitona
ERGEG
28 rue le Titien
1000 Bruxelles
Belgium

28 October 2010

Dear Fay

Gas Balancing Rules on European Gas Transmission Networks Draft Pilot Framework Guideline

EDF Energy welcomes the opportunity to respond to this draft pilot framework guideline (FG) on gas balancing; the intention of which is to set out clear and objective principles for the development of a network code.

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, renewables, coal and gas-fired electricity generation, combined heat and power and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including both residential and business users.

This FG could potentially have significant implications for balancing markets in Member States and at a European level as we move towards a single European internal gas market. Few Member States will align directly with the target model and therefore much change might be needed (at significant cost) in order to harmonise regimes across all Member States. It is therefore paramount that a balance is struck between implementing the target model in all Member States and the level of detail and complexity needed to progress towards a harmonised balancing market in gas. It is also important that more established markets are not undermined by the need to harmonise balancing rules across Europe.

Our detailed responses are set out in the attachment to this letter and our key points are as follows:

- The impact on market participants and consumers should be considered carefully when implementing the final target model. It might be advantageous to implement a simplified daily regime that complies with the 3rd Package rather than one which is more complicated resulting in higher costs and implementation issues.
- A balance should be struck between the level of detail and prescription in the code and that which is essential to implement the target model.
- Careful consideration should be given to the design of balancing regimes and the level of costs consumers should be directly exposed to.
- The balancing rules should aim to promote member state and cross border trade

- Credit and collateral are important considerations when designing market arrangements and this should be considered in more detail. Suitable credit arrangements are needed to ensure market participants and consumers are protected.
- We support ERGEG's proposal of using tolerances until markets get up to speed
- ERGEG refers to within-day products, such as profiling charges, as "constraints" when we believe ERGEG may mean "rules". This is an important distinction as the 3rd Package should seek to optimise the appropriate amount of network and constraints
- Finally, we support the use of appropriate impact assessments to identify the cost-benefit of implementing elements of the target model in order to protect the interests of market participants and consumers.

Should you wish to discuss any of the issues raised in our response or have any queries please contact my colleague John Costa on 020 3126 2324, or myself.

Yours sincerely,

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Head of Transmission & Trading Arrangements
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Attachment

EREG Draft Comitology Guidelines on Gas Balancing – E10-GNM-13-04

EDF Energy response to your questions

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

Question 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 agree that EREG has covered the main problems and recognise that the other prerequisites such as Capacity Allocation and Management procedures and Transparency are being covered by comitology procedures. However, we list below several other important factors for a well functioning market that have not been covered such as:

- Credit – efficient and effective credit arrangements are needed to ensure consumers are protected from the potential costs of defaulting shippers and the high costs of credit.
- Gas Quality – variations between markets and Member States need to be addressed, however, we note that this is part of the CEN project
- IT systems – these should be practical, compatible and easy to use to maximise data flows and minimise the level of manifest errors.

These are all prerequisites for a well functioning market and examples of where their absence can lead to inefficient costs being incurred can be found in the introduction the UK Balancing regime in 1996. Wholesale market prices escalated dramatically within a few months of market opening, and in the introduction of NETA where there were several large manifest errors. The issue of different currencies and units of measurement also need to be considered.

Question 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?

We agree with the scope and objectives of this FG. We support the implementation of the target model via a phased approach which would seem more realistic in terms of time needed for effective implementation. We also welcome the comparison and consideration of interactions with the electricity markets.

Question 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?

We would expect the FG to establish network codes that NRAs could realistically and efficiently implement and this may mean revisions to certain national rules. We recognise that there is a compromise between implementing the target model in a realistic and cost effective way and changing national balancing regimes; the two do not necessarily go hand-in-hand. For example, where the balancing regime is intraday, this does not necessarily need to change to be able to introduce a daily balancing regime, as this can be achieved by simply adding an extra balancing incentive at the end of the day.

Whilst this FG should strive for harmonisation it should not mandate a prescribed solution where a simpler option of compliance can be found. This will help protect consumers from inefficient costs being incurred if markets are expected to replicate each other. If the FGs are too prescriptive or detailed this may delay harmonisation of balancing regimes and might incur higher costs. Derogations, if appropriate, may be a way to allow compliance with the FGs where harmonisation is not possible.

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

We agree with the introduction of interim steps in order to implement the target model. This will assist less developed markets to comply and will lead to realistic milestones in achieving harmonisation.

Question 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?

We believe 12 months to implement a balancing regime is a tight time frame which would only be realistic for markets where little change is required to comply. A level of discretion should be given to NRA's to be able to implement the model in their market in the most realistic and effective way.

We would support the consideration of longer timescales for Member States to be able to implement the balancing codes.

Question 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?

Nomination procedures should be harmonised at cross border points. However, whilst they should be harmonised within the balancing zone itself, if possible, we do not believe it is essential. It is important to analyse the impact on trading and liquidity when considering the level of harmonisation needed.

Question 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?

No, we believe the requirements of Article 21 seem to be adequately reflected in section 3.

The role of network users and TSOs

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

As stated above, we support harmonisation where possible however there may be other ways possibly at a national level to protect consumers from inefficient and unnecessary costs.

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

We support the principle of the TSO having a minimal role in the market, as in the UK where the TSO takes residual balancing actions. This promotes trading, liquidity and competition between market participants and should be encouraged.

Question 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?

We do not understand the use of the word “constraints” in this question or whether ERGEG is suggesting they be promoted. The Third package should seek to optimise the appropriate amount of network and constraints so we believe ERGEG means “within-day rules.”

We recognise that within-day balancing rules have a purpose where there might be a lack of flexibility in the particular network and rules are needed to incentivise appropriate behaviours and flows. However, we ultimately believe that the market should operate with an optimum level of constraints to allow efficient trading and competition to flourish. This is the case in the UK where there are within-day rules on flows and profiles, such as ramp rates and renomination rules; however these are not considered as constraints. There are also few penalties as Shippers have strict Licence obligations to follow certain rules. This is better than, for example, imposing financial penalties. Indeed, it has been proven that financially penalising Shippers for not following within-day rules does little to change behaviour.¹

¹ The “Incentivised Nomination Charge” was set to zero after 6 months after analysis showed it made little difference to Shipper’s balancing behaviour.

Question 11: Is balancing against a pre-determined off-take profile a useful interim step?

We agree there is merit in balancing against a pre-determined off-take profile, both in developed and less mature markets as it would create a level playing field for all participants and remove barriers to trade. However, we do not believe in matching renominations, where a change in Entry flows requires an equal change in Exit flows as this might restrict trade and the development of liquid markets.

Question 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?

We believe that this option could be open to TSOs and markets that are less developed with limited access to flexibility. However it is important to note that it is the market's role to sell flexibility, not the TSO's who could be considered to be in a privileged position. It is important that the TSO's role is distinct from Shippers and other market participants so as not to stifle investment and competition.

TSOs should only sell their system flexibility where there is a clear physical reason to do so, where there is no impact on security of supply and where there is a clear market benefit.

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

We support the use of tolerances for new and developing markets to ensure that market participants have time to adapt to the new market and to prevent inefficient costs being incurred.

TSO obligations on information provision

Question 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?

We believe the level of information provision required in Art. 21 is sufficient. However, this should not undermine the work of the regional initiatives where the level of market information provision may be greater. It should also be periodically reviewed to ensure the market is receiving an efficient amount of information necessary to operate efficiently and effectively.

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

Information transparency is a prerequisite for the efficient and effective operation of any market. It allows parties to more accurately understand the system supply and demand

balance in order to be able to respond to market signals. This creates competition and is likely to lead to more efficient balancing and system operation.

The disadvantages are small especially where information is made available to all market participants on a level playing field. However, there can be market distortions and manipulation where the TSO publishes information that exposes individual shippers' commercial positions. This should be avoided and the less than 3 rule being promoted by ERGEG in their transparency framework Guideline should guarantee this.

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

Any information provision is normally beneficial however it should be subject to a cost-benefit analysis where the implications are great or unknown. We believe TSOs have the information necessary to balance and operate their networks and therefore the cost of releasing this to market participants should not be too expensive.

Balancing periods

Question 17: What are your views on our assessment of the policy options?

We believe ERGEG has undertaken a comprehensive assessment of the balancing period policy options.

Question 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 ERGEG has covered all the options however we believe consideration be given as to whether or not a "Pseudo balancing regime" should be accepted, especially in markets where the costs of implementing a fully physical daily balancing regime is costly, timely and complicated. For example, a few Member States have spent considerable time and money developing sub-daily regimes but it doesn't necessarily mean that these have to be scrapped to be able to introduce a daily balancing regime that complies with the spirit of the target model and the Third package. We welcome ERGEG's thoughts on this alternative route to implementation.

Question 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.

We believe that balancing periods and start time should be harmonised where possible and where it is cost efficient to do so. However, as stated above we do not believe that complete harmonisation through prescriptive and detailed codes is necessary particularly where the costs outweigh the benefits to consumers. We believe a compromise should be considered when deciding whether a regime complies with the essence of the target model. Some discretion by the relevant NRA should be considered and we welcome ERGEG's and the EC's view on this.

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

We believe a day strikes the right balance between the length of time for imbalances to occur and the ability for Shippers to resolve them. We note that the UK had an initial monthly balancing regime called “soft landing” for 6 months when the market opened in 1996 to allow the market to get used to balancing and this may be required for Member States where no balancing market currently exists.

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

We support the target model proposal of a daily balancing regime with imbalances reconciled at the end of the balancing period. However, as stated above, we do not believe that within-day constraints are necessary especially where they are penal for lesser developed markets which might find it difficult to comply with.

Question 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)?

Total costs are unclear; however, in the UK costs are likely to be lower than other Member States as the UK already has a daily balancing regime which is largely compliant with the target model. However, it will be interesting to understand how daylight saving time will be managed across EU Member States.

TSO buying and selling of flexible gas and balancing services

Question 23: Do you agree with our assessment of the policy options?

Yes

Question 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?

Yes, we agree that TSO should balance using a market balancing platform. However we stress the need to promote competition, trading and liquidity in the development of the balancing market.

Question 25: What are the costs of implementing the target model in your Member State?

Total costs are unclear however likely to be minimal as the UK already has a daily balancing regime that is largely compliant with the target model.

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

There are very few interim steps required in the UK.

Question 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?

No, we agree that balancing platforms are not needed where markets are sufficiently competitive and liquid to enable TSO procurement on the wholesale market.

Question 28: Is it appropriate for TSOs to procure balancing services on the wholesale market and/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?

We believe it is important for TSOs to procure balancing services on one market only and this should be the same market that market participants use to balance.

Question 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?

Yes, through the procurement of system reserve for example ahead of time. In the UK this is called Operating Margin and can be procured both from the TSO's assets (LNG storage etc) or from the market through contestable services that are similar (e.g. from storage operators).

Imbalance Charges

Question 30: Do you agree with our assessment of the policy options?

Yes we agree with the assessment of policy options.

Question 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.

Yes. We believe this is an area that should be harmonised where possible. Such arrangements might help align commercial arrangements between Member States and balancing zones. The difference in imbalance costs and methodologies has often been cited for inefficient flows across interconnectors and cross border points that flow against prices. For instance, one balancing zone (A) may have a higher price than another (B) and yet energy flows from (A) to (B). This might be due to the end of day imbalance cost in (B) being higher than in (A).

Question 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 broadly agree with the target model. We support a cost-reflective imbalance charge and believe that an imbalance charge should still exist even if the TSO does not take balancing action. This exists in the UK through the application of default marginal Cashout prices based on the costs of system flexibility and works well to incentivise balancing when the TSO doesn't take an action or takes an action at a price within the default range.

However, there has been much debate recently in the UK on how these default Cashout prices should be set and what costs should be included. We would welcome some guidance of which elements ERGEG believe should be included.

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

The total costs are unknown however are likely to be relatively small depending on the level of change.

Question 34: What are your views on the interim steps in the document?

The interim steps appear to be a sensible and practical route to hit the target model.

Cross-border cooperation

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

The assessment has included a number of logically feasible options.

Question 36: Do you agree with our assessment of the policy options in this section?

Whilst the options mentioned in the document are logically possible they need to be more sensitive to local conditions. Some networks are structurally long others are short in capacity and the benefits of liberalisation for consumers will differ depending on the amount of spare capacity in the network.

It is more a question of what type of risks gas shippers face in each regime and we stress the importance of the codes not being too prescriptive at this stage.

Question 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

EDF Energy agrees that OBAs seem useful for TSO's to resolve constraints at cross border points by taking balancing actions on behalf of other TSO. However it is important to note that TSOs have a distinct position in the market and should not take positions such as a market maker as the consultation suggests. This would require TSOs to be financially trained and registered as traders which may run counter to their TSO role and conflict with Shippers roles.

**EDF Energy
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