

**ALPIQ**

**Response to the ERGEG public consultation on  
Pilot Framework Guidelines on  
capacity allocation**

**Ref: E09-GMN-10-05**

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## **Introduction**

Alpiq is a new leading energy company based in Switzerland and active for our customers in the fields of energy and energy services. We generate and transport electricity and engage in electricity and gas trading and sales.

We are active in 30 European countries. Across Europe, in 26 countries, our energy trading and sales subsidiaries maintain direct contact with our customers. Energy services are delivered by 30 companies at around 200 different locations. Our power generation facilities are spread across Europe, to guarantee optimal security of supply for our customers. We operate power stations in Switzerland, Italy, France, Norway, Hungary, Germany and the Czech Republic. And we are currently building new power stations in Germany, Italy, France, Bulgaria and the Czech Republic.

### ***1. 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?**

We strongly support the Framework Guideline as they are aiming at the right direction and can achieve non-discriminatory and transparent capacity allocation and fulfil the capacity allocation principles set out in the Third Package of Energy legislation.

We further support the harmonization of market designs through EU-wide binding rules instead of a large variety of instruments which national regulators can select.

We welcome the coordination between TSO in offering products and harmonizing processes.

Traders welcome improvements, facilitating trading at cross-border interconnection points. However, there should be an adequate time for the implementation of the proposed measures in the Framework Guideline.

The Framework guideline needs to be clear and detailed on auction rules to avoid adverse market impact and to ensure consistency across Europe.

The target model of 'coupled' gas markets in conjunction with implicit capacity auctions has our particular interest and we will stay actively engaged in further steps towards this model.

We are of the opinion that existing contracts need to be adjusted to new regulatory environment.

In this context and in the overall aim of the ERGEG Guidelines we strongly welcome the German Regulators current procedure (file no.: BK7-10-001) from 9 February 2010 where the BNetzA makes several concrete, market-oriented and practical suggestions on issues such

as capacity allocations and long-term contracts. We urge ERGEG to take these recommendations into account.

**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).**

The measures will reduce transaction costs for our pan-European gas procurement portfolio. In general the availability of capacity and the need to build new capacity will become much more transparent. Through this one will be able to buy and sell gas more easily.

The booking of interruptible capacity, today the last resort of new entrants will be more appropriately incentivised for those who have storage in a market and can accept a probability of interruption. Better defined and harmonised rules on interruptibility will create more reliable products that ultimately will help the network operator to increase firm capacity.

The harmonisation of methods will reduce IT system costs and deployment of country-specific features.

## ***2. Scope of the Arrangements***

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

We support ERGEG's focus on all booking points between EU Member States and between market areas within Member States. We further welcome that the guideline applies to capacity calculated by TSOs but would expect that such mechanisms are as transparent as possible. *Nevertheless* exit points to end consumers and distribution networks, entry points from supply-only / upstream networks, entry points from gas production facilities, entry points from LNG-terminals, entry/exit points to or from storage facilities should also be included, as they are important feature of the value chain which cannot be left out.

## ***3. Existing contracts***

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

Existing contractual arrangements can prevent market entry into domestic downstream markets by competitors from adjacent markets.

By virtue of the principle of legal security, it will be very difficult to justify the modification of existing contracts – those that were negotiated *bona fide* under the former regulatory regime - over a period of 6 months after the entry into force of the Framework Guidelines.

However, as from the entry into force, these guidelines TSO should forcefully ensure that:

- Any new primary capacity be allocated according to the new rules;
- Contracted but unused capacity be surrendered (according to the "Use it or lose it" principle) and tendered in auctions;
- So called "black clauses" (see next question below) are deleted from existing contracts;
- contracts shall be renewed for a reasonable time period (depending on the market competition situation)

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

Yes, following "black-clauses" should be amended and no longer valid:

- Tacit re-conduction clauses (under which contracts are automatically renewed for an equal period of time)
- Clauses implying unclear termination rights
- Clauses forbidding the resale/subleasing of unused capacity

***Experts have discussed if existing/legacy contracts should be amended 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?***

Many capacity booking agreements are made back-to-back with underlying supply agreements. Under this assumption, there are instances a) where capacity is effectively used to fulfill supply obligations and b) other instances where contracted capacity is not used.

a) In the case of contracted and used capacity

A fair compensation mechanism (e.g. Financial Transmission Rights) should be granted for any surrendered capacity, as this will inevitably affect the ability or cost of the capacity holder to meet its supply obligations. However if national and/or European competition authorities properly scrutinize and discipline (through behavioral remedies) long term supply agreements (in case of horizontal or vertical market foreclosure), these situations should become increasingly rare and disappear.

b) In the case of contracted but unused capacity

It is relatively easy to imagine solutions for reallocating the capacity such as release on secondary markets. In any case the capacity release should always be undertaken by a market based auction procedure.

If regulators are serious about prohibiting of any kind of discrimination among market participants, both new market participants and those with interruptible capacity rights should be able to bid on an equal footing for new firm or interruptible capacity.

#### ***4. 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?**

The creation of a fully integrated European Gas Market should ultimately lead to the abandonment of cross-border capacities and to the creation of only a few large zones.

In order to achieve this goal we fully support enhanced cooperation of TSOs as to exchange of relevant data, harmonization of capacity products and both capacity calculation and allocation procedures and the creation of large balancing zones. The cooperation of adjacent TSOs must be accompanied by closer cooperation of the relevant NRAs and the abolishment of inconsistent national regulation. It should lead to cross-border balancing zones where network operators coordinate and apply implicit congestion management methods for the rather unlikely event of bottlenecks. Hence any measure that establishes the need to book cross-border capacities has to be cooperatively examined as to whether physical bottlenecks exist. Only if it has been proved that significant and long-lasting physical bottlenecks exist or if the merging of two zones would lead to a reduced availability of firm capacities at the edges of the zone explicit methods of capacity allocation should be considered.

Furthermore, tariff regulation must set the right incentives for closer cooperation of TSOs.

#### ***5. 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?**

A harmonised European solution is welcome, in particular with regard to standardization of capacity products, data transfer, allocation mechanism, timeline and procedures (i.e. auction design). The network code should also foster the establishment of a European "ISO" who orchestrates the different (physical network operators) and manages cross-border balancing zones. Only with this centralised approach network operators feel comfortable and incentivized to maximise capacity into the zone. Therefore we are of the believe that a binding cross border European network code on issues such as capacity allocation should state the generic conditions to be included in all transportation/access contracts to ensure harmonisation across all EU networks.

**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?**

While we believe that European network operators should apply the Edig@s Standards. We wish to reiterate the importance of standardised communication procedures as they are one of the most important factors to harmonise exchange of information among TSOs and their users. Only this, together with the harmonisation of contracts, methods of congestion management and data transfer will ensure a maximum compatibility of networks and therefore a maximisation of capacities into the system. This applies inter alia to nomination procedures. However, since the implementation of new formats and procedures is always time-consuming and cost-intensive, only a strict standardization would allow for economies of scale. A broader approach and less stringent implementation would potentially lead to a negative cost-benefit-analysis.

**6. Capacity products**

**What are your views of our proposals regarding capacity products?**

We welcome the target to bring more available firm capacity to the market and support new products as part of the solution.

Capacity products offered at cross-border points shall be fungible with common gas trading products on either side of the point to facilitate trading of them.

Interruptible capacity is a crucial instrument that will increase the overall availability of firm capacity. Only interruptible capacity products however that have well defined terms of

- probability of interruption
- maximum duration of interruption
- Max. frequency of interruption

will be of commercial use to network users and can be priced under prudent methods of cost regulation.

Capacities should be booked, nominated, traded and invoiced in energy units. Especially as energy is traded in energy terms, capacity must not be subject to changes of quality - elements that only the network operator can control. As the range of standard products may consist of intraday (RoD)-products and thereby apply to a duration of less than a day, MWh/h should be applied rather than GWh/d.

The reference temperature used in Capacity Booking should be the same as the reference temperature in Nomination Procedures to avoid the misuse of capacities.

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

We agree with the idea of defining a small set of standardised capacity products (see above). The principle that they must not overlap is secondary to the fact that network operators shall sell as much capacity as possible and that they have to manage their overall portfolio. We propose a European-wide adoption of a uniform calendar-day because this eases system issues and billing and it is congruent with electricity products. Especially the latter is important for the increasing convergence of gas and power markets.

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

Alpiq fully supports that network operators offer any capacity that is available up to the last minute of physical exercise. This may be relevant only at very few days of the year. But only a very tight and disciplined obligation to market all capacity available will maximise network use and enhance security of supply. As mentioned, capacity products should be in line with traded products and therefore comprise day ahead and Rest-of-the-Day capacity.

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

We support an EU wide harmonisation of market design through EU-wide binding rules. Any cross-border rule should be identical at least throughout large regions. We therefore propose the implementation of the same mechanisms for all cross-border entry and exit points, which are binding throughout the EU. Therefore we prefer the same set of products at every interconnection point.

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

Generally, interruptible Entry products can be helpful to shippers where demand is flexible (e.g. dual fuel production/ generation) or where the shipper has storage within the zone. Depending on the balancing zone there might be a clear structural need to offer interruptible capacity.

Interruptible capacity must be priced according to its risks and inferiority. As the ultimate goal of the network operator must remain to maximise his income he may want to offer the maximum amount of firm capacity as this will generate more income. This should be achieved by TSOs offering product combinations including interruptible according to the market needs in a consistent method for all points.

## **7. Breakdown and offer of capacity products**

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

Setting aside a share of the available capacity for short term use should in our view be used with extreme caution. In fact with efficient use-it-or-lose-it methods the market should regulate supply and demand especially in the short term. Primary capacity provision based on auctions might apply a principle of staggered products where long-term products are auctioned once a year, quarterly products are auctioned 4 times a year etc. This would allow users to better tune capacity bookings with their actual requirements.

On this topic the Framework Guidelines are too unspecific and introduce additional NRA approval procedures that should be avoided. Furthermore we believe that there are more effective and efficient ways to optimise network utilisation that should also be considered, such as implicit auctions of short term available capacity.

## **8. Cross-border products**

### **Recital 19 of Regulation (EC) 715/2009 states that gas shall be traded independently of its location in the system. Do you think that cross-border products will facilitate the exchange of gas between virtual hubs of adjacent markets?**

Combination of exit capacity from one zone and entry capacity into the adjacent zone to create a hub-to-hub service is supported. And this should lead to a limitation of the possibility to trade natural gas at the border within the European Area.

It will be difficult to implement combined products at the borders of the Community. As import/export contracts generally specify that gas is delivered at the border where the custody transfer facilities are located, a transfer still requires a single "Entry" or "Exit" product. Changes to these contracts, such as moving the delivery point to a hub, may have significant commercial consequences but must not be avoided.

We support an abandonment of the possibility at border points as only combined products enhance implicit auctions and facilitate the maximisation of freely allocatable capacity.

### **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?**

Yes. While bundling would not limit the possibilities to trade, flange trading at border points would unnecessarily reduce liquidity. The UK example may show that trading at the beach is indeed a possibility. But this applies to the production contracts into the NBP system. Equally



we would tolerate flange trading where gas enters the Community or comes from indigenous production.

Limiting flange trading by compulsory booking of combined/bundled products would require the adaptation of all cross-border supply contracts with delivery at a flange. The argument that this would lead to the renegotiation of the entire contract, since the delivery point has always strong implications on the management and distribution of risk between the involved parties can not be sustained in our view. Apart from import contracts with non-EU producers where it may be difficult to enforce those measures, we believe that a renegotiation will not bear additional risks or costs.

TSOs must implement the bundling so that it includes all booking points between two balancing zones/hubs. This means that it will not be necessary to procure entry and exit capacities to a single booking point separately. As set out above, besides the need of enhanced cooperation of TSOs, the offer of bundled products has to be supported by the respective regulators and consistent regulatory frameworks in the states concerned. In cases, where additional investments are necessary for offering bundled products, the question how these investments are reimbursed in the tariff regulation framework also needs to be addressed adequately.

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

Combined products may be an interim step if the bundling is not enforceable. We are concerned that the Guideline does not specify a clear approach but leaves it to the discretion of the NRAs to define terms and conditions of combined products (in comparison to bundled products) and to decide how to handle combined products. We would welcome a consistent and harmonised approach at all interconnection point. If combined products will be implemented as an interim step, they have to bundled Exit capacities at the one side and bundled Entry capacities at the other side of the point as a minimum measure. As lined out, in our view there is no need for combined products but good reasons for bundled products.

**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?**

In general we support the bundling of capacity. The process should however not reduce available capacity, hence each network must be cooperate and maximise capacity available.

## **9. Capacity allocation**

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

We support the idea that TSOs offer capacity on a regular basis for all firm products, and agree that an auction is the preferred mechanism to allocate scarce capacity (existing and future). Also we welcome that ERGEG has addressed the potential allocation by means of implicit auctions. However, attention must be paid when designing auction terms to avoid unintended adverse effects. Lessons should be drawn from the experience with auctions in the UK gas market. We do not believe that auction terms should be specified in the Framework Guidelines, but recommend that ENTSOG designs detailed auction terms in close cooperation with all stakeholders.

In general auctions should be clearly designed. For the allocation of day-ahead capacities or other capacities (free, becoming free by expiring of existing contracts or newly built) with a duration of less than one year, auctions should be implemented. The goal should be to establish coordinated auctions of the TSOs concerned for all capacity durations. Fostering cooperation between adjacent TSOs also requires further cooperation between the involved regulatory authorities. The auction dates should be fixed and the auction deadlines have to be in line with gate closure times of the relevant gas exchanges. TSOs also have to publish in advance which capacity products are available at the respective auction. Lot sizes must be aligned with current market practises.

We propose auctioning with a market clearing price, which means that all shippers of the auction pay the same marginal price which is determined by the highest capacity offer which is successful in the auction. All participants in the auctions have to be treated equally. The reserve price for physical flow should be the cost-based regulated tariff.

The additional revenues from capacity auctions shall exclusively be employed to remove the congestion at the respective IP (or further downstream). All processes need to be harmonised with existing national regulations – or national network tariff regulation needs to be adopted. A prerequisite for a fair price finding in auctions is effective CMP to ensure that unused capacities become available to the market in different time-frames.

The development of the specific mechanism for implicit auctions must be consulted with all market parties.

We would further welcome the use of a single platform for both secondary and primary capacity products to ensure liquidity and cost efficiency.

### **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?**

Yes, we believe that auctions will ensure that firm capacity is allocated to those parties that value it most. Moreover, applying the same auction process consistently across all

interconnection points will ensure network users quickly become familiar with operating the process.

In our sector, namely the supply of gas to power stations, auctions for capacity combined with effective management procedures will enhance liquidity, transparency and competition. Suppliers will be able to adopt integrated long and short run procurement/supply strategies throughout Europe rather than the current piecemeal nationalistic 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?**

We do not support pro rata allocation as an interim step or as any other part of the solution. Pro rata allocation has the disadvantage that in general none of the participating shippers receives capacity according to his needs – thus also resulting in strategic bidding behavior.

***10. 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?**

We fully support the creation of a liquid market for capacity products including primary and secondary capacity. Therefore, we support harmonized capacity products and anonymous procedures. However, the price of secondary capacity should not be linked to the price of primary capacity. Otherwise a seller would not be able to offer his capacity below the price of primary to sell at least parts of it, if demand is low. Sellers should be able to “slice and dice” their capacity into bits according to the needs or that of their customers.

We believe that supply and demand will regulate the type of contracts and hence we do not believe that there is a need to define secondary products in more detail.

TSOs should be required to facilitate secondary trading by recording trade and adjust each network users capacity holdings accordingly, regardless of whether it was conducted on an exchange or not. TSOs should also facilitate assignment of capacity where the obligations associated with that capacity transfer permanently between users.

## **11. 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 welcome initiatives to create joint booking platforms for allocation of primary capacity and trading of secondary capacity. However, this should not restrict shippers to trade secondary capacity without using the booking platform. We do not believe that OTC-transactions should be banned. In the long run, a common auction platform would be highly desirable. Such a common auction platform could be developed from already existing platforms, e.g. in Germany trac-x. We also think that implicit auctions should be considered for short-term allocation at a later stage. In implicit auctions, capacity and commodity is sold together. We would welcome a harmonised treatment of all capacity trading aiming for a common auction platform mechanism.

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

Yes, we agree. However, there should be no restrictions or discrimination for holders of capacities to market them separately in a secondary market. Market participants have to be able to adapt their capacity holdings to changes in their underlying production, purchase, sale and consumption decisions over time.

An active secondary market of capacity rights is therefore essential to realign capacity rights between users over time and to ensure the optimal use of the transmission network. To trade capacity freely in secondary markets, shippers must have the possibility to divide capacity into its constituent parts, to be able to sell an individual season, month, day or even hour taken from e.g. an annual capacity booking. The original shipper shall have the choice either to transfer only the right to use the capacity or - with the consent of the TSO - to transfer the complete contract including all rights and obligations. The whole process must be facilitated by TSOs by ensuring that contractual rights to capacity can be transferred freely between market participants in the secondary market.

It is important that a common platform of the TSOs for secondary trading is established. The target must be to include all the entry and exit points at market area boundaries / national borders and exit points at storage/LNG sites in this platform. In order to enable seamless and efficient operations the operational setting (i.e. processes, tools and contracts for capacity booking, trading and usage) should be standardized, fit for purpose and very efficient.

In our opinion the joint allocation of primary and secondary capacity products can foster this process.