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Dear Mrs. Fay Geitona

EREG - European Regulators' Group for  
Electricity and Gas

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### **EDISON'S COMMENTS ON ERGEG CALL FOR EVIDENCE "CEER VISION PAPER FOR A CONCEPTUAL MODEL FOR THE EUROPEAN GAS MARKET"**

#### WHO WE ARE

Born in 1881, Edison is one of Europe's oldest energy companies. In 2009, it reported sales revenues of 8,867 mln €, and is carrying out an ambitious investment plan in the electricity and gas sectors. Edison had to diversify its business, when the national monopoly on electricity was established in Italy in 1963. Thanks to the first wave of EU Directives in 1996, it could re-focus its business on energy once again, this becoming the largest new entrant on the Italian market.

With 50,3 TWh produced in 2009, it is now Italy's second largest electricity generator. Thanks to 7,000 MW of new highly efficient and low emission plants (CCGT thermo plants, as well as hydro and wind power plants), the Company has now a total installed capacity of 12,500 MW. In the hydrocarbons business, Edison has an integrated presence in the natural gas chain, from production to importation, distribution and selling, with sales of 13.2 billion cubic meters in 2009.

In 2009 the new LNG terminal in Rovigo started to contribute to the diversification of Italy's supply sources with its regasification capacity of 8 bcm of natural gas a year, equal to 10% of Italy's demand for natural gas. The start up of Galsi and ITGI pipelines will further connect Italy to Algeria and Caspian Sea, two areas rich in hydrocarbons.



## GENERAL COMMENTS

Edison welcomes the opportunity to respond to the CEER Call for Evidence on a conceptual model for the European Gas Market and recognizes the importance of developing a target model providing an overall guidance for the process that will lead to the creation of an internal gas market in Europe. The current lack of integration between different national markets, as well as the low level of cooperation among system operators, as correctly highlighted by ERGEG during recent the Workshop held in Wien, is in fact an obstacle preventing market operators and final customers to fully benefits from the positive outcomes of the liberalisation process.

The 3<sup>rd</sup> Package already includes important measures that will foster the integration of markets: we refer in particular to the introduction of Framework Guidelines (FGs) and Network Codes (NCs) that will surely contribute to pave the way to the European internal market. Nonetheless, the process of drafting and approval of FGs and NCs has highlighted the risk of inconsistent outcomes, given that interacting issues will be treated in separate documents. The market model will therefore provide a positive contribution insofar as it will set a general framework and coherent criteria to be used to draft and assess the FGs and NCs, in order to ensure a high level of consistency among the regulation of different areas.

## COMMENTS TO THE QUESTIONS

*1. What are in your view the main goals to be aimed at by the gas target model beneath the high-level policy goals set out by the 3rd Package?*

Edison believes that the main goals of the target model should be aligned with the three pillars defining the EU Energy Policy: the model should indeed allow final customers and market operators to benefit from the positive outcomes of the process of liberalization and of the increasing level of competitiveness on the market, still securing supplies and achieving sustainable development. In particular, the target model should contribute to the process of harmonisation and integration of markets as well as pave the way to a more efficient functioning of the internal gas market. As we highlighted in the general comments, the achievement of these high level objectives will be possible if the model will provide a clear and consistent guidance for the development of the FGs and NCs.



Furthermore, the target model should be designed in such a way that takes into consideration the future challenges that will characterise European gas markets and in particular, the need for a more flexible gas system provided the increasing use of gas as back-up fuel for power generation, as a consequence of the growing penetration of intermittent RES in this sector.

*2. What are in your view the major developments and anticipated changes in the European gas market (on national and international level) and where would a target model bring added value? Including:*

- a. the role of long term capacity contracts in the future European gas markets;*
- b. the role of hubs / gas exchanges.*

The major developments that will be faced by the European gas market can be summarised as follows:

- European indigenous production will decrease and import from non-EU countries will consequently increase;
- import from non-EU countries will be more diversified provided the growing market share for LNG and the role that will be possibly played by unconventional sources;
- gas will be essential to design a strategy aimed at reducing CO<sub>2</sub> emissions, being the most flexible and economic fuel to back up intermittent power generation from RES;
- liquidity and transparency on gas hubs/exchanges are progressively increasing, paving the way to a more competitive environment.

In such a scenario, we believe that a role for long term contracts should be preserved to ensure an adequate level of security of supply: long term contracts represent the certainty of a reasonable return for operators investing in capital intensive infrastructures and, in our opinion, they will keep playing an important function by creating a framework that secures the necessary level of commitment to invest in new capacity.

The target model should therefore represent a solution that is able to strike the right balance between the necessity to create the right incentives to new investments and the need to further develop gas exchanges.



*3. What are in your view the key elements of a conceptual model for the European gas market to contribute to non-discrimination, effective competition, and the efficient functioning of the internal gas market? Please include views on the key aspects of market design such as, capacity allocation and congestion management procedures, network tariff arrangements, wholesale market pricing, balancing arrangements and, gas quality specifications? Please consider the interaction of these arrangements.*

As concerns the key aspects of the market design, we would like to recall some of the main aspects that we already highlighted in our responses to consultations on CAM, CMP and balancing.

#### **CAPACITY ALLOCATION**

Ensuring an efficient allocation of transmission capacity is a key point for the development of competitive gas markets. On the other hand, we also believe that when defining the rules regulating the allocation of capacity, security of supply should remain one of the main concerns, to be reflected by the possibility to book long term capacity and to get exemptions in case of investments in new infrastructures. These measures can surely contribute to create a stimulating framework for operators to invest in such capital intensive projects.

As concerns the bundling (hub-to-hub) of capacity, we would like to express our support to the introduction of bundled products as optional, keeping for market operators the possibility to trade also other products. In particular, we oppose any obligation to re-allocate capacity that has already been allocated with existing contracts. Edison indeed believes that one of the basic points of the target model should be the respect of existing contracts, which should be considered as fully defined property rights as they are.

#### **CONGESTION MANAGEMENT**

The introduction of more effective congestion management procedures will surely contribute to optimise the use of existing transmission capacity. Edison is in favour of measures that allow solving commercial congestions on IPs via a market-based approach, which should always be preferred to any solution restricting the possibility of users to take advantage of the rights they have purchased. For this reason, we strongly support any measure aimed at incentivising TSOs to maximise available capacity and developing liquid and well-functioning secondary markets.



As concerns the management of congestions on storage and LNG infrastructures, we think that the differences with gas transportation should be duly considered. In particular, with reference to the possible application of UIOLI, Edison would like to express its concern in relation to the following issues:

- being storage the main balancing tool, shippers should be able to use their capacity with a high degree of flexibility,
- the existence of PSOs and seasonal constraints will make the definition of “underuse” and the reasons behind it very complicated.

### **BALANCING**

Edison supports ERGEG recent proposal to introduce a market-based balancing mechanism, which should have the following characteristics:

- Daily balancing. No within-day restrictions should be introduced if the system is capable to deliver enough flexibility. Should within-day restrictions prove to be necessary in some systems, they shall not be imposed in a discriminatory manner only on certain categories of users.
- Frequent within-day re-nomination windows, even close to the end of the gas day, coupled with the possibility for shippers to be consequently active on the gas market, therefore fully using the flexibility resources available within the system.
- Maximum interaction between gas and power markets (in terms of nomination and re-nomination windows, etc), therefore allowing users to maximise the existing synergies
- The introduction of tolerances (at least as an interim step) could be crucial to cope with the scarcity of flexibility, which could be worsen by the low liquidity of wholesale gas markets. In any case, tolerances should be set equitably across all network off-takes.
- Provided that the provision of information to network users is essential for a market-based balancing mechanism to work efficiently, Edison recommends the introduction of high quality service standards with which TSOs, as well as DSOs, should comply. Having access to timely and reliable data on the system and on their portfolios, network users will have all the tools to carry out an accurate forecast, making balancing against pre-defined off-take profiles unnecessary



*4. What level of detail, e.g. level of harmonisation, do you expect from the CEER vision paper on a conceptual model for the European gas market? For example:*

- a. Do we need a definition of an EU-wide gas day? If yes, what should this definition be?*
- b. How deep should the "reach" of the EU gas market model be, i.e. should it encompass DSOs? Is there a trade-off between vertical depth (i.e. including all levels of national gas markets) and horizontal depth (i.e. integrating balancing zones cross border)?*

As non-binding and conceptual model, the CEER vision paper should provide a general guidance, whereas detailing at an operational level should be a task of FGs and NCs. In general, we believe that the target model should not be designed as a "one fit all" approach, but on the contrary it should provide a set of tools and measures among which each National Regulator could choose the most suitable solution to be implemented in its own national system. Though harmonisation should eventually be the final outcome of the whole process, it should be achieved with respect of the main peculiarities and of the different stages of development of national systems. For instance, we support the introduction of interim steps, such as the presence of tolerances for systems where flexibility is scarce and that are evolving towards a market-based balancing mechanism.

With reference to the specific questions:

- a) As we already stated in our responses to previous consultations, the adoption of an EU-wide gas day and a common time zone reference is crucial for the integration of different markets. Their definition should follow a consultation with all stakeholders. In particular, the possible alignment of the gas day with the electricity day (0-24) should be object of an impact assessment to identify deriving costs and benefits.
- b) We believe that there are some areas where the role played by DSOs is crucial for the efficient functioning of the system and should therefore be addressed by the model. This is particularly true with relation to balancing, where the commitment of DSOs to provide timely and reliable data on customers' off-takes is paramount to allow network users to efficiently manage their portfolios.

*5. Which areas or aspects of the gas market should be affected by the target model and what are the constraints for such a model?*

*6. Which areas or aspects of the gas market should be excluded from the target model description and left to national/regional decision making?*



In our opinion, consistently with the main goal that we identified for the target model (i.e. providing high-level guidance for the process of drafting FGs and NCs), we think that it should deal with the main issues identified by the 3<sup>rd</sup> Package to be regulated by NCs, leaving the room for market-driven forces to shape the development of the remaining aspects of the market. National regulators should be left the responsibility to implement the most crucial elements, which could need to be adapted to each national system's characteristics, such as for instance the existence of factors that require for the definition of transitional periods before the implementation of the target model.

*7. What are the options for integrating the currently fragmented European markets? Are there any existing models you would like to recommend? In case your answer is yes, we would be interested to learn about the features of this model and if there are also any drawbacks in this model in your view.*

*a. Should we merge balancing zones to create cross border or regional balancing zones or market areas? How many balancing zones does Europe need and how big should they be?*

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

As concerns market coupling, we believe that the implementation of this model in gas markets and the possibility to accomplish the successful and efficient results achieved in electricity should be further explored, taking into due consideration the peculiarities that make gas markets different from electricity. Notwithstanding, we do not have currently enough elements to assess ERGEG's proposal and we reserve the possibility to elaborate further comments on the occasion of next consultation.

Whatever the target model will be, we recommend any implementation be anticipated by an impact assessment, evaluating the costs and the benefits of the measures that will be introduced. The realization of pilot project within the framework of the Gas Regional Initiatives could also represent a valuable solution to test the efficiency of the proposed mechanism.