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**ENTSOG response to CEER's Call for Evidence on a
"Vision for a conceptual model for the European gas market"**

Dear Fay

Thank-you for the opportunity afforded to ENTSOG to present its initial views about the above paper at the 3 December workshop. The attachment with this letter provides some elaboration (beyond this cover letter) upon the ideas ENTSOG presented in Vienna and some initial ideas on the structure of the conceptual model for the European gas market framework.

The development of a vision for a conceptual model for the European gas market ("Target Model") could give useful support to the upcoming work associated with the development of framework guidelines, network codes and subsequent comitology proposals, implementation of the recent Security of Supply regulation and to the formulation of proposals to progress the recent Infrastructure Package. The Target Model should therefore guide the many separate activities and ensure coherence and progress towards the single European gas market. An inclusive process will therefore be essential to deliver a clear, concise and widely acceptable Target Model given that the resulting proposal has no legal force.

The transmission infrastructure and the associated access rules will be the foundation upon which the European gas market will be built. The assets and access rules must therefore be aligned with both market and political aspirations whilst at the same time the framework must respect the underlying physical and economic reality of gas transmission –including financing of the necessary investments-, the gas supply chain & Europe's gas importation dependence and general desire to improve diversity of source of supplies.

Collectively the TSOs (via ENTSOG) must play a major role to inform the Target Model formulation; the experiences of financing, building and operating the network and developing the commercial access frameworks defines a unique perspective that will be essential to develop a robust Target Model and then to progress to its implementation. A substantial ENTSOG/TSO effort will also be essential to enable implementation. Thus ENTSOG's early involvement in the formulation of a Target Model will ensure robust outcomes.

ENTSOG has therefore convened a task force to develop ENTSOG's input to the Target Model process. ENTSOG notes that the next workshop to be held in Bonn on 22 February will consider a range of alternative models and that these are expected to be based upon preparatory work that has been undertaken between regulators, the Florence School of Regulation and wider stakeholders.

By definition choosing between alternative models will necessarily go beyond establishing objectives for the European gas market; it will imply that policy choices will be made and that a suitable impact assessment will be necessary. The complex interactions inherent both within the European gas regimes and in its interaction with the electricity regime demand a holistic evaluation. For example a market coupling approach has been promoted in electricity. However this approach needs careful consideration for gas in the context of different realities of the gas and electricity environment .

Transparency about suggested models at this early stage of development would be helpful to assist the ENTSOG deliberations to inform ENTSOG's contribution to the Bonn workshop and its interactions with regulators, their consultants, wider stakeholders as well as the anticipated subsequent workshops.

ENTSOG notes that the Madrid Forum XVIII asked ERGEG to co-ordinate the development of the target model during 2010. Given that ACER becomes operational in March this year and that the Target Model should inform a substantial proportion of ACER's work (most notably its role in framework guideline and network code process but also wider activity including cross-border dispute resolution) ENTSOG suggests that the Target Model development is passed to ACER at its foundation and is subject to the ACER governance process before a proposal is sent to the Commission.

ERGEG (subsequently ACER post 3 March 2011) and Commission should liaise regularly during the development to ensure coherence of Target Model and other initiatives, including policy options for the Commission's implementation of the Infrastructure Package. Given the criticality of the transmission infrastructure and access arrangements ENTSOG should be invited to provide its opinion to this group.

Careful consideration also needs to be given to the views of Member States so that the key features of the Target Model are capable of implementation to a sufficiently consistent basis across Europe to deliver the benefits of the single European gas market.

ENTSOG looks forward to receiving material defining the potential models for consideration at the Bonn workshop and to early interaction with regulators to ensure that ENTSOG can provide high quality inputs to inform the development of the Target Model.

A handwritten signature in blue ink, appearing to read 'Vittorio Musazzi'.

Vittorio Musazzi
General Manager, ENTSOG

cc: Inge Bernaerts, Head Unit Electricity & Gas, DG Energy, European Commission

Attachment

ENTSOG response to CEER's Target Model Consultation

Early work on the pilot Capacity Allocation Methodology (CAM) and Balancing framework guidelines, Congestion Management Principles (CMP) Comitology proposals, the development of the Security of Supply regulation and the Commission's communication on the Infrastructure Package have indicated the inter-relationship and inter-dependence of all of these areas. The aspiration to develop a Target Model (TM) for the European gas regime is not new but the many parallel developments during the second half of 2010 have indicated the usefulness to develop a TM to inform all these works and future developments and to ensure coherence and coordination between all the initiatives.

The Madrid Forum XVIII agreed that a European Gas Target Model should be developed and invited "the Commission and the regulators to explore, in close cooperation with system operators and other stakeholders, the interaction and interdependence of all relevant areas for network codes and to initiate a process establishing a gas market target model."

ENTSOG expected to be involved already in the early phases of consideration of the TM. Now, with some preparatory work done, ENTSOG welcomes that the development will become more open and has committed resources to the initiative by convening a dedicated task force to support the TM development process.

The transmission infrastructure and the associated access rules will be the foundation upon which the new European gas market will be built. The assets and access rules must therefore be aligned with both market and political aspirations whilst at the same time respecting the underlying physical and economic reality of gas transmission – including financing of the investments-, the gas supply chain & Europe's gas importation dependence and the diversity of source of supplies

Collectively the TSOs must play a major role to inform the TM formulation; the experiences of financing, building and operating the network and developing the commercial access frameworks provides a unique perspective that will be essential to develop a robust Target Model and then to progress to its implementation for which TSOs will be majorly responsible.

- Goals of the Target Model

The Target Model should define the high level design for the single European gas market to ensure a specification of the interaction and inter-dependence of the constituent elements of the regime. This is essential to inform the development of the individual framework guidelines and network codes. It must provide clear objectives, ensure coherence and avoid inconsistencies

and inefficiencies between framework guidelines and network codes as well as facilitating the definition of the scope of each code development.

The role of the TM however will extend far wider than the framework guidelines and network codes. For example the Commission will be working to develop policy proposals to implement many aspects of the Infrastructure Package and the TM development provides an opportunity to provide some coherence and consistency across the multiple ongoing initiatives that impact European Gas market Developments.

- The nature of the Target Model

The concept of the “target model” does not exist in the Third Package or in other legislative instrument.

The TM therefore must “sit above” other initiatives but cannot be legally binding. To deliver benefits it therefore has to deliver a framework broadly acceptable to the generality of actors, particularly those who will be later involved in making lower level policy choices about implementation. Thus fully inclusive processes will be necessary in the development. The challenge should not be underestimated and ENTSOG believes that substantial interaction with a wide range of actors (particularly including ENTSOG) will be essential and in the preparatory work probably beyond the current planned level of several public workshops.

Given that ACER becomes operational in March this year and that the TM should inform a substantial proportion of ACER’s work (most notably its role in framework guideline and network code process but also wider activity including cross-border dispute resolution) ENTSOG suggests that the TM development is passed to ACER at its foundation and is subject to the normal ACER adoption process before a proposal is sent to the Commission. Some form of Commission adoption might be desirable as well.

The TM should then be considered to define the context within which the other framework guidelines and network codes can be developed, and particularly the Commission’s setting of priorities within the 3 Year Plan development process. Additionally the TM should also inform other Commission initiatives including, for example, implementation proposals for the Infrastructure Package.

- Timeline for developing the Target Model

It is essential that the Target Model development is conducted in a manner that minimises potential disruption to other framework guideline / network code developments and other initiatives (e.g. Infrastructure Package policy development) that are already progressing. Whilst the process needs to be mindful of what has been done it is essential to expect that some revisions to proposals already under development might be necessary. Some consequential knock-on effects to framework guideline and network code activity already undertaken may therefore result, hence timely TM delivery will be necessary.

ENTSOG believes that Quarter 1 2011 might afford a reasonable period for high level scoping of the Target Model project. Then a six month timeline (comparable to the Third Package framework guideline process) could be used to develop the final Target Model possibly for ratification at Madrid late in 2011.

It is essential that the Commission and ERGEG (subsequently after establishment ACER) liaise closely to ensure overall coherence of TM and wider interactions. Given TSOs' essential role to provide and operate the infrastructure as well as facilitating gas markets it is vital that ENTSOG has the opportunity to give its view and to have a "seat at the table". Perhaps the Commission's Planning and Monitoring Group could achieve this by providing timely support, early identification of any potential impacts on work in progress and a project planning and coordination role.

- The structure of the conceptual model for the European Gas Market Framework

The gas transmission framework can be considered to cover three major areas. The first is the existing transmission infrastructure which defines the backbone of the regime. Given the enhanced infrastructure requirements new infrastructure investments will be needed. The second is the market rules that define how system users gain access and use the network. The third is technical rules and standards (including gas quality) as well as operational rules that define the detailed interactions and communications necessary to support system operation/interoperability.

The TM must provide sufficient guidance to ensure coherence of the entire framework and to enable the more detailed aspects of the European gas market framework to be completed via framework guidelines, network codes and Comitology proposals together with other legislative instruments where appropriate.

- Infrastructure and Investment

Market requirements, the Security of Supply regulation and the Commission's Energy Infrastructure communication all indicate a requirement for network investment in an increasingly challenging business environment. Gas will have an additional role; often as back-up fuel to intermittent electricity generation. Load factors might be expected to reduce with the value of network capacity being determined by shorter term option values.

It is not clear that current risk distributions (between specific system users requiring capacity, and both today and future wider users and TSOs) inherent within today's investment framework will deliver the infrastructure required to satisfy the political aspirations.

The approach to market-based investment and its interaction with centrally planned or assisted developments should be addressed as a priority. The TM must at least provide clear principles that could inform other activities including the funding and cost recovery of asset infrastructure investment.

- Market rules to encourage trading markets and hubs

Commercial framework should be supportive of trading and the movement of gas across Europe to be determined by market signals provided by wholesale gas prices. Provided that capacity is not physically constrained, differences in gas prices should reflect a fair cost-based value for the transportation service between two locations. Commercial rules should enable easy access to the system, enabling system users to optimise their gas flows within Europe in a better functioning internal gas market. The Target Model should not prescribe a specific approach to the size of balancing zones; efficient non-discriminatory, transparent and either market-based or cost reflective access arrangements will enable efficient gas market operation without a requirement to pre-determine capacity and balancing zone sizes.

- Technical and operational rules

Technical and operational rules (including gas quality, business rules, units, IT) must enable the proper functioning of the market. Information and data exchange between actors will require the development of agreed standards and protocols.

Whilst these will be essential to complete the implementation of the market design these are matters that the detail of which will not be explicit in the TM definition but which should be addressed in subsequent activities and, where appropriate, in the development of the network codes which should take account of existing common practices.

- Content of the Target Model

The Commission's Third package guidelines and codes paper¹ provides an analytical framework that could be helpful to define the scope of the TM. However the TM does not need to define the detail of all codes but rather to provide a high level description of the model to ensure that the interactions and interdependence between codes and other areas (e.g. the improvement of the infrastructure investment regime) are understood and that the TM is consistent with the delivery of the single European gas market.

- Level of detail in the Target Model

It may not be possible to prescribe the level of detail necessary in the TM at this stage. The early work should therefore be considered as a scoping phase to better inform an assessment.

The Target Model needs to meet the goals of providing a blueprint, avoiding inconsistencies, ensuring coherence and facilitating a sufficiently tight definition of scope for each separate initiative that will define the European gas market and particularly the framework guideline / network code development.

¹ Discussion Paper – Third Package guidelines and codes D92008)/C2/MS/MvS/FE 18 September 2009

- Read across from other models

Experience from other environments, particularly European electricity regimes, may be relevant to inform gas TM but the appropriateness of the read across needs careful consideration taking into account fundamental differences in physics, market environment, network access arrangements, supply/demand (particularly scale of cross-border energy flows) positions. For example a holistic assessment of the market coupling concept needs to consider implications for both longer and shorter term capacity procurement as well as balancing rules. A robust impact assessment will be essential to inform both the policy choices implied by the TM and to provide a sound basis for subsequent work.