POWEO

Pilot Framework Guideline on capacity allocation

An ERGEG Public Consultation Paper

POWEO's Contribution
26 February 2010

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?

POWEO strongly supports the development of a Network Code (NC). The Framework Guidelines (FG) as currently drafted have identified all the major issues, though some of them would need further details at the FG stage. These are for instance:

- Existing Contracts: the scope of "existing contracts" needs to be defined more precisely.
- Capacity Allocation: there are numerous options when designing OSP or Auctions. The FG should provide some sort of design guidelines.

NC based on these guidelines would be a key step towards the harmonization and integration of the European Gas Market, but shall not be the end game as the NC will need to be regularly discussed for improvement, based on experience and feedback from all stakeholders.

- 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).

- Existing contracts: as stated above, we cannot assess the impact on existing contracts until we get a better understanding on what the ERGEG suggests on this matter. We would like to point out that this would affect not only capacity contracts, but also gas supply contracts on which the price depends on capacity costs.
- Capacity products: we welcome the definition of a limited number of capacity products. As already answered in the recent GTE+ consultation, as long as there are at least Daily, Monthly, and 12-monthly products (either Oct-Sept or April-March), we do not foresee any major negative impact on the gas market.
- Cross-border products, combined or bundled products: these measures would be a major improvement for capacity bookings, and would enable shippers to manage their booking requirements in a much more efficient way.
- Capacity Allocation Mechanisms: streamlining mechanisms would also be a major improvement for capacity bookings, and would enable to have clear, non-discriminatory and transparent processes
- Remarketing of booked capacities: whenever auctions are used as an allocation mechanism, we believe that TSOs should offer a service of resale of booked capacities, following the example set by CASC-CWE on electricity[1]

[1] See section VIII article 8.02
http://www.casc-cwe.eu/media/pdf/CWE%20Auction%20rules_V_1_1.pdf

Scope of the Arrangements

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

POWEO supports the scope of the framework guidelines. For the avoidance of doubt, "interconnection points (IPs) between adjacent entry-exit systems within the same Member State" should include all such IPs, whether they link 2 TSOs or not. For instance, the North-South link on GRTgaz network should be included.

- 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?

There are three types of existing contracts.

1. Historical (legacy) contracts that were concluded prior to the liberalisation of the market.
2. Long-term contracts concluded in the context of Open Seasons to finance and build new capacity.
3. Other existing contracts, such as multi-year contracts that were concluded recently, after the liberalisation of the market.

The main challenge that existing contracts - and particularly historical ones – create, is contractual congestion, even when there is no physical congestion. Many IPs in Europe fall into that category, and that is purely due to the fact that incumbents, who used to hold most of (if not all) available capacity do not optimise, or resell it, on the secondary market (or on the gas market through market spreads).

- 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?

POWEO believes that such clauses should be amended for all types of existing contracts.

- 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?

POWEO supports this proposal. As a matter of fact, the recent GDF SUEZ commitments constitute a step forward to free up historical capacity and prevent contractual congestion.

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?

POWEO supports the scope of this proposal.

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?

It would be valuable to define standardised General Terms and Conditions for transportation contracts. These already exist among some TSOs (for example, the TSOs on NetConnect Germany), and could progressively be extended to adjacent TSOs, with the target objective to have a unique set of such GT&Cs.

- 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?

A standardized communication procedure and technology (e.g. based on EDIG@S) between TSOs and shippers would streamline and facilitate pan-European operational aspects.

Capacity products

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

POWEO supports the scope of this proposal.

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

POWEO strongly supports this proposal. It is critical for the integration of the European gas market. As stated above, Daily, Monthly and 12-monthly products (either Oct-Sept or April-March) should be sufficient for shippers to structure their portfolio. We do not believe that multi-year products are required, except through Open Seasons for the development of new capacities in order to finance the investments. For existing capacities, we believe that Multi-year products bring limited value, and may even in some cases block the market and create barriers to entry. We are therefore not in favour of such products. That being said, should the majority of shippers express a need for this type of product, we would insist for the percentage of total capacity offered under this product to be very limited, and certainly much lower than 80%, which is a level currently used by some TSOs.

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

Day-ahead capacity is critical, however we do not believe that within-day is required: UIOLI mechanisms and/or liquid within-day gas market can ensure that capacity utilisation is maximised.

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

First of all, POWEO strongly supports bundle products. This would solve the issue of having separate products on each side of an IP. Then, having the exact same products offered at every IP across Europe is not critical at this stage and might be difficult to implement across Europe all at once, but it could be done progressively, IP by IP. Overall, this should be aimed for as a target model, and as such should be included in the NC.

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

On any given product, Interruptible capacity should only be offered once all firm capacities (on that product) have been sold.

Taking this question a step further, once a shipper holds interruptible capacity on a given product (eg. Annual), and should there be firm capacity becoming available on a shorter lead time (eg. Monthly), then the shipper should have the option, but not the obligation, to convert its interruptible capacity into firm capacity for that given product (Monthly).

Breakdown and offer of capacity products

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

First of all, "short term capacity" needs to be clearly defined, as it might have different meaning for each shipper. Does it include Day-Ahead, Monthly, Yearly products? In our answer, we consider that it includes all products of one month or less. (Note: this is consistent with our answer to the GTE+ survey conducted in December 2009).
POWEO is in favour of setting aside a minimum amount of capacity for short term products. Such capacity enables shippers to seize market opportunities and adapt their short-term portfolio to their needs.

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?

In the target model, the European gas market should be a set of hubs linked through capacity. Therefore cross-border products (to be more precise, any IP between two adjacent systems) would clearly facilitate trading between adjacent hubs.

- 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?

Trade at the border is a heritage from the past that should and will disappear once bundled products are offered. POWEO strongly supports full bundling, not only of cross-border capacity but for all IPs between two adjacent systems (eg. IP between GRTgaz and TIGF is not cross-border, but should still be bundled).
This argument goes not just for boosting virtual hubs liquidity, it is also to concentrate the number of points where gas can be exchanged and ensure better integration of the market. Besides, without bundled products, secondary markets for capacity have little chance of developing.

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

POWEO believes bundled products cannot be easily implemented at once, therefore combined products are perfectly acceptable during a transition phase.

- 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?

Yes, this would help to concentrate liquidity by reducing the number of IPs for which capacity products are available and would avoid sub-optimisation of capacity use.

Capacity allocation

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

POWEO believes that auctions are the most appropriate allocation mechanism for all capacity products. This mechanism is non discriminatory, it provides a market signal for the valuation of the capacity, and is aligned with best practices of the electricity markets.

It is worth noting however that auctions would only be efficient where combined or bundled products are offered.

In addition, POWEO only supports products of duration of one year or less for existing capacities. Should it be decided to keep multi-year products, we would point out that auctions for these products might be delicate as the success of auctions depends strongly on the liquidity of the underlying gas market. As it is limited to the near curve for the time being, using auctions for multi-year products might not lead to valid economic signals, at least until the gas market develops down the forward curve. OSP might therefore be more appropriate for multi-year products at this stage.

- 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?

As this mechanism would lead to revenues different from the regulated revenues (either higher or lower):

- Any additional revenues generated from auctions, beyond the regulated revenues, should be used for the development and de-bottlenecking of the network.
- Any loss of income, below the regulated revenues, should be socialised and recovered by the TSO through overall tariffs reviews.

In certain markets where most capacity is booked through historical contracts, the introduction of auctions on certain products where limited capacity is available might lead to price distortion. It is therefore important to ensure that (i) sufficient capacity, as a percentage of overall capacity, is available for allocation through auctions, and (ii) that no single market player has leverage on the auctioned capacity.

Detailed design of auctions should be studied at the national (or cross-border) level, under a set of pre-defined recommendations from the ERGEG.

On a sidenote, shippers active on GRTgaz network are currently reviewing allocation methods for the North-South link, where auctions and OSP are studied (as part of the “Concertation Gaz, Capacity Allocation” workshop). The conclusion of this analysis should be available in May 2010, and might be a useful concrete example to understand implications and design parameters of auctions.

- 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 recognize that some shippers may not be comfortable with auctions. If that were the case, and the majority of shippers were not in favour of auctions, OSP could be acceptable, as an interim step only. (Or for multi-year products, please see above)

Based on our experience with the North-South link on GRTgaz, where OSP (with pro-rata) is used, many shippers bid 100% of available capacity to ensure maximizing their allocation, but running the risk of being over-allocated. In turn, over-allocation leads to under-utilization of capacity, as most shippers do not optimize their capacities on the short-term markets, either through the secondary market or through the gas market. Our suggestion on the design consists in increasing the number of rounds, each of the round allocating smaller size blocks of capacity. Doing so would avoid potential over-allocation, and would allow shippers to fine tune their requirements as the OSP rounds take place sequentially. Also, for efficiency reasons, it would make sense to hold the entire OSP allocation over just one day instead of running it over weeks.

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?

Absolutely, primary market should be designed in a way that secondary market can be integrated automatically. POWEO strongly believes that the market model set by the electricity market for the North West region (CASC-CWE) should be used as a model for the gas market. Under that model, secondary capacity is offered via resale of capacity. Please refer to the above question “General” for further details.

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?

Yes. Again, please see CASC-CWE. Such a platform would be useful for efficiency, transparency and automation.

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

Yes. Again, please see CASC-CWE.