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European Regulators' Group for Electricity and Gas  
Council of European Energy Regulators  
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Send via E-Mail  
E-Mail Copy to: DG Tren, Mr. Joachim Gewehr.

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**Capacity Management - ERGEG Public Consultation:  
Pilot Framework Guidelines on capacity allocation.**

Dear Mrs. Geitona, dear Mr. Gewehr,

Shell appreciates the opportunity to respond to the ERGEG Consultation Paper on Pilot Framework Guidelines on Capacity Allocation (CAM; reference E09-GNM-10-05) and the Recommendations for Congestion Management (CMP, reference E09-GNM-10-07).

The following comments are offered on behalf of Shell Energy Europe Limited, London, and affiliated companies in the Royal Dutch/Shell Group ('Shell'), who collectively trade as 'Shell Energy Europe' and who comprise the European gas, power and CO2 marketing and trading businesses of Shell.

Shell Energy Europe markets gas and power to industrial, utility, distribution and commercial customers through 14 offices across Europe. Along with its affiliates and joint venture partners, Shell Energy Europe is active in 19 countries, serving 8,000 customers along the value chain.

In the European upstream business, Shell has been a leading producer of gas for decades with production in the UK, the Netherlands, Norway, Denmark, Germany and Italy.

Before going into details, we would like to make some general remarks about the work done so far on CAM and CMP.

- We welcome the concept of a target model for gas market in Europe. Although we do not fully agree with the model itself (see comments below), the prescriptive approach is much more appropriate than former 'toolbox approach'. We see a clear case for stringent rules and principles for CAM and CMP with only minor competencies for National Regulatory Authorities (NRAs) to interpret and apply.
- We regret that intentions of ERGEG are not always clearly stated. Several key matters are described very vague:
  - Existing contracts: ERGEG's view on necessary amendments is not given. Neither is a definition of term 'legacy contracts' in the questionnaire (this is the case for both the CAM and the CMP proposals). The issue has been addressed at the Brussels Workshop on February 2<sup>nd</sup> quite clearly

- and we welcomed the statement from the regulators that existing capacity bookings will remain untouched. Nevertheless, such a clear statement is not part of the official proposals published by ERGEG.
- Bundling of products: Does the ERGEG proposal promote obligations for bundling of capacity products – or is it an additional option, and trading at flange/Interconnection Point (IP) remains possible in medium/long term future? Is it the intention to eliminate intra-European traded points, which are not a ‘virtual hub’ as mentioned in the ‘target model’ description?
- Limitation of re-nomination rights (CMP document): There is no indication as to which level of ‘limitations’ could occur. To make things even more vague, the decision if and how to limit might be different from NRA to NRA.
- Further implementation process:
  - CAM will be brought forward as a pilot for the new framework guideline process. We have concerns that appropriate involvement of grid capacity customers is not guaranteed in one of the most critical phases of the whole process, i.e. the development of the Grid Codes by ENTSO-G. We therefore propose that either (i) ENTSO-G is explicitly requested to assure appropriate stakeholder (capacity users) involvement in the grid code development process, or (ii) the development of framework guidelines in more detail by ERGEG and consultation with stakeholders before handover to ENTSO-G takes place.
  - Implementation of the CMP principles: The comitology process is a powerful tool to achieve harmonized rules in a relative short period of time. Therefore, this procedure should be used once consensus about key issues has been achieved. This is not the case at the moment, thus a more inclusive approach should be taken.
  - We would have preferred CAM and CMP to have been brought forward in a joint, “non-comitology” process.
- The following comments relate more specifically to the CAM questionnaire:

## 1. SCOPE OF THE ARRANGEMENTS

### F1 General Rules

*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?*

There are two main issues, which we would like to share:

- Existing contracts. We are concerned about consequences for existing contracts (see comments above). In general, we would expect an appropriate commercial and operational migration path to the new CAM framework.  
The new rules should focus on future needs and assure that the gas flows into the European market are not disturbed and arrangements for long term supply contracts are not jeopardized.  
The CAM framework guideline is a “pilot project”, i.e. a test for the new Grid Code development process. In such a test environment we would have preferred a proposal with less potential impacts for existing commercial positions and security of supply. The pilot project should focus on the processes to (i) increase firm capacity offers (e.g. overbooking) and (ii) allocation of the new capacity offers, instead of opening up existing contracts (contract durations, restrictions for title transfer, etc.).
- There is a need for new investment in European gas infrastructure. We would have appreciated a more supportive approach for new investments and the willingness to accept price signals as a

potential indication for physical congestions. In our view it should have been clearly stated that auction revenues above regulated tariffs should be (partly) used to invest in projects removing the respective physical congestions.

*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 key issues from our perspective are:

- Interference with existing capacity bookings at IP and between market areas (e.g. termination of existing contracts, change in contractual rights, CMP: limitation of re-nomination rights). These measures would significantly affect existing commercial positions.
- Security of Supply: In most markets, capacity bookings are aligned with the sales as well as the purchase contracts. If respective capacity contracts are opened up, this backing of long-term gas supply contracts with suppliers from outside the EU (and even within) could become much more difficult or even impossible. Fulfilment of contractual obligations could not be guaranteed (e.g. minimum take). As a consequence, suppliers may be unwilling to provide longer term gas sales arrangements within the EU, undermining market stability, and the willingness of producers to export to EU countries might erode.

On the other hand, improvements in some key areas would significantly push forward the internal market, which we would be very supportive of in order to facilitate the development of a genuine, well-functioning, open and efficient market in gas: For example improving cooperation of grid operators, facilitating secondary capacity trading, as well as standardizing contracts, conditions and communication processes.

## **F1.1 Scope of the Arrangements**

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

In general yes – with one exception: Entry points from (domestic – intra-European) upstream facilities should be added to the list of grid points which would not be subject to the guidelines. With overall declining domestic production and non-existing congestions at these points, it is neither efficient nor does it support the development of a well-functioning and open market if these points are included. Even worse, gas producers might be reluctant to invest in new production capacity if the long-term route to market would be at risk.

## **1. ADAPTION OF EXISTING CAPACITY CONTRACTS**

### **F1.2 Existing contracts**

*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?*

See general remarks above.

*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?*

See above. ERGEG's communication about necessary amendments is not very clear – sometimes even contradicting. Of course, some changes may be needed in order to develop the market in an orderly fashion, but in general this must be a managed process and for the sake of a stable economic and

commercial environment to encourage investment and competition, there should be a common understanding that market participants can rely on existing contracts in order to fulfil existing obligations.

*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?*

See above.

### **3. TSO COOPERATION**

#### **F1.3 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?*

We are very supportive of improved inter-TSO cooperation and the measures proposed. We would promote an even more demanding obligation for cooperation of grid operators in order to facilitate the development of a genuine, well-functioning, open and efficient market in gas.

Irrespective of the wording, this guideline (F1.3) is one of the reasons why we believe that involvement of grid users/stakeholders is crucial when it comes to grid code development. The likelihood for appropriate grid codes addressing the needs of capacity users is much higher if ENTSO-G is challenged by stakeholders.

### **4 CONTRACTS, CODES AND COMMUNICATION PROCEDURES**

#### **F1.4 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?*

Yes, if done with a clear focus to improve trading and improve efficiency of processes.

Care should be taken that measures do not constrain trading opportunities needed for a functioning market. In order to optimize supply and demand with natural gas, the market participants need a variety of capacity products. We therefore propose:

- Not to reduce range of product offers just for the sake of “harmonizing” contracts.
- Not to enforce bundled products at interconnection points.

*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?*

Yes. An internal market with harmonized communication procedures will seriously improve efficiency (IT systems etc). Care should be taken that appropriate transition periods for implementation and adaptations is granted. Depending on complexity of changes, the plan for implementation should provide for a transition period of at least one year between specification by authorities and mandatory application should be foreseen.

### **5 + 6 CAPACITY PRODUCTS (FIRM / INTERRUPTIBLE)**

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

From our perspective, the market is mainly interested in firm capacity offers with a focus on medium- to long term duration (month, year, multiple years). Short term offers are necessary (e.g. for balancing), but shouldn't be the main focus and driver for changes.

The products offered should be standardized and cover the following durations: hourly/rest of the day (only if necessary for balancing), Day, Month, Year and multi-year contracts up to 15 years. All of the products should be available as firm and interruptible offers (exemption: intra-day firm only).

With regard to the firmness of the product offers, we would appreciate if NRAs would promote a very stringent, unambiguous position encompassing the following principles:

- Access to firm capacity is the markets key interest.
- Holders of firm capacity should not be exposed to interruption risks. Firm capacity has to be firm. ‘Shame concepts’ (e.g. statistical firm capacity) which have been introduced by some TSOs are not acceptable.
- Interruptible Capacity should be offered as an optimisation tool only in cases firm capacity is sold out. Therefore, we support the principles described in F.2.2.
- Transparency: Customers must have the chance to evaluate their risk of being interrupted (on a daily basis). Once they have been interrupted, an easy and fast assessment of reasons must be possible.
- Tariffs for interruptible capacity shall be sufficiently below charges for corresponding firm capacity’ (as quoted in CMP paper). We would suggest to be even more concrete: The spread should be such that there is no incentive for TSOs anymore to maximize offer of interruptible capacity at the cost of firm capacity offers. At least in some European countries, such a measure could trigger additional firm ca capacity offers by TSOs.

*Do you agree with the idea of defining a small set of standardised capacity products that do not overlap?*  
Yes, if the ‘small’ set covers the products described above.

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

This depends very much on the further development of the balancing regimes. The decision should be taken according to balancing requirements.

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

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

No. If firm capacity is available, interruptible shouldn’t be offered. In general, gas deliveries have to rely on real physical capacity to move the molecules from the source to the end-consumer. In most cases, interruptible capacity is just a contractual workaround to get access to physical capacity which is then used to supply customers.

In order to fulfil market needs, the TSOs should focus on measures to maximise firm capacity offers; incentives which could contradict this objective should be eliminated.

## **7 BREKADOWN AND OFFER OF CAPACITY PRODUCTS**

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

Based on our experience, we doubt the effectiveness of such a measure. Especially if the held back capacity is primarily reserved for day-ahead (or even shorter) products.

Nevertheless, if regulatory authorities expect advantages for dedicated interconnection points, we would propose to further test this measures with a low limit for capacity held back. Preferably at IPs where new, additional capacity becomes available (via physical de-bottlenecking or measures described in the CAM proposal). If appropriately implemented, such a process would not negatively interfere with existing contracts.

In addition, NRAs would have the opportunity for further analyses of the concept, which is - in our view - still too vague to assess in detail, e.g. issues like cost coverage for 'capacity which is set aside', or interference with open season processes and other investment initiatives.

## **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?*

Yes, but see comments below.

*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?*

No (see also reply to 4: Contracts, codes and communication procedures). In order to optimize supply and demand of natural gas, the market participants need a variety of firm capacity products.

We would therefore prefer an improved co-operation of TSOs and introduction of standardized products such that entry and exit bookings could be easily matched if demanded by the grid users (as proposed in CAM, section F2.4.1 Combined Products).

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

No. We support the introduction of combined products – nevertheless do not agree that they just should be an interim solution. They should remain even as the market develops, such that delivery at interconnection points remains possible.

*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 – but care should be taken that total amount of firm capacity at new IP will not be reduced below amount of offer before integration took place. In addition, delivery at the new IP should be possible in future, too.

## **9 PRIMARY CAPACITY ALLOCATION**

### **F3 Capacity allocation**

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

We are assuming that the auction mechanism will be designed in a way that prices are reflecting/are allowed to reflect scarcity of capacity. If this is guaranteed, auctions should be the standard mechanism.

We do not agree with the proposal that 'auction revenues exceeding the regulated tariffs shall be used for different aims in accordance with national provisions ...'. Instead it should be clearly stated, that these kind of revenues should be (partly) used to invest in projects removing the respective congestions.

*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?*

This would require significant effort to adapt, develop and introduce IT systems. The main mitigation action would be to provide for an appropriate transition period.

*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?*

No, the system should be directly transferred to auctions. We do not support additional interim steps as we believe they add to the implementation effort. Instead, prolongation of the transition period from current allocation system to auctions should be considered by the relevant regulators.

## **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 under-lying primary capacity market?*

We support the harmonization of products and procedures with the exemption of the interference into the price mechanisms (e.g. capping as described in the Impact Assessment).

If a market-based approach is to be implemented, the NRAs shouldn't immediately try to limit or eliminate key market mechanisms, i.e. reaction of price to market signals.

## **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?*

Yes.

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

Yes, if combined OTC commodity/capacity trades will not be affected.

I trust you have found these comments useful.

Yours sincerely,



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