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**Committee on the Implementation of Common Rules
on the Transport, Distribution, Supply and Storage of Natural Gas
DG ENER**
Rue De Mot 24-26
B-1049 Bruxelles
BELGIUM

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EU Network Code on Capacity Allocation Mechanisms in Gas Transmission Systems

Dear EU Gas Committee Member,

The European Federation of Energy Traders (EFET)¹ welcomes the latest version of the Capacity Allocation Mechanisms Network Code (CAM NC) drafted by the European Network of Transmission System Operators for Gas (ENTSOG) and reviewed by the Agency for the Cooperation of Energy Regulators (ACER) and the European Commission. To ensure an informed Comitology discussion in the first half of 2013, we would like to bring to your attention several important remaining concerns. The issues in the paragraphs below are accompanied by specific suggestions for revising the text of the Code available in the mark-up document attached with this letter.

Our key concerns and suggestions are as follows:

- **Quotas for new capacity** to be held back for the short term should not be included in CAM, but should be part of a wider discussion on market mechanisms for new / incremental capacity, work on which is already underway. It does not make sense to make decisions in one network code that would unduly constrain the development of other rules that are still under discussion.
- **Quotas for existing capacity:** 20% of the capacity should be held back for the annual monthly auctions, as this will ensure that more capacity is available for new entrants and short-term trading than suggested in the current draft proposal.
- **Capacity products** need to be more flexible to enable shippers to tailor their capacity bookings according to their needs. For this reason, we propose enabling shippers to

¹ The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org.

book capacity in quarterly strips up to two years ahead, instead of one year ahead as suggested in the current draft, and to book monthly strips up to a year ahead.

- **Bundling of capacity.** We support bundling of capacity, but we are concerned about regulations requiring Transmission System Operators (TSOs) to sell only bundled products, without being able to sell unbundled capacity where there is not yet full consistency of capacity products and contractual terms on either side of an interconnection point. This would lead to the unnecessary destruction of capacity offered to the market as TSOs would sell capacity based on the lowest common denominator of capacity available on one side of the interconnection point. This is inconsistent with requirements that TSOs offer for sale the maximum quantity of capacity (Article 6).

Quotas for new capacity

One of our main concerns is the decision to incorporate new technical capacity (incremental capacity) into the scope of Article 8 (6), which means that capacity quotas (reserving capacity for short-term auctions) will also apply to all new capacity. Whilst we agree that for centrally planned capacity it might be logical to have the same capacity quotas as in CAM for existing capacity, we do not support capacity quotas in cases where the size of the capacity enhancement has been determined by commitments from market participants. TSOs should be required to make available the capacity demanded by all market participants where it is economic and efficient to do so; building less would not fulfill market needs, whilst building more would risk stranded assets and additional costs for consumers.

If TSOs are obligated to offer new capacity to the market whenever bids for capacity in the long-term auctions exceed the available capacity, then market participants have an opportunity to bid and obtain incremental / new capacity every year. This negates the concerns of ACER and the Commission that markets will be foreclosed as a result of all new capacity being booked in one auction. We have consistently argued for this approach of regular opportunities for market participants to bid for new capacity and we are currently working with the Council of European Energy Regulators (CEER) on market mechanisms for investment in incremental capacity. It is premature, in our view, to set constraints for how market mechanism for new capacity should work via requirements in CAM without sufficient discussion. We note that proposals for reservations applying to new capacity were not made by ACER until the second half of 2012, and have not been subject to full industry discussion or analysis in the context of market mechanisms for new capacity.

To reiterate, it is our belief that for incremental capacity market-based mechanisms are a superior tool on which to base investment decisions, as they reveal the true level of market demand rather than relying solely on forecasts by central planners. Therefore, as indicated in our mark-up document, **we suggest amending Article 2 (3) to incorporate Articles 8 (6) as part of the provisions applicable only to existing, *not* to new technical capacity.**

Capacity quotas for existing capacity

Our second concern relates to the capacity allocation methodology (Articles 8 (6) and 8 (7)). We have continuously argued that at least 20% of the existing capacity should be reserved for short-term allocation to provide greater flexibility for network users, not least for new entrants, to profile capacity. While we are pleased to see that this issue has partially been taken into consideration in the latest draft of the Network Code, in our view **reserving 10% for the annual yearly and 10% for the annual quarterly auctions cannot ensure that an adequate amount of capacity is actually left for *short-term allocation*, i.e. year-ahead, month-ahead, day-ahead and within-day auctions.**

With this concern in mind, we suggest redrafting the Code to **ensure that at least 20% of the existing capacity is reserved for the *annual monthly auctions*** (see our mark-up of Article 8 (6) and 8 (7)), with any unsold capacity from these auctions being offered via the rolling monthly and daily auctions.

The idea of capacity auctions for annual monthly products was developed by ENTSOG in an earlier draft of the Code from 21st June 2011. We suggest re-introducing this idea by **inserting a new Article 13 covering a slightly revised version of the section on annual monthly capacity auctions developed by ENTSOG in 2011**. The benefit of annual monthly auctions is the greater flexibility it gives market participants to shape their capacity bookings according to their capacity needs, compared to annual quarterly auctions. For example, it would enable shippers to book more capacity for January, a winter month, than for March where winter is ending. With a quarterly product a market participant would have to book a flat quantity for January, February and March.

Capacity Products

If the above change to the auctions is implemented, then the capacity available for annual yearly and annual quarterly auctions would be part of the quota (not more than 80% of the existing technical capacity) reserved for medium and long-term allocation. In this case, 20% of capacity would be available for shippers to buy on a year-ahead basis. To ensure greater flexibility for network users to profile capacity, two additional changes would benefit the functioning of the market. As suggested in our mark-up of Article 11, **yearly capacity products should be available for booking from three to fifteen years ahead, while quarterly capacity products, as presented in our mark-up of Article 12, should be available for booking up to two years ahead**. As with the introduction of annual monthly auctions, this approach gives participants greater flexibility to profile their capacity bookings closer to the time of use of the capacity.

Following from the above, the new CAM Network Code would enable participants to book capacity as follows:

- Between Years +3 and +15 into the future, a flat annual product (i.e. the right to flow gas at the rate of x GWhd for one year). Auctions to be held once a year.

- For Years +1 and +2 into the future, a flat quarterly product (i.e. the right to flow gas at the rate of x GWhd for one quarter). Auctions to be held once a year.
- For Year +1 a flat monthly product (i.e. the right to flow gas at the rate of x GWhd for one month). Auctions to be held once a year.
- For the Month +1 (i.e. the following month), a flat monthly product (i.e. the right to flow gas at the rate of x GWhd for one month). Auctions to be held once every month.

Bundling of capacity

We support the objective of joint sale of fully consistent capacity products from one TSO system to the next, but are **concerned that inconsistent capacity products might be ‘bundled’ together, leaving in place the underlying contractual problems and restrictions on trade.** In particular, we are concerned that bundling may lead to sterilisation of capacity. This is because the capacity at any Interconnection Point (IP) is dependent on the gas flows and system configuration upstream and downstream of that IP. This makes it entirely possible that there may be, for example, greater exit capacity at an IP from the upstream system, than there is entry capacity into the downstream system. Where bundling takes place between two separately operated TSO systems it will have to be on the basis of the lesser capacity. However, this precludes the possibility of potential optimisation by traders matching different entry and exit capacities on either side of the flange. For instance, a trader may take the view that he could match firm capacity on the exit side with interruptible capacity on the entry side because he considers the risk of interruption to be small. Alternatively, he may do so if he believes that firm capacity may become available as a result of Use-It-or-Lose-It measures or overselling and buyback, as foreseen in the Congestion Management Procedures.

Therefore, in our view, the most prudent approach to bundled products would be to strengthen **the obligations on TSOs to provide consistent capacity products before they are bundled together** (see our mark-up of Article 19 – new Article 20 (2) in our draft). Moreover, until bundled capacity is offered through a single Capacity Contract, network users shall be able to unbundle the capacity associated with the two Capacity Contracts of the transmission system operators concerned (new Article 20 (6) in our draft). It is worth noting that bundling of capacity will not reduce the number of contractual relations that participants will have, as, although there might be a single capacity product between two systems, a shipper will still have to have separate contracts with each TSO, unless the TSOs form a joint venture or become one company.

Capacity calculation and maximisation

Lastly, in relation to capacity calculation and maximisation, as suggested in our mark-up of Article 6, we strongly encourage the incorporation of provisions requiring the publication of capacity calculation methodologies, as well as greater exchange of information among TSOs. In our view, it is essential that the methodologies are approved by National Regulatory Authorities (NRAs) in consultation with stakeholders and that TSOs have incentives to maximise the

available technical capacity. Regulators should also monitor and audit the way in which TSOs calculate their available capacity.

My colleagues and Member Company representatives remain at your disposal should you have any questions or if you would like to discuss our suggestions at any time during the comitology process. We believe our suggestions will enhance the proposed Network Code and lead to the faster creation of a true internal gas market for Europe.

Yours sincerely



Dr Colin Lyle

Chairman of the EFET Gas Committee

CC:

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