

## **DGEC proposal of an *Ordonnance* on the reform of the storage obligation**



EFET comments – 20 November 2015

The European Federation of Energy Traders (EFET)<sup>1</sup> welcomes the opportunity offered to market participants to comment on the draft legislation reforming third party access to underground gas storage capacity in France.

However, we regret the very short timeline provided for submitting comments on the draft legislation, as well as the absence of the accompanying regulatory documentation (including in English), preventing us from forming an educated opinion on the overall framework to be introduced.

We welcome DGEC's decision to introduce the "auction + compensation" mechanism which EFET supported in its answer to the public consultation rolled out in April 2015<sup>2</sup>. EFET is committed to the creation of an attractive and competitive European gas market. To complete the construction of this market, it is necessary to establish coherent and market-based rules in all Member States as soon as possible. The current state of the French rules for access to underground storage significantly differs from European standards and is fully based on obligations rather than a market mechanism. The proposed mechanism, if well designed, can deliver the results EFET is seeking. However, EFET believes that the current draft stands mid-way between the implementation of a workable market-based mechanism and the current system based on a storage obligation. This situation will undoubtedly lead to a less efficient outcome. As a consequence, EFET would recommend the Ministry to review the draft to propose a robust market-based mechanism delivering the highest level of efficient storage capacity reservation.

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<sup>1</sup> The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent, sustainable and liquid wholesale markets, unhindered by national borders or other undue obstacles. We currently represent more than 100 energy trading companies, active in over 28 European countries. For more information, visit our website at [www.efet.org](http://www.efet.org).

<sup>2</sup> EFET response to the DGEC consultation on third party access to underground storage of natural gas and storage obligations submitted on 17 April 2015, available at: [http://www.efet.org/Cms\\_Data/Contents/EFET/Folders/Documents/EnergyMarkets/ElectPosPapers/NatRegLevel/~contents/FW823JBMU9X9T36V/EFET\\_DGEC-consultation-storage\\_17042015.pdf](http://www.efet.org/Cms_Data/Contents/EFET/Folders/Documents/EnergyMarkets/ElectPosPapers/NatRegLevel/~contents/FW823JBMU9X9T36V/EFET_DGEC-consultation-storage_17042015.pdf).

### **1. On the determination of the need for storage capacity in the PPE**

Whilst EFET agrees the PPE seems to be the appropriate vehicle to give a forward view on the need for storage capacity in France, there seems to be some inconsistencies between the theoretical perimeter of the storage capacity currently in operation and the scope considered as the cost base of the storage operator. This needs to be clarified.

Moreover, EFET questions the proposal to include all existing storage facilities into the perimeter of regulated assets until the end of the second PPE period (i.e. 2023) without a thorough cost-benefit analysis. We believe a transparent process aimed at identifying the amount of storage capacity needed to underpin security of supply should take place well in advance of 2023.

### **2. The definition of a minimum annual stock necessary to ensure peak demand**

Whilst EFET does not reject the rationale for this proposal, the legislative treatment as currently foreseen in the draft *Ordonnance* seems insufficient.

Firstly, the “minimum stock” should be the result of a risk assessment for which the methodology and parameters are transparent and subject to a public consultation. It seems that the risk assessment foreseen in the EU regulation on security of supply could be appropriate for this analysis.

Secondly, the *Ordonnance* should include a deadline for the publication of this “minimum stock” given that this value will have implications on the commercial strategies implemented by shippers to book storage capacity. To this end, we propose to publish this “minimum stock” at the latest on 31 December each year.

Thirdly, this “minimum stock” must be accompanied by a reference date at which this volume must be achieved. In our opinion, this date should not be before 1 November, the notional start of the withdrawal season.

### **3. The marketing of underground storage capacity through auctions**

EFET welcomes the introduction of auctions as the only allocation process for storage capacity in France. This will bring the commercialisation rules in France in line with European best practice. However, a number of principles must be kept in mind when developing the legislative framework surrounding the parameters of these auctions.

EFET stresses the importance of setting the reserve price at a level sufficient to incentivise shippers to participate in the auction and use storage capacity on the basis of its extrinsic and intrinsic value. We believe such a principle should be at the foundations of the new regulatory framework for storage and enshrined in the *Ordonnance*.

If the reserve price for storage products is in the money, any shippers with an interest in storage for the supply of a customer portfolio or for pure trading activities will enter in the auctions and bid up to the value they are willing to pay for such storage products. For simplicity reasons, we suggest setting the reserve price at 0€/MWh or at the marginal cost of running the storage facility in order to maximise storage capacity sales in most foreseeable cases.

Alternatively, the storage auctions reserve price should be based on live market prices. A coherent reserve price could either be determined very close to the day of the auction to make sure the reserve price is commercially attractive at the time of the auction or be based on quoted market price prevailing on future specified dates. The provision envisaged in the *Ordonnance* seems to set these reserve prices long before the auctions actually take place which could result in auctions failing to meet market participant's expectations and storage capacity remaining unsold, if not designed carefully.

As a consequence, EFET recommends amending recital II of Article 5 to account for this fundamental need to have reserve prices in line with live market prices. In particular, CRE should not submit prices for decision by the Minister but simply come up with a formula which, when applied, will give the reserve price applicable in each auction based on prevailing market prices. In terms of auction mechanism, EFET believes that the most fundamental point is to ensure that storage sales are maximised and a fair price is determined for the considered storage product. Ascending price auctions, already used for cross-border capacity, is one possible way of meeting this criterion.

It is also worth noting that transmission tariffs applied at storage entry and exit points will also affect the extent to which shippers consider storage to be a commercially attractive.

#### **4. Regulation of revenues for storage operators and introduction of a compensation mechanism**

EFET welcomes the reference to the "efficient operator" as the key concept for regulating French storage operators.

However, EFET underlines the need to introduce financial incentives in this regulation framework. Financial incentives have effectively improved the quality of service provided by TSOs and DSOs. We expect similar outcomes for storage operators. On the contrary, the absence of financial incentives usually leads to slower efficiency improvements, if any.

With regard to the compensation, EFET believes that some principles must be kept in mind:

- **The compensation should only apply to domestic exit points** and not to cross-border entry and exit points. French gas consumers benefit from the security of supply standards and should bear the costs. An increase in cross-border costs would disincentivise shippers to ship gas to France;
- If integrated into the transmission exit tariffs to regional exit zones, the compensation should be subject to a specific regulatory treatment strictly separated from the normal transmission tariffs;
- The calculation of the compensation should be completely transparent and based on the characteristics of the customers benefitting from the security of supply standards.

## **5. Last resort obligation in case of insufficient reservations during auctions**

**EFET does not support the creation of a last resort obligation.** In a well-designed mechanism, all available and necessary capacity for shippers to ensure security of supply criteria shall be booked and no last resort mechanism shall be needed.

As highlighted at point 3, the auction reserve price should be determined with the objective of attracting as many market participants as possible in the auction process. In case an auction does not lead to the desired level of reservation, another auction should be launched with a lower reserve price in order to meet market expectations.

In case a last resort obligation is deemed necessary, the decision to trigger it should be made later than 1 March as envisaged in the *Ordonnance* so as to leave time for remarketing unbooked capacity. EFET believes that 1 May is an appropriate deadline for such a mechanism.

Finally, EFET questions whether a penalty price of 130% of the reserve price of the considered storage product is justified in the case of suppliers with storage booking deficits. Some shippers may already have an abundance of flexibility within their portfolios and booking late storage capacity involves increased costs to meet technical requirements as well as lower optimisation potential, thus already negatively impacting non-compliant shippers.