

Responses to Draft CAM Network Code Consultation

Consultation Response Sheet

Please complete the fields below and send via email using the subject, "Response to the CAM NC consultation" to info@entsog.eu by 3 August 2011.

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Question 1: Do you consider that the level of detail in the draft NC is appropriate for an EU Regulation?

Response:

There is a balance between providing detail which runs the risk of being quickly outdated and providing some general objectives which may not be useful for the national TSO's. EDF Energy believes some flexibility for TSOs is needed to develop their own policies taking account of local conditions in the context of enhancing European trade. In this respect we welcome the insertion in paragraph 1.5 that existing codes with more detailed provisions can be maintained as long as they are consistent with the general principles of the Network Code. In this regard it may be useful to have a set of "relevant criteria" which these codes have to comply with, such as improved competition, value for consumers, environmental benefits etc. This exists in the UK Uniform Network Codes regime and helps focus attention at the comitology implementation stage. We note the references to the relevant sections of the Directives where such criteria is maintained, however it might be useful to spell out these objectives in each Code as a reminder of their purpose.

Finally, we believe the implementation of this code should be reviewed after perhaps one year to identify areas of improvement. As this is the first European Code to be implemented through comitology there will be significant learning opportunities to be had.

For the code we need

1. Clearly defined objectives
2. Carefully specified requirements for contracting parties
3. Enough detail to ensure we are able to comply with the code

Applying this perspective to the code we find the following

Part of code (Section)	User Requirement
1.3 Transparency	We believe the NC could make reference to other European legislation which might impact and interact with this Code. For example we know there is a body of European law on price discrimination which the code will have to be consistent with and may be helpful to include a reference to.
1.5	We welcome the inclusion of this paragraph to clarify exactly to what extent Member States will have to comply. We agree that the Member States codes should be able to introduce or maintain more detailed provisions than those set out herein provided that such measures are consistent with the general principles set out in this Network Code. This will avoid any unnecessary complexity and duplication from re-writing already compliant codes. This will also remove the risk of bringing more advanced and liberalised markets backwards which would not be in the consumer's interest.

2 Application	This seems appropriate.
3 Principles of Cooperation	It would be useful to emphasise the objective of cooperation and focus on how disputes could be reconciled if they arose. The status of the Handbook is important as the detail will be crucial in determining the effectiveness of cooperation. Users will need a commitment for transparency in this process as it underpins the markets operation.
4 Allocation of Capacity	This might be an area where a change in the code could be necessary if the 10% figure in 8 (b) or 4.6 (7. B) is found to be too little or too much. It is here where an efficiency objective could be more useful than a precise figure.
5 Cross Border capacity	We would like more detail on how a number (three or more) of IP's will coordinate firm capacity if they form a known transit route for example.
6 Interruptible	More detail would be useful on what basis the TSO's will pro rata capacity if it is anything other than simply dividing the capacity by the number of shippers with the same contractual timestamp
7 Tariffs	More detail is required on how the revenue shortfall and collection will work in practice. We need assurance that "timely" means timely for all participants not just TSOs as it could be interpreted to be. Market participants need stability and predictability in tariffs and constantly changing tariffs would not be in the consumer's interest. The Code should not envisage tariffs changing by more than twice a year. It is much preferable to have one transparent set of tariffs ahead of the year in question.
8 Booking Platforms	Whilst we share the ambition to minimise the number of capacity booking platforms ultimately leading to one single EU platform, it should also be noted that the objective is to facilitate capacity booking and trading. This could mean that there are several booking platforms but all similarly designed to make it easier for users to understand. This may be simpler , more effective and realistic than to assume one platform covering potentially hundreds of IPs across Europe.
9 Exceeding required decisions	More detail would be useful on how the views of the stakeholders will be taken into account during the consultation period (9.1).
10 Adaptation implementation and interim period	A clause that allows for slippage may be useful if there are technical reasons why the code could not be implemented. For example if there was a delay in implementing the auction systems.

Question 2: Should this NC set out detailed rules? If so, do you consider that where changes are necessary, they should be made through the change process foreseen in the Third Package, or (if legally possible) through a separate procedure where modifications can be made following stakeholder request and discussion?

Response:

The UK system has licence conditions that are generally broad in their application and codes that are highly detailed. Code changes are highly flexible through a modification process involving industry participants and the regulator in contrast to licences that set out the general obligations of industry participants operating in a market. We have found that the principles have remained broadly consistent over the last ten years but some detail has been revised through the industry codes processes.

EDF Energy sees that there is a trade off between detail and broad objectives and that a market requires both to be present in a regulatory regime for it to work effectively. We strongly favour a revision process for the more detailed requirements as we have experienced major changes in the UK's gas industry necessitating reform of the detail. Furthermore, this process facilitates innovation in both trading and the use of physical assets. It is also the case that comitology is the correct procedure for changing the general principles of market liberalisation which are by definition likely to remain static for long periods of time. Future impact on industry resource needs to be taken into account also in striking the balance between detailed rules which may have to be change as opposed to loosely defined rules which have to be complied with in spirit. Detailed rules should only be employed where necessary such as technical parameters necessary for safe and efficient system operation.

Question 3: In your view, is it credible that principles and details of CAM mechanisms could be separately identified? What elements of this (or other) code(s) might be considered for a "lighter" change process and how might such changes be made binding?

Response:

Yes, we believe it is credible to separate principle from detail in the code in a similar way that primary legislation informs licence conditions and network codes in the UK.

Question 4: How do you consider that a process to review the handbook, and to modify it where necessary, should be designed?

Response:

As the UK experience shows the scope to innovate by modification has real value as identified by Ofgem in their impact assessments of successfully implemented modifications. If the change process is to be effective it should mirror the codes developed by Member States such as UK or Ireland.

Question 5: Do you agree with the NC proposal for long term auctions of quarterly products? If not, please explain your proposed alternative and the rationale for this.

Response:

Quarterly products are likely to meet some shipper's needs and so should be included as capacity products. However, we recognise that longer duration products of one year or more may be attractive to certain parties with longer-term requirements and this could be allowed through linking of quarters.

Question 6: Do you consider that the auction design set out in the draft NC includes sufficient measures to allow system users to purchase the long-term capacity they want? If not, how could the measures be improved, while remaining consistent with the FG and keeping the complexity of the auction design to a manageable level?

Response:

The auction design could consider products longer than a year so long as a robust mechanism to surrender unused capacity is in place (UIOSI). We recognise that the auction mechanism in the draft NC is largely based on the UK Long-term auction design that is certainly a tried and tested mechanism. However, we wouldn't say it was the only way and encourage new alternative methodologies to be put forward which might offer improvements.

Furthermore, there needs to be a mechanism to signal and offer incremental capacity and this was raised at the auction workshop held on the 20th July. The NW Code is not clear how incremental signals, where demand exceeds supply at an IP, will be dealt with other than allocation scaling. Furthermore this might create an incentive for Users to bid for more capacity than needed. To counter this effect it would be useful if these signals could be turned into potential TSO investment where it is clear more physical capacity is needed.

More transparency around how the bid step prices will be calculated is also needed. This will help Users understand whether or not to bid for extra capacity and for new investments to be made in different parts of the EU network where costs may differ.

Question 7: Do you consider that the within-day auction proposal set out in the draft NC could be improved from a user perspective? If so, what improvements would you suggest?

Response:

We are broadly content. Information provision across a number of borders will of course be critical if gas is to be shipped across Europe which goes back to the objective of developing a single traded capacity platform if this is feasible.

Question 8: The draft NC proposes that TSOs will implement all auction systems at all Interconnection Points (IPs). However, if no purchases of capacity are made in within-day or day ahead auctions at a particular IP over a certain period of time, do you consider that it would be appropriate to suspend these auctions for some time, in order to reduce operational costs?

Response:

No, we believe that auctions should always be kept open as there is no guarantee that physical flows on the day will be to the level bid in the capacity auction. This will mean the potential for extra capacity to be released to the market is maximised – a priority for an efficient and effective market. We expect to see an efficient implementation process but wonder what the real savings will be as the costs of running a platform are likely to be fixed with zero marginal cost in the very short term. If this intuitive expectation is incorrect then we would expect to see a suspension.

Question 9: Do you consider that the auction algorithms set out in the draft NC are appropriate for the Standard Capacity Products to which they are proposed to apply? If not, what modifications would you suggest?

Response:

Auctions are economically efficient mechanisms for price discovery if and only if the products are something that is actually valued by the bidders. For this reason we do not think that the result of the same auction design but with different capacity products will yield the same revenue for the TSO or allocate the same capacity for Shippers. Furthermore, the assessment of the package is linked to the facilitation of cross border trade. An auction which can successfully allocate capacity across a number of borders will have to offer the right products in the first place. The auction may facilitate the efficient price discovery across a single border but this will have to be set against an imagined optimisation of gas (and not capacity) across multiple borders. It could be that a shipper who wants to move gas over three or more borders but only secures capacity in two auctions process will not have delivered anything useful to them and yet the differences in the value of the gas is where the benefit is accrued not the transmission capacity.

If we take this approach, we might find a large number of potential products that could be offered if destination is the key criteria. We note in figure 1 that there are at least 27 potential time and distance based products which are required for shipping gas across four member states. This could mean that it might not be feasible to offer the number of products which shippers might value and therefore alter the efficiency of the market.

Figure 1: Time and Distance Based Capacity Products

Product (Time): As we have now between individual hubs	Product (Distance): Not available at present but clearly of value to shippers
WD	Hub a to b Hub a to b to c Hub a to b to c to d
DA	Hub a to b

		Hub a to b to c Hub a to b to c to d
	MA	Hub a to b Hub a to b to c Hub a to b to c to d
	1 QTR	Hub a to b Hub a to b to c Hub a to b to c to d
	2 QTR	Hub a to b Hub a to b to c Hub a to b to c to d
	3 QTR	Hub a to b Hub a to b to c Hub a to b to c to d
	4 QTR	Hub a to b Hub a to b to c Hub a to b to c to d
	Annual	Hub a to b Hub a to b to c Hub a to b to c to d
	1 year plus	Hub a to b Hub a to b to c Hub a to b to c to d

Question 10: Do you believe that any of the potential alternatives described would be more suitable? In particular, do you consider that a Pay-As-Bid methodology would be more appropriate than uniform price, particularly for auctions of shorter duration products?

Response:

EDF Energy does not support pay-as-bid methodology in these auctions and broadly supports the described methodology. However, there should be a mechanism to allow the auction to close early after a defined period of stability is witnessed, if there has been no movement in bids or any impact on prices for an amount of time for example. This will avoid a one day auction lasting 10 business days and will also minimise any potential anti-competitive behaviour from developing.

Question 11: Under an open-bid algorithm (whether uniform price or pay as bid), do you consider that ten bids per user is a sufficient number?

Response:

The number of rounds determines the number of opportunities a shipper has to signal to the market the value it attaches to an auctioned capacity product. In practice it is likely to mean a number of quarters were closed out early and others continued to be open seemingly indefinitely if there was congestion. This being the case the auction was not effectively determining the value of constrained capacity.

In this type of design the numbers of opportunities to signal prices affects the efficiency of the design. We suggest in cases where-

- The capacity is in a congested area it might be worthwhile increasing the number of rounds
- The capacity is long it seems sensible to call a halt to the auction after clearing the volumes

Therefore, we prefer a flexible approach to the bid algorithm.

Question 12: Do you consider that mechanisms supporting value discovery should form part of the NC? If so, which mechanisms do you believe would be most effective?

Response:

The process of value discovery is linked to a number of factors including the size, portfolio, risk mandate, business plan and strategy of the individual shipper. This being the case the process is to a large extent exogenous to the bidding rules as ultimately Shippers capability to bid is limited by these factors. Any restriction being placed on users to amend bids during the bidding window could potentially impact on the shipper's ability to develop a rationale strategy in the context of its internal resources. As the process of value discovery is linked to the shippers as much as it is with the TO, it makes sense to minimise the impact of the NC on their behaviour as one of the objectives of the auction should be to induce "truthful bidding."

Question 13: In your view, how could a split of bundled capacity between existing holders of unbundled capacity best be arranged?

Response:

Any forced split of bundled capacity therefore must be fair and transparent for all parties. Shippers should at least be given the opportunity to find agreement between themselves on this issue before any regulatory intervention be attempted.

Question 14: In your view, what effect would mandatory bundling have on network users? Please provide supporting evidence, if available.

Response:

Market rules should always aim to offer flexibility in the way that parties carry out their businesses. Mandatory bundling could limit *existing* cross border trade if incorrectly applied. Equally liberalization will not be enhanced if there are no suitable products available for new entrants. In particular it should provide -

- Access to capacity in the first place
- Opportunity to take advantage of price arbitrage

- Increased scope for innovation

Therefore, we suggest that an approach that respects both perspectives. This is only likely to make a difference for constrained IP's.

Question 15: Do you consider that the approach to bundled capacity set out in the NC is appropriate, within the constraints of the FG?

Response:

We broadly agree with the approach to bundle capacity as set out in the NC but it may have to be refined (see below).

Question 16: Do you consider that the process set out in the draft NC for determining the sequence of interruptions is appropriate? If not, what system would you prefer?

Response:

We can see how the “timestamp” rule creates an incentive to buy capacity as early as possible. However, we believe that the incentive is already there as parties will want to ensure interruptible is secured as soon as possible in case it runs out. An alternative method would be to scale back all interruptible capacity prorated by volume held taking into account what might have already physically flowed. E.g. TSOs should not be able to scale back more than 1/24th flow rate at any IP.

Question 17: ENTSOG would welcome feedback, observations and suggestions related to this section of the supporting document and to Annex 2. Do you consider that ENTSOG has correctly identified the key tariff issues in these sections?

Response:

The key issue for any auction design is always linked to the actual usefulness of the product that is being sold as much as the rules themselves. However, we believe the economic principles should apply to short-term products to be sold at zero or close to zero prices reflecting the short-run marginal cost of making that capacity available.

ENTSOG need to be cognisant of the issue of price discrimination as developed in EU competition law. We do not see any exemption from competition law so any revenues over and above what is allowed under price control arrangements is monopoly rent as (a) we can establish a relevant market (pipeline) (b) a reference price agreed by the regulator (c) buyers who have no close substitutes to transmission capacity.

Question 18: What is your view of the process that ENTSOG has followed in order to produce the draft NC? Would you recommend that ENTSOG use a similar process to develop future NCs? What approaches would you suggest to enable ENTSOG to improve the process?

Response:

We believe ENTSOG has done a good job in ensuring EU stakeholders were engaged in drafting the NC through consultation and workshops. These have been useful and in particular the auction simulation. We have also found ENTSOG staff helpful with ad-hoc enquiries.

Question 19: ENTSOG is developing a new website and would welcome stakeholder views on how to make it as useful as possible. What are your views about the current ENTSOG website, www.entsog.eu, and what could be improved?

Response:

It would be useful if the ENTSOG website could hold more information and data on real-time flows at IPs. This could start with periodic within day information but would lead to greater use of capacities, competition and potentially less constraints. From a user perspective the consultation area should be made as user friendly as possible.

Do you have any other comments or observations you would like to make?

Response:

EDF Energy would like to make some observations linked to the simulation in the Auctions workshop.

Table 3 Observations from the Auction Workshop

Aspect of Auction Design	Observed Impact in group	Policy Remedy
Stepped Prices (4.2- 4.4 draft code)	<ul style="list-style-type: none"> Varied significantly over different across networks e.g. A, B, C in the example and within pricing bands e.g. P 3 P4 Impacted on bidding strategy- large and seemingly random differences between bands would disproportionately shape the impact on bidders budget and therefore the price signal Likely to shape the type of signal between shippers. 	<p>General comment-</p> <p>Different costs between networks are linked to network efficiency and the regulators activity in price control</p> <p>Recommendations-</p> <ul style="list-style-type: none"> An auction design that offers

	<ul style="list-style-type: none"> There were no bidding constraints in the proposed auction design between different rounds so shippers were encouraged not to bid until the last round or tried to influence the process by strategic behaviours. 	<ul style="list-style-type: none"> capacity prices in increasing increments such as an ascending clock auction Transparent understanding of calculation and rationale for differences between pricing bands/ steps. Need to establish impact on behaviour of wide/ narrow banding.
Bidding Window	<ul style="list-style-type: none"> Non uniform bidding times meant that it was difficult to interpret the results of the auction This meant there was an element of doubt in the assessment of the market. 	<p>General comment-</p> <p>For signalling to work a balance has to be struck between the assessment of the outcome of each round of the auction and the timings between rounds</p> <p>Recommendation-</p> <ul style="list-style-type: none"> Would be preferable to increase the time between successive rounds?
Cross Border trade	<ul style="list-style-type: none"> For shippers who wanted gas across a number of networks capacity in one was not worth anything if others could not be secured. In any allocation volumes could suddenly become available if transit capacity was not secured. 	<p>Recommendations-</p> <ul style="list-style-type: none"> Will have to integrate capacity for transit in some way.
Outcome	<ul style="list-style-type: none"> Two out of the four shippers did not get capacity they required to the extent that it was not possible for them to offer supply contracts over a year. It was also not clear the extent to which traders were able to trade on favourable terms? 	<p>Recommendation-</p> <p>Need to consider impact on competition both up and down stream of capacity uncertainty.</p>