

## Responses to CAM Network Code – second formal consultation on new or modified concepts

### *Consultation Response Sheet*

Please complete the fields below and send via email using the subject title, “Response to the CAM NC consultation” to [info@entsog.eu](mailto:info@entsog.eu) by 14 November 2011.

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Countries in which your organisation operates:

How would you describe your organisation?

<input type="checkbox"/>	Association (please specify type)
<input type="checkbox"/>	End user
<input type="checkbox"/>	Network user
<input type="checkbox"/>	Trader
<input checked="" type="checkbox"/>	Other (please specify) Supplier, Trader, DSO

In the questions below, ENTSG would be grateful if respondents could clearly indicate their preferred option and provide a brief but **fully reasoned justification** for their choice. This applies equally whether you agree or disagree with any ENTSG proposal as it is important that ENTSG is able to extract the clear views of all respondents. If you do not respond to a question, ENTSG will assume that you have no view on this issue.

**Question 1 (Standard Capacity Products to be auctioned): which option do you prefer, and why?**

<input checked="" type="checkbox"/>	Option 1: Quarterly only
<input type="checkbox"/>	Option 2: Integration of yearly product (Post consultation proposal)

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

E.ON prefers Option 1 'Quarterly products only', since they provide flexibility to shippers to profile their bookings over the year. Concerns that "speculators" will be able to squeeze "genuine" shippers are misguided since "speculators" who try to book capacity but do not have gas to flow against it will not succeed, due to the Congestion Management Procedure proposals. TSOs will have the option of selling additional capacity rights and there is long term Use it or Lose it. In the new environment it is less likely that shippers pay for capacity that they do not intend to use, as the economic argument for doing so will no longer exist. Further arguments in favour of Option 1 are:

- Yearly products could entail an increased need for CMP as a result of unused capacity during the summer period. The Option 2 proposals significantly lessen the ability to profile capacity

bookings according to needs across a year. As a significant portion of gas flow can be seasonal, the restriction to booking only yearly products in the long term auctions automatically creates a potential problem of contractual congestion as shippers will be booking annual products based on their peak demands, which means they have excess capacity in non peak periods. To avoid contractual congestion, shippers have to use the secondary market or congestion management procedures have to be applied. Both are less efficient than being enabled to book only the necessary capacity in the first place.

- In Option 1, the 10% of technical capacity reserved for short term use will be released in the annual monthly auctions ahead of the relevant gas year; in Option 2 it would be released a month ahead. Option 2 is therefore less practical for new entrants (for whom it was designed) as they would only have certainty of their capacity holdings a month in advance.

Finally, it is not clear how the sale of both yearly and quarterly products could be made possible within the long term auction.

**Question 2 (Start date for yearly product): which option do you prefer, and why?**

- |                                     |  |
|-------------------------------------|--|
| <input type="checkbox"/>            | Option 1: Yearly product starts on 1 <sup>st</sup> January |
| <input checked="" type="checkbox"/> | Option 2: Yearly product starts on 1 <sup>st</sup> October |

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

Please refer to our answer to Question 1. If yearly products are to be introduced, we prefer yearly products to start on October 1<sup>st</sup>. This would give participants in both power and gas markets a couple of months between transport / transmission capacity auctions in either commodity. However, serious problems will arise if it is not fully harmonised throughout the EU. This problem does not occur with the use of quarterly products.

**Question 3 (Auction algorithms: overall methodology): which option do you prefer, and why?**

- |                                     |  |
|-------------------------------------|--|
| <input type="checkbox"/>            | Option 1: Multiple round ascending clock auction |
| <input checked="" type="checkbox"/> | Option 2: Single round volume based auction      |

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

Under option 1, shippers will not, in most cases, be able to adjust bids according to the outcome of other auctions. For example, due to the restriction to increase volumes at subsequent price steps in the auction at Point B (being the second cross-border point in a chain) the shipper cannot match the capacity he has already acquired at Point A (being the first cross-border point in the same chain) which has closed at an early price step. The limitation of bid revision also leads to bidding behaviour which undermines the advantages of the auction design. It was observed in the workshop on 3<sup>rd</sup> November that shippers only bid at P0 in the first bid window. Therefore it was not possible for a market demand curve to be derived, and shippers could not see the overall demand for capacity at given price steps. This was due to the fact that shippers can increase their bids at price steps on the second day of the auction but cannot reduce them. Therefore, given at this stage they do not know at what price the auctions would clear, it makes sense for them only to bid at P0, rather than bid a whole price stack.

Option 2, is indisputably the most simple, least time consuming and hence less costly auction design, which is therefore supported by E.ON. Much of the debate on amending the 'pure' single round

design that ENTSG proposed at its current draft NC seems to have arisen because bidders would not bid “real” bids until just before auction closure, either because there is no point bidding if shippers do not expect to change their bids, or because of fears that bidding will reveal shippers’ individual strategies. This would allegedly make it more complicated for shippers to assess the demand and hence the fair market value of the capacity. In practice however shippers won’t enter LT capacity auctions without a clear auction strategy, i.e. a ‘stop buy’ limit, based on their specific business case rather than on the willingness of others to pay more. Value discovery mechanisms would therefore not add benefits to the majority of shippers, but would certainly add uncertainties with regards to when the clearing price will be revealed and would substantially complicate the process and hence increase costs. Lack of value discovery is therefore not a valid argument for the use of option 1 and a single round auction model should be implemented to save time and cost.

**Based on the above, we propose the following single round auction model:**

- **A single round, volume based auction**
- **Limit the time taken by the auction. A couple of hours should be sufficient**
- **No early closure rules or bid revision limitations**
- **Naturally, shippers may change their bid stack as desired until the time of the actual auction, both to reduce their bids or to increase them (volume and price flexibility in both directions)**

Whilst all auction options have their positive and less favourable elements, we believe option 2 is the best option, taking into account the comments made above.

#### Question 4 (Limitation of price steps): which option do you prefer, and why?

- |   |   |
|---|---|
| X | Option 1: Do not limit number of price steps (Post consultation proposal) |
|   | Option 2: Limit number of price steps                                     |

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

Any type of pro rata allocation of capacity is not in line with the spirit of a market based mechanism such as auctions and should be avoided.

#### Question 5 (Minimisation of unsold capacity): which option do you prefer, and why?

<input type="checkbox"/>	Option 1: Minimise unsold capacity (Post consultation proposal)
<input checked="" type="checkbox"/>	Option 2: Draft CAM NC proposal

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

Any unsold capacity should be rolled over to the next shorter term auction, to provide flexibility to shippers to profile their transport contracts to their needs.

**Question 6** (Sunset clause: choice of default rule): which option do you prefer, and why?

<input checked="" type="checkbox"/>	Option 1: Maximum default rule with cap at technical capacity
<input type="checkbox"/>	Option 2: "Partially unbundled" default rule

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

In a "bundled world" unbundled capacity has no value for shippers.

**Question 7** (Sunset clause: further questions): Please provide any views, information or evidence in relation to the further questions raised by ENTSG in section F.2 regarding the sunset clause.

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**Question 8** (Tariffs: split of auction premium from bundled products): which option do you prefer, and why?☐

Option 1: Keep split of auction premium proportional to reserve prices as default (Post consultation proposal)

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Option 2: Split of auction premium into equal shares as default

Please justify your choice. ENTSG would particularly welcome any views on why the alternatives to your preferred option may not be technically feasible.

Given that at present, capacity prices are different at one side of an IP compared to the other, splitting the auction premium from bundled products proportional to reserve prices could seem a fair way to re-distribute the premium. However, TSOs and NRAs currently have considerable discretion how to transform overall capital and operational expenditures into specific tariffs at specific IPs. A proportionate distribution would incentive TSOs to allocate costs to congested rather than non-congested points and thus increase their share in an auction premium. Therefore we favour option 2, a split of auction premiums into equal shares, as this avoids putting an incentive on cost re-allocation between IPs.