ACER

Agency for the Cooperation of Energy Regulators

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OGP response to ACER's Public Consultation Paper "European Energy Regulation: A Bridge to 2025"

OGP welcomes the opportunity to respond to ACER's Public Consultation Paper on the topic "Energy Regulation: A Bridge to 2025". In this response we only comment on proposals related to the functioning of gas wholesale markets.

We agree with ACER's comment in the introduction of its paper that "The vast array of possible future developments is challenging for any analysis". For this reason the framework of regulation needs to be sufficiently robust to deal with a changing environment. In our view a functioning competitive market provides the best mechanism to respond to market changes. Market mechanisms will select the most efficient response to any change and are flexible enough to accommodate shifting trends and unforeseen events. ACER's focus should be on promoting a functioning market and regulatory interventions in the market should be limited to situations where there is clear evidence of market failure. This has proved to be successful in the gas wholesale market, which operates as a competitive market especially in the Northwest European region where the internal market measures have been implemented to a large extent already.

We acknowledge that the vision of a single European electricity market is facing serious challenges due to the different national policies to support RES-based generation. The huge sums of money that are spent on subsidies for renewable electricity generation have the effect of reducing wholesale electricity prices as well as CO2 prices. Both effects distort the electricity market and reduce the competitiveness of gas-fired power generation with an additional cost for the tax payer. Our suggestion would be to re-establish more market mechanisms in the electricity market and definitely stay away from interventions in the gas market in response to failing electricity markets.

ACER should also be conscious that well intended regulatory interventions can have serious negative consequences. As an example, the financial regulations (REMIT and EMIR) may facilitate regulatory oversight, but the increased administrative burden may cause parties to exit the market and reduce liquidity.

Question 1: Have we identified correctly the issues and trends within each area of the energy sector?

> In our view, uncertainties in demand and supply are inherent to energy markets. History has shown that market predictions often fail. Gas demand is influenced by economic growth and climatic conditions but also by exogenous events and political factors. In a functioning market, gas demand will always be balanced by supply, whether the market is growing or declining. The completion of the internal gas market is the best response for dealing with future uncertainties.
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> We believe the gas market can play an important role in facilitating gas-fired power generation, both in base load service and in flexible service, but this should be consistent with the gas balancing market. The network code on Gas Balancing provides for a harmonized system of daily balancing. To the extent that changes in gas off-take by gas-fired generators can be accommodated in the gas transmission system at no additional cost (sufficient line-pack) the generators could be shielded from imbalance charges. When gas-fired generators exceed the line-pack flexibility and transmission system operators are required to take action to balance the system, it is only fair and reasonable that the generators who cause the imbalance pay for the balancing costs. The network code on Gas Balancing also provides for the possibility of within-day obligations, subject to approval by the national regulatory authority, to incentivise network users

to take appropriate balancing actions during the day and avoid cross subsidies. As the gas system has much more flexibility compared to the electricity system, gas balancing costs to gas-fired generators should be small compared to the value of the flexible electricity they produce.

We share ACER's concerns about the timely delivery of infrastructure. We fully support the statement that "the core focus of regulators is to create a regulatory framework that facilitates the delivery of efficient investment". However, some of the regulatory actions can – unintentionally – undermine the investment climate. We refer to ACER's Framework Guidelines on Tariffs, which make long-term capacity bookings unattractive (see response to question 2) and to the procedures associated to PCIs, which appear to work contrary to the objective of facilitating investments.

Question 2: Have we identified an appropriate regulatory response?

OGP supports the statement that ACER's "immediate regulatory priority is the full and effective implementation of the requirements of the Third Package's network codes and (…) to secure the continued development of deep and liquid wholesale gas markets". We would welcome more initiatives from ACER to improve coordination through better cooperation and collaboration between NRAs. Implementation of the CMP guidelines was lacking a coordinated approach, making the rules ineffective. We call on ACER to ensure effective implementation of the European rules on both sides of interconnection points that focus on the removal of barriers and impediments. Given the different stages of gas market development across the EU, this could best be coordinated between neighboring NRAs or in the Gas Regional Initiatives. In this manner implementation of the network codes in other Member States could benefit from pilot projects and best practices that were identified.

We support ACER's statement that "market signals should drive the required investment decisions". This requires a regulatory framework that supports long-term capacity bookings which are needed to underwrite future infrastructure investments. While ACER acknowledges that regulators have a critical role to play in facilitating investments, we are concerned that some of the regulatory actions actually undermine the investment climate. We refer to the following aspects of ACER's Framework Guidelines on Tariffs and the guidance paper on a CAM amendment for incremental and new capacity which make long-term capacity bookings unattractive:

- existing long-term capacity contracts with fixed prices are not respected and neither are network users protected against significant price increases due to changes in the regulatory regime;
- mandating floating prices for long-term capacity commitments;
- discriminatory pricing which favours short-term capacity products;
- yearly adjustment of multipliers and seasonal factors;
- timing of tariff publication delinked from auction calendar;
- capacity allocation rules that favour short-term bookings in case of technical limits to developing incremental and new capacity.

ACER should consider the impact of its initiatives on the investment climate and take account of the clear signals from stakeholders with an interest to support infrastructure investments.

More in general, while we believe that market integration is a desirable outcome, we are convinced this should be the result of continued implementation of the Third Package by means of completing in a coherent and consistent manner the work on the EU Network Codes already completed and currently in the making rather than top-down market re-organization. Much remains to be done in terms of effective implementation, including:

- overcome the inconsistencies that prevent the offer and the use of bundled products;

- support the continued improvement of the functionalities of PRISMA, or other capacity booking platforms;
- support the conclusion of interoperability agreements and OBAs to ensure the optimal performance of the balancing systems;
- ensure implementation of the CMP guidelines that is compatible across borders;
- ensure a smooth transition to the new tariff regime without putting at risk the performance of existing contracts;
- work on a mutually recognised licence for all network user activities across the EU based on purely technical and financial capabilities.

While we agree that integration of market zones can contribute to competition and liquidity there are also some drawbacks which need to be considered. Merging market zones may require significant infrastructure investments when the zones are not well connected. Whether these investments are justified should be assessed on a case-by-case basis. Market integration covering multiple Member States introduces additional practical problems of bridging differences in national legislation, including taxation, and aligning national regulatory authorities.
We do not believe that ACER should strive to achieve liquidity at all European gas hubs for products far ahead of delivery (e.g. 36 months out) as this seems unrealistic. A more realistic goal would be to achieve sufficient price convergence with adjacent hubs at the day-ahead and month-ahead stage.

Question 3: Which regulatory actions are most important and should be prioritised?

We agree that progress towards an integrated gas wholesale market to date has been uneven across the EU. The necessary building blocks are in place and these have already been implemented to a large degree in the Northwest European region. We agree with ACER that a more targeted approach in certain regions could be more efficient than adding another layer of one-size-fits-all interventions at EU level. We expect that implementation of the Third Package and the network codes will also develop and connect gas hubs in other European regions, in line with the Gas Target Model. We support that regulators act to ensure compliance with mandatory European rules, but beyond this we believe regulatory intervention in the gas wholesale market is not warranted.

We support ACER's initiative to develop the process for modifying network codes. Implementation of the codes will inevitably reveal inconsistencies between the different rules and the need to implement change. The process for adaptation of the codes needs to be fit-for-purpose and as efficient as possible, while ensuring stakeholder involvement.

Question 4: Are there other areas where we should focus?

We do not see any other areas where ACER should focus.

We look forward to a continued dialogue with ACER.

Best regards,

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About OGP: The International Association of Oil and Gas Producers (OGP) represents the interests of companies engaged in the exploration and extraction of oil and natural gas, as well as national and other related industry associations. OGP membership spans the globe and accounts for more than half of the world's oil output and about one third of global gas production. From our London office, we foster cooperation in the area of health, safety and the environment, operations and engineering, and represent the industry before international organisations, such as the UN, IMO and the World Bank, as well as regional seas conventions, such as OSPAR, where we have observer status. OGP Europe in Brussels represents before the EU OGP members who are active in Europe.

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