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Document title: ACER Position on Capacity Mismatch Issue

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ACER
Agency for the Cooperation of Energy Regulators

ACER views on an issue related to bundling of capacities known as 'capacity mismatch'

A response to ENTSOG's comments on the capacity mismatch issue

7 December 2015

I. INTRODUCTION

The CAM network code (CAM) has introduced the concept of bundled capacity products at interconnection points (IP). Under CAM, Transmission System Operators (TSOs) need to maximize the offer of such products, which leads to circumstances where network users holding unbundled capacity bookings on one side of an IP may not find the equivalent unbundled capacity on the other side of the interconnection. This problem is described as the "capacity mismatch issue".

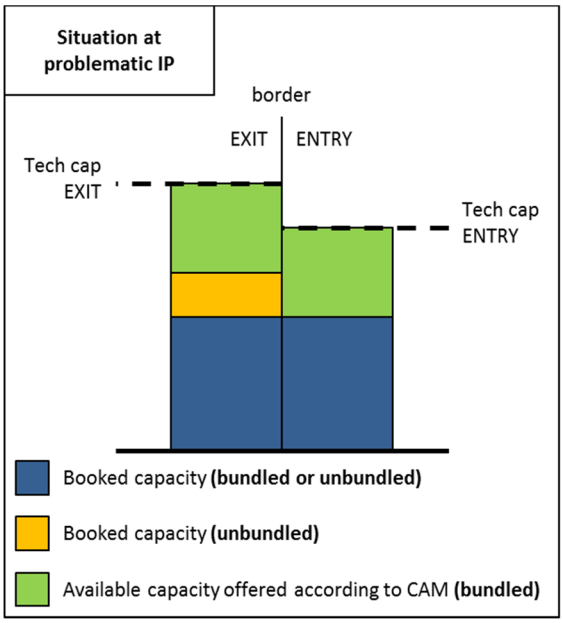
ACER was contacted by ENTSOG and EFET when they opened discussions with stakeholders through a public consultation in April 2015 and two workshops, in May and June 2015, where ACER was invited to present its views. In July 2015, ENTSOG and EFET published a recommendation paper on four issues related to bundling of capacities. Regarding "capacity mismatch", ENTSOG and EFET recommended three options: the capacity conversion mechanism, the capacity conversion mechanism with maximization of bundled capacity offered and the allocation of auctions leftovers. Some details on their respective implementation have been provided even though some technical and legal aspects remain uncertain (e.g. compliance with CAM and the CMP Guidelines).

ACER considers that solutions can be found on a case-by-case basis without changing CAM. The objective of this document is to outline ACER's views and understanding of the capacity mismatch issue.

II. DESCRIPTION OF THE "CAPACITY MISMATCH" ISSUE

ACER notes that ENTSOG, EFET and network users were aware of the bundling provisions in CAM for a long time and that the Article 20 of the CAM NC includes a clause inviting network users to make their "best efforts" to bundle their past bookings through voluntary agreements. However, hardly any network users have so far bundled their past bookings. Perhaps network users preferred to keep their unbundled products in order to take advantage of it or perhaps contractual or commercial obstacles did not allow the network users to book capacity to bundle with their existing unbundled capacity. Thus, mismatches resulting from past trade-offs aimed at minimizing network users' financial commitments might not require any action by TSOs and NRAs.

ACER acknowledges that the mismatch can also occur when network users holding unbundled capacity contracts only at one side of an IP where **only** bundled capacity is offered. This can lead to the following (financial) problem. If those network users want to transport gas across such an IP, and they cannot book the corresponding unbundled capacity on the other side, they are left with buying bundled capacity while paying for unbundled capacity they cannot use (except if interruptible capacity is on offer, which however does not provide the required planning reliability for network users). In this document, **ACER will only address this scenario of capacity mismatch**.



Although ACER agrees with ENTSOG's theoretical description of the issue, the extent of the capacity mismatch issue remains unclear. **ENTSOG and EFET have not yet provided further details regarding the extent of the problem (e.g. number and location of IPs, capacity mismatch volumes at stake).**

Furthermore, ACER agrees with ENTSOG, that the national and international legal framework is sufficient to handle this problem. The heterogeneity of situations across IPs rather advocates for a **case-by-case treatment** (per IP and with NRA agreement). Therefore, ACER describes a way of solving the subject of capacity mismatch considering the following principles.

III. PRINCIPLES FOR FINDING A SOLUTION TO THE CAPACITY MISMATCH ISSUE

a. Parties requesting particular action from NRAs or ACER should **demonstrate the importance of the problem** and that it does not result from specific concerns from individuals.

b. Any mechanism adopted to facilitate bundling of existing unbundled contracts should be applicable at IPs where no unbundled capacity products are available. Such a mechanism is not relevant at those IPs where unbundled capacity products are offered on a regular basis in capacity auctions on the "short" side of the IP since the entry into force of CAM, but are not booked.

c. A mechanism should be used when network users cannot reach a bundling agreement with other network users holding unbundled capacity on the other side of the IP under Article 20 of CAM.

d. Any mechanism adopted shall be **non-discriminatory** and must **not distort capacity auctions**.

e. Any mechanism adopted should help to **maximize the capacity offered to the market**.

f. Any mechanism adopted cannot impose a binding modification of transmission contracts. Forcing parties to amend or terminate an existing convention could be considered as an infringement to contractual freedom.Therefore, a mechanism can only lead to **modifying contracts if agreed** by both network users and TSOs.

g. Unless agreed by the TSO and relevant NRA(s), network users should **not be allowed to reduce the amount of firm capacity** they have previously booked **nor their financial commitments.** When short-term capacity products are booked and "multipliers" apply, they should be invoiced to network users.

h. The mechanism should be **compatible with the existing European legal framework**.

IV. ACER PRELIMINARY PROPOSAL: "Capacity Conversion Mechanism"

According to the principles presented above, ACER has considered the options outlined in ENTSOG's recommendation. The "capacity conversion mechanism" seems the most feasible and practical option to address the issue of capacity mismatch when deemed appropriate.

ACER's proposal based on ENTSOG's concept is the following:

a) Network users may request the application of the "capacity conversion mechanism" where users have unbundled capacity on only one side of an IP and cannot buy unbundled capacity for the other side because there is only bundled capacity offered in the auction.

b) The capacity conversion mechanism should only be used according to principles described in the section III of this document.

c) Under the scenario described in point (a) above, network users holding unbundled capacity may participate in annual, quarterly or monthly capacity auctions, to buy an amount of bundled capacity at least equivalent to the amount of unbundled capacity considered potentially "redundant". Where tariff multipliers[1] are used for short-term products, these multipliers apply to bookings of short-term bundled products even with the application of the capacity conversion mechanism.

d) If agreed by TSO(s) and relevant NRA(s), the amount of annual unbundled capacity previously contracted by the network user may be converted into the corresponding part of the newly acquired bundled product. The capacity conversion is always limited by the duration of the newly acquired bundled product. During this time the network user will not have to pay for "redundant" units of unbundled capacity[2]. For the avoidance of doubt, network users benefitting from the capacity conversion mechanism will, in any case, retain their rights and obligations on the unbundled capacity exceeding the amount converted. The network users will fully recover their rights and obligation on all the unbundled capacity once the bundled capacity product expires.

e) The recourse to the capacity conversion mechanism shall not affect the minimum share of technical capacity reserved for short-term capacity auctions, as defined in the Article 8 of CAM NC, even in the event of contractual congestion. The relevant NRA may decide to restrict the volume of capacity eligible for the capacity conversion mechanism.

f) Once a capacity conversion is executed, the redundant units of unbundled capacity formerly owned by the network user are returned to the TSO (for the time the newly acquired bundled product lasts). Such capacity becomes available capacity and has therefore to be fully (re-)offered to the market in the subsequent auction(s) in accordance with the CAM NC.

[1] Defined in the current version of the draft tariff network code published by ENTSOG

[2] If (regulated tariff + premium) of the old product < price of the newly acquired capacity, the network user will not have to pay for the unbundled capacity redundant with the newly acquired bundled product. However, in case auction premia and multipliers were previously paid for the unbundled product, the network user remains (partially) liable towards the TSO.

V. CONCLUSION

ACER agrees with ENTSOG, that the national and international legal framework is sufficient to handle this problem. At this stage, ACER does not see a need for a pan-European action such as amending CAM or adopting one specific mechanism for all IPs. The heterogeneity of situations across IPs rather advocates for a **case-by-case treatment** (per IP and with NRA agreement). Therefore, ACER details in this paper a mechanism aiming at solving the subject of capacity mismatch.

ACER considers that **the "Capacity Conversion Mechanism" is compatible with the existing legal framework** and the principles outlined in section III. It could be used without amendments of the CAM NC or CMP GL. It can be adapted for use at IP level, provided that the relevant NRAs and TSOs agree on the option being useful and in line with the specific terms and conditions approved by the NRA.

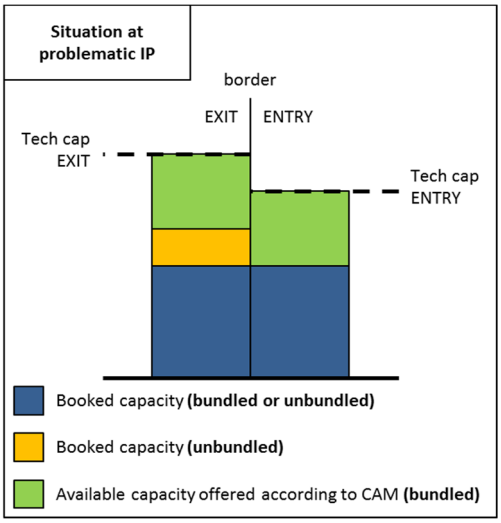
ACER notes there was limited information on the extent of the capacity mismatch and is willing to revisit its views in the future, when further information is available.

ACER does not rule out other possible solutions being developed and used for individual cases. Although ACER selected the capacity conversion mechanism for further comment, ACER encourages TSOs and users to explore all options.

Annex: Description of the functioning of the capacity conversion mechanism

The procedure works as follows:

Suppose there is an IP with higher technical capacity on the exit than on the entry side (called “Tech cap EXIT” and “Tech cap ENTRY” in the graphic below). An amount of capacity is already booked (dark blue boxes) without causing any problems and is not taken into further consideration. The green boxes illustrate the available amount of capacity.

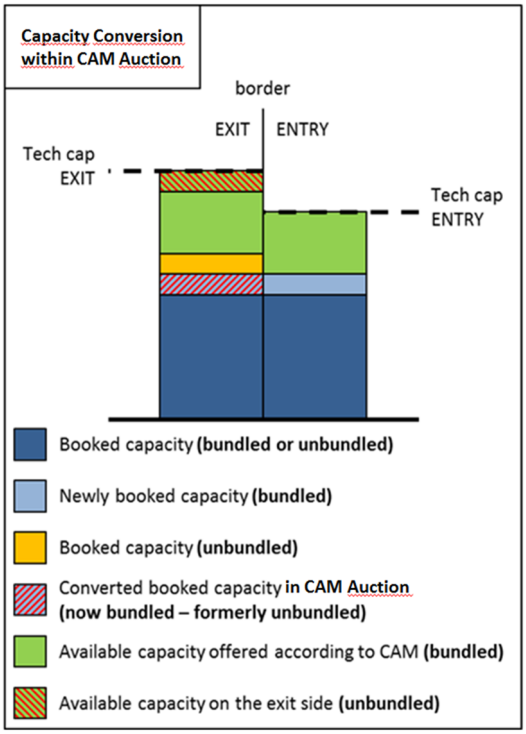


The capacity mismatch results from the unbundled capacity held by a network user on the exit side without corresponding capacity on the entry side (yellow box). Let the amount of booked annual unbundled capacity in the network user’s portfolio be **10 units**.

In order to allocate corresponding capacity on the entry side, **the network user may participate in annual, quarterly or monthly auctions** to buy a level of bundled capacity at least equivalent to the unbundled one he is willing to convert.

The network user would participate in the auction like any other network user, but announcing beforehand that he is willing to convert unbundled capacity. The “capacity conversion” can be realised only if there is no risk of discrimination or distortion of shippers’ willingness to pay. The following graphic shows an example where a network user books monthly bundled capacities (5 units) to use the conversion mechanism to lower its overall unused capacity on the exit side (light red-blue boxes in the graph hereafter). However, the mechanism shall not affect the minimum share of technical capacity reserved for short-term capacity auctions. **Multipliers on short-term products apply as usual; the capacity conversion does not prevent network users from paying higher short-term tariffs** (see the application of multipliers foreseen in the draft network code on tariff structure harmonization). The network user will then pay the monthly tariff for the 5 units of bundled monthly products without any discount.

5 units of the amount of annual unbundled capacity previously contracted by the network user are converted into the corresponding part of the newly acquired monthly bundled product by the TSO. This mechanism works as a **100% commercial discount service**, provided by the TSO, on the unbundled part which is redundant with the newly acquired bundled capacity. **The conversion is always limited to the duration of the newly acquired bundled product** (one month in this case).



The graphic shows the result of the conversion mechanism. After the conversion the network user keeps in his portfolio:

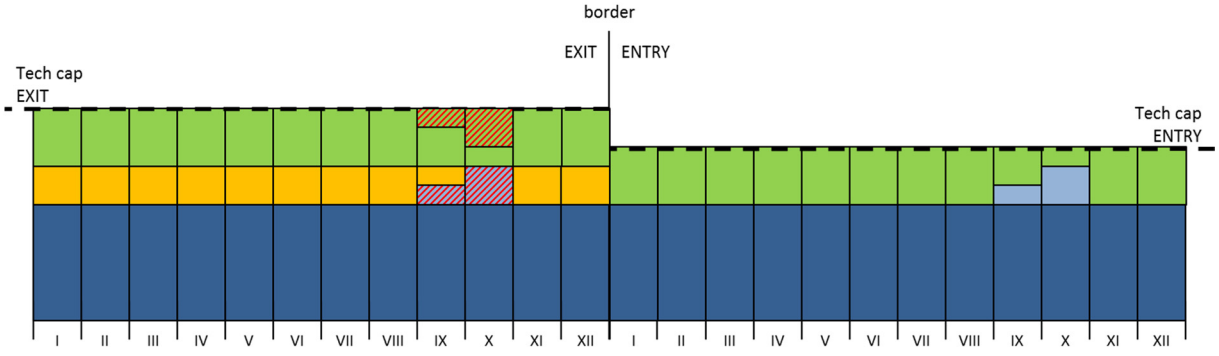
- **the newly acquired bundled product:** 5 units of bundled monthly products (light blue box on the entry side)
- a total amount of **10 units on the exit side** (as before) split into
  - 5 units of **unbundled capacity that could not be converted**, on which the network user pays the initial tariff (yellow box)
  - **5 units of unbundled capacity that has been converted. The commercial discount service applies on this 5 units of unbundled capacity (blue and red striped box), redundant with the newly acquired product.** Those 5 units result from the capacity conversion of 50 % of his annual unbundled capacity into 5 units of monthly bundled capacity

Through the conversion the 5 redundant units of unbundled capacity (formerly owned by the network user) are returned to the TSO, who should then re-offer them to the market. In this example, they will be part of the day-ahead auctions for one month (green and red striped box) at this IP.

- The **converted capacity will be returned to the TSO only for the time the newly acquired bundled product lasts.** During this time the network user will not have to pay for the redundant unbundled capacity[3]. But the network user still owns and has to pay for the remaining unbundled capacity until the contract for bundled capacity ends.
- T**he converted capacity returned to the TSO can only be proposed at the next auction(s) of the IP where the capacity mismatch occurred**.

[3] If (regulated tariff + premium) of the old product < price of the newly acquired capacity, the network user will not have to pay for the unbundled capacity redundant with the newly acquired bundled product. However, in case auction premia and multipliers were previously paid for the unbundled product, the network user remains (partially) liable towards the TSO.

The following timeline illustrate this issue:



Each month is represented on the exit and on the entry side. The network user owns 10 units of annual unbundled capacity on the exit side and occasionally buys bundled capacity on a monthly basis.

From January to August the network user does not buy any bundled product and no capacity conversion takes place. Each month he pays for 10 units of unbundled capacity on the exit side.

For September, the network user acquires monthly capacity of 5 units. Thus, 5 units of his 10 units of annual unbundled capacity on the exit side are converted and 5 units are returned to the TSO to offer them in the following day-ahead auctions of this particular IP, for September (one month). So in September, the network user pays for 5 units of unbundled capacity on the exit side and for 5 units of bundled capacity on both sides.

For October, the network user acquires 10 units of bundled capacity. Thus, the TSO converts the total amount of unbundled capacity on the exit side, so that the network user pays only for 10 units of bundled capacity. 10 units of unbundled capacity are returned to the TSO to offer them again in the following day-ahead auctions of this particular IP, for October (one month).

Since the network user does not acquire any new capacity for November and December, nothing is converted and he will pay for the 10 units of unbundled capacity on the exit side each month.

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