

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.

Name

First and Last Name: Maria Elena Fumagalli

Organisation

Company/Organisation Name: Edison SpA

Job Title: Head of Regulatory Affairs

Contact details

Email: affari.regolamentari@edison.it

Tel: +39 02 6222 7117

Mobile:

Address

Street: Foro Buonaparte 31

Postal Code: 20121

City: Milano

Country: Italy

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

Edison considers that the level of detail adopted by ENTSG is appropriate to achieve the final objective to harmonise the allocation of capacity across all Member States: setting general high-level principles to provide guidance to the process should be the aim of ACER's Framework Guidelines, whereas Network Codes should be intended as operational documents designing clear procedures for TSOs and network users.

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?

As explained above, we think that the level of detail adopted by ENTSG for the draft NC is appropriate. National experience shows that the NC should be able to rapidly evolve with the market and therefore a simplified change process should be introduced, if legally possible, for issues that are not questioning the general principles introduced by the Framework Guidelines (i.e. the elements that we identify in answer to question 3 as possible subjects for a "lighter" change process).

A possible simplified procedure could envisage the following steps:

- Each network user (holder of a transportation contract)/association shall be entitled to request a modification to the NC, by sending the proposed amendment, duly justified, to ENTSG, copy to ACER.
- Every year, ENTSG shall report to ACER on the requests of modification received, duly justifying which of them will be considered and consulted with market and which ones will not be considered. ENTSG will also justify and consult the market on its proposals to amend the NC.
- A supervisory role and final approval of ACER is a must.

In case of need to modify general principles, the regular process including comitology will be required.

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?

See response to previous question.

In principle we think that the more operational provisions, for instance the ones regarding the auction design (e.g. number of booking windows, number and characteristics of standard products, etc), should be object of a "lighter" change process, given that the design of auction mechanisms

which are able to deliver efficient outcomes is often the result of a “learning by doing” process, which could need some modifications at the initial stage of implementation.

In order to make “lighter” changes binding, we suggest the adoption of the process that we described at Question 2: the constant and active involvement of stakeholders and the supervisory role of ACER, which should approve any minor change to the Network Code, will legitimate the modifications as binding.

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

Edison believes that the same process suggested at question 2 should be adopted to review the handbook: the handbook could represent a useful tool, but it shall be avoided that any change to the handbook generates impacts on the general provisions of the NC.

In any case, we recommend that any proposal to modify the handbook is timely notified by ENTSG to the market and adequately consulted with network users.

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.

Edison is very concerned about ENTSG’s proposal to offer long term capacity only under the form of quarterly products. In our opinion, the proposed auction design, auctioning each single quarter separately, introduces a high risk for shippers of not being able to book long (one year and longer) consecutive periods without intermediate gaps.

Moreover, the presence of yearly capacity products will facilitate for market participants the transition towards the new allocation regimes, given that most European countries are now allocating long-term capacities in form of annual products and are currently considering quarters and months as short-term products.

We therefore recommend that ENTSG introduces yearly capacity products as the standard capacity products to allocate long term capacity. If there is unsold annual capacity, it could then be auctioned in form of short term products (quarters, month, etc), which could result useful for shippers willing to profile their bookings.

The introduction of yearly capacity products will also ensure the full compliance of the NC with the Regulation 715/2009, which states at art. 2 that “long term services are services offered by the TSO with a duration of one year or more”.

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?

As explained in answer to Question 5, we believe that the absence of an annual capacity product will undermine the possibility for users to purchase long-term capacity, if for long term capacity we use the same definition as for Art. 2, Reg. 715/2009. For this reason, we highly recommend the introduction of yearly capacity products to allow shippers to cope with their need to book long term capacity to comply with long-term supply contracts.

Moreover, we have some concerns on the proposed design of the auction for long-term capacity. The introduction of a 10 days booking window in a single round auction, where allocation takes place only on the last day of the window, could turn to be useless (or even counterproductive) if no “value discovery mechanisms” are put in place. In fact, the objective of introducing more transparency and information for market participants in order to adapt their bidding behaviours, could not be achieved if there are no obligations for market participants to bid from the first window. Given the absence of constraints, it is likely that booking patterns could result distorted by strategic behaviours: bidders could decide of not participating or bidding very low during the first windows in order to distort the price signal and “surprise” the market with high bids at the last and crucial window. As a consequence of these common tactics, the clearing price emerging from every intermediate window will not be able to provide a reliable signal to market participants.

The introduction of “value discovery measures”, as suggested by ENTSG in the Supporting document could partially help to prevent speculative behaviours. For example, imposing to shippers to participate to every bidding window and to bid every day a volume for price step which is equal or higher than the previous day’s bid, could avoid this strategy. On the other hand, we are concerned that such measures will have the final effect of “stiffening” the auction, reducing bidders’ freedom to change their bids according to the information provided at the end of each day of the booking window.

For the above explained reasons, we are in favour of the application of the same auction design applied by ENTSG to day-ahead and within-day capacity to long term capacity products. In brief, we **support the application of a single model of auction, a single-round open-bid uniform-price auction algorithm, to all capacity products.**

The advantages of the proposal to apply the same model of auction to all capacity would be:

1. Less complexity of the auction design. Both TSOs and network users will have to get familiar with only one type of auctions
2. Reduction of implementation costs for TSOs and shippers in adapting their IT systems and in carrying on long-term auctions for 10 days bidding windows
3. No need to define “value discovery mechanisms” for long-term auctions. Long-term auctions could be run in one single round: shippers will submit once their bids and TSOs will rank them according to the bid price
4. The possibility for shippers to submit their own price bids on long term and monthly products will allow them to express the exact value that the capacity has for them.

Moreover, it will avoid complicated analysis on how TSOs should set different price steps to avoid inefficient outcomes in a volume-based auction.

5. An algorithm where clearing price is the highest price step at which demand is greater than or equal to the offered capacity, will ensure that there is no unsold capacity. In our opinion, avoiding cases where capacity available for long-term allocation is not completely allocated is of paramount importance to ensure that all shippers are able to purchase the long-term capacity they want.

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?

We think that the within-day auction design proposed by ENTSG provides an appropriate response to market needs. The allocation of within-day capacity via auction, instead of FCFS, is important to let the real value of within-day capacity emerging. This will be increasingly important considering the future evolution of balancing regimes, where access to cross-border within-day capacity (in systems where also upstream supply contracts can be re-nominated in a flexible manner) will play an important role.

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?

First of all, we would like to confirm our view that implementing the same auction model (a single-round open-bid uniform-price auction algorithm with a single day booking window per product) to all IPs and for all capacity products will already contribute to lower operational costs.

That said, we think that short-term auctions should never be suspended: given that the demand for day-ahead and within-day capacity is mainly related to the need of covering “last-minute” variations in demand, it is unlikely that TSOs will be able to exactly predict in advance if demand for day-ahead and within-day products is there or not on a specific day.

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?

As explained above, we support the application of the open-bid uniform-price auction algorithm foreseen for day-ahead and within-day capacity to all standard products. See answer to Question 6 to have an overview of the advantages of our proposal.

Our concerns on the application of a volume-based cleared-price algorithm are the following:

1. Bidding against pre-define price steps will limit shippers’ ability to price the capacity at the

exact value they are willing to pay for it.

2. Deriving the clearing price as the lowest price step at which demand is smaller than or equal to offered capacity increases the risk of having unsold capacity, if the demand curve does not cross the offered capacity exactly where a price step is jumped. We believe that this will not represent an efficient outcome.
3. Pre-defined price steps also poses the critical issue of how fixing different steps in a way that avoids distortion in the functioning of auctions. Having 29 steps implies that:
 - a. If the spread between each step is too big, the risk of having a large amount of unsold capacity increases, as well as the risk of having a clearing price that does not reflect the real that shippers will give to capacity;
 - b. If the spread between each step is too small, the path towards P29 will be shorter, consistently reducing the difference between P0 and P29. This will increase the convenience for market participants to bid large volumes also for high prices. In facts, if the maximum P29 is lower than the cost of the cheapest alternative sources (e.g. storage or LNG capacity, etc), it is likely that each users will ask for the same (or very similar) amount of capacity at each price step and, at congested IP, demand will still exceed offer at P29. The pro-rata in this case will impact a larger number of users.

➔ **The application of the uniform-price open-bid auction algorithm to all capacity will make unlikely having this situation:** in facts, given that each shipper will submit 10 independent bids, each participant can decide on how much volume and for which price he is prepared to incur in the risk of being pro-rated and, in any case, the pro-rata will be limited to the volumes for which shippers placed a lower bid. If we take as example the table at page 23 of the Supporting Document, we can see that Shipper 1 is allocated all the 200 units of capacity for which he bids a price which is higher that the clearing price (i.e. 10,5) and he is only pro-rated on the 100 units for which he bids a price of only 9, being therefore ready to accept a higher risk of not being successful.

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?

We do not support the introduction of Pay-as-Bid, but the application of a single round open-bid uniform price auction for all standard capacity products.

In any case, if ENTSGO decides to apply a volume-based auction, we think that it shall not be a single-round auction based on a 10-days booking window, but a multiple-step auction, where users always have the chance to actively decide whether or not to place a bid at a higher price. In this case, an accurate definition of different price steps, in consultation with market operators, is needed.

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?

We think that 10 bids (price and volume) are sufficient, if the open-bid algorithm is applied both to short-term and long-term capacity.

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?

See also answer to question 6.

As highlighted above, we think that the application of an open-bid uniform price auction for all capacity products, implying a single booking window per standard product, will eliminate the need for the introduction of “value discovery mechanisms”, as in such an auction model shippers will have limited possibility to adopt strategic behaviours to distort the information provided to the market.

In case ENTSG confirmed its intention to apply a single-round volume based auction with 10 days booking window for long-term capacity, mechanisms to reduce behaviours aiming to distort the information provided at the end of each day will surely need to be introduced. Nevertheless, the final outcome will be, as we said, to limit shippers’ ability to modify booking behaviours during the auction following a logic of portfolio’s optimization.

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

We share ENTSG’s view that TSOs should not be entitled to unilaterally change existing transmission contracts; nor the final decision should come from a third party. In our view, the decision of how to split bundled capacity should be left to the negotiation between existing holders of unbundled capacity.

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

We believe that the introduction of bundling products will surely contribute to simplify the activity of shippers being active on interconnected markets, making a single booking procedure and nomination sufficient to reserve capacity at both sides of an IP. Nonetheless, we are concerned that the mandatory definition of bundled products as the only capacity products to be offered in Europe within 5 years from the entry into force of the NC, will lead to complicated renegotiations of existing supply contracts. For this reason, we support the introduction of bundling (at least until existing contracts will terminate their validity) as a possible option and not as the only product.

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

Yes, Edison shares ENTSOG's approach towards bundling.

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?

In the Supporting Document ENTSOG states that if all users pay the same price for capacity, the sequence of interruptions will be based on the time when the contract has been signed, according to the principle of "last come first interrupted". Nevertheless, if all capacity is allocated via auction (therefore at the same moment in time), it is not clear how will be possible identifying which contract was signed before.

In general, we think that the sequence of interruptions should be based on the price paid by each shipper, according to the principle that the shipper who paid less for the capacity is first interrupted. If ENTSOG is thinking of applying to interruptible capacity clearing price auction, all shippers will pay the same price and therefore we think that this principle can be applied taking into consideration the bids of each shipper. In order to make this mechanism working, we suggest that after the end of the auction process, when capacity is allocated, each successful bidder receives (on an anonymous basis) information on the list of bids expressed, or better, of the relative probability of being interrupted.

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?

Edison shares ENTSOG's proposal to apply a reserve price to all capacity and we believe that calculating it as a percentage of the regulated tariff is the simplest and most fair way.

As concerns the management of over-recovery we think that the decision of using it to invest in incremental capacity or to lower the tariff of the following year should be left to each NRA, in consultation with involved TSOs and market participants, since this issue is strictly related to the way how tariffs are designed in each national system. However, our general preference is for using over-recovery to lower PO of the following year.

Both in case of under and over-recovery, we think that the impact on the tariffs of the following year should be limited to the PO of the capacity of the specific IP where under/over-recovery took place and not widespread to all the IPs of the system.

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

The entire process followed by ENTSG to produce the draft NC can be considered highly satisfactory: clear steps and deadlines have been set in the Project Plan and consulted with market and Launch Documentation represented a first useful input to discuss within companies about the possible options. A high level of involvement of stakeholders was also reached by organizing frequent stakeholders joint working sessions. Nevertheless, given the increasing number of European meetings to be managed, we would recommend –if possible- the introduction of live streaming tools to allow interested parties to follow the discussion on the web, similarly to what has been implemented by CEER for the GTM workshops.

We feel that the work is generally based taking into account North-West systems and we therefore claim for a major consideration of characteristics of transmission systems and markets of other European areas.

Question 19: ENTSG 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 ENTSG website, www.entsog.eu, and what could be improved?

We think that the website is very clear and well structured.

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

We do not have any additional comment.