ACER

Agency for the Cooperation of Energy Regulators

The Director

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Mr. Malcolm Webb
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Mr. Marshall Hall
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By e-mail only

Subject: ***The Agency will not propose the Network Code amendment request to the European Commission (letter under embargo)***

Dear Mr. Webb, Mr. Cox and Mr. Hall,

On 24 July 2014, the Agency received the joint submission of Oil and Gas UK and Gas Forum proposing an amendment to the Network Code on Capacity Allocation Mechanisms ('NC CAM')[1] and the Network Code on Balancing ('NC BAL')[2]. In the submission, the two organisations proposed to allow the UK and Ireland to derogate from the obligation of adopting the common times of the Gas Day[3], as defined by Article 3(7) of the NC CAM.

The referred submission gave a high level description of the problem perceived by the two organisations, while the Agency needs a detailed justification to consider an amendment of

[1] COMMISSION REGULATION (EU) No 984/2013 of 14 October 2013 establishing a Network Code on Capacity Allocation Mechanisms in Gas Transmission Systems and supplementing Regulation (EC) No 715/2009 of the European Parliament and of the Council, OJ L273/5, 15.10.2013
http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013R0984&from=EN

[2] COMMISSION REGULATION (EU) No 312/2014 of 26 March 2014 establishing a Network Code on Gas Balancing of Transmission Networks, OJ L91/15, 27.03.2014
http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0312&from=EN

[3] from 5:00 to 5:00 UTC winter time

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the text of the two approved network codes. The Agency therefore requested further clarifications and supporting data from the submitting parties on several occasions. Following the provisions of Article 7(2) of Regulation (EC) No 715/2009, the Agency also consulted stakeholders on the amendment request. The public consultation took place from 19 January to 9 February 2015. The Agency shared with stakeholders the non-confidential versions of the documents collected by the Agency at that point in time. The responses to the public consultation were published on the Agency's website. A summary of the main arguments provided in the public consultation is annexed to this letter and will be published on the Agency's website 24 hours after sending out this letter.

To summarise the request, your organisations claimed that aligning the Gas Day used by UK upstream producers and terminal operators to the uniform CAM Gas Day will cost your members at least £40-50 million (€50-60 million), with no means to pass these costs on to customers. In the submission, the associations argued that adopting the uniform CAM Gas Day would have negligible or even negative benefits for downstream users in the UK, if two Gas Days were to exist after the implementation of the NC CAM in the UK. Your submission further outlined that the two Gas Days would create additional balancing risks and uncertainty at the interface points in the UK between upstream and downstream, as well as decrease NBP liquidity by the upstream players moving their gas sales to the beach, where the referred risks and uncertainties may not be present.

The Agency has carefully considered the submission and the documentation provided by the submitting parties and the consultation results. The Agency will not consider the amendment proposal further for the reasons outlined below.

On the **substance**, first of all it should be pointed out that the burden of proof to argue the case for amending the network codes is on the requesting parties. In the Agency's view, they have not satisfied this requirement, as:

- **the arguments provided were not convincing.** In particular:

  - **Unsubstantiated claims**

  Significant elements of the submitting parties' reasoning remained unsubstantiated, despite repeated information requests by the Agency. For example, the Agency strived to understand whether the one-off costs for upstream producers to switch to a different Gas Day would not be outweighed by the benefits of improved market integration. This key element was not fully clarified by the parties and was not presented to the Agency in a detailed and differentiated manner, by including other interests and/or viewpoints that different market participants, other than UK upstream, may have.

  - **Cost-benefit analysis**

  The mere fact that certain stakeholders face certain costs in implementing certain Network Code provisions certainly does not justify amending the Network Code, given that such costs are inevitable in the process of European harmonisation. Therefore, such costs would have to be weighted against the overall benefits such harmonisation brings. In particular, the submitting parties did not provide the Agency with a credible cost-benefit analysis for the different scenarios and effects on the downstream market. Certain aspects, like the negative (financial) effects for shippers flowing gas from the continent to the UK if the UK is permitted to retain its current Gas Day, have not been appropriately analysed or explained. Even if the aggregated cost estimates of the parties were right, there would be benefits of the uniform CAM Gas Day which would have to be weighed against such costs. A common start and end time to the Gas Day would make cross-border trading seamless, and should improve hub-to-hub linkage. The impact assessment of the European Commission also claimed that the CAM provisions will foster liquidity at hubs, due to bundled products and auction based allocations. Expected efficiency gains of a uniform CAM Gas Day (e.g. regarding bookings for daily capacity on the interconnectors) have not yet had the chance to materialise and could have been considered by the parties in the submission. In addition, the sunk costs of those already implementing the current provisions – such as the downstream sector, National Grid (UK), Gaslink (Ireland) and some producers – should have been taken into account in such a cost-benefit analysis.

- **Liquidity**

In connection with the cost and benefit analysis, the Agency notes that the submitting parties have neither modelled the claimed negative impacts on NBP liquidity, nor have they analysed the possible scenarios that a changed upstream behaviour (in case the proposed derogation were not to go forward) could cause at the NBP, giving appropriate weight to the role downstream shippers play at the NBP.

- **The information provided by the requesting parties was incomplete**

- **Profiles**

Information on the real production profiles, in particular whether they have a pattern or a "flat" profile, was requested by but not communicated to the Agency. The more flat the production profiles are, the more appropriate other means of reconciliation (than a derogation to the NC CAM) would be.

In terms of process, the main reasons for not further considering the amendment request are the following:

- **NC development process**

The NCs CAM and BAL were prepared and discussed for a number of years with the full involvement of stakeholders. The NC CAM development process under ERGEG/ACER (e.g. the consultations on FG CAM, the ENTSOG consultations on NC CAM) allowed the upstream industry to contribute. Some companies with upstream interests participated in the consultations, like Shell, ExxonMobil and BP, although their contributions did not target the Gas Day provision. There was ample opportunity for interested parties to raise the disputed point during the Network Code development process, rather than after it had been finalised.

- **Lack of new evidence**

The parties' submission also failed to add new evidence, which could not have been included in the original NC development process. The conducted public consultation did not deliver new arguments, which were not known at the time the NC CAM was drafted. Beyond the UK upstream players, the consultation attracted limited stakeholder interest.

- **Timing**

An amendment proposal has considerable lead time, in particular if provisions with obvious market impacts are debated. Should the Agency have retained the proposal, the Agency itself would have had fully to assess, in an independent manner, the costs and benefits of the proposal, possibly amend the text proposed by the requesting parties, before submitting the amendment to the European Commission. This process could take up to a year. In addition, the Agency received the amendment request a year after the problem had been identified by the UK upstream industry, during which period important implementation steps have already been taken by midstream and downstream players.

- **Implementation**

The derogation could substantially delay the overall implementation of the NC CAM and BAL in the UK, as the implementation of the two network codes is linked. A possible amendment proposal would increase uncertainty in the UK code implementation, until a final decision is adopted by the Commission.

- **Precedent**

Allowing amendments to go ahead without novel elements or arguments and strong market support could easily undermine the credibility of the Framework Guidelines /Network Codes development processes in general, and set the precedent that requests which are not included during the NC development process could be introduced into the network code successfully at a later stage, via the amendment process.

In the light of the above, the Agency will not submit the proposed amendment to the European Commission for consideration.

The Agency welcomes the efforts of the Gas Day Industry Workgroup[4] to develop interim solution(s) to deal with the one-hour difference between the (partially not adapting) upstream sector and the downstream sector, allowing the UK upstream sector to adapt in a more flexible manner.

The Agency will publish the results of its analysis, including this letter, 24 hours after sending it to the submitting parties. The Agency requests the submitting parties to keep the content of this letter under embargo until the 24 hours have elapsed.

Yours sincerely,

Alberto Pototschnig

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[4] Involving UK upstream producers, terminal operators, network users (incl. non-producing ones), National Grid (TSO), the Claims Validation Services Limited (CVSL), DECC and Ofgem.

Annex: Summary of the main arguments, in favour and against the amendment proposal, provided in the Public Consultation:

Arguments raised in support of the OGUK amendment proposal (“keep UK Gas Day”)	**Arguments raised in opposition to the OGUK amendment proposal (“uniform EU Gas Day”)**
• A change is unnecessary and costly (>30m£) for producers and downstream network users • Different Gas Days in the UK and continental Europe have not hindered cross-border trade so far • Cross-border trade (in the UK region) cannot further improve, as within-day flexibility is already provided for • Gas from the UK Continental Shelf will face a risk premium (competitive disadvantage), if the UK upstream and downstream players would operate under different Gas Days • NBP’s liquidity is at risk, as some producers may then deliver gas to the “beach” (instead of NBP) • No benefits could be expected from this provision to the downstream shippers • No obstacles currently present at NBP (NBP is performing best in EU) • Interim solution (“option A”) may not be implemented on time • No legal obligation for upstream to change • No cost-benefit analysis for uniform EU Gas Day has been done • Inadequate consultation in the NC CAM process for producers	• Uniform Gas Day implementation is already ongoing, and costs have been already faced (e.g. for IT changes) → a revision of the implementation would be difficult and costly, and additionally implementation timelines could not be met, if the amendment goes ahead • Difficulties to introduce bundled products (e.g. at Bacton), if gas day is not harmonised • Removes an existent trade barrier, as due to non-harmonised Gas Days: there is a need to buy capacity products on both sides of a border for two consecutive days, to cover the desired 24 hours • Benefits of a uniform Gas Day for the UK gas hub and the surrounding hubs through closer linkage between them • Uniform Gas Day needed to remove complexities in Balancing • Potential loss of possible efficiency gains for operators active in several EU markets and with a potential to benefit from a harmonised gas day • EU harmonisation is the agreed goal, there should be no exceptions / derogations • The proposal is counterproductive and a “step backwards” in the development of the Internal Energy Market. • (Interim) solutions are under development and could make transition possible • UK Gas Day is a domestic issue • Gas Day issue has been discussed during NC CAM development and some producer organisations as well as producers were present in the debate