

**OGP response to CEER Public Consultation Paper Ref: C12-GWG-87-03
“Market-Based Investment Procedures for Gas Infrastructure: Issues and Approaches”**

Public consultation questions

1. *Have you participated in an Open Season process for cross-border capacity? If so, what are your views on the process?*

OGP is an association of Oil & Gas Producers and as such has not participated in Open Season processes but OGP members individually have. We acknowledge that Open Season processes organized in the past did have shortcomings in terms of transparency and coordination. Some of our members have indicated instances where it was not possible to ensure that finally allocated capacity matched with capacity requests, and the outcome was not predictable. Processes like that are considered a very suboptimal tool to allocate incremental capacity. Although these shortcomings could possibly be addressed, we believe that the coordinated auctions introduced under the CAM Network Code provide an opportunity to combine existing and incremental capacity in a single allocation mechanism.

2. *In light of your experience, do you consider that current methodologies (for example, Open Seasons) to decide on investments are an appropriate way to identify and integrate new cross-border capacity, or is there a need to move away from them? If so, what would be your preferred alternative and why?*

The complexity of the Open Season process may be increased when existing capacity is allocated through auctions, as provided by the CAM Network Code. Instead of having two separate allocation processes for existing capacity and for incremental capacity, we prefer an integrated auction process for both existing and incremental capacity, save in the case of major infrastructure projects crossing multiple borders as referred to in the response to question 4. We also refer to the response to question 6 for the reasons why we prefer integrated auctions.

3. *Do you think the paper addresses the right questions? What (if any) are the additional questions that should be addressed? What in your view are the main problems that need to be resolved?*

We welcome the CEER paper on *Market-Based Investment Procedures for Gas Infrastructure* and believe the paper addresses the right questions and the main problems that need to be resolved, with exception of tariff issues. We noted that tariffs will be kept outside the scope of this work, but it is not clear that tariff issues (e.g. non-discrimination between holders of existing capacity and additional capacity; distribution of economies of scale) will actually be addressed in the context of developing guidelines on harmonised transmission tariff structures.

4. *What should be the scope of this paper? Should our proposals apply to cross-border points only, or should they also apply to entry points to LNG terminals and entry/exit points to and from storage? Why or why not?*

Since we prefer an integrated auction process for both existing and incremental capacity, the scope of a European framework for incremental capacity should be consistent with the scope of the CAM network code for existing capacity and deal with cross-border interconnection points between adjacent entry-exit-systems.

We acknowledge that the auction process may be more complicated for major infrastructure projects crossing multiple borders. For such major infrastructure projects, Directive 2009/73/EC allows for an 'exemption process' (Article 36) that requires, amongst other things, an open season procedure. Hence, capacity exempted according to Article 36 should also be outside the scope of this work.

5. *What in your view needs to be harmonized on a European level, what can be done at other levels?*

The integrated auction process for existing and incremental capacity needs to be harmonized on a European level, including the design of the integrated auction process and transparency requirements related to the economic test. The parameters that are used in the economic test can be set by the NRAs involved. Please also see our response to question 8.

6. *Do you agree with the proposals to allocate incremental cross-border capacity via an auction? Why or why not? What are the advantages/disadvantages of using auctions vs. Open Seasons (in cases where Open Seasons do not include an auction in the allocation phase)?*

Yes, we agree with the proposals to allocate incremental cross-border capacity via an auction. Advantages of using auctions vs. Open Seasons are:

- No discrimination between existing and incremental capacity allocated at the same time and for the same IP and period (these are identical products for a network user);
- Long-term auction process for existing capacity will only generate useful information when users can signal the need for incremental capacity;
- More transparency to network users about what additional demand would be required to meet the economic test criteria.

A possible disadvantage could be the complexity to deal with incremental capacity from major infrastructure projects crossing multiple borders. The CEER work should address in which cases this justifies that Open Seasons could be used, just like projects that apply for the Article 36 'exemption process' mentioned in the response to question 4.

7. *What in your view should be the key considerations for the economic test? How could it be designed? How should risks/costs be allocated?*

Risk/cost sharing has experienced considerable change as result of regulatory initiatives and market developments. With increasing market liquidity, there is a trend towards more short term products. This might affect the economic test. Where the Framework Guidelines on CAM specify that at least 10% of available capacity shall be set aside for short term services, there is also a minimum % of capacity that needs to be contracted as long-term service to trigger an expansion investment.

A key consideration for the economic test is that it should be designed to establish whether there is an *economically reasonable*¹ demand for additional capacity, and not to guarantee an economic return on the investment. For the economic return it makes no difference whether the incremental capacity is sold for 10 years as a long-term product or each year as annual capacity for 10 consecutive years, provided there is a genuine need for capacity and there is no discrimination between holders of short-term and long-term capacity.

The economic test should address which portion of the investment costs should be carried by the long-term capacity bookings and which portion is expected to be recovered from short-term bookings (at the IP and at domestic entry/exit points) or is rolled into the TSO asset base and smeared across all users. The economic test should be fully transparent to network users: the criteria to pass the test (subscription level) should be published and also the reason why the subscription level is set as it is.

8. *Would a fully harmonized economic test across Europe be appropriate, or would it be sufficient to harmonise only the general principle to investments? Why or why not?*

Although we would prefer a fully harmonized economic test across Europe, we acknowledge that this would not be in line with the provisions of Directive 2009/73/EC, according to which tariffs are to be decided on by the national regulatory authorities. This would allow NRAs to take into account potential effects on security of supply and market integration when setting the threshold for capacity expansions.

We believe it should be possible to harmonize general principles that apply to incremental capacity, including the design of the integrated auction process and transparency requirements related to the economic test.

9. *How often should market testing be conducted?*
a) *when potential demand is identified in the annual TYNPD process;*
b) *annually; or*
c) *every two years (when potential demand is identified in the community-wide TYNDP)?*

We prefer option a) as in our view, the market testing (integrated auction process) should be conducted every year when the annual TYNDP has identified potential demand.

10. *If auctions used to allocate existing capacity result in a congestion premium over the reserve price, at what instance (if at all) should TSOs consider a future enhancement? Please refer to the frequency of occurrence of a premium as well as the size of the premium.*

We believe that an integrated auction for incremental and existing capacity would provide a better and more timely indication of the need for a future enhancement. Considering the lead times generally required for pipeline expansion projects, reacting to congestion premiums would not be a good approach to identifying the need for investment.

11. *What other criteria could be used to identify a need for investment (e.g. frequency of interruptions of interruptible capacity)?*

¹ In accordance with Article 13(2) of Directive 2009/73/EC

See response to question 10 above. We believe that an integrated auction for incremental and existing capacity would provide a better and more timely indication of the need for a future enhancement. Considering the lead times generally required for pipeline expansion projects, reacting on the frequency of capacity interruptions would not be a good approach to identify the need for investment.

12. How could the allocation process be organised? Should existing and incremental capacity be allocated jointly (integrated auction) or as part of a separate process? How could an integrated auction work? (Please take into account different tariff regimes, i.e. fixed and floating when answering.)

Existing and incremental capacity should be allocated jointly through an integrated auction process that could conceptually work like this:

- + potential demand for incremental capacity is identified in the annual TYNDP process (this should normally not come as a surprise to TSOs);
- + TSOs determine the efficient costs of capacity enhancements to meet potential incremental demand (would only apply to a limited number of IPs where the need for incremental capacity has been identified);
- + TSOs make a proposal for an economic test in accordance with the harmonized general principles (see response to question 8);
- + economic test is submitted to regulatory authorities for approval;
- + network users can bid for capacity through an integrated long-term auction that includes existing and incremental capacity for the next 15 years (as per CAM NC);
- + preferably the tariffs would be fixed (not floating) to provide certainty to users bidding at the auction. This should be explored within the Tariff FG and NC process;;
- + when the auction confirms sufficient demand to pass the economic test for the expansion investment, all capacity bids for incremental capacity can be accepted;
- + if the economic test is not passed, only existing capacity will be allocated to the highest bidders.

13. Should shippers' bids into the market test for incremental capacity be binding? If so, how should this best be achieved?

Shippers' bids into the market test for incremental capacity should be binding, just as the TSOs commitment to expand capacity should be binding, provided the economic test has been met and the regulatory approvals have been obtained.

14. What in your view should be the approach to regulatory approval?

- a) automatic if the economic test has been met and bidding process run correctly;*
- b) subject to separate regulatory approval processes?*

In our view the economic test criteria for the offer of incremental capacity should be subject to a regulatory approval process – including stakeholder consultation – prior to the start of the auction. After the auction process, the regulatory approval for building incremental capacity should follow 'automatically' when the regulatory authorities are satisfied that the economic test has been met and the auction process ran correctly.