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DIRECTORATE-GENERAL FOR ENERGY

Directorate B - Security of supply, Energy markets & Networks
The Director

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ERGEG Gas Working Group
The Chairman Walter Boltz
Brussels

**Subject: Capacity allocation Framework guideline
Commission's evaluation under Article 6(4) of the Gas Regulation**

Dear Mr Boltz,

Thank you for your letter of 16 June 2010 and the draft framework guideline on capacity allocation rules submitted therein.

In application of the principle governing this project, i.e. that the procedural rules under the third package shall be resorted to as if the provisions of the third package provisions would already apply, the Commission has examined the draft in accordance with the provisions of Article 6(4) of the Gas Regulation and come to the following conclusions:

The draft framework guideline introduces several new elements to the field of capacity allocation, which the Commission believes will be very beneficial to the internal gas market. In particular, the design of harmonised capacity products, the creation of hub-to-hub products by means of bundling of capacities cross-border, and the introduction of market based capacity allocation mechanisms lead the way to more efficient capacity allocation and to enhanced competition.

The draft framework guideline does not, however, in all aspects contribute to non-discrimination, effective competition, and the efficient functioning of the market. In particular:

- The draft framework guideline prescribes that the network code shall foresee in several areas that the final determination of the applicable regime shall be made by the national regulatory authorities concerned on a bilateral basis per interconnection point. The Commission believes that such an approach is not suitable to achieve European harmonisation as envisaged and as required by the third package. The number of individual or bilaterally agreed decisions to be taken will lead to unacceptable delays and cause significant administrative burdens in the course of their establishment and their subsequent application. The Commission therefore calls upon ERGEG to revise

the draft framework guideline so that it enables ENTSG to draft a network code which entails the highest possible degree of harmonisation without requiring subsequent negotiations and decisions by national regulatory authorities.

- The draft framework guideline introduces two new concepts, i.e. that of "bundled services" and that of "virtual interconnection points". The draft framework guideline does not sufficiently clarify how both concepts relate to each other and how their interaction would go about in practise, in particular with respect to the timing for the introduction of virtual interconnection points. The rules for combining bundled capacity into virtual interconnection points shall ensure that the technical capacity resulting at any bundled interconnection point and at any virtual interconnection point is not lower than the sum of the previously separate bundled capacity products.
- The draft framework guideline foresees a transition from flange trading to hub-to-hub trading, as a consequence of the exclusive application of hub-to-hub ("bundled") capacity products within five years. In order to facilitate this process, the draft framework guideline should provide a default rule addressing this transition which should aim at leaving supply contracts intact with respect to essential elements such as the obligation to deliver a certain amount of gas for a certain period of time. The default rule shall at least address the determination of the new delivery point(s), the re-allocation of the booked capacity, and the principles of re-allocation of costs. It shall ensure a level playing field in the transitional period. It should not allow suppliers to invoke the transition in transmission arrangements as a pretext to cancel existing supply agreements.
- The draft framework guideline foresees several alternatives for capacity allocation which should be chosen by national regulatory authorities as they best see fit. This approach bears the danger of undermining the creation of a harmonised capacity allocation regime across the EU. Therefore, the draft framework guideline should foresee market based capacity allocation as the only way. An auction mechanism should be designed by ENTSG in such a way that the mechanism itself can mitigate possible concerns arising from specific market characteristics. Pro rata solutions should thus not be needed. First-come-first-served should be applied only for within day allocation.
- The draft framework guideline does not address possible rules on reserve prices for auctions. In particular, the allocation design including the issue of appropriate, if any, reserve pricing, for capacity becoming available as a result of the application of potential or existing congestion management procedures should be covered by the framework guideline, as this type of capacity allocation will be outside the scope of the Commission's work on congestion management.
- The draft framework guideline should foresee auctions to be used to allocate all capacity products on the basis of existing capacities. With respect to capacity yet to be built, auctions may provide useful signals, but would probably not be sufficient.
- The draft framework guideline should clarify which rules apply to firm and which rules to interruptible capacities.

- It should also clarify whether in the context of the creation of harmonised and bundled capacity products the gas day needs to be harmonised.

The Commission therefore requests that ERGEG review the framework guideline within three months of receipt of this letter and re-submit it to the Commission. May I also encourage ERGEG to apply, fully in line with the spirit of this pilot, the decision making procedures which will be applied by the Agency. This should hopefully facilitate decision making with respect to controversial matters and would yield valuable information on the effectiveness of the decision making procedures foreseen for the Agency. My staff will be happy to meet and discuss the substance and the process related to this next step.

i.O. 

Heinz Hilbrecht

c.c.: Madrid Forum, Monitoring Group, ENTSOG, Mr Pototschnig, Mr
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