



Ofgem consultation – Guidance on the Third Party Access regulatory regime for gas storage facilities in Great Britain

Response by E.ON

General comments

The current relatively 'light touch' regulation of gas storage is one of the successful elements of the liberalised gas market in Great Britain. Allowing storage operators a high degree of freedom in how they price and offer their services in competition with other forms of flexibility in the market, either under nTPA or TPA exemptions, has proved to be central to this success. Ofgem and its predecessors' policy of separating and de-regulating storage services from transportation businesses, together with the removal of price regulation, has allowed new owners and new entrants into the market, with storage services offered at prices and terms determined by the market. The balanced approach to TPA exemptions adopted by Ofgem has in recent years positively encouraged investment in a number of storage projects.

We are becoming increasingly concerned, however, that Ofgem may be moving towards a more intrusive stance on the regulation of storage, and the guidance set out in this document seems to create more questions than it answers. In particular, the lack of detail on Ofgem's proposed methodology means that we are unsure whether the use of pivotal analysis to determine which storage operators have significant market power (SMP) will increase or reduce commercial freedom for such businesses.

We understand that it is not Ofgem's stated intention to increase the scope of regulation nTPA, but it is not possible to judge whether this is indeed the case without a more detailed understanding of the pivotal analysis proposed. Parties need to know clearly where they stand and in particular whether they are likely to be considered, based on Ofgem's methodology, to have SMP.

That then leads to questions as how closely parties will feel obliged to follow Ofgem's nTPA guidance, and whether a failure to follow that guidance precisely could make parties (especially those judged to have SMP) concerned that they may be acting contrary to EU law and all the regulatory risks and sanctions that that would entail. The natural tendency would be to follow the guidance even where parties felt the requirements to be excessive, and it is then only a short step for nTPA to effectively become rTPA.

It is important to note that many of the prospective larger storage projects will necessarily mean that parties acquire large market shares of storage capacity and thus would almost certainly be considered by Ofgem to have SMP. However, it is important to recognise that such investments are only likely to be possible if backed by longer term agreements with a number of players. There is a real risk that such projects would be precluded if parties felt they had to follow the approaches to offering capacity to the market set out in Ofgem's suggested nTPA guidance.

We also do not believe it is helpful to be too prescriptive in defining how parties should offer capacity to the market. This is not only stifles innovation, but is inappropriate and potentially inefficient as different types of storage facilities have different operational characteristics which necessarily require different services to be offered.



Our other major concern is the potential 'read across' to the TPA exemption regime. If the analysis described in the consultation document were to be applied to the exemption regime, it would make TPA exemptions less likely to be granted or even lead to exemptions being revisited. This increase in regulatory uncertainty is likely to make even large players much less willing to invest.

We therefore believe that it is imperative that Ofgem clarifies its intentions with regard to storage regulation, both in respect of nTPA and of TPA exemptions. If Ofgem is to use pivotality analysis in regard to nTPA, (and based on the information available to date, we are not convinced that this is an appropriate basis for determining SMP) its detailed analysis and modelling must be made available to the industry. Parties can then decide whether they are willing to invest, depending on whether they feel that the regime allows sufficient commercial freedom to operate successfully in the market or not, depending into which category they expect to fall (nTPA with SMP, nTPA without SMP or TPA exemption).

Our detailed responses are set out below and are intended to assist Ofgem in its formulation of its nTPA guidance. They are based on information and analysis contained in the consultation and should not, unless specifically stated otherwise, be viewed as offering support for the approach advocated by Ofgem.



Responses to Ofgem's questions

Chapter three

Question 1: Should pivotal gas volume be used when assessing SMP? If no, please explain why.

1. The decision on TPA should be taken only in regard of storage facilities for which access is economically and/or technically necessary for other market participants. Ofgem has already carried out this analysis on a case by case basis, and we do not see the need to introduce further tests or conditions to be met in order to define additional specific rules for TPA. Further tests or conditions increase regulatory uncertainty, and can mean that investors will conclude that they have less commercial freedom than might actually turn out to be the case.
2. As Ofgem notes in section 3.4 of the consultation document, there are a number of instruments available to market participants seeking to manage load variation, and it is possible for a market player to have an apparently large share of the market for one or other of these instruments at a point in time without actually having significant market power. This means that any assessment of SMP will need to consider all sources of flexibility, and not just gas storage in isolation.
3. Market players will compete to improve the availability of valuable flexibility instruments in their portfolio and this should be seen as a positive effect of competition and as a normal response to security of supply pressures.
4. A pivotal analysis could be used to assess the concentration in flexibilities and eventually emphasize the need to promote the development of further (competitive) flexible instruments, thus acting on conditions to improve competition. However, it is difficult to assess Ofgem's current proposal for assessing pivotality on the basis of the information in the consultation document. We would like to see Ofgem provide much more detail on the methodology proposed, including the time periods that will be used, the factors that will be considered and any assumptions that will be used to underpin the calculations. It would be very helpful if Ofgem could share the model with market participants, as this would enable storage operators and potential storage developers to make a more accurate assessment of the likelihood of obtaining exemption from the TPA regime for a project.

Question 2: Is the proposed figure of ten per cent of pivotal gas volume an appropriate threshold for defining SMP? If no, what is an appropriate threshold?

5. A pivotal analysis could be used to assess market power, but as stated above, without a detailed understanding of the modelling that will be used (for example, the time periods over which market power will be assessed), it is difficult to comment on an appropriate level to set the threshold.

Question 3: Is it appropriate to also consider market outcomes to assess whether a market player may have SMP at lower levels of pivotality?

6. See response to question 2 above.



7. It should be noted that the detection of market misconduct – including the analysis of market outcomes – will be part of a specific EU regime to ensure integrity of the wholesale energy markets. The European Commission is developing a suite of legislation that is intended to strengthen regulatory supervision of energy trading and facilitate the detection and deterrence of market abuse, through reporting obligations and clear prohibitions of trading on insider information and market manipulation, in a coordinated way at EU level.

Question 4: Are there any additional factors that should be used when considering if a market player has SMP?

8. See response to question 2 above.

Chapter four

Question 1: What factors should be taken into consideration when defining the maximum capacity of a group of facilities?

9. We question Ofgem's suggestion that all of the facilities in a group should be subject to the same regulatory arrangements. We believe that this would limit innovation in terms of the products and services that are available to customers.

Question 2: What concerns, if any, do market participants have with Ofgem's preliminary views on capacity allocation? What concerns, if any, do storage users have with the use of allocation mechanisms other than auctions to allocate capacity, particularly standard services?

10. We believe that market-based access to storage is essential to ensure market integration, appropriate investment signals on the flexibility market and liquidity. We believe markets will deliver the most efficient portfolio of flexibility instruments (including flexible production, domestic and foreign storage flexibility, flexible procurement contracts, and intraday products) at lower cost than any regulated regime.
11. Therefore we support the statement in 4.32 that *"These provisions are intended to ensure that storage services are allocated to the market participants that place the highest valuation on the capacity irrespective of who the customer is. Further, these provisions promote dynamic efficiency by requiring the allocation mechanisms to provide the appropriate economic signals for facilitating investment"*. Allocation mechanisms used around the continent such as "capacity goes with the customer" limit storage capacity to a specific target group and hamper cross-border transactions and efficient allocation of flexibility across the EU.
12. We would like to emphasise that auctions should not be perceived as the only mechanism for efficiently allocating storage capacity to the market.

Question 3: Does the use of auctions provide market participants with sufficient safeguards that any market player with SMP will provide standard services to the market on a non discriminatory basis? What other measures/safeguards in relation to how any market player with SMP allocates capacity could be considered?

13. We believe that the SSO should work with its customers to determine the products and services that are needed, and there is therefore no need for a rigid regime of standard



products to be imposed. Indeed, a prescriptive regime could be counterproductive, and may stifle innovation. Auctions are one of a number of potential mechanisms that could be used to demonstrate compliance with TPA requirements.

Question 4: Do market participants consider that the prevailing anti hoarding arrangements currently in place at GB storage facilities that are subject to the TPA regime are appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

14. In principle, we believe that the current mechanisms described in Ofgem's paper make the existing GB arrangements consistent with the Gas Regulation requirements.

Question 5: Do market participants consider that the mix of interruptible and firm storage services is appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

15. Yes.

Question 6: Do market participants consider that the existing arrangements for the secondary trading of storage capacity are appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

16. Yes.

Chapter five

Question 1: What levels of consultation should SSOs undertake when developing main commercial conditions for the first time and when proposing amendments to the standard terms and conditions?

17. Where substantial changes are proposed, a traditional consultation process over a minimum of 28 days would be appropriate. However, minor changes should be possible by customer notification.

Question 2: Are there aspects of an SSO's main commercial conditions where small changes are likely to have a significant impact on system users?

18. Amendments following changes in the regulatory framework might be considered of minor importance, for example, but since they can be implemented in different ways, a consultation may be worthwhile.

Question 3: Should SSOs be expected to formally consult or test the market before changing existing services or offering any new services to the market? If no, please explain why.

19. We believe that the products and services offered to the market are a commercial matter for the SSO, who would be likely to market test its products before launching them in the competitive market. We do not believe there is any need to mandate a formal consultation, nor does a requirement to do so exist in the Third Package.



Question 4: Should SSOs be expected to offer a minimum threshold of capacity on a short term basis? How should SSOs determine the minimum proportion of capacity that should be sold on a short term basis?

20. This seems more appropriate to rTPA regimes than nTPA. That said, it might be relevant for established storage operators judged to have SMP to offer a minimum threshold of capacity on a short term basis. In this case, a figure of 20% might be considered to encourage new entry, and add market depth. However, it is unclear to us how this might work in practice. Large storage investments will almost certainly have to be backed by long term contracts for primary capacity with a number of market participants, and requiring the SSO to reserve an amount of capacity that must be made available to the market on a short term basis may undermine this. Ultimately, it is surely how these primary capacity holders make secondary capacity available to the market that matters.
21. Unlike transportation capacity where minimum levels of capacity can be important to prevent potential foreclosure of the market by long term capacity holders, storage is not (in the GB context at least) an essential for market participants, given the availability of substitute sources of flexibility available (e.g. 'swing', LNG, interconnector flows and demand side response from gas fired generation).

Question 5: Should SSOs be expected to offer bundled capacity as part of their standard services? Should SSOs be expected to also offer unbundled capacity as part of their standard services? Please explain your views.

22. As stated previously, we do not support the mandating of standardised products. SSOs could offer bundled or unbundled products, depending on the demand for them. Our experience is that there is currently little demand for unbundled products.
23. However, to facilitate secondary marketing and where the market demands it, the primary capacity holder should be allowed to split their bundled product into its component parts. That is, where products are sold in bundled form (i.e. x units of injectability, y units of space and z units of deliverability), these should be capable of being unbundled for resale in the secondary market without customer switch.

Chapter six

Question 1: What factors should Ofgem take into consideration when assessing a market player's flexible gas requirements and, in particular, need for storage services?

24. We believe that the position of flexibility instruments in market players' portfolios depends on several factors, including the level of risk acceptance, which cannot be simply assessed through a series of pre-defined parameters. Those variables can also change overtime and any regulatory intervention might discourage normal adaptive behaviour in the free market.
25. In our view, one of the most transparent ways in which related undertakings of SSOs subject to the TPA regime purchase storage services is through the primary market allocation i.e. taking part in the auction together with other market participants. However, the crucial



consideration is not the mechanism for release of capacity but that flexibility is made available to the market in an open and non-discriminatory manner.

26. Finally, we believe that where there is a risk of hoarding an excessive amount of capacity (for example, where clear SMP exists and there is no reasonable justification for holding such capacity) it may be appropriate to set a maximum amount of capacity that can be bought from a related undertaking.

Chapter seven

Question 1: Do SSOs provide sufficient information on the services they offer and the terms and conditions of access? Is any further information required? Are there any improvements that could be made to how information is provided by SSOs?

27. We believe that the information already published in GB is sufficient.

Question 2: Do SSOs provide sufficient information on the maximum capacity and the level of utilisation? What further information is required? Are the current timeframes for providing this information appropriate?

28. We believe that existing arrangements in GB are appropriate.

Question 3: Should SSOs publish the information required under section 19(4) on their websites or should NGG undertake this role for all SSOs?

29. SSOs own websites could be used, but we believe it would be more efficient, and simpler for customers, if all the information were to be published on National Grid's website instead of or as well as on the SSO own websites.

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