CEPSA GAS COMERCIALIZADORA

IBERIAN GAS INTEGRATION:
Public Consultation
Sept 15th

CGC'S ANSWERS TO QUESTIONS 1 TO 6

Firstly we appreciate the thorough analysis that CNMC, ERSE and ACER came out with as a common background to this public consultation.
In this sense we would like to thank the team involved with this report for the effort paid on it.

Question 1: Would you agree with the analysis made on current market situation and on the major issues affecting the creation of an Iberian market?

We agree basically on the pro's and con's inherent to each of the three considered models for the Iberian Market integration.
We also agree that the implicit allocation model would be the most convenient and realistic one to be implemented in the short term.
It needs to be added though:

-That this analysis does unfortunately not include any data for 2013 and first half 2014. Nevertheless, in our view the results of the analysis would be still valid for most of the conclusions. This is due to the fact that the large excess of gas infrastructures in both Iberian markets becomes more apparent with the current further-decreasing demand forecasts. In this context we believe as shippers that amortization of already built infrastructures should definitively prevail over any new investments on unnecessary incremental or new capacity (e.g.: a third Interconnection Point between Spain and Portugal should be either cancelled or at least postponed until larger future demand and proper CBAs prove that its construction is needed).

-The integration of the two Iberian markets by itself might not be sufficient in order to achieve a reasonable level of liquidity regardless of the chosen method. In fact, both markets show similarities in their supply patterns, with a significant relative weight of LNG and a large deficit of interconnection capacity with Northern Europe. Therefore, improving interconnections with the main European Hubs should become the first priority as an efficient way for enhancing liquidity in the Iberian market.

Question 2: Do you agree with the implementation of the wholesale market with implicit allocation of capacity as a step for market integration, but aiming for an even more integrated market in the longer term?

Not necessarily. In our view a lot of necessary information concerning the suitability of future integration steps will only come out once this first step is fully implemented. Such includes the actual implications of Implicit Allocation, and probably their interactions with demand trends in both markets in the meantime. The Iberian market could by then be fully reassessed in order to establish whether or not the Implicit Allocation model is the first step towards further integration.

At this stage, then, we can only express the following concerns if any eventual steps were to be taken beyond this first one:

1/Aiming for further integration in the long run will remain subject –for sure- to an actual institutional support by both MSs. Such support is not to be taken for granted, in our view.

2/Most of the intended liquidity & price convergence improvements should be provided already by a suitable, timely implementation of First Step.
Those two being our main commercial issues concerning the Iberian market integration, focus should be set on correctly implementing the Implicit Capacity Step rather than on looking beyond. Therefore, fully squeezing the beneficial effects of Implicit Capacity from the very beginning should be considered first. In this sense, a market scenario featuring full implicit allocation of available capacity at the VIP and a cero interconnection tariff should be targeted as soon as possible in both senses of the VIP.

3/Any further integration alternative beyond this First Step of Implicit Capacity would involve removing the VIP with far more unclear implications. Therefore additional CBAs should be performed once this first step has been firmly established. Finally, such future CBAs should take into consideration then the relevant changes in Interconnection Points in France (e.g. PEGs Mergers between 2015-2018, Pirineos VIP up-grading in 2015…).

Question 3: What are the most important aspects to take into account and to harmonize from a regulatory point of view for the creation of the wholesale market with implicit allocation?

We fully agree with this Public Consultation Paper stating that the above option proves entirely achievable in terms of regulatory harmonization. Being a realistic model is in fact one of the main advantages for its timely implementation, as mentioned in Question 1.
As shown in the Paper's Way Forward, a relevant part of the required regulatory harmonization is either already implemented or under development. That is because of the binding implementation of the CMP and the NCs of CAM (through its SGRI early implementation schedule), Balancing and Interoperability, that will carry on until 2016.
The key aspects for regulatory harmonization would in this context be :

-The common Market Platform to be shared, who runs it and how, and the costs split. The Iberian Electricity markets integration (MIBEL) is surely to be used as a departing stage, from which all well-functioning features can be kept or improved if possible. In this sense, we consider that one single market platform (with two virtual nodes indeed) should be harmonized in both Countries' regulations for Implicit Capacity Allocation. The main reasons why there should be no room for more than one platform are in our view fixed costs efficiency and concentration of liquidity. Unfortunately, our forecast is for low to moderate liquidity remaining, at least in the short to mid-term.

-Daily Implicit Capacity available:
A threshold needs to be agreed by both NRAs so as to the Maximum Implicit daily capacity to be offered. Given the current low levels of the VIP utilization rate, we would support that 100% of the available capacity be implicit. In our view, short term cross-border gas flows might be encouraged by such flexibility (implying full optimization of the VIP as opposite to current low utilization rates). This is due to the fact that this model makes available instant capacity for all users bearing gas from the platform including those not holding explicit capacity.
Consequently, liquidity might well be increased to some extent under this regulatory scenario.
From the European Network Codes perspective, we would like to underline that the fact of making full available capacity implicit entirely complies with the CAM Regulation (UE) Nº984, which allows it provided that relevant NRAs agree on it (Article II, 4). Of course, any capacity allocated prior to the implementation of this model would be removed from the implicit capacity platform. Finally, CMP at the VIP should also be conveniently harmonized. In this sense any capacity eventually released through CMP should be immediately added to the implicit capacity allocation so as to contribute to its maximization. This is not a short term issue though, since congestion at the VIP looks quite unlikely now.

-Regulated Price of VIP Capacity:

- Coordination of regulated tariffs for bundled capacity in both senses is suitable, in spite of the fact that they do not need to be set up at an identical level. Ideally, a price as close to cero as possible should be regulated in both senses of the VIP, as mentioned in Question 2, in order for liquidity to be fostered and prices to fully converge as long as capacity is available (at least at an initial stage to help induce the non-existent cross-border flow of gas)
- Short Term 'secondary market' capacity price signals (e.g. spread between Cross-border lower offers for NG at the cheaper side of the border and the higher bids at the more expensive side) need to interact with regulated tariffs at the VIP, as mentioned . Such spread will show the actual price for spot capacity which the market can afford from the cheaper to the more expensive side of the VIP. In this sense, any previously allocated reserve prices should be taken into consideration as feasible through a model that makes them compatible with spot capacity market prices. Such crucial model should be designed by precisely harmonized regulation in both countries, which must also take into consideration the Framework Guidelines issued by ACER on Capacity Tariffs.

-TSO's & Operator issues

As per the Public Consultation Paper, integration of balancing regulations is not a 'must' under this model. Therefore, integration of both regulations should be focused mainly on structuring VIP single nominations, which should be channeled through the Market Platform Notifications to both TSOs by the market Operator. All those VIP-related issues need to be coordinately implemented across both MS's Natural Gas regulations from the upper level (ley 98HC in Spain) reaching down to the Market Platform Rules and their developments (Circulares de Mercado, etc), that are currently being drafted already in Spain.

In this sense, some topics to be considered are:

- The potential coordination of TSOs when balancing their respective systems in order to neutralize their positions whenever they are opposite to each other, as long as it improves efficiency.
- Regulated System gas from each node to be traded in the platform (fuel gas, system linepacks, Last Resource Gas) need to be harmonized as well indeed.
- Interoperability harmonization by both TSOs at the VIP, with the precise updating of the corresponding Interconnection Agreements.

Question 4: Which is the best model for the integration of Iberia in the longer term? Market area model, trading region or others?

We would not be against a single balancing zone for Iberia, as would involve the Market area model. But such full integration would only be worth it as long as this option turns out less costly in terms of our TPA costs overall. We cannot afford paying higher tariffs altogether in any case.
We insist that in our view the most significant increases to market liquidity/price convergence should come out from a coordinated inter-European hubs integration rather than from a full Iberian integration whose timing is not linked to the former.
Having said that, and provided that relevant CBAs support it, a trading region would look probably reasonable in the mid-term as a second, transitional step towards full integration both from an institutional point of view and from the different stakeholders' implications.
But this choice will only become a priority once the first step is fully accomplished and Interconnections with TTF, Powernext and the rest of the relevant European hubs have been improved.

Question 5: When and how the Balancing Network Code and the Interoperability Network Code should be implemented to contribute to the goal of the Iberian market?

The 'when' depends much on the TSOs availability for implementing the relevant changes required. The sooner the better from the entry into force of both NCs as long as system operators are ready. If a transition period is required, as is the case in Spain, a realistic approach should be taken on the Balancing NC as to whether it is fully implemented earlier or later over 2016.
From our side, we are fully ready for all the flexibility reduction and therefore encourage full implementation of the Balancing NC soonest within the mentioned period and conditions. We do not encourage therefore, setting up any flexibility boundaries for balancing that would eventually make it more complex for further merging of the two markets. If going for a single balancing zone in the long term a simple and fair departure point would be no flexibility everywhere.

Question 6: Identify any issue you think is important to achieve further integration. How would you set the timing and prioritization for the discussion/implementation on these issues?

We come up here with a 5-steps road map. Such would apply only once Implicit Capacity gets implemented.

1. Check 1st step is efficiently functioning
2. Check PEG/TTF/NCG Interconnection Points are fully available
3. Check Price convergence
4. CBAs on further Integration into one Entry-Exit Area with either one or two Balancing zones
5. Assess institutional support