

REN's answer to ACER, ERSE and CNMC Public Consultation on "Study about models for integration of the Spanish and Portuguese gas markets in a common Iberian Natural Gas Market" – 15 September 2014

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?

In general, the report gives a clear and comprehensive insight of the Spanish and Portuguese natural gas markets' current situation and can be taken as a starting point for a further integration analysis that is to be carried on in the future. Nevertheless, some aspects regarding this analysis could be clarified, namely for instance the average utilization rate of the interconnection points. As these cross-border points are currently almost exclusively used as entry points, utilization rates should be assessed per flow direction, i.e. in the direction Spain to Portugal and not considered the overall transmission capacity in both directions. For instance, under this premise, total natural gas imports from Spain at Campo Maior interconnection point (IP) during 2012 and 2013 registered an average rate of 56%.

Actually, when considering market integration analysis and the possibility of existence of congested pipeline connections within a market region, one should also look at peak utilization rates, as these bear more significance when considering infrastructure utilization than mere average rates, which may be misleading regarding the final goal of the analysis. This relates also to the market impact. It is obvious the effect of peak capacity shortage in market splitting.

Between 2011 and 2013 peak daily capacity at the cross-border entry points has been above 80% of the technical capacity at Badajoz/ Campo Maior IP and 60% at Valença do Minho/ Tuy IP, reaching 70% utilization rate considering both IPs aggregated.

We also agree and stress out the importance of the LNG share in the Iberian Peninsula as a diversification of energy sources contributing to lower gas prices through a greater energy mix (besides contributing also for security of supply), serving as a flexibility tool for market agents, especially smaller ones, and also the advantage of having a large overall LNG storage capacity that may offer more opportunities for traders to manage arbitrages or for allowing newcomers to enter the market through spot contracts with LNG suppliers.

Nevertheless, a few other details appear on the report and should be reviewed:

- 1) Although of a much smaller scale when compared to UGS (underground storage) or LNG Terminals, linepack storage should not be considered as a storage facility, as it is meant for keeping the transmission network operational. A pipeline at its full capacity has a linepack margin of zero!
- 2) REN and Enagás have agreed to present single capacity values across the year, not distinguishing anymore summer and winter capacity values

The expansion of the Portuguese LNG Terminal and its storage capacity increase was concluded in June 2012 (not at the beginning of the year, as referred to under 4.1.6.1.)

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?

No. REN considers the implementation of a wholesale market with implicit allocation of capacity only for day-ahead and within-day capacity and only as a small fixed percentage of the existing capacity. For the longer term trade and integration of the wholesale market, capacity should be bought separately because this is never a spot decision. As a possible first step for a future market integration, rules that support the model should be commonly agreed between NRAs, Competent Authorities of Spain and Portugal and the TSOs. Such specific rules that enable the offer of implicit capacity products as referred in our note, along with regular capacity auctions, in addition to other provisions regarding trading mechanisms within the Iberian region (in LNG Terminals or UGS facilities), should be sufficient to promote liquidity in the wholesale market in the Iberian Peninsula, with obvious advantages for the market in general.

It is though important to assure that an independent market operator be designated, who assures the full and non-discriminatory access to the trading platform according to national rules in force in both countries, who is responsible for the management of the trading platform, continuously publishing prices of traded products and promptly notifying the global system managers of both countries of agent's final gas positions.

The evolution to a more integrated market shall follow a Roadmap, established by NRAs and Competent Authorities of both countries and the participation of stakeholders, and be subject to a permanent and thorough market monitoring conducted by national and European supervisory bodies.

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?

In REN's view, the main aspects that should be taken into consideration are the following:

- A continuous trading in a common Iberian trading platform shall be implemented for daily products. Clearance will be performed by the market operator for daily positions;
- The gas day should be harmonized between both countries;
- The gas reference temperature to be used should also be harmonized;

- Cross-border tariffs should be gradually eliminated, as tariff models between Portugal and Spain are harmonized;
- Two Virtual Trading Points (VTPs), one in each balancing system, should exist,. Prices of daily gas products traded on the Iberian trading platform should appear at the same time on both VTPs, with the corresponding tariff (if applicable) embedded in the gas price;
- For a start, the model shall consider only daily (day-ahead and within-day) capacity products. All other capacity products, as foreseen under Reg. 984/2013 (CAM NC) shall be allocated according to CAM rules;
- As a way to test the market's receptivity, the level of capacity to be offered in an implicit model should be limited, with a gradual increase, as the model is been tested and market participants require more capacity; Such gradual increase in technical capacity to be allocated to the daily implicit model shall be agreed between TSOs and NRAs;
- A market operator shall be designated, who will be responsible for the trading platform access and management.
- While trading gas at the Trading Platform, TSOs shall be exempted of cross-border tariffs for physical balancing purposes, as the gas flown through the interconnection is meant for balancing activities, not for consumption and is marginal compared to the available capacity.

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

REN is of the opinion that a trading region model would best fit future market needs and that it is still too early to speak of a full market integration, which could although be envisaged as the ultimate goal of market participants.

Any solution for the future should be compatible with the integration of the Iberian market with the French gas market and with EU integration.

Therefore, a set of intermediate measures regarding harmonization and coordination between operators and regulators in both countries are key to ensure a stable and sustainable transition from current market arrangements to a trading region model. Some of these measures are currently underway or are concluded (harmonization of capacity allocation mechanisms and cross-border tariffs, creation of virtual interconnection point), but it is desirable that other initiatives on a regulatory level could follow and be taken in a coordinated way between both countries, especially, but not limited to, those related to European network codes implementation.

Other requirements at operational level are also crucial, such as an agreement on the technical management of the interconnections, including operational measures in case of emergency.

The trading region model has the virtue of maintaining separate balancing regions within countries, because only the delivery flows from the virtual balancing point would

be subjected to balancing, the supply to the virtual balancing point would have no deviations. This is an important condition that should be held. However, before choosing a model, Portugal and Spain should consider looking at pilots in other regions, where these have been implemented and try to take possible lessons from these initiatives. For instance, the integration of southern French regions PEG Sud and PEG TIGF, as from April 2015, by means of a trading region model will be an interesting opportunity to be followed closely, as well as the example in Germany.

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?

A complete implementation of both Network Codes (NC) is in REN's opinion not accomplishable in the short term (ST), as many provisions within both codes require great regulatory changes in both countries, part of which are currently being addressed by NRAs and TSOs. It is a fundamental condition to implement at least some provisions foreseen in both Network Codes (e.g. gas day harmonization, nomination management procedures, IT development) to be able to create a proper functioning Iberian gas market. A full integration, though, would require not only the complete implementation of these two NCs but would also call for more coordination between TSOs and NRAs and could be envisaged in the future. Still, it is important to assure that the necessary steps be taken cautiously by all involved parties and allow stakeholders to participate from the beginning in order to avoid unnecessary hurdles or setbacks when implementing agreed measures and thus obstructing the creation of a functioning and liquid market.

For Portugal, considering the current level of maturity of the Portuguese gas market and the corresponding low liquidity of short term (ST) capacity products, REN thinks that at least a 2 year implementation plan for the full application of the NC on Balancing (after its entering into force) would be desirable.

Regarding the Interoperability NC, important aspects related to IT development that are mandatory in order to allow TSOs to comply with CAM NC as from its entry into force (e.g. on the auctioning of daily capacity products) are already part of a common roadmap and are underway but at least one year will be required.

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?

REN thinks that there are some issues that being essential to enable the functioning of a wholesale market should be considered as being of common interest for market players and costs thereof should be smeared across network users, as they all globally

will benefit from it. These would include the use of a common capacity trading platform and a capacity booking platform, two main blocks for the capacity management within the region.

Another important aspect is the need to ensure an efficient use of storage infrastructures, and LNG Terminals, across the Iberian Peninsula.

Additionally, attention should be drawn to the need of avoiding the existence of any type of limitation or congestion on the transportation of gas within the Spanish and the Portuguese transmission systems, allowing for traders to freely book gas (and capacity) at the trading platforms regardless of its entry point in the corresponding balancing area.

Allow for proper tariff structure and level harmonization within the Iberian peninsula for the interconnection flows to pay for actual costs avoiding cost pancaking in cross border flows, (proper entry exit models and options may overcome this problem).

Define a framework for capacity availability in cooperation with system managers of both Portugal and Spain to avoid congestions and maximize the intraday trade possibilities.

Give the tools to Global System Managers to buy and sell gas in the market for balancing purposes without price limitations and give liquidity to the market.