



Draft RF/GG vision of “Coordinated Open Season” for “New Capacity” within ENTSOG “Incremental Proposal”

**Andrey A.Konoplyanik – Alex Barnes,
Workstream 2 “Internal market”, Russia-EU Gas Advisory Council &
Russia-EU Informal Consultations
on EU Regulatory Topics /(3rd EU Energy Package)**

**2nd JSWS on ENTSOG “Incremental Proposal” (CAM NC amendment),
Brussels, ENTSOG, 26 February 2014**



COS: Objective and Context

- Aim to develop CAM NC amendment for coordinated open season(s) for new capacity that enables new sources/routes of gas supply to reach Europe:
 - New capacity is capacity which does not yet exist
 - For projects which cross three or more entry-exit zones & thus should be large in size (economy of scale) compared to existing TSOs
- Capacity developed by this route would be subject to all aspects of TEP (CAM, CMP, Balancing) as the proposal is aimed at developing a regulated approach for new capacity, as an alternative to Article 36 Exemption.
- Proposal is consistent with TEP, ERGEG Guidelines for Good Practice for Open Seasons (GGPOS-2007) and ACER Guidance on Incremental Capacity.
- Issues discussed with regulators, ACER & EU Commission & ENTSOG representatives and other stakeholders as part of the EU-Russia Informal Consultations/GAC process since 2010 (see reserve slides), esp. during 2013
 - Series of workshops within Case Study Task Force, June-Sept'2013
- Proposal sent to ACER on 17th September 2013 as part of input to ACER thinking on Guidance on Incremental Capacity (a final in a series of COS-related doc's from Consultations/WS2 GAC).



Auction & Open Season are *two different economic models* => separate procedures within TEP/CAM NC

Market test

Incremental vs New Capacity

Criteria: 1IP, size...

Incremental Capacity

Auction

Incremental Capacity *offered* by TSO to market participants (potential shippers) = *top bottom* approach => *system-based*

Criteria: new IP, 2IP+, size...

New Capacity

Coordinated Open Season (COS)

New Capacity *requested* by market participants (potential shippers) from TSO = *bottom up* approach => can/should be *project-based* (see reserve slides)

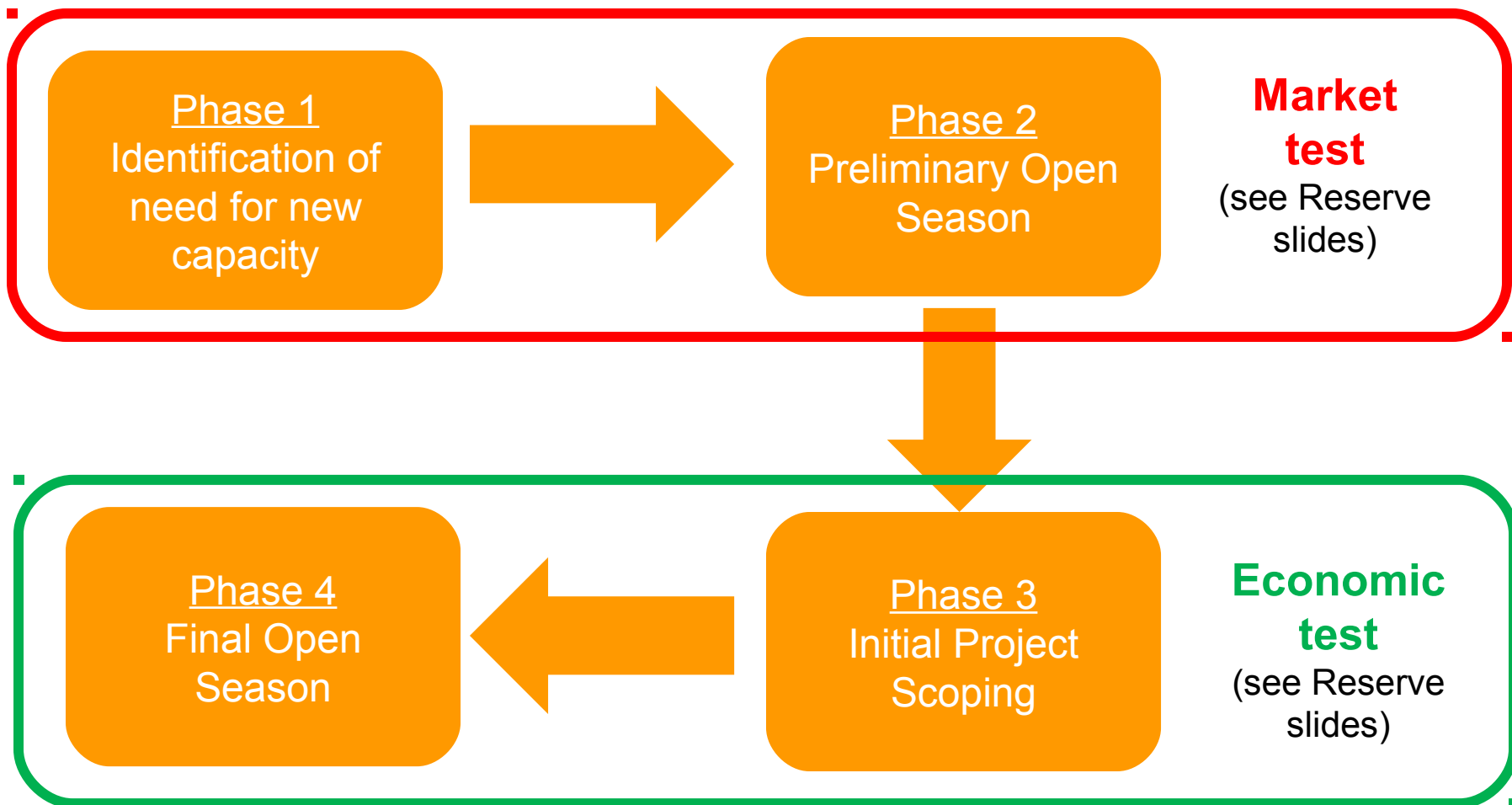
CHINESE WALL BETWEEN TWO PROCEDURES

At least until economic test on COS gives negative result (see reserve slides)



Outline structure of the Open Season

(as proposed in RF/GG 'COS-Strawman' Paper)





COS Phase 1: Identification of need for new capacity

Three alternative ways in which a project may be initiated:

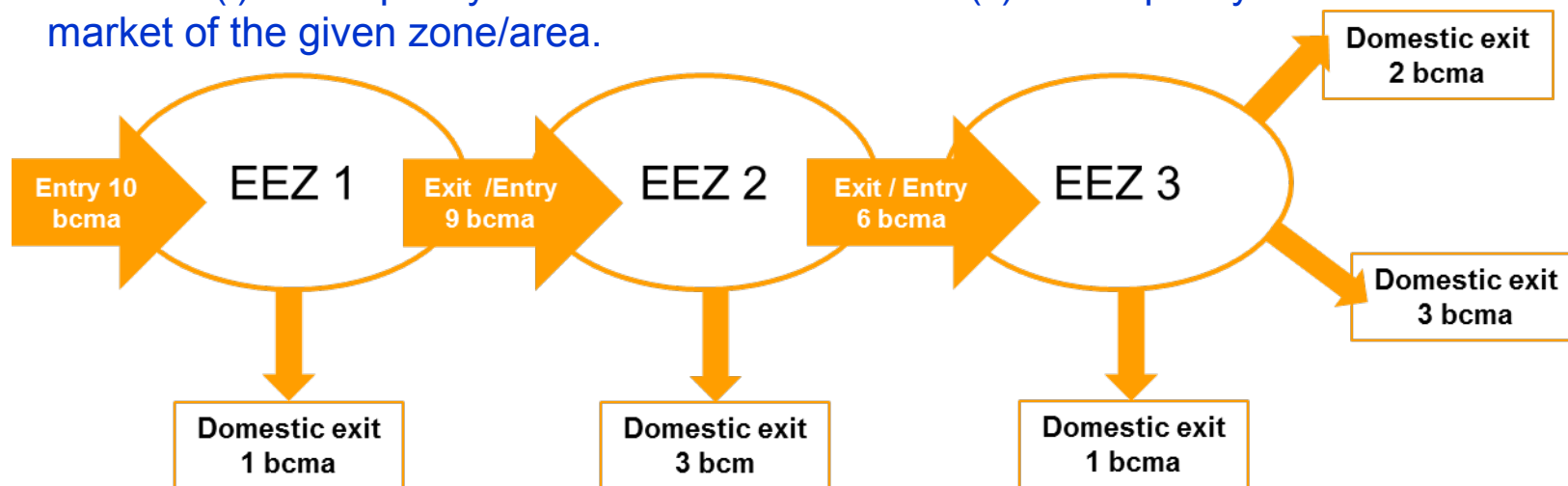
- **Shippers** request capacity for new supply routes either within the EU or from outside the EU to market zones within the EU.
- **Project developer** announces intention to develop project, subject to confirmation of shipper demand, for capacity following discussion with potential shippers (e.g. large non-EU producers)
- **National TSOs** announce intention to develop project, subject to confirmation of shipper demand, for capacity following publication of analysis in Ten Year Network Development Plan

In all cases it will be helpful if a close dialogue is held with NRAs, ACER and the EU Commission to help their decision making in later phases.



COS Phase 2: Preliminary Open Season

- All open seasons must consider bids from any type of shipper so long as they meet the bidding criteria of the open season
- Project developer / TSOs publish Open Season process procedures and timetable and request non binding Letters of Intent (LoI) from shippers stating their capacity requirements.
- Shippers submit LoI's detailing quantity of entry and exit capacities they require in each entry-exit zone. In addition shippers will be required to distinguish within each zone between (i) exit capacity to another zone/area and (ii) exit capacity into the domestic market of the given zone/area.



The aim of this preliminary phase is to gain an estimate of likely demand for additional capacity in order to enable initial estimates of the likely costs and quantities of capacity that may be offered



COS Phase 3: Initial Project Scoping

- Based on shippers' Letters of Intent TSOs / project developers performs initial design studies to plan:
 - best route for infrastructure, incl. combination of new & available (existing un-booked) capacity
 - forecast costs and
 - level of investment in new infrastructure required, incl. use of existing un-booked capacity.
- Opportunity for further discussion with interested shippers (those who signed Letters of Intent) to refine project design prior to finalization of project design:
 - Iterative process to ensure the best match between shippers' requests and what capacity can be offered at a given cost vs what tariff should be paid to cover all capacity requests from the shippers
 - Minimize any mismatches and risks that shippers will not receive the capacity they are prepared to pay for.
- Based on final project design NRAs confirm regulatory treatment of project so that shippers have regulatory certainty prior to making binding commitments in final open season phase:
 - (e.g. how tariffs will be set, incl. system-based vs project-based approach
 - tariffs control review periods,
 - how to deal with under or over recovery issues,
 - linkage with TSOs existing Regulated Asset Bases in case of system-based approach etc.)

Phase 3 is aimed at ensuring that all parties have a clear view of what is required to enable them to make binding decisions in the final phase (Phase 4 below).

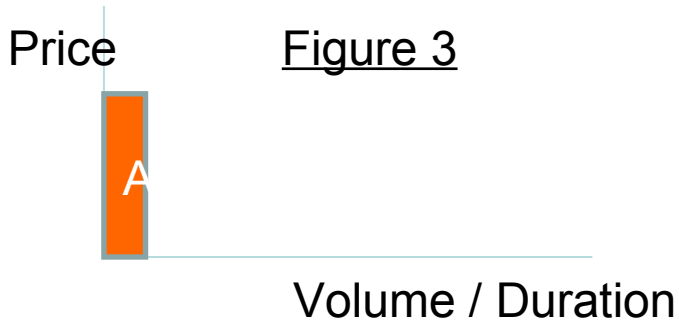
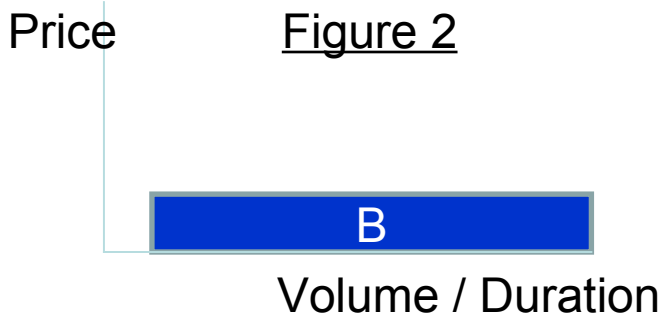
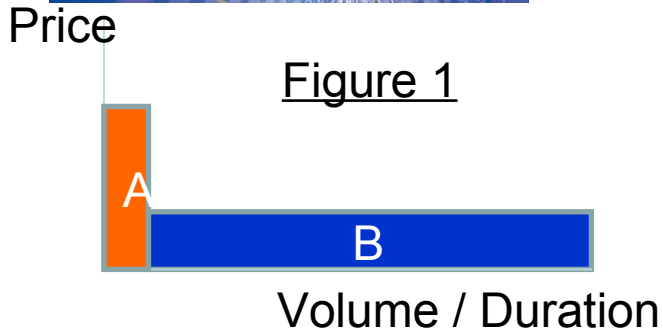


COS Phase 4: Final Open Season

- NRAs, ACER and EUC confirm regulatory treatment of the project.
 - These regulatory terms and conditions (see (3) of Phase 3 above) form a part of the binding open season commitments that shippers are required to sign to be allocated capacity.
- TSOs / Project developer start final phase by providing necessary information to shippers:
 - defined timetable,
 - tariffs (system-based vs project-based),
 - terms and conditions for capacity once booked,
 - minimum bid requirements,
 - capacity allocation methodology and
 - the parameters of the economic test
- Shippers are required to submit binding offers for capacity subject to the terms and conditions of the open season.
- Following close of process for submission of binding offers, TSOs / project developer allocates capacity:
 - If economic test not met, no capacity allocated. Consider if offer second opportunity to amend bids to help meet the test or to move to CAM NC auction (see reserve slides).
 - If economic test met, allocate capacity first to shippers whose bid value has greatest Net Present Value (quantity booked * duration * price * Discount rate) as this indicates greatest contribution towards meeting economic test and greatest willingness to pay in NPV terms (see next slide).



Why willingness to pay does NOT equal pay as bid



Figures represent the economic test
Figure 1 shows the result if allocation is based on highest bid for an annual strip of capacity
A is allocated Year 1, B is allocated the remaining years

Economic Test is met overall

BUT

B contributes more to passing the economic test but will not want to accept capacity as he receives no capacity in Year 1

AND

Although A has paid more for capacity than B, A's bid is not sufficient on its own to meet the economic test

Use of CAM algorithm does NOT take account of need for shippers to book contiguous strips of capacity => NPV-based approach suits best for this



RESERVE SLIDES



History

- **20.09.2007:** CEC announced preparation of Third EU Energy Package (TEP) & its basic provisions, which have been permanently criticized since then by RF authorities as creating new risks & uncertainties for energy supplies to EU
- **02.09.2009, Alpbach:** W.Bolts proposed to A.Konoplyanik to organise a meeting between EU & Gazprom to explain to RF/Gazprom EU intentions regarding TEP in gas; counter-proposal to organize a series of regular informal consultations between both parties where RF/GG will also explain its justified concerns & visions of TEP-related new risks & uncertainties for gas supplies
- **19.01.2010, Vienna:** 1st round of RF/GG-EU Informal Consultations on TEP (EU Co-chair: W.Boltz; RF/GG Co-chair: A.Medvedev, coordinator: A.Konoplyanik);
- **24.02.2011, Moscow:** Russia-EU Gas Advisory Council (GAC) established; Coordinators: RF Energy Minister & EU Energy Commissioner
- **17.10.2011, Vienna:** 1st GAC meeting, three WSs organised, WS2 “Internal market” created based on Informal RF/GG-EU Consultations (EU Co-chair: W.Boltz, RF Co-chair: A.Konoplyanik)
- **31.01.2014, Vienna:** 19th round of Consultations & 12th WS2 GAC meeting

COS is a key issue at Informal RF/GG-EU Consultations/WS2 GAC process



Some of available doc's at RF/GG COS proposal within Consultations/WS2 GAC since 2010

- New Legislative Framework in the EU Gas Sector (3rd EU Gas Directive and its influence on non-EU companies within the EU market). Exchange of views on regulatory issues between Russian and EU Gas Regulation Experts (Item 4: New Infrastructure). – 1st round of Consultations, 19.01.2010, Vienna
- ...
- “Draft proposal on the procedure to meet market demand for gas transportation capacity based on EU-wide coordinated ‘Open Seasons’” (joint WS2 paper for 20.07.2012 GAC meeting). – 11th Consultations/4th WS2 GAC, 26-27.06.2012, Moscow
- ...
- CEER Blueprint on Incremental and New Capacity: Proposal for Open Season Procedure (‘COS-Strawman‘ Paper) - 18th Consultations/11th WS2 GAC, 10-11.09.2013 , Saint-Petersburg (transmitted to ACER 17.09.2013)



COS: Market test vs economic test

- “**Market test**” & “**Economic test**” are two consecutive steps in COS capacity allocation procedure
- **Market test** (*first step*) : TSOs to test appetite of the market participants – potential shippers (capacity users) for transportation capacity
- **Economic test** (*second step*): TSOs to evaluate whether potential demonstrated shipper’s appetite for transportation capacity at each IP/CBP (and/or at ring-fenced “route/combination of market zones/traded areas”) is “economically reasonable and technically feasible” (Art.13.2 Third EU Gas Directive)



Market test: specific features

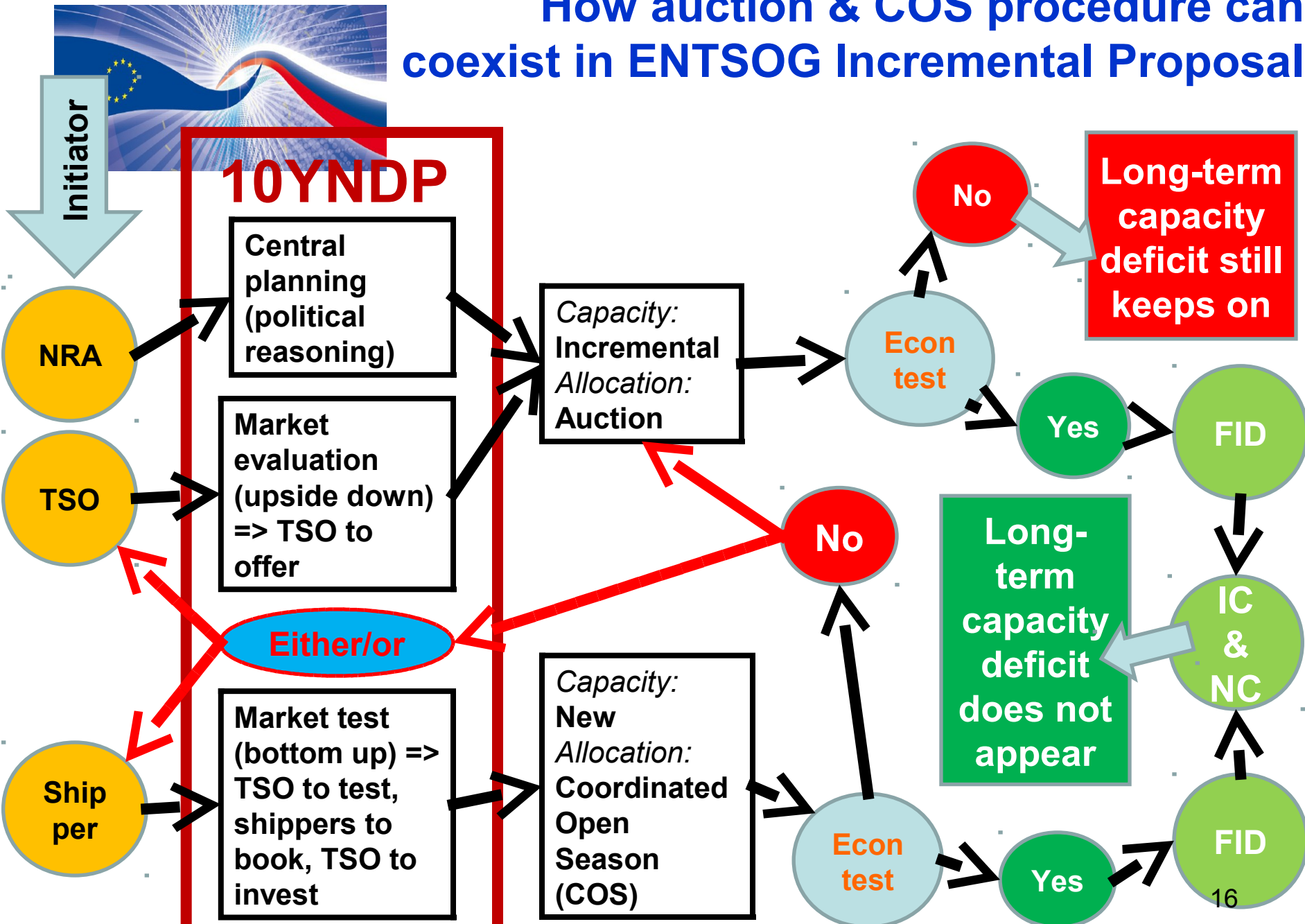
- Proposed to be organized:
 - as integral part of 10YNDP,
 - both for existing & not yet existing capacity,
 - both at each existing & potential new IPs (e.g. within the EU) & at each existing & potential new cross-border points between EU & non-EU (CBP)
 - for allowed future period, e.g. up to 15Y forward,
 - on a regular basis (annual or bi-annual),
 - on a synchronized basis, e.g. simultaneously at all IPs/CBPs within & at the borders of the EU



Economic test: specific features

- To summarize shippers requests for capacity provided at “market test” phase of COS & to structure best effective configuration of draft capacity allocation at each IP/CBP:
 - Existing vs Incremental vs New Capacity ,
- To asses whether sum-total shippers’ demand for capacity proves economic justification for creation of “new capacity”:
 - New Capacity: ring-fencing & creation of cross-border ITSO where proper (incl. project-based tariffs for pay-back period); after pay-back
- Based on NPV analysis to proposed to market participants best effective (e.g. financeable & cross-border coordinated) configuration of new capacity

How auction & COS procedure can coexist in ENTSOG Incremental Proposal





Incremental Proposal & New Capacity: proposed correlation between CAM NC & NC HTTS

	Existing Capacity	Incremental Capacity	New Capacity
Capacity allocation mechanism (<i>CAM NC + amendment</i>)	Auction	Auction	Coordinated Open Season (+ cross-border project ring-fencing + new project-based ITSO)
Tariff methodology (<i>draft NC HTTS</i>)	System-based	System-based	Project-based (project ring-fencing through pay-back period)

(*) CAM NC = Capacity Allocation Mechanism Network Code; NC HTTS = Draft Network Code on Harmonised Transmission Tariff Structures

Draft solution for TSO coordination for new cross-border capacity within E-E EU zones: COS, ring-fencing, ITSO



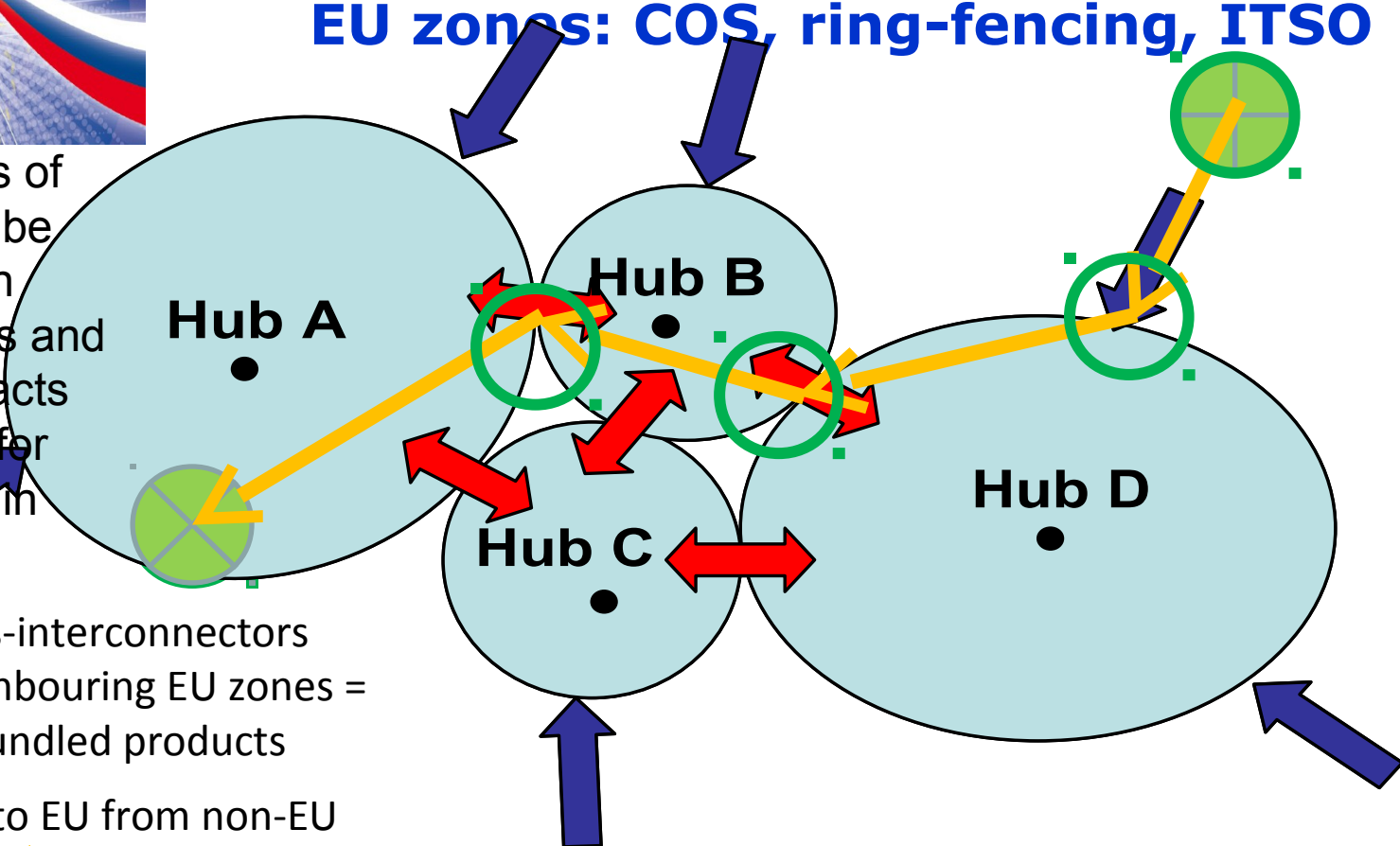
Parameters of new IPs/CBPs to be coordinated within chain of the zones and with supply contracts backing demand for new capacity within each zone

Pipelines-interconnectors between two neighbouring EU zones = single IPs with bundled products

Supplies to EU from non-EU

Non-EU producer
Its EU customer

New Capacity = multiple IPs with bundled products to be balanced, cross-border coordination of TSOs to avoid two types of contractual mismatches:
 (1) at each IP: between term supply & transportation contract, and
 (2) at all IPs on the route from zone to zone: between bundled products at each IP



Thank you for your attention

Andrey A. Konoplyanik

+ 7 499 503 6006

andrey@konoplyanik.ru

a.konoplyanik@gazpromexport.com

www.konoplyanik.ru

Alex Barnes

+ 44 774 775 6032

alex.barnes@gazprom-mt.com
