

MEMO

COMMENTS TO THE INCREMENTAL CAPACITY PROCESS 2019/2020 FOR ELLUND - ENERGINET GAS TSO

1. Introduction

Energinet Gas TSO (the Danish gas TSO, hereafter Energinet) hereby responds to the German TSO's incremental capacity consultation via FNB Gas, and towards Gasunie Deutschland (hereafter GUD), as we disagree with the legal reasoning and the process in general, leading to the decision of reducing the firm capacity at Ellund southbound on the German side towards GUD, to zero. This letter will at the same time be sent to the Bundesnetzagentur and the Danish Utility Regulator (hereafter DUR), as we find it necessary at this point in time to inform the regulators about our position as well.

Energinet especially highlights that:

- GUD reduced the firm capacity at Ellund southbound to zero, without informing or consulting Energinet as a first step, in line with the requirements of NC CAM Article 4 and 6
- The capacity reduction was mainly based on historical use, and not on possible future demand.
- Energinet's involvement in the incremental process for Ellund in 2019 was strictly mechanical, as the process until the Demand Assessment Report is required from NC CAM, no matter the market conditions. Thus, Energinet's input to the report, does not approve or acknowledge the reduction of the firm capacity to zero.
- Energinet never agreed on GUD reducing the capacity, nor to the use of the incremental process as a mean to secure investments in restoring the capacity. Energinet has made this clear to GUD on several occasions.
- Energinet finds that the incremental capacity process is not the correct procedure to determine the future capacity needs for Ellund, neither legally, nor practically.
- Energinet therefore cannot be part of a joint proposal within this ongoing process.
- Energinet acknowledges that capacity must of course be continuously discussed and adapted to the needs of the market, but this must be done in cooperation between the TSOs according to the correct procedures set out in NC CAM chapter 2.

2. Timeline

The following timeline, shows the development of the relevant topic, in chronological order:

1. 2nd February 2019: Energinet discovers that GUD has reduced the southbound firm capacity at Ellund, from approximately 3,600,000 kWh/h to zero, from 1 January 2020. This is discovered at the ENTSOG Transparency Platform.
2. 6th February 2019: Energinet meets with GUD in Hannover, where Energinet asked for an explanation of the capacity reduction. GUD explains that the reduction is due to the Ellund compressor station, which requires significant maintenance, to be sure that the capacity can be guaranteed as firm. Also, GUD considered that the demand for southbound capacity would be low in the future, based on Baltic Pipe and the Danish analysis assumptions. GUD also informed that the capacity had been reduced to zero at this point in time, in order for the market to forward their non-binding demand indications in the coming incremental process the same year. Thus, GUD's rationale was to reduce the capacity first and then collect possible non-binding demand indications, to ensure an investment signal for the maintenance. Energinet did not agree to GUDs reasoning and clearly stated at the meeting that we disagree and found it incorrect to use the incremental process for such a purpose.
3. 5th April 2019: Energinet publishes the document "User involvement in network planning" to inform the market of the future capacities for all entry/exit points in the Danish system, so the market is prepared for the incremental capacity process and can respond to possible needs for new capacity.
4. 1st July 2019: the annual auctions at Ellund are concluded at PRISMA. Hereafter, the incremental process starts, where the market had 8 weeks to forward demand indications for incremental capacity (until 26th August 2019).
5. 26th August 2019: both Energinet and GUD receives non-binding demand indications for Ellund southbound capacity of 2,500,000 kWh/h, from October 2022.
6. 21st October 2019: Energinet, GUD and Open Grid Europe (hereafter OGE) publishes a joint Demand Assessment Report for Ellund, concluding that the incremental process should only continue on the German side of Ellund, as Energinet have enough capacity to meet the demand of 2,500,000 kWh/h, so no incremental capacity is needed on Danish side of Ellund. Energinets involvement in the incremental process was strictly mechanical and limited only to capacity demand on the Danish side, as the process until the Demand Assessment Report is required from NC CAM, no matter the market conditions. As a TSO, you cannot choose not to execute the incremental process at interconnection points, even though you disagree with how the assessment is executed by the adjacent TSO.
7. 15th November 2019: Energinet is informed by OGE and GUD, that the market consultation for incremental capacity that should be concluded in the beginning of 2020 is postponed to the summer 2020, due to a large number of incremental indications received in all of Germany.
8. 23rd June 2020: Energinet meets with GUD, where Energinet again questioned the reason behind removing the southbound capacity. GUD now explained that the reasoning behind was the new LNG terminals in GUD's area. GUD also explained their legal position, being that there had not been long-term bookings for Ellund southbound for some years, and therefore it was GUD's legal interpretation of EU and German law, that capacities were allowed to be removed from Ellund for other demand. Energinet again questioned the process and expressed our disagreement with the reasoning.
9. 31st July 2020: Energinet is informed by OGE and GUD, that the market consultation will start in mid-August, and is forwarded the draft consultation document. In the document there is a calculation of the costs to secure southbound capacity at Ellund. It is mentioned in the document, that possible southbound capacity will not be available before 2027, which was new information to Energinet.
10. 14th August 2020: GUD publishes Project Proposal regarding market area Denmark for consultations, with closing 10th September 2020.
11. 1st September 2020: Energinet meets with GUD, to inform about our formal consultation and communication with the regulators in Denmark and Germany in this matter.

3. Legal assessment

Energinet would like to point out the following with regards to EU-regulation and the above stated timeline:

As an overall conclusion Energinet finds, that it is not in accordance with the EU regulation that a TSO on its own removes 100 % of the firm capacity at an interconnection point with the result that the incremental capacity process is then needed to secure investments in new technical capacity.

Such process is not in accordance with the fundamental purposes of the EU regulation in this area: to ensure the proper functioning of the internal gas market. For this purpose, the market requires access to cross-border firm capacity.

In the network code on capacity allocation mechanisms and gas transmission systems (NC CAM) this is reflected on several levels. In the preliminary considerations no. 3) the importance of further progress in the cross-border competition and market integration is underlined, and in no. 4) it is stated, that this requires a well-functioning network of interconnected transmission grids that allows gas to be shipped according to price signals.

In pursuing this purpose, the NC CAM in chapter 2 states some principles of cooperation that have not been met by GUD in this matter:

Regarding GUDs need to conduct significant maintenance on the Ellund compressor, this should have been coordinated with Energinet according to the guidelines in art. 4.

Regarding GUDs need to change the capacity due to LNG-terminals, this should have been done in cooperation with Energinet according to the guidelines in art. 6.

As for the use of the incremental process, NC CAM clearly distinguishes between existing and incremental capacity, defining the latter as “possible future increase via market-based procedures in technical capacity or possible new capacity created where none currently exists”.

Energinet finds it is not in accordance with the EU regulation that a TSO on its sole discretion by removing existing capacity can create a situation where “none currently exists” in order to use the incremental capacity process, whether it is to secure an investment signal for ordinary maintenance or for creating new technical capacity.

This would mean (as is the fact now regarding Denmark and southbound capacity in Ellund) that a TSO on its own could decouple an EU member state from the European gas market, to make room for gas from a non-EU country.

Furthermore, GUD removing capacity has a value for the market in terms of short-term optimization, and then asking the market for long-term capacity contracts to express the value, is not the intention behind the incremental capacity process.

With regards to all the above Energinet finds, that the incremental capacity process is not the correct procedure to determine the future capacity need for Ellund, neither legally nor practically. Energinet therefore cannot be part of a joint proposal within this ongoing process.

Energinet acknowledges that capacity must of course be continuously discussed and adapted to the needs of the market, but this must be done in cooperation between the TSOs according to the proper procedures set out in NC CAM chapter 4.

4. Market view

Energinet has been in contact with a number of market participants, who question the process and rationale of reducing the firm capacity at Ellund southbound to zero. In general, shippers express the need for southbound capacity for the daily optimization. Also, a specific need for capacity has been expressed in the incremental process (see point 6 in the timeline above).

Also, market participants express concerns on the decoupling of the Danish gas market from the northwest European market. In general, the pricing of the Danish gas market is strongly correlated with the prices in Germany and the Netherlands, due to the firm capacity at Ellund. Without firm capacity in one direction, Denmark will de-facto be decoupled, and the proxy-hedging possibility via the liquid gas markets in Germany and the Netherlands will no longer be possible to the same degree.

As the main flow in the Baltic Pipe is expected to go directly from Norway, through Denmark and to Poland, the connection to Germany will still be of significant relevance for short-term optimization and pricing in Denmark in the future.

Finally, to our knowledge, no long term capacity bookings for new LNG volumes have been concluded, and based on German market studies and dialogue with market participants, we assess that the actual need for firm transmission capacity from new LNG terminals in North Germany is not more certain than the need for southbound capacity at Ellund from Danish North Sea or Norwegian production.

Yours Sincerely

Jeppe Danø

Market Director, Energinet Gas TSO