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**Response on the joint public market consultation of Transgaz, FGSZ and Gas Connect Austria
on a Capacity Allocation Concepts in the RO-HU-AT Open Season Procedure**

Dear Sir/Madam,

We welcome the joint consultation by the transmission system operator companies Transgaz, FGSZ and Gas Connect Austria regarding a capacity allocation method to be applied in a contemplated binding open season for the booking of new or incremental cross-border transmission capacity at the Romanian-Hungarian and Hungarian-Austrian border.

We generally support regulatory frameworks which facilitate investment in infrastructure and gas supply development. We expect the new and/or incremental transmission infrastructure between Romania and Hungary and Hungary and Austria to better interconnect these markets thereby increasing security and diversity of supply to consumers, promoting competition and market efficiencies, and support gas resource investment and development.

An open season – as discussed in the joint consultation document - for the booking of cross-border transmission capacity is a mechanism to test market interest in capacity and, based on firm capacity bookings, (partially) transfer the risk of an investment into transmission capacity from the investor (in this case system operators) to the user of that capacity. To the extent the user of the capacity can enter into corresponding sales agreements the cost associated with the capacity commitment are meant to be recuperated through gas sales revenues.

While it is desirable to underpin investments into new or incremental transmission capacity with capacity bookings, users may not be prepared to enter into long-term capacity commitments if they

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cannot conclude corresponding long-term sales agreements. Hence, the result of an open season may be that the amount of capacity being committed to is insufficient to justify the investment alone.

This dilemma is recognized in the Network Code on CAM in gas transmission systems as currently amended (ACER Recommendation 04-2015 on the amendment to the EU Regulation No 984/2013) and the Network Code on Harmonised Transmission Tariff Structures for Gas ("NC TAR") as re-submitted by ENTSOG to ACER. These Network Codes introduce the concept of an "economic test" by the transmission system operators when deciding about an incremental capacity project. Article 37 of the NC TAR enables national regulatory authorities to approve an "f-factor" that takes into account "positive externalities of the incremental capacity project on the market and/or the transmission network". Such positive externalities should include amongst others the increase of security and diversity of supply to consumers, positive effects on the level of competition and market efficiencies, and supporting effects for gas resource investment and development.

Hence, if the transmission system operators conduct a joint open season (also called "alternative capacity allocation method" under the aforementioned NC CAM) the economic test and the f-factor need to be carefully designed taking into account positive externalities and that in increasingly shorter term, competitive markets individual users may not be prepared to enter into long term capacity bookings.

With these introductory statements allow us to respond to your questions in more detail:

4.1. Would you support a possible capacity allocation design other than those described in Regulation 984/2013/EU, i.e. ascending clock algorithm or uniform price algorithm?

- **Yes ✓**
- No
- N/A

If yes, which?

Taking account of Article 20d (Principles for alternative capacity allocation mechanisms) of the NC CAM we deem the auction procedures stipulated in the NC CAM as not suitable because the RO-HU-AT incremental capacity project involves more than two entry-exit systems; because capacity bids will likely be requested along several interconnection points during the allocation procedure; and because users may have a need for conditional capacity bids to be allowed during the allocation procedure.

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Therefore we support that an alternative capacity allocation mechanism should be applied as foreseen under Article 20d (2) of the ACER Recommendation 04-2015 on the amendment to the Network Code on CAM.

Method No. 3 - as described in this joint public market consultation on Capacity Allocation Concepts in the RO-HU-AT Open Season Procedure - contains key elements which are conducive to a potential successful outcome of an Open Season procedure.

4.2. Do you have any preference between auction algorithms, e.g. ascending clock, uniform price or pay-as-you bid?

- **Ascending clock algorithm** ✓
- Uniform price algorithm
- Pay-as-bid
- I have no preferred auction algorithm

If you have any preference, please state your reason.

The ascending clock mechanism is the most transparent of the three listed auction algorithms as it provides information about the aggregated industry demand for capacity at a given Interconnection Point after each bidding round. This better enables bidders to assess potential scarcity and adjust their bids. This tentatively prevents over- or underpayments.

4.3. In case of Method No. 2, which batch of single-year products would you prefer, e.g. 5, and/or 10 and/or 15 years?

- ☒ **5-year batch** ✓
- ☐ 10-year batch
- ☐ 15-year batch

The shorter term batch covering 5-year periods allows for better tailoring of capacity booking profiles. However, we favour the ability for bidders to bid for single-year products individually combined with a priority scheme for large shippers.

4.4. Would you allow conditional bidding during the open season procedure?

- **Yes** ✓
- No
- N/A

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Conditional bids during the open season procedure should be allowed to enable bidders to manage risk thereby facilitating user participation in an open season procedure. Conditional bids allow bidders – amongst others – to align the timing of entering multiple, often significant commitments such as sales or purchase arrangements or investment decisions.

4.5. If conditional bidding during the open season procedure is allowed, which type of conditionality would you deem necessary?

- ☐ **Booking across a number of years** ✓
- ☐ **Booking across different interconnection points** ✓
- ☐ **Minimum quantity** ✓
- ☐ **Other: (please specify)** ✓ **see below**

All of the three listed types of conditionality should be allowed in an open season procedure. The listed types would allow bidders to enter into capacity commitments commensurate with potential commitments under e.g. sales- or purchase agreements, i.e. typically a certain capacity profile over a period of years which requires transmission capacity over multiple Interconnection Points.

In addition, dates should be defined by which preliminary capacity bookings under open season procedures become final and binding. This would allow iterative decision making processes and back-to-back commercial arrangements such as final investment decisions for significant investment projects (e.g. upstream resource developments, power plants or storages), gas sales and purchase agreements and transmission capacity bookings.

4.6. Would you prefer ex ante or ex post conditionality in the open season's capacity allocation design? Please state your reasons.

As alluded to in our answer to question 4.5, we believe that both forms of conditionality have their place in the design of a capacity allocation process as they serve different purposes:

Ex ante conditionality is a tool to allow bidders to tailor their bids better to their capacity needs thereby improving the chance of a successful auction result and confirmation of preliminary bids by the bidders.

Ex post conditionality is a tool to allow bidders to step back from their bids made during an auction (i.e. their preliminary bookings) thereby better enabling bidders to enter into related commitments subsequent to the capacity auction and better manage back-to-back risks as described above.

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4.7. Do you have any comment on the above mentioned Methods?

The design elements of capacity auction method no. 3 (yearly capacity products for each IP; priority to highest bidder commitment; bids are preliminary and non-binding up to a defined date; and if the economic test is not met the TSO can cancel the bookings) seem to best address the requirements of potential bidders to manage risks associated with multiple, often significant related commitments such as sales and purchase arrangements or investment decisions (see also our responses to question 4.4 and 4.5):

- The ability to book yearly capacity products for each IP separately allows for the booking of capacity profiles tailored to the need of bidders thereby maximizing the capacity available to other bidders.
- The priority concept for highest bidder commitment ensures that individual bids in a given year and/or at only one IP do not potentially frustrate a successful outcome of an open season. Priority can be determined based on the contribution to the system operator's cost recovery taking into account e.g. the product of the amount of capacity bidden for per year times the number of years.
- The definition of a date at which the preliminary bookings become final and binding allows bidders to confirm their preliminary bookings thereby facilitating an iterative entering into commitments related to the capacity offered in the open season (see also our response to question 4.5).

Allow us to point out that upstream resource development investment projects require significant upfront investments and require access to a sufficiently sized market. Such significant investments are often partially or fully underpinned by (a chain of) long-term commercial arrangements including long-term sales or purchase agreements. These agreements typically are conditional upon availability of firm transportation capacity. Hence, the date at which a preliminary capacity booking under an open season procedure becomes final and binding must be carefully determined. Such a date should ideally be *after* final investment decisions have been taken and/or long-term commercial arrangements have been entered into. However, the corresponding open season procedure should ideally be conducted *before* the above stated final investment decisions and/or long-term commercial arrangements to provide assurance to the parties that transportation capacity will actually be made available by the transmission system operator.

Furthermore, when entering into the above stated transportation capacity arrangements potential project risks from transportation tariffs should be transparent and options to minimize investor risks should be available such as the offering of "stable tariffs" for bookable capacity.

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4.8. Would you have a preference for any of the above mentioned Methods?

- Method 1
- Method 2
- **Method 3 ✓**
- None of these
- I have no preference

If you have any preference, please state your reason.

We have a preference for Method no. 3 combined with an ascending clock auction method and the types of conditionality listed under question 4.5.

We suggest that the period in which the open season procedure takes place and the date at which the preliminary bookings need to be finally confirmed and become binding are carefully determined following dialogue with stakeholders.

Please do not hesitate to contact us in case you have any questions or would like to discuss.

Sincerely,



John L. Knapp

Managing Director

ExxonMobil Exploration and Production Romania Ltd.

