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Bundesnetzagentur für Elektrizität,
Gas, Telekommunikation, Post und
Eisenbahnen

Beschlusskammer 7

Mrs. Diana Harlinghausen

*Subject: consultation regarding
the Festlegungsänderung BK7-16-050 (Konni Gas)*

Dear Mrs. Harlinghausen,

Hereby Gazprom export LLC (also acting on behalf of its affiliated companies) (hereinafter – GPE) would like to respond to the public consultation within the ongoing process of „Festlegung zur Einführung eines Konvertierungssystems in qualitätsübergreifenden Gasmarktgebieten“ (Konni Gas BK7-16-050) regarding creation of a conversion system for cross-quality gas market areas in Germany.

GPE understands the security of gas supply concerns of Bundesnetzagentur and stresses that only a cost reflective ex-post conversion fee mechanism can guarantee the necessary price signals and lead to economically efficient behaviour by shippers. GPE considers Bundesnetzagentur's intention to reform the German conversion system by April 2017, however action should already be taken by October 2016, as any continuation of the conversion levy is severely discriminating against H-gas shippers and all storage users. We consider it as extremely unfair and unacceptable that GPE, as the major H-gas supplier, is burdened by additional levies more than any other market participant despite not causing any conversion costs.

The level of the NCG conversion levy of 0.15 €/MWh for winter 2016-2017 proves that NCG accepts a continuation of its inappropriate market role of being the main L-gas buyer and which causes the nonsensical and unfair cross-subsidisation towards sellers of L-gas control energy and inefficient sales to L-gas customers via commercial conversion. The inaction of Bundesnetzagentur to prevent a punitive

conversion levy for winter 2016-2017 is unacceptable. Further prolongation of the application of the conversion levy will be almost unbearable for H-gas suppliers and may eventually increase the prices on the German gas market once importers pass on conversion levy costs and decrease the long-term booking capacity demand.

The excessive levels of commercial conversion due to a low conversion fee have already proven to be very inefficient this winter, which makes the proposed ex-post conversion fee the only viable option to limit future conversion costs and reduce commercial conversion activity to an adequate level. Anything else would be damaging to the German gas market as a whole. Based on the concrete proposals made by Bundesnetzagentur about the gas quality conversion system, GPE supports the ex-post fee provided that the full cost of conversion is attributed to the causers of such cost. Depending on further developments of the issue GPE reserves the right for any legal action with respect to any further decisions of Bundesnetzagentur.

In the following paragraphs GPE will comment on the specific proposals made by Bundesnetzagentur, highlighting why the ex-ante conversion fee is not a viable option at all.

Ex-ante conversion fee:

The proposed ex-ante conversion fee is very similar to the existing conversion fee and does therefore not provide any improvement.

The suggested limit of 0.45 €/MWh to be paid by real causers of the conversion costs is far too low because as soon as the spread between H- and L-gas is above the fee, shippers will withhold L-gas imports from the Netherlands and instead make use of the commercial conversion, which leads to extraordinary costs and can threaten security of gas supply. This is proven by NCG's expected high conversion costs for winter 2016-2017, which is reflected by the very high and damaging conversion levy for the same period.

Bundesnetzagentur intends to strike the right balance between sufficient gas quality conversion and limiting market operators' roles of being the main L-gas procurer. However, the ex-ante approach is simply not flexible enough as the balance changes every day depending on market prices. In this light it does not seem sensible to permit L-to-H conversion at zero cost, because if German L-gas markets would trade below H-gas this could create considerable conversion costs which are currently unexpected.

The proposed conditions for market operators to increase the conversion fee at short notice are very vague and undermine the intention of giving shippers certainty over future conversion costs. Due to continuously changing market spreads and potential fee adjustment at short notice, setting the ex-ante conversion fee and conversion levy over the period of an entire year exacerbates the inefficient cross-subsidies whilst neither guaranteeing any certainty for forward trading nor security of gas

supply. In fact, publishing the ex-ante conversion fee and conversion levy six weeks before 1st October is far too late for annual storage bookings concluded before the storage year starting the preceding 1st April.

Economic inefficiencies of the ex-ante fee are further exacerbated by the fact that the conversion levy is still applied to entry flows instead of end consumers. This constitutes an undue barrier to cross-border trade and harms the European Single Energy Market. Allocating part of the conversion costs on transits is a cross-subsidisation from the end-consumers of Germany's neighbour states to the local North-West German L-gas shippers and consumers. Since the conversion levy is also reflected in the sales of L-gas control energy to market operators, the levy mechanism leads to even higher conversion costs. It is hard to understand that Bundesnetzagentur further discourages storage usage with a high conversion levy on storage withdrawals, despite concerns about security of gas supply. If Bundesnetzagentur opts for the ex-ante conversion fee, any resulting conversion levy should apply to end consumers only.

Lastly, the proposed payout mechanism towards those who paid the conversion fee is highly unfair. H-gas importers and H-gas storage users who never use the L-gas network pay millions via the conversion levy, but any surplus of the conversion account would be paid out to those shippers causing the inefficient conversion costs! This constitutes a severe distortion of the causer-payer principle.

Ex-post conversion fee:

The ex-post conversion fee approach provides an efficient steering mechanism and fully abides by the causer-payer principle. By making those shippers who cause expensive conversion costs directly pay for it, the possibility to optimise and arbitrage is largely reduced and the unacceptable cross-subsidization from H-gas importers, domestic producers and storage users to L-gas shippers is largely reduced because the conversion levy will be minimal or zero. Any large gas market price moves will be flexibly reflected in the respective ex-post conversion fee and conversion in either direction will be covered in a very cost-reflective way.

Improved information provision by market operators on aggregate linepack and quality specific control energy demand would further strengthen the market and improve predictability of the ex-post conversion fee. Overall with the ex-post conversion fee the German L-gas market price will be adequately based on either Dutch imports or the real cost of converting H- to L-gas, rather than a large scale cross-subsidisation.

As described above, the suggested ex-ante conversion fee does not provide real certainty over the cost of conversion either, with short publication leadtime and market operators having discretion to adjust at short notice. Abolishing the

conversion levy due to the ex-post conversion fee would furthermore reduce the large variety of German fees and levies which are very harmful to the German and European gas market.

Further points:

Bundesnetzagentur could strengthen the rule that shippers are not allowed to convert in order to trigger control energy demand. With the ex-ante conversion fee the rule is ineffective, because shippers will be able to convert whenever the H- to L-gas spread is below the TTF price plus transportation cost to import Dutch L-gas.

Conclusion:

In conclusion, the proposed ex-ante fee leads to large inefficient costs, does not provide adequate certainty for market participants, harms security of gas supply by making imports, long-term transportation capacity booking and storage less attractive, constitutes a massive cross-subsidy from importers, storage users and domestic producers towards those shippers who make use of commercial conversion and further damaging the trust of the gas market players regarding the stability and the predictability of the German gas market in whole. All of the above severely violate the causer-payer principle, whilst the ex-post fee would better solve all of the above issues and be in line with the causer-payer principle.

Deputy Director General for Gas

