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BUSINESSEUROPE COMMENTS ON THE COMMISSION PROPOSAL FOR A REGULATION CONCERNING MEASURES TO SAFEGUARD SECURITY OF GAS SUPPLY AND REPEALING DIRECTIVE 2004/67/EC

Executive Summary

BUSINESSEUROPE supports a more harmonised European framework and a strengthened coordination process for a more rapid and more effective reaction to supply disruptions with minimum standards and emergency plans, when market-based mechanisms prove not to suffice in a crisis situation.

However, BUSINESSEUROPE urges policy-makers to refrain from an excessively centralist and potentially market-distorting approach when designing new legislation for measures to safeguard security of supply. Costly and burdensome or prescriptive measures should be avoided. The main responsibility for a secure gas supply should lie with the supply companies themselves. Market-based mechanisms must therefore run as long as possible and undue intervention by the Commission in the assessment and coordination of national emergency measures must be avoided. Only in the last resort and in acute crisis situations should Member States turn to regional or Community intervention.

Minimum common requirements should be defined at EU level for gas infrastructure and crisis management, following sound risk analysis, in-depth impact assessment and clarification of the uncertainties in the proposed legislation. Against this background, Member States should be allowed to design appropriate national frameworks which take into account their national specificities and circumstances.



Introduction

On 16 July 2009 the European Commission presented a draft regulation to deter supply disruptions in the gas sector and to put in place a Europe-wide crisis mechanism should such interruptions occur. The regulation is intended to supersede directive 2004/67/EC on security of gas supply.

Ensuring a secure gas supply has become an increasingly important issue in the last few years for all companies in Europe, energy producers, suppliers and energy users. As stated by the Gas Coordination Group in the aftermath of the last gas crisis, the actions taken by the gas industry to limit major inconveniences for consumers have proven to be efficient and successful for facing the emergency. Nevertheless, the crisis also demonstrated that Member States' level of preparedness varied significantly. BUSINESSEUROPE therefore supports the Commission's approach, which requires all Member States to take their proper share in a collective effort to increase security of supply.

For this reason, BUSINESSEUROPE supports the proposal for a more harmonised European framework, strengthened coordination and clear decision-making process for a more rapid and more effective reaction to supply disruptions with minimum standards and emergency plans, when market-based mechanisms prove not to suffice in a crisis situation.

A. General principles for designing measures to secure gas supply

BUSINESSEUROPE believes that the design of Community measures for ensuring a secure gas supply should be inspired by the overall principle of avoiding an excessively centralist and potentially market-distorting approach that does not take due account of market signals, which are the essential building blocks for any action in a liberalised market. Any improvement in the legislation on security of gas supply must therefore be based on the following principles:

- In general, market mechanisms should run as long as possible, avoiding costly and burdensome or prescriptive measures potentially leading to market distortions.
- On the basis of adequate preparatory work (assessment of risks affecting the security of gas supply at national level, impact assessments of possible EU legislative measures, improving the clarity of some provisions in the proposed legislation), minimum common requirements should be defined at EU level for gas infrastructures and crisis management. Member States should then design appropriate national frameworks, taking into account their specificities and current situations. National frameworks should consequently set up general obligations allowing operators to define their industrial strategy and best combine the various existing flexibility tools.
- In addition to the national level, security of supply should also be addressed at the regional level, and cooperation mechanisms between competent national authorities should be organised.



- Increased transparency and harmonisation is needed as regards congestion management, cross-border capacity allocation mechanisms and information on capacity availability. More efficient use of congestion management revenues would also provide the right incentives for Transport System Operators' (TSOs) investments. An investment-friendly regulatory and legal framework should be ensured.
- Any new measure should be based on a sound impact assessment to guarantee its adequacy and cost-efficiency.
- The cost impact on the non-protected industrial consumers must be minimised.
- New legislation on security of gas supply must be compatible with the provisions in the 3rd energy liberalisation package.

B. Specific comments on the proposed regulation

1. Reconsider the legal form of the proposed legislation

The Commission's decision to repeal the current directive 2004/67/EC and replace it by a regulation is questionable. A regulation requires direct application in Member States and does not give them the flexibility to take account of national circumstances. This is particularly important given the different characteristics in gas markets, supply portfolios, geographical location and geological specificities of Member States.

2. Base measures to protect security of gas supply on market mechanisms

BUSINESSEUROPE believes that measures to protect security of gas supply must be based as much as possible on market mechanisms. The main responsibility for a secure gas supply should therefore lie with the supply companies themselves. Only in the last resort and in acute crisis situations should Member States turn to regional or Community intervention. This three-pronged delimitation of responsibilities as currently applicable should be maintained in the future EU legislation on security of gas supply and be enshrined more firmly in the legislation.

In the case of an acute crisis situation where market mechanisms prove not to suffice, all market participants have to contribute to overcome the crisis.

3. Base the standard for gas infrastructure ("N-1 standard") on a thorough risk analysis and impact assessment

According to the draft regulation (article 6) each Member State would have to ensure that, in the event of a gas supply disruption of the largest supply infrastructure ("N infrastructure"), the gas supply can still be maintained, even in periods of extreme cold, for sixty days thanks to the remaining infrastructure ("N-1 infrastructure").

European Industry basically supports the introduction of a well defined European N-1 concept and welcomes the approach based on individual responsibility, which can encourage investments in greater security of supply.



However, there are still uncertainties surrounding the currently proposed N-1 standard. There are cross-references between the supply standard and the infrastructure standard. Provisions in article 6 and Annex I are complex and results arising from the application of the N-1 rule may be different depending on the interpretation of the parameters in Annex I. Moreover, the N-1 standard as currently defined might lead to huge investment needs, which could translate into significant costs and higher gas prices for final consumers.

Therefore BUSINESSEUROPE calls for a removal of these uncertainties and for the future legislation to be based on:

- A careful assessment of risks affecting the security of supply at national and /or regional level, if Member States so decide
- Thorough impact assessment of possible national measures to address these risks. This impact assessment will need to test the economic, technical and operational feasibility and cost-effectiveness of crisis response measures based on the N-1 standard. There is a need to prove that additional infrastructure measures are fully justified. BUSINESSEUROPE believes that the N-1 standard should lead to proportionate and feasible measures and should preserve the necessary leeway to account for national/regional specificities.

4. Minimise the cost impact on the non-protected industrial sector

The impact assessment should consider in particular the costs that any future legislation will impose on industrial gas consumers, who could face significantly increased access charges to the gas infrastructure due to the extra investment by gas operators, resulting from EU legislation. For these reasons, the future legislation should make sure that costs incurred by gas undertakings to implement security of supply and infrastructure standards feed into national and cross-border tariffs in the most cost-efficient, transparent and non-discriminatory manner. Cost should be fairly allocated between the systems implementing those measures and those benefiting from them. Avoiding or minimising additional access charges for industrial consumers is essential since the draft regulation assigns the benefit of increased supply security mainly to the protected household sector. The extent of any new obligations for gas operators must be defined in a reasonable way in order not to impose significant extra costs on industrial sectors, which are not protected in the context of article 7 of the draft regulation and which are exposed to international competition.

5. Maintain companies' freedom to choose how to achieve the N-1 standard

To ensure cost-effectiveness, it is indispensable that companies and Member States retain the freedom to decide what infrastructure measures to take in order to achieve the N-1 standard. This freedom must also be maintained regarding the installation of commercial gas storage facilities or implementation of reverse gas flows.

Infrastructure measures can best be steered and coordinated via the national and EU ten-year network development plans provided for in the third internal energy market



package, since these are drawn up by network operators and European Network of Transport Systems Operators-Gas (ENTSO-G), and then verified by the European Agency for the Cooperation of Energy Regulators (ACER). In this way, it is ensured that gas infrastructures are tailored to national and regional market structures, yet are still coordinated at EU level. A blanket obligation to implement reverse gas flows on all interconnectors should be rejected for reasons of efficiency and cost. Any decision to install reverse flows must be taken on the basis of a cost-benefit analysis. Solutions going beyond commercial measures and involving high costs should be viewed in a critical light.

6. Consider actions on demand

The present proposal lays its focus on supply infrastructures (N-1 infrastructure standard and reverse flows), whereas it should also address possible actions on demand, which could be economically more effective and would better respect the functioning of the market. Better management of the diversity of gas contracts to possible interruptible customers at the national or regional level would be compatible with the functioning of the market and could lead to an internalisation of the security of supply cost (the additional cost of security of supply being paid by the final beneficiary of such security of supply).

7. Avoid undue intervention by the Commission in the assessment and coordination of national emergency measures

In order to respect the well established three-pronged delimitation of responsibilities between companies, competent authorities and the Community as currently applicable, the powers conferred on the Commission in articles 4 and 10 (for example the right to instruct national competent authorities and natural gas undertakings to change their actions) must be supplemented by provisions aimed at avoiding any slippage towards unjustified intervention.

In addition, a threshold for declaring a Community emergency if it loses as little as 10% of daily EU gas imports or if more than one national competent authority has declared an emergency is too low and could discourage Member States from preparing themselves for crisis cases.

8. Establish clear and quantifiable criteria for emergency declaration and measures

The draft regulation does not clearly define the conditions which would lead to declaration of an emergency by a national competent authority and application of an emergency plan. In order to limit potential market distortions or market abuse and to ensure a level playing field, visibility and a clear and stable framework to gas operators, these conditions must be clearly defined. The decision to declare or lift a declaration of emergency as well as the actions taken must be based on objective and quantifiable criteria, accessible at any time for all actors in the gas value chain.



Furthermore, the definition of each crisis level (article 9(2)) remains unclear. Each crisis level should therefore be explained in detail and clearly distinguished from each other.

9. Avoid undue restriction of gas flow across borders in an emergency

The emergency plan shall not introduce any measure unduly restricting the flow of gas across the borders and shall ensure that cross-border access to storage facilities or other gas infrastructures such as LNG terminals is maintained also in case of emergency on commercial terms and duly taking into account contractual obligations.

10. Attribute a stronger consultative role to the gas coordination group

BUSINESSEUROPE welcomes the maintenance of the gas coordination group in the draft regulation. Since the role of this technical committee has proven to be a very important one and since its function should go far beyond being solely advisory, the Commission should closely involve all stakeholders when deciding about the exact composition of the group. Since the gas coordination group is best placed to assess the gas supply situation and provides for a suitable cooperation platform between industry, national and Commission officials, the Commission should consult the group before declaring emergency situations or taking any measures and should be bound by its decisions. The gas coordination group should further be strengthened with additional members from the gas industry and large-scale industrial consumers.

11. Limit reporting obligations to information strictly necessary for assessment of the supply situation

The draft regulation requires detailed obligations from Member States and natural gas companies to report about infrastructure-related agreements and gas supply contracts with third countries or companies in third countries (article 12.6). Even though BUSINESSEUROPE believes that a minimum level of market transparency can help in assessing the gas supply situation, reporting obligations should be limited to information strictly necessary for assessment situation. The business confidentiality of gas companies should be safeguarded and the administrative burden kept as small as possible.

12. Place solidarity deliveries between Member States on a commercial basis

In the event of regional or EU-wide disruptions of the natural gas supply, it should be possible for solidarity deliveries from other Member States to be made on a commercial basis. This principle takes account of the primary responsibility of each energy company for the energy supply. The gas supply disruptions in January 2009 proved that this works in practice.

13. Support regional cooperation

Under the draft regulation, Member States can form regional, cross-border cooperation to assess their vulnerability against the N-1 infrastructure standard and/or to establish



their prevention and emergency plans accordingly. BUSINESSEUROPE is in support of this option since it will increase the flexibility of national players for securing the natural gas supply and will increase the integration and liquidity of gas markets which are still nationally oriented to a large extent. It should however also be taken into consideration that regional cooperation in a crisis situation requires the availability of necessary interconnection infrastructures to enable gas movements within a region. At the same time, regional cooperation must be advantageous for all participants and existing standards in Member States must not be undermined.

14. Take account of specific constraints affecting certain groups of individual industrial customers

Industrial natural gas customers, especially large-scale consumers, are dependent on a continuous supply of natural gas. Given that short-term fuel alternation using dual-purpose combustion installations is not possible without upheaval in many areas of primary industrial production (e.g. glass, metals, steel), industrial energy consumers can do very little to react flexibly to supply disruptions. Hence, the establishment of crisis mechanisms (article 9.1(2)) must take account of the different constraints of individual industrial customers. In the event of a gas supply disruption and a consequent forced fuel switch (see Annex III), it has to be ensured that there will be no penalties based on existing environmental legislation (e.g. in the case of increased CO₂ emissions). Attention has to be paid to the balance between costs incurred by large industrial natural gas customers in comparison with the benefits they gain from security of supply policies.

C. Thoughts on the need for a broad, long-term perspective on security of supply

BUSINESSEUROPE urges the EU to complement the development of a rapid-response mechanisms for short-term gas crises with establishment of adequate framework conditions encouraging the realisation of the necessary investments in gas networks, infrastructures and interconnections needed to ensure the long-term security of gas supply and efficient functioning of the internal market.

Sufficient investments in cross-border interconnection infrastructure are crucial, particularly for interconnections of strategic European interest. The Presidency Conclusions of the European Council of May 2007 stated that achieving at least 10% gas interconnection capacity use, compared with total gas demand, will be vital. Everything must be done to let market forces play their role in this respect. In some specific cases, obstacles might however impede market-driven investments in infrastructure. In these cases the Commission should conduct an analysis of such obstacles and propose specific measures to remove them.¹

¹ The Confederation of Spanish Employers (CEOE) considers that improving security of supply may justify developing more capacity than strictly needed for trading purposes and may justify anticipating future long-term transportation needs.



Finally, BUSINESSEUROPE believes that besides preventive and crisis mechanisms and a sufficient increase in energy infrastructure, increased energy efficiency and a strengthened EU external energy policy will be crucial.
