

Mr. Andris Piebalgs
Member of the Commission
European Commission
B – 1049 Brussels

09L218

Brussels, 22 April 2009

Dear Mr. Commissioner,

Thank you for your letter dated 9 March 2009 and the opportunity to share with you our views on the January gas crisis. EUROGAS welcomes the Commission's effort to involve the industry in the ongoing analysis with a view to draw balanced conclusions.

Please allow a few **general remarks** before responding to your specific questions.

EUROGAS is appalled by the unprecedented, complete and sustained disruption of gas flows from Russia through the Ukraine to the European Union Member States. The unacceptability of this behaviour, no matter what the reasons, has been made unequivocally clear in a joint letter to Messrs. Miller and Dubina by four of Gazprom's major European customers. We believe that this message should not be forgotten, e.g. on the recent Ukrainian Investment Conference the "innocent observer" might have got the impression that the crisis occurred due to technical shortcomings and fixing these would prevent any potential future crisis, which we all know is not the case.

Moreover, we believe it is very important to acknowledge the effectiveness of a multitude of industry actions alleviating or at least mitigating the impact of the Russian supply shortage, as e.g. summarized in the IEA report delivered at the Gas Coordination Group.

The well diversified supply portfolios of a number of European import companies, combined with the appropriate investments in commercial storage, meant that the effect of the supply shortage was not at all noticeable in North-West and South-West Europe. As you know, various successful efforts were undertaken by gas companies to mitigate the effects of the shortage in Eastern European Countries via regional solidarity actions, although one must acknowledge that the disrupted physical flows in these regions – with a larger physical dependency on Russian molecules and limited interconnection with Western neighbours – could not be fully compensated. It should be emphasised, however, that even in these countries there was, despite temporary industry curtailments, no restriction of gas supplies for households, hospitals, retirement homes, schools and also for heating generation to households. E.g. in Slovakia, industry curtailments could be lifted after West to East reverse flow from the Czech Republic could be arranged. Commercial arrangements such as swaps and short term trades allowed a quick response to consumers' needs.

We consider it thus fair to conclude that the strong commitment of the various functions of the European gas industry, by exercising cross-country cooperation, with the capacity and ability to react quickly and decisively have proven key factors in the crisis management whilst obeying the defined statutory tasks and responsibilities of the market participants. Conversely, this demonstrated that even during such a crisis no regulatory intervention, be it ex ante or ex post, was necessary to face the challenges and find solutions. The European gas industry was able and capable to manage the situation by itself.

Since the crisis we have witnessed various initiatives using the crisis as an argument for legislative or regulatory actions both on national and European level. We note e.g. tendencies to give priority to the interests of some individual Member States (protectionism, island solutions) and to introduce economically inefficient solutions (strategic gas storages without due economic analysis neglecting the commodity related specifics) and solutions hampering the internal energy market. Whilst we are principally supportive of improving matters where there is room for improvements, including economically viable additional investments, we would like to caution against any tendencies for protectionist reactions or uneconomical and bureaucratic solutions.

As to **lessons learned** we would like to distinguish between lessons for politics and lessons for industry, based on the principal understanding that there should be a healthy "division of labour" between the two, in order to attain the best results for the security of supply for Europe:

For politics, it becomes clear that a consistent European energy policy with emphasis on competitiveness and sustainability, but also on security of supply is indispensable. Moreover, an energy policy with an effective security of supply component must rely on an element of external energy policy, involving Member States, industry and EU Institutions. Furthermore, it has proven important and effective to speak with one voice. Such policy must be implemented in a determined manner and articulated around strong elements such as compliance with international Treaties and respect of transit and supply contracts. In addition the EU should reinforce its external energy dialogues and should strongly support EU companies in their investments in production countries.

Regarding our industry, we wish to share the following conclusions. Firstly, we should accelerate our efforts to further diversify our supply base. That also applies to the diversification of transit routes, but more importantly to tapping new sources of origin, i.e. the Caspian and the African regions as well as LNG. Moreover, in view of declining indigenous (flexible) production, we should continue to invest in commercial storages to cater for the modulation of increasing base load influx. In conjunction with that, we see the need for infrastructure investments "towards" Europe as well as "within" Europe. The latter shall also enhance, on the back of the commercial merits of the need for additional imports, the interconnectivity of the Single European Market. At the same time, interconnectivity investments should be carried by integral supply economics and should not entail unreasonable and disproportionate increase in the costs for European consumers and industry.

When asked which **recommendations** we might propose for both industry and public authorities, we would like to comment as follows:

As to industry, we refer to the lessons learned as outlined above, i.e. to strengthen the diversification of supply portfolios and of transit roads.

As for public authorities, we also refer to the statements on lessons learned above with regard to the need for a European energy policy with appropriate ingredients of foreign policy aspects. Moreover, we would like to caution against "actionism" and hasty conclusions on national as well as European level which might well turn out costly at best or even counterproductive. As already mentioned, certain efforts towards national protectionism would damage rather than enhance further the supply security of the Single European market. The worst that could happen would be national emergency arrangements which, in the event of supply disruption, would create national "islands" hampering the free flow of gas into and out of individual Member States. However there has to be a trade off between economic viability and a remaining (disruption) risk, the latter to be mitigated by good relations management with suppliers and transit providers on business as well as political level.

With regard to crisis management in case of a major supply disruption, the existing Gas Coordination Group could be supported by workgroups to develop potential regional solutions based on cooperation and solidarity. As the crisis also showed it is not possible to prepare for all kinds or situations in advance. Too rigid specifications would have been detrimental and could have possibly narrowed the creativity for drafting solutions.

Europe should also develop a coherent and consistent package of actions to ensure that Europe can compete successfully for LNG in the global market since LNG might be an interesting aspect to enhance security of supply at least for some Member States. These actions should maximize the commercial potential for LNG to play an important role in the internal market and include dialogue with LNG producers on enhancing production. EU should improve information on network flows, within and upstream of the European network.

Regarding **transparency and exchange of data** in the course of the crisis, experience has shown that there was in principle good cooperation between gas companies concerned. To ensure visibility of required data, it is essential that all Member States implement and enforce the transparency requirements set out in European energy legislation. Additionally, some improvements on cooperation on cross-border gas flow transparency permitting the TSOs to monitor flows entering the EU might be a tool for an early warning mechanism in case of problems. Communication between network operators, suppliers and shippers might be also improved through the Gas Co-ordination Group with third (producing and transit) countries also involved as necessary.

During a time of supply disruption, certain national rules on timeframes for capacity booking could be temporarily rescinded or at least shortened. Urgent crisis situations call for immediate industry actions and long lead-times have to be avoided in order to safeguard supply to consumers and ensure market flexibility.

The **reverse flow of gas and cross - border interconnections** played a very important role and prevented, in number of cases, the negative economic impact of gas and supply disruptions. As already pointed out, additional reverse flow capabilities have to be analyzed from several points of view (economic efficiency, commodity availability etc.). National regulators should consider all such investments when approving investment plans and setting network tariffs or tariff methodologies. ERGEG could have a role in facilitating the cooperation of national regulators in the development of improved cross-border measures. It also appears useful to study this further with a view to identify and implement some decisive "quick fixes" and economically inexpensive solutions. New interconnections or new transmission routes are mid-term or long-term measures resulting from and riding on the economics of supply projects and aimed at diversifying and strengthening the security of supply for the European market.

Commercial gas storage played a helpful role and was an invaluable source of additional supply capacity during the crisis. It should be noted, however, that storage can never substitute completely for a continuous base load supply stream and withdrawal performance decreases in the process of emptying the storage facility. Eurogas welcomes the recognition by the Commission that there is insufficient evidence to decide on the need for obligatory gas storage. The development of commercial storage should be encouraged by authorities wherever economically and technically feasible, whilst recognizing that differences exist between Member States, for example in their geological characteristics.

To conclude we are convinced that whilst it is the role of authorities to define common security of supply objectives, it is the role of industry players to develop the physical and contractual tools to achieve such objective. Europe needs competitive gas/energy companies, capable to efficiently operate at EU and international levels in often complex situations whilst being effective counterparts to larger non-EU actors and producers. We hope that we have answered your questions though we realise the complexity of issues at stake will require a continuous dialogue.

Yours sincerely,



Domenico Dispenza