

**POSITION PAPER ON PROPOSALS ON THE INTERNAL MARKET:  
A STRATEGY FOR A COMPETITIVE, SECURE MARKET**

**THE INTERNAL ENERGY MARKET**

1. The Communication “An Energy Policy for Europe” identifies the need for progress in the areas of unbundling, effective regulation, transparency, infrastructure, network security, capacity and principles of public service as requirements to achieve a European gas grid and a truly competitive European-wide energy market.
2. Eurogas considers that the development of competition requires a wide set of conditions, ranging from the existence of sufficiently available capacity and commodity, an improved level of liquidity and transparency to an appropriate stable and reliable regulatory framework enhancing private investments and the guarantee of non-discriminatory access and operation of the network, as well as unhindered customer switching.
3. To achieve progress towards a sustainable, secure and competitive energy market, policy should focus on measures that will improve market integration, especially in terms of delivering better co-operation among regulators and also TSOs, and measures guaranteeing non-discriminatory access. In the view of Eurogas, a well functioning market will necessitate policies focused on
  - **improved regional co-operation** as a step towards a fully integrated EU market focused on a better harmonized regulatory process and measures to enhance co-operation among TSOs and remove barriers to competition.
  - **non-discriminatory access and system operation.**

Together, these will improve wholesale market functioning.

**Improved regional co-operation and regulation**

4. Eurogas supports the range of actions proposed in the Energy policy package to achieve improved market integration: effective regulation in every Member State through the harmonization of the powers and the reinforcement of the independence of energy regulators; acceleration of the harmonization of technical standards and development of common business practices necessary to improve interoperability and to permit cross border trade to work effectively; increased co-ordination and co-operation between Transmission System Operators; increased transparency; regulatory co-operation; fast-track planning and approval procedures for infrastructure projects.
5. Eurogas endorses the need for an enhanced supra-national regulatory oversight and improved co-operation among TSOs but the scope and activities of any new structures within this aim must be clearly determined and the issues for which they would be responsible well defined<sup>1</sup>. An approach has to be developed to deliver targeted progress in areas reflecting market priorities, and in this system users have a key role in determining the necessary services, harmonized business practices, network planning, and interoperability standards (unless purely technical). Enhanced European regulatory activity and reinforced TSO co-ordination and co-operation should provide an appropriate focus for all users’ interests and related parties’ views.
6. Independently of whether or not there is a structural approach for a GTEplus, TSOs should be encouraged, at regional level and in the framework of the creation of regional markets, to improve their bilateral (or multilateral) co-operation by harmonising their rules with regard to cross-border flows, and by facilitating joint market initiatives (e.g.

<sup>1</sup> These points have been elaborated on in the Position Paper on Improved Market Integration (07PP279) - [http://www.eurogas.org/publications\\_positionPapers.aspx](http://www.eurogas.org/publications_positionPapers.aspx).

hubs, intra-day balancing markets). The role of EASEE-gas should also be strengthened in order that it can offer additional support to the network of independent regulators in following up specific operational practices and standards.

7. Eurogas considers that improved co-ordination with enhanced transparency and grid interoperability will facilitate regulatory and TSO cross-border co-operation and more liquid markets. An optimal use of interconnection capacity and its co-ordinated extension will also boost cross-border trade opportunities and enhance competition and security of supply. Eurogas also thinks the activities of both the Madrid Forum and the Gas Regional Markets initiative present possibilities for achieving progress on the basis of improved implementation of the existing Access Regulation and also other voluntary initiatives for practical co-operation that will achieve results. These processes should at the same time allow identification of any need to change the Guidelines on Access attached to the Regulation.
8. Eurogas supports the proposal for an effective supra-national regulatory approach, which could be delivered by different means such as a reinforced European network of independent regulators, but insists that the role and powers of any “new” regulatory institution including in relation to national regulators have to be clear.
9. In the view of Eurogas, the national Regulators should have the necessary resources and harmonised powers to carry out their duties effectively and correctly, including due consideration for the European dimension. While performing their statutory duties, however, regulators have the possibility to exercise significant discretion in their decisions, and Eurogas therefore advocates that they should adhere to Guidelines for Good Regulatory Practice<sup>2</sup> to improve transparency of decision-making.

#### Non-discriminatory access and system operation

10. It is of paramount importance that suppliers, shippers and consumers have unhindered access to network services under transparent and non-discriminatory conditions. Transmission unbundling plays a fundamental role in guaranteeing confidence that this requirement is met. Solutions, however, to strengthen effective unbundling should be proportionate and take into account not only the need to guarantee non-discriminatory access but also the need to improve market development and integration and the need to have strong European companies when negotiating with non-European producers and by that ensuring security of supply for Europe. Solutions should be based on a detailed and careful assessment of their effects on market development and their consequences on the efficiency and strength of gas companies. Additional points to be taken into account are:
  - 1- The major differences between gas and electricity lead to differing assessments of the factors to be considered.
  - 2- ISO models mostly concern electricity, are in any case relatively recent and are introduced in different market contexts which makes it difficult to use them as useful examples.
  - 3- It is a challenge to assess fully the present model adopted in the EU (legal, functional and accounts unbundling) as the legal provisions are not yet fully implemented or have been recently implemented, in particular in the new Member States.
  - 4- Eurogas considers that there is no proof that an ownership unbundled model delivers higher investment levels than an integrated model and vice-versa.
11. Three approaches to effective unbundling have been examined by Eurogas:

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<sup>2</sup> Eurogas Proposed Guidelines for Good Regulatory Practice (07NO250 of 25.4.2007): available at website [www.eurogas.org](http://www.eurogas.org)

## **1- A further development of existing legislation**

Most Eurogas members consider that it is too early to conclude whether the existing legal, functional and accounts unbundling is insufficient and a new model is required. Nevertheless there are concerns that some problems of discrimination (or perception of a risk of discrimination) exist and require a reinforcement of the existing model.

A further development of legal, functional and accounts unbundling would improve non-discriminatory access, although this would require additional regulation and control measures to be put in place in order to avoid any perception of a risk of discrimination. Full attention should be given to the proposals contained in the draft ERGEG Guidelines on functional and informational unbundling.

Further legislation and/or regulation and control measures imply an additional burden but avoid the problems arising in other models regarding (i) a possible violation of property rights and the freedom to conduct a business as enshrined in European and/or national law, (ii) investment uncertainty (including cross-border investment) and (iii) a changing strategic outlook for the European energy sector whereby some companies could be weakened at the expense of others.

## **2- Ownership unbundling of transmission infrastructure**

Ownership unbundling is seen by the European Commission and ERGEG as the most effective and clean option. It is claimed it would have a positive effect on market integration as it would make agreements and mergers between TSOs easier.

Several companies are concerned that mandatory ownership unbundling would lead to the weakening of European energy companies, which would reinforce the existing imbalance with non-EU players, in particular natural gas producers, who have a determining influence on the worldwide natural gas market since they are not subject to the same rules as European energy companies as they are totally or partially state-owned and protected from foreign competition through monopoly rights.

Forced ownership unbundling may also lead to long-lasting legal disputes centred on a violation of property rights.

In some European countries, however, the adoption of ownership unbundling is seen as a positive element to improve competition and security of supply. Formerly integrated companies in those countries explain that they have found ways to offset any negative impact on their financial structure and have maintained their strength with regard to non-EU producers based on other aspects (such as for example the ownership of other infrastructure assets or the existence of a large and competitive market).

## **3- Independent system operator**

Depending on the model, the Independent System Operator approach could provide non-discriminatory access to infrastructure, with limited negative financial effects on gas companies which would continue to own transmission assets. It is a flexible approach that can be adapted to different realities. In particular in its regional form, it would also be a good means to develop regional markets and drive forward cross border cooperation as a stepping stone towards a single European gas market. It should, however, be noted that an ISO+ model would have the same effects as ownership unbundling.

The ISO should be responsible for network access, operation and co-ordination of network planning. Network planning should be handled by the ISO taking into account the views of all stakeholders. Investment remains one of the basic responsibilities of network owner, and should a TSO not make an investment for which there is real market demand, the ISO should be allowed to open the investment to other investors.

The additional regulation that could be needed under an ISO model is directly linked to the functions which the ISO has to carry out and the geographic area for which a single ISO is responsible.

Regional ISOs could provide non-discriminatory network access and operation and, at the same time, be a powerful instrument to develop market integration by means of harmonization and development of cross-border transmission. In this case, possible consequences for the market and decision making process with regard to infrastructure have to be considered

12. In conclusion, in the light of the considerations summarized above, Eurogas considers that any legislative measure to reinforce effective unbundling should be proportionate and should guarantee that:
- Network access and operational functions are independent from other activities of the network owner, thus ensuring a non-discriminatory access.
  - Investment planning takes into account the needs and views of all gas market stakeholders, and that sound, market driven, transparent investment decisions are taken in the interests of security of supply at European level.
  - Progress is facilitated toward better co-operation among TSO activities leading to integration of markets.

As long as these results are achieved, different solutions are possible, and no single solution at European level is required.

### **Differences between Gas and Electricity**

13. Furthermore it is important to keep in mind when considering the unbundling issue the differences between gas and electricity.  
Main differences include
- Security of supply issues: gas is a primary energy which is largely imported into the community from non-EU and from non-OECD countries. Geo-political issues will be a critical factor with regard to future supplies, while electricity can be less vulnerable in that regard, being a secondary energy generated from a variety of primary fuels.
  - Flexibility: gas can be stored whereas electricity is not storable and electricity implies higher constraints in real time grid monitoring.
  - The financial strength and risk profiles of the companies are different, as most electricity companies also own generation assets, whereas grids may often be the most significant assets of gas companies.

These have consequences that should be reflected in policy making.

### **Secure Supply**

#### **Delivering the Necessary Investment**

14. Eurogas recalls that European gas consumers will only be able to enjoy the benefits gas brings in a competitive market if security of supply is assured. Available timely construction of infrastructure throughout Europe is therefore an important pre-requisite for a European market. Investment planning has to respond to market signals and take into account the needs of all players. Therefore there has to be clarity and consensus on the investment framework, including a common understanding on drivers for investment, investment responsibility, and investment procedure.

15. The main investment criterion for any investor is the rate of return which relates notably to the commercial and regulatory risk and should provide sufficient incentives to invest. Investment responsibilities have traditionally fallen mainly on TSOs. Improved TSO and regulatory co-ordination should further the development of a network meeting the needs of an integrated European market. The investment challenge is, however, so crucial that the opportunity to invest should be opened to the largest possible number of investors.
16. Article 22 of Directive 2003/55/EC recognizes the legitimacy of exemption from general third party access provisions for certain projects. It is particularly important that this exemption be possible, for new infrastructures with high investments at stake. These should benefit from reservation systems that support the long-term viability of these projects. Each project, however, has to be assessed individually.
17. Eurogas underlines the importance of a framework conducive to investment, underpinned by the following elements:
  - a clear and stable regulatory framework
  - recognition of long-term supply contracts
  - removal of administrative barriers for the construction of infrastructure
  - regulated network tariffs that admit a fair return on the investor's risk portfolio
  - transparent and harmonized procedures for setting access tariffs and for the allocation of capacities
  - reinforced co-operation between regulators and among operators
  - harmonized regulatory and operating procedures to facilitate cross-border connections
18. Beyond Europe's borders, further investments are also required to increase availability of import capacity. Mobilizing the necessary investment involves intensified efforts, often in geopolitically sensitive regions. Therefore a framework is needed that recognizes the risks and provides appropriate incentives. It should be a priority of the European agenda to facilitate such investments in support of all the actors involved in the project, and investors need to be confident that no change in the regulatory framework will have an adverse impact on the economics of their venture.

#### Solidarity between Member States and storage

19. Eurogas considers that preference has to be given to delivering solidarity through a well-functioning internal market, and that this will require interconnections as well as availability of commodity and capacity in a liquid market. Eurogas fully agrees that diversification of supply should be a principal objective. Member States' policies are complemented by the Security of Gas Supply Directive (2004/67/EC) and the activities of the Gas Co-ordination Group in which Eurogas is active, which employs practical resources to help meet the objective of a coherent EU policy, and to deliver solidarity.
20. One area which Eurogas positively identifies as requiring further action concerns the need for a Regulation on access to storage, as the voluntary Guidelines are not adequately followed. To facilitate, however, a swift adoption of a Regulation and to minimise regulatory uncertainty in this key area, Eurogas recommends the Regulation follow as closely as possible the existing Guidelines.
21. Eurogas has, however, reservations about the idea of strategic gas storage. Although it is unclear what the Commission has in view, Eurogas would be concerned if this involved volumes of storage outside the commercial market, solely maintained against the possibility of a crisis. In the view of Eurogas, decisions concerning the extension and operation of storage capacities are best made by companies from a commercial point of view and the only restrictions, Eurogas can envisage on the contribution of storage to the market are physical limitations.

22. Additional storage is necessary in Europe, and storage needs should be addressed in relation to expected needs of users (taking into account risk scenarios). Obligations to build and fill storage to keep for an unspecific supply security, would not just be very expensive, but would also lead to disincentives for commercial storage as it would cause uncertainties for commercial investors.
23. Eurogas considers that the way forward is to build on national approaches involving monitor levels and other crisis avoidance policies. An EU level blanket approach would introduce too much rigidity, in turn undermining the development of market mechanisms. Member States have to be allowed to develop proportionate responses and retain the freedom to employ different measures.