

REVISION OF THE DIRECTIVE 2004/67/EC ON SAFEGUARDING SECURITY OF NATURAL GAS SUPPLY

1. In responding to the Communication on the Revision of the Directive 2004/67/EC, Eurogas reaffirms the main elements of its position on gas security:

Security of supply is effectively delivered within a fully functioning internal market, supported by a policy framework conducive to the promotion of investments and entrepreneurial activity;

Good relations with supplier and transit countries are crucial. Although it is the companies' responsibility to conduct commercial relations with suppliers, their activities should be supported by EU and national dialogues with non-EU producers, producing and transit countries;

The roles and responsibilities of the different market actors and stakeholders should be clear, and there needs to be a shared understanding of the expectations on the different parties in the event of a crisis;

A number of steps can be taken to ensure that the EU achieves a better overall gas supply security, and is better prepared for any possible future supply disruption

- Directive 2004/67/EC set up appropriate principles to address security of supply, and is serving as a useful overall basis for improved security of supply policy. In particular the current Gas Coordination Group is proving a valued resource. Eurogas agrees, however, that the Directive should now be evaluated and necessary improvements introduced
- each Member State should be responsible for setting its national security of supply standards in relation to its market characteristics, and the instruments it will support to meet these standards in a framework that is compatible with the internal gas market. There is, however, scope for exploring more regional cooperation based on a common understanding of these national approaches. Improved coordination of national approaches will contribute to overall European solidarity
- a contribution of well-diversified supply portfolios including at European level a balance of long and short-term contracts, internal market mechanisms, improved cooperation and coordination among TSOs to deliver compatible services will be a foundation for improved supply security
- also the Agency for the Cooperation of Energy Regulators (ACER) has to oversee the development of effective converging technical rules and regulations and the Ten Year Development Plan, to enhance the robustness and interoperability of connected European grids
- in principal energy networks should be market-driven and self financing. Regulatory authorities should recognize the long-term benefits from investments which are not always quantifiable, such as enhancement of security of supply, and should ensure a fair, transparent return on new investments influencing the energy security of EU Member States
- market transparency should be improved in line with system users' suggestions
- building on the work of the EMOS unit, industry and policy makers should share views to ensure that forecast supply/demand scenarios are coherent and consistent

- through the Gas Coordination Group, a reinforced coordination and information exchange among Member States will further enhance security of supply, and provide a basis for a pragmatic approach to solidarity
2. Moreover, lessons can be learned from the January supply crisis. Eurogas has published separately its main conclusions, but overall the view is that market mechanisms and industry's rapid responses made a significant contribution to minimising the impact of the crisis in most countries. Where there were serious consequences, then these were because the market could not work efficiently and improvements are required. We have in mind principally greater market transparency, more options on bi-directional flows and improved interconnections and interoperability of the European gas systems.
 3. The answers to the questions in the Communication are to be understood in the context of the principal points.
- 1) How to define comparable security of supply standards that put equal, reasonable burden on market players while respecting the differences between Member States?**

As stated by the European Commission in its Communication, the current SOS directive has not provided for a harmonized framework in Europe: each country has elaborated its own definition of "security of supply" and "crisis of supply" and more or less rigorous policies have been set up at national level. For example, according to the Communication of the Commission on the Directive 2004/67/EC, the national definitions of partial disruption vary largely in terms of percentages and durations.

Equally the Commission is right in recalling that the differences between Member States in defining security of supply standards have to be respected, as the conditions determining such standards are very different in different Member States, as are the instruments the Member States would employ in the event of supply problems. In order that a robust level of security is reached throughout the EU, Eurogas recommends in the first place

- reinforcing the role of the Gas Coordination Group in monitoring by way of improved information exchange that all Member States have in place potential measures to meet possible security of supply disruptions
- the Commission to review the Member States' activities and advise them of any concerns they have. Member States giving cause for concern should seek to introduce improvements by choosing the most efficient means (among those listed in the annex of Directive 2004/67) to reach the required security of supply. In general, the principle of subsidiarity will apply to take account of the specificities of each Member State, but measures detrimental to intra Member State commercial transactions must be prevented, as these would present barriers to the internal market and negate solidarity aims and arrangements.

Security of supply standards must therefore take account of the supply situation, market characteristics, climatic conditions, the (share of natural gas in the) energy mix, the likelihood of shocks and the ability to withstand shocks in each Member State.

Within this framework approach, therefore, and in order to ensure a clear overview of the situation, Eurogas would strongly encourage a pragmatic risk based approach to assess each Member State's vulnerability to supply shocks. An EU methodology to assist Member States in carrying out their risk assessments should be explored, with the aim of increasing their transparency (and/or the homogeneity). A risk based approach considers the exposure to risk of each Member State based on its usage of gas, the range of sources and supply routes. Alongside this is an assessment of the tools available to that same Member State to react to a supply shock, be this from the demand side response of interruptible contracts and switching to alternative generation fuels, from the flexibility of storage assets and from the extent of

interconnection and the likely response in the marketplace for demands for additional gas flows. Through a combined risk based approach, each Member State can thus establish its risk profile and put in place the most appropriate safeguards to face likely disturbances. The security of supply standards resulting from this risk based approach should be specified by each Member State, for example in terms of accepted probability levels for peak and winter supply shortages. Eurogas considers that transparency on these standards will provide a better basis for any solidarity arrangements.

This risk-based approach would probably show that some Member States are well prepared for a crisis, while others have to improve their situation. Their improvements achieved if necessary through national action plans will contribute to the levels of security of supply at EU level, and at the same time again provide a better basis for any solidarity actions. This risk-based approach would take account of the assessed level of exposure to risk of different countries and the national circumstances that may shape its ability to achieve the capability of meeting determined disturbances. Results of the risk-based approach might be shared within the forum of the Gas Coordination Group which could help some Member States in evaluating and defining their strategies. This should also ensure that a common language on security of supply emerges.

The risk-based approach should not, however, become too detailed or onerous in terms of explanations or demonstration requirements; its strength lies in its adaptability.

Eurogas is aware of the ongoing discussion on an N-1 standards approach, according to which the failure of the largest gas infrastructure and/or supply source into a Member State should be compensated by the capacity of the remaining gas infrastructure. This approach is chosen by a few Member States but should not be a rule throughout the EU. In many Member States, notably those where the largest source covers 100% of supply, it would be an uneconomic approach. Solutions have to take into consideration the different supply patterns as well as different national grid configurations and cross-border links.

2) Should the Directive extend mandatory protection beyond households to power generators, small and medium sized enterprises or other vulnerable customers?

This question requires in depth consideration, in view of the diversity of situations in Europe and only preliminary comments can be given at this stage.

Household customers require protection not least because of the risks to life itself and because they have no alternative when disruption strikes, but with regard to other categories of customers, such as public buildings and other small users, Member States have different approaches in place reflecting their interests, and this should not be changed, although transparency on respective measures could be encouraged, perhaps as part of the risk-based approach mentioned above.

Eurogas considers that, large industrial customers can more easily engage in demand side response. They may be willing to incur interruption to operations for a period of time and in some Member States indeed may have entered into interruptible contracts in anticipation of occasional disruption. These large customers may also have an alternative source of fuel available to them, e.g. oil. The generation sector will also have alternative generation sources, which can be used if there is disruption to one source of fuel. There will be different combinations of actions in different Member States, and an attempt to harmonize approaches carries a risk of distorting decision-making and arriving at sub-optimal solutions.

It must be remembered that each measure potentially entails additional costs, ultimately paid for by consumers and that the benefit will – hopefully – rarely be necessary.

Therefore the Directive should not extend mandatory protection beyond households.

3) How should the regions for security of gas supply be best defined?

In respect of the variety of situations in Europe, a regional approach should be adopted for co-ordinated implementation of shared objectives. This acknowledges that as we move towards an internal European market, the regional level should also be taken into account when the aforementioned risk based approach is being applied by the individual Member States. This indeed encourages or requires Member States to work together to ensure that at least collectively they have sufficient SOS measures in place to respond to potential crises. By working together, Member States can thus take advantage of a greater range of tools that will ensure a more coherent approach to security of supply Europe-wide and improve the basis for a pragmatic approach to regional cooperation and EU solidarity.

Defining the regional boundaries best suited to address SOS concerns is not straightforward. The location and level of interconnection is not static and thus the ability of Member States to offer solidarity in times of crisis will vary over time as market structures evolve and competition develops. Here it should be respected that energy markets, in terms of hubs and congestion zones do not always mirror political borders. A country's ability to respond to a supply disturbance may also vary depending on the crisis' origin. The severity or duration of any crisis could also lead to a narrower or wider region being involved.

The first decision perhaps is whether to accept the existing GRI as a basis also for security of supply. In so far as robust and interoperable markets will contribute to security of supply objectives, this would seem a practicable approach. Perhaps it could be used as a starting point to assess the extent to which these regions are appropriate to deal with supply security, taking account of interconnections and interdependencies, but other issues could also be addressed in determining the relevant zones including

- the supply pattern including diversity and main axis links
- potential infrastructure including storage development
- share of gas in electricity generation

4) What should be the precise actions defined in the Community mechanism, in the regional and EU emergency plans? How can solidarity be economically compensated?

The first step of an EU crisis management mechanism is to identify (as early as possible) that there is a crisis at EU level. One entity is necessary at EU level to declare the occurrence of such a crisis. It has to be determined whether it is necessary that a preset list of conditions be established to decide if Europe (or a zone) is in a crisis, or whether it is sufficient that one or more Member States declare that their national emergency plans cannot manage the situation, or both. Eurogas agrees with the Commission that such national emergency plans need to be established under some harmonized principles. Furthermore, an approach to be defined at three levels (national/regional/European) should be promoted.

As to the precise community mechanism that should be set up at European level, it is difficult to elaborate a complete answer at this stage. An analysis of the recent crisis should give some practical insight. As a general approach, however, the risk assessment previously set out in response to question 1 should be carried out to assess different countries/markets' susceptibility to different types of supply shock and a preliminary approach can be developed following those results. Without listing each and every potential type of crisis, it is difficult to list the accompanying precise actions that might be necessary for a community mechanism in regional or EU emergency plans. It could be useful for industry and policy makers to develop and discuss crisis scenarios, within the aegis of the Gas Coordination Group.

An important part of the community mechanism is the availability of an early warning about problems. Therefore cooperation on border flow transparency, to permit direct monitoring of flows entering the EU, should be promoted. Also the role of the Gas Coordination Group to

improve first-hand communication between network operators, suppliers and shippers could be developed. Actions to facilitate the management of emergency situations should be promoted.

During a crisis at EU level the Gas Coordination Group should also be the main platform for exchange of information and assessment of the situation, based on Member States' reporting in accordance with a pre-agreed common format. The Gas Coordination Group should facilitate the communication between the Commission, Member States' national authorities and industry, but it has to deliver fast and efficient communication.

Irrespective of a community mechanism that could be activated after the identification of a crisis and that should in any case be based on market principles, it is important to encourage the conclusion of prior arrangements between companies, on the model of insurance contracts. Indeed, some supply companies preventively enter into mutually profitable commercial agreements with other suppliers to upgrade the SoS of their respective portfolios. Conclusion of such prior arrangements may also ensure that interconnection capacity is built or reserved, and that send-out- or production capacity and/or working volume is kept available, so that a wider range of solidarity options can be effectuated, once a crisis occurs.

It is also essential that the roles and responsibilities of different market players in the event of a crisis are clear. The subject of roles and responsibilities should also be covered in the national emergency plans.

5) How can security of gas supply be strengthened at lowest cost?

First and foremost security of supply policy must enable markets to deliver. The expected third liberalisation package introduces or reinforces a number of measures for this, including greater transparency of networks and storage usage, clearer rules on capacity allocation and congestion management, greater regional cooperation between network operators and between national regulatory authorities as well as harmonised rules for greater system efficiency.

Also one should not overlook the fact that security of supply does not only cover cases of short term disruptions. In a longer term perspective, a security of supply policy aims at establishing a framework enabling supply companies to contract gas supply portfolios that are satisfactory in terms of quantity, diversity, price, reliability and fair market power balance with producers. Mechanisms such as long term gas supply contracts should therefore be supported along with encouragement of the further development of liquid markets.

Eurogas would be pleased to bring its expertise to the development of the eventual proposals. The industry point of view is fundamental to the definition of a sound approach.