

EUROGAS POSITION ON SOS REGULATION**REGULATION ON SECURITY OF GAS SUPPLY REPEALING DIRECTIVE 2004/67/EC**

With its proposal published on July 16 2009, which provides for both preventive and emergency measures, the European Commission intends to reinforce the European framework relating to the security of gas supply.

Eurogas shares the European Commission's objective and **supports some essential principles promoted in the draft Regulation**: (i) the use of market based mechanisms as long as possible to ensure security of supply ; (ii) the definition of both preventive and emergency measures ; (iii) the need for a clear decision-making process at the EU level, particularly when several Member States are facing emergency situations and market based mechanisms alone are no longer sufficient to deal with the emergency; (iv) the promotion of regional actions; (v) the importance of information exchanges in particular in crisis situations.

However, Eurogas considers that **the draft Regulation still requires clarifications and improvements**. In commenting on this proposal, Eurogas would like to address the following issues: infrastructure and supply standards; definition of crisis levels; stakeholder roles and responsibilities; the regional approach; transparency of information.

I- On the infrastructure and supply standards proposed by the draft Regulation**1- On the necessity to clarify proposals and assess national and regional situations before setting up EU binding minimum standards (Art.6 and 7)**

The current text of the proposed Regulation would impose strong obligations upon Member States and natural gas undertakings since they would be obliged to comply within a very tight time schedule with high binding standards concerning both infrastructures and supplies (Articles 6 and 7). For reasons of technical, operational and economic feasibility as well as unclear definitions, **Eurogas considers that such an approach is not appropriate and suggests an alternative proposal which would be more progressive whilst effectively improving the current situation.**

Eurogas' proposal for an alternative process

Eurogas agrees that **common minimum supply and infrastructure objectives should be effectively explored at the European level**. However, for the reasons mentioned below, Eurogas believes that **a two-step approach would be more appropriate**. Indeed, rather than setting up mandatory European standards at this stage, the future Regulation should focus more on the requirement for Member States to carry out a **thorough risk and impact assessment and analyse their situation on the basis of a sound common methodology**.

The risk and impact assessment shall be carried out by each Member State in accordance with the common methodology, whilst allowing the Member State to take into account particular national circumstances and specificities where appropriate. The results shall be reflected in preventive action and emergency plans. These plans should be subject to peer review, possibly within the Gas Coordination Group (GCG), to ensure their appropriateness on a European level, notably with respect to cross border issues, as well as their mutual consistency. Similar plans could also be prepared at the regional level.

The suggested approach would represent an effective step forward from the current situation. It could finally pave the way for exploring a more prescriptive approach based on binding common European minimum standards for security of supply provided they would be based on a sound impact assessment, lead to proportionate measures which would be feasible from a technical and economical point of view and preserve the necessary leeway to take into account national and/or regional specificities.

The desirability of such an alternative approach is supported by the following difficulties which we see as regards the standards proposed by the draft Regulation:

Unclear definitions

Lack of clarity

Despite the draft Regulation defining infrastructure and supply standards in specifically dedicated Articles (Article 6 / Annex I and Article 7 respectively), there are still cross references and links between the proposed standards. This leads to confusion and for this reason the draft Regulation should be amended to clearly indicate if and when proposed standards are aimed at supply respectively infrastructure operations.

Serious problems with the “N-1 rule” definition

The N-1 rule is designed to ensure sufficient gas infrastructure capacities in the event of disruption. Provisions provided in Article 6 and Annex I are highly complex and are too unclear to ensure a harmonised implementation. This is notably the case as regards the notion of “*outflow capacity*”, especially when considering how to measure transit capacities and to take into account impacts in other countries (the cascading effect). Moreover, for the definition of “*the demand*” which should be taken into account in the calculation, it is not clear whether this refers to total consumption, firm demand, or demand from protected customers. To clarify this definition, Eurogas considers that demand shall refer to protected customers in order to ensure consistency between the infrastructure and supply standards. Finally, the climatic conditions to be considered are also unclear. Depending on the interpretation given to the different parameters, **results arising from the application of the N-1 rule might be totally different and thus put into question the meaning and implications of such a standard.**

Nature of supply standards

Article 7.1 defines binding supply standards aimed at preserving deliveries for protected customers even in the event of severe climatic conditions. Moreover, Article 7.2 requires the national competent authority to take measures to ensure gas supplies to protected customers for the period of sixty days of exceptionally high gas demand during the coldest weather period statistically occurring every twenty years, also in the event of an Emergency according to Art. 9.2 (3). **Such a provision might lead to an obligation which could be impossible for companies to fulfil, if the category of protected customers would not be limited to household customers.**

A doubtful economical, technical and operational feasibility

As regards the N-1 rule

For some Member States, **the N-1 rule may lead to huge investment needs in new capacities, generating significant costs and strongly impacting gas prices for final customers.** Its economic consequences must therefore be soundly assessed. This does not appear to have been the case at this stage.

Moreover, **in the case of a regional approach, the draft Regulation does not clearly state who will be in charge of the implementation of such standards,** nor does it state how the issue of cost allocations for regional based investment should be addressed within the regulatory framework.

Furthermore, the time needed to meet the requirements will vary considerably depending on national situations. It seems therefore difficult to set up a tight common deadline for all Member States. In any case, complying in 3 years with the N-1 rule is not realistic: **significant investments in new interconnections would require at least 5 or 6 years depending on their nature.**

Last but not least, in some Member States, the N-1 rule may not be the most appropriate and economically optimal standard to ensure security of supply.

As regards reverse flows

Imposing permanent physical capacity to transport gas in both directions on all interconnections **should not be required without first assessing whether it is technically and/or economically possible or appropriate in individual circumstances.** Again, a prior impact assessment is required. In this regard, the derogation process foreseen in the draft Regulation goes in the right direction but does not provide for a sufficiently clarified framework.

2- As regards the definition of protected customers

While household customers certainly require protection, Eurogas considers that a possible extension of the category of protected customers at EU level is a highly complex and sensitive topic requiring sound impact assessments. Moreover, extending the scope of protected consumers should remain a national prerogative since its appropriateness and adequacy should be assessed in light of national circumstances, notably the structure of the energy mix and the importance of gas in this mix. Therefore, the draft Regulation should not extend mandatory EU protection beyond households.

When Member States consider widening the scope of 'protected customers', they would have to consider the following points:

- Article 7.2¹ provides very prescriptive and broad obligations to be applied with respect to protected customers. These might not be technically and/or economically feasible for a wide definition of protected customers;
- an extended definition may involve a significant part of the national gas consumption and should be examined using a detailed cost/ benefit analysis;
- impacts at regional level should also be assessed, notably as regards the situation of neighbouring countries and the ability of any mechanisms used to cooperate with other Member States for each crisis level to adequately cope with a crisis;
- any measures to exercise solidarity in case of Emergency should be focused on household customers.

II- On the definition of crisis levels

Eurogas believes that the crisis levels as proposed in Article 9.2 and defined by the Commission could lead to confusion. During the first two stages, the market is fully expected to solve the problem, but during a real crisis/emergency, when market mechanisms alone are insufficient to cope with the crisis, the Member States should be involved.

¹ Notably, Article 7.2 foresees the obligation to supply protected consumers during any period of 60 days even in the case of an Emergency situation.

Each stage should be explained in detail and clearly distinguished one from the other to avoid any confusion in the event of an emergency. The three crisis levels we would propose can be summarised as follows:

- (i) early warning – information suggests that supply conditions could deteriorate in the near term. The market is expected to solve the problem without the intervention of the Competent Authority.
- (ii) alert – the supply disruption event that was forecasted occurs, but its scale does not yet warrant the declaration of an emergency under (iii) below. The market is expected to solve the problem without the intervention of the Competent Authority.
- (iii) emergency intervention – market based mechanisms have proven insufficient in managing the emergency and thus intervention by the Competent Authority is required within the framework of the emergency plan. Market based mechanisms and non-market based mechanisms may operate alongside each other in this phase.

Moreover, Article 9.2 should emphasize that regional solutions based on market based cooperation between undertakings should be possible at every crisis level.

Finally, Article 9.6 gives the Commission one week to verify whether the declaration of an Emergency is justified and whether it does not impose an undue burden on the natural gas undertakings and on the functioning of the internal market. We consider this to be too long.

III– On the need to clearly define the role of the different stakeholders

1) Need for a clear decision making process

Eurogas supports the need for a clear allocation of responsibilities between the different stakeholders. **This is especially critical in very severe emergency periods where several Member States are affected and where market based mechanisms alone are no longer sufficient to resolve the situation.**

Article 10 concerning “*community emergency responses*” addresses such specific situations and raises complex questions as regards the respective competences of the Commission, national competent authorities and Member States and who should have the final say. In this respect, **Eurogas would like to recall the industry’s need for a clear and stable legal framework.** In order to provide for rapid and appropriate actions, any overlapping of competences between the different authorities shall be avoided and this requires a well-defined and efficient decision-making process at the European level.

2) Role of gas companies

Article 3.1 of the draft Regulation clearly recognizes that “*security of gas supply is a task of natural gas undertakings*”. However, the three-level-approach defined in the 2004 Directive to ensure security of supply (I: companies; II: Member States; III: the Commission), is no longer clearly reflected in the draft Regulation. This principle should be reinstated in the draft Regulation as suggested in Chapter II of this paper concerning “the Definition of crisis levels”. Natural gas undertakings have indeed a key and leading role in ensuring security of supply.

In the case of an Emergency situation, the Commission should not have the power to directly require gas undertakings to change their actions as stated in Article 10.4 (1). Indeed, from the text of the draft Regulation it is clear that:

- the competent authority designated by each Member State shall be responsible for the implementation of the emergency measures provided in the draft Regulation; and

- the preventive action and emergency plans shall contain actions to be taken by, amongst others, natural gas undertakings.

Natural gas undertakings will be in direct relationship with national competent authorities and therefore should not receive instructions directly from the Commission because these instructions may not be in line with the actions the undertakings are expected to take in the context of the applicable national plans. **Therefore to avoid any conflict of duties and responsibilities and to ensure a clear legal framework, the reference to gas undertakings in Article 10.4 (1) should be deleted.**

3) Role of the Gas Coordination Group

As an expert Body composed of different stakeholders (gas industry representatives, ENTSO-G, the relevant customers, the national competent authorities and ACER), **the Gas Coordination Group (GCG) seems to be the best forum for discussion, sharing of experiences, as well as formal consultations and coordination with interested parties.**

Therefore, as proposed in Article 11 of the draft Regulation, the GCG should facilitate the coordination of the measures relating to security of supply. To that extent, as stated in Article 4.6, **the GCG should be routinely consulted by the Commission when reviewing national preventive action and emergency plans.**

This dialogue, cooperation and coordination **should in our view be maintained in times of emergency.** The current text of **Article 10 does not provide for a clear recognition of the role of the GCG in such a situation.** To clarify this point, Article 10.3 should explicitly state that the coordination process run by the Commission must involve the GCG, and Article 10.4 should foresee discussion within the GCG before any binding decision is taken by the Commission on Member States or national competent authorities; such discussions and coordination process should, however, at all times duly respect the confidentiality of commercial information.

IV – On the adequacy of a regional approach

The current draft recognises **the importance of the regional level and provides for a strong requirement for solidarity and coordination between Member States.** There is notably an obligation for the national competent authorities to address cross-border issues and to cooperate in order to ensure preventive action and emergency plans are mutually consistent. Member States are also encouraged to jointly elaborate regional plans. Finally, a strict prohibition is set up as regards any non cooperative behaviour, notably in the event of a crisis. **Eurogas considers that these essential principles should be preserved.**

Defining the regional boundaries best suited to address security of supply concerns will, however, not be straightforward. The location and the level of interconnection between Member States are not static, nor do energy markets always mirror political borders. **It should therefore be explored to what extent these regions could be best defined by the GCG after consultation with the gas industry.** We would propose that this should be done by taking into account the results arising from a risk-based assessment run at EU level, which should consider not least the location of existing and planned infrastructures as well as gas supply routes. Finally, the regions should group Member States which have strong links in terms of solidarity or where such links are to be further developed. The existence of interconnections is a key instrument for security of supply; solidarity is not feasible without sufficient interconnections. Building on this, solidarity arrangements should be implemented by means of commercial agreements and/or where applicable by agreements concluded between Member States.

In order to achieve these regional goals, it is essential that all of the institutions involved as well as natural gas undertakings consider how they will effectively work together and cooperate. For example, the efficiency of the GCG might be strengthened by allowing the possibility to create specific sub-groups addressing security of supply issues at regional level.

V- On transparency requirements

1- The need to preserve the confidentiality of commercial agreements

Eurogas fully supports the need to prepare emergency measures in advance, notably through commercial agreements since it enables market based mechanisms to fully play their role as long as possible, also in case of an emergency.

According to Art 9.1 (10), **national or regional emergency plans** should include a **list of predefined actions** such as **commercial agreements between natural gas undertakings**. According to Article 4.5, these plans are to be published and notified to the Commission. This raises concerns on confidentiality for those parties engaged in the commercial arrangements referred to.

Indeed, commercial agreements contain, by definition, highly sensitive commercial and corporate information. The communication of their existence and a fortiori the release of some or all of their content might seriously undermine the implementation of the contracts, lead to market distortions and even be prejudicial to security of supply (notably as regards the necessity to preserve the bargaining power of EU gas suppliers in their negotiations with external producers). **Therefore, Eurogas considers that the inclusion of commercial agreements in national plans, as foreseen in Art 9. 1 (10) should be deleted.**

2- The need to preserve sensitive information arising from supply contracts.

According to Article 12.6, **some highly sensitive data concerning supply contracts concluded with external producers** would have to be delivered by gas companies directly to the Commission.

Eurogas understands the need to enhance transparency for clearly defined purposes and with respect to specific information. However, the draft regulation requires **information that appears to be unnecessary to ensure security of supply and would instead raise very serious confidentiality issues.** Therefore, **it should be first clearly explained why the collection of this kind of information is necessary and proportionate to meet the objectives of the proposed Regulation.**

In addition, a consensus should be reached on the type of information to be collected and the way to submit it (for instance, it could be submitted through the national competent authorities in an aggregated format).

In addition, precise rules should be established clearly stating **to whom the information would be circulated and how assurance would be given as regards compliance with confidentiality requirements.**

Indeed, **insofar as such data would be notified to the Commission or to the national competent authority, strict rules applying to their staff should be set up.** For instance, for staff which has been exposed to this information, ex post cooling off periods might constitute an interesting option to be explored.