April 2022

Eurogas position on 'minimum gas storage obligations'

Eurogas recognises that the current market dynamics emerging from the geopolitical situation requires particular attention. The negative summer/winter spread limits incentives for market participants to put gas into storage and may not provide sufficient incentives for suppliers to factor in possibly security of supply risks. Eurogas recognises that additional incentives are necessary. EU energy market interventions require a balanced approach to avoid unintended consequences with potentially long-lasting negative effects on an otherwise well-functioning market.

The EU gas market is currently confronted with:

a) A potential Security of Supply risk in case of a sudden significant disruption of Russian gas supplies to Europe
b) High and volatile gas wholesale prices that impact gas consumers and indirectly also electricity consumers

Both problems are linked and interdependent, but a solution to one of the problems will not automatically solve the other and may even exacerbate it. For example, while imposing a minimum storage obligation may have a positive impact on Security of Supply *(provided that minimum storage levels are achieved before a significant supply disruption occurs)*, it also risks to further exacerbate the problem of high and volatile gas wholesale prices.[1]

Eurogas views regarding the proposed Amendments to Regulation (EU) 2017/1938

Art 6a (2) – Eurogas welcomes that the mandatory filling level for 2022 has been lowered to 80%. We recognise that such a target can in principle be a reasonable tool to respond to the current unprecedented crisis situation. However, Eurogas notes that a one-size-fits-all storage filling level applicable in each Member States may not be proportionate and may adversely impact some Member States.

National gas storage capacities compared to domestic demand vary greatly in the EU. Some have sufficient storage to cover their entire demand or more and some hardly have any storage capacities. Moreover, some Member States do not rely on gas storage capacities to modulate winter-summer demand. They may for instance rely on LNG.

It may therefore be appropriate to lower the filling targets at national level depending on national circumstances and where it is demonstrated that alternative tools are available to ensure security of supply.

Moreover, it will be critical to ensure that the mechanisms deployed to achieve the target are first and foremost market based. The Regulation must not undermine the validity of existing storage contracts for 2022.

Mandatory filling levels represent a market intervention. A persistent undermining of the commercial gas storage market must be avoided, as it could have disproportionate effects. It will therefore be necessary to continue to monitor the situation and assess, not only the level of a storage target but

[1] It is worth noting that the negative summer/winter spread was significantly exacerbated between 2 March, when first rumours about an 80% storage obligation at EU level emerged and 8 March, when a 90% obligation was announced as part of REPowerEU.

also whether a general storage target continues to be necessary in the long-term[2].

Art 6a (3) – Eurogas recognises that a degree of interim filling level requirements is needed if and when an overall EU storage obligation is defined. The definition of fewer milestones at Member State level should be considered. Eurogas considers that the national trajectories as currently proposed (intermediary filling levels) have a very strong limiting impact on market flexibility and lead to devaluation of storage facilities. Tailor-made solutions at Member State level would be a more efficient approach, which could be agreed in conjunction with the Commission. The European Commission's role should be limited to monitor filling levels and issue recommendations to Member States that are not making sufficient progress towards hitting the fill target.

Art 6a (6) – We welcome that the filling target does not apply in case of emergency. In case of a significant supply disruption or capacity restriction, it may be impossible to meet filling targets. However, we regret that the situation is limited to a Union or regional emergency situation being declared by the European Commission. We believe that filling targets should also not apply in those cases in which the emergency, has been declared by a Member State, or in case of a significant supply disruption making it impossible to meet filling targets. In such situations, the filling target should not be applicable in the concerned Member State.

Art 6a (7) – We would recommend a more flexible deviation rule on the filling trajectories (to be revised in accordance with our comment on Art. 6a (3)) and consider that it should also apply to 2022 targets. If filling trajectories are applied a 2% underfill tolerance is not enough, especially for this year due to short-term planning. We recommend a general rule of a underfill tolerance of up to 5 %, depending on the reasons for deviation.

Art 6b – Eurogas favours market-based mechanisms to make storage attractive. We welcome the recognition that measures 'shall not unduly distort competition or the effective functioning of the internal market'. We therefore consider that market-based measures must be prioritised. Measures that intervene in the market should only complement, but not replace market-based mechanisms.

> **Art 6b (1) (a) – The implementation of storage obligations for suppliers represents a barrier to market entry and an obstacle to the development of a liquid market.** Gas suppliers would be obliged to buy "out of the money" storage products without giving them the possibility to fully valorise them within their portfolios due to the fill target and any filling trajectories.
>
> Policy should in any case favour the definition and use of market-based mechanisms, and improvements to the current market rules, introducing further incentives to ensure adequate levels of booking/filling of storage and flexibility tools useful for preventing emergency situations.
>
> The introduction of obligations, or the use of interventions by regulated entities, should not represent a "shortcut" with respect to these market mechanisms, but should only be taken into

[2] The precise cost is impossible to predict with certainty as the market evolves continuously. Eurogas estimates the gross compliance costs for a 80% storage obligation in 2022, assuming 600 TWh of gas storage to be filled by 1 November and current wholesale price trends to be in the tune of €60bn, although this gross figure will be reduced by the extent to which booked capacity has already been hedged.

consideration on a residual basis and in the event of failure of appropriately designed market measures. When such residual options are implemented, suppliers should be compensated for the costs incurred.

Example: *After the introduction of the Polish storage obligation in 2017 the volumes of west-east cross border flows to Poland considerably decreased. The number of counter-parties active at the Polish hub (and not-affiliated to the incumbent) dropped dramatically and liquidity and supply competition also suffered. These were essentially the effects of shippers being forced to buy local storage from a limited number of actors and keep gas in store without the opportunity to monetise it, whereas storages across the Polish border, in Germany, Hungary, the Czech Republic, were eligible only if provided with firm yearly transport capacity to Poland - a requirement both inappropriate to increase SoS and prohibitively expensive. The Polish storage obligation is a good example for how particularly storage regulations supposed to increase supply security may implicitly raise market entry barriers and roll back previous improvements that were aimed at developing a truly integrated European gas market.*

Art 6b (1) (b) – Obligations on owners of storage to tender the capacities could be one of the options. For example, a proposal could be built based on the French and Italian mechanisms supporting the allocation of storage capacity, which have proven effective to ensure high storage level, above the EU average. In particular, the allocation of storage capacities via auctions in which products are allocated at their market value (and not the regulated tariff) makes these products more attractive for users.

In order for this option to be effective in a situation with negative summer/winter spreads, this would require removing the floor for storage capacity prices and allowing them to become negative. It would have to be ensured that storage owners are adequately compensated.

Art 6b (1) (c) – Eurogas considers that it should be left to the Member States to determine the entity that manages the purchase of any strategic stocks.

This should be reflected in the definition of 'strategic stocks' (Art 1 (1) (30)), which should not specify the TSOs as the entity to carry out those functions. Moreover, it should be made clear that strategic storage can only be activated in case of a physical supply emergency situations, and shall not be used to suppress market signals.

Where Member States chose such an option, it should in any case only complement other market-based mechanisms to incentivise minimum storage levels in order to provide a further guarantee in terms of security of supply. Questions on how and where the costs incurred by the TSOs or balancing operators are recovered would also have to be addressed.

Art 6b (1) (d) – Eurogas supports the general principle of improved coordination instruments to ensure the use of LNG to fill storage facilities.

Specifically, with regard to the joint procurement of gas or LNG, the proposal as drafted raises many questions and it remains unclear how such a mechanism would work. In a situation where the market still works, the creation of a joint purchasing structure should only be voluntary, involving market players, under conditions of guaranteed competition. In the event of a crisis - for example a disruption in Russian gas supplies - then provisions exist in European texts (SoS Regulation provisions). But if Member States were to intervene (e.g., tender for LNG purchases), they would in any case have to rely on commercial market players to purchase the gas volumes.

Eurogas also notes that long-term contracts are an important instrument for both enhancing security of supply and price predictability. LTCs underpin investments, maximise utilisation of LNG and pipeline infrastructure and incentivise production. This is especially true in a globalized LNG market where Asian buyers are competing to secure additional volumes. Market-based mechanisms could be considered to make medium/long-term contracts, which may not always be maximised, available to the system to ensure supply adequacy and provide medium-long term price signals.

Art 6b (1) (e) – Eurogas welcomes the proposal to provide financial incentives for market participants. One such mechanism could be two-way contracts for difference. Such a mechanism could incentivise storage capacity booking and filling by correcting the economic and financial effects of low or negative summer/winter spread and of high market price levels. Other market-based incentives, such as call options or fill tenders could also be envisaged.

Art 6b (1) (f) – Eurogas recognises the proposal to apply the 'use it or lose it' (UIOLI) principle in case target levels are not achieved. Unused capacity could also be released on an interruptible basis, to ensure that the flexibility of the capacity for the storage user will not be limited. It should be aimed at suppliers whose behaviour is clearly contrary to the objective of filling up storage target, and should not harm shippers acting in good faith, who should also continue to be able to have a certain flexibility in the use of their capacities.

Users with storage capacities contracted before the entry into force of the filling obligation and the UIOLI mechanism, should be left with the possibility to terminate their contracts and to offer them on the secondary market. This is necessary because the filling obligation and the UIOLI rules were not applicable when the capacity was contracted, resulting in a significant change in the regulatory framework (with respect to the one in force when the storage contract was signed) and, as a consequence, in the terms and conditions of the booked product.

Art 6c – Eurogas in general supports the burden sharing principle. However, the characteristics of Member States should be taken into consideration. It should be explicitly recognised that Member States have very different gas storage-demand ratios and that some Member States do not require gas storage capacities domestically or in neighbouring countries to modulate winter/summer demand. Moreover, we consider that the possibility for Member States to develop burden sharing mechanisms should be extended to Member States that have gas storage, but possibly not sufficient in relation to their demand and with no other means to modulate their demand and to ensure their security of supply.

Moreover, we note, that a lot of questions remain open and how such agreements could effectively be developed in the short-term. Member States are likely to require more details to find proper working solutions to tackle existing problems for instance regarding the solidarity principle or Art 13 of the SoS Regulation. In addition, examples exist of well-established of cross-border use of storage on a commercial basis, as well as security of supply products provided for in some Member States.

Art 6e – Eurogas recommends that the scope of the storage fill target and any trajectories is limited to seasonal underground storage. Fast cycle storage (e.g., salt caverns) should be left out of the target, as they are not used for seasonal modulation. It is also crucial that filling trajectories, if any, must ensure enough flexibility in order to fill the storages efficiently and allow for any technical or safety related constraints.

Eurogas views regarding the proposed Amendments to Regulation (EC) No 715/2009

Art 13 – Eurogas recognises the proposal to apply a 100% tariff discount to capacity-based transmission tariffs at entry points from and exit points to storage facilities. We welcome the proposal to keep the measure under review. It should be noted that Member States already today can decide to apply 100% tariff discounts, via the existing Tariff Network Code. It should be noted that a 100% discount increases transport tariffs for other network users and as such represents a form of cross-subsidisation. We therefore welcome that the Commission will re-examine this tariff discount after 5 years. In general, Eurogas considers that local regulatory regimes for example tariff levels or logistics costs such as IP tariffs and related pancaking effect can have a more important influence on cross-border competition between storage assets.