POSITION PAPER

July 2008

EUROPEAN COMMISSION STAFF DRAFT INTERPRETATIVE NOTES FOR ARTICLE 22 OF DIRECTIVE 2003/55 ON THE GAS INTERNAL MARKET

EUROPEAN REGULATORS' GROUP FOR ELECTRICITY AND GAS (ERGEG) DRAFT GUIDELINES (5.03.2008) ON THE REGULATORY APPLICATION OF ARTICLE 22 OF DIRECTIVE 2003/55

EXEMPTING NEW GAS INFRASTRUCTURES FROM THIRD PARTY ACCESS PROVISIONS

BUSINESSEUROPE COMMENTS

BUSINESSEUROPE considers that achieving significant progress in the competitive functioning and progressive integration of the European internal energy market is important. BUSINESSEUROPE fully shares the view of the European Commission that the competition of internal market is the only means to address, in an efficient and economically viable fashion, both the compelling targets imposed by the sustainability targets and the growing concerns for security of European supplies. In this regard, BUSINESSEUROPE believes that a favourable framework for infrastructure investments, ensuring both certainty for investors and pro-competitive measures , will prove to be the key challenge for EU policy-makers, both in the coming months, and in the light of the third energy package.

In this respect, BUSINESSEUROPE welcomes the efforts of ERGEG and the European Commission, in order to align best practices and clarify the way exemptions are assessed across EU Member States. It should be recalled that all industry stakeholders (including the Madrid Forum Joint Working Group meeting in July 2007 and the Madrid Forum October 2007 session) have on past occasions called for a careful assessment of actions in this field, in order not to jeopardise ongoing investments or much needed further developments, whilst safeguarding the role of the exemption procedure for exceptional cases.

CLARIFICATIONS NEEDED

First of all, in order to avoid uncertainties and misinterpretations in the framework for investments in new infrastructures, a certain degree of harmonisation and consistency across parallel processes is needed, especially when it comes to the scope and definitions applied within the exemption procedures. Proper functioning of exemptions as well as a sound pro-competitive effect of their application are also to be regarded as a key area for developing a common understanding and leveraging best practices.

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In particular, the Commission should better clarify its position in relation to the possible overlaps of the following processes:

- explanatory notes on article 22 of Directive 55/2003/CE;
- ERGEG guidelines on the regulatory application of the same article;
- regulatory guidelines concerning the SEE (South East Europe) region[1]

A streamlined approach will also be necessary for discussions regarding the proposed changes in article 22 of the gas Directive, as envisaged in the framework of the third energy package.

There are a number of questions:

1. **<u>What type of infrastructures can be subject to an exemption regime? What is the role played by the sources of natural gas in the process of evaluation and assessment?</u>**

The criteria whereby an infrastructure can be considered an "interconnector" should be clarified, thus ensuring consistency in the interpretations of the scope for granting an exemption. In the Commission's explanatory note (point 19) the definition of "major new gas infrastructure" can be applied to interconnectors between Member States (as defined by art. 2.17 of the gas Directive), to LNG and storage facilities. The definition applies also to significant increases/modifications to existing infrastructures, provided that they enable the development of new sources of gas (it is not clearly defined how this provision would apply to LNG and storage facilities). The definition of "major new gas infrastructure" can also be applied to projects which involve a high degree of cost and risk and that concern a market with a relevant size.

It should be noted that, while the need to provide advance information on the supply contracts or other elements proving the source of gas is established concerning an upgrade of infrastructures, this provision is not explicitly developed in details.

A further clarification is needed on the criteria and the degree of applicability of the exemption regime to part of the capacity or to part of the infrastructure. In particular when an exemption regime is granted to part of an infrastructure (e.g. to part of a cross-border pipeline), it is necessary to clarify what degree of regulatory consultation has to take place and what role the outcome has to play when the final decision is assessed at Community level (including potential pro-competitive remedies). If the exemption regime is thus foreseen for a limited part of an infrastructure, as in the case of an interconnector, there is a lack of clarity on how this provision might be assessed in the case of storage and LNG facilities, while preserving a case-by-case approach. This lack of clarity should be remedied.

[1] The approval/definition of regulatory guidelines in this region is proceeding together with the implementation of Gas Directive. Therefore, the explanatory notes released by the Commission could be a legal reference for the infrastructures affecting this region.

2. **How does the duration of the exemption relate to the risk associated with the investment?**

There is no explicit provision in the Commission's new explanatory notes as regards establishing a criterion for the definition/limitation of the duration for an exemption regime. It is worth recalling that the previous notes made reference to the payback period of the investment.

The Commission indicated during the Madrid Forum that the payback period of investment should be as long or longer than the exemption period. However this link is not made explicit in the Commission interpretative notes.

Furthermore, the source of gas is referred to in several documents (including past Commission decisions) as a significant element for the purpose of carrying out the risk assessment of the exemption request.
It is necessary to clarify how the link between foreseen gas sources and the investment risk should defined by the Regulators within a case-by-case assessment.

3. **Who is the ultimate owner of the exempt capacity?**

The Commission apparently considers that an open season procedure automatically guarantees the pro-competitive impact of the infrastructure as well as of the exemption decision. Much too little attention is paid, however, to the fact that the owner of the capacity, as resulting from an open season procedure, might itself not fall under the criteria set out for the exemption procedure in the first place (e.g. being a dominant player and thus encompassing the risk of not matching the first criterion). A more detailed assessment of the criteria currently highlighted shall be foreseen, in order to prevent exempted capacity being awarded to already dominant players. As an example the mentioned criterion of establishing a ratio between, on the one hand, the share of capacity of the infrastructure exempted by the decision to the benefit of a dominant player, and in the other hand its relevant market share, appears to be far too generic.

4. **What is the open season procedure (and how should it be regulated)?**

In both the ERGEG documents and the Commission's notes significant reference is made to the Open Season procedure as a key instrument for pursuing an application for exemption. In the Commission's explanatory notes a reference is made to the ERGEG Guidelines on open season (GGPOS) for the procedural issues concerning this practice.

In this respect it should actually be recalled that open season procedures are referred to on different occasions, where they are aimed at addressing different issues; they must thus be conceived, especially when they fall under the case-by-case practice foreseen in the exemption procedure, according to specific regulatory approaches, in particular when dealing with:

Regulated infrastructures (for which remuneration comes through the Regulated Asset Base - RAB)

- Open season is an *ex-ante* market test for a further development of the investment plans carried out by the transmission system operators in *regulated infrastructures*; in this case will the infrastructure fall under the conditions drawn by paragraph 2 ("application") of the GGPOS?

Exempted infrastructures (merchant)

- Ex-ante: open season is an instrument to accomplish the first and the second test envisaged by article 22 provisions. In this respect ERGEG has not yet developed a specific methodology for this kind of open season to happen (as per paragraph 2 of the GGPOS), neither has the issue been addressed in the ERGEG document. It should therefore be made explicit that the same assessment of the exemption criteria should apply in this case to both applicants of the exemption procedure and holders of the open season final capacity allocation. This is necessary in order to guarantee full consistency in the process and avoid the risk of "à la carte" procedures or discrimination across different assessments.
- Ex-post: in this case, open season should be a *remedy* aimed at safeguarding competition and balancing potential drawbacks in the exemption procedure. Nevertheless, the ratio between regulated and exempted capacity in this case must be determined in advance, in order to avoid an ex-post change in the parameters – e.g. the level of risk demonstrated by the business plan - according to which the exemption was granted in the first place. Furthermore in this specific case the open season procedure is regulated by the authority that requested the remedy in the framework of case-by-case assessment of the exemption request (and/or its revision by the European Commission). The open season is thus subject to specific needs, adjustments and conditions, as envisaged by the national competent authority under the supervision of the Commission.

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