



Position Paper on ERGEGs road map for a competitive single gas market in Europe

ERGEG has presented a discussion paper for public consultation on November 21st, 2005 concerning the development of a roadmap for a single competitive European Gas Market.

I. Questions on the General Part

GEODE welcomes the discussion paper as an important working basis. It regards the monitoring of the progress so far and the definition of a concrete working program as of major importance for the development of an internal gas market. The road map gives a capacious overview on the different deficiencies and therefore poses a good starting point for the further steps. ERGEG's approach mainly addresses **GEODE's** concerns. Further remarks will be made corresponding to the relevant points.

II. Questions on the Introduction

GEODE appreciates the approach of setting out precise requirements by investigating specific stages of development. Experiences can thereby be used efficiently and false estimations can be avoided. Nevertheless the regional initiatives should not be strictly limited on trading hubs but always keep in mind the development of the entire market system, even if only in the affected region. Otherwise an imbalance between the functioning of trading hubs and of other parts of the networks might occur. In addition, liquidity needed for effective trading on hubs and in between hubs can only be reached by considering the structures located underneath.

III. Questions on the current state of European gas markets

GEODE agrees with ERGEGs position that the existing legislative framework does not address all required conditions for a competitive market and the conditions addressed are not fulfilled sufficiently yet.

1. Unbundling

The new unbundling requirements set out in the Gas Directive have recently been adopted in most Member States. **GEODE** supports the general separation of the network operation from the rest of a vertically integrated company on TSO-level. These aggravated requirements were a consequence of a discriminatory practice by TSOs. A strict supervision of the new

unbundling requirements should form the basis for the decision whether to go even further and introduce ownership unbundling. In particular in Great Britain such separation has been the basis for the market entry of new players. British Gas even had to offer relatively high prices as long as it retained a market share of more than 40 %. This case exemplifies that the European institutions are still far from using all options for the regulation of the European Gas Market.

Beside ownership unbundling **GEODE** would like to stress the need for cross-border unbundling and the consideration of the therewith aligned questions of jurisdiction. A single gas market can only be achieved, if unbundling rules can not be circumvented by affiliations in other Member States. **GEODE** therefore strongly supports ERGEG's position and would like to urge the Commission to remain aware of both options.

2. Storage facilities

Access to storage facilities is currently regulated by Good Practice Guidelines adopted by the Madrid Forum. **GEODE** supported this adoption as a first step into the right direction. Should however the supervision of these guidelines result that the TSOs do not apply the relevant provisions, the European Commission should take the initiative and work out a proposal for a regulation on access to storage facilities. The recently adopted Regulation on access to gas transmission networks provides a good example for European legislation based on the participation of market players.

3. Investment security

Security of investors will be best provided, if liquidity and network access are improved. A functioning internal market does not only mean the absence of long term contracts but the possibility to offer the use of infrastructure to a multitude of potential contract partners. **GEODE** warns that the fear of losing investment security by turning away from contracted access should not lead to an extended use of exceptions from TPA.

Cost-orientation does not necessarily mean that investments could not be profitable, because both the Directive and the Regulation include this aspect and the risk could therefore be evaluated and taken into account by the relevant authorities. The national and EU legal framework must be consistent to create legal certainty and "development-perspectives" must be presented to encourage investments. Beside, the need to open up facilities to third parties might already be an incentive by itself, because existing infrastructure now has to be attractive to keep up in competition. Improving and extending would therefore be a necessary step anyways.



IV. Requirements/priorities for action

GEODE also agrees with the requirements of the building blocks ERGEG exposes, especially with respect to two major points, the establishment of a single European Gas Market strongly depends on:

- Network Access (Entry-Exit-Systems)
- Market Liquidity

Still **GEODE** would like to point out that both are not only necessities among the others, but prerequisites for every building block and should therefore be focused on first.

1. Network Access - Entry-Exit-Systems

GEODE strongly welcomes that there is a general consensus on entry-exit-systems as the best approach for network access. The idea of this system is to simplify trading procedures for the shipper within one market zone. **GEODE** wants to underline to be in favour of enlarging market zones to facilitate trading instead of creating a commercial service to manage interface between network users and multiple TSOs, which would require additional rules, contracts, monitoring and expenses. **GEODE** therefore accentuates, that by enlarging the market zones in an entry-exit-system a commercial service to manage interface for shippers would not be required, but inter-action would lay within the responsibilities of the TSOs.

Large market zones combined with fees calculated irrespective of individual transactions reduce the number of contracts and provide foreseeable network fees. Currently a multitude of market zones deters third parties from entering the market. The number of market zones should therefore be minimized. Large market zones would cover different hubs and storage facilities. Different hubs within one market zone would not only result in inter-hub competition but also in hub-to-hub competition. The same applies to storage facilities. If the use of such facilities within one market zone does not depend on the individual transaction, each shipper will decide case by case which hub or storage he might use. Market zones must therefore cover more than one network and should not be restricted to just one Member State. Ownership cannot be a relevant factor for the definition of market zones. **GEODE** would like to emphasize that action in this field is urgent as in particular the creation of sub-networks by individual network operators (e.g. in Germany) will increase the number of market zones.

GEODE also points out that the regional initiatives shall not reinforce existing borders between market zones though they are considered to be a progress on the way to a single market.

2. Market Liquidity

a) Long term contracts

Improvement of market liquidity is still insufficient, though it is essential for efficient trade. The gas networks are natural monopolies. Non-discriminatory network access for third parties is therefore of central importance, but long-term import contracts regulate the flow of gas into the Member States. Demarcation clauses, in which the free re-sell of imported gas is forbidden, or destination clauses worsen the market liquidity. Improvement needs to be achieved double tracked. First by reviewing long term contracts, to accommodate them to the aim of creating a competitive single market. Second by access to new sources, which has to be achieved to facilitate the creating of portfolios of upstream gas supply.

b) LNG

Due to the long-term decline of gas production within the EU, LNG will have to contribute to market liquidity and should therefore be focused on. According to Article 22 Gas Directive major new gas infrastructures, i.e. interconnectors between Member States, LNG and storage facilities, may, upon request, be exempted from the provisions on inter alia third party access. New LNG-facilities are a precondition for an increasing input of LNG into the EU. Such potential quantities support market liquidity. However, the non-application of the rules on third party access poses a serious threat to new market participants. An enhanced liquidity could be controlled by the few major players which already dominate the Gas market. The European Commission and in particular the national regulatory authorities should grant exemptions based on Article 22 Gas Directive only in a limited number of individual cases. The Article must not be used to restrict market entry by building new LNG facilities.

V. Gas and oil prices

Another important point all involved parties should keep in mind, are gas prices. The price for gas is based on the price of the competing energy sources, usually light fuel oil. The price for gas is not set by market procedures on basis of "offer and demand"-principles. This oil-based pricing system is therefore not compatible with an effective and competitive European Gas Market. Furthermore, the price for oil is significantly influenced by the OPEC-Cartel and a limited number of other oil producers. With regard to the increasing role of gas as an energy source, **GEODE** strongly supports any efforts by the European Commission or individual regulatory authorities to introduce market based prices.



VI. Conclusion

GEODE honors that much has been done so far: The Gas Directive sets out unbundling requirements to prevent any conflict of interests due to vertical integration on TSO level. The Regulation on access to gas transmission networks defines minimum requirements for TPA. Guidelines which are annexed to this regulation provide the chance for the European Commission to state requirements more precisely. But further development is still necessary to ensure that the legislative frame work will address all relevant aspects of a single market and will lead to the desired results.

GEODE therefore welcomes ERGEGs effort to point out priorities and to set out the way forward in the roadmap, also in view of increasing liquidity at hubs.

Still **GEODE** would like to emphasize, that focusing on the improvement of market liquidity in general and non-discriminatory TPA in the entire market network is indispensable for creating a single competitive European gas market and should therefore be taken as a basis for any other effort.

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