

ERGEG Gas Focus Group / Storage & Balancing TF
Guidelines for Good Practice for Gas Storage System Operators (GGPSSO)
Storage National Report - Italy

Introduction

On 15 September 2005, during the 10th Madrid Forum, ERGEG presented the preliminary results of its first monitoring exercise on the implementation of the GGPSSO. The Forum asked ERGEG to produce a follow-up report on the implementation of the Guidelines for the 11th Madrid Forum, to be held at the beginning of May 2006. On 7 December 2005, ERGEG published the final results of its report on "Monitoring the implementation of the GGPSSO". In parallel, ERGEG proposed to undertake a second monitoring exercise assessing the effectiveness of the GGPSSO, and the functioning of the market for storage services.

The two main findings of ERGEG's first monitoring report on the implementation of the GGPSSO were that:

- the level of implementation of some key areas of the GGPSSO was insufficient;
- compliance with some specific requirements of the GGPSSO needed further investigation, which might in some cases require **assessment at national level**.

The Terms of Reference of ERGEG's second monitoring report on the implementation of the GGPSSO, approved during the 17 January GFG meeting, call for a series of actions aimed at addressing these issues. As indicated in the Terms of Reference, it would be extremely helpful if each ERGEG member with storage facilities in their jurisdiction produced a short national report on storage (5 to 10 pages) (hereafter referred to as the "Storage National Report"). These reports should focus on those GGPSSO requirements which are easier to monitor at national level, e.g. confidentiality requirements.

The present document sets the basic outline of the Storage National Report. By outline, we mean a description of the main sections the Storage National Report ought to contain, in order to ensure a minimum degree of consistency between the different reports. The exact content of each section is however left to the discretion of ERGEG members, who are better positioned than the Gas Storage & Balancing TF to assess what issues are of critical importance in their respective markets.

The information presented in the 2005 Regulators' national reports should constitute the starting point.

The deadline for submitting the completed Storage National Reports is **14 March 2006**.

In order to ensure that all interested parties are consulted, ERGEG will send out a questionnaire to SSOs. Storage users will be consulted from May 2006, to gather their feedback on the implementation of the GGPSSO requirements after 1 April 2006. Their views will be particularly important in assessing implementation of the GGPSSO.

EREG intends to publish an initial report on the implementation of the GGPSSO in May 2006 and it expects to present its findings at the next Madrid Forum. EREG will issue a final report on implementation after it has an opportunity to consider responses to its initial report.

Any question on this questionnaire should be directed in the first instance to:

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1 Background information on storage in your country

1.1. Update of the information already presented in the 2005 Regulators' national reports, especially in case of further developments regarding the storage in market (or anything else affecting the storage market) in your country

Italy's storage system is composed of depleted reservoirs operated by Stoccaggi Gas Italia Spa (Stogit, 97.7 % of the market) and Edison Stoccaggio Spa (2.3% of the market) . Given the incidence of residential heating on Italy's total demand and Italy's strong dependency on imports, storage is essential to the gas chain's overall balance.

Stogit, an unbundled Eni Group company (100% owned by Eni S.p.A.), operates eight storage facilities, seven of which are located in the Po Valley (Brugherio, Cortemaggiore, Ripalta, Sergnano, Settala, Minerbio and Sabbioncello). The eighth and last storage facility is located in central Italy (San Salvo). Stogit's total active reserve (gas that can be extracted and re-injected seasonally, otherwise known as "working gas") amounts to about 13 bcm, 8 bcm of which is used for modulation, production operations and TSO purposes. Strategic storage accounts for 5.1 bcm.

Edison Stoccaggio, an unbundled Edison Group company (100% owned by Edison S.p.A.), has two small storage facilities (Cellino in Abruzzo, and Collalto in Veneto), with a total active reserve of about 339 mcm.

The Ministry of Productive Activities has granted Stogit authorizations to convert two new reservoirs into storage facilities at Alfonsine and Bordolano and to expand its existing storage facility at San Salvo, which will allow Stogit to increase its total active reserve by 3.7 bcm (work on the three facilities has however been temporarily suspended).

Authorisation procedures are also underway for six new storage sites (5 depleted reservoirs and 1 aquifer facility), for a total nominal capacity of about 5 bcm. The authorizations are to be assigned to three companies: Edison Stoccaggio, Independent Gas Management, and Geogas.

Stogit and Edison Stoccaggio offer three basic types of services: modulation storage (including storage for TSO purposes), storage for production purposes, and strategic storage.

On 21 June 2005, AEEG established the rules and criteria for access to the national storage system and the supply of related services. These are contained in Decision 119/05 and replace a provisional system in place during the past three years. The Decision includes immediately applicable rules as

well as criteria for the drafting of storage codes by storage companies. The rules and criteria aim at ensuring maximum transparency and impartiality and non-discriminatory access to storage.

Decision 119/05 not only regulates basic services; it also makes it possible to directly negotiate customized services, consistently with the general criteria contained in the Decision and principle of non-discrimination. The Decision also covers interruptible services. It reaffirms the possibility of transferring storage capacity from one user to another in the event that a consumer switches suppliers, and the possibility of trading capacity and gas in storage for ex-post imbalance resolution or other purposes. The Decision also includes measures aimed at addressing the problems posed by the current scarcity of storage capacity. These measures include a capacity allocation mechanism based on a precise order of priorities, strict provisions for unauthorized use of strategic reserves; detailed provisions for the coordination of the overall system by storage companies and constant monitoring of the performance of the system and of the patterns of storage users' behavior over the course of the year.

Decision 119/05 also contains transparency requirements. Among other items, SSOs must publish on their website a list of services offered with corresponding commercial conditions and available capacities, detailed year-ahead maintenance, upgrading and decommissioning plans, as well as figures regarding daily use of injection and withdrawal capacity updated on a weekly basis.

Finally, Decision 119/05 contains important provisions allowing for the sale and exchange of capacity and gas between market participants.

1.2. Description of your competences in the area of storage and of the role of any other bodies/entities involved (where applicable examples of the decision making process would be helpful, i.e. for tariff/price setting or capacity allocation mechanisms).

Under law 481/1995 and Legislative Decree 164/2000, the main functions of AEEG with regard to storage are:

- 1) tariff-setting;
- 2) the definition of rules with regard to transparency and capacity allocation guaranteeing free access to storage services
- 3) the definition of the criteria to be followed for the drafting of storage codes.
- 3) the out-of-court settlement and arbitration of disputes between users.

The main functions of the Ministry of Productive Activities relate to security issues and authorizations/exemptions for new investments

2 Effective implementation of the GGPSSO

2.1 Roles & responsibilities of Storage System Operators

2.1.1. Existence of a document setting out all terms and conditions for the use of storage by affiliates under GGPSSO § 1.3 and overall assessment:

- ? is such document in line with the general requirements of non-discrimination contained in the GGPSSO?

Such a document is not necessary in Italy where access to storage is regulated, and contracted on the basis of a standard storage agreement containing terms and conditions that apply uniformly to all market participants including affiliates of SSOs.

2.2 Necessary TPA services

2.2.1. Institutional arrangements surrounding exclusion of capacity from TPA:

- ? what entities are responsible for making decisions on this matter;
- ? what role does each of them play in the overall process?

Exemptions pursuant to article 22 of Directive 2003/55, to workover and maintenance and to article production operations are set and monitored by the Ministry of Productive Activities. AEEG is consulted regarding exemptions pursuant to article 22 of the Directive and also sets the norms through which the TSO gains access to storage (capacity used by the TSO for system operations is not exempt from TPA but the TSO is given priority access).

2.2.2. Role of your regulatory authority (and any other bodies/entities involved) in designing the menu of services offered by the SSO:

- ? is it completely up to the SSO to design services offered or is a relevant national regulatory authority consulted or in charge of approving this offering?

Pursuant to Italian Legislative Decree n. 164/2000, AEEG is responsible for approving the storage code developed in consultation with users (the approval process is still underway). This code must comply with the criteria laid out in Decision 119/05 and must describe the full range of services offered by each SSO. Legislative Decree 164/2000 states that three services are mandatory if requested: modulation storage, storage for production purposes and strategic storage.

2.2.3. Storage services tariffs/pricing methodologies:

- ? is your regulatory authority (or any relevant national regulatory authority) involved (e.g. by benchmarking storage tariffs, by regulating tariffs)?

Storage tariffs are regulated by AEEG. The law does not require the adoption of a benchmarking approach to tariff setting. Instead it requires the use of a price cap methodology.

The first regulatory period (2002-2006) ends on 1 April 2006. AEEG just set the storage tariff for the second regulatory period (2006-2010) via Decision 50/06 of 3rd March 2006. The new tariff is a single national storage tariff to be applied by both Italian SSOs.

2.2.4. Overall assessment of the menu of services offered by the SSO(s):

- ? are storage services offered in a way that facilitates competitive, non-discriminatory, and efficient access to best meet storage users' needs (in accordance with the requirements of the GGPSSO 3.3)?

As was previously mentioned (see point 1.1), Italy has been experiencing a critical scarcity of storage capacity during recent winters which has influenced and put pressure on the development of storage services. Given this context it has been difficult to develop storage services in a way that facilitates competitive, non-discriminatory, and efficient access so as to best meet storage users' needs. However efforts have been made to design capacity allocation mechanisms and congestion management procedures supportive of competition even in the face of potential bottlenecks (see point 2.3.1) and to impose the offer of unbundled services.

2.3 Capacity allocation and congestion management

2.3.1. Capacity allocation procedures and congestion management mechanisms, and the development of competition:

- ? are these arrangements likely to create undue barriers to market entry and not prevent market participants, including new market entrants and companies with a small market share, from competing effectively (in accordance with the requirements of the GGPSSO 4.1.a&c)?

Capacity allocation procedures and congestion management mechanisms are set by AEEG and aim at providing the necessary tools to enter the market. Capacity is allocated according to the following order of priorities: a) strategic storage b) storage for TSO purposes c) storage for production purposes d) modulation storage. Inside the modulation storage category, storage for household is prioritized. In case customers switch supplier, a rucksack or "capacity goes with the customer" rule sets in. When congestion occurs, pro-rata mechanisms are in place to ensure non-discrimination between storage users.

2.3.1. Description of the relationship between storage contract durations and capacity allocation procedures / congestion management

Because of the scarcity of storage capacity and allocation priority given to household customers, who may switch suppliers from one year to the next, only annual contracts are allowed. Longer contract durations could pose problems in terms of capacity hoarding and discriminatory capacity allocation.

2.3.3. Description of the relationship between PSO (Public Service Obligations) and capacity allocation procedures/congestion management

In Italy, market players that import gas from non-EU countries are requested by law to book strategic storages and, consequently, are given priority access to storage space relative to market players using facilities for seasonal modulation. The Ministry of Productive Activities sets the amount of relevant storage capacity that can be booked (currently 5.1 bcm). In addition, an obligation is placed on household suppliers, which are obligated to ensure supplies in the case of a "1 out of 20" winter. Priority access to storage space is also conferred onto market players to satisfy this obligation.

2.4 Confidentiality

2.4.1. Overall assessment of the arrangements in place to ensure that no information available to the SSO concerning its storage business is passed to other parts of the any affiliate (e.g. databases

related to storage operations kept separate, new IT systems being developed in vertically integrated undertakings developed separately for the storage business, separate buildings for the SSO and for the supply business):

- ? have these arrangements been monitored and by whom?
- ? are these arrangements effective?

Italian SSOs are legally unbundled, which makes the GGPSSO less indispensable than in other countries. Yet the GGPSSO requirements are important because they help reinforce an independence which legal unbundling alone cannot ensure. However, we note that even full compliance with GGPSSO requirements cannot ensure full independence in terms of information and, even more importantly as the Italian experience shows, in terms of governance and investment decisions. Indeed, despite a persisting excess of storage demand, Stogit has invested very little in new capacity, and this can be interpreted as a way to preserve ENI's dominant position in the downstream supply market. As was mentioned earlier in this report, Stogit has authorizations to convert reservoirs in Alfonsine and Bordolano and to expand an existing storage facility at San Salvo which would allow Stogit to increase total active reserve by 3.7 bcm. However, since 2001, Stogit has increased storage capacity by only 0.75 bcm. AEEG has overseen the liberalization of Italy's gas and electricity sectors since 1995, and has been able to witness the flaws of legal unbundling on numerous occasions. The weakness of legal unbundling with regard to gas transmission is in fact recognized by Italian law, which calls for ENI to lower its stake in the gas TSO to 20% by 31 December 2008. In a notice sent to Parliament and Government on 8 August 2005, AEEG called for similar measures regarding storage.

2.4.2. Overview of the content of the code of conduct/compliance programme with main strengths/weaknesses highlighted

Stogit and Edison Stoccaggio have codes of conduct which apply to the whole of ENI Group and Edison Group's staff. Edison's code of conduct contains three sections on ethical principles, behavioral rules and implementation rules. It consists of general business prescriptions that do not strictly address the relationship between affiliates of a same group. The implementation and any violation of the code of conduct are supervised by a Compliance Officer.

2.4.3. If compliance to the confidentiality requirements of the GGPSSO is poor:

- ? is it an issue for the development of the market for the storage capacity?

Since Italian legislation goes beyond GGPSSO requirements, our focus goes a little beyond compliance with GGPSSO requirements. The real barriers we see to the development of the market are the lack of storage capacity, lack of investments in new capacity, and ENI's control of affiliated storage facilities to maintain an excess of storage demand, create a barrier to entry for new entrants and preserve its dominating position in the downstream market. Once again, the solution to these problems would be full ownership unbundling. Codes of conduct can help ensure confidentiality of information but are insufficient because they leave margins of discretion to SSOs which can be utilized by to behave in a manner that may favor affiliates.

2.5 Transparency

2.5.1. Description, where applicable, of the process followed in case some of the information required by the GGPSSO is not published by the SSO(s) in your jurisdiction (e.g. notification to national regulator)

Most of the transparency requirements contained in the GGPSSO are already contained in national laws, Ministerial decrees and AEEG Decisions. They are mandatory and operators are subject to penalties in case of non-compliance. So far no action has been taken to correct violations.

2.5.2. Description, where applicable, of the process followed in case a storage user has made a request to a SSO so that the information about the aggregate use of storage is not published (e.g. review of the decision made by to national regulator).

Not applicable to Italy: storage users cannot ask for this kind of exemption.

2.6 Secondary markets

2.6.1. General assessment of the extent to which secondary markets are developed or undeveloped in your jurisdiction

Secondary trading of capacity and gas in storage is fairly developed. As was previously mentioned in this report, Italy's current regulatory framework lays out the basic principles underlying secondary trading: both gas and capacity can be sold or exchanged between market participants. Decision 119/05 establishes that AEEG will publish another Decision describing procedures for secondary trading in further detail. This new Decision will allow AEEG to further facilitate the development of secondary trading in Italy.

3 Need for other measures beyond the GGPSSO

3.1. Proposal of additional measures, at European level, if indeed the GGPSSO are not sufficient to ensure fair, transparent and non discriminatory conditions for access to storage, in the light and in the spirit of Directive 2003/55.

AEEG believes that under their voluntary form the GGPSSO have not proved to be of great impact on the storage market.

We also note that even high compliance levels may hide unfair and discriminatory conditions for access to storage. The GGPSSO's confidentiality requirements in particular seem ineffective in terms of inhibiting discriminatory use of storage facilities by SSO affiliates. The GGPSSO also do not resolve problems linked to biased investment decisions and congestion, which are of central importance if any third party access to storage is to occur. The GGPSSO's limited impact on TPA to storage in the primary market also affects the development of secondary markets. As we mentioned in previous sections of this report, the best solution to these problems, in cases where storage has not developed into a fully competitive industry, would be legislative action requiring full ownership unbundling of dominant SSOs, or at a minimum strong regulatory oversight.