Comments on
Capacity Allocation on European Gas Transmission Networks Pilot Framework Guideline
(Ref: E09-GNM-10-05, 10 December 2009)

N	Page	Item	Subject	Comment
1	2/10	**Abstract**	"… and to submit a non-binding framework guideline …"	Despite this clear indication about non-binding character of the Framework Guideline, the whole following content/substance of the document from its very beginning proves the contrary – the legally binding character of the Framework Guideline since it is establishing the core elements of the legally binding network codes to be developed later based on the legally binding Directive & Regulation. It is quite difficult to understand how it is possible to incorporate a legally non-binding document (Framework Guideline) into the subordinated vertical of legally binding documents to which Framework Guideline is an integral party to: legally-binding Directive 2009/73/EC at top level, legally-binding Regulation 715/2009 at second-top level, legally *non*-binding (???) Framework Guideline at third-top level, legally binding Network Code at fourth-top level. Please comment on this contradiction.
2	4/10	**F1.1 Scope**	…entry points to supply-only networks, entry points from LNG-terminals, and entry/exit points to or from storage facilities are not subject to this Guideline.	What is considered to be a "supply-only networks"? It seems that there is no definition of this term in the 3rd Package. There is no definition of the term "supply" in the Regulation 715/2009, and the definition of "supply" in the Directive/73/2009 is very broad ("'supply' means the sale, including resale, of natural gas, including LNG to customers" (recital 7), while "'customer' means a wholesale or final customer of natural gas or a natural gas undertaking which purchases natural gas" (recital 24)). (1) Whether the networks, located both within and outside the EU, through which Russian gas supplies are transported up to delivery points located within the EU, should be considered as "supply-only networks"? Whether exit points of such networks should be consider as "cross-border interconnection points" to which "the rules in this Guideline apply to"? (2) One of the basic philosophies of the 3rd EU Energy Package is to "create gas

				transport through zones instead of along contractual paths" (Gas Regulation 715/2009, recital 19). What and how this intention corresponds with the existing legal order of transit organized on a long-term basis "along contractual paths"?
3	4/10	**F1.2 Existing contracts**	"…transmission system operators shall amend all relevant clauses in capacity contracts and/or all relevant clauses in the general terms and conditions underlying the capacity contract existing prior to the application of this code in line with the implemented provisions within 6 months after entering into force of the code.."	Provisions F1.2 look very dangerous as it is unclear at this stage what particular items and provisions can be touched by these requirements. • Since it is not clear from F1.1 (see comment 2 above) whether the provisions and the (legally binding? – see comment 1 above) rules of this Guideline should apply to exit points of the existing transit systems through which Russian gas is supplied into the EU, whether it is not possible to interpret F1.2 in a way that demanded amendment need to be implemented in Russian long-term gas supply contracts with EU companies which contracts have their delivery points ("cross-border interconnection points" or "entry points of EU networks") inside the EU?
4	5/10	**F2 Third party access F2.1 Capacity products**	"…transmission system operators determine the firm and interruptible capacity3…" <u>Footnote 3:</u> As defined in art. 2 (20) of the Gas	Art. 2 (20) of the Gas Directive 715-2009 defines "available capacity". It is Art. 2(12) and 2(16) which define, correspondingly, "interruptible" and "firm" capacity.

			Directive 715-2009	
5	5/10	**F2 Third party access F2.1 Capacity products**	"…The capacity product design shall aim at developing of competitive gas markets."	From our view, in the interest of both gas consumers and producers, the capacity product design shall aim not only at developing of competitive gas markets (within the EU), but also at creating investment stimuli and guarantees for non-EU producers/investors in upstream non-EU projects. It is new investment in the non-EU gas producing states that will bring new gas flows to the EU market and would facilitate to its competitive character. This means that the capacity product design need take into consideration not only trade-related short-term products, but also investment-related long-term products with the understanding that for the investment-related activities in developing new gas production capacities the terms "long-term" and "short-term" shall be defined differently to their definition in Art. 2(14) and 2(15) of the Regulation 715/2009, according to which a dividing line between "long-term services" and "short-term services" is just one year period. For investment purposes long-term period equal to one year only is just a short-term one. For investment purposes duration of long-term period of capacity products shall exceed the pay-back periods in order to exclude contractual and/or physical congestion problems. An illustrative example: capacity product with the duration of 3 years will fall under definition of "long-term" in the 3rd EU Gas Package (according to Regulation 715/2009), but will not be sufficient for investors in new upstream gas production facilities and would not be considered in practical terms as "long-term" since it will not cover objective investment needs of the gas producers. This means that economic sense of definitions "long-term" in gas production and gas transportation (capacity allocation) should correlate to each other which they does not nowadays in the 3rd EU Gas package.
6	5/10	**F2 Third party access F2.1 Capacity products**	"The offer and use of separate capacity for transit purposes shall be forbidden".	Despite the very clear and restrictive statement in regard to transit and transit-related capacity, the term "transit" is not defined and is hardly ever mentioned in all gas-related documents of the 3rd EU Energy package: (1) The term "transit" is mentioned only once in the EU Gas Directive (2009/73/EC) - in preamble of the paragraph 6 of Article 52 "Reporting", according to which "the Commission shall, no later than 1 January 2006 (???), forward to the

				European Parliament and Council, a detail report outlining progress in creating the internal market in natural gas", including, in particular (in the third bullet point), "*the conditions of transit*": • Does the lack of attention to transit matters & absence of definition of the term "transit" mean that the authors of the 3rd EU Energy package are not actually interested in the transit-related issues? Or this need to be understood in a different manner, for instance, that the EU would prefer that transit-related issues (both within and outside the EU) need to be regulated by the common set of universal internationally-binding rules, including for the EU, such as, for instance, the Energy Charter Treaty (ECT) and its draft Transit Protocol (the only available today set of international legally-binding rules related to transit)? • What does the term "transit" mean in the 3rd EU Gas Directive? Is it a common legally-binding understanding in accordance with Article 7 of the ECT with regard to the fact that all EU member states and the EU as a whole are the ECT Contracting Parties? (2) In the Regulation 715/2009, transit is mentioned only in Paragraph 8 of Annex I-1 ("Guidelines on third-party access services concerning transmission system operators"), where it is stated that "transmission system operators shall cooperate with other transmission system operators in coordinating the maintenance of their respective networks in order to minimize any disruption of transmission services to network users and transmission system operators in other areas and in order to ensure equal benefits with respect to security of supply *including in relation to transit*". • The problems & the questions are similar to those stated above under (1). (3) Finally, in this Pilot Framework Guideline for Capacity Allocation the term "transit" is mentioned only once as well (in the cited par. F2.1 of Article 5 "Capacity Products"), where it is rather categorically prohibited to offer and use the particular transmission

				capacities for the transit purposes in the framework of the third-party access (par. F2 is entitled "Third Party Access") by stating that "The offer and use of separate capacity for transit purposes shall be forbidden", without any visible relation with the previous context. • What is the meaning of the term "separate capacity" in this regard? • Whether the consequences of this proposal, if adopted and implemented, for the existing transit flows of non-EU suppliers within the EU territory (through the territories of the individual EU member-states) have been analyzed and if so, what is the proposed solution of the economic and legal problems which would arise? • Whether this draft proposal is not in contradiction with the provisions (the letter and the spirit) of Article 7 "Transit" of the Energy Charter Treaty (to which both the EU and the EU member-states are the Contracting Parties) aimed at providing for stable, reliable and non-interruptible transit which can be best achieved by providing separate (either physical or contractual) capacity for transit? At least Article 1.2 "Definitions" of the draft Energy Charter Protocol on Transit, which was agreed at a technical level by the experts of the EU and of the RF, in the definition of "Available Capacity" for Transit (as the term "Transit" is defined in the ECT) is aimed at contractual separation of capacity for transit purposes. • What is to be done if the gas pipeline in question has obtained the required exemptions, and the signed contracts presume exactly the transit through some EU member state using 100% of the gas pipeline capacities? Can such transit be effectuated, or should the pipeline be under-loaded? And what is to be done if, not regarding the exemptions, there are simply no other claimers for these capacities?
7	6/10	**F2.3 Breakdown and offer of capacity products**	"…Depending on the market's needs and conditions, transmission system operators shall	The existing definitions of "short-term" (less than a year-long) and of "long-term" (more than a year-long, see. Art. 2(15) and 2(14) of the Regulation 715/2009 correspondingly) refer mostly/only to trade services and do not correspond to the investment activities in upstream. From the producer point of view "long-term" should mean a time-horizon exceeding pay-back period for its upstream investment project.

			determine the breakdown of available capacity between the different long and short term capacity products."	An illustrative example: So in order to diminish investment and transportations risks, and to exclude transportation capacity congestion problems, and thus, finally, to diminish the costs of gas to the end-users, the "long-term" should be re-defined or (if not possible) address upstream investors, including non-EU investors, considerations. How this issue should be addressed in the Framework Guideline and Network Code?
8	6/10	**F2.3 Breakdown and offer of capacity products**		Mechanism of "breakdown of available capacity between the different long and short term capacity products", presented in the first paragraph, might be reasonable assuming that allocation is already realized for existing long-term contracts (i.e. allocation of a part of technical capacity in line with existing long-term supply contracts). Such allocation should be done well in advance of any other capacity allocation procedure (for instance, through the open season procedure). • It is not clear from the Guidelines whether this is a case and what does the term "available capacity" mean to which F2.3 applies. • Whether the term "available capacity" is defined here (in framework Guidelines) according to its rather broad definition in Regulation 715/2009, recital 20, or according to it most detailed definition in draft Energy Charter Protocol on Transit? • If, on the contrary to the above-stated, the mechanisms of breakdown presented in this section are to be applied to all capacity, or in definition of "available capacity" not all four deductions are taken into account (as agreed in its definition within the draft Energy Charter Protocol on Transit) then this mechanism definitely can't be acceptable because it will place on equal footing the long-term supply contracts linked to long-term investment decisions, on the one hand, and the short-term/spot transactions related to trade (resulted with physical deliveries) and speculations (not resulted with physical deliveries) of gas. Equal treatment of different types of transactions (with different economic background) in these circumstances should be considered as discrimination of long-term contracts.
9	7/10	**F2.4 Cross-**		Complex topology of networks in question may lead to real problems in implementation of this section. For instance, exit pipeline system may lead to a

		border products F2.4.1 Combined products		number of adjusting zones, with different corresponding capacities while, for instance, an entry system is a single pipeline. So though formally a TSO may suggest the same exit capacity (equal to an entry capacity) for a combination of exit pipes, but physically capacity available for users will depend on flow directions.
10	7/10	**F2.4 Cross-border products F2.4.2 Bundled products**		It is completely unclear whether "bundled products" as they are described in this section can be effectively presented to the market. Arguments expressed above regarding F2.4.1 can be significantly enforced in case of complicated topology of a set of zones.
11	8/10	**F3 Primary Capacity Allocation**	"Capacity allocations shall not take place outside the standard allocation procedures as applied according to this Guideline".	Further to this statement, only three paragraphs are further presented in the F3: (1) F3.1 Auctions; (2) F3.2 Pro rata; (3) F3.3 First come first served. Does this mean, that: • these three options presents the closed list of standard allocation procedures? • since such allocation procedure as "lottery", despite the fact that it has been even used in practice within the EU (for instance, within the capacity allocation procedure in May 2008 at the second stage of expansion of the TAG pipeline), is not included in the list of "standard allocation procedures as applied according to this Guideline", it shall not be implemented further within the EU?
12	8/10	**F3 Primary Capacity Allocation F3.1 Auctions**	"The network code shall set out that firm capacity products are allocated via auction. The network code shall set out the principles and possible options of anonymous and transparent online-	There is no reference to implementation of necessary investments when there is clear evidence that in the reasonable time horizon available capacity is zero or not sufficient for market needs. There should be therefore clear link between provisions of chapter F3 and Ten Years Network Development Plan, and corresponding procedures should be in full coherence. If such coherence is properly established then the role of auctions (F3.1) would be quite different – auctions might be used only for short term allocation procedures. In the current text of F3.1 there is no such limitation.

			based auction procedures."	
13	9/10	**F3 Primary Capacity Allocation** **F3.3 First come first served**	"The network code shall set out that transmission system operators jointly offer and allocate any firm capacity becoming available after allocation of day-ahead firm capacities according to the first come first served principle or via an auction. […] With the possible exception of intraday capacity, transmission system operators shall not allocate any capacity according to the first come first served principle".	Whether there is no contradiction between the first and the last sentences of this paragraph? It seems, that they are mutually exclusive…
14				Conceptually, we see a whole set of discrepancies which need to be addressed and settled: • The long-term contracts are considered important as well as the necessity of their fulfillment, and at the same time the mandatory requirement to release some portion of capacities for the short-term deals have been stated. The Russian party has made its proposals how to settle this issue to the mutual benefit of all the parties involved during the negotiations on the draft Energy Charter Protocol on Transit, but such release should be provided with the corresponding development of infrastructure as well as

				regulation (motivation) of this process, and not by means of forceful restriction of the possibility to fulfill the existing contracts. • It is not substantial for the most of existing transportation contracts of transit character how they are (would be) titled ("transit" or "transportation" contracts), or whether the special capacities will be allocated for them, if the character of such contracts is adequately considered (long-term continuous contracts, ones with flexible nominations by the purchaser) and their fulfillment is provided. The draft Guideline does not demonstrate such understanding, and the requirement to review all existing contracts and to bring their content in line with the new rules (Art. 2 "Adaptation of existing capacity contracts"), which are absolutely not yet clear for the moment, seems potentially dangerous for the (security of) EU gas supply. • Increased attention given to liquidity assurance problems in the draft Guideline does not provide clear results, since, to our opinion, it is not accompanied by the adequate attention to the investment process which is an obligatory precondition of increasing liquidity of any market; and, as it is well known, creation of the liquid market is effective, if either the significant excessive supply capacities are already available (in result of past investments of suppliers stipulated by the corresponding incentives) or adequate current investments are provided.

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