



Mrs. Fay Geitona
Secretary General
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Dear Mrs. Geitona

BG Group Response to ERGEG Public Consultation on Draft Guidelines on Article 22 Exemptions.

BG Group welcomes the opportunity to comment on ERGEG's Draft Guidelines on Article 22 Exemptions.

We have the following general comments:

- The Article 22 Exemption process has been a valuable means for enabling investment in new infrastructure in Europe. It enables regulators to regulate only where it is necessary because of issues of potential or actual market failure (for example where there is a natural monopoly), and tailor the nature of the exemption to the individual circumstances of the project applying for exemption.
- Guidelines on Article 22 Exemptions can be helpful in giving greater certainty and clarity to project developers as to what is required when applying for an exemption. However they should not be a substitution for regulators and the European Commission being able to decide each case on its merits, according to how an application meets the criteria as detailed in the Second Gas Directive. (EC/2003/55).
- It is, however, essential, that full or partial exemptions do not enable dominant players to bypass the requirements for regulated third party access, and thereby prevent the development of a liberalised European energy market. This is especially important in a world where dominant players are part of vertically integrated undertakings, and where TSOs are not ownership unbundled. For this reason a rigorous competition assessment of the relevant markets, and the project's impact on those markets, is essential.
- Exemptions should not be seen as a substitution for investment by regulated TSOs or other regulated infrastructure owners or operators. It is therefore essential that regulated infrastructure companies have clear frameworks, incentives and obligations that enable them to meet market demand for new investment, and maximise the release of existing capacity. Although this issue is outside the scope of this consultation it is essential if Europe is to develop a liberalised energy market with an appropriate balance of exempt and regulated infrastructure.

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Do you consider the described general principles and guidelines appropriate to achieve a consistent and transparent framework for competent authorities when deciding on exemption procedures?

Overall yes, subject to the comments elsewhere in this response.

It is also important that regulators have clear and transparent processes for granting exemptions, including consultation of market participants. The Guidelines should consider asking for greater transparency as to how decisions on exemptions are made by the relevant authorities.

Do you consider the present scope of eligible infrastructure to be too narrow?

No. We do not consider it appropriate, for example, that TSOs could apply for exemptions for transmission infrastructure. Rather TSOs should have the correct incentives and obligations to meet reasonable market demand for new infrastructure.

Do you consider open season (or comparable) procedures an important tool in assessing market demand for capacity with respect to determining the size of the project applying for exemption, as well as in the subsequent capacity allocation? Should open season (or comparable) procedures be mandatory?

Open seasons can be a useful tool in assessing market demand for capacity and in allocating that capacity. They can be useful in assessing whether a project applying for an exemption has shown that it would be beneficial for competition by enabling new sources of supply or new entrants to a market. However they should not be mandatory as it may be possible for a single company project developer to meet the exemption criteria without an open season. The success of infrastructure projects may depend on the choice of the companies involved in the project. An open season may add uncertainty to this project which could cause it to fail. In addition, an open season may bring an incumbent into the project which could have implications for the nature of an exemption. It should be up to a project developer to decide how best to structure his project in order to obtain an exemption which suits his needs. The form of any exemption should then be decided by the regulator based on analysis of the exemption application on a case by case basis.

Should open seasons also be used to allocate equity?

No. An "open season" for equity in the project could compromise the financial viability of the project and thereby cause it to fail. It is not clear how an open season for *equity* would improve third party access to *capacity*.

Some stakeholders think that Art. 22 should be applied differently to LNG terminals as they may be generally better suitable for enhancing competition and security of supply than other types of eligible infrastructure. What is your point of view on this? If you agree, how should this be reflected in the guidelines?

Article 22 already allows regulators to assess exemptions on a case by case basis. By definition this enables them to take account of specific circumstances of LNG projects, their differences with other infrastructure projects, and their ability to enhance competition and security of supply.

Are the described criteria for assessing the effects of an investment in infrastructure on enhancement of competition in gas supply appropriate?

Overall, yes. Market share analysis is nonetheless not sufficient on its own; an assessment of barriers to entry and the ability of companies to compete for customers,

and customers ability to switch, is also important. However it should be noted that a simple decrease in a dominant player's market share as a result of a project may still leave that player with considerable market power. It would therefore be hard to see how a project in such circumstances could be granted an exemption.

Are the described criteria for assessing the effects of an investment in infrastructure on enhancement of security of supply appropriate?

Yes.

Are the described criteria for the risk assessment appropriate?

Yes.

Are the described criteria for assessing whether the exemption is not detrimental to competition or the effective functioning of the internal gas market or the efficient functioning of the regulated system to which the infrastructure is connected, appropriate?

There is one case where the described criteria is not appropriate. In cases where the project might "cause constraints on the regulated system requiring investments having a significant adverse effect on the welfare of system users", regulators should consider if the framework governing the regulated system is appropriate. It would be unfortunate for example, if TSOs which were part of vertically integrated undertakings, were able to use this criterion to frustrate the projects of new entrants who would otherwise qualify for exemption. TSOs should have clear and transparent mechanisms governing network investments and who should bear the costs. Project developers should be able to take these into account when developing their proposals. So long as projects are able to meet the relevant criteria (for example booking procedures, level of commitment etc.) for new investment they should be able to connect to the regulated system.

To what extent should consultations with neighbouring authorities be done?

Where the exemption concerns an interconnector, there should be consultation with neighbouring authorities. It would be helpful if the relevant authorities can agree a joint consultation process to minimise the regulatory burden on market participants.

Parts 3.3.1.1 and 3.3.1.2 of the proposed guidelines deal respectively with partial and full exemptions. Do you consider the described decisions (partial/full exemption) appropriate in safeguarding the goal of Directive 2003/55/EC in making all existing infrastructure available on a non-discriminatory basis to all market participants and safeguarding the principle of proportionality

Partial exemptions can play a role in enabling investment in new infrastructure whilst retaining some measure of regulatory control. Care must be taken that partial exemptions are not used as a means to enable dominant incumbents to benefit from exemptions. Similarly partial exemptions should not be used as means to continue to regulate infrastructure where it would be appropriate to have a full exemption. As with all exemptions, every project and potential exemption should be considered on a case by case basis recognising the trade-offs between the different forms of exemption.

When assessing the duration of the exemption, it may be necessary to take into account factors other than the payback period of the infrastructure. For example new sources of supply may need certainty of capacity over a period to make their project viable. As with all aspects of an exemption regulators should consider such issues on a case by case basis taking all relevant factors into consideration.

Do you believe that Art 22 exemptions should also benefit incumbents or their affiliates? If yes in what way and to what extent?

It is difficult to see how Art 22 exemptions could be granted which benefit *dominant* incumbents or their affiliates without being detrimental to competition. However it is possible that a project could benefit an existing market participant who had no or very limited market power. In such a case the competition analysis would show that an exemption would not be detrimental to competition.

Do you agree that under certain circumstances, deciding authorities should be entitled to review the exemption? How can it be assured that this does not undermine the investment?

It is appropriate for the regulatory authorities to have the option to review an exemption. However the circumstances under which such a review takes place must be very clearly laid out in advance, there must be scope for the exempted project to rectify any problems rather than automatically lose its exemption, and the terms of review must be relevant to the original conditions on which the exemption was granted. Any review procedure should not be able to be used as a means for “backdoor” regulation as this would create uncertainty for projects and would be detrimental to investment.

Should you have any queries please do not hesitate to contact me on ++ 44 118 929 3442 or at alex.barnes@bg-group.com.

Yours sincerely

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