

Response by IFIEC Europe WP Gas to the DG Competition Energy Sector Enquiry, Draft Preliminary Report.

IFIEC Europe (IE) represents the interests of industrial energy consumers in Europe for whom energy is a significant component of production costs. Energy prices are therefore a key factor for their global competitiveness. This part of the response deals with Gas.

General Comments

1. IE welcomes and supports the analysis made by DG Competition. However, IE stresses that some clarifications have to be made and would like to use the opportunity to make some recommendations regarding the way forward.
2. The report gives a thorough analysis of the issues but it remains an analysis and IE is concerned at the paucity of decisive measures needed to correct the situation now prevalent in the EU. We are looking for clear specific actions which will be taken to correct the shortcomings of the market soon, in order to safeguard a reliable and sustainable supply of gas to industrial gas consumers at competitive and transparent prices in the long term. This objective is perfectly in line with the Lisbon Agenda, which gave priority to the implementation of a framework in which the long-term competitiveness of the European industry is to be developed.
3. Failure to progress the liberalisation process, resulting in gas prices which are uncompetitive globally, despite plentiful availability of gas from sources relatively close to Europe, has already caused significant hardship to manufacturing industry in the EU. Time is now of the essence and tough actions must be taken.

Specific Comments by Section. (Restricted to Section B: Gas and Section E Way Forward)

I.1 Main market features

We have no comments.

I.2 The regulatory framework

Paragraph 38. IE notes the ineffectiveness of non-binding instruments. The most recent example is the Guidelines for Good Practice for System Storage Operators (GGPSSO). In the experience of our members much of the agreement which was hotly debated as part of the Madrid process has not been implemented by the gas companies.

Paragraph 40. This key issue of concentrated market structure is identified but not properly addressed. It is also rather misleading to suggest that the problem is all 'inherited from the monopoly era'. There are examples of market concentration increasing in the 'liberalised' market. Even in parts of the EU where competition is regarded as successful, e.g. the UK, we have concerns. A clear distinction must be drawn between the retail market, largely supplying domestic and small commercial consumers, and the wholesale market, which effectively sets the price to industrial customers. The retail market is very competitive with suppliers fighting for market share on relatively tight margins. The wholesale market, on the other hand is much less competitive and severe lack of liquidity creates problems for industrial customers who, quite reasonably, want to fix their gas prices more than a month or two into the future. In the Netherlands, competition is being hindered because most gas originates from one market player, controlling both domestic production and a large share of the import. Hence, downstream players are forced to source most of their gas from this dominating party.

Paragraph 44 deals with derogation from Third Party Access rights. IE believes that the report fails to give a balanced view of the issue which has arisen. Virtually every recent infrastructure project in the EU has qualified for exemption. The reality is that the powerful gas companies simply inform national governments that projects will not go ahead without derogation from TPA and that statement appears to be taken for granted on every occasion.

Paragraph 45 deals with unbundling. IE believes that full ownership unbundling in the case of storage, pipelines, and LNG facilities is absolutely essential.

I.3 Gas wholesale markets

Industrial and commercial customers must have freedom of choice over contractual terms.

It is important that ways are found to ensure development of liberalised wholesale markets taking account of the comments made above in I.2 paragraph 40.

II.1 Concentration

IE fully agrees with the conclusions in this section of the report.

IE notes that the 2nd Gas Directive has yet to be implemented in a number of member states.

More radical gas release programmes are needed under the proper working conditions and terms. If not, these programs will have adverse effects as shown recently in the South of France. In the Netherlands a 'small fields

policy'¹ was put in place a number of years ago in order to preserve the large Groningen field and keep its flexibility properties at a required level. IE does not oppose against any arrangement made as such, but this arrangement takes away any incentive from small fields producers to sell gas to third parties apart from the incumbent, thereby increasing the incumbent's market power.

Tougher co-ordinated cross-border regulation is required.

The voluntary GGPSSO guidelines must be enforced immediately.

Measures to encourage market liquidity need to be implemented.

Difficult issues which result from the nationally or European dominance of a few large producers including Gazprom need to be addressed.

II.2 Vertical Foreclosure

IE fully supports the conclusions,

Use It or Lose It (UIOLI) regulations must be put in place and rigorously applied.

Tougher legislation is required to prevent vertical foreclosure.

Regulators must urgently address the fog which surrounds transportation bottlenecks which we believe are largely (but not entirely) contractual rather than physical.

II.3 Market Integration

IE agrees that the conclusions reflect the status quo.

IE believes that imaginative solutions are required. Ownership unbundling of transit pipelines is needed. Governments or the Commission may need to play a role, e.g. as guarantor, in ensuring funding is available for new capacity.

It is important to separate infrastructure issues from gas market issues.

A market conformable congestion management system is required to avoid any commercial congestion. In our experience congestion due to contractual constraints is more frequent than real physical congestion. If auctions are used as a mechanism to allocate capacity in the case of physical congestion, the revenues must be re-invested in additional capacity.

¹ arrangement of the Dutch State that enables small fields producers to sell the produced gas at a set price to the incumbent Gasunie, the party controlling the market-dominating Groningen field

II.4 Transparency

IE has consistently emphasised the need for timely release of information on all aspects of infrastructure. We re-emphasise the need for real time information on gas flows. This information must be available to any interested party and, in order to hasten the liberalisation process, the excuse of commercial confidentiality must be set to one side at least as a temporary measure.

GGPSSO guidelines must be enforced immediately, specifically with regard to transparency provisions. Despite agreeing to these guidelines via the Madrid process in April 2005 most storage companies have yet to comply with the already minimal requirement for weekly reports of quantities injected, withdrawn, and in store.

II.5 Price Issues

IFIEC agrees with the conclusions.

IE believes that market based gas prices in the long run suit market development best. However, as long as the market(s) functions nationally and imperfect, the risks of a gas to gas market are disastrous for worldwide competing manufacturing industries, as can be seen in the UK.

It is imperative that in a single liberalised market, industrial consumers have freedom of choice and the ability to negotiate terms and conditions which are appropriate to seller's and buyer's needs. It would seem appropriate for sellers who operate in more than one EU country to be required to make available to customers in any country the same terms and conditions which they offer in any other country.

E. Way forward

IE does not believe that it is 'premature to take position at the current stage of assessment'. Clearly urgent actions are required. Additional firm and tight regulation including a 3rd Gas Directive is required. It is clear that voluntary agreements have not been successful.

A total unbundling of TSO's and all other activities of incumbents is required.

All exemptions from TPA provisions must be re-opened and be made subject to tough Use It or Lose It (UIOLI) or other allocation provisions.

DG Competition must instigate individual cases against incumbents and any other gas market players not operating in compliance with competition legislation.

Supply companies (including subsidiary companies of large corporations) operating in the EU must offer their customers in a particular member state the choice of the same terms and conditions as they offer in other countries.

It is necessary to check at the European level that infrastructures (pipes, storage, quality conversion terminals, and LNG facilities) are adequately designed according to the development of the gas demand, and to promote the required investment programs. As an absolute minimum, an annual forecasting survey should be conducted to assess the situation over the next 10 years, based on the lengthy deadlines associated with the implementation of new gas infrastructures. The regulatory body is a key element in this process and must be sufficiently powerful to prove effective.

The various regulatory methods of the different State Members should be harmonized where required.

We support the move to a single, liberalised European gas market.