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GLE position paper on LNG business

Context and scope of the work

In the last few years the gas market has drastically changed due to the new regulatory framework introduced by the Gas Directives on common rules for the internal market in natural gas (previously 1998/30/EC and, afterwards, 2003/55/EC). Some of the LNG issues addressed by the Second Gas Directive have been taken into account by GLE, in particular articles which explicitly address issues related to LNG activities¹ and all the other articles and definitions that are of general application for regulated activities and that shall be applied also to LNG facilities.

Currently the LNG business in Europe is growing extraordinarily due to the development of the LNG demand and of the LNG role as an alternative source of supply, which is developing in different historical context. In fact each European country has adopted different processes and has implemented specific operational practices tailored on the market needs of the single area.

LNG supply presents different impacts and contribution across Europe and the growth of LNG share within the European gas consumption shows the importance of new infrastructures and the crucial impact of the regulatory regime.

GLE has discussed and analysed the possibility to share common management procedures for the business rules of regasification terminals.

Aim of this position paper is to present the GLE position, taking into accounts terminal operators' needs on some of the principal issues concerning the LNG business in Europe, with the objective finalized to give indications on further development regarding the establishment of rules in a liberalized context.

¹ Articles 2 (commas 1, 9, 11, 12, 14), 19 and 22

LNG competition in the European regulatory context

- An analysis of the LNG business shows its upstream-driven nature: investments, operating expenditures and returns on capital show that highest costs are concentrated in the first steps of the LNG chain, while profits tend to decrease along the chain up to downstream. On the other hand, the regasification activity is the only step of the whole chain to be regulated. The upstream-driven nature of the business underlines the importance of common principles for the LNG business, with particular regard to the remuneration of the regasification segment, in order to avoid risks for national or regional bottlenecks which could negatively affect the development of the whole LNG chain. A solid rate of return should reflect the risks associated to the LNG business;

It is also a fact that regulation with respect to LNG regasification different throughout the EU. Looking at the Second Gas Directive different principles could lead to LNG regasification potential constraints, like different approaches on regulation between new and old terminals and short term contractual duration for the access to the terminals, which generates uncertainty on business fundamentals affecting project financing for the whole LNG chain.

Taking into consideration the previous points, regulation should point out:

- The constitution of a stable and predictable regulatory framework, according to the long term specificity of the LNG business: LNG terminals are capital-intensive projects based on long term nature. In the case of the terminals operating under TPA system, regulatory stability is required to allow the huge investments related to the LNG chain.
- A stable regulatory framework, with particular regard to the rules concerning terminals: an unstable regulatory framework would hinder the LNG market development. This means that LNG business should not be constrained in a binding and detailed European regulatory regime, irrespective of the status of competition and historical development in the downstream market place in which each terminal is involved;
- Long term commitments: either through a stable and predictable regulatory framework in the case of rTPA, or through long-term contracts in the case of partial or total exemptions, a long term commitment needs to be established for LNG terminals. This long-

term commitment should be coherent with the other steps of the LNG chain, taking into account the long term specificity of the business. The implementation of long term commitments would - on one hand - reduce the volatility and the enterprise risk for terminal operators and - on the other hand - give more contractual confidence for terminal users;

- Financial incentives: the regulatory framework should provide a regime of financial incentives based on a solid rate of return to support the LNG infrastructure development.
- The strict application of article 22 exemptions: In deciding to grant an exemption to LNG terminals connected to systems where LNG terminals under rTPA are operating, the regulatory framework should set up conditions which prevent an unfair competition between new exempted terminals and those which are operating under TPA regulation.

In addition to the regulatory issue GLE believes that the application of some basic rules to all regasification terminals are key points in order to increase the role and the contribution of the LNG in achieving a competitive gas market, particularly with regard to the:

- Level of transparency provided by terminal operators, including the publication of terms and conditions applied to the regasification terminal (non discriminatory access to capacity for third parties), available capacities, operational procedures (i.e. ship approval procedures) and tariffs concerning either the regulated services or the non regulated ones;
- Need of cooperation among all the stakeholders involved in the LNG business. This is a relevant and crucial issue to find efficient solutions in the LNG business management. GLE is well favorable to establish a constant and productive dialogue with all the LNG stakeholders (regulators, producers, terminal users, traders), in order to manage efficiently the LNG activity;
- Market efficiency, interoperability and integration with the transmission network, having the regulators a key-role, for the increasing of a fair competition in the whole gas business.

Business rules

With regard to LNG business rules GLE believes that it's important to identify and harmonise common criteria among terminal operators concerning procedural and operational rules relevant for the access to and the operation of each regasification terminal. Particularly:

- The definition of shared guidelines and procedures for the determination of the technical regasification capacity, taking into account the specificity of each regasification terminal;
- The determination of basic rules for the LNG ship access authorisation to regasification terminals, avoiding discrimination among accepted ships and maintaining safety in terms of ship/terminal operations and system integrity;
- The definition of possible business models (e.g. send out rules) taking into account specificities of each country, that would give efficiency both to the terminal operators and to the terminal users, maintaining interoperability with the transmission network.

Management rules

With regard to LNG management rules GLE believes that, in order to guarantee the correct and efficient use of the regasification terminal, the LNG business would benefit from a clear definition of the roles and responsibilities of the parties involved in the LNG process. Particularly:

- The minimum role of a terminal operator would involve safety, technical integrity, reliability and efficiency of the regasification terminal, refraining from discrimination among users and providing them with the information they need for efficient access to the system;
- The minimum role of a terminal user is the duty to sign the relevant terms and conditions to enter into contracts with terminal operator, delivering LNG and off-taking the regasified flows in accordance with contractual specifications, capacity booking, technical rules, scheduling procedures and balancing rules.

Services offered by European terminal operators

Concerning the analysis of services alternatively influenced by market demand or offered by terminal operators, GLE focused the discussion on which services should be offered by terminal operators under regulated tariffs, ensuring the respect of such conditions to the terminal users. At this proposal GLE considers that:

- there are some “ancillary services” necessary for regasification (unloading, operational storage and regasification) offered by terminal operators subject to TPA and published tariffs;
- there is a set of “specific services”, technical or trading, not necessarily subject to regulated tariffs. These specific services could / have to be treated in a liberalized market system in order to promote competition between different type of gas chain undertakings and to attract new investments and market liquidity.

LNG tariff

Concerning the analysis of tariff structure and taking into account the specificity of each country, GLE believes that:

- LNG terminals are capital-intensive projects with a perspective of long term period. The rate of return of LNG projects must reflect the level of risk attached to the investment and has to be taken into account by the Regulator where revenue setting for regasification terminals is among its duties;
- Capital expenditures in regasification terminals should have to be recovered through access charges paid by terminal users. In order to guarantee security of supply, LNG capital expenditures and operational costs should be remunerated.

LNG quality

Regasification terminals operate, within a range of values, irrespective of the gas quality parameters that depend on the final market of each area. GLE believes that - regarding the different gas qualities that can be discharged - gas quality adjustments could be made by the terminal operators, when possible, and have to be paid by the terminal users without creating barriers to access to the terminal itself.