

GIE Position Paper on:

"Quo Vadis EU gas market regulatory framework? – Study on Gas Market Design in Europe

The EU Commission has launched a study under the title "Quo Vadis EU gas market regulatory framework – Study on a Gas Market Design for Europe". The aim of the study is to provide a substantiated analysis as to whether the current regulatory framework in the EU gas sector is the most effective in order to maximize overall EU welfare.

GIE is fully supporting the notion that the gas market should contribute to maximizing the overall EU welfare and help achieve EU energy and climate targets. It is with that in mind that infrastructure operators have played an active role in developing the current gas market. This is a gas market that according to ACER has continued to progress and where market dynamics seem to work better and better, to the benefit of the users of the gas system.

GIE is committed to be an integrated part of this development and aims to ensure that the existing gas infrastructure continues to provide benefits to the European consumers in the transition towards a more sustainable energy system. GIE will continue its commitment to contribute to the dialogue on creating the most efficient gas market.

A DEVELOPING EUROPEAN GAS MARKET

Since the major reform of energy markets in the context of the 3rd energy package, gas markets in Europe consist of comprising entry-exit zones with trading hubs providing price signals for the market. Market liberalization, integration and diversification of supply have been achieved in most regions since 2009 by adequate levels of infrastructure. Gas infrastructure in Europe is utilised efficiently and in most regions it enables gas to be moved freely between market areas, to the locations where it is most highly valued by gas market participants. This helps building a liquid and competitive gas market while strengthening security of supply for EU consumers.

It should be taken into consideration that EU gas regulation and network codes are still under implementation in EU member states. This indicates that the full potential of what can be achieved within the existing gas market model is yet to be seen. Moreover, it is evident that there is currently no "one size fits all"-solution due to different stages of market development across Europe. Radical reforms would thus risk increasing complexity significantly for market participants and infrastructure operators without necessarily achieving any substantial welfare gains. Consequently, GIE does at this stage not see a need for a major reform of the EU gas market framework.

A SINGLE EUROPEAN MARKET ZONE?

Individual stakeholders are pushing for a significant change of the gas market for instance by creating a single EU gas market zone with entry/exit points and tariffs on EU external border points. This approach is currently not fully explored and may entail its own inherent challenges – especially when taking into account that the European gas market is on different stages of development. Moreover, it would be necessary to implement a form of inter-TSO compensation mechanism, which would raise complexity and challenge the business cases of existing infrastructure. Thus the consequences of disrupting existing contractual relations and potentially erase the confidence of investors would have to be considered.

Further, a single European market zone will require that different regulatory regimes in the member states are further aligned, e.g. in relation to cost regulation. That is a highly complex task, which would also create a need for increased interference by regulators and surrender of power to a not yet existing pan-European regulator that will struggle to handle the diversity of market developments in Europe.

GIE believes instead that the best way forward to better integration in EU energy markets will result from increasing hub to hub competition. Therefore, GIE proposes a thorough fine tuning of the current regulative framework focusing on removing barriers that disturb market functioning.

There can be situations where further diversification of gas supply sources and market integration may provide additional value. The current market rules already allow for this and new developments are currently taking place. Market mergers should be encouraged where it provides sufficient benefits. That is not possible to evaluate on EU-wide level. This requires a market based bottom-up approach in order to assure that the market areas are mature enough to merge and avoid creating supersized market areas that are technically impractically and for instance blurs market signals for new infrastructure.

GIE suggests that a regional approach to further market integration is considered instead of a single market zone concept respecting the different levels of market development. Such approach could help bringing fragmented national markets into regional hubs. Furthermore, cross-border market modelling could be used to analyse on a regional level potential of welfare gains from market mergers.

GIE acknowledges that merged markets have a potential to remove barriers to trade with commodity and infrastructure services. However, it should be considered that forced market mergers across the EU would significantly increase complexity for market players, operators of gas infrastructure and regulators alike. Without individual market specific analyses it will remain unclear to what extent market mergers will actually increase EU welfare.

A HORIZONTALLY INTEGRATED AND MORE SUSTAINABLE ENERGY SYSTEM

The current gas market design has – as it has been the case with the power market design - been developed in recent years in cooperation with the European Commission, ACER and ENTSOG through the network code process with the ambition of creating an internal market for gas.

However, the similar governance process should not overshadow the fact that the gas and electricity markets are significantly different in many ways: Most noticeable are the gas system's unique properties, which cannot be compared to electricity, - in particular the gas system allows cost efficient storage and transport of large volumes of energy across continents and seas.

Gas and electricity markets do already closely interact with each other. Given the accelerating uptake of electricity from renewable sources and the increasing need for backup electricity generation from gas, an ever closer cooperation between the two systems is expected in the future. There is thus value in increased horizontal integration across energy markets. While massive investments are planned and realized in electricity infrastructure, the EU natural gas system, which is already well connected in most parts of Europe, requires fewer investments and should thus be utilized to the benefit of the EU consumers.

Linking electricity and gas markets has practical implications for policy makers; network development decisions should be taken in a holistic manner and not focus on electricity only. System adequacy assessments should therefore take into consideration the conversion of renewable electricity, e.g. into hydrogen (power to gas), which would allow efficient storage and transport of

renewable electricity in a gaseous form. This role has to be recognized by regulators, who should focus more on overall system performance and exploiting synergies.

Moreover, GIE see potential for finding cost efficient emission reductions by building stronger links to other sectors, e.g. through promoting hybrid heating solutions and wider use of gas in maritime and heavy transportation.

NEW CHALLENGES FOR A SECURE ENERGY SUPPLY IN EUROPE

High security of supply for consumers is crucial in the transition towards a sustainable future, which will be characterized by highly volatile energy production. Consequently, as gas flows become more variable, and demand changes, gas infrastructure operators have to deal with a more intermittent utilization of some infrastructure assets. This challenges established market mechanisms of allocating and pricing capacity for storage and transmission. Therefore, the high value of flexibility and storage services for green and natural gasses needs to be reflected in a new regulatory framework. Moreover, the overall value of a secure gas supply must not be neglected and should thus be included in a more consistent way in market pricing and a fair cost sharing when it comes to under-utilized and stranded assets. Setting a methodology for valuing secure energy supply in the new gas market design could additionally serve as an important part of preparing a coordinated regional approach to secure gas supplies in stress situations.

REGULATORY FLEXIBILITY IN TIMES OF CHANGE

Europe is facing an accelerating transition of the energy system and the operators of gas infrastructure need to be an integrated part of the transition. In particular in the preparation of the regulatory preconditions, which are needed for infrastructure operators to be innovative and contribute to the transition by offering new services and bringing new technologies to market.

Examples where flexibility should be allowed for regulated infrastructure operators is cooperation with players on Power-to-Gas, bio-methane and gas for mobility. The already existing gas infrastructure, being well interconnected in most parts of Europe, could under the right regulatory framework play a significant role in transport and storage of renewable energy.

A new market design should help provide a robust and flexible regulation that provides sufficient support that the sector needs in order to nurture these technologies and ensure that new and innovative business models are brought to the market. Operators of gas infrastructure need legal flexibility and financial muscles to take on this innovative role and develop new products that would help in the transition towards a more sustainable energy system.

CONTINUED INVOLVEMENT

GIE remains engaged in the discussion on how to maximize overall EU welfare through development of the gas system. It is important that changes in the gas market design are proportionate in relation to any identified shortcomings. It is worth keeping in mind that the current market model is still under implementation and any major changes in market development should be subject to a thorough impact assessment in order to ensure that all stakeholders continually have the right incentives to develop the European gas market.