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Position Paper

on the amendment to the Regulation on the Security of Natural Gas Supply (SoS Regulation)

Follow-up positions and implementation proposals of BDEW

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1 Introduction

On 16 October 2014, the European Commission presented an evaluation report on the Regulation on the Security of Natural Gas Supply (Natural Gas SoS Regulation) in the scope of the publication of the stress test results (gas supply situation in winter 2014/15). In that report, the implementation of the regulation was assessed and approaches for a reform were identified.

In preparation for reviewing the Natural Gas SoS Regulation, on 15 January 2015, the EU Commission opened a consultation on the amendment of the Regulation in which BDEW had participated with a position statement on 1 April 2015. The results of the consultation on the amendment to the Natural Gas SoS Regulation were published by the EU Commission on 10 June 2015.

In this position paper, BDEW would like to take the opportunity to adopt a specific position on individual topics of the consultation results and submit further implementation proposals. This is based on the BDEW positions compiled in the position statement of 1 April 2015 with the aim of guaranteeing a secure natural gas supply on a European level:

BDEW believes there can be no doubt that - as has been the case until now - the secure supply of natural gas can best be provided through an open, liquid, well-connected and transparent European natural gas market with different sources of supply, including storage facilities, intelligent solutions on the demand side and with a secure investment climate. The rules of the Third Internal Energy Market Package should therefore be completely implemented in all EU member states.

From the point of view of BDEW, the following basic tenets are of key importance in the further structuring and strengthening of an internal European market for natural gas and thus the lasting guaranty of a secure gas supply:

- The current Natural Gas SoS Regulation already provides a broad range of instruments for achieving the specified infrastructure and supply standards. **When selecting the measures, the proven three-stage decision making approach (1st stage: natural gas companies, 2nd stage: member states, 3rd stage: European Union) should be preserved.** As far as the definition of protected consumers and of the supply standard is concerned, however, each member state should demonstrate transparently that the requirements of the Natural Gas SoS Regulation are met or complied with.

- To further strengthen the internal market, measures to provide security and emergency relief within the scope of the Natural Gas SoS Regulation should be designed to ensure they **preserve market mechanisms as long as possible** in the event of a disruption to supply. The introduction of additional emergency mechanisms at a European level should be avoided unless there is a demonstrable necessity and unless an assessment has been made as to the positive effects on security of supply.

- **In the opinion of BDEW, an EU member state should only qualify for solidarity assistance once it has adequately fulfilled the supply standard**. When developing the solidarity mechanisms between the EU member states, compliance with the existing provisions of the Natural Gas SoS Regulation for the specification of the group of protected consumers by the EU member states is an important step, so that in the event of a Union-wide or regional shortage, the requirements of solidarity placed on EU member states do not lead to the unequal treatment of identical consumer groups. The provisions within the Natural Gas SoS Regulation already form a suitable basis for ensuring that the definition of protected final consumers of gas is as uniform and harmonised as possible on a European level. The provisions should therefore be maintained in their current form.

- **Improved European coordination in respect of the implementation of the provisions of the Natural Gas SoS Regulation (risk assessment, emergency and preventive action plans) is to be welcomed.** The European Commission and the Gas Coordination Group (GCG) should therefore be provided with more precise information as to how each member state ensures that, for example, cross-border load flows within the internal market are not or not unduly restricted.

Alongside these existing positions, the intention of this position paper is to go into greater detail on individual possibilities for change in the Natural Gas SoS Regulation and highlight specific implementation proposals. The possibilities presented are intended to serve as a basis for further discussions.

2 Additional BDEW positions and implementation proposals

2.1 Infrastructure standard: reverse flow capacities and improved calculation method

The infrastructure standard describes the obligation of EU member states to ensure that any infrastructure that remains after disruption of the single largest infrastructure has sufficient capacities to satisfy a level of daily peak load which has a statistical probability of occurring once every twenty years.

Analyses of the EU internal market reveal that the EU member states or regions which would be especially affected by, for example, a disruption to the Ukrainian transit route are those which do not yet sufficiently meet the infrastructure standard due to a high dependency on one import route. Even just the consistent implementation of the existing requirements of the Natural Gas SoS Regulation on the level of the EU member states would enable the EU internal market to be significantly strengthened. In order to strengthen the internal market, the EU member states should therefore ensure they fully implement the requirements regarding

the infrastructure standard. Therefore, an expansion of the gas infrastructure is to be encouraged as part of the necessary action to be taken.

2.1.1 Reverse flow can help countries meet the infrastructure standard

Setting up physical reverse flow capacities at selected border interconnection points is thus in principle suitable for strengthening the infrastructure standard. The EU member states should therefore create the possibility for physical reverse flows in particular wherever this serves to achieve the infrastructure standard. The existing rules on cost allocation have proven to be effective and should therefore be maintained.

Germany already completely fulfils the infrastructure standard (n-1) in accordance with the provisions of the Natural Gas SoS Regulation without having set up additional reverse flow capacities. While projects for establishing reverse flow capacities were indeed identified in the German network development plan and in the European "Projects of Common Interest", the necessity of these projects is viewed in particular with respect to the distribution of natural gas sources that will change in the future. These projects systematically help to increase the security of supply by diversifying the sources of supply.

In addition to the security of supply, the establishment of reverse flow capacities at border crossings is another means of connecting liquid natural gas trading centres (hubs). The linking of liquid markets raises efficiency and the competitive intensity among the connected regions. However, in this respect, clear market indicators are necessary that justify an increase in capacity. Cost-benefit analyses and market tests are necessary to provide the relevant economic indicators and underpin investment decisions in order to substantiate decisions on the establishment of reverse flow capacities.

A de facto upgrading of the infrastructure to establish reverse flow capacities at border interconnection points should not be formalised across the board in the Natural Gas SoS Regulation. Investments should only be made when indicators substantiate that newly established reverse flow capacities will increase the security of supply by diversifying the sources of supply of a country or that they increase efficiency and competitive intensity in the markets and thus yield corresponding economic advantages. **However, the regulatory provision for implementing reverse flow capacities at any and all border interconnection points would lead to increased costs by investments in new capacities which would not be covered by an equivalent benefit.** This position goes along with BDEW's opinion that additional measures and provisions within the Natural Gas SoS Regulation should only be undertaken when their positive effect on the security of supply can be proven.

The target group for the identification of the need for reverse flow capacities based on their actual contribution to the security of supply and their effect on the market should be the European and national network development plans. Consideration in terms of regional network development plans also appears expedient in order to be able to determine specifically the cross-border benefits of establishing reverse flow capacities.

2.1.2 Calculation method often does not reflect reality

The purpose of the infrastructure standard is to ensure that the demand in the respective area can still be sufficiently covered even after a disruption to the largest import infrastructure. As part of the calculation method for the infrastructure standard, here, the gas demand (D_{max}) is interpreted as meaning "total domestic gas consumption". As such, the formula totally ignores all export flows. Within the internal market, however, situations of capacity dependency exist between certain nation states which are consequently not taken into account by the infrastructure standard. For example, Sweden is reliant on the use of import capacity from Denmark. A secure supply of natural gas in Switzerland is absolutely dependent on the use of German export capacity at the border interconnection point at Wallbach. In the opinion of BDEW, therefore, the availability of such capacity and situations involving cross-border dependency within the EU internal market should be taken into account in the requirements governing the infrastructure standard.

The current position is that the existing calculation formula for the infrastructure standard suggests that the total input (entries, production and storage facilities) is available to cover the demand in each of the calculated regions. However, in actual fact, the entries also include volumes which really belong to the exports – in particular in Germany, which is a major transit country. Furthermore, dependency exists between entry and exit volumes in the form of contractual allocations which affect the profitability of import points. However, the existing calculation method only includes the total capacities and is therefore an inadequate reflection of reality.

BDEW therefore suggests, as part of the amendment to the Natural Gas SoS Regulation, changing the calculation method to ensure that the natural gas infrastructure is not only designed to sufficiently satisfy the internal market, but also, in the case of transit countries, to maintain regular transit volumes in shortage situations, even in the event of a disruption to the largest import infrastructure. The calculation method of the infrastructure standard should therefore be extended to include a suitable factor in the formula. BDEW recommends extending the denominator as required and adjusting the Natural Gas SoS Regulation to that effect in order to make the calculation method as realistic as possible.

Should this adjustment fail to meet with approval, BDEW alternatively suggests as a minimum taking the export flows into consideration in the formula's numerator. This would at least avoid the total exclusion of the export flows in future, with minimal need for adjustment.

In general, it must be taken into consideration that in the first instance, each member state itself is responsible for establishing the infrastructure-related options for a sufficient supply to meet the domestic demand and the transit flows. There must also be an equal level of security that the cross-border use of this infrastructure is not unduly restricted (cf. implementation proposal for the installation of a cross-border transmission system operator (TSO) emergency communication system). A member state positioned upstream in a transport corridor must therefore take into consideration that even in the event of a shortage, it will at least be possible to maintain normal volumes of gas outflow. The fact that, furthermore, an economically balanced optimal distribution of gas volumes via short-term transactions in the liquid market also takes place across borders, remains unaffected. In order to be able to maintain this ex-

change in the event of shortages, the infrastructure standard should be greater than 100 % based on the n-1 criterion.

BDEW suggests that, to improve the calculation method and make the result more realistic, export volumes also be taken into consideration in addition to the consumption in the denominator of the calculation formula:

$$N-1[\%] = \frac{EP_m + P_m + S_m + LNG_m - I_m}{D_{max} + \boldsymbol{EXP}_{\emptyset(2a)}}$$

As a minimum standard, BDEW alternatively suggests at least taking the export flows into consideration in the calculation method's numerator:

$$N-1[\%] = \frac{EP_m + P_m + S_m + LNG_m - I_m - \boldsymbol{EXP}_{\emptyset(2a)}}{D_{max}}$$

BDEW believes the two-year average of the export flows should be used for this purpose. This would both rule out distortions caused by any situational examination of the export flows at individual moments (e.g. peak export flows, the maximum domestic demand or maximum sum of both components), and include capacitive dependence between entry and exit volumes. This would adequately reflect the regularly occurring, average gas outflow from a member state within the infrastructure standard. In the event that, for example, changes made to the export infrastructure during the observation period of two years resulted in significant and justifiable changes, the effect should be reviewed, evaluated and included as required in a case-by-case analysis.

2.2 Adjustment of cross-border gas flows

In Germany, based on the respective provisions of Article 16, paragraph 2 of the Energy Industry Act (EnWG), TSOs are, under certain circumstances, entitled and also obligated without contractual basis to adjust all gas infeeds, gas transport and gas outfeeds in their respective networks to the requirements of a secure and reliable operation of the network, or to demand this adjustment. This includes, amongst other things, limiting or fully interrupting load flows at border interconnection points. At a national level, export flows do not form a part of the group of protected customers. Consequently, there comes a point where the network operators have to restrict or interrupt those flows over protected customers or defined system-relevant gas-fired power stations.

However, in such cases, it is unknown how the exchange of information between the TSOs required for such measures is undertaken by the nation states in question and how the liabil-

ity situation is to be assessed when adjustments are made to cross-border load flows. Such measures not only regularly have an effect within the scope of the Energy Industry Act, but also within the member states whose load flows are being restricted.

The Natural Gas SoS Regulation includes criteria on which to base answers to the questions raised. According to this, the member states, in particular the competent authorities, must ensure in all events by implementing the emergency plan in Article 10, paragraph 7 of the Natural Gas SoS Regulation that

- no measures are introduced which unduly restrict the flow of gas within the internal market at any time;
- no measures are introduced that are likely to seriously endanger the gas supply situation in another member state; and
- cross-border access to infrastructure in accordance with Regulation (EC) No. 715/2009 is maintained as far as technically and safely possible, in accordance with the Emergency Plan.

However, in this respect it is unclear when load flows are being “unduly” restricted within the internal market, when the gas supply in another member state is seriously endangered and from when the cross-border access to infrastructures in harmony with Regulation (EC) No. 715/2009 according to the emergency plan can no longer be maintained. So far, a clear approach to handling export flows can thus not be deduced from the aforementioned specifications of the Natural Gas SoS Regulation.

The Natural Gas SoS Regulation does prescribe a general principle of solidarity in respect of protected customers, however how this should be implemented on an operational level is not described. There is no transparency as to how the interruption or restriction measures affect the natural gas supply of the neighbouring EU member state and whether, for example, an interruption will already lead to a supply shortage for protected customers in the neighbouring country.

As far as BDEW is concerned, the basis of any solidarity measures and for the equal treatment of member states in the application of such measures in an emergency, is strict compliance with the existing provisions of the Natural Gas SoS Regulation with the nation states specifying the group of protected customers and transparent compliance with the supply standard of the Natural Gas SoS Regulation. Therefore, an extensive examination is required as to whether the existing national regulations are in line with the European framework definition. BDEW believes that an examination of the national regulations and, where necessary, a modification thereof would lead, as far as possible, to a uniform or harmonised definition of protected customers in the member states.

As part of any greater harmonisation, effort should also be made to include further substantiation of the provisions in Article 9 with regard to the capacities to be taken into consideration in

the calculation method for the supply standard, in order to further unify the capacities on which the national prevention and emergency action plans are based. Based on the standardisation of the national definitions of the group of protected customers, it must be possible to operationally adjust cross-border load flows in emergencies and thus overcome and compensate for emergency situations by means of solidarity among the union of states.

2.2.1 Exchange of information in a cross-border communication process

There is currently no rule requiring gas supply companies, in particular TSOs, to exchange information across national boundaries in advance of any action to determine which measures would unduly restrict the internal market. In a crisis situation, TSOs only have at their disposal information from voluntary bilateral agreements concluded between themselves.

BDEW therefore proposes implementing a binding, cross-border communication process between TSOs and, where necessary, competent authorities for the exchange of information.

To this end, each TSO should install an emergency communication system with its neighbouring TSO with the aim of exchanging data to prevent any undue restriction and serious threat to the supply according to Article 10, paragraph 7 of the Natural Gas SoS Regulation. The application of non-market-based measures within the domestic territory or at border interconnection points must comply with the principle of proportionality in this regard.

For this purpose, it is necessary to agree upon the data required for communication in a crisis situation in advance, and specify clearly defined areas of responsibility for the communication process. In a crisis situation, the TSOs will communicate the capacity required to supply the protected customers to the border interconnection point in question. Irrespective of the crisis situation, the TSOs will regularly communicate a substitute value for the required capacity that will be used if in the event of a crisis situation, the capacity value is not updated by the neighbouring TSO.

2.2.2 Exemption from liability of the participating TSOs

The adjustment of border interconnection point load flows is, in addition to other non-market-based measures, an important instrument for the compensation of existing local shortage situations. The Natural Gas SoS Regulation lists these adjustments as important measures for eliminating shortages. It is therefore of great importance that TSOs are able to apply these measures in a legally watertight framework so that local shortage situations can be compensated for as quickly as possible and more far reaching effects can be avoided.

In the event of local shortages in which neither a national nor an international emergency has been declared and the thus (according to German law) associated liability regulations apply, there currently exists an uncertainty with regard to liability law in terms of the application of load flow adjustments at border interconnection points. It is unclear how liability is allocated in

the case of cross-border damages resulting from non-market-based measures being applied at border interconnection points, in particular where such measures are employed for the purpose of securing the supply of protected customers in the neighbouring country. No mechanism exists either, to provide an objective allocation of the costs thereby incurred.

In order to standardise the governance of these cross-border matters, the member states should therefore be required to exempt the TSOs from liability with respect to the reasonable restrictions of load flows in the sense of Article 10, paragraph 7 of the Natural Gas SoS Regulation. Such a regulation should be incorporated in the amended Natural Gas SoS Regulation.

The national regulation of Article 16, paragraph 3 of the Energy Industry Act (EnWG) could serve as a benchmark with regard to an exemption from liability. According to this, in the event of an adjustment according to Article 16, paragraph 2 EnWG, all of the respective obligations to perform affected by this are suspended up to and including the resolution of the emergency situation or disturbance. Liability for financial losses is excluded, insofar as the preconditions according to Article 16, paragraph 2 EnWG exist. German legislators justify this with the particular complexity of the situation and the time pressure when selecting the measure to be undertaken. Without any exclusion of liability it would not be possible to rule out that, in view of inestimable liability risks for the network operator, there would be an incentive not to act in emergency situations.

If, due to an increased liability risk, non-market-based measures according to Article 16, paragraph 2 EnWG are not seized upon, the risk may also increase that a regional shortage situation develops out of what is, in the first instance, a local shortage situation and this potentially develops further still into a national or international emergency. However, it is worth avoiding this – i.e. as soon as local shortages occur. For this purpose, in addition to the national legislators, it is also necessary for the European legislator to create legal security through a comprehensive exclusion of liability – irrespective of how the relevant national legal regulations are structured. What is important, is that by undertaking any cross-border measures, no liability risk arises for the network operators.

BDEW believes that TSOs should be entirely exempt from liability when adjustments are made to cross-border load flows insofar as the legal preconditions for the specific adjustment exist. In accordance with Article 16, paragraph 2 EnWG in conjunction with Article 10, paragraph 7 lit a of the Natural Gas SoS Regulation, TSOs are entitled to make adjustments to cross-border load flows insofar as these are not unreasonable. In Article 16, paragraph 3, the German EnWG law includes within its scope an exemption from liability for such an adjustment by the TSOs. On the other hand, adjustments of load flows not only regularly have an effect within the scope of the German Energy Industry Act (EnWG), but also in the member states whose load flows are being restricted. In contrast to the German EnWG, the Natural Gas SoS Regulation currently fails to provide sufficiently concrete regulation with respect to the liability law issues resulting from such adjustments to load flows. **However, in addition to other non-market-based measures, load flow adjustments at border interconnection points represent an important instrument for eliminating a local shortage**

and for preventing far reaching effects, which is why TSOs should be able to undertake the measures within a legally watertight framework.

In order to standardise the governance of such cross-border matters, the member states should be required to exempt the TSOs from liability with respect to any reasonable restrictions of load flows. Article 16, paragraph 3 EnWG could serve as a benchmark for an appropriate provision.

2.3 Coordination of measures in shortage situations

2.3.1 Consolidation of the early warning system

From a German point of view, several provisions conflict with one another in the event of shortage situations. The national Gas Emergency Plan designates a national crisis team, while the Natural Gas SoS Regulation implements a Gas Coordination Group (GCG). Furthermore, in Germany, local crisis teams are also designated.

In this respect, it is unclear how the crisis teams or GCG will be able to fulfil their respective consulting and coordination functions in reality during shortage situations. It is also necessary to examine whether an exclusively consulting or coordinating function of the local and national crisis teams is constructive. Up until now, the crisis teams, for example the national crisis team, request the support of other market participants or associations only as and when required.

In the opinion of BDEW, the procedural cooperation should be specified with regard to the scope of the crisis teams and the GCG and their make-up and composition, such that the consulting function can be utilised in shortage situations and provide an adequate contribution to crisis management.

The early warning system can, by implementing a European communication platform, enable the timely identification of restrictions or threats to the security of supply for Germany and the EU. Participating TSOs use this platform within the early warning team to exchange important information on the status of the TSOs and to coordinate suitable measures in the event of a crisis situation. The expert teams can also support other coordination centres, e.g. the GCG, when assessing the supply situation in Europe in order to improve the transnational crisis management.

The *East* early warning team that has already been established as an association mainly of TSOs that transport gas originating from Russia, offers opportunities for the timely identification and localisation of potential restrictions or threats to the security of supply from the respective area and allows relevant decision-making bodies to be informed in good time and react in a timely manner. The early warning system thus already makes a considerable contribution to the security of supply and crisis prevention.

BDEW welcomes the activities of the East early warning team as part of the early warning system and supports an expansion to include the North-West team as a further part

of this system. BDEW believes that the early warning system should be developed further and integrated in the international crisis mechanism.

2.3.2 Preservation of voluntary swap procedures

In shortage situations, critical network situations can make it necessary to transfer cross-border load flows with one or more adjacent TSOs in order to manage the specific situation. These transfers are performed where practical and feasible in accordance with internationally agreed-upon processes, and within the German legal framework they represent a network-related measure in accordance with Article 16, paragraph 1 EnWG.

A number of European network operators function according to these processes ("swap procedures between European TSOs"), which are currently practised successfully without contractual agreements; in addition to such transfers in shortage situations, the process is also agreed upon in other situations, e.g. to minimise the effects during maintenance work or for the mutual optimisation of network operations.

There are currently no regulations in place regarding a contractual agreement among the supporting TSOs. **Nevertheless, previous experience shows that this reciprocal, voluntary support functions well in shortage situations and can make a valuable contribution to shortage management.**

However, the willingness of the participants to volunteer is a core element of the TSO convention. Any possibly statutory stimulation or formalisation of the measures would severely restrict this aspect and thus impair the optimisation potential provided by the participants. In addition to the obligatory character, any necessary formalisation of the billing mechanisms would have a negative effect on the willingness to participate and thus reduce the provision of optimisation potential.

BDEW believes that the freedom to volunteer to participate in swap procedures should remain; however, in future, swap procedures should only be undertaken simultaneously and with a neutral balance, as they are today.

The foundation for the agreement on swap procedures is the voluntary offer of participating TSOs to flexibly adjust their transport volumes. The voluntary nature and the option of arbitrary cancellation of an offer if sufficiently notified provide incentives to participate for an increasing number of TSOs and so far this has led to consistently positive results and experiences for the participants.

In their current form, swap procedures also represent an effective means of avoiding shortages in an international context. On a European level in particular, swap procedures should therefore be anchored within the scope of the Natural Gas SoS Regulation as a voluntary, network-based measure.

In order to continue to ensure the balance neutrality of swap procedures, it should, also in the future, only be possible to undertake appropriate transfers of transport volumes if they are

carried out simultaneously; the expansion of swap procedures at staggered times (within a delivery day) is not envisaged.

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