



Draft Guidelines on Article 22 An EREG Public Consultation Paper

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Table of Contents

| | | |
|----------|---|----------|
| 1 | INTRODUCTION | 5 |
| 2 | GENERAL PRINCIPLES ON ARTICLE 22 EXEMPTIONS | 5 |
| | 2.1 Competition in Supply / Security of Supply vs. rTPA..... | 5 |
| | 2.2 Eligible Types of Infrastructure..... | 6 |
| | 2.3 Role of market dominant players vs. “newcomers” | 7 |
| | 2.4 Defining Markets | 7 |
| | 2.5 Investment Climate and Risks Attached..... | 7 |
| | 2.6 Minimum TPA Requirements and Effective Anti-Hoarding Mechanisms | 7 |
| | 2.7 Consistency of Decisions | 8 |
| | 2.8 Procedural Approach..... | 8 |
| | 2.9 Role of open season procedures and capacity allocation | 8 |
| | 2.10 Reviewing the exemption | 9 |
| | 2.11 Institutionalised and co-ordinated proceedings | 9 |
| 3 | ARTICLE 22 GUIDELINES | 9 |
| | 3.1 Eligible infrastructure..... | 9 |
| | 3.2 Requirements..... | 10 |
| | 3.2.1 Enhancement of competition in gas supply | 10 |
| | 3.2.1.1 Market definition | 11 |
| | 3.2.1.2 Assessment of market structure | 11 |
| | 3.2.1.3 Enhancement of competition in the relevant market | 12 |
| | 3.2.1.4 Ownership-/company structure | 13 |
| | 3.2.2 Enhancement of security of supply | 13 |
| | 3.2.3 Risk assessment | 13 |
| | 3.2.4 Unbundling requirements | 14 |
| | 3.2.5 Charges requirement..... | 14 |
| | 3.2.6 Internal market | 15 |
| | 3.3 Decision..... | 15 |
| | 3.3.1 Scope of exemption..... | 15 |
| | 3.3.1.1 Partial exemption..... | 16 |
| | 3.3.1.2 Full exemptions | 18 |
| | 3.3.1.3 Conditions | 18 |
| | 3.3.2 Co-ordination and Co-operation | 20 |
| | 3.3.3 Market participation and consultation..... | 20 |

| | | |
|----------|---|-----------|
| 3.3.4 | Early notification of the Commission | 20 |
| 4 | RESPONDING TO THE PUBLIC CONSULTATION..... | 21 |
| 4.1 | Questions for stakeholders..... | 21 |
| | Annex: Other Art. 22 provisions not relevant with respect to these guidelines | 23 |

PREAMBLE

Having regard to Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and especially Article 22 thereof, aiming at the promotion of effective competition and security of supply by incentivising efficient investments in new infrastructure projects, while at the same time recognising the need for non-discriminatory access to relevant infrastructures, ERGEG agrees upon the following guidelines which constitute a harmonized and transparent framework for competent authorities when deciding on exemption procedures.

1 INTRODUCTION

This consultation aims at producing draft guidelines on Art. 22 of directive EC/2003/55, subsequently to be embedded in an overall ERGEG paper. It is based on the findings of ERGEG's draft report on Art. 22 exemptions¹ as foreseen in ERGEG's 2007 work programme. The practice of granting exemptions has been documented in the said report. This consultation is also a reaction to the European Commission's invitation to ERGEG for submitting early comments on the New Gas Infrastructure Investment Regulation (NGIIR). This consultation will not deal with institutional questions within the Energy Community or with the legal framework on third party access to infrastructure outside the European Union. Finally, this consultation will not address procedural questions concerning the legislative implementation of some or all its contents under the Energy Community Treaty.

2 GENERAL PRINCIPLES ON ARTICLE 22 EXEMPTIONS

Guidelines on Art. 22 should be designed within the legal framework set by existing Art. 22. Should changes in Art. 22 become necessary at a later stage, ERGEG will draft respective proposals or comments in a separate paper. It is appropriate to establish general principles which can form the basis of more detailed guidelines. These principles need to take into account the rationale of the exemption regime as well as its advantages and drawbacks, especially with respect to establishing a single European market for natural gas. Finally, such principles must remain within the scope of existing Art. 22.

The present guidelines should be used by deciding authorities to guide their decisions when considering Art. 22 applications as a way of filling a gap before any binding guidelines are developed. As shown in the analysis report on the European Regulators Experience with Art. 22 exemptions of Directive 2003/55/EC [E07-TF-01-01], a significant amount of infrastructure projects have either received exemptions or are in the process of requesting exemptions. This shows the need for a harmonized or at least a consistent and improved approach for implementing Art. 22. This is the aim of the present guidelines

2.1 Competition in Supply / Security of Supply vs. rTPA

It is crucial that there is an appropriate framework for facilitating and incentivising efficient investment both for the development of competition and for helping to ensure security of supply. The "default regime" for investment is for a regime where access is open to third parties – and the majority of investment in infrastructure in the EU falls under this category. However, there are circumstances where investment may not be undertaken if subject to all of the requirements associated with a regulated TPA regime – with a possible negative impact on competition and security of supply. It is because of this that the existing legal framework in the EU allows for the possibility of investment that is not subject to all of the requirements of the rTPA regime. Art. 22 of the Gas Directive allows for the possibility for investment to be brought forward under a framework where some or all of the requirements of rTPA do not need to be applied.

¹ Treatment of New Infrastructure, Part 1 (GII-3/b): European Regulators Experience with Art. 22 exemptions of Directive 2003/55/EC, Interim results.

However, competent authorities should use Art. 22 restrictively² – as it represents a deviation from rTPA - and thoroughly assess the benefits of any new infrastructure (i.e. for competition and security of supply) against the “costs” of exempting it from an open TPA regime. Such an assessment will determine whether an exemption should be granted to a new infrastructure project, and if so, what form it should take and whether any mitigating steps (i.e. conditions) should be put in place to ensure that the impact on competition and security of supply from granting the exemption is beneficial. As such there can be “different types” of exemptions. Exemptions can be given for an entire facility or for a part of a facility; they can also be given for tariff regulation only, or for regulated TPA as a whole. A wide ranging exemption will facilitate the investment but will hamper TPA. Conversely, a limited exemption will preserve TPA but may not be sufficient in order to facilitate the investment. A correct balance must therefore be found, based, once again, on a thorough analysis of the costs and benefits of the particular project on a case-by-case basis.

Art. 22 includes 5 tests to help competent authorities conduct this analysis. The goal of the present guidelines is to provide additional guidance to competent authorities – both on how these tests should be carried out and on the form and nature of exemptions that should be granted. If competent authorities throughout the EU adhere to the present guidelines and conduct their analysis in an equally thorough way, this should help establish a level playing field for investors and infrastructure users across the Union – by increasing the level of consistency in the decisions taken in respect of an exemption. The guidelines will also help to ensure that where an exemption is granted, it is appropriate to the particular project.

2.2 Eligible Types of Infrastructure

The scope of existing Art. 22 limits the exemption regime to **interconnectors** and **LNG** and **storage** facilities. This scope needs some clarification in that it should encompass (in line with the general framework and the definitions of the directive) **new technologies** which serve the same purpose as the ones listed in Art. 22³.

Art. 22 does not allow exemptions for transmission facilities other than interconnectors. ERGEG considers that this is appropriate as investment in the transmission system should be through the default regime with full TPA access.

In the application of Art. 22, one could consider different treatment for duplicable and non-duplicable infrastructure, in that the latter would require stricter treatment. Where infrastructure can reasonably be duplicated by third parties, preconditions for exemptions could be less strict (the need to keep infrastructure as open to TPA as possible would still need to be seriously taken into account). In determining the classification as non-duplicable infrastructure, the following conditions could be applied

- environmental reasons, where it is not feasible (or extremely difficult) to obtain additional authorisations (e.g. building permits);

² E.g. Case C-495/04, *A.C.Smits-Koolhoven*, [2006] ECR I-3129, para 31.

³ I.e. new LNG technologies.

- scarcity of resources, in particular where the geological, geographical or local constraints do not allow development of additional underground storage or LNG facilities to cover the needs of the market;
- costs (e.g. economies of scale when building such an infrastructure).

2.3 Role of market dominant players vs. “newcomers”

Art. 22 para. 1a), which requires that the new infrastructure enhance competition and Article 22 para. 1e), which requires that the exemption is not detrimental to competition, make it very difficult for dominant market players (in most cases so-called incumbents) or their affiliates to receive TPA exemptions and in particular wide ranging TPA exemptions as there is a significant risk that the granting of an exemption in such circumstances would have a negative impact on competition by fortifying an already dominant position in the relevant markets unless there are substantial compensating benefits. On the other hand, it is important to let newcomers meeting the 5 tests benefit from Art. 22. Where the only effective means of market entry is by establishing new infrastructure, e.g. due to lack of available capacity on existing infrastructure, the granting of an exemption may be justified.

2.4 Defining Markets

One crucial criterion in Art. 22 is the definition of the relevant market(s). The effects of new infrastructure on competition in supply, security of supply, competition of the internal gas market, as well as incumbency, depend centrally on the defined market. For example, a company can have a dominant position in a national market while being a newcomer to a wider regional or European market. Similarly, a new infrastructure may fortify a company's position in a national market, but enhance competition in another national or the wider regional or European market. The market definition should take into account the results of the consultation procedure under 3.3.2.

2.5 Investment Climate and Risks Attached

The risk addressed under Art. 22 para. 1 b) can generally only be assumed to be relevant for an exemption where the project sponsor or other possible investors would not be able to invest in the necessary new infrastructure under a regulated TPA regime. To determine whether this is the case, a market consultation or other means of assessment should be conducted with respect to the specific infrastructure investment.

The deciding authority should verify the risk assessment provided by the applicant using appropriate methods.

2.6 Minimum TPA Requirements and Effective Anti-Hoarding Mechanisms

Where only a partial TPA exemption is granted (i.e. to a proportion of the capacity) a non-exempted part of the infrastructure will be reserved for TPA. Anti-hoarding mechanisms shall apply to both the non-exempted and the exempted part. Regimes like use-it-or-lose it seem most appropriate to help ensure efficient utilisation of capacity in returning actually unused capacity to the market.

2.7 Consistency of Decisions

In order to ensure consistency of decisions throughout the EU, all deciding authorities will need to assess the benefits and costs of any exemption in an equally thorough way, using the present guidelines as a basis. Indeed it is necessary to avoid forum shopping from promoters in the sense of choosing the country with the lightest regulation. Although it is crucial that the form/nature/conditions of any exemption are proportionate to the individual project/market – which will be determined by the underlying competition assessment.

2.8 Procedural Approach

Deviations from the requirements of rTPA should only be as wide as is necessary to facilitate the investment that would otherwise not be brought forward. This results from the principle of proportionality⁴.

2.9 Role of open season procedures and capacity allocation

Open season (or comparable) procedures are an important tool in assessing the market need with respect to determining the size of the project as well as in the subsequent capacity allocation. Open seasons also might in some cases have a cost in a broader sense for the sponsor as well as bidders which might undermine the feasibility of some projects. Where the NRA, in the case of interconnectors after consulting other affected NRAs, is satisfied that the project sponsor has sufficiently proved that an open season would undermine the feasibility of the project the NRA may not require the project sponsor to conduct an open season. This may in particular be the case where a small market operator is not in a position to open up its facility to third parties, and the resulting benefits in terms of competition might make this disadvantage to the market still acceptable in the overall context. The open season procedure shall follow ERGEG's GGPOS with any necessary variations. It must be ensured, that the result of the open season is not such that the incumbent receives a capacity share perpetuating or enhancing its dominant position. The results (or potential outcomes, where final results are not available) of the Open Season Procedure should be submitted together with the application to grant an exemption. The final decision to grant an exemption has to take into account the results of the Open Season Procedure and generally the way primary capacity is allocated given the circumstances of each project.

⁴ See ECJ, C- 261/81, fn. 17 (Rau/ De Smedt); ECJ, C- 147/81, fn.12 (Mercur Fleisch- Import/ Hauptzollamt Hamburg- Ericus). Another source for this finding is the **principle of rule and exception, according to which an exception to a general rule must be interpreted restrictively**, as confirmed in ECJ, C- 303/98 F, 34, 35 (Simap); C- 241/99 fn. 29 (CIG); C- 403/01 fn. 52 (Pfeiffer *et.al.*) and ECJ, C- 495/04, fn. 31 (Smits- Koolenhoven).

2.10 Reviewing the exemption

Compliance with the criteria and/or specific conditions imposed for granting an exemption should be monitored by the NRA. If these criteria are not satisfied anymore or if the conditions imposed are infringed upon, the NRA should be able to review the exemption. In order not to discourage investment, there should be clear and stable rules laying out the circumstances under which the exemption could be reviewed.

2.11 Institutionalised and co-ordinated proceedings

Where interconnectors affect the system in more than one country, it is necessary to ask NRAs to co-ordinate their respective proceedings (cf. Art. 22 para. 4 d). Under the current legislative and institutional EC framework, a one-stop-shop solution, which may be desirable for the market, seems not feasible in the EU. Decision-making power is rested with national authorities, who are subject to national court jurisdictions.

3 ARTICLE 22 GUIDELINES

The following guidelines are based on the existing structure and substance of Art. 22. They are the result of the draft NGIIR and the work of ERGEG workstream “treatment of new infrastructure” as well as discussions within ERGEG’s ad hoc taskforce “NGIIR” and ERGEG’s Gas Focus Group. For the sake of clarity, the original wording of Art. 22 is quoted in a box before the actual guideline text.

3.1 Eligible infrastructure

Art. 22 para. 1: Major new gas infrastructures, i.e. interconnectors between Member States, LNG and storage facilities [...]

Art. 22 para. 2: Paragraph 1 shall apply also to significant increases of capacity in existing infrastructures and to modifications of such infrastructures which enable the development of new sources of gas supply. [...]

Eligible infrastructure shall comprise interconnectors between Member States, LNG and storage facilities as well as infrastructure on the basis of **new technologies**, that is identical with the three infrastructure types explicitly mentioned in the Directive with respect to size, purpose, and economic relevance⁵

⁵ I.e. new LNG technologies. In May 2007, ERGEG sent its advice on “The regulatory treatment of new LNG technologies” to the European Commission, analysing to which extent some new regasification technologies fall under the infrastructure definitions of the Gas Directive.

3.2 Requirements

Art. 22 para. 1: [...] under the following conditions:

The requirements listed hereunder are of a general nature and apply in addition to the guidance on the range of exemptions and conditions (see below, 3.3.)

Art. 22 para. 1 (a): the investment must enhance competition in gas supply and enhance security of supply;

In assessing the two criteria of enhancing competition in gas supply and security of supply, a comprehensive analysis shall be used in order to decide whether expected improvements outweigh expected drawbacks affiliated with exemption of the infrastructure.

3.2.1 Enhancement of competition in gas supply

The criterion of the enhancement of competition in gas supply will in most cases require the most extensive proof by the applicant and examination by the deciding authority. When assessing this criterion, the deciding authority shall mainly focus on the relevant market. The impact of the project on the markets of neighbouring countries shall be assessed with assistance from the competent foreign authorities, where requested by the deciding authorities. The result of this assessment has to be considered when deciding about the exemption.

In assessing a project's potential impact on competition, the relevant authorities shall define the relevant markets and assess the position of the applicant and/or the proposed user in the relevant markets. For the definition of the relevant markets and the assessment of competitive effects, the relevant authorities shall apply analytical techniques that are consistent with requirements in European Competition Law and with the precedents established by the competition authorities of the EC⁶ with respect to Art. 82 EC Treaty, EC merger regulation⁷ and the Commission's implementing regulation⁸. It is important to assess whether the exemption itself has a negative impact on competition (Art. 22 (1) e)).

⁶ See COMMISSION NOTICE on the definition of the relevant market for the purposes of Community competition law, published in the Official Journal: OJ C 372 on 9/12/1997, http://ec.europa.eu/comm/competition/antitrust/relevma_en.html.

⁷ Council Regulation (EC) 139/2004 of January 20, 2004 on the control of concentrations between undertakings. <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:024:0001:0022:EN:PDF>

⁸ Commission Regulation implementing council regulation 2004 L 133/1; <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:133:0001:0039:EN:PDF>

Under these requirements, the following issues shall be examined:

3.2.1.1 Market definition

The relevant market for competition issues is established by defining the relevant product and geographic markets. While the relevant product market is defined by substitutes on both the demand and supply side of the market, the relevant geographic market is defined to comprise the area in which the undertakings concerned are active and in which the conditions of competition are sufficiently homogeneous.

The objective of defining a market is to define the boundaries of competition between firms and to identify those actual competitors of the undertakings involved that are capable of constraining those undertakings' behaviour and of preventing them from behaving independently of effective competitive pressure.⁹

3.2.1.2 Assessment of market structure

After the relevant markets have been defined the applicant's and the proposed user's expected market position after the investment, capacity allocation, and the market structure need to be analysed. Market shares, concentration levels and barriers to market entry provide useful first indications of the market structure, of the market position and the competitive importance of the applicant and the proposed user.

According to Community case law, market shares of 50% or more may in themselves be evidence of a dominant market position.¹⁰ The relevant market share levels for ascertaining a dominant market position of the applicant and the proposed user in national markets may be different in the respective national laws of the Member States, whereas a coherent application of national and European law must be ensured. Further criteria for market assessment may be, *inter alia*, financial power, vertical integration, and potential competition.

- a) The applicant must provide information on his market position as well as that of designated shippers in supply or production or export or import of natural gas in any jurisdiction affected by the project or the exemption, including affiliates and related companies that have such a position or a substantial relationship thereto.
- b) In the case that a project company is controlled solely or substantially by a producer or supplier that has a dominant position in the importing and exporting countries, the overall impact on competition will be assessed taking into account these elements.

⁹ See COMMISSION NOTICE on the definition of the relevant market for the purposes of Community competition law, published in the Official Journal: OJ C 372 on 9/12/1997.
http://ec.europa.eu/comm/competition/antitrust/relevma_en.html.

¹⁰ See Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (2004 C 31/5) as well as relevant case law on Art. 82 EC.

- c) To this effect, the following items shall be assessed, based also on information provided by the applicant:
- Market definition
 - Analysis of market shares
 - Analysis of effects on upstream and downstream markets
 - Existing and (other) potential competitors; comparing and ranking the proposed project with other existing and planned projects.
 - Capacity share of the proposed project in relation to the total capacity in the relevant market
 - Legal and other barriers to market entry
 - Predominant cost structure in the relevant market
 - Offer of planned products and degree of differentiation
 - Possible alternatives
 - Expected behaviour and reaction of companies already active in the market.

3.2.1.3 Enhancement of competition in the relevant market

The criterion of the enhancement of competition requires that a dominant player who wants to benefit from an exemption must prove that his market position will decrease as a result of the exemption and must show how the investment is intended to enhance the position of smaller players. Such an enhancement of competition in the relevant market could be given in case of:

- Market entry of new competitor(s)
- Diversification of supply sources of gas: New gas sources are opened up and a greater volume of gas is available to the market
- Diversification of suppliers: Increased number of suppliers enter the relevant markets
- Decrease in the market position of a dominant player.

An enhancement of competition is of course not sufficient per se in order to obtain an exemption. The enhancement of competition has to be substantial enough to justify the exemption and the four other tests of the Directive need to be met – e.g. it is also necessary to ensure that the exemption itself does not have a negative impact on competition.

In addition, competent authorities should make sure that they look at the overall impact on competition of a new infrastructure, not just the impact on market shares. If a dominant player builds a new facility and opens it up to other shippers, its market share might go down, but the dominant player may gain other competitive advantages on other fronts.

Finally competent authorities should remember that there is a greater likelihood that competition will be enhanced when an exemption is given to a new entrant.

LNG terminals and some interconnectors can provide access to alternative sources of upstream gas supplies and storage facilities can provide alternative sources of flexibility, which could be of benefit to new entrants.

3.2.1.4 Ownership-/company structure

The relevant regulatory authority shall apply the following rules with respect to the ownership-/company structure:

The project sponsors must provide the regulatory authorities with information on:

- the ownership of the project company
- its by-laws and allocation of voting rights
- any management links or substantial financial or contractual relationships between the project company and the proposed users of the infrastructure
- if the deciding authority determines that any of the shareholders or users with sole or substantial control of a project company has significant ties to gas sales or production activities in the exporting country, sufficient information from the project company concerning information on gas sales or production in the exporting country has to be provided in order to enable the calculation of market shares and a determination whether the project company is controlled in the above mentioned sense by anyone having a dominant position in the exporting countries.

3.2.2 Enhancement of security of supply

When determining whether a project enhances security of supply¹¹, possible criteria can be:

- Total amount of new capacity
- Diversification of national / European supply sources (competent authorities should take into account the benefits in terms of supply diversification brought about by new infrastructure which is able to take in gas from diverse geographic sources)
- Needed capacity expansions to meet future demand

In case of not easily duplicable infrastructures, the NRA should, where feasible, also assess the level of competition and security of supply that would result from granting an exemption for the same project to another interested sponsor, if any.

When assessing enhancement of security of supply, the deciding authorities also shall focus on their national markets. Possible impacts on security of supply outside the relevant jurisdiction shall be assessed by the competent foreign authorities (see above 3.2.1).

3.2.3 Risk assessment

Art. 22 para. 1 (b): the level of risk attached to the investment is such that the investment would not take place unless an exemption was granted;

¹¹ Exemptions are no better for enhancing security of supply than regulated investment. Exemptions are tools for facilitating investment that otherwise would not take place.

Regulators shall provide a stable, foreseeable and legally binding regulatory framework and consideration of special tariff treatment of new infrastructure projects.

- a) Deciding authorities shall investigate the financing of such projects under a system of regulated TPA and shall compare the findings to the information on the proposed infrastructure, relying on information concerning the regulated gas network, tariffs and demand in the destination countries – which the regulator will obtain from the project sponsor or applicant and verify against other sources.
 - b) Deciding authorities shall make this determination based on the results of the market analysis and on the following (minimum) information to be provided by the applicant:
 - throughput estimates
 - estimated construction and operating costs of the project
 - expected depreciation period
 - expected rate of return
 - expected revenues
 - explanation as to why these expectations cannot be met under a regulated TPA regime.
- Another issue NRA should look at is whether the risk is such that it would be beneficial to let investors bear it, instead of imposing it on users in the form of a regulated tariff system for the proposed infrastructure.

3.2.4 Unbundling requirements

Art. 22 para. 1 (c): the infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose jurisdictions that infrastructure will be built;

The unbundling requirements of the Directive should equally apply here.

3.2.5 Charges requirement

Art. 22 para. 1 (d): charges are levied on users of that infrastructure;

The project sponsor will have to prove in connection with the information to be provided on costs, revenues, depreciation, etc. if and to what extent charges are levied on users. If the scope of the requested exemption includes exemption from tariff regulation, the applicant must at least prove that charges will be applied in a non-discriminatory manner.

3.2.6 Internal market

Art. 22 para. 1 (e): 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.

- a) the applicant will provide the relevant information on the project design and anticipated flows to the destination market, and consult with the respective TSOs;
- b) the project will be deemed compatible with the “efficient functioning of the regulated system to which the infrastructure is connected” if the regulatory authorities determine that:
 - the project will not cause constraints on the regulated system requiring investments having a significant adverse effect on the welfare of system users including end-consumers;
 - in particular the project economics are not unduly influenced by peculiarities (e.g. simplifications, socialisation of certain costs) in the tariff system of the regulated infrastructure, making an inefficient bypass commercially attractive.

Competent authorities should also assess the impact that a particular TPA exemption may have on TPA more generally throughout the system, based on how reliant the system is on a particular piece of infrastructure.

3.3 Decision

Art. 22 para. 3 (a): The regulatory authority referred to in Article 25 may, on a case by case basis, decide on the exemption referred to in paragraphs 1 and 2. However, Member States may provide that the regulatory authorities shall submit, for formal decision, to the relevant body in the Member State its opinion on the request for an exemption. This opinion shall be published together with the decision.

The decision by the competent authority of whether to grant an exemption and if so its nature, and any mitigating conditions that are required, will be determined by the five tests prescribed in Art. 22. The deciding authority’s goal in “designing the decision” shall be a balanced approach between the investor’s needs and the market’s need for TPA. The next sections show different ways in which exemptions could be structured and mitigating conditions that could be put in place.

3.3.1 Scope of exemption

The exemption can be granted from legal requirements arising from the articles listed in Art. 22 of Directive 2003/55/EC as well as from Regulation 2005/1775/EC. Art. 16 (b) of Regulation 2005/1775/EC should be interpreted in a way that when only part of the infrastructure is exempted or where the exemption only applies to part of applicable rules, the remaining provisions remain applicable.

3.3.1.1 Partial exemption

Art. 22 para. 1: [...] may, upon request, be exempted from the provisions of Articles 18, 19, 20, and 25(2), (3) and (4) [...]

Art. 22 para. 3 (b) (i): The exemption may cover all or parts of, respectively, the new infrastructure, the existing infrastructure with significantly increased capacity or the modification of the existing infrastructure.

Exempting only part of an infrastructure (i.e. only allowing part of the infrastructure capacity to be exempted) and / or only a part of the rTPA rules are tools that can be used to mitigate the impact of an exemption on regulated TPA, safeguarding the goal of directive 2003/55/EC of making all existing infrastructure available on a non-discriminatory basis to all market participants and safeguard the principle of proportionality.

“Partial exemptions” shall be defined as exemptions with respect to:

a) Part of the infrastructure

If the overall benefits of a full exemption do not outweigh the costs thereof on the default regime of rTPA, granting the exemption for only part of the capacity on that infrastructure can be one solution to ensure that the principle of proportionality is upheld.

Another tool to help achieve this is to grant an exemption for forward flows but not for **backhaul flows**.

b) Part of TPA rules

Another means of ensuring that the decision is proportional is to grant an exemption from some rules and not others, for example from tariff regulation but not from regulated TPA as a whole.

c) Combined solution of a) and b)

The above mentioned tools (including open seasons, which was mentioned earlier) can also be used in combination, which could be designed as follows, subject to the general conditions identified above:

- **Partial exemption from tariff regulation (negotiated TPA)**

All or part of the infrastructure could be exempted from tariff regulation. This would remove the obligation of the operator to have tariffs approved by the regulator, whilst tariff setting would need to be conducted in accordance with objective, transparent and non-discriminatory criteria.

If an exemption is granted for the tariffs but not for the TPA requirements to a sponsor which is also (affiliate to) a user of the infrastructure, the capacity allocation will be organised in such a way that this user is not favoured compared to other users. Some allocation mechanisms should then be avoided as they are potentially discriminatory. A user which is also sponsor of the project could indeed buy capacity at such a high price that nobody else could compete with and this without significant prejudice as the amount is paid to himself (or to an affiliated company).

- **Partial TPA-exemption in the form of authorisation to allocate capacity under long term contracts¹²**

All or part of the capacity to the infrastructure could be allocated under long-term contracts. This tool will help investors underwrite the financial cost of a project by providing certainty with regard to future revenue recovery. In addition, it can give the investor some additional certainty with respect to unexpected changes in the regulatory framework. In some countries where tariffs are subject to yearly regulatory renewal, tariffs could be set for a longer period of time. In order to allow for the broadest possible access to the infrastructure, there could be several independent segments of the total capacity determined for long-term capacity contracts to be allocated to different users, with due regard to the possibility of short-term allocation. Allocation of capacity is best based upon open season.

- **TPA-exemption in the form of initial capacity allocation to preferred customers (exclusion of TPA)**

All or part of the capacity of the infrastructure could be exempted in a way that removes the obligation to organise a non-discriminatory allocation procedure (e.g. open season).

This category of exemption may be particularly appropriate where TPA-requirements (in particular capacity allocation by means of open season) would worsen competition, especially in the case of investors with low market share or new entrants requesting exclusive use of the infrastructure in order to facilitate market entry.

¹² Notwithstanding this section, it is noted that granting an Art. 22 exemption is not a prerequisite for the conclusion of long-term capacity contracts under the regulated TPA regime, between TSOs and shippers. As ERGEG and the Commission have expressed, long-term capacity contracts are fully compatible with the rTPA regime and retain their value for the development of infrastructure, as long as they have no adverse impact on competition. The exact legal implications of long-term capacity contracts under competition and regulation law are yet to be examined. Current guideline 1 (1) annexed to Regulation 2005/1775/EC requires that TSOs “offer firm and interruptible services down to a minimum period of one day”. According to Art. 12 Regulation 2005/1775/EC Member States may provide for more detailed measures.

3.3.1.2 Full exemptions

Full exemptions encompass the entire capacity on the infrastructure. They may be granted when, in addition to passing the five tests, the principle of proportionality is upheld because the overall benefits of a full exemption outweigh the costs of such an exemption on the default TPA regime. At the same time, as described below, conditions can be used to mitigate any negative impact on the market.

3.3.1.3 Conditions

Art. 22 para. 3 (b) (ii): In deciding to grant an exemption, consideration shall be given, on a case by case basis, to the need to impose conditions regarding the duration of the exemption and non-discriminatory access to the interconnector.

Art. 22 para. 3 (b) (iii): When deciding on the conditions in this subparagraph account shall, in particular, be taken of the duration of contracts, additional capacity to be built, the modification of existing capacity, the time horizon of the project and national circumstances.

Art. 22 para. 3 (c): When granting an exemption the relevant authority may decide upon the rules and mechanisms for management and allocation of capacity insofar as this does not prevent the implementation of long term contracts.

Conditions on the duration of the exemption and the non-discriminatory access to the infrastructure as mentioned in Art. 22 para. 3 (b) (ii) shall be interpreted as referring to all kinds of infrastructure under the scope of Art. 22. The mere mention of an “interconnector” is too narrow and would, if taken literally, unjustly treat new LNG infrastructure and storage less strictly.

Duration of the exemption

- a) The exemption shall generally not be longer than the expected and efficient pay-back period of the project as assessed by the NRA. A shorter duration shall be justified, where the risk connected to high investment volumes will sink significantly once a significant share has been remunerated. The duration of the pay-back period shall be assessed, taking into account in particular comparing different scenarios of revenue streams.
- b) Where the deciding authority’s considerations depend at least partly on market predictions, a clause for revision shall be attached to the exemption, subject to procedural admissibility of such clauses. This clause shall be sufficiently specific as to the conditions under which the exemption may be revised and shall explicitly mention the consequences of such revision. Investors need to know upfront under what circumstances exemptions may be reviewed. These circumstances should be reasonable and stable.
- c) An exemption may also be reviewed due to other factors besides imprecise market predictions. For example,
 - when market circumstances change markedly (permanently) such that the exemption has a negative impact on competition/security of supply and therefore customers

- when mergers, takeovers, or other forms of company restructuring result in a change in market design and market share. Applicants are obliged to notify the deciding authority on any such changes.
- when competent authorities witness capacity hoarding;
- when capacity is transferred to an affiliated shipper of the project sponsor which increases its market dominant position
- the conditions associated with the exemption have been continuously and materially not met by the infrastructure operator, owner or users
- if there is a material change to the degree in which the requirements of the exemption are met with respect to the facility as the result of any action or omission of the facility owner, operator of the facility or through putter.

In these cases as well, in order to maximise investor certainty, there will need to be clear and stable rules laying out the reasons why an exemption might be reviewed. Any decisions regarding the modification of an exemption must be proportional to the circumstances that arise. A revocation of an exemption should be seen as a last resort given the impact that it could have the cost of investment in the future.

Non-discriminatory access

Where only a partial TPA exemption is granted, a non-exempted part of the infrastructure will be reserved for TPA. An appropriate solution is to provide non discriminatory access by means of open season allocation procedures. Anti-hoarding mechanisms shall apply to both the non-exempted and the exempted part. Regimes like **use-it-or-lose-it** seem most appropriate to ensure that the respective part is efficiently used by being returned to the market. These arrangements must ensure the effective and efficient use of capacity, which is equally necessary for TPA and exempted infrastructure.

Duration of contracts

Without prejudice to long term contracts needed to make an investment feasible, due regard should be also given to the need for short term contracts in order to allow for competition. The competent authorities shall ensure compliance with relevant legislation as well as other relevant developments¹³.

Mechanisms for management and allocation of capacity

- a) Where the facility is open to TPA, deciding authorities shall ensure appropriate implementation of mechanisms for capacity allocation.
- b) For all exemptions, deciding authorities should be able to impose appropriate congestion management measures (e.g. UIOLI measures) so as to make sure that capacity is used to the fullest extent in response to market demand and that the exemption fulfils its original role;
- c) when conditions are imposed, the NRA shall, where appropriate, approve the design of their implementation prior to the start of commercial operation of the infrastructure;

¹³ [E.g. judgment of the Court \(Grand Chamber\) of 7 June 2005, OJ C 70 of 2.03.2003.](#)

- d) the NRA shall check the compatibility of the rules/practices prevailing on the exempted infrastructure with the connected systems;
- e) a secondary market for capacity, or a UIOLI system can only work successfully if some operational rules are harmonised or at least consistent with other related systems and the services within a given facility are standardised as necessary.
- f) Effective anti-hoarding provisions, e.g. short-term and / or long-term use-it-or-lose-it requirements should apply to all infrastructure, whether exempted or not from TPA. These conditions must be non-discriminatory, transparent and proportionate. It would not be reasonable for the operator of a facility to be against economical access by third parties when the capacity is unused, that is, when the holders of capacity did not nominate its use.

Transparency

Deciding authorities should assess if and to which degree transparency requirements (e.g. for technical capacity etc.) have a negative impact on the investment decision. With respect to LNG and storage facilities, the transparency requirements stipulated by GGPLNG and GGSSO can be used as a basis.

3.3.2 Co-ordination and Co-operation

Art. 22 para 1 (e): [...] In the case of an interconnector any exemption decision shall be taken after consultation with the other Member States or regulatory authorities concerned.

The deciding authorities shall apply the following procedural rules:

- a) Upon receiving an Art. 22 application, the deciding authority shall notify other concerned authorities without undue delay.
- b) The deciding authority shall share all the relevant documentation with other concerned authorities, including at least a summary, in English, of the necessary information to be provided by the applicant, and give the other concerned authorities at least four weeks time to respond in writing, unless a shorter deadline is prescribed by law.
- c) The deciding authority shall inform other concerned authorities of the intended decision.
- d) Other concerned authorities shall safeguard all confidentiality requirements determined by the deciding authority.

3.3.3 Market participation and consultation

Where the participation of significantly affected market parties is not already prescribed in national legislation, deciding authorities shall at least conduct an open market consultation and take the relevant findings into account.

3.3.4 Early notification of the Commission

The European Commission should be notified of a planned or pending application for exemption as early as possible in the process.

4 RESPONDING TO THE PUBLIC CONSULTATION

Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and especially Article 22 thereof aims at the promotion of effective competition and security of supply by creating incentives for efficient investments in new infrastructure projects, while at the same time recognizing the need for non-discriminatory access to relevant infrastructures. ERGEG agrees upon the following guidelines which constitute a harmonized and transparent framework for competent authorities when deciding on exemption procedures.

The underlying Guidelines on Article 22 are designed within the legal framework set by the existing Art. 22. The guidelines should be used by deciding authorities to guide their decisions when considering Article 22 applications. As shown in the analysis report on the European Regulators Experience with Article 22 exemptions of Directive 2003/55/EC [Ref: E07-TNI-01-04]¹⁴, a significant amount of infrastructure projects have either received exemptions or are in the process of requesting exemptions. This shows the need for a harmonized or at least consistent and improved approach for implementing Article 22. This is the aim of the present guidelines.

ERGEG invites all interested parties to comment on the issues raised in this paper – and in particular those questions highlighted below. Any comments should be received by **2 May 2008** and should be sent by email to **article22@ergeg.org**.

Following the end of the public consultation period, ERGEG will publish all comments received from stakeholders. Any respondents wishing ERGEG to treat its contribution as confidential should clearly state this in their reply and endeavour to give any confidential material in annexes that can be separated from publishable non-confidential material.

4.1 Questions for stakeholders

- ◆ 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?
- ◆ Do you consider the present scope of eligible infrastructure to be too narrow?
- ◆ 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?
- ◆ Should open seasons also be used to allocate equity?

¹⁴ cf. ERGEG's Report on Article 22 Exemptions, Ref: E07-TNI-01-04, 13 September 2007

http://www.ergeg.org/portal/page/portal/ERGEG_HOME/ERGEG_DOCS/ERGEG_DOCUMENTS_NEW/GAS_FOCUS_GROUP/E07-TNI-01-04_Art.%2022-AnalysisReport_finalLAST.pdf

- ◆ 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?
- ◆ Are the described criteria for assessing the effects of an investment in infrastructure on enhancement of competition in gas supply appropriate?
- ◆ Are the described criteria for assessing the effects of an investment in infrastructure on enhancement of security of supply appropriate?
- ◆ Are the described criteria for the risk assessment appropriate?
- ◆ 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?
- ◆ To what extent should consultations with neighbouring authorities be done?
- ◆ 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?
- ◆ Do you believe that Art 22 exemptions should also benefit incumbents or their affiliates? If yes in what way and to what extent?
- ◆ 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?

Annex: Other Art. 22 provisions not relevant with respect to these guidelines

For the sake of completeness, the remaining Art. 22 provisions, which in the context of these guidelines are not further elaborated on, are quoted here:

Art. 22 para. 3 (d): The exemption decision, including any conditions referred to in (b), shall be duly reasoned and published.

Art. 22 para. 4: The exemption decision shall be notified, without delay, by the competent authority to the Commission, together with all the relevant information with respect to the decision. This information may be submitted to the Commission in aggregate form, enabling the Commission to reach a well-founded decision. In particular, the information shall contain:

- (a) the detailed reasons on the basis of which the regulatory authority, or Member State, granted the exemption, including the financial information justifying the need for the exemption;
- (b) the analysis undertaken of the effect on competition and the effective functioning of the internal gas market resulting from the grant of the exemption;
- (c) the reasons for the time period and the share of the total capacity of the gas infrastructure in question for which the exemption is granted;
- (d) in case the exemption relates to an interconnector, the result of the consultation with the Member States concerned or regulatory authorities;
- (e) the contribution of the infrastructure to the diversification of gas supply.

Within two months after receiving a notification, the Commission may request that the regulatory authority or the Member State concerned amend or withdraw the decision to grant an exemption. The two month period may be extended by one additional month where additional information is sought by the Commission.

If the regulatory authority or Member State concerned does not comply with the request within a period of four weeks, a final decision shall be taken in accordance with the procedure referred to in Article 30(2).

The Commission shall preserve the confidentiality of commercially sensitive information.