Exemptions to Third Party Access for new infrastructures in the European Community gas sector

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The exception that defies the rule?

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1. INTRODUCTION

Energy is high on the agenda. It is vital to the needs of present day society. At the same time it is a sector that poses perplexing dilemmas for policy makers. They must take into account, amongst others, socio-economic, financial, geo-political and strategic considerations all at the same time. Notwithstanding these complexities, the EU has the ambition to become more involved in the wide array of issues that energy brings along.[1]

Natural gas (hereinafter: gas) is an essential commodity to meet the ever growing demand for energy.[2] As a result of the ongoing depletion of EU gas fields,[3] few Member States can (still) rely solely on domestic reserves. Some argue that liberalising this sector is the only way to ensure a secure level of supply in the years to come, since it could give incentives to increase the capacity and efficiency of gas infrastructures.[4] The topicality of the matters discussed in this thesis is highlighted by the recently adopted EU Reform Treaty.[5] This Treaty focuses more on energy policy than the previous Treaties It aims to improve, *inter alia*, the internal energy market and the security of supply.

If the gas market is ever to become successfully liberalised,[6] several thorny matters must be dealt with. Especially access issues remain challenging. According to the European Commission, (potential) gas suppliers must have effective, transparent and non-discriminatory access to the gas networks.[7] This is essential to achieve a market structure in which competition can thrive.[8] The last few decades, high entry barriers have prevented easy access by potential competitors (which shall be referred to as 'third parties'), which in turn made competition difficult.[9]

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[1] See the speech by Commission President Barroso, delivered at 22 March 2006 in Brussels during the inauguration of the *Maison des energies renouvelables*: 'Europe needs an energy strategy which balances three objectives: tackling climate change, guaranteeing the competitiveness of the European economy and ensuring long-term security of energy supplies'.

[2] For an indication of the increase in demand, see the report by the International Energy Agency (2003, *infra* note 23). See also Annex III of this thesis on p. 82.

[3] *Ibid.*

[4] See e.g. *The Economist*, 14 April 2007, p. 2.

[5] For the latest information on the draft EU reform Treaty, see: http://ec.europa.eu/commission_barroso/president/focus/council_062007_en.htm#key (last visited 25 September 2007). This reform Treaty is not yet in force and will be up for vote during the next Intergovernmental Conference.

[6] The liberalisation of energy markets is one of the aims of the EC Treaty, see Articles 3(1)u, 154(2), 157 EC & 175(2)(c) EC.

[7] Including transmission and distribution networks.

[8] See e.g. the speech given by the – then – European Commissioner for competition Monti, 'Applying EU Competition Law to the newly liberalised energy markets', at the World Forum on energy regulation in Rome on 6 October 2003, accessible at http://ec.europa.eu/comm/competition/speeches/index_theme_26.html (last visited 25 September 2007).

[9] For a general overview, see Slot, 'Energy and competition', *CMLRev* 1994, p. 511-548. See also Kuipers, De Rijke & Schong, 'Energie en mededinging: verkenning van een mijnenveld', in: Ottow, Eeken & Edens *et al*. (ed.), *De rol van het mededingingsrecht in gereguleerde markten*, Boom Juridische uitgevers: Den Haag 2001. See in particular p. 93-97.

The distinctive features of the gas sector (which shall be discussed in more detail in par. 2.4) have prompted the Community institutions to tackle access issues not only by way of general competition rules, but also with sector-specific legislation.[10] The latter rules envisage a fully opened market for gas supply as of 1 July 2007. This necessitates access for potential competitors (the so-called 'third parties').[11]

Since competition thus presupposes that potential competitors are able to enter the relevant market, the principle of Third Party Access (TPA) is a key concept in the quest for a well-functioning gas market.[12, 13] Notwithstanding the possible merits of TPA for competition, however, the access regime must also take into account other interests, such as the security of supply. This is particularly apparent when dealing with the establishment of new gas infrastructures. Although TPA should (at least in principle) be applicable, the principle may decrease incentives to finance such projects, since investors greatly value *exclusive* supply contracts. If this leads to the infrastructure not being built at all due to a lack of finance, the overall gas supply capacity will not increase. In turn, this may harm the security of supply.

In order to strike a balance between the different interests at stake, the sector-specific gas legislation enables the National Regulatory Authorities (NRA's) to exempt a new gas infrastructure from TPA. Although such exemptions must take into account a wide range of relevant facts and circumstances, the conditions are rather vague and can thus be interpreted in many different ways. Only few rules have been enacted on the European level to provide guidance.

Therefore, it is important to examine how the exemption rules are being applied in practice. In particular, I shall discuss the exemptions which have been granted for the benefit of new gas infrastructures.[14] Whenever relevant and helpful,[15] I will also deal with similar issues in other (network-bound) sectors.[16, 17]

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[10] See e.g. the second gas Directive (*infra* note 124) and Regulation 1775/2005 (*infra* note 137).

[11] Article 23(1)(c) of the second gas Directive, *infra* note 124. For an overview of the time schedule, see Ashe-Taylor & Moussis, 'EU Competition Law and Third Party Access to gas transmission networks', *Utilities Law Review* 2004/2005, p. 105.

[12] For a concise explanation of the concept of a 'network industry', also see Lapuerta & Moselle, 'Network Industries, Third Party Access and Competition Law in the European Union', *Northwestern Journal of International Law and Business* 1998/1999, p. 454-456.

[13] Another similarity between the different network industries is their common historical pattern, also see Lapuerta & Moselle 1998/1999, *supra* note 12, p. 455.

[14] Whenever relevant, I shall compare the regulatory framework of the gas sector with that of other network bound sectors, especially the electricity sector. According to Palasthy ('Third Party Access in the Electricity Sector: EC Competition Law and Sector-Specific Regulation', *Journal of Energy and Natural Resources Law* 2002 (p. 8)), the general ideas underpinning the rules covering network bound sectors are to a large extent transposable. For a similar view, see the 'Notice on the application of competition rules to access agreements in the telecommunications sector' (OJ 1998, C 265/02, in particular par. 13).

[15] Such as the electricity sector. Notwithstanding the similarities between the gas and the electricity sectors, one should also take into account the differences between the two. First, gas is a primary energy source (and can therefore only be produced where there are gas fields), while electricity is a secondary energy source. Second, gas can be stored for long periods of time, which is not the case for electricity. Third, the gas sector is also more often subject to long-term supply contracts, mostly caused by the large-scale investment a gas network needs. Fourth, the gas market is dominated by a small number of non-EU suppliers. Lastly, there is a slow pace of technological progress. Most of these market features strengthen the position of incumbents, which are less likely to be

Before doing so, however, I believe it is important to first sketch the general characteristics of the gas sector as such (chapter 2). I will show what the impact of the general competition rules may be (chapter 3).[18] Thereafter, the sector-specific rules shall be dealt with (chapter 4).[19] Chapter 5 will deal with the relationship between these two sets of rules. Also, the latest developments in this field shall be discussed (chapter 6).

After that, I will put forward and analyse the exemptions given by various domestic authorities (chapter 7). I shall have regard to the United Kingdom, the Netherlands and Italy, since these are the only countries where such exemptions have been granted.[20] While doing so, I shall also examine the regulatory frameworks of these Member States. A comparison of these exemption orders shall be given as well (chapter 8).

In sum, I will explore the effect of both the general competition and the sector-specific rules on the liberalisation of the gas market. In addition, their influence on access issues shall be dealt with. More specifically, it shall be examined how exemptions to Third Party Access are granted by the Dutch, British and Italian authorities for the benefit of new gas infrastructures. In particular, I will analyse how the conditions of this exemption possibility are applied in practice.

'dethroned' as a result of innovative products by new market entrants, than in, say, the telecommunications market. See e.g. Cameron, 'Completing the internal market in energy: an introduction to the new legislation', in: Cameron (ed.), *Legal aspects of EU energy regulation: implementing the new directives on electricity and gas across Europe*, OUP: Oxford/New York 2005, p. 12.

[16] Such an approach seems to be supported by the similar way in which the Commission has tackled access issues in the different segments of the energy sector. The different 'waves' of regulatory initiatives to increase competition in the energy sector have always consisted of legal documents on both electricity and gas. From a substantive point of view, these documents mostly contain very similar provisions.

[17] See also Slot & Skudder, 'Common features of Community law regulation in the network-bound sectors', *CMLRev* 2001, p. 87-129.

[18] See Palasthy 2002, *supra* note 14, p. 2. He considers that the entire regulatory framework must be examined in order to reach viable conclusions on TPA matters.

[19] It is to be noted that general competition rules and sector-specific regulation are very much interlinked. See e.g. the Telecom Access Notice, OJ 1998, C 265/2, par. 58.

[20] According to the European Commission's website, these are – until now – the only Member States from which the Commission has received decisions on exemption matters, see: http://www.ec.europa.eu/energy/gas/infrastructure/exemptions_en.htm (last visited 25 September 2007). It must be added here, that one Member State seems to have been omitted – namely Greece. That country also took part in the assessment of the Poseidon interconnection, as shall be seen in more detail in par. 7.4.5 below.

2. THE EUROPEAN COMMUNITY GAS SECTOR

2.1 Gas: a vital commodity

In order to appreciate the wider context of the issues under review, it is important to illustrate the importance of the gas sector. Gas provides a large part of global – and EU – energy demand.[21] It constitutes a separate market from other energy markets, mostly as a result of its imperfect substitutability.[22] Many factors indicate that the gas sector will become ever more important in the upcoming years, mainly caused by a steadily growing demand.[23, 24, 25] This growth relates, *inter alia*, to the increased use of gas for the generation of electricity. Alternative ways to generate electricity (such as burning coal) are becoming less attractive, mostly due to their high level of CO_2 emissions and the restrictions placed thereon.[26] But also environmental concerns may increase gas demand, since gas is seen as a relatively 'clean' energy source. Other circumstances which add to the importance of gas are the practical barriers to a more productive use of renewable energies and the (political) push for a reduced use of nuclear power.[27]

2.2 Liberalisation of the gas markets

Article 4(1) EC stipulates that the Community and the Member States shall act in accordance with the principle of an open market economy with free competition.

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[21] According to the Energy Information Administration of the US Departement of Energy (accessible via http://www.eia.doe.gov/pub/international/iealf/table18.xls, last visited 25 September 2007), natural gas provided almost a quarter of global energy needs in the last few years.

[22] See e.g. Roggenkamp, Rønne, Redgwell & Del Guayo (eds.), *Energy Law in Europe – National, EU and International Law and Institutions*, OUP: Oxford 2001, p. 236-237. This assertion is supported by several European Commission decisions concerning mergers of energy utilities. See e.g. Press release IP/94/805, which concerned the Commission's examination of the proposed acquisition involving gas utility Distrigaz and electricity company Electrabel. The Commission approved the proposal, holding that the gas and electricity sectors constitute two different markets as the 'capability for substitution (…) between these two sources of energy' was anything but perfect.

[23] The International Energy Agency, in its World Energy Outlook Insights 2003, predicted total gas demand in the EU-25 would annually increase by 1,8 % between 2002 and 2030, going from 473 to 786 bcm. During the same period, EU production is projected to decrease from 240 bcm to 147 bcm. Thus, this study foresees an annual 'supply gap' of 639 bcm by 2030.

[24] The growth in gas demand is forecasted to be particularly strong in Southern Europe, triggered by the high number of power generation facilities which run on gas there. See Kjärstad & Johnson, 'Prospects of the European gas market', *Energy Policy* 2007, p. 886-887.

[25] The surge in gas demand is not only projected in Europe, but also for instance in Australia. There, gas consumption has increased by 6,9% annually over the last 25 years. Until 2020, it is foreseen to grow by another 3% every year. See Dickson, Short, Donaldson & Roberts, 'Australian energy: key issues and outlook to 2019-20', in: *Australian Commodities* 2002, p. 203-205.

[26] Total emissions will have to go down from 1646,1 to 1623,85 million tons of CO_2 between 2005 and 2012. Although this decrease is perhaps smaller in size than some people would have hoped for, it needs to be underlined that it is still a 1,4% reduction in a period in which, because of economic growth, emissions normally would have gone up. Accordingly, the scheme could indeed have quite an impact. See Directive 2003/87/EC of 13 October 2003, OJ 2003, L 275/32.

[27] Kjärstad & Johnson 2007, *supra* note 24, p. 86.

Although this objective also applies to the European energy market (and the gas sector in its wake), it has not yet fully been achieved.[28]

Admittedly, the European energy market has come a long way in the last few years.[29] For instance, back in the 1990's, the ECJ still had to deal with strict import and export monopolies in various Member States.[30] This rigid market structure was sustainable due to two main reasons.[31] First, there were (still) large domestic gas reserves which resulted in excess supply.[32] Second, the supply from third states was not considered to be a potential problem.[33] During the last couple of years, however, reserves have been dwindling, domestic production has fallen and prices have been steadily on the rise. Also, the supply by some third states sometimes seems, at best, uncertain.[34]

Liberalisation – and third party access in its wake – is believed to be capable of taking on these issues, by e.g. promoting competition, tackling incumbent rigidity and strengthening intra-Community gas trade, dynamism and efficiency.[35, 36]

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[28] See the Commission Report on the Energy Sector Inquiry of 10 January 2007 (SEC(2006)1724), in particular p. 7-11. See also *The Economist* (15 September 2007, 'European energy: breaking up is hard to do', p. 71-72), which argues in favour of splitting up energy companies. In addition, the article warns that protectionism may block effective reform of the European energy market.

[29] A comparison of 'old' and recent articles shows that the level of competition has gradually been going up in the last decade. For the 'old' articles, see e.g. Beeston & Charbit, 'Third Party Access in the Energy Sector in EC Law', *Oil and Gas Law and Taxation Review* 1995, p. 5-10 and Ehlermann, 'Quelles règles de fonctionnement pour le marché intérieur de l'énergie?', *Revue du marché commun et de l'union européenne* 1994, p. 450-459. For the recent articles, see e.g. Spanjer, 'European gas regulation: a change of focus', *Department of Economics Research Memorandum*, Leiden University 2006 and Kjärstad & Johnson 2007, *supra* note 24.

[30] See, *inter alia*, the judgments in Case C-157/94, *Commission* v. *The Netherlands*, [1997] ECR I-5699; Case C-158/94, *Commission* v. *Italy*, [1997] ECR I-5789; Case C-159/94, *Commission* v. *France*, [1997] ECR I-5815 and Case C-160/94, *Commission* v. *Spain*, [1997] ECR I-5851. Also see the Case Note by Slot in *CMLRev* 2006, p. 1183-1203.

[31] For more details, see e.g. Spanjer 2006, *supra* note 29, p. 2-5.

[32] As a consequence, the excess supply had lead to very low gas prices. This gave little (political) impetus to attempt to pull down costs *via* liberalisation efforts.

[33] Spanjer 2006, *supra* note 29, p. 3. He argues that the producer countries were believed to be so reliant on Foreign Direct Investment from consumer countries, that they would have little incentive to act in a non-constructive way when the supply of gas is concerned.

[34] One ought not to disregard the political dimension that this topic has. See e.g. the observations that Russia is using gas largely as a tool to regain global power (*The Economist*, 1 July 2006, p. 2) or the ideas of setting up an 'OPEC-like' cartel in the gas sector (*The Economist*, 14 April 2007, p. 13-14). Also see the recent dispute between Russia and Ukraine on gas prices, and Russia's subsequent threat to stop gas supply, e.g. in *The Financial Times*, 31 December 2005, p. 1.

[35] For general observations surrounding TPA and the (European) gas sector, see e.g. White, 'Third party access to gas pipelines', *OGLTR* 1990, p. 191-194; Salter, **'**Third party access to gas and electricity transmission systems in the Community: third party access - your flexible friend?', *JERL* 1993, p. 27-35; Alliance of European Lawyers, 'Third party access in the energy sector - an introduction', *OGLTR* 1995, p. 3-4; Candon, 'Liberalisation of the gas market in the EU', *OGLTR* 1998, p. 353-355; Schong & De Rijke, 'Harmonising the liberalisation of the natural gas and electricity markets: is a single European energy market within reach?', *ULR* 2001, p. 3-7; Trischmann, **'**LNG into Europe: European regulation - American style?', *IELTR* 2004, p. 233-243; Fernandez Salas, Klotz & Moonen, 'Access to gas pipelines: lessons learnt from the Marathon case', *EC CPN* 2004, p. 2, 41-43.

[36] For articles on TPA with regard to specific Member States, see e.g. Christoff, 'Belgium - gas: third party access: energy agenda for Belgian presidency of Council of Ministers', *OGLTR* 1993, p. 31-

2.3 Cross-border networks

In order to achieve a fully liberalised market in energy across the EU, free access must not only be provided within national networks, but also across borders. In its sector inquiry, the Commission underscored the undesired effects of a possible compartmentalisation along national boundaries.[37] This stance corresponds with the Commission's overall energy policy objective to establish a so-called 'Trans European Energy Network'. According to the Commission, such an interconnected system is needed for 'increasing competitiveness in the electricity and gas markets [and] reinforcing security of supply'.[38]

2.4 The gas market: a network bound sector

The gas market is one of the so-called 'network bound' sectors,[39] in which a storage, transmission and/or distribution network is needed to compete. National incumbents often have (or had) a monopoly on these infrastructures. However, the market can be only fully liberalised if third parties have access to these infrastructures as well.[40, 41]

32; Meessen & Perilleux, 'The concept of third party access in the energy sector in Belgian law', *OGLTR* 1995, p. 11-12; Agboyibor & Damay, 'Third party access in the energy sector in France', *OGLTR* 1995, p. 13-15; Meier & Uwe Pritzsche, **'**Third party access to energy grids: the German legal environment and recent developments', *OGLTR* 1995, p. 16-20; Pijnacker Hordijk, 'Third party access in the electricity and natural gas sectors in the Netherlands', *OGLTR* 1995, p. 21-25; Uwe Pritzsche, **'**Germany: third party access', *OGLTR* 1995, p. 4; Oldziej, 'Restructuring the electricity and gas power industries in Poland', *OGLTR* 1995, p. 26-29; Laver & Borresen, 'Third party access to electricity and natural gas networks in Sweden', *OGLTR* 1995, p. 34-37; Musil & De Keijzer, 'The concept of third party access in the gas sector in the Czech Republic', *OGLTR* 1995, p. 38-39; Meier & Uwe Pritzsche, 'Germany: gas - third party access', *OGLTR* 1994, p. 38-39; Wiedemann & Kunth, 'Germany: gas - Federal Supreme Court rules on denial of TPA', *JERL* 1995, p. 13(2), 132-133; Schröder, 'Germany: third party access to gas pipeline refused', *ECLR* 1995, p. 104-105; Meier & Uwe Pritzsche, 'Third-party access in Germany after the VNG decision', *OGLTR* 1995, p. 307-309; Vahrenwald, 'European gas law', *OGLTR* 1995, p. 330-346; Pastor Ridurejo, **'**Spain: energy sector - liberalisation', *OGLTR* 1996, p. 116-118; Cameron, 'Spain: gas - new decree - very limited access to pipeline network granted', *JERL* 1997, p. 294-296; Byok, 'New investment opportunities in German energy', *IFLRev* 1999, p. 24-25; Markert, 'Prospects and problems for German gas competition', *OGLTR* 1999, p. 37-40; Gruber & Kunth, 'Germany: access to the German energy market', *IFLRev* 2000, p. 7-9; Pastor Ridurejo, 'Network access in Spain', *IELTR* 2000, p. 5, 120-125; Borner, 'Negotiated third party access in Germany: electricity and gas', *JERL* 2002, p. 27-39; Horstmann, 'Liberalisation of electricity and gas markets in Germany', *IELTR* 2003, p. 116-128; Zenke, 'Germany's electricity and gas markets stand alone: negotiated third party access', *JERL* 2003, p. 143-152; Mullerat, Jarques & Colome, 'Legal framework for natural gas in Spain', *JERL* 2004, p. 59-65; Davis, 'Poland: gas and electricity - third party access', *IELTR* 2005, p. 51-52; De Angelis, 'Access to upstream and downstream infrastructure in Italy: analysis of the regulated context and lessons learned from the first years of liberalisation', *IELTR* 2006, p. 227-239.

[37] DG Competition report on energy sector inquiry 2007, *supra* note 28, p. 67 *et seq*.

[38] See http://ec.europa.eu/ten/energy/index_en.htm (last visited 25 September 2007).

[39] Other network sectors include e.g. electricity, telecommunications and rail transport.

[40] For the importance of an efficient access regime vis-à-vis energy networks, see e.g. Wälde, 'Access to Energy Networks: A precondition for Cross-border Energy and Energy Services Trade', *Journal of Energy and Natural Resource Law* 2001 (Volume 9), accessible via http://www.dundee.ac.uk/cepmlp/journal/html/volume9.php (last visited 25 September 2007). He argues that '(l)iberalisation of cross-border energy (…) trade is not possible without an effective

Such an access regime is only effective if the regulatory framework duly considers the distinguishing features of network industries.[42, 43]

An important feature of the gas sector is that the set up of infrastructures requires enormous investments. Gas suppliers usually need the financial help from outside investors to cover these investments. Such financiers obviously wish to have the greatest security possible that their investment can be recouped.[44] Hence, they have a preference for long-term exclusive contracts. These contracts guarantee a steady influx of revenue for the gas supplier. However, such contracts may have disadvantageous side-effects on the macro level, as they hinder access to networks and are thus capable of foreclosing effective competition.[45]

Another particularity is that policy makers will probably never allow the gas market to become fully subject to competition. That is to say, a completely liberalised market is believed to be incapable in satisfying all the relevant interests.[46] This holds particularly true for the 'security of supply'. This principle entails a right for individuals to receive gas, even if such a delivery would not be profitable for the supplier.[47] However, under pure market conditions, an undertaking has little incentive to supply under unprofitable terms. Therefore, in order to satisfy the different – and sometimes opposing – interests at stake, an intricate balance must be struck.

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system of providing a *standardised, easily managed and predictable access* to energy networks: electricity transmission grids, gas pipelines and distribution systems [italics added, TvdV]'.

[41] Lapuerta & Moselle (1998/1999, *supra* note 12, p. 474) argue that the access regime as regards third parties must aim for three important objectives. First, the rules must strive for competition in all segments of the market where that is feasible. Second, the incumbent should be prevented from earning monopoly profits from the network. Third, the legislation must offer the network owner reasonable compensation for stranded costs.

[42] Albers, 'The new EU Directives on energy liberalization from a competition point of view', in: Cameron (ed.), *Legal aspects of EU energy regulation: implementing the new directives on electricity and gas across Europe*, OUP: Oxford/New York 2005, p. 41.

[43] See also Wälde 2001, *supra* note 40, chapter 1. He states that Third Party Access is 'an essential condition for creating competitive national energy markets and for creating a competitive cross-border energy markets. Without TPA, existing energy monopolies operate in effect a necessary toll-gate for market entry; the benefits of new supplies and competition go to existing operators rather than to consumers and the economy at large'.

[44] See Cross, Hancher & Slot in: Roggenkamp *et al.* (2001, *supra* note 22, p. 256) suggest that 'long-term take-or-pay contracts [may] contribute to the realization of upstream gas investments, especially in the case of non-EC gas producers'. They also argue that the absence of such contracts may endanger the security of supply of gas.

[45] If the existing network capacity is devoted completely to meet the requirements under existing agreements, new entrants are obviously disabled to access the market. For an assessment, see Slot, 'The impact of liberalisation on long-term energy contracts', *Journal of Network Industries* 2000, p. 287-303.

[46] Some observers argue that liberalisation may, due to market imperfections, not deal with various relevant issues. See e.g. Mahan (ed.), 'Natural gas supply for the EU in the short to medium term', *Clingendael International Energy Programme*, The Clingendael Institute: The Hague 2004. In the preface of this document, Van der Linde brings forward that liberalisation mainly tackles price issues, but fails to sufficiently take into account two other key concerns, namely the security of supply and environmental concerns.

[47] The security of supply has not only been adopted by many Member States, but by the Community rules as well. See the Council Directive 2004/67/EC of 26 April 2004 concerning measures to safeguard security of natural gas supply, OJ 2004, L 127/92.

3. THE GENERAL COMPETITION RULES

3.1 Introduction

The next two chapters will analyse the effect of the general and the sector-specific competition rules on the gas sector. Since this basically concerns the interaction between primary and secondary Community law, chapter 5 shall discuss the interaction between these two sets of rules.

3.2 Article 81 EC

Only few gas supply agreements have been notified to the Commission under Article 81(3) EC.[48] Accordingly, the Commission has only occasionally brought forward its views on compatibility of gas supply agreements with Article 81 EC.[49] Nor have the Community Courts dealt with many such cases. Here, several agreements that *were* reviewed by these two Community Institutions shall be discussed.

An important assessment by the Commission involved the notification of the Gas Interconnector Agreement.[50] This agreement concerned a Joint Venture for the purposes of the construction and operation of a sub-sea gas link between the UK and Belgium. This interconnection was the first of its kind between these two countries, effectively linking the UK and the Continental gas markets.[51] The project's main agreement was concluded for a period of 20 years. The Commission approved the agreement because of its openness and its transparency, since the project was 'widely publicised' and as 'all interested undertakings were invited to participate'.[52] In addition, the Commission held that the project had pro-competitive effects, since (1) it would open up formerly inaccessible markets from both sides and (2) it contained enough possibilities for third parties to obtain, through negotiation, access to the Interconnector's transmission capacity. In sum, the Commission appeared to take into account the financial needs of the project, and therefore did not require that access must be provided *per se*.[53] As shall be seen below in chapter 7, the same line of reasoning is also used by the National Regulatory Authorities when reviewing agreements for large new infrastructure projects.

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[48] This paragraph only mentions the most important assessments of Article 81(3) EC by the Commission. Cases not mentioned in the main text (since they do not seem to be of particular relevance) include the long-term supply contracts in the electricity sector in *Pego* (OJ 1993, C 265/3) and *Scottish nuclear* (Commission decision 91/329, OJ 1991, L 178/31); and the exclusive supply provisions that were reviewed in e.g. the *Shotton* (OJ 1990, C 106/3) and *Industrial gases* cases (See European Commission, *XIXth report on competition policy*). However, one may question to what extent these decisions can be transposed to the gas sector. Especially with regard to facilities where the relevant sunk costs have already been covered over the years, it is unlikely that the Commission would apply similar exemptions. See Cross, Hancher & Slot in: Roggenkamp *et al*. 2001, *supra* note 22, p. 257.

[49] Cross, Hancher & Slot in: Roggenkamp *et al*. 2001, *supra* note 22, p. 257.

[50] European Commission, *XXVth Report on Competition Policy* (part II), p. 125-126.

[51] Ashe-Taylor & Moussis 2004/2005, *supra* note 11, p. 106.

[52] See e.g. Cross, Hancher & Slot in: Roggenkamp *et al*. 2001, *supra* note 22, p. 258.

[53] *Ibid*.

The Commission also seemed relatively lenient in the *Viking Cable* case. This project concerned a sub-sea cable between Norway and Germany for the transmission of high-voltage electricity. Although the relevant agreement included a 25-year exclusivity period, it was not deemed to be contrary to Article 81 (or 82) EC. According to the Commission, the long-term arrangements were 'indispensable' to secure the viability of the project.[54]

For its part, the ECJ appears to have put forward a somewhat more stringent approach vis-à-vis access issues. In the *Almelo* ruling,[55] the ECJ considered that exclusive supply and purchase agreements concluded between local and regional suppliers of electricity were not compatible with Articles 81 and 82 EC. As the agreements were not notified to the Commission, Article 81(3) could not be applied. However, the ECJ did consider that, in principle, Article 86(2) EC could be applicable. The ECJ held that:

> 'Restrictions on competition from other economic operators must be allowed in so far as they are necessary in order to enable the undertaking entrusted with such a task of general interest to perform it. In that regard, it is necessary to take into consideration the economic conditions in which the undertaking operates, in particular the costs which it has to bear and the legislation, particularly concerning the environment, to which it is subject'.[56]

The ECJ thus considered that it is up to the national courts to assess whether the exemption is justified. It is uncertain how this last reference relates to the gas market. Gas distribution companies, like in the electricity companies in *Almelo*, are under the obligation to ensure reliable and cheap supplies. It could thus be questioned to what extent long-term gas supply contracts can be justified by referring to the requirements of public interest imposed on undertakings.[57]

It seems from the cases examined above that the Commission is not all too strict in its review vis-à-vis agreements that enlarge the capacity and the interconnection of gas infrastructures. Also, the Commission favours agreements between parties that appear to be willing to comply with rules that facilitate Third Party Access.

In sum, Article 81 EC can provide a workable scope of review to determine whether or not certain conduct in the energy sector is permissible.

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[54] See the notice pursuant to Article 19(3) of Regulation 17 concerning case COMP/E-3/37.921 (*Viking Cable*), OJ 2001, C 247/11.
[55] Case C-393/92, *Gemeente Almelo and others* v. *Energiebedrijf IJsselmij*, [1994] ECR I-1477.
[56] *Almelo* Case, *supra* note 55, par. 49.
[57] See Cross, Hancher & Slot in: Roggenkamp *et al*. 2001, *supra* note 22, p. 257.

3.3 Article 82 EC & the 'essential facilities doctrine'

Since the gas sector is network bound, incumbent gas network owners and operators which exercise control over their infrastructures will normally have a 'dominant position', triggering the application of Article 82 EC.[58]

Within this thesis I shall concentrate on the 'essential facilities doctrine' (EFD) arising from Article 82 EC.[59] If the conditions of this doctrine are fulfilled, it may compel an owner or an operator to allow a third party to have access to its 'facility'.[60] The EFD will only apply if such access is indeed indispensable to compete in the relevant network industry.[61] The EFD was first adopted by various courts of lower instance from the United States.[62] In *Aspen Skiing*,[63] the U.S. Supreme Court appeared to endorse this doctrine. It held that, under certain circumstances, a refusal to cooperate with rivals may amount to anticompetitive behaviour and hence violate the Sherman Act.[64] Lately, however, the U.S. Supreme Court appears reluctant to uphold the EFD,[65, 66] and only does so in exceptional circumstances.[67] This was shown in the recent *Verizon* judgment.[68] The U.S. Supreme Court stressed that it had never endorsed the EFD as such, a 'doctrine crafted by some lower courts'. Moreover, it held that there is 'no need either to recognize it or to repudiate it here'.[69]

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[58] Obviously, this is caused by the economic inefficiency to construct an alternative network, establishing the potential competitor's dependence on the incumbent.

[59] For a thorough – although somewhat outdated – examination of the EFD, see Temple Lang, 'Defining legitimate competition: companies' duties to supply competitors and access to essential facilities', *Fordham International Law Journal* 1994/1995, p. 439-500. Also see Cross, Hancher & Slot in: Roggenkamp *et al*. 2001, *supra* note 22, p. 259 *et seq*.

[60] Such a facility can consist of many things, such as 'harbours, ports for shipping lines, computer reservation systems for airlines, and high voltage electricity transmission lines and gas transmission pipelines for energy companies', as described by Slot & Johnston, *An Introduction to Competition Law*, Hart Publishing: Oxford and Portland (Oregon) 2006, p. 128-129.

[61] Ashe-Taylor & Moussis 2004/2005, *supra* note 11, p. 110.

[62] See also Areeda, 'Essential facilities: an epithet in need of limiting principles', *Antitrust Law Journal* 1989, p. 841 *et seq*.

[63] U.S. Supreme Court, *Aspen Skiing Co.* v. *Aspen Highlands Skiing Corp*., 472 U.S. 585, 601 (1985). An earlier case with a similar background was *Otter Tail Power Co.* v. *United States*, 410 U.S. 366 (1973).

[64] See §2 of the Sherman Antitrust Act, 26 Stat. 209, 15 U.S.C.

[65] Several cases already indicated that the EFD would only be upheld in exceptional circumstance. This stance values the freedom for businesses to act as they wish. See e.g. the U.S. Supreme Court's ruling in *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919). In *Verizon* (*infra* note 68) there is another indication: '*Aspen Skiing* is at or near the outer boundary of §2 [the provision of the Sherman Act prohibiting anti-competitive behaviour, TvdV] liability'.

[66] In the *Verizon* ruling (*infra* note 68), the U.S. Supreme Court explained why it had difficulty with upholding the essential facilities doctrine. It held that '(c)ompelling (…) firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since *it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities* [italics added, TvdV]'.

[67] See *Verizon* (*infra* note 68), in which the U.S. Supreme Court states that: '(w)e have been very cautious in recognizing such exceptions'.

[68] U.S. Supreme Court, *Verizon Communications Inc.* v. *Law Offices of Curtis v. Trinko, LLP*, 540 U.S. 398 (2004).

[69] The U.S. Supreme Court summarises it stance by the phrase: 'where access exists, the [essential facilities] doctrine serves no purpose'.

Under Community law, the EFD seems to have found a higher level of acceptance. There have been several cases in which the ECJ held that a refusal to provide access to a certain facility is contrary to Article 82 EC.[70, 71] In any case, the facility in question must be truly essential to enter the downstream market. A refusal to grant access hereto would thus not only be incapable of being objectively justified, but would also entail a risk that all competition shall be eliminated. An additional requirement is that the third party is not able or cannot reasonably be expected to replicate the facility in question.[72]

One of the leading cases covering the EFD is *IMS Health*.[73] In this case, the ECJ stressed that a refusal to grant access (*in casu*: to an IP right) can only be abusive if the undertaking seeking the use of the relevant facility[74] has the intention of introducing a new product or service that is not (yet) offered by the incumbent.[75] It is uncertain to what extent this particular criterion can be transposed to network facilities in general and the gas sector in particular.[76] One may reason that the supply of a new product possible; namely by differentiating in the quality and the features of the supplied gas. This would refer mainly to the gas' calorific value (being either high or low). However, in practice it is not easy to supply gas with another calorific value than the one already in use in that particular Member State. As to the high-pressure long-distance gas pipes, no two sorts of gas can be supplied at the same time. Also, new infrastructures usually have to be connected to existing ones, since few new projects directly connect producers with consumers. The new infrastructure's construction must hence follow the design of the existing one, in order to process gas having the same features. Therefore, third parties can hardly be expected to introduce

[70] See e.g. *infra* note 72. See e.g. Nyssens and Schnichels in: Faull & Nikpay, *The EC law of competition*, OUP: Oxford 2007, p. 1457-1458 and Whish, *Competition Law*, LexisNexis Butterworths: London 2003, p. 675. See also Commission's *XXIIIrd Report on Competition Policy* (1993), p. 669.

[71] Apart from the ECJ, the Commission has also put forward its views on the EFD. It considers this principle to apply to facilities 'without access to which competitors cannot provide services to their customers'. See Commission decision, *Sea Containers/Stena Sealink*, OJ 1994, L 15/8.

[72] See e.g. Joined Cases 6/73 and 7/73, *Commercial Solvents* v. *Commission*, [1974] ECR 223; Case 27/76, *United Brands Co.* v. *Commission*, [1978] ECR 207; Case 238/87, *Volvo AB* v. *Erik Veng (UK) Ltd.*, [1988] ECR 6211; Joined Cases C-241/91 P and C-242/91 P, *RTE and ITP* v. *Commission*, [1995] ECR I-743 ('Magill'); Case C-7/97, *Oscar Bronner GmbH & Co KG* v. *Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co KG*, [1998] ECR I-7791. See also the Opinion of Advocate General Jacobs in *Bronner* of 28 May 1998. He suggested limiting the EFD's field of application to situations in which the dominant undertaking has 'a genuine stranglehold' on the downstream or related market. In his view, two (necessary, but not sufficient) conditions are that (1) the owner of the facility must be the only source of access to the facility, and (2) the facility must present the only means to compete on the downstream or related market. See par. 65-68 of the Opinion.

[73] Case C-418/01, *IMS Health GmbH & Co OHG* v. *NDC Health GmbH & Co KG*, [2004] ECR I-5039. For a broad examination of the issues raised by this ruling – as well as similar ones –, see Geradin, 'Limiting the scope of Article 82 EC: what can the EU learn from the U.S. Supreme Court's judgment in *Trinko* in the wake of *Microsoft*, *IMS* and *Deutsche Telekom*?', *CMLRev* 2004, p. 1519-1553.

[74] The relevant facility in the *IMS Health* case was a copyright.

[75] Although the ECJ underlined that there must also be 'potential consumer demand' (see par. 38, 49 & 52) for such a product or service, this criterion seems to have little substance in itself. Obviously, any undertaking acting in an economically rational way would not offer a product or service for which there was (at least in their view) not even *potential* consumer demand.

[76] See Slot & Johnston 2006, *supra* note 60, p. 128-129.

new services or goods *via* existing gas pipelines.[77] Coming back to the criterion of *IMS Health*, a refusal to provide access might not be abusive if the wording of this judgment interpreted *stricto sensu*.

Nevertheless, *IMS Health* may not be of particular relevance to the gas sector, since the applicable regulatory regimes are different from one another. In the context of *IMS Health*, there were no sector-specific rules enabling access. It could be argued that that was the primary reason why the ECJ used general competition rules to provide *ex post* TPA. This situation is to be distinguished from the gas sector, in which there *is* sector-specific legislation that enables *ex ante* TPA.[78]

The ECJ's case-law does not provide guidance on how the EFD relates to the gas sector. In any case, the Commission does make it clear that it believes that gas pipelines are capable of constituting 'essential facilities'.[79] If this stance is accepted by the ECJ, the EFD could significantly strengthen access by third parties.

3.4 Conclusion

The general competition rules can support the liberalisation of the energy markets. In particular, they can stimulate competition, for instance by allowing agreements that lead to better cross-border networks, or by opposing conduct that blocks access to essential facilities. These rules could thus function as a way to facilitate access for third parties.

However, the general competition rules cannot be understood as an overall panacea to establish a well-functioning access regime.[80] First, since the introduction of Regulation 1/2003 the Commission, as a rule, no longer makes *ex ante* competition law conformity checks.[81] Indeed, Article 10 of Regulation 1/2003 enables the Commission to decide that, 'where the Community public interest (…) so requires', Article 81 EC is not applicable to an agreement. The Commission is not obliged to give such *ex ante* decisions. Although it is true that many undertakings themselves perform competition law conformity checks, this does not give certainty that the agreement in question is indeed in line with competition rules.

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[77] This is arguably different in the electricity sector. In the electricity market, one could think of consumer demand which has been generated in an alternative (environmental friendly) way. Certain quantities of such 'green' power can be put on the network depending on individual consumer demand. In the gas sector, however, it is much harder to differentiate between various ways of production.

[78] Namely, the first and second gas Directives (see par. 4.2 & 4.3 below). See also Regulation 1775/2005 (par. 6.3 below).

[79] See Commission's *XXIIIrd Report on Competition Policy* (1993), p. 141-143 on the *Disma* case. See also Whish 2003, *supra* note 70, p. 675.

[80] This is also indicated by the second gas Directive's preamble. Recital 2 stipulates that 'significant shortcomings and possibilities for improving the functioning of the market remain' inspite of the applicability of the general competition rules on e.g. long-term contracts (recital 25).

[81] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, OJ 2003, L 1.

This is problematic, since the gas sector sometimes needs *ex ante* assurances that certain conduct will be compatible with competition law, especially if an undertaking wishes to set up a costly new infrastructure.

Second, it could be questioned if the general competition rules can sufficiently take into account the gas sector's many particularities (see par. 2.4 above). More specifically, these rules are not designed to make a sufficiently balanced enough approach in individual cases, where e.g. the advantages of exclusive agreements must be outweighed vis-à-vis the importance of access for potential competitors.

Apart from the Treaty provisions on competition, the merger regulation may also be relevant.[83] Indeed, this regulation does not always apply since mergers in the energy sector often do not satisfy the '2/3-rule'.[84] However, the *Gas Natural – Endesa* case[85] shows that the Commission is sometimes able to use the merger regulation to impose conditions, also relating to access issues.[86] This is especially the case if such application supports the principle of non-discrimination.[87]

Since the general competition rules did not fully succeed in opening up the European energy market, the Community legislator laid down sector-specific rules, which included various provisions on access issues. These shall be discussed in the next chapter.

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[83] Regulation 139/2004/EC of the Council of 20 January 2004 on the control of concentrations between undertakings [2004] OJ L 24/1.

[84] The 2/3 rule can be found in Article 1(2) of the merger regulation:
'A concentration has a Community dimension where:
(a) the combined aggregate worldwide turnover of all the undertakings concerned is more than EUR 5000 million; and
(b) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 250 million,
unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State [italics added, TvdV]'.

[85] *XXIIth Report on Competition Policy* (2000), p. 154..

[86] For more general reading on merger policy in the energy market, see Nyssens & Schnichels in: Faull & Nikpay 2007, *supra* note 70, p. 1464-1473.

[87] Nyssens & Schnichels in: Faull & Nikpay 2007, *supra* note 70, p. 1456.

4. THE SECTOR SPECIFIC RULES

4.1 Introduction

As seen in the previous chapter, the general competition rules could strengthen the internal gas market.[88] In some instances, they can provide access for third parties. However, as was concluded in par. 3.4, these rules are not capable, on their own, of establishing a fully competitive European gas market.

Therefore, sector-specific rules were set up in order to complement the general competition rules. These rules were considered more appropriate to take into account the characteristics of this sector and to make a more balanced appraisal between all the relevant interests at stake.[89] In particular, the sector-specific rules aim at striking a fair balance between enhancing competition, protecting the security of supply and stimulating investments in new infrastructures.[90]

4.2 The first gas Directive

4.2.1 Introduction

The Community Institutions adopted Directive 98/30[91] to assist the phased opening of the European gas markets to competition.[92] The objective of Directive 98/30 (hereinafter: 'the first gas Directive') was to develop 'a truly competitive, European wide gas market, based on the highest standards of security of supply and consumer protection'.[93]

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[88] For the main *rationale* behind strengthening the internal gas market, see e.g. *The Economist*, 14 April 2007: '(…) [gas] importing countries would face less risk if they fostered an integrated market'.

[89] See e.g. Lapuerta & Moselle (1998/1999, *supra* note 12, p. 475). These authors argue that three major reforms need to be implemented in the energy sector. First, they are in favour of vertically unbundling the former incumbents. Second, they argue access prices need to be regulated directly and need to be based on the actual costs incurred. This would hopefully stop incumbents from charging monopoly prices. Third, they put forward coverage of stranded costs through the use of fees which are explicitly dedicated to that purpose. In their opinion, this would lead to 'proper compensation in an efficient, non-discriminatory and transparent manner'.

[90] This is mentioned particularly in recitals 1, 2, 8, 25, 30, 31 & 32 of the first gas Directive's preamble (*infra* note 91).

[91] Directive 98/30/EC of the European Parliament and of the Council of 22 June 1998 concerning common rules for the internal market in natural gas, OJ 1998, L 204/41.

[92] It was not the first Community Directive aiming to facilitate the internal energy market. See e.g. Directive 91/296/EEC of 31 May 1991 on the transit of natural gas through grids (OJ 1991, L 1474/37) and Directive 90/377/EEC of 29 June 1990 concerning a Community procedure to improve the transparency of gas and electricity prices charged to industrial end-users (OJ 1990, L 185/16). See also Directive 94/22/EC of the European Parliament and of the Council of 30 May 1994 on the conditions for granting and using authorizations for the prospection, exploration and production of hydrocarbons, OJ 1994, L 164/3.

[93] See the speech by Energy Commissioner Piebalgs, 'The EU gas market developments – the Case of the Baltic Sea region countries', speech given in Vilnius on 8 May 2006.

4.2.2 Security of supply

The first gas Directive regards the security of supply as a key objective of gas policy.[94] Indeed, the first gas Directive accepts that sometimes the security to supply can only be guaranteed by imposing public service obligations.[95] In effect, this objective is thus capable of taking precedence over competition interests.[96] This applies in particular if 'in their [the Member States'] view, free competition, left to itself cannot necessarily guarantee' the security of supply.[97]

4.2.3 The Third Party Access regime of the first gas Directive[98]

Apart from the security of supply, the first gas Directive also attempts to improve access for third parties. Recitals 21 and 23 of the first gas Directive's preamble stress the need for an effective access regime. Article 14 of the first gas Directive states that Member States must set up a regime that enables TPA.[99]

The first gas Directive allows the Member States to choose between two different access regimes, being alternatively based on either 'regulated' or 'negotiated' TPA.[100, 101] Regulated access means that the State sets the applicable prices and conditions under which new competitors can obtain access.[102] Within this regime, Article 16 determines that Member States should give a 'right to access' to the system on the basis of published tariffs, terms and obligations.

Under negotiated access, (potential) new competitors must enter into negotiations with the network owners or operators to determine the conditions under which access is provided. Article 15(1) makes clear that Member States must establish a framework in which effective access can take place. Otherwise, negotiations to this end would remain fruitless. In addition, Article 15(2) states that natural gas undertakings must publish their commercial condition for the use of the system.

Irrespective of the method used, the applicable procedures must at least be objective, transparent and non-discriminatory.[103] Most Member States choose regulated TPA as the cornerstone of their access regime.[104]

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[94] The 'security of supply' is mentioned in Recital 12, Articles 3(2) and 25(3)(b) of the first gas Directive.
[95] See in particular Recital 12 of the first gas Directive.
[96] *Ibid.*
[97] *Ibid*.
[98] The first gas Directive entered into force in August 1998, and had to be implemented before August 2000.
[99] See Article 14 of the first gas Directive. For a short examination, see Lapuerta & Moselle 1998/1999, *supra* note 12, p. 459.
[100] Article 15 of the first gas Directive deals with negotiated access, while Article 16 of the Directive is concerned with regulated access.
[101] A similar approach was used with regard to the electricity sector, see Palasthy 2002, *supra* note 14, p. 4.
[102] Lapuerta & Moselle 1998/1999, *supra* note 12, p. 455.
[103] Article 14 of the first gas Directive.
[104] Germany was the only exception, having opted for negotiated TPA.

4.2.4 Derogations from TPA under the first gas Directive

Article 17 of the first gas Directive provides various possibilities to derogate from the principle of TPA.[105] The most important of these include a lack of agreement between parties,[106] a lack of capacity[107, 108] and a lack of customer eligibility.[109] Moreover, TPA may be derogated from if this is necessary for the performance of public service obligations imposed by Member States.[110] Also, Member States may temporarily suspend TPA as a way to compensate utilities for having incurred 'stranded costs'.[111]

4.2.5 The problems after initial liberalisation

Several problems surfaced after the adoption of the first gas Directive. First, there were vast differences in the pace of national implementation. Second, many actors, particularly new entrants, argued that access to infrastructures was still subject to discriminatory conditions.[112] Third, many authors were of the view that the incumbent gas companies still had a great deal of market power. This rendered third parties unable to compete effectively.[113]

The common denominator of these complaints is that the harmonization measures in the first gas Directive were not always effective. The Member States could still protect national incumbents from market forces.[114] In addition, the regime of negotiated TPA, as such, did not prove to be a success.[115, 116] Other access-related problems resulted from ill-defined tariffs, an insufficient degree of system inter-operability and non-transparent rules.[117]

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[105] For the derogations from TPA which were enabled by the first electricity Directive, see Palasthy 2002, *supra* note 14, p. 10-16.

[106] This is important to ensure the freedom of contract. However, the parties must obviously have made reasonable efforts to come to an agreement. In any case, the conditions sought by the access applicant may not be objectively unfair or unjustified.

[107] This issue is all the more pressing with regard to the use of cross-border interconnectors. These facilities, linking national pipelines to one another, are vital to achieve cross-border competition, but may also end up as bottlenecks due to the fact they usually have a very limited capacity.

[108] Again, similar provisions exist in the context of the electricity sector, see e.g. Palasthy 2002, *supra* note 14, p. 12.

[109] The Directive limits the benefits of TPA rules expressly to 'eligible customers'. These are customers which have the legal capacity to contract for, or to be sold, natural gas in accordance with Articles 15 and 16 of the first gas Directive; see Article 18(1) of the first gas Directive.

[110] Article 17 of the first gas Directive.

[111] This follows from Article 9(2) of the first gas Directive.

[112] This discrimination predominantly relates to the new entrants' believe that the domestic rules in place *de facto* favoured incumbent undertakings. See e.g. the Commission Report, *supra* note 28, p. 7-8. The Report stresses that such discriminatory tendencies are indeed still present today. See also recital 2 of the second gas Directive, which states the 'significant shortcomings' as regards the transmission and distribution tariffs' non-discriminatory nature.

[113] See Cameron 2005, *supra* note 15, p. 9.

[114] See e.g. Cameron 2005, *supra* note 15, p. 9 & 12-13.

[115] Germany's reliance on *ex post* action by competition authorities, instead of the creation of an *ex ante* regulatory framework, was subject to much criticism, see *ibid*.

[116] This failure by negotiated TPA is not in line with the theories put forward by 'Chicago School' of economists. They *do* support such a TPA regime, since this would still uphold incentives for incumbents to offer access on conditions that promote efficient entry. See Lapuerta & Moselle 1998/1999, *supra* note 12, p. 455, 460-463. However, the rejection of negotiated TPA (in the second gas Directive) *is* in line with the negative experiences in the United Kingdom, where such a regime failed. See *ibid*., p. 463-467.

[117] Cameron 2005, *supra* note 15, p. 9.

Another difficulty arising from the wide Member State discretion was that, although a level playing field was envisaged,[118] suppliers in some countries were immediately subject to competition (such as in the UK and Finland), while undertakings in other countries could (at least partially) still benefit from regulatory 'protection' (such as in France).[119] This gave a noteworthy competitive advantage to the undertakings in Member States which did not fully liberalise their energy markets. For instance, they were able to carry out cross-border take-over bids whilst being protected from market forces themselves. For example, French utility Electricité de France (EDF) went on a buying spree in the UK, making it the fourth-biggest electricity supplier in that country. The same strategy was successfully used by a few other 'protected incumbents'. According to *The Economist*, '(o)bservers of the European [electricity] market believe, gloomily, that it may ultimately come to be *dominated by three large*, *well-entrenched national champions*: EDF, and the two German companies, RWE and E.ON [italics added, TvdV]'.[120] In the gas sector, Gaz de France (GDF) intended to spend EUR 17.5 billion mostly on buying gas-distribution companies in Europe.[121]

Thus, although the first gas Directive did have some beneficial effects, it failed to fully establish a well-functioning European gas market. One could argue that the rules had the effect of setting up as many liberalised markets[122] as there were Member States.[123]

4.3 The second gas Directive

4.3.1 Introduction

In order to tackle the aforementioned difficulties surrounding the first gas Directive, the Community legislator adopted Directive 2003/55 (hereinafter: 'the second gas Directive' or 'the Directive'), repealing the first gas Directive.[124] The second gas Directive, much like the first gas Directive, attempts to set up a European gas market.[125] It wants to accelerate and align the liberalisation efforts in the various Member States.[126, 127] The second gas Directive envisages non-discriminatory access

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[118] See recital 23 of the first gas Directive.
[119] Albers 2005, *supra* note 42, p. 49.
[120] *The Economist* 9 July 2005, 'In name only?', p. 54.
[121] *The Economist* (*ibid*.), p. 56.
[122] Although the level of liberalisation actually achieved varied considerably from one Member State to the other, I refer to all of them as 'liberalised markets'.
[123] Cameron (2005, *supra* note 15, p. 9) refers to it as a 'patchwork' of several markets.
[124] 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 repealing Directive 98/30/EC (OJ 2003, L 176/57). Although recital 1 of this document mentions the first gas Directive's 'significant contributions' to the development of the EC gas market, recital 2 acknowledges the 'significant shortcomings' of the system in place and stresses the possibilities for improvement.
[125] See the speech by Energy Commissioner Piebalgs, *supra* note 89.
[126] Ashe-Taylor 2004/2005, *supra* note 11, p. 105.
[127] In fact, the main objectives and means to achieve these goals are very similar to the ones used in the first gas Directive. The second gas Directive aims at the creation of an internal energy market via efficiency gains, lowering prices, improving the level of services and increasing competitiveness. The means are the opening up of domestic markets, the unbundling of uncompetitive activities

to gas infrastructures. The Member States were required to implement most substantive provisions of the Directive before 1 July 2004, with full market opening due on 1 July 2007.[128]

Under the Directive, Member States are required to set up specialised 'National Regulatory Authorities' (NRA's). These must protect effective competition and a non-discriminatory TPA regime.[129] The Directive empowers the NRA's with, *inter alia*, the ability to manage the level of tariffs and to determine the conditions under which access takes place.[130]

The second gas Directive has two major thrusts. First, it attempts to strengthen efforts to unbundle former incumbents.[131] Second, it aims at improving TPA, relying mostly on the establishment of a regulatory framework rather than negotiation between parties. From this choice, it can be inferred that the Community legislator favoured the regime of regulated TPA.[132]

Notwithstanding its focus on free access, the second gas Directive appears quite lenient to long-term (exclusive) contracts. Such agreements 'will continue to be an important part of the gas supply' within the EC and 'should be maintained as an option' for the relevant undertakings in so far as these do not infringe the rules laid down by the Directive and the Treaty.[133] More specifically, Article 18(3) stipulates that the Directive shall not encroach upon 'the conclusion of long-term contracts', as long as these comply with the general competition rules.

4.3.2 Security of supply

Article 3 of the second gas Directive states that the security of supply is of major importance. Member States must continuously monitor if it is attained in practice.[134] Unlike the first gas Directive, however, it does not clearly state that the security of supply should in principle prevail over competition interests.[135] Perhaps this is an indication that TPA is somewhat more on the forefront than in the first gas Directive. It seems that the balance between these TPA and the security of supply is more delicate than before, and that only a case-by-case analysis can determine which interest must prevail.

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from (potentially) competitive ones and the introduction of third party access. See e.g. Spanjer 2006, *supra* note 29.

[128] Article 31 of the second gas Directive.

[129] Recital 21 of the second gas Directive

[130] Cameron 2005, *supra* note 15, p. 11.

[131] For the unbundling of transmission system operators, see Article 9 of the second gas Directive. For the unbundling of distribution system operators, see Article 13 of the second gas Directive.

[132] Apart from that, it must be noted that the choice for regulated TPA was, in itself, not all too surprising. Most Member States had hitherto worked with a system of regulated TPA, which they deemed necessary to lower the market power enjoyed by vertically integrated incumbents.

[133] See recital 25 of the second gas Directive.

[134] Article 5 of the second gas Directive.

[135] See recital 21 of the second gas Directive.

4.3.3 Cross-border networks[136]

The second gas Directive, unlike the first gas Directive, pays ample attention to cross-border networks.[137] The second gas Directive aims for the open access to gas interconnectors. This is likely to lead to more competitive markets, where supply and demand could meet on a European level and where allocation of resources takes place in a more efficient way. The Directive may also facilitate substantial economies of scale advantages, as undertakings would – at last – be able to supply throughout the Union. Lastly, it could significantly stimulate competition in countries with (formerly) vertically integrated incumbents which are not (yet) completely unbundled,[138] as these entities will be less able to foreclose market entry due to their decreased market power.

In sum, the second gas Directive's aim to improve cross-border competitiveness will most likely have a significant effect on domestic markets.

4.3.4 The Third Party Access regime of the second gas Directive

Article 18 of the second gas Directive is the core access provision of the second gas Directive. It stipulates that Member States must ensure the implementation of an inclusive and an effective TPA regime. Paragraph 1 of the provision merits to be cited in full:

> '(m)ember States shall ensure the implementation of a system of third party access to the transmission and distribution system, and LNG facilities based on published tariffs, applicable to all eligible customers, including supply undertakings, and applied objectively and without discrimination between system users. Member States shall ensure that these tariffs, or the methodologies underlying their calculation shall be approved prior to their entry into force by a regulatory authority referred to in Article 25(1) and that these tariffs – and the methodologies, where only methodologies are approved – are published prior to their entry into force.'

Article 18(1) of the Directive has a broad scope, applying to all vital gas infrastructures. It facilitates TPA by focusing on objective and non-discriminatory tariffs. The provision aims to increase transparency *via* the disclosure of tariff methodologies. Moreover, it puts forward regulated TPA as the standard regime, laying down that Member States should publish and regulate access tariffs.

The Directive provides for two noteworthy exceptions from the principle of regulated TPA. First, Article 19(1) of the Directive enables Member States to opt for *negotiated* TPA in the case of gas storage facilities.[139] Second, Article 20 of the Directive leaves

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[136] This paragraph has been largely inspired by Albers 2005, *supra* note 42, p. 46.

[137] For the importance of cross-border networks, see par. 2.3 above. See also other legislative documents focused on these issues, see in particular Regulation 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission networks (OJ 2005, L 289).

[138] Albers 2005, *supra* note 42, p. 47.

[139] Article 19(1) of the second gas Directive.

the access regime to upstream pipeline networks largely to the discretion of the Member States.[140]

Apart from these exceptions, the Directive also provides a possibility to request an exemption from TPA for the benefit of new gas infrastructures.[141]

4.3.5 Exemptions to TPA for new gas infrastructures[142]

Article 22 of the Directive provides a possibility for NRA's to grant an exemption from the principle of TPA to 'major new gas infrastructures'. The undertakings involved in such infrastructures are accordingly not required to provide access if – and to the extent that – they have received an exemption. The *rationale* behind this provision is to provide incentives for investors, by allowing them to fully reap the benefits of the new infrastructure project.[143]

According to Article 22(1) of the second gas Directive, an exemption may be granted if the project meets the following conditions:[144, 145]

1. 'the investment must enhance competition in gas supply and enhance security of supply;[146]
2. the level of risk attached to the investment is such that the investment would not take place unless an exemption is granted;[147]
3. the infrastructure is owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that interconnector will be built;
4. charges are levied on users of that infrastructure;

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[140] Article 20 of the second gas Directive.

[141] See also Cameron 2005, *supra* note 15, p. 13.

[142] See Hernández & Gandolfi 2005, 'EU exemptions to TPA for new gas infrastructures' in: *Energy Regulation Insights* (issue 24), NERA Economic Consulting 2005, p. 1.

[143] Even despite the fact that the second gas Directive shows a clear preference towards *regulated* TPA, Article 22 of the Directive shows that traces of *negotiated* TPA can still be found. In fact, this provision reintroduces the possibility to negotiate the exact scope of TPA, be it under strict case-by-case supervision from the NRA's and the European Commission.

[144] See the Interpretation Note of DG Energy & Transport on Directives 2003/54-55 and Regulation 1228/03 in the electricity and gas internal market, 'Exemptions from certain provision of the third party access regime' (30 January 2004), p. 4. See: www.ec.europa.eu/energy/electricity/legislation/doc/notes_for_implementation_2004/exemptions_tpa_en.pdf (last visited 25 September 2007). See also Cameron 2005, *supra* note 15, p. 16.

[145] Hernández & Gandolfi (2005, *supra* note 142, p. 2) argue that these requirements vary considerably *qua* verifiability. In their view, conditions (3) and (4) necessitate the submission of all relevant legal documents by the applicant. In this respect, the latter part of condition (5) seems less challenging, since this can be satisfied by a submission from the relevant entity that it shall work in a transparent and efficient manner with the operator of the connecting system. Conditions (1), (2) and the first part of condition (5) are considerably less well verifiable, as they depend on economic analysis which needs to take into account many unknown variables.

[146] In principle, an exemption should not be awarded to an incumbent which is a dominant market player in the relevant market. See the Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 5.

[147] Also, the principle of proportionality (between the requested exemption and the level of risk) 'plays a decisive role'. See *ibid*.

5. the exemption is not to the detriment of competition or the effective functioning of the internal gas market; or the efficient functioning of the regulated system to which the infrastructure is connected'.[148]

In general, exceptions to principles must be interpreted in a restrictive manner and must accordingly be applied in a meticulous way.[149] The same applies to the possibility to grant exemptions. For further guidance during the assessment of these conditions, the Commission has issued an 'Interpretation Note' to offer guidance with the assessment of these conditions.[150] I shall examine the most important issues discussed in that document.

The first relevant point is obviously what the notion of 'new major infrastructure' actually means. According to the Interpretation Note, it must deal with a new infrastructure or an adjustment that would significantly increase the capacity of the existing infrastructure. Such new infrastructures may only benefit from an exemption if the main financial commitment to construction has been made after 15 July 2003.[151]

In order to assess if a project is 'major', the Commission refers to the costs passed on to the (final) customers. If the latter's bills 'significantly increase', then there is a presumption of high cost. For assistance, the Commission provides a general rule of thumb: if the capital costs of a project would exceed € 10,- per connected customer in total, then the project is to be regarded as a 'major investment'.[152] Still, the Commission admits that this is by no means an ironclad rule. It must therefore be seen in practice how this assessment is carried out.

According to the Interpretation Note, there are two minimum criteria to determine whether or not a project must be considered as 'risky' (see point 2 of the conditions described above).[153] First, the investment must bring along sunk costs since the facility cannot be used for any other purpose than its original one. It seems likely that all gas infrastructures meet this criterion, since these cannot be used for commercial activities other than the supply of gas. This also seems to apply to LNG terminals. Such infrastructures – including mooring docks for LNG vessels and regasification facilities – cannot be easily used for other purposes than processing LNG.[154] Second, the infrastructure's projected benefits should be either relatively low or uncertain. Such a situation may arise when 'alternative competing investments [are] being

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[148] Although the scope of condition (5) is similar to condition (1), the Commission does make a distinction between the two. It views condition (5) as being more narrow than condition (1), as the latter will have regard more to general markets circumstances. Still, the Commission admits that the difference is 'difficult to evaluate' in practice. See *ibid*.

[149] A legal principle provides the general rule. Other considerations may derogate from that rule. A principle provides the main point of reference when reviewing an issue on which that rule is applicable. Since such rules should be applied 'in principle', any exceptions should not be easily accepted. See the Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 1. Although this note offers valuable insights, it must be acknowledged that the document is not legally binding.

[150] See the Interpretation Note by DG TREN of 30 January 2004, *supra* note 144.

[151] I.e. after the publication date of the second gas Directive.

[152] Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 2.

[153] *Ibid*.

[154] As shall also be shown below in chapters 7 & 8.

made'.[155] Apart from that, it seems that gas infrastructures, designed to cater for a fast-moving market but taking many years to build, will inherently suffer from a certain degree of uncertainty. Based on these conditions, therefore, most new infrastructures in the gas sector are likely to be deemed 'risky'.

The Interpretation Note suggests that a sign of 'good will' by the infrastructure developers shall be favourably received. They can do so by offering third parties an opportunity 'to gain access to the new facility at the planning and feasibility stage'.[156] Otherwise, developers should assess the possibilities for TPA for at least a certain percentage of its capacity. Lastly, the scope and duration of the exemption ought to be proportionate to the aim pursued.

All exemptions must be assessed on a case-by-case basis.[157] In addition, exemptions shall not be accepted if these would have the result of creating or reinforcing a dominant position.[158] Also, exemptions may in principle not be granted where it is unlikely that a 'similar competing piece of infrastructure' is to be constructed which would be able to provide a similar service as the proposed infrastructure.[159] Especially this latter condition is noteworthy, as it could have undesirable effects. Within the EU, there are many areas where two large gas infrastructures could not economically viably coincide. The Interpretation Note may thus have the following effect. As no *second* infrastructure is to be set up, the *first* infrastructure would not benefit from a TPA exemption. If this leads to the first infrastructure not being set up at all, this rule could, at least for the areas in question, endanger the very security of supply the Directive aims to protect. Apart from that, the requirement that a 'similar competing piece of infrastructure' should be constructed also appears to be inconsistent with the notion (as explained above) that infrastructures are considered 'risky', and would thus more easily be granted an exemption, if *no* such 'alternative competing investments [are] being made'.[160] It is thus unclear how a competing piece of infrastructure relates to the possibility of receiving an exemption.

Apart from the exemption regime, the Interpretation Note also refers to an alternative:[161] namely the possibility for regulators to adopt specific rules for certain parts of the infrastructure, be they existing or new.[162] Although it would exceed the purposes of this thesis to elaborate on this much further, these solutions could be quite helpful in practice. Nonetheless, such alternatives can also have a harmful effect on the internal market. This effect is likely to occur if many (parts of) infrastructures are

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[155] Other examples include: 'variations in consumption projections, (…) changes in world market conditions for primary fuels or an above average amortisation period for such type of investment'. See the Interpretation Note by DG TREN of 30 January 2004 (*supra* note 144, p. 2).
[156] *Ibid*. The document mentions in particular the possibility of an 'open season' procedure.
[157] The Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 1. The basic premise of the exemption regime is as follows: '(e)xemptions will (…) only be granted *exceptionally* and on a *case-by-case* basis [italics added, TvdV]'.
[158] *Ibid*. See also Cameron 2005, *supra* note 15, p. 16.
[159] The Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 1-2.
[160] *Supra* note 155.
[161] *Ibid*., p. 3.
[162] Of course, such specific legislation must be in line with all other applicable legislation.

subject to different sets of rules, which reduces transparency and thus hampers the establishment of a level playing field.[163]

Lastly, it is important to underline that the decision by domestic authorities to regard new parts of infrastructures differently from the existing ones 'must be clearly justified'.[164] Although the Directive does require the production of certain information,[165] it – as well as the Interpretation Note – does not explain in great detail how thorough the NRA's justification on this point should be. For instance, the Directive and the Interpretation Note do not state if this particular part needs a quantitative analysis comparing the new infrastructures with the existing ones.

4.3.6 The procedure to grant an exemption

If an undertaking wishes to benefit from an exemption, it has to make an application to the NRA.[166] Such an application can either relate to a 'full' or a 'partial' exemption.[167, 168] The NRA will make an assessment and eventually publishes a fully reasoned decision, which is subsequently forwarded to the applicant and the Commission.[169] According to Article 22(4) of the Directive, the Commission may request that the regulatory authority or the Member State concerned amend or withdraw the decision to grant an exemption within two months after receiving a

[163] Obviously, neither the Commission nor the ECJ favours such compartementalisation, which could in effect render nugatory the internal energy market the EC Treaty aims to set up. For the Commission, see e.g. its Energy Sector Inquiry Report (*supra* note 28), in particular par. 44. For the ECJ, see e.g. the *VEMW* judgment (*infra* note 183), par. 62.

[164] See the Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 1.

[165] According to Article 22(4) of the second gas Directive, the following information must be provided:
(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'.
It should be noted, however, that these provisions have not been elaborated upon in much further detail, arguably leaving a great deal of Member State discretion what the provisions actually mean.

[166] Cameron 2005, *supra* note 15, p. 16.

[167] Obviously, a 'full' exemption relates to a situation in which there will be no TPA at all, while a 'partial' exemption only relates to a specific part of the infrastructure. See Articles 18, 19, 20 & 25(2), (3) and (4) of the second gas Directive.

[168] See also the Interpretation Note by DG TREN of 30 January 2004 (*supra* note 144, p. 4).

[169] If an exemption is granted, the NRA should at least provide information as to the following aspects:
1. 'the reasons on the basis of which an exemption is granted;
2. the analysis undertaken to assess the effect on competition;
3. the considerations concerning the time period and the share of the total capacity for which the exemption has been granted;
4. the result the consultation with the Member States or regulatory authorities concerned and
5. the contribution of the infrastructure to the diversification of gas supply'.
See the Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 6. Also compare the requirements laid down in Article 22(4) of the second gas Directive, *supra* note 187.

notification. This two month period may be extended by one additional month where additional information is sought by the Commission.[170] Thus, the exemption decision made by the NRA is directly applicable, unless the Commission chooses to amend or withdraw it.[171]

Notwithstanding the need for the Commission's approval, in practice NRA's still enjoy a high level of discretion in their assessments. For instance, the latter may still draft specified rules for certain types of infrastructures, including the possibility to offer incentives to undertakings in order to develop specific forms of investment.[172]

4.3.7 Reviewing the second gas Directive

The implementation of the second gas Directive into national law has hardly been a smooth process.[173] Since the Commission claims that many deficiencies persist at the domestic level,[174] it decided to launch 34 infringement procedures against 20 Member States for violation and non-transposition of the second electricity and gas Directives.[175] The Commission argues that most NRA's lack sufficient independence, competences and discretion.[176] It aims to tackle this issue along two lines. First, the competences of NRA's need to be widened, by allowing them to decide on *all* relevant issues.[177] Second, decisions taken at the national level should not be contrary to the EC internal gas market.[178] In any case, consistency of the decisions is vital. This

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[170] Article 22(4)(e) of the second gas Directive.

[171] For the procedure on the application of exemptions, see Cameron 2005, *supra* note 15, p. 16.

[172] Cameron 2005, *supra* note 15, p. 17.

[173] Communication from the Commission to the Council and the European Parliament – 'prospects for the internal gas and electricity markets', COM(2006) 841 final, 10 January 2007.

[174] See the Commission communication of 10 January 2007 (*ibid*.), par. 1.3. According to this document, the main deficiencies are the following:
1. '(r)egulated prices preventing entry from new market players;
2. (i)nsufficient unbundling of transmission and distribution system operators which cannot guarantee their independence;
3. *(d)iscriminatory third party access to the network, in particular as regards preferential access being granted to incumbents for historical long contracts*;
4. (i)nsufficient competences of the regulators;
5. (n)o information given by the Commission on public service obligations, especially as regards supply tariffs;
6. (i)nsufficient indication of the origin of electricity, which is essential in particular to the promotion of renewable energy [italics added, TvdV]'.

[175] See par. 9 of the conclusions of the 12th meeting of the Madrid Forum, *infra* note 210.

[176] See the Commission Communication of 10 January 2007, *supra* note 173.

[177] According to the Commission Communication of 10 January 2007 (*supra* note 173, par. 2.2.1), the NRA's need strong *ex ante* powers with regard to the following fields:
1. '*all aspects of third party access to networks*;
2. access to gas storage;
3. balancing mechanisms;
4. market surveillance of e.g. power exchanges;
5. compliance with functional and account unbundling for distribution system operators;
6. *all cross border issues*;
7. consumer protection including any end-user price controls;
8. information gathering;
9. sanctions for non-compliance [italics added, TvdV]'.

[178] See the Commission Communication of 10 January 2007 (*supra* note 173, par 2.2.1).

necessitates thorough coordination between the different NRA's and the Commission.[179]

4.3.8 Conclusion

TPA is a legal principle considered to be imperative to establish an internal gas market. The second gas Directive attempts to improve the effectiveness of TPA, focusing e.g. on regulated tariffs. Nevertheless, there are certain exemptions to this principle. Article 22 of the Directive enables NRA's to exempt 'major new gas infrastructures' from TPA. Such exemptions are sometimes deemed necessary to develop the market and to improve competition in the long run.

In theory, it seems hard to obtain an exemption from TPA. Various documents stress the importance of the TPA principle, and seem to regard any exemption as an *ultimum remedium*. It remains to be seen, however, if this is the practice.

4.4 Conclusion

Apart from the general competition rules, the gas sector is also regulated by sector-specific rules. The first gas Directive failed to achieve a fully liberalised market. The second gas Directive seems to have been more successful in creating a competitive market. This Directive improves access for third parties. It also introduces a balanced system in which access may be denied, for instance if an undertaking has received an exemption under Article 22 of the Directive.

[179] *Ibid*., par 2.2.2.

5. THE RELATIONSHIP BETWEEN THE GENERAL AND THE SECTOR SPECIFIC COMPETITION RULES

5.1 Introduction

This chapter examines the relationship between the general and the sector-specific competition rules on the gas sector. Since this basically concerns the interaction between primary and secondary Community law, regard must be had to the *Tedeschi*[180] and *Docmorris*[181] cases.

In the *Tedeschi* and *Docmorris* cases, the ECJ held that if a certain area of law provides for total harmonisation, one should have regard only to the rules laid down in the relevant Directive instead of the EC Treaty. Thus, e.g. when dealing with access issues, it is important to examine the exact scope of the sector-specific rules (*in casu* the second gas Directive).

5.2 The *VEMW* ruling

5.2.1 Introduction

The *VEMW* judgment is a good example of the interaction between primary and secondary Community law in the energy sector. Therefore, it shall be discussed in detail. This case dealt with the interpretation a non-discrimination clause provided by Article 7(5) of the first electricity Directive.[182] It is important to the issues discussed in this thesis, as it provides an important reference how various interests are valued by the ECJ.[183] Although this case related to the electricity sector, it seems that many of its considerations can be transposed to the gas sector as well.

In *VEMW*, the ECJ was asked to give a preliminary ruling on the lawfulness of preferential treatment of undertakings which had to comply with certain public policy requirements agreed upon *before* liberalisation took place.[184] In this case, the effect of Community principles on long-term electricity supply contracts[185] thus played a key role.[186]

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[180] Case 5/77, *Tedeschi* v. *Denkavit*, [1977] ECR 1555.
[181] Case C-322/01, *Deutscher Apothekerverband eV* v. *0800 DocMorris NV*, [2003] ECR I-14887.
[182] Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity (OJ 1997, L 27).
[183] Case C-17/03, *Vereniging voor Energie, Milieu en Water* v. *Directeur van de Dienst uitvoering en toezicht energie*, [2005] ECR I-4983. Also see the Case Note by Hancher in *CMLRev* 2006, p. 1125-1144.
[184] This treatment consisted of the preferential allocation of importation capacity in order to honour long-term electricity supply contracts.
[185] These contracts were concluded in accordance with Article 2 of the Dutch Law on Electricity (*Electriciteitswet*) of 16 November 1989. The agreement with the longest duration *in casu* was concluded for a period of twenty years.
[186] See the Opinion by Advocate General Stix-Hackl of 28 October 2004 in Case C-17/03, par. 4.

5.2.2 Opinion Advocate General

In her Opinion, Advocate General (AG) Stix-Hackl concluded that the agreements *in casu*, although contrary to Articles 81 and 82 EC, were justified under Article 86(2) EC.[187] The AG argued that the secondary Community legislation did not, as such, preclude long-term contracts.[188] More importantly, however, the AG held that the incumbent has been entrusted with services of general economic interest within the meaning of Article 86(2) EC.[189] The AG considered the national legislation in question to be proportionate to the aim of carrying out the long-term contracts.[190, 191] Therefore, the AG concluded that the preferential treatment did not contravene the principle of non-discrimination.

Hence, the preferential treatment could be justified in principle.[192] The AG argued that the national court should assess whether the relevant conduct is proportional. However, since the agreements were justified on the basis of Article 86(2) EC, she deemed the non-discrimination principle (as can also be found in Article 7(5) of the first electricity Directive) not to be breached.

5.2.3 European Court of Justice

The ECJ adopted a different approach than the AG. Its ruling suggests that the preferential treatment of incumbents by Member States is not to be accepted due to its discriminatory effects.[193] The ECJ stated that, in practice, competition in the Netherlands *only* operates 'by way of electricity generated outside that Member State'.[194]

The ECJ relied heavily on Article 24 of the first electricity Directive. This provision enabled the Commission to allow a temporary derogation from certain (access) provisions therein, but did not clarify the relationship with the general competition rules. The ECJ stated that Article 24 provided the *only* derogation possibility.[195] The Netherlands did not make use of this possibility. Thus, the assessment on the non-discrimination principle's application should be made *in full* relating to the *entire* network system.

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[187] *Ibid*., par. 46-47.
[188] *Ibid*., par. 63.
[189] The AG refers to Case C-157/94, *Commission* v. *The Netherlands*, [1997] ECR I-5699, par. 32, in which the ECJ decided that the incumbent did perform such services. See par. 74-75 of the Opinion.
[190] In effect, it must be reviewed if rules could be envisaged with a less harmful effect on the claimants. See par. 80 of the AG's Opinion (*supra* note 186).
[191] The AG also refers to the justifiability of the preferential treatment under review. She underlines the requirement that the allocation of importation capacity should not exceed the quantities used in the long-term agreements, see par. 86 of the Opinion. Moreover, the AG stresses that any preferential treatment should be subject to a time-limit in line with the long-term contract in question (par. 88 of the Opinion). Lastly, the level of charges applied to the incumbent may also be relevant (par. 89 of the Opinion).
[192] See Hancher 2006, *supra* note 183, p. 1128-1129.
[193] *VEMW* Case (*supra* note 183), par. 45 *et seq*. The ECJ refers, *inter alia*, to case C-280/93, *Germany* v. *Council*, [1994] ECR I-4973, par. 67. According to the ECJ, the principle of non-discrimination requires that comparable situations are not treated in a different way, except when such a difference in treatment is objectively justified.
[194] *VEMW* Case, *supra* note 183, par. 49.
[195] The Netherlands did not make use of this derogation possibility.

The strict application of the non-discrimination principle means that no regard may be had to the undertaking's specific rights and obligations (such as the obligation to provide cheap energy, see *Almelo*, par. 3.2). According to the ECJ, any other approach would endanger a smooth changeover from a 'monopolistic and compartmentalised' market to an 'open and competitive' one.[196] In the ECJ's view, open access to the network in issue is vital.[197] The preferential treatment under review could therefore not be justified.[198]

5.2.4 Comment

In *VEMW*, the ECJ implicitly held that the first electricity Directive provided for total harmonisation. It could be doubted whether that that was indeed the case. The first energy Directives were unclear on the degree of harmonisation, especially as regards transmission, distribution system operation, the rules applying to transport and the allocation of available capacity on international interconnectors.[199] Even so, the ECJ followed the *Tedeschi* approach. Since the ECJ assumed that there was total harmonisation, it was not possible to examine the potential application of Article 86(2) as the only possible derogations were determined by the first gas Directive itself.

The ECJ upholds a very strict interpretation of the principle of non-discrimination.[200] Thus only technical (not being contractual) capacity limits can justify a refusal to provide access. According to Hancher, 'the situation for gas may (…) be different as Article 18(3) on TPA expressly allows for the conclusion of long-term contracts insofar as they comply with competition rules'.[201]

It is unclear how the ECJ's approach relates to the 'second' energy Directives. In the second electricity Directive, TPA is dealt with only by Article 20. Article 3(8) of the second electricity Directive contains an exhaustive list of the objectives which can constitute 'public service obligations' and which could thus justify a refusal to provide access. Recourse to Article 86(2) EC is no longer possible. In any case, the wording and the purpose of Article 3(8) of the second electricity Directive suggests that it cannot derogate on the non-discrimination principle as stipulated Article 9 of the Directive.

The interpretation notice of the Commission notes that the *VEMW* ruling is applicable 'in substance and in spirit' to the gas sector.[202] According to Hancher, 'this rather opaque statement fails to cast much light on the complex framework for ascertaining the legality of "legacy" contracts in the sector as opposed to State measures reserving capacity for their continued execution'.[203] This holds particularly true since the

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[196] *VEMW* Case (*ibid*.), par. 62.
[197] *Ibid*., par. 63.
[198] *Ibid*., par. 66.
[199] Hancher 2006, *supra* note 183, p. 1137.
[200] *Ibid*., p. 1138.
[201] *Ibid*., p. 1140.
[202] SEC(2006), 26 April 2006.
[203] Hancher 2006, *supra* note 183, p. 1143.

second gas Directive leaves more possibilities for the continued validity of such contracts than the electricity Directives.[204]

Lastly, it should be noted that the derogation of Article 24 of the first electricity Directive could only be applied for national or public law measures adopted to deal with long term contracts. The provision did *not* apply to the underlying private law contracts. Therefore, such agreements must still be assessed under the general competition rules.

5.3 Conclusion

The chapters above illustrate the impact of and the relationship between general competition and sector-specific legislation on TPA issues in the gas sector.

The general competition rules can oppose anti-competitive behaviour if certain conditions (see above in chapter 3) are fulfilled. In those circumstances, they can facilitate access for third parties. Nevertheless, Articles 81 and 82 EC (including the EFD) do not establish a fully effective access regime in the gas sector. An important disadvantage is that since the general competition rules are usually applied by the Commission *ex post facto*, their pro-active effect (apart from self-assessment by the undertakings themselves) is limited. This is even more apparent after the introduction of Regulation 1/2003.[205] As a rule, it is no longer possible to receive an *ex ante* conformity check with Article 81 EC, while there may be a need in the gas sector for such assurances in advance, especially when deciding to invest in a new infrastructure.

Another disadvantage of the general competition rules is that they do not provide a framework in which a genuinely balanced appraisal can take place of all the different interests in the gas sector. The gas market is a particularly complex sector to strike a fair balance between competition and other interests, such as the security of supply. As regards new infrastructures, this can only be done in an effective way *before* the relevant conduct (namely: the investment) takes place, since investors demand certainty that the project will be in conformity with competition rules.

There was hence a need for sector-specific rules. The second gas Directive regulates various key issues. This Directive provides the only relevant scope of review if the subject is within its scope and the rules of the Directive provide for total harmonisation.

Nevertheless, the Treaty provisions may still be relevant. Recital 25 of the second gas Directive suggests that these and the sector-specific rules are both relevant when assessing long-term gas supply contracts. It reads as follows:

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[204] Such as Article 32(1) of the second gas Directive, which acknowledges the continued validity of transit gas contracts concluded in compliance with Directive 91/296 on transit through natural gas grids (OJ 1991, L 147/37).

[205] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, OJ 2003, L 1.

> 'Long-term contracts will continue to be an important part of the gas supply of Member States and should be maintained as an option for gas supply undertakings in so far as they *do not undermine the objectives of this Directive and are compatible with the Treaty*, including competition rules. (…)'

The same applies for public service obligations. Article 3(2) of the second gas Directive stipulates that 'full regard' shall be had to the relevant Treaty provisions.

In sum, general competition and sector-specific rules will have to be jointly applied in order to achieve a free internal gas market. In practice, the sector-specific rules are needed to fine-tune the liberalisation efforts, as only these can bring forward detailed and balanced rules on whether or not to allow access in any given situation.[206]

[206] Slot & Johnston 2006, *supra* note 60, p. 129. They refer to various OFT guidelines: *Concurrent Applications to Regulated Industries* (OFT 405) and *Application in the Energy Sector* (OFT 428). Slot & Johnston also refer to the *Verizon* case (*supra* note 68), '(f)or an intriguing US perspective on these matters'.

6. THE LATEST DEVELOPMENTS

6.1 Introduction

Before turning to the individual exemption orders, it is important to have regard to the most recent developments, since (the decisions on) access issues ought not to disregard the wider framework of the EC gas sector.

6.2 The Madrid Forum

The Madrid Forum,[207] set up in 1999, provides an 'informal framework' in which different organisations involved in the gas sector regularly discuss matters surrounding the internal gas market. Within this setting, TPA is intensely debated.[208] The conclusions of the Madrid Forum provide general guidelines for the entire sector.[209]

At its most recent meeting,[210] held in February 2007, the Madrid Forum underlined 'the need for consolidating rapid progress' after the implementation of the second gas Directive.[211] Also, it stressed the importance to comply with Regulation 1775/2005 (see the following paragraph).[212] The Madrid Forum emphasised the significance of transparency as a way to guarantee non-discriminatory access to gas networks.[213] It held that 'inadequate transparency is detrimental to competition and therefore confidentiality can only be exceptionally used as an argument for less

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[207] In essence, the Madrid Forum 'was set up to discuss issues regarding the creation of a true internal gas market. The participants are national regulatory authorities, Member States, the European Commission, transmission system operators, gas suppliers and traders, consumers, network users, and gas exchanges'. See the website of the Madrid Forum, http://ec.europa.eu/energy/gas/madrid/1_en.htm (last visited 25 September 2007). See also the minutes of the 1st meeting, which took place on 30 September and 1 October 1999, available at: http://ec.europa.eu/energy/gas/madrid/doc_1/minutes_1st_forum.pdf (last visited 25 September 2007).

[208] On the 1st meeting of the Madrid Forum, access issues were the main topic in three of the four sessions. See the minutes of the 1st meeting (*ibid.*), p. 1-3.

[209] Several Madrid Forum conclusions are of particular relevance to Third Party Access. During the 5th, 6th and 7th meeting, 'guidelines for good TPA practice' were on the agenda. The conclusions put great emphasis on tarification issues. The minutes are available on the following websites, which were all last visited on 25 September 2007:
http://ec.europa.eu/energy/gas/madrid/doc-5/conclusions_madrid5.pdf (5th meeting; see in particular Annex II of that document, p. 9-13);
http://ec.europa.eu/energy/gas/madrid/doc-6/conclusionsmadrid6.pdf (6th meeting);
http://ec.europa.eu/energy/gas/madrid/doc-7/00_madrid7_conclusions.pdf (7th meeting; here one can find the revised version of the 'guidelines for good TPA practice', p. 6-18).

[210] See the conclusions of the 12th meeting of the European Gas Regulatory Forum, available at: http://ec.europa.eu/energy/gas/madrid/doc-12/conclusions.pdf (last visited 25 September 2007).

[211] See par. 1 of the conclusions of the 12th meeting of the Madrid Forum (*ibid.*).

[212] Par. 6 of the conclusions of the 12th meeting of the Madrid Forum (*ibid.*). The Forum also referred to the monitoring efforts vis-à-vis Member State compliance to this Regulation, as carried out by the European Regulators' Group for Electricity and Gas (ERGEG).

[213] Par. 11 of the conclusions of the 12th meeting of the Madrid Forum (*ibid.*).

transparency'.[214] The Madrid Forum applauded the adoption of guidelines for good 'open season' practices, which allows undertakings to compete for the initial allocation of network capacity.[215]

In short, the Madrid Forum deals with a large number of practical issues to enhance the functioning of the internal gas market. Its guidelines could *de facto* have a notable impact on the TPA regime in this sector.

6.3 Regulation 1775/2005

In September 2005, the European Parliament and the Council adopted Regulation 1775/2005, primarily dealing with TPA issues with regard to gas networks.[216] This Regulation is meant to complement and support the effectiveness of the second gas Directive. It entered into force on 1 July 2006.

Many provisions of this Regulation are based on the conclusions reached in the context of the Madrid Forum.[217] The Regulation seeks to further harmonise the access regime of intra-Community gas networks, setting out detailed rules to optimize TPA.[218] The Regulation states that such rules, by their very nature, 'cannot be sufficiently achieved by the Member States'.[219] For that reason, the Community is competent to adopt legislation in this field.

The Regulation contains various provisions which aim to support TPA.[220] This includes the application of the 'use it or lose it' (UIOLI) principle.[221] This principle means, in essence, that any capacity not used by the contracting parties must be made available to the market.

Nevertheless, Article 16(b) of the Regulation stipulates that none of its provisions shall apply to new gas infrastructures exempted from TPA under Article 22 of the second gas Directive. In my view, this all-encompassing exception clause is disappointing. Although obviously not all TPA requirements could be applicable after an exemption has been granted, some provisions had been useful to uphold nonetheless. This is particularly true for requirements dealing with transparency, non-

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[214] Par. 15 of the conclusions of the 12th meeting of the Madrid Forum (*ibid*.).
[215] Par. 30-33 of the conclusions of the 12th meeting of the Madrid Forum (*ibid*.).
[216] Regulation (EC) No 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission networks, OJ 2005, L 289/1.
[217] Recital 2 of Regulation 1775/2005 (*ibid*.). See also Ashe-Taylor & Moussis 2004/2005, *supra* note 11, p. 105.
[218] The provision of the Regulation must be read in conjunction with the 'Guidelines on Third Party Access', which can be found in the Annex of the document. These Guidelines can be amended by the Commission and its provisions are therefore very flexible. The Commission has the competence to do so in accordance with Articles 5, 7 and 8 of Decision 1999/468/EC.
[219] See Recital 23 of Regulation 1775/2005 (*supra* note 137).
[220] See Regulation 1775/2005 (*supra* note 137), in particular Article 5 (on the principles of capacity allocation mechanisms and congestion management procedures); Article 6 (transparency requirements); Article 7 (balancing rules and imbalance charges) and Article 8 (trading of capacity rights).
[221] Recital 11 of Regulation 1775/2005, *supra* note 137.

discrimination and the UIOLI principle. Even though the Regulation states that the Madrid forum guidelines will remain applicable to new infrastructures exempted from TPA, these guidelines may not have the desired effect. Soft law may be beneficial, but in areas of particular difficulty (such as the EC gas market), preference must go out to provisions of hard law.

6.4 Commission report on energy sector inquiry

On 10 January 2007, the Commission published the final version of a report based on the energy sector inquiry it had carried out.[222, 223] The report concluded that competition in this sector was far from perfect. Many of the report's findings relate to a lack of (effective) TPA.[224]

The Commission proposed several remedies, many of which – again – focused on TPA. These remedies are based on an integrated and broad approach, making use of all available instruments under competition law.[225]

In this respect, some of the most important remedies consist of the introduction of so-called 'gas release programmes',[226] the opposition of long-term contracts and capacity

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[222] DG Competition Report on Energy Sector Inquiry, SEC(2006) 1724, 10 January 2007.

[223] In tandem with the Report, the Commission submitted the 'Communication from the Commission to the Council and the European Parliament – prospects for the internal gas and electricity markets', COM(2006) 841 final, 10 January 2007.

[224] This holds true for the following issues found by the Commission: the high level of market concentration (which leads to 'little new entry in retail markets', see p. 7 of the Report (*supra* note 28)); the vertical foreclosure (which 'constitutes a major obstacle for new entry', even 'despite the existing unbundling provisions', see p. 7 of the Report. The report mentions more specifically 'the prevalence of long-term supply contracts between gas producers and incumbent importerts', see p. 8 of the report); the high level of market integration (which causes '(i)nsufficient or unavailable cross-border capacity', as well as the situation in which '(n)ew entrants are unable to secure transit capacity on key routes and entry capacity into new markets, see p. 8 of the Report. The findings also mention the fact that the primary capacity on transit infrastructures is controlled by incumbents on the basis of contracts concluded before liberalisation (so-called legacy contracts), which are not subject to current TPA rules; the lack of transparency (which leads to the current 'information asymmetry' between incumbents and their possible competitors, and obstructs third parties to enter a market, see p. 9 of the Commission Report); ineffective price formation (since in several Member States, prices are regulated and set at 'very low levels', which disable new competitors from gaining market access via prices lower than the ones used by the incumbent. In any case, as gas contracts make use of price indices that are based on oil (derivatives), price formation is little dependent on changes in supply and demand. Also, 'restrictions on how customers can dispose of their gas, in combination with restrictive practices regarding delivery point' significantly hinder competition, see p. 10 of the Report and the characteristics of the markets for LNG (since LNG is regarded by the Commission and other regulators as important to promote competition and strengthen the security of supply, several large investments in LNG facilities have benefited from exemptions from TPA obligations. See p. 11 of the Commission Report.

[225] See p. 12 of the Commission Report, *supra* note 28.

[226] 'Gas release programmes' are 'programmes under which incumbents – either as a result of legislation aimed at enforcing the aim of gas market competition or on a voluntary base e.g. as a commitment means to settle a merger or an anti-trust investigation – are required to sell off a part of its contracted suppliers', see http://ec.europa.eu/energy/gas/madrid/doc-5/long-term-contracts-gas-release-22-01-2002-draft.pdf (last visited 25 September 2007). The Commission views such

hoarding,[227] strict application of the UIOLI principle,[228] improved access to market information[229] and the increase of gas transmission capacity.[230] Also, long-term reservations on infrastructures must be confronted, as these entail the risk of 'cementing' the market.[231]

With regard to new networks, the Commission observes that 'substantial investment' is needed 'in new infrastructures such as transit pipelines, interconnectors and LNG-terminals'.[232] Therefore, the Commission holds that exemptions may be important, especially if these apply to facilities that enable the entry of new competitors or the link-up with new sources of gas supply.[233] However, any exemption decision must be based on a case-by-case examination following 'very strict rules'.[234] In any case, the allocation of capacity may not 'perpetuate the current level of foreclosure observed on existing transit pipelines'.[235] Furthermore, the Commission holds that, while deciding on a possible exemption,[236] the nature, scope, parties to and duration of the contracts must all be duly considered.[237] Lastly, the initial capacity 'should be allocated pursuant to a pro-competitive process'. This refers to the need for an 'open season' procedure.[238] Such a procedure is thus 'crucial' to an outcome that is not harmful to competition,[239] which is in turn a condition to grant an exemption.

All in all, although the Commission endorses the value of exemptions, it argues that TPA must be provided as far as possible.

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gas release programmes as a way to enhance market liquidity and increase the possibilities for third parties to enter the market. Additionally, increased hub liquidity may result in price formation based on differences in supply and demand, rather than the price of oil (derivatives). See p. 12 of the Commission Report (*supra* note 28).

[227] Capacity hoarding may occur when e.g. no effective UIOLI regime is in place, and third parties are thus denied access to the facilities even in the event that there is available capacity. See p. 13 of the Commission Report, *supra* note 28.

[228] See p. 16 of the Commission Report, *supra* note 28.

[229] *Ibid*.

[230] *Ibid*.

[231] In its Report, (*supra* note 28, par. 240) the Commission warns that various incumbents may be benefiting more from the current market developments than third parties. It states that: 'it appears that *the additional primary capacity* resulting from previous capacity increases on the five highly congested pipelines under analysis has, for the most part, *ended up in the hands of the companies that already controlled the pre-existing primary capacity* [italics added, TvdV]'.

[232] See par. 236 of the Commission Report, *supra* note 28.

[233] See the 'Commission staff working document accompanying the Communication from the Commission – Inquiry pursuant to Article 17 of Regulation (EC) No 1/2003 into the European gas and electricity sectors (Final Report)', COM(2006) 851 final, par. 255.

[234] The Commission, in its Report (*supra* note 28, par. 237) reiterates the balance that must be struck: '(i)t is important, therefore, that the regulatory regime strike [*sic*] a balance between providing the right incentives to build new capacity and ensuring that any long-term contracts do not have detrimental effects on competition'.

[235] *Ibid*., par. 257.

[236] Commission Report, *supra* note 28, par. 238: '(t)he granting of an exemption is subject to a number of conditions, including, crucially, that the exemption not be detrimental to competition'. The Commission refers to the CEER paper 'Investments in gas infrastructures and the role of EU national regulatory authorities'.

[237] See par. 239 of the Commission Report, *supra* note 28.

[238] Or a similar procedure, organised *before* the expansion, which also has the effect of allowing third parties to participate in the expansion. See the Commission Report, *supra* note 28, par. 239.

[239] See par. 241 of the Commission Report, *supra* note 28.

6.5 EU Reform Treaty

The topicality of liberalisation and access issues in the gas sector is illustrated by the EU Reform Treaty,[240] adopted by the European Council meeting in June 2007. This Treaty will for the first time include a provision on energy policy, giving the EU an improved legal basis to legislate in this area. It will define the objectives of EU energy policy as (i) ensuring a functioning internal energy market, (ii) ensuring security of supply, and (iii) promoting energy efficiency and renewable energy sources. The Treaty will also attempt to improve the interconnection of national energy infrastructures. The final texts of these provisions will be (probably) agreed upon in the upcoming months.

[240] For the main documents on the EU Reform Treaty, see http://ec.europa.eu/commission_barroso/president/focus/council_062007_en.htm#key (last visited 25 September 2007).

7. CASE STUDY – THE EXEMPTION REGIME IN PRACTICE

7.1 Introduction

As shown in the chapter above, there are several guidelines and principles which are relevant when an exemption under Article 22 of the second gas Directive is under review. This chapter will examine the exemption decisions by the domestic authorities in order to determine how this provision works in practice.

By September 2007, ten applications were notified to the Commission.[241] These concerned the construction of LNG terminals in the UK (Dragon, South Hook and Isle of Grain), the Netherlands (Gate, Eemshaven and LionGas) and Italy (Rovigo[242] and Brindisi). Also, exemptions were requested for interconnectors between the UK and the Netherlands (Balgzand Bacton Line)[243] and between Italy and Greece (Poseidon). Three UK projects (Caythorpe, Holford and WINGAS) which have not yet been made public by the Commission shall be discussed as well.

According to the European Commission, the authorities' assessments have 'to achieve a balance between *ex ante* incentives to invest and competition once the investment has been made'.[244] The following paragraphs shall explore how the NRA's try to strike a balance between these goals.

Before doing so, it is useful to clarify a few things. First, the authorities under review all put forward an 'interim' decision before laying down a 'final' one. The former is open to comments from interested parties. My review will relate primarily to the final exemption orders, although I will also mention interim decisions whenever relevant.

Second, one must take into account that in the countries under review, the NRA's final exemption decision is formally an *advice* to the competent Ministry. The Ministry is competent to amend, revoke or accept this advice. However, as the Ministry's assessments usually do not differ from the ones drafted by the NRA's, I shall focus on the latter. I will mention whenever there was a (publicly known) divergence of views.

Third, it should be reiterated (see par. 4.3.6) that the Commission is competent to amend or withdraw exemption granted by the NRA's.[245] As shown above, the NRA's decision is directly applicable until the Commission chooses to amend or withdraw that decision.

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[241] See http://ec.europa.eu/energy/gas/infrastructure/exemptions_en.htm (last visited 25 September 2007).

[242] The Rovigo project is also known as the 'North Adriatic LNG terminal', see http://www.adriaticlng.com/pagine/home.aspx (last visited 25 September 2007).

[243] Although the Dutch and the British authorities conducted a separate assessment of the exemption request (see par. 7.2.4 & 7.3.3 below), I deal with it as constituting one single application vis-à-vis the Commission, since the outcome was substantively the same.

[244] See p. 11 of the Commission Report (*supra* note 28).

[245] Article 22(4)(e) of the second gas Directive. The Commission is able to do so within a time span of two months.

7.2 The United Kingdom[246]

7.2.1 Regulatory framework

In 2004, the United Kingdom adopted the 'Gas Third Party Access Regulations' (Gas Regulations).[247] These regulations implement the TPA provisions of the second gas Directive, by amending section 19A of the Gas Act 1986. According to the new subsection (5) of that provision, the British NRA Ofgem[248] is competent to grant an exemption. It may do so when the use of the facility by third parties is 'not necessary for the operation of an economically efficient gas market',[249] and if a number of conditions have been met.[250] These requirements are very similar (but not always identical) to the ones specified in the Directive.[251]

It should be noted that Ofgem 'does not consider that there are any material differences' between the gas Regulations and the Directive.[252] Still, it can be questioned why the wording in the national implementation measure had to be different if the material assessment is exactly the same. For lawyers, different words usually have different meanings.[253]

The UK and EC texts are divergent in a number of ways. First, the UK Gas Regulations do not mention that the exemption should lead to an *increase* in competition, but rather determine that the exemption may not be 'detrimental to competition'. It accordingly accepts an exemption that does neither increase, nor is to the detriment of, competition. This part of the UK text thus seems to be more lenient

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[246] For the sake of simplicity, I shall only refer to the 'United Kingdom' for the purposes of my thesis, even where, for instance, relevant documents refer to 'Great Britain'.

[247] See 'The Gas (Third Party Access) Regulations 2004', Statutory Instrument 2004 No. 2043. Available at http://opsi.gov.uk/si/si2004/20042043.htm (last visited 25 September 2007). The Gas Regulations 2004 came into force on 26 August 2004. This document amended the Gas Act 1965, the Gas Act 1986 and the Petroleum Act 1998.

[248] Ofgem is an acronym for 'the Office of Gas and Electricity Markets'.

[249] Section 19(A)(5) of the Gas Act 1986, as amended by the Gas Regulations.

[250] *Ibid*.

[251]
1. 'the facility or (as the case may be) the significant increase in its capacity will promote security of supply;
2. the level of risk is such that the investment to construct the facility or (as the case may be) to modify the facility to provide for a significant increase in its capacity would not be or would not have been made without the exemption;
3. the facility is or is to be owned by a person other than the gas transporter who operates or will operate the pipeline system connected or to be connected to the facility;
4. charges will be levied on users of the facility or (as the case may be) the increase in its capacity;
5. the exemption will not be detrimental to competition, the operation of an economically efficient gas market or the efficient functioning of the pipeline system connected or to be connected to the facility; and
6. the Commission of the European Communities is or will be content with the exemption'.

[252] See e.g. Ofgem final views in Dragon, *infra* note 286, par. 1.3.

[253] For the European Court of Justice, the *same* words even sometimes have different meanings, depending on the context of the provision.: 'a mere similarity in the wording of a provision (…) is not sufficient to give to the wording (…) [a similar] meaning'. See Case C-63/99, *Gloszczuk*, [2001], par. 48; Case 270/80, *Polydor and RSO Records*, [1982] ECR 329, par. 14-21; Case 104/81, *Kupferberg*, [1982] ECR 3641, par. 29-31; Case C-312/91, *Metalsa*, [1993] ECR I-3751, par. 11-20. *A contrario*, one can infer that different words may thus very well have different meanings.

towards granting an exemption.[254] Second, condition (2) (on the level of risk surrounding the project) refers to costs that 'would not have been made'. This refers presumably not to sunk costs which are yet to be sustained in the future (a requirement to benefit from an exemption, see par. 4.4.5), but to stranded costs *already* incurred in the past. Such a reference cannot be found in the Directive. A third – albeit small – difference is to be found in condition (3), which mentions the (future) connectivity to 'pipeline systems', not to the more general notion of 'infrastructures'.[255] Fourth, the Gas Regulations refer to the Commission's approval in condition (6). This is valuable, as it indicates the key role of this Institution in exemption matters. As shall be seen below in paragraph 7.3, such a referral is not explicitly laid down in the Dutch Gas Act. A last difference relates to the concept of a 'new facility', which the UK legislation defines as a facility whose 'construction is completed' after 3 August 2003.[256] The Directive uses a different definition, namely that the 'main financial commitment' must have been made after 15 July 2003.[257, 258]

7.2.2 Exemption policy

The domestic exemption policy is laid down in a joint consultation document of the UK Department of Trade and Industry (DTI) and Ofgem.[259] It stipulates three minimum requirements for an exemption to be granted. First, the initial offer of capacity to the market should be effectively allocated. Second, there must be effective measures in place to guarantee that capacity is not hoarded. This could require the use of the UIOLI principle. Third, there needs to be an adequate flow of information to the regulator and – in some circumstances – to the market.

Some general thoughts on access matters can be found in a research report from the Joint Energy Security of Supply Working Group (JESS). This report states that, since the UK 'becomes more dependent on imported gas', there is an ever-growing need for 'new gas supply sources as well as investment in infrastructure projects' in order to

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[254] At least in the view of the Commission. It considers these criteria as being similar, but distinct: '(c)ondition (5) has similarities with the first conditions with the objective of defending a competitive market. However in this case it is noted that the exemption itself *should not be to the detriment of the competitive functioning of the market* [italics added, TvdV]'. See the Interpretation Note by DG TREN of 30 January 2004 (*supra* note 144), p. 5.

[255] It is unclear whether that can lead to problems in practice. Undoubtedly, in practice pipeline systems shall be the main infrastructures used in connection to the facilities in question. Still, it cannot be excluded that the Directive also wanted to target other infrastructures, such as regasification facilities.

[256] Section 19(E)(1) of the Gas Act 1986, as amended by the Gas Regulations.

[257] See par 4.3.4 above.

[258] Admittedly, I have found no examples where this divergent approach has lead to any difficulties in practice. Another issue to be noted is that after the entry into force of the Gas Regulations, on 26 August 2004, obviously *all* storage facilities which would be constructed would be considered as 'new' (as in all these cases, the construction will be due after 3 August 2003).

[259] See 'LNG facilities and interconnectors, EU legislation and regulatory regime, DTI/Ofgem initial views', DTI/Ofgem, June 2003, available at: http://www.energy.ca.gov/lng_docket/documents/lng_bibliography/02_Information_Relating_to_LNG_Terminal_Access/b_Europe/25_UK_LNG_exemption_rules_draft.pdf (last visited 25 September 2007).

keep pace with demand.[260] These policy considerations arguably have a sizeable impact on the exemption decisions.

Similar to the other NRA's, Ofgem retains the right to revoke the exemption order. In principle, a revocation should be seen as an *ultimum remedium*, since dialogue between parties is the preferred way to sort out any possible issues. Still, as shall be seen below, this discretionary power forms one of the bases of Ofgem's assessments.[261]

7.2.3 Conditions

In its exemption orders, Ofgem usually lays down several 'standard' conditions. First, the information provided by the requesting party has to be 'accurate in all material respects'. Second, the requesting party must provide Ofgem with detailed information concerning the initial and the expansion capacity. Third, the requesting party must actively update Ofgem of any other relevant data.[262, 263] Fourth, the requesting party must comply with any instruction given by Ofgem. Fifth, Ofgem retains the right to amend or revoke the decision. Such a situation will occur if the facts and/or circumstances under which the exemption was granted significantly change. Sixth, Ofgem will also amend or revoke the decision if it is requested to do so by the European Commission. Lastly, Ofgem also retains the right to transfer the exemption to another facility owner.

7.2.4 Balgzand Bacton Line – United Kingdom

* Introduction

In September 2003, Gastransport Services (hereinafter: GtS), the Dutch gas transmission system operator, requested an exemption for the 'Balgzand Bacton Line' (hereinafter: BBL). The BBL is a pipeline between the UK and the Netherlands,[264, 265] with an initial capacity of 8 bcm in 2006, which is projected to rise to 17 bcm in 2008. As the BBL concerned both the UK and the Netherlands, the procedure to decide on

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[260] See the Joint Energy of Supply Working Group, *Third Report*, November 2003, par. 25. Apart from new sources, the document mentions in particular the necessity for an increase of imports from Norway and from 'Europe' via interconnectors.

[261] See e.g. par. 2.47 & 2.48 of the Ofgem final views in the Grain case (*infra* note 306). First, if there is any possible problem, Ofgem will enter into discussions with the parties concerned. Second, the parties involved shall always be awarded a 'reasonable opportunity' to remedy the situation at hand.

[262] This condition primarily deals with the way how the relevant undertakings comply with all the applicable (access) rules.

[263] The document mentions the Gas Act 1986, the Utilities Act 2000 or the Energy Act 2004. See e.g. the Ofgem final views in the South Hook case (*infra* note 276), p. 25.

[264] In its request for an exemption, GtS compares the BBL with other planned projects such as the gas import facility via the Isle of Grain LNG terminal (4,5 bcm), Milford LNG harbour (6-12 bcm) and the expansion of the present-day Interconnector between the Netherlands and the UK (which would have an additional capacity of 8,5 bcm).

[265] According to the Dutch gas network operator Gasunie, the BBL is one of 'the first steps' in order to accommodate 'the long-term demand for the transport of both Dutch and foreign flows', see http://www.nvnederlandsegasunie.nl/en/freemarket.htm (last visited 25 September 2007).

the request was said to have been done in close cooperation between the British and the Dutch authorities.[266]

* Assessment
Ofgem held that the conditions had been met and accordingly granted the exemption request. The exemption will last until 2022 and shall apply to the full capacity.[267] Ofgem held that the envisaged UIOLI arrangements were vital to the approval, as that would prevent any anti-competitive hoarding of capacity.[268] Ofgem also underlined its competence to revoke the decision,[269] suggesting that future abuse would not be likely since the BBL would be under constant monitoring. It serves as an additional argument to grant an exemption even though not all the conditions have been manifestly met. Furthermore, Ofgem stressed its approval of the BBL's objective, transparent and non-discriminatory charging methods.[270]

* Conditions
BBL had to comply with the standard conditions as explained in par. 7.2.3 above.[271]

* European Commission
In accordance with Article 22(4) of the second gas Directive, the Commission sent a request to Ofgem with the aim of amending the exemption. The Commission stressed that the exemption ought only to apply in respect of the duration and capacity specifically covered by the initial contracts signed by the BBL Company. Also, the exemption should not apply to any gas flowing from the UK to the Netherlands (the so-called 'reverse gas flow'). Via an open letter[272] of August 2005,[273] Ofgem honoured both of the Commission's requests.[274]

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[266] From the Netherlands, the Ministry of Economic Affairs and the DTe were involved. From the UK, the Department of Trade and Industy and the Office of Gas and Electricity Markets took part in the procedure.
[267] See the 'Application by BBL Company for an interconnector licence to participate in the operation of the Balgzand Bacton Line', Ofgem final views of April 2005, par. 2.37.
[268] It also held that condition 13 will ensure that the maximum amount of capacity is made available to the market. See Ofgem final views in the BBL case (*supra* note 267), par. 2.13.
[269] Ofgem final views in the BBL case (*supra* note 267), par. 2.13-2.15.
[270] See also condition 10 of Ofgem's final views (*ibid*.).
[271] See par. 7.2.3 above. This condition has been laid down in the Ofgem final views in the BBL case (*supra* note 267), p. 33. The information provided had to be accurate; Ofgem maintains the right to revoke the exemption under certain circumstances, as well as the right to amend the exemption if this is requested by the European Commission.
[272] Strangely enough, this open letter was apparently forwarded to the BBL Company and to the European Commission (both to the Energy and the Competition DG), but *not* to the Dutch regulators. One could question if such apparent lack of cooperation is desirable.
[273] For this letter by Ofgem of 9 August 2005, see: http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/Amendment%20to%20the%20exemption%20order%20issued%20to%20BBL%20Company.pdf (last visited 25 September 2007).
[274] Ofgem did so on the basis of condition 12 of the gas interconnector licence granted to BBL Company in respect of the Balgzand Bacton Line. This condition lays down the possibility of Ofgem to revoke an exemption already given.

7.2.5 South Hook

* Introduction

In September 2004, South Hook LNG Terminal Company Ltd (hereinafter: South Hook)[275] requested an exemption for the capacity of its new import facility. Two months later, Ofgem submitted its final views, approving the exemption as all the relevant criteria were met.[276] The exemption shall last for 25 years and will apply to the entire capacity[277] of the project, completely as requested.[278]

* Assessment

In its decision, Ofgem had regard to the following considerations. First, it stated that the security of supply would be strengthened *because* South Hook enables the use of new gas new sources.[279] As to the level of risk involved, Ofgem considered that it was 'difficult to see how the risks associated with this project can be mitigated by anything other than some form of long-term contractual support'.[280] It concluded that the level of the risk involved is 'likely' to merit an exemption. As no objections to that interim conclusion were raised, the condition was considered to be met in the final decision. As to the charges levied, it is interesting to note that although Ofgem obliged South Hook to publish its tariffs in its initial views, it did not restate this requirement in its final decision. Lastly, Ofgem submitted that, in principle, long-term exemptions are possible, especially given the European Commission's decisions accepting exclusive energy contracts lasting for many years (such as the 25-year agreement concerning the interconnector between the UK and Belgium).[281]

* Conditions

In its decision, Ofgem laid down only standard conditions.[282, 283] Also, Ofgem reiterated its revocation competence,[284] providing a guarantee that any anti-competitive risks could be dealt with despite the exemption order.[285]

* European Commission

The European Commission approved the exemption granted without laying down further conditions.

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[275] South Hook is a Joint Venture owned by Qatar Petroleum and Exxon Mobile.

[276] See the 'Application by South Hook LNG Terminal Company Ltd under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986', Ofgem final views of November 2004.

[277] The initial capacity would be 10,5 bcm per year, with a possibility to add additional capacity of another 10,5 bcm per year. Ofgem final views in the South Hook case (*ibid*.), p. 24.

[278] Ofgem final views in the South Hook case (*ibid*.), p. 25.

[279] *Ibid*., par. 2.4.

[280] *Ibid*., par. 2.7.

[281] See par. 3.2 above.

[282] Ofgem is competent to lay down conditions on the basis of Section 19(C)(3)(b) of the Gas Act 1986, as amended by the Gas Regulations 2004.

[283] The conditions are laid down in Ofgem final views in the South Hook case (*supra* note 276), p. 25-26.

[284] Pursuant to Section 19(C)(4) of the Gas Act 1986, as amended by the Gas Regulations 2004.

[285] See Ofgem final views in the South Hook case (*supra* note 276), p. 27-28. Also, Ofgem has the competence to revoke the exemption in a number of cases, for instance if there is a significant change in the material facts of the case or if the facility owner is found to be in breach of the UK Competition Act.

7.2.6 Dragon

* Introduction

In October 2004, Dragon LNG Limited (hereinafter: 'Dragon') submitted its request for an exemption.[286] Dragon wished to construct an LNG importation and regasification facility. After an 'open season' procedure, capacity in the facility was to be sold to two undertakings.[287] In its preliminary views, Ofgem stated that Dragon's application was 'likely to meet all the criteria for exemption and, as such, this project could be expected to have an overall positive impact on competition and security and diversity of supply for the UK'. In February 2005, Ofgem gave its final views on the issue, and held that the criteria have been met.[288] Therefore, Ofgem granted an exemption with regard to – as requested – the entire proposed capacity of the facility[289] lasting for 20 years.[290]

* Assessment

Ofgem considered that the import facility would improve the security of supply, as the total volume of supply will increase.[291] In its interim decision, Ofgem put forward a highly pragmatic approach. It stated that it strives for a 'more favourable' regulatory regime than those existing in third countries. Otherwise, new LNG infrastructure projects could be rescheduled to other countries such as the US, which could eventually harm the security of supply in the UK and the EU.[292]

Furthermore, Ofgem accepted that the level of risk involved was sufficiently elevated. Ofgem held in its initial views that this requirement was 'likely' to be met. Since no respondent made any objections, Ofgem maintained its position. As to the duration of the exemption, it considered 20 years to be appropriate and compatible with EC law, referring e.g. to the *Viking Cable* and *European Night Services* decisions.[293] Ofgem stated that a review of the exemption after a certain period of time is not a desirable option, since that would create uncertainty amongst investors.[294]

In its final decision, Ofgem accepted to grant the exemption for the full 100% of the capacity.[295] This was despite its initial request to Dragon to consider adding 25% of

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[286] See 'Dragon LNG limited: Application for an Exemption from Section 19D Gas Act 1986 (as amended by the Gas (Third Party Access) Regulations 2004 implementing Directive 2003/55/EC)', Ofgem initial views (version for public consultation, October 2004).

[287] *In casu*, the relevant undertakings would be British Gas Group and Petronas (which are also the owners of Dragon). See Ofgem initial views in the Dragon case, *supra* note 286, p. 1.

[288] See the 'Application by Dragon LNG Limited under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986', Ofgem final views of February 2005.

[289] The initial capacity would be 6 bcm per year, with a possibility to add additional capacity of another 6 bcm per year. Ofgem final views in the Dragon case (*ibid.*), p. 21.

[290] *Ibid*., par. 1.15.

[291] *Ibid*., par. 2.3. The underlying sentiment is well indicated by the following sentence: '(i)t is clear that as UK production declines, projects such as [Dragon] will play an important role in enhancing security of supply', see Ofgem initial views in the Dragon case, *supra* note 286, par. 5.1.

[292] Ofgem initial views in the Dragon case, *supra* note 286, par. 5.1.

[293] For *Viking Cable*, see above in par. 3.2. For *European Night Services*, see Joined Cases T-374/94, T-375/94, T-384/94 & T-388/94, *European Night Services* v. *Commission*, [1998] ECR II-3141.

[294] In Ofgem's view, such an option would thus have the effect of impairing the necessary investments. See the Ofgem initial views in the Dragon case, *supra* note 286, par. 5.2.1.

[295] Ofgem initial views in the Dragon case, *supra* note 286, par. 3.2.

capacity, which could then be excluded from the exemption. Dragon submitted that such an increase in capacity would significantly delay the project and would thus endanger the project as a whole.[296] It is noteworthy that Ofgem accepted Dragon's objections, even though these referred to operational complexities rather than actual impossibilities.[297]

Finally, Ofgem submitted that Dragon complied with all the other requirements as to unbundled ownership,[298] the charges levied on consumers[299] and the impact on competition.[300] With regard to the last condition, it is to be noted that Ofgem regards the UK market as being sufficiently 'dynamic' to exclude the possibility of market foreclosure.[301] In short, Ofgem expected the project to have an overall positive impact on competition.[302]

* Conditions
Ofgem only laid down standard conditions.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.2.7 Grain

* Introduction
In August 2004, Grain LNG Limited (hereinafter Grain),[303] which planned to construct a new LNG import facility, issued a request for an exemption.[304, 305]

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[296] Dragon submitted that proposed size of the facility is 6 bcm per year. Ofgem's request related to a capacity increase of 1,5 bcm per year. Dragon submitted that such an augmentation would necessitate a drastic change of plans, which would probably delay the construction work. This could endanger the project as a whole. See Ofgem initial views in the Dragon case, *supra* note 286, par. 3.2(b).

[297] See e.g. Ofgem initial views in the Dragon case, *supra* note 286, par. 3.2(c), (e) and (f).

[298] Ofgem final views Application by Dragon LNG Limited under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986, par. 2.9 & 2.11. Available at: http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/10028_2005.pdf

[299] Ofgem final views in the Dragon case (*ibid.*), par. 2.16. However, Ofgem also considers that Dragon does not need to publish its tariffs (*ibid.*, par. 2.12). It is satisfied if it would be the only one that would receive Dragon's information on the applicable tariffs.

[300] Ofgem final views in the Dragon case (*ibid.*), par. 2.25-2.27.

[301] Ofgem final views in the Dragon case (*ibid.*), par. 2.18. This is particularly interesting, as Ofgem backs up its stance by referring – when assessing the requirement on the security of supply – to documents warning for the future problems in the UK gas supply (see the research document by JESS, *supra* note 260).

[302] Ofgem final views in the Dragon case (*ibid.*), par. 2.27.

[303] Grain is a Joint Venture between British Petroleum and Sonatrach.

[304] For the full version of Grain's application for an exemption, see http://www.nationalgrid.com/NR/rdonlyres/2810BDC1-3CEC-4313-A8E9-6E2E829C477E/14411/GrainLNGRTPAExemptionApplicationConsultationRespon.pdf (last visited 25 September 2007).

[305] For more information on the Grain facility, see http://www.nationalgrid.com/uk/GrainLNG/background/ (last visited 25 September 2007).

* Assessment

Ofgem held that all the criteria have been satisfied.[306] The creation of a new source of gas will aid the security of supply, which will in turn boost competition.[307] Furthermore, Ofgem stressed that the exemption is indeed indispensable for the investment to be made. This is quite remarkable, since at the time the investors agreed to finance the project, the current regulatory framework was not yet in place and Ofgem was accordingly not (yet) able to officially grant an exemption.[308] At the time, investors were apparently satisfied with an informal (and non-binding) comfort letter that Grain would *probably* be exempted.[309] Ofgem held that Grain does not need to publish its tariffs (not even to Ofgem itself), as these are 'commercially confidential'. The resulting decrease in market transparency was seemingly less important.

Ofgem was pleased to note that Grain had conducted an open season procedure.[310] Also, Grain's implementation of a number of anti-hoarding measures was favourably received, even though the actual – or potential – effects of these measures were not investigated in depth.[311] Indeed, Ofgem merely mentioned in a general way that the UIOLI principle would have to be respected.[312] The same approach was used vis-à-vis Grain's pledge to publish certain types of information to facilitate trading on the secondary market.[313] Ofgem concluded by arguing that the project has 'material benefits' to upstream markets, and does not have a 'material adverse effect' on the downstream market.[314] Therefore, all the criteria have been met and the exemption is

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[306] See the 'Application by Grain LNG Limited under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986', Ofgem final views of December 2004, par. 1.12 & 1.14.

[307] Ofgem final views in the Grain case (*ibid.*), par. 2.3 & 2.5.

[308] It is to be noted that Grain's decision to invest was taken before DTI and Ofgem were competent to issue exemptions from TPA. However, Grain did receive verbal guidance from DTI and Ofgem 'that *it could expect to be exempt* as and when formal powers became available [italics added, TvdV]'. In my opinion, this approach is perhaps a bit premature. The assurances given by the UK authorities should only be given after a thorough case-by-case analysis. See also Ofgem's final views in the Grain case (*supra* note 306), par. 2.10.

[309] That is to say, if all the criteria in the (then) draft second gas Directive would be adhered to. See Ofgem final views in the Grain case (*supra* note 306), par. 2.7.

[310] Ofgem final views in the Grain case (*supra* note 306), par. 2.22. Grain did so with regard to both the first and the second phase trading.

[311] Ofgem final views in the Grain case (*supra* note 306), par. 2.29. According to Ofgem, Grain needs to show, 'at the very least', that spare capacity shall be made available to the market in a transparent manner.

[312] *Ibid*. Ofgem states that anti-hoarding measures are the 'ultimate objective'. Also, it argues that third parties should have access to excess capacity 'so as to maximise the use of the LNG import terminal concerned'.

[313] *Ibid*. Grain pledged to set up a website 'to facilitate secondary trading and sub-letting by the primary capacity owners'. According to Ofgem, this provided an 'important part' of granting the exemption.

[314] Ofgem final views in the Grain case (*supra* note 306), par. 2.34. Downstream markets are not likely to be affected if one has regard to the two undertakings involved in the Joint Venture, BP and Sonatrach. Ofgem does not consider BP's present market share in the retail markets in gas supply to UK industrial/commercial and power station customers to be at a level that it is likely to have unfavourable effects on competition. Moreover, it was taken into account that BP apparently had little interest in the gas supply to UK consumers. Ofgem holds moreover that the other undertaking, Sonatrach, is a new competitor in the downstream market. As a consequence, the project is likely to have pro-competitive effects.

granted for the full capacity of the facility lasting for 20 years for the initial capacity, and 25 years for any additional capacity.[315]

* Conditions
Ofgem only laid down standard conditions.

* European Commission
During its Sector Inquiry, the Commission observed that a significant share of the berthing slots at the Grain terminal were not used by the two shippers, and suggested that the UIOLI principle could be applied.[316] Subsequently, Ofgem requested the operator and the users to review the framework for secondary trading of berthing slots and capacity at the facility.[317] The parties concerned made various changes, which included a stricter UIOLI regime. From now on, if a similar situation would occur, the slots would have to be made available to third parties.

7.2.8 Caythorpe

* Introduction
In February 2005, Caythorpe Gas Storage Limited (hereinafter: Caythorpe)[318] issued an application for an exemption.[319] The request related to a depleted gas field, which was envisaged to be turned into a gas storage facility. Despite the large size of the facility,[320] CGSL intended to have only a single customer, with whom a long-term agreement could be made for the storage of gas.

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[315] The facility is projected to have an initial capacity of 4,5 bcm per year and an expansion capacity of 10 bcm per year. Ofgem final views in the Grain case (*supra* note 306), par. 2.65.

[316] For a summary of the relevant facts, see the 'Commission staff working document', *supra* note 233, par. 265: '(t)he entire capacity of the LNG terminal in Isle of Grain in the UK has been allocated for 20 years to a joint venture between BP and Sonatrach. During its investigation, the Commission found that an important share of the berthing slots of the terminal was not used by the two shippers. The Grain LNG operator offered some of the available capacity to the market by publishing a notice on its website, but no third party expressed an interest in using these specific slots, regardless of the general interest that several gas companies had expressed in using the terminal facilities'.

[317] See the two letters written by Ofgem, to be found on the following websites (last visited 25 September 2007):
http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/12165-255_05.pdf and
http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/14882-134_06.pdf.

[318] CGSL is a wholly owned subsidiary of Warwick Energy Limited.

[319] For the decision by Ofgem on the application of Caythorpe of 5 July 2005, see
http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/11073-16505.pdf (last visited 25 September 2007).

[320] The storage facility is projected to have a total capacity of 3.000 GWh, with a deliverability of 120 GWh per day and an injectability of 90 GWh per day.

* Assessment
Ofgem adopted a very wide market definition, holding that Caythorpe would hold a mere 3% share of the product market for 'flexibility in Great Britain'.[321] Ofgem admitted that it is difficult to accurately define what that market is.[322] It held that the unclear demarcation between market sub sectors in any case warrants a wide definition. In addition, Ofgem did *not* narrow down its scope to already existing storage facilities. The market assessment included several storage facilities that were 'likely' to be build in the near future.[323, 324] This category even included 'potential' future facilities.[325]

Moreover, Ofgem rejected one of the respondent's complaints that the number of exemptions already granted in the UK would have a cumulative detrimental effect on competition. It argued that it already sufficiently took into account such concerns.[326] In sum, Ofgem held that TPA was not necessary and approved the exemption for the complete capacity of the project. While it explicitly referred to the possibility of revocation, Ofgem did not impose a time limit for the exemption.

* Conditions
Ofgem only laid down standard conditions.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.2.9 Holford

* Introduction
In September 2005, INEOS Enterprises Limited (hereinafter: INEOS) filed a request for an exemption for a capacity increase of the Holford storage facility.[327] In its application, INEOS stressed that it was in the process of negotiating contracts which would allow the import and the export of gas; as well as the trading of gas. These negotiations were said to depend on the fact whether or not an exemption would be

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[321] Ofgem final views in the Caythorpe case (*supra* note 319), p. 2. As a consequence, wider market definitions were disregarded. If one would have regard, for instance, to the overall market for gas and LNG storage space, Caythorpe's market share would amount to 7%.
[322] Ofgem final views in the Caythorpe case (*supra* note 319), p. 4. Any distinction made between short, medium and long duration facilities can therefore not be based on a clear distinction by product markets.
[323] Namely the storage facilities at Humbly Grove, Aldbrough and Byley.
[324] Ofgem final views in the Caythorpe case (*supra* note 319), p. 4.
[325] Ofgem adds that although it 'has not included all potential future storage facility projects in its market definition, these potential projects indicate that investors are responding to market signals to invest and that the likelihood of such investments is not merely theoretical but represents an actual competitive constraint on the behaviour of those already operating in the market'. See *ibid*.
[326] *Ibid*.
[327] For the decision by Ofgem on the application of INEOS Enterprises Limited of 15 December 2005, see http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/12324-276_05.pdf (last visited 25 September 2007).

granted. Moreover, INEOS underlined the facility's small size.[328] Finally, if the project would go ahead, INEOS could be a new player in the UK gas storage market. It thus concluded that the project would increase supply diversity and competition.

* Assessment
Ofgem agreed with all the submissions made by INEOS. It stated that the facility in question is very small in size when compared to the overall relevant market.[329] As a consequence, TPA is 'not necessary' *in casu* to achieve an economically efficient gas market.[330] Therefore, Ofgem granted an exemption for the full capacity of the facility. As in Caythorpe, the exemption applies indefinitely, until Ofgem decides to revoke it.

* Conditions
Because of the facility's small size, Ofgem considers that UIOLI requirements are not necessary.[331] Apart from that, only standard conditions were laid down.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.2.10 WINGAS

* Introduction
In June 2006, WINGAS Storage UK Limited (hereinafter: WINGAS)[332] applied for an exemption.[333] WINGAS planned to convert a gas field[334] into a storage facility.[335, 336] In its application, WINGAS submitted that it would put in place a UIOLI regime, and that it would sell any excess short term capacity 'on a firm or interruptible basis'.[337] It also stressed that its conduct would be non-discriminatory.[338]

* Assessment
In a very concise decision, Ofgem granted an exemption to the full capacity of the storage facility.[339] The exemption applies indefinitely.[340] Again, the small size of the

[328] Ofgem final views in the Holford case (*ibid*.), p. 1. According to INEOS, the storage facility represented less than 1% of the relevant domestic market.
[329] Ofgem final views in the Holford case (*ibid*.), p. 2.
[330] *Ibid*., p. 2.
[331] *Ibid*., p. 2-3.
[332] WINGAS is a Joint Venture between ZMB Gasspeicherholding GmbH (Austria) and WINGAS GmbH (Germany). In turn, the latter is a Joint Venture between Wintershall AG (Germany) and OAO Gazprom (Russia).
[333] As laid down in Section 19B of the UK Gas Act.
[334] *In casu* the Saltfleetby gas field near Lincolnshire, where the gas reserves have been going down rapidly in the last few years.
[335] For the decision by Ofgem on the application of WINGAS of 30 August 2006, see http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/TPAccess/Documents1/15258-WINGAS%20Decision%20Letter%20Final.pdf (last visited 25 September 2007).
[336] The gas storage facility is projected to have an operational capacity of around 7.650 GWh. On a daily basis, it will be possible to withdraw 85 GWh from and inject 45 GWh in the facility.
[337] Ofgem final views in the WINGAS case (*supra note* 335), p. 1-2.
[338] *Ibid*., p. 2.
[339] *Ibid*., p. 2-3.

field removed the need for TPA.[341] This conclusion seems to be ill at ease with the market shares put forward by Ofgem itself, namely 12% of the overall market for gas storage.[342] The market for 'flexibility' (as used in Caythorpe) was not mentioned at all, although under that definition WINGAS would have a smaller market share.[343] Lastly, Ofgem admitted its 'enthusiasm' that WINGAS plans to lay down an UIOLI framework. The mere fact that there were no actual UIOLI provisions under review was seemingly of little importance.

* Conditions
Ofgem restated that it will continue to review the effects of the exemption granted. The conditions it lays down are identical to the ones already used in the other exemption reviews.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

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[340] *Ibid*., p. 6.
[341] See the final views by Ofgem in the WINGAS, *supra* note 335, p. 2.
[342] Ofgem final views in the WINGAS case (*supra note* 335), p. 2. With this amount of total capacity, WINGAS will have the biggest UK storage facility by a great margin. The Saltfleetby capacity is 62% bigger than the number two storage facility, namely Welton (projected to start operations in 2007).
[343] Since the 'market for flexibility' is an arguably much wider concept than the 'market for gas storage'.

7.3 The Netherlands

7.3.1 Regulatory framework

Article 18h of the Netherlands gas act 2000 (Gaswet; hereinafter 'the Dutch gas act')[344] implements Article 22 of the second gas Directive.[345, 346] The criteria mentioned in this Article are almost identical to the ones stipulated by the Directive.[347]

Still, there are a few textual differences. The most noteworthy of these can be found in condition n° 5 (cf. footnote 347 and par. 4.3.5 above). The Dutch text appears to leave more leeway for refusing an exemption. In the Dutch gas act, an exemption is allowed insofar it does not 'hinder competition' ('belemmert'), while the Directive enables an exemption if it is not 'detrimental' ('ten koste van') to competition. It could be argued that an exemption could 'hinder' competition without being 'detrimental' to it. The former means that competition cannot operate to its fullest, while the latter implies that effective competition is not possible at all.

Initially, the exemption applications were assessed by the specialised energy regulator DTe. Since an organisational reshuffle in 2005,[348] in which the DTe was made part of the NMa, the exemption orders were formally made on behalf of the NMa.

The exemption may apply to a part or to the whole of the relevant networks and facilities.[349] The NMa may issue specific conditions.[350] In any case, the NMa must

[344] In full, this Act is named 'Wet van 22 juni 2000, houdende regels omtrent het transport en de levering van gas'.

[345] Article 18(1) of the Dutch Gas Act assigns 'our Minister' (namely the Minister of Economic Affairs, see Article 1(1)(a)) as the competent authority to grant exemptions. Before making his/her decision, the Minister receives advice by the Dutch Competition Authority, see Article 18h(4). It must be remembered, however, that any decision as to the approval of an exemption does not enter into force before the term has passed in which the Commission can put forward its own views (as stipulated in Article 22(4) of the second gas Directive). If the Commission decides to change or withdraw the exemption, the domestic authority must wait until the Commission gives a final decision as laid down in Article 30(2) of the second gas Directive.

[346] As in Article 22 of the second gas Directive, exemptions within the meaning of Article 81h of the Dutch gas Act may apply to large-scale, new cross border transport pipelines, LNG and gas storage facilities. Another possible field of application is with regard to proposed networks or facilities that would significantly expand the present-day capacity, and would as a consequence stimulate the development of new sources of gas supply, see Article 18(2) of the Dutch Gas Act.

[347] 1. 'The proposed network or facility enhances both competition during the supply of gas and the security of supply.
2. The risk of the investment needed for the proposed network or facility is so elevated, that the construction would not take place without an exemption being granted.
3. The ownership of the network or the facility belongs to another entity than the operator of the network or the infrastructure on which the new network or the new facility shall be connected.
4. The users of the network or the facility are charged with a certain tariff.
5. The exemption does not hinder competition or the effective functioning of the internal market; or the effective functioning of the network or the facility on which the new network or the new facility shall be connected'.

See Article 18(1)(a)-(e) of the Gas Act. The text, as presented here, is a translation by the author.

[348] See e.g. *Kamerstukken I* 2004/2005, 29 992 A.

[349] Article 18(3) of the Dutch Gas Act.

[350] Such as conditions with regard to the duration of the exemption, as well as to access issues, see Article 18(6) of the Dutch Gas Act. Other possible conditions relate to the management and the

take into account the duration of the agreements, the size of the newly created capacity (or the change of the existing capacity), the duration of the project and any other relevant circumstances.[351]

The Minister of Economic Affairs remains competent to amend or revoke an exemption which has already been granted.[352] This can be done, *inter alia*, if the information provided by the requesting parties proves to be incorrect or incomplete, or when the relevant factual circumstances change drastically.[353]

7.3.2 Exemption Policy

Although documents as to the Dutch exemption policy are not comprehensive, they do provide some indications. The Minister of Economic Affairs, competent in this field, stressed the case-by-case nature of the assessment.[354] That is perhaps why general rules on these matters have not been laid down. Nonetheless, the Minister did state that he was, in principle, favourable to projects that increase the diversification of gas supply, or that strengthen the security of supply.[355] In his view, these aims can be achieved primarily by building new LNG facilities and interconnectors.[356]

7.3.3 Balgzand Bacton Line – the Netherlands

* Introduction

Separate from the review by the Ofgem, the Dte also conducted an assessment of GtS' BBL project.[357] Like in the UK, the Dutch authorities approved the request.[358]

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allocation of network and facility capacity, see Article 18(7) of the Dutch Gas Act. It should be noted that the latter conditions may *not* interfere with the execution of long-term contracts.

[351] Article 18(6) of the Dutch Gas Act.

[352] This competence is said to be implied in the authority to grant exemptions in the first place.

[353] Other possibilities include the following: if the undertaking concerned does not abide by the provisions of the Dutch Gas Act (obviously not applying to the articles on TPA); if the undertaking concerned is bankrupt of insolvent or if there are 'other reasons' on to doubt the capability of the undertaking concerned to meet the requirements attached to the exemption. It must be emphasized that this list of reasons to amend or revoke the exemption is non-cumulative. See e.g. the Advice by the Dutch Competition Authority NMa (public version) of August 2006 (*infra* note 370), par. 8.

[354] See in particular *Kamerstukken II* 2006/2007, 29 023, 40, p. 10.

[355] *Ibid*.

[356] For DTe's policy to exempt new LNG facilities from the TPA regime, see the 'informatie en consultatiedocument regulering en ontheffing LNG' at: http://www.dte.nl/images/Informatie-%20en%20Consultatiedocument%20regulering%20en%20ontheffing%20LNG%20-%20FINAL_tcm7-84183.pdf (last visited 25 September 2007).

[357] GtS is a subsidiary of Gasunie, the main Dutch gas infrastructure company.

[358] In its request, GtS relied on Article 22(1) of the second gas Directive. At the time (the end of 2003), this provision had not yet been implemented into Dutch legislation. GtS argues that the proposed infrastructure merits an exemption, as the necessary investments need long-term contracts to mitigate the risk involved. The total investment of the BBL, in GtS' submission, totals around EUR 500 million.

* Assessment
In March 2005, the DTe submitted its final assessment of the BBL project.[359] It held that the project would create an important connection between the UK and Dutch markets, and actually forms an integral part of a broader framework of network improvements.[360] As a result, the BBL would be beneficial to the diversification of Dutch gas supply. Moreover, the increase in gas exports does not enlarge the risk of a gas shortage in the Netherlands, as sufficient entry capacity would preserve the sector's flexibility.[361] The DTe underlined the importance of the 'open season' GtS organised in order to allow potential consumers to book a certain amount of capacity for the long term. [362]

The DTe also considered that the actual risk surrounding the project is difficult to evaluate, let alone to quantify. Therefore, it explicitly had regard to the *perception* ('perceptie') of the risks involved, concluding that these were sufficient to merit an exemption.[363] The BBL thus did not need to produce 'a real quantification' of the risk.[364]

The DTe held that an exemption should be given to the full capacity for 16 years.[365, 366] It stated that there was 'no real need' ('geen echte concrete noodzaak') to limit the duration in question.

* Conditions
As said, the exemption is very much based on the actual circumstances of the case. Most conditions therefore relate to a possible material change in the relevant facts. Moreover, the BBL must evaluate its UIOLI regime. If it does not work satisfactorily, the BBL must, in cooperation with the domestic authorities, alter the system.

After the expiry of the exemption, the BBL shall be subject to a regulated TPA regime.[367]

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

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[359] See 'Ontwerpaanvraag Gastransport Services (GtS) voor een ontheffing voor de Balgzand Bacton Leiding (BBL)', Advice by the DTe (public version) of 25 March 2005. At the time when this conclusion was put forward, the relevant TPA and exemption rules had been implemented in Dutch law.
[360] *Ibid*., par. 24.
[361] *Ibid*., par. 22.
[362] Apart from this, the open season was also meant to establish the final tariffs and the exact conditions of access to the BBL. See e.g. 'Ontwerpaanvraag Gastransport Services (GtS) voor een ontheffing voor de Balgzand Bacton Leiding (BBL)', Advice by the DTe (public version) of 25 November 2003, par. 1. This document is available at: http://www.dte.nl/images/12_13041_tcm7-3749.pdf (last visited 25 September 2007).
[363] *Ibid*., par. 40.
[364] *Ibid*., par. 43.
[365] This time-span corresponds with the total duration of the initial contracts, which lasted until 1 December 2022.
[366] See par. 65 of the DTe Advice in the BBL case, *supra* note 362.
[367] *Ibid*., par. 60.

7.3.4 Gate

* Introduction
Gate terminal (hereinafter: Gate)[368] wishes to construct a LNG regasification facility in Rotterdam harbour.[369] It requested an exemption for the full capacity, lasting for 25 years.[370]

* Assessment
In its assessment, the NMa[371] had regard to both the Dutch market and the North Western European market.[372] It held that the project will not decrease competition, provided that dominant undertakings are given access to only a limited amount of capacity.[373] The NMa seemed pleased with the following promises by Gate. First, the allocation of the primary capacity took place *via* an open season procedure on a 'first come, first serve' basis.[374] Second, a well-structured UIOLI system was set up.[375] Third, Gate intended to facilitate trade on downstream markets.[376] All these factors showed Gate's intention to allocate future capacity in a non-discriminatory manner.

The NMa held that the project strengthens competition and the security of supply, since it would aid diversifying Dutch gas supply.[377] Moreover, the NMa emphasized its competence to monitor the exemption's effect as a way to secure future competition. Gate must actively provide operational data to facilitate this process.[378] In addition, the NMa stressed that it greatly valued the presence of a general pro-competition clause that Gate uses in agreements with capacity users.[379]

According to Gate, the exemption is necessary in particular to mitigate the risks involved.[380] According to the NMa, the risk assessment, ideally, only relates to *actual financial* risks.[381] Still, the NMa held that the *perception* of the risks is very important

[368] Gate is a Joint Venture between Koninklijk Vopak NV and NV Nederlandse Gasunie.
[369] For general information concerning the project, see http://www.gate.nl/en/ (last visited 25 September 2007).
[370] See the 'Aanvraag Gate terminal voor een ontheffing voor LNG installatie', Advice by the NMa (public version) of August 2006. This document is available at: http://www.dte.nl/nederlands/actueel/DTe_Nieuwsberichten/Advies_DTe_over_LNG_terminal_Gate.asp (last visited 25 September 2007).
[371] The document stated that the case was handled by the Dutch competition authority NMa. No reference is made to its specialized energy unit DTe.
[372] According to the NMa, the North Western European market consists of Ireland, United Kingdom, France, Germany, the Netherlands and Belgium. See the NMa Advice in the Gate case, *supra* note 370, par. 19.
[373] NMa Advice in the Gate case, *supra* note 370, par. 19.
[374] *Ibid*., par. 21.
[375] *Ibid*., par. 22.
[376] *Ibid*., par. 23. Gate offers capacity holders two possibilities to sell capacity on the secondary market. First, they can bilaterally sell the capacity themselves. Second, Gate can sell the capacity on behalf of the capacity holder *via* an Electronic Bulletin Board.
[377] *Ibid*., par. 32.
[378] *Ibid*., par. 27.
[379] See *ibid*. This practice is copied from Ofgem, see e.g. the Grain case, *supra* note 306.
[380] *Ibid*., par. 4.
[381] Thus, regard must be had to risks relating to price, volume and finance. In short, only financial risks are relevant. NMa thereby disregards, in principle, considerations concerning technical, operational and licensing risks. NMa Advice in the Gate case, *supra* note 370, par. 34.

as well, concluding that that risk *in casu* is sufficiently high.[382] Again, the NMa appeared to be heavily inspired by the exemption decisions rendered in the UK (see also the UK Gas Regulations, par. 7.2.1 above).[383]

The NMa held that the other conditions have also been met,[384] and accordingly granted the requested exemption. The exemption extends to the full capacity of the facility. The NMa considered that, taking all the underlying data into account, the relevant costs can be fully recouped within a time-span of 20 years (and not, as requested, for 25 years),[385] and accordingly approves the exemption for that time-frame.[386]

* Conditions
The NMa recommended imposing several instructions and conditions.[387] These put a strong emphasis on an effective, transparent and non-discriminatory UIOLI regime,[388]

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[382] NMa Advice in the Gate case, *supra* note 370, par. 37.
[383] Which is also admitted by the NMa, see its Advice in the Gate case, *supra* note 370, par. 43. The NMa also recalls that Gate will need to compete with LNG facilities in the UK. It mentions the interconnectors currently in place. In sum, the NMa appears to suggest that an exemption is also needed to ensure a level-playing field.
[384] Here, it is to be noted that the NMa views condition (1) ('(t)he proposed network or facility enhances (…) competition') as being the same as condition (5) ('(t)he exemption does not hinder competition'). This does not appear to be in line with the Commission's view that *does* consider these conditions to be different (see *supra* note 148).
[385] The NMa states that: '(t)he review as to which part of the capacity should be exempted, is highly interlinked with the question whether or not the investment could be carried out *without* the exemption' (see the NMa Advice in the Gate case, *supra* note 370, par. 78).
[386] Accordingly, Gate's request for an exemption lasting for 25 years was not fully endorsed. The NMa brings forward that the Minister of Economic Affairs should in any case not grant an exemption for a period below 15 years.
[387] See the NMa Advice in the Gate case, *supra* note 370, par. 87-88.
[388] The UIOLI requirements in Gate were as follows (see par. 28):
a) '(t)he exemption holder ensures that it, any legal persons associated with it, and the users of the LNG infrastructure shall not harm competition and comply with the Gas Act, excluding the provisions falling under the exemption;
b) (t)he exemption holder ensures that the allocation of regasification capacity to the users of the LNG facility improves, or does not deteriorate, competition on the internal gas market. [The NMa] informs the exemption holder annually of the parties with which it may, only after permission by [the NMa] enter into an agreement;
c) (t)he exemption holder applies an UIOLI regime that is efficient, transparent and non-discriminatory. A minimum of 1 month before the due date the capacity is released and notified to the secondary market;
d) (t)he exemption holder makes an annual evaluation of the allocation and information supply, which it reports to [the NMa];
e) (t)he exemption holder adjusts the allocation regime or the information supply if [the NMa] requests to do so; thus if the regime does not function, this can be adjusted in consultation with [the NMa];
f) (t)he exemption holder includes a provision in its contracts that it may amend the contract for the benefit of e.g. UIOLI or transparency;
g) (t)he exemption holder provides, without delay, all relevant information to the Minister [of Economic Affairs] or [the NMa];
h) (t)he exemption holder reports any changes as regards the information submitted during the exemption request, as well as changes as regards name and address of the exemption holder to the Minister [of Economic Affairs] and [the NMa]'.

without however specifying what such a regime should look like.[389] Lastly, any changes to the relevant circumstances could bring about a change in the exemption order.[390]

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.3.5 Eemshaven

* Introduction
Eemshaven LNG[391] (hereinafter: Eemshaven), a joint venture, wishes to construct a LNG regasification terminal, which is projected to supply gas for its two parent companies. Eemshaven requested an exemption from TPA for the full capacity[392] lasting for 20 years.[393]

* Assessment
In May 2007, the NMa laid down its decision.[394] The NMa held that Eemshaven met all the conditions. Since Eemshaven will supply to its parent companies only, no open season capacity allocation took place.[395] The NMa stated that this way of primary allocation was acceptable because the project is likely to benefit competition anyway.[396] The high amounts of LNG capacity available ensure sufficient choice for gas customers. In addition, the NMa submitted that Eemshaven would at least 'not worsen' competition, in effect using the same approach as the UK legislation that does not take the *increase* of competition as a condition.[397] The NMa held that the perception of the risk surrounding the investment was sufficiently high,[398] even though the exemption request submitted that the initial investments would be covered by funds of the parent companies – and not by outside investors.[399] The NMa accepted Eemshaven's wish to hold the highest degree of financial flexibility, leaving open the possibility for future loans. Eemshaven's submission that regulated tariffs would significantly add to the overall risk profile of the project was also accepted. An

[389] In any case, the UIOLI regime must be regularly reviewed. See *ibid*., par. 87d.
[390] If the relevant circumstances have been altered to the extent that they can no longer justify the exemption order, the NMa can use its competence to alter or revoke its exemption decision.
[391] Eemshaven LNG Terminal B.V. was a 50/50 joint venture of Conoco Phillips, Inc. and Essent N.V. However, as of the beginning of September 2007, Conoco Phillips stepped out of the Eemshaven project, see *De Volkskrant* 19 September 2007, 'Kolencentrale NUON van de baan'.
[392] The new facility is projected to have a capacity of 12 bcm per year.
[393] In its request, Eemshaven submitted that it complied with all the applicable rules, including Regulation 1228/2003 (OJ 2003, L 176/1). Whatever the merits of this statement, its reference seems to be irrelevant: Regulation 1228/2003 deals with electricity and not with gas.
[394] See the 'Verzoek tot ontheffing van gereguleerde derdentoegang overeenkomstig artikel 81h van de Gaswet', Advice by the NMa in the Eemshaven case, The Hague 2007. Available at: http://www.dte.nl/images/Advies%20Eemshaven%20openbaar_tcm7-104941.pdf (last visited 25 September 2007.
[395] See the final decision in Eemshaven, *supra* note 394, par. 17.
[396] *Ibid*., par. 21.
[397] See the UK legislation as discussed in par. 7.2.1.
[398] Final decision in Eemshaven, *supra* note 394, par. 36.
[399] *Ibid*., par. 39.

additional reason for granting a full exemption is that Eemshaven will have to compete with the UK's LNG terminals which have been granted such exemptions as well (see above in par. 7.2.5 – 7.2.7).[400]

* Conditions
The NMa stressed the importance of an effective UIOLI regime, laying down very similar – but slightly more detailed – conditions as in Gate.[401] These conditions, which refer mostly to transparency issues (and include the possibility to change the UIOLI regime even *after* the conclusion of the agreements), appear to be inspired by the conditions Ofgem usually lays down.[402] Moreover, the NMa held that the exemption decision would have to contain an explicit clause enabling the Minister and/or the NRA to amend and revoke the exemption under certain conditions.[403]

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.3.6 LionGas

* Introduction
LionGas B.V. (herinafter: LionGas)[404] wishes to construct a LNG regasification facility and requested an exemption for the full capacity lasting for 20 years.[405]

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[400] *Ibid*., par. 44.
[401] The UIOLI conditions are as follows (par. 28):
a) '(t)he exemption holder ensures that it, any legal persons associated with it, and the users of the LNG infrastructure shall not harm competition and comply with the Gas Act, including the exemption;
b) (t)he exemption holder ensures that the allocation of regasification capacity to the users of the LNG facility improves, or does not deteriorate, competition on the internal gas market. [The NMa] informs the exemption holder annually of the parties with which it may, only after permission by [the NMa] enter into an agreement;
c) (t)he exemption holder applies an UIOLI regime that is efficient, transparent and non-discriminatory;
d) (t)he exemption holder makes an annual evaluation of the allocation and information supply, which it reports to [the NMa];
e) (t)he exemption holder adjusts the allocation regime or the information supply if [the NMa] requests to do so; thus if the regime does not function, this can be adjusted in consultation with [the NMa];
f) (t)he exemption holder includes a provision in its contracts that it may amend the contract for the benefit of e.g. UIOLI or transparency;
g) (t)he exemption holder provides, without delay, all relevant information to the Minister [of Economic Affairs] or [the NMa];
h) (t)he exemption holder reports any changes as regards the information submitted during the exemption request, as well as changes as regards name and address of the exemption holder to the Minister [of Economic Affairs] and [the NMa]'.

Most of these conditions were already included in the Gate decision (*supra* note 370, par. 28), but here they are slightly more elaborate and detailed.
[402] See also the final decision in Eemshaven, *supra* note 394, par. 25, where the NMa explicitly refers to the situation in the UK.
[403] Final decision in Eemshaven, *supra* note 394, par. 90.
[404] LionGas is a subsidiary of 4Gas B.V., a company owned by the Carlyle Group.

* Assessment

In June 2007, the NMa rendered its decision.[406] It accepted LionGas' submission that regulated (and thus: annually changing) tariffs would create insecurity as to the level of future revenues.[407] LionGas' open season procedure was favourably received.[408] The NMa moreover held that LionGas sufficiently showed the intention to lay down effective UIOLI provisions,[409] even though LionGas stated that it did not perceive such arrangements in its contracts as being necessary ('niet direct de noodzaak ziet voor UIOLI afspraken in haar contracten').[410] LionGas stated that it perceives the risk as sufficiently high. It referred, *inter alia*, to the future risk that the NMa could make use of its competences in an unjustified way (!).[411] The NMa was not convinced that the risk was such that project would not be set up without the exemption, and advised the Minister to further investigate the risk involved.[412] Even if an exemption would be considered necessary, LionGas submitted insufficient information to decide on the duration of a possible exemption.[413]The NMa seemed equally unimpressed by LionGas' draft contracts, suggesting these looked like 'copies of another exemption holder in the UK'.[414] It stressed that these contracts did not sufficiently take into account the Dutch Gas Act.

* Conditions

If the Minister decides to grant the exemption, the NMa suggested to impose the same conditions as its decision in Eemshaven.[415]

* Minister of Economic Affairs

According to the *Energeia* of 26 July 2007, the Dutch Minister of Economic Affairs has approved to fully grant the exemption as requested.[416] Since this decision has not yet been published, there is unfortunately no possibility to examine it any further.

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[405] The facility is projected to have an initial capacity of 9 bcm. LionGas states that it will potentially increase this capacity to 18 bcm.

[406] See the 'Aanvraag LionGas B.V. voor een ontheffing van gereguleerde derdentoegang overeenkomstig artikel 18h Gaswet', Advice by the NMa, The Hague 2007. Available at: http://www.dte.nl/images/Advies%20LionGas%20openbaar_tcm7-104712.pdf (last visited 25 September 2007)

[407] Final decision in LionGas, *supra* note 406, par. 4.

[408] The open season took place under transparent and non-discriminatory conditions. See the final decision in LionGas, *supra* note 406, par. 22. The NMa also refers to an e-mail of LionGas, in which it states its 'intention to charge identical prices for identical services'.

[409] Final decision in LionGas, *supra* note 406, par. 25. Again, no actual UIOLI regime was under review.

[410] LionGas also states that it intends to include provisions in its contracts that avoid the hoarding of capacity. Still, it will depend on the negotiations with other parties whether or not such provisions will be included in the end. See the final decision in LionGas, *supra* note 406, par. 19.

[411] Final decision in LionGas, *supra* note 406, par. 36.

[412] *Ibid*., par. 42.

[413] *Ibid*., par. 67.

[414] The NMa perhaps referred to Dragon, which is also a subsidiary of 4Gas B.V. See the final decision in LionGas, *supra* note 406, par. 73.

[415] Final decision in LionGas, *supra* note 406, par. 27.

[416] See the *Energeia* of 26 July 2007, available at: http://www.essentendexfixeerprijs.nl/index.asp?id=54&nieuwsid=398 (last visited 25 September 2007).

* European Commission

The European Commission approved the exemption granted without laying down further conditions.

7.4 Italy

7.4.1 Regulatory framework

In August 2004, Italy implemented the second gas Directive via Act n° 239/04.[417] The basic rule on exemptions for new infrastructures is laid down in Article 1(17) of the Act.[418] The Act has been elaborated upon in a ministerial decree of 11 April 2006,[419] which provides more detailed substantive and procedural rules surrounding the exemption decision. However, there is little structure in the way the conditions of the second gas Directive are presented: they are completely interwoven with other requirements. Another particularity of the decree is that it states that Regulation 1775/2005 must apply vis-à-vis non-used capacity.[420] This is interesting, since this Regulation explicitly states it does not apply to new infrastructures falling under Article 22 of the second gas Directive.

In Italy, different from the UK and the Dutch exemption procedures, the competent Ministry (that of Economic Development)[421] appears to be more on the forefront than the NRA (the AEEG).[422] For instance, the Ministry's assessments are more detailed than those drafted by the AEEG. Still, it should also be noted that the conclusions reached by the AEEG and the competent Ministry have not differed yet.

7.4.2 Exemption policy

I have found no documents that explain Italy's exemption policy.

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[417] Act of 23 August 2004, n° 239 (*Gazzetta Ufficale* 13 September 2004, n° 215).

[418] Article 1(17) of Act n° 239/04 states that: '(i)f an investment is needed, directly or indirectly, in order to realise new infrastructures or interconnection between the national gas transport grid of a EU Member State and the Italian transport grid, or in order to realise new regasification LNG terminals or new underground storage facilities, or in order to increase the capacity of already existing infrastructures, insofar it allows the development of competition and of new natural gas supply sources, the newly established capacity may benefit from an exemption of the provisions regarding the right of Third Party Access. The exemption is to be granted, on a case by case basis, for a period of *at least 20 years* and for a percentage of *at least 80 %* of the new capacity, by the Ministry of Productive Activities [currently: The Ministry of Economic Development], after being advised by the Authority for Electric Energy and Gas [the AEEG, the Italian NRA]. With regard to the realisation of new interconnection infrastructures, the exemption is to be granted after consultation with the competent authority of the Member State concerned. The exemptions granted before the entry into force of the present Act within the meaning of the legislative decree of 23 May 2000, n° 164, shall remain in force and the rights deriving from Article 27 of the Act of 12 December 2002, n° 273, for the concessions issued within the meaning of the rules in force and for the authorisations issued within the meaning of Article 8 of the Act of 24 November 2000, n° 340. By decree, the Minister of Productive Activities defines, in every individual case, the principles and the procedures relating to the access to the national gas grid as laid down in this paragraph, with respect for any (future) Community measures in place [translation and italics added, TvdV]'.

[419] See the decree of 11 April 2006 by the Minister of Productive Activities (*Gazzetta Ufficale*, 12 May 2006, n° 109).

[420] See Articles 6, 7 and 8 of the Ministerial decree of 11 April 2006, *supra* note 419. See in particular Article 6(5).

[421] Hereinafter: 'the Ministry'. It was used to be called the 'Ministry of Productive Activities'.

[422] See for instance the Poseidon case (see par. 7.4.5 below), where the Ministry's review is lengthier and more detailed than the one carried out by the AEEG.

7.4.3 Rovigo

* Introduction
GNL Adriatico Srl requested a 25-year exemption in relation to 80% of the total capacity of its new LNG facility.[423]

* Assessment
In January 2005, the AEEG granted the request, holding that the remaining 20 % shall be made available to TPA.[424] In a very concise decision, the AEEG referred to general documents touching upon access issues. After a short assessment of the facts, it held that the project was not contrary to competition. Quite the contrary, the increased level of capacity could even have long-term pro-competitive results. The AEEG submitted that off-shore LNG terminals such as Rovigo are rare and much needed.

* Conditions
The AEEG did not lay down any specific conditions. It did, however, make a general reference to the need to 'respect' all the applicable rules and to the requirement that dominant parties may, in principle, not benefit from the exemptions.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.4.4 Brindisi

* Introduction
As in Rovigo, Brindisi LNG SpA[425] requested a 20-year exemption for 80 % of the capacity of its new LNG terminal.[426]

* Assessment
In April 2005, the AEEG laid down its decision, which was more detailed than in Rovigo.[427] When assessing the effects of competition, the AEEG referred extensively to the general characteristics of the Italian gas market. In particular, it took note of the dominant position of the national incumbent Eni SpA in the supply of gas.[428] The Brindisi project would introduce a new competitor, which the AEEG deemed beneficial for competition.[429]

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[423] Terminale GNL Adriatico Srl is a Joint Venture by Qatar Petroleum, ExxonMobil and Edison Gas.
[424] The assessment by the AEEG is available at: http://www.autorita.energia.it/docs/04/206-04.htm (last visited 25 September 2007).
[425] Brindisi LNG SpA is a 100 % subsidiary of BG Italia SpA.
[426] Brindisi was projected to have a send out capacity of initially 8, and later 16 bcm per year.
[427] For the assessment by the AEEG, see http://www.autorita.energia.it/docs/05/046-05.htm & http://www.autorita.energia.it/docs/05/046-05rt.htm (last visited 25 September 2007).
[428] The AEEG reiterates that, in 2003, Eni SpA had a 68 % share in the market of natural gas consumption in Italy. When an undertaking has a market share that surpasses 50 %, there is a presumption of dominance: see Case C-62/86, *AKZO* v. *Commission*, [1991] ECR I-3359, par. 60.
[429] Or, seen from a broader perspective: the Brindisi project would *strengthen* the position of an already existing competitor with a relatively low market share, *in casu* British Gas.

The AEEG admitted that it did not possess sufficient information to carry out a quantitative analysis of the effects of the project. However, this posed no great obstacle, since the project would have considerable benefits to the gas supply as a whole. In particular, the AEEG stated that this facility would link up the Italian market to infrequently used areas of production, referring in particular to Libya.

Therefore, the exemption was granted as requested.

* Conditions
In a very general reference, the AEEG held that Brindisi should abide by all the applicable rules. More specifically, the AEEG seemed to greatly value an effective functioning of the UIOLI principle, but left the actual implementation to the parties concerned.[430]

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

7.4.5 IGI (Poseidon)

* Introduction
The Interconnection Greece-Italy (IGI, or 'Poseidon')[431] project aims to realise a gas pipeline with a capacity of 8-10 bcm per year between these two countries. Poseidon is said to indirectly connect Italy with around 50% of the global gas reserves.[432] The parties concerned[433] requested an exemption for 100% of the initial capacity,[434] lasting for 25 years.

* Assessment
The assessment has been made in close cooperation between the Italian and Greek authorities. As the decisions did not differ substantively, the following examination is also to the Greek authorities' exemption order. In January 2007, the Italian Ministry laid down its decision. It explicitly emphasises the 'strategic relevance' of the project.[435] It considers that Poseidon has been earmarked a 'priority project' by European[436] and national authorities alike.[437] Poseidon could become a vital hub to

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[430] Nonetheless, this requirement has not been elaborated upon in much detail.
[431] IGI and Poseidon are used interchangeably here, although formally Poseidon is merely a part of the IGI project. However, it is the only relevant part for the purposes of this thesis.
[432] *Via* Greece and Turkey, Poseidon would connect Italy with Russia, the Middle-East and the Caspian Sea region.
[433] Namely Edison SpA and DEPA SA, which set up Poseidon Co as a Joint Venture.
[434] As the request concerned the initial capacity, it would apply to a maximum of 8 bcm per year.
[435] It refers mainly to the increased gas demand in Italy and the European Union. The extra supply which Poseidon would generate could accordingly aid competition in the long run.
[436] See Decision 1229/2003/EC (OJ 2003, L 176) and Decision 1364/2006/EC (OJ 2006, L 262). The latter refers to IGI as a 'project of European interest'.
[437] The Ministry refers to an agreement of 4 November 2005, in which Italy and Greece both recognized the high importance of the project.

meet demand from the West with supply from the East. The project is thus considered as a key project to strengthen the security of supply.[438]

Competition would benefit as a result of Poseidon, since there would be an extra possibility to supply the European internal market. Also, new undertakings would enter into the Italian market. And in a broader framework, the project could become a part of a future 'Mediterranean hub'.

The level of risk involved was also considered adequate, according to the analysis carried out by the Ministry. This risk assessment took into account operative, technological, economic, normative and even political aspects.

Accordingly, the exemption as requested was approved.

* Conditions
The Ministry laid down a number of conditions, most of them relating to the respect of all applicable rules. It refers explicitly to the requirements of transparency and non-discrimination. Also, the Ministry wishes to receive various pieces of information by the applicant. The most noteworthy condition is that any inverse flows of gas (from Italy to Greece) do not fall under the exemption.

* European Commission
The European Commission approved the exemption granted without laying down further conditions.

[438] It is interesting to note that the Italian Ministry is the only NRA referring to the Interpretation Note by the Commission; both Ofgem and the DTe/NMa do not do so.

8. COMPARISON OF THE EXEMPTION ORDERS

8.1 Introduction

As was shown in the previous paragraphs, all exemption requests have been granted by the NRA's (or, as in LionGas, finally by the competent Ministry). The Commission has accepted all these decisions up to now. The NRA's[439] do not seem to uphold a very strict review in their assessments vis-à-vis the conditions stipulated in Article 22 of the second gas Directive. Before concluding that a certain condition has been met, their reasoning is usually very concise. Sometimes, the NRA's do put forward a more elaborate analysis. But here, they mostly reason in a generic way, implying that any new facility will be likely to increase the security of supply and competition. Those assessments do not appear to be completely based on a thorough case-by-case analysis, which should have regard only to the specific facts and circumstances of the individual case.

Still, it must also be noted that the projects under review are similar in a number of respects. All the facilities will enlarge total capacity in the market. Moreover, they are believed to alleviate certain 'weak spots' in the immature Community gas sector. They do so by attracting supply from previously untapped sources,[440] or by creating cross-border interconnections, LNG terminals and storage facilities in depleted gas fields. Policy documents suggest that such activities are much needed. Another relevant similarity is that none of the applications had been (solely) made by an incumbent. Granting an exemption would in effect allow a new competitor to enter the market. Requests partially made by incumbents were arguably dealt with in a stricter way. This is indicated by the NMa's Gate decision, a project which involved the Dutch incumbent Gasunie. This was the only case in which the exemption was not fully granted as requested.[441]

In my view, even if the meticulousness of the examinations differs, I believe there is a consistent *rationale* underpinning the exemption decisions. But first, regard must be had to how the conditions are applied in practice.

8.2 The conditions

* Impact on competition & security of supply (1)
As any exemption impinges on a legal principle, one may reason that its foreseeable impact on competition ought to be thoroughly examined. However, the decisions do not clearly show such an assessment. The NRA's have little difficulty upholding that (at least in the long run) competition will benefit. In the same way, they easily accept that the exemption will increase the security of supply.[442] Both interests are seen as

[439] Namely Ofgem in the UK, the AEEG in Italy and the NMa (previously the DTe) in the Netherlands.
[440] See for instance the Brindisi project (see par. 7.4.4 above), which would attract gas from Libya.
[441] In this case, the applicant asked for an exemption for 25 years, but received an exemption for 'just' 20 years.
[442] According to the Commission, this criterion can only be satisfied if the application presents 'a comparative and quantitative analysis of the security of supply position', both with and without the

closely linked,[443] and are believed to benefit directly from an increase in total network capacity. Since new infrastructures will by their very nature increase capacity, both conditions are considered to be met with relative ease.

One may question if this approach is justified. If the security of supply and competition will *de facto* always benefit from an exemption, the principle of TPA could be derived of its *effet utile* with regard to new facilities. In that case, one could question why the conditions of Article 22 of the second gas Directive have been introduced in the first place. Admittedly, an effective UIOLI regime could prompt TPA in practice. However, that regime will only apply if and in so far there is unused capacity. If no available capacity exists, third parties are still unable to obtain access.

In addition, the Directive's condition that competition must be *enhanced* is not always taken into account. This is particularly clear from the UK and Italian legislation.[444] It is also visible in the Netherlands, as the Gate exemption decision shows. Here, the fact that the project would probably not *decrease* competition, was used as a sufficient argument that overall competition would *increase*. Therefore, the Dutch NRA seems to have adopted the same approach in practice.[445]

* Risk (2)
In the UK and the Netherlands, the assessment focuses not on the actual level of risk, but on the *perception* hereof. This means that an essentially objective examination including a quantitative analysis (as demanded by the Commission in its Interpretation Note, see par. 4.3.5) is replaced by a subjective one. Thus, if the applicant (the only relevant party in this respect) holds that it regards the level of risk as too high, this condition is met. As regards Italy, I was unable to find any genuine assessment regarding this condition.

* Ownership (3)
The requirement on unbundled ownership is satisfied with a formal *legal* separation of organisations. This can be achieved with relative ease, by creating different legal entities for the organisations in question. It is irrelevant if these continue to be *de facto* intertwined.

* Charges levied (4)
Obviously, any profit-seeking undertaking needs to benefit from its assets. Charges are thus levied, satisfying this condition.

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proposed infrastructure. This study must review the situation which is likely to occur if the investment would not take place. Lastly, any alternatives to this investment should be considered. See the Interpretation Note, *supra* note 144.

[443] See e.g. Ofgem final views in Grain, *supra* note 306, par. 2.34: 'as the project would enhance the overall level of gas supply, this should increase competition to the benefit of customers, a benefit that would otherwise not have existed'. Thus, competition is believed to be enhanced as a result of the increase in total capacity.

[444] See par. 7.2.1 & 7.4.1 above.

[445] See e.g. the NMa's assessment of Eemshaven, *supra* note 394.

* To the detriment of competition (5)
Although the Commission regards this condition to be different from condition (1) (see footnote 148 above), it is not treated as such by the NRA's: they suffice with a reference to condition (1).

* Conclusion
In practice, the conditions are relatively easy to meet. In this respect, one must have regard to the strong link that the authorities uphold between total network capacity, diversification, the security of supply, and the level of competition. An increase in capacity is thus most likely to improve all other factors as well. Hence, one may justifiably hold that the exception[446] has, in practice, become the rule vis-à-vis new gas infrastructures.

8.3 The NRA assessments

8.3.1 Approach
All three authorities adopt a pragmatic approach. For instance, the UK authority explicitly expresses its objective to establish the 'most favourable regulatory scheme'.[447] In this regulatory 'competition' with other countries,[448] there seems to be little reason to adopt a stringent approach vis-à-vis new infrastructures. The Dutch NMa seems to have adopted the same approach in its latest decisions, suggesting that *not* giving a full exemption would mean a competitive disadvantage vis-à-vis UK gas companies for the new gas infrastructures in the Netherlands.

In addition, the NRA's are quite lenient in their assessment of the conditions. First, while Ofgem used to assess whether or not the conditions were actually met,[449] nowadays it seems satisfied if the conditions are 'likely' to have been met.[450] The NMa adopts the same approach. Second, a lack of relevant data apparently poses few obstacles to conclude that the conditions have been met.[451] Similarly, Ofgem's interim decisions often state views without any supportive arguments or data. If no comments are made to these decisions, Ofgem will consider them as being correct in the final exemption order.

The lenient stance by the NRA's appears to be 'facilitated' by the possibility to revoke the exemption in the future. If the exemption proves detrimental to competition, the authorities still have a possibility to revoke it. This is most clear in the UK, where Ofgem has accordingly turned to the granting of exemptions for an indefinite period of time. Indeed, Ofgem stresses that it will constantly monitor the market in order to safeguard competition.[452] Be that as it may, an exemption should

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[446] Namely, the possibility of an exemption from TPA.
[447] See Ofgem initial views in the Dragon case, *supra* note 286, p. 23.
[448] Ofgem mentions the US as a key competitor in this respect.
[449] Ofgem final views in the Grain case, *supra* note 306, par. 1.12.
[450] See e.g. Ofgem final views in the South Hook case, *supra* note 276.
[451] See the NMa's assessments of BBL (*supra* note 362) and Gate (*supra* note 370).
[452] See in particular Ofgem's final views in the BBL case (*supra* note 362, par. 2.15), where it states that: '(i)n relation to competition in the gas supply market and, in particular, to the possibility of anti-competitive behaviour in the retail gas market, Ofgem monitors the retail gas market on a

not be awarded *because* there is a possibility to revoke the primary decision. It should be granted based on the merits of the case under review.

Another undesirable feature of the exemption orders is the fact that they pay little attention to transparency issues. Although there is a consensus that 'inadequate transparency is detrimental to competition',[453] the authorities often consider that there is no need for the undertakings to publish their tariffs.[454] However, transparent tariffs could for instance increase the effectiveness of the UIOLI regime.

Lastly, sometimes the authorities justify the exemption given by referring to general market circumstances, which are such that an exemption will not adversely affect competition. In Dragon, Ofgem considered that the UK market is sufficiently 'dynamic' that market foreclosure is unlikely to occur.[455] However, even if competition is already at a (relatively) high level, it should be considered that the application of TPA could have improved competition even more.

8.3.2 The necessity requirement

Since TPA is a principle, an exemption should only be awarded *if* and *insofar* it is necessary. This follows, *inter alia*, from the Commission's Interpretation Note.[456] The authorities should thus perform a necessity test. Such a review goes hand in hand with the principle of proportionality, since the alternative that is least harmful to competition must be chosen.

The cases show that the authorities do not conduct such a necessity test. See e.g. the Holford, Caythorpe and WINGAS cases, in which TPA was not deemed necessary *because* of the facility's relative small size. This conclusion was reached even with regard to the 12 % market share held by WINGAS, which was far greater than that of its competitors. More importantly, however, is that Ofgem appears to turn the necessity test 'upside down'. It examines whether there is a *need to allow third parties*, instead of a need to allow an exemption.[457]

In my opinion, the scope of the exemption (namely, the percentage of total capacity to which it applies) should also be in line with the necessity requirement. However, the British and Dutch authorities have only granted exemptions relating to the full capacity, without showing whether this is truly necessary to satisfy investor's needs. Even where the authorities brought forward a preference for additional capacity which

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continuing basis and will investigate market structures and conduct that may give rise to competition concerns'. Ofgem thus provides an assurance that it will keep on monitoring the level of competition in the relevant markets.

[453] Par. 15 of the conclusions of the 12th meeting of the Madrid Forum (*supra* note 210).

[454] In Grain, the applicants were not even need required to inform Ofgem of this data (*supra* note 306).

[455] Ofgem final views in the Dragon case (*supra* note 286), par. 2.18. This is particularly interesting, as Ofgem refers to – when assessing the requirement on the security of supply – documents warning for the (future) storages in gas supply (see the research document by JESS, *supra* note 260).

[456] The Interpretation Note by DG TREN of 30 January 2004, *supra* note 144, p. 2.

[457] See Ofgem final views in the Holford case, p. 3. When reviewing an exemption, 'Ofgem makes its assessment of whether the use of the facility by other persons is necessary for the operation of an economically efficient gas market in light of the current and likely future state of the gas markets in any point in time'.

could be made subject to TPA,[458] the refusals by the applicants to do so were finally accepted. Only the Italian authorities have granted exemptions relating to less than 100 % of the capacity. In my view, this approach corresponds to the status of TPA as a legal principle.

As to the period of time, most exemptions were granted for a period of between 20 and 25 years. This is a more or less standard duration of gas supply contracts (see par. 3.2 above), which were also accepted as such in the context of Article 81(3) reviews.[459] However, other examples are more worrisome. The last three UK exemptions (all covering gas storage facilities) were exempted indefinitely. TPA will thus only apply if a ground for revocation arises. Since these grounds are similar to the conditions on which the exemption has been granted in the first place, a possibility for revocation will not easily arise. This approach could foreclose facilities to competition for a long period of time. Another example is the Dutch assessment of BBL, in which the DTe stated that there was 'no real need' to limit the duration in question. One may justifiably question if this is a relevant – and justifiable – consideration when making an exemption to a stated principle. Indeed, the UIOLI principle still applies in these situations and could thus facilitate access. Nonetheless, indefinite exemptions mean that exclusivity is the point of departure, instead of access.

Finally, any possible alternatives to a full exemption lasting for many years are not duly considered (and usually not even mentioned) by the different authorities.[460] Their assessments accordingly lack a proportionality test that takes into account alternatives that would have the lowest possible impact on competition.[461]

8.3.3 Market definition

The market definitions differ strongly *per* NRA. As to the geographic market, the British authorities hold that the relevant geographic market is Great Britain. The Dutch authorities have regard mostly to the North-Western European market, since its main trading partners in gas are located in that region. In Poseidon, the Italian authorities even take the entire *European* market into account.[462] Although the Poseidon pipeline would arguably strengthen cross-border networks within Europe, it seems nonetheless a bit premature to already consider the entire EU as a single market for gas.[463]

As to the product market, an interesting definition is made by the UK as regards storage facilities. Such facilities are considered to be a part of the 'market of

[458] Such as Ofgem in the Dragon case (see par. 7.2.6 above).
[459] See e.g. the Gas Interconnector Agreement (see par 3.2 above), which was concluded for 20 years; and the *Viking Cable* Agreement (see par 3.2 above), which was concluded for 25 years.
[460] Such as a partial exemption, an exemption for a shorter period of time or by making use of the NRA's competence to lay down specific rules in a certain case. See e.g. the Dragon case, *supra* note …, in which a respondent put forward a request to publish the tariffs (par. 2.15 Ofgem final views); or the South Hook case, *supra* note …, in which a respondent argued that the exemption period should be shortened (par. 2.37 Ofgem final views).
[461] See for instance the possibilities that exist to give a partial exemption, see Articles 18, 19, 20 & 25(2), (3), (4) of the second gas Directive.
[462] See for instance AEEG's assessment of Poseidon (see par. 7.4.5 above).
[463] Especially considering all the supply difficulties in the gas sector (see chapter 2 above).

flexibility'.[464] This is arguably a very wide (and vague) concept, as a result of which undertakings will not easily attain a position of dominance. The other NRA's have not laid down any explicit reference to a particular product market.

A broad market definition makes the need for competition law intervention less pressing. The exclusivity of the supply agreements will be less able to foreclose the relevant market. Therefore, these market definitions seem to decrease the NRA´s incentive to uphold the principle of TPA.

8.3.4 Possible reasons for the adopted approach

I believe that the permissive approach by the NRA's can be partly explained by broader policy and even geo-strategic considerations. Indeed, many agree that there *is* a great need for more international networks and a greater diversification of energy sources and supply.[465] Therefore, new projects that strengthen cross-border interconnectivity or that introduce new supply possibilities (such as LNG) are likely to be favourably received. Basically, only new projects can genuinely aid the security of supply.[466] A short term decrease in competition in one section of the market is then seen as less harmful. Also, one must consider that new projects enlarge (the total amount of) capacity. As consumers will have more possibilities to satisfy their energy needs, an increase of competition is likely in the (already existing) non-exempted parts of the network.

Indications that a lenient approach to exemptions is justified can also be found in the underlying regulatory instruments.[467] For instance, the second gas Directive deems long-term contracts to be vital in the energy sector, even where this could hoard capacity and thus lower competition.

Although these general policy objectives are not always explicitly mentioned, I do believe they form a strong *rationale* for the NRA's lenient assessments.

8.4 The national authorities and the Commission

As shown above, the NRA's appear to be more lenient in their approach than suggested by the Commission's Interpretation Note. According to the latter, any exemption must follow an intricate case-by-case examination following 'very strict rules'.[468] In any case, the allocation of capacity may not 'perpetuate the current level of foreclosure observed on existing transit pipelines'.[469]

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[464] Ofgem final views in the Caythorpe case, *supra* note 319.

[465] See *The Economist*, 14 April 2007, p. 13-14: 'The way to see off a single overmighty supplier *is to diversify, with investment in a range of suppliers*, lots of transactions and pipelines "unbundled" from the big utilities [italics added, TvdV]'.

[466] Which is obviously an important policy objective (see chapter 2 above).

[467] For instance, see Article 18(3) second gas Directive. This provision stipulates that long-term contracts, as such, are not touched upon by TPA, if and in so far they comply with the general rules of competition. This is a further indication that there is much leeway for making an exception to the rules on TPA.

[468] The Commission, in its Report (*supra* note 28, par. 237), reiterates how the assessment ought to be performed: '(i)t is important, therefore, that the regulatory regime strike [*sic*] a balance between

Nevertheless, both the NRA's and the Commission seem to aim for the same (policy) objectives. With regard to new infrastructures, the Commission observes that 'substantial investment' is needed 'in new infrastructures such as transit pipelines, interconnectors and LNG-terminals'.[470] The Commission holds that exemptions can be important, especially if these target facilities that enable the entry of new competitors or the link-up with new sources of gas supply.[471] This also follows from the Commission's objective to stimulate the set up of so-called 'Trans European Energy Networks'.[472] This project obviously needs new infrastructures (especially cross-border interconnectors), which in turn will often be set up only if exemptions from TPA are granted.

As to the scope of the review performed by the NRA's, it must be stated that apart from its concise Interpretation Note, the Commission offers few rules or clarifications that could work as guidance.[473] In my view, the Commission could offer more help for national authorities by enacting additional guidelines. On the other side, the domestic authorities do not seem to apply the few criteria that the Commission did put forward. The AEEG is the only authority making reference to the Interpretation Note,[474] although it does not use it extensively either.

The fact that the Commission has (up until now) accepted all the decisions taken at least indicates that its own methodology does not lead to different conclusions. This suggests the influence of joint NRA-Commission policy objectives aiming for an increase of the security of supply and the diversification of gas supply sources. According to the NRA's, new cross-border interconnections could help to achieve these objectives.[475] The same line of reasoning can be found in the Commission's assessment of cross-border infrastructures in the framework of general competition law (see par. 3.2 above).[476]

However, there seem to be several differences. Various documents[477] confirm that the initial focus of the Commission lies on competition, while the NRA's often use the security of supply as their main starting point. Another difference is that the

providing the right incentives to build new capacity and ensuring that any long-term contracts do not have detrimental effects on competition'.

[469] *Ibid*., par. 257.

[470] *Ibid*., par. 236.

[471] See the 'Commission staff working document', *supra* note 233, par. 255.

[472] For additional information on the Trans European Energy Networks, see http://ec.europa.eu/ten/energy/index_en.htm (last visited 25 September 2007).

[473] Indeed, the very few rules (even non-binding ones) and recommendations by the Commission do not contain a comprehensive system on the basis of which exemption assessments can be made. Indeed, as the rules are incomplete, the Interpretation Note is scarcely used by the domestic authorities.

[474] The NMa's Eemshaven decision (*supra* note 394, par. 42) also mentioned the Explanatory Note, but this was only a quote of the exemption request.

[475] This is particularly apparent in the AEEG's review of Poseidon (see par. 7.4.5 above) and the NMa and Ofgem's assessment of BBL (see par. 7.2.4 above).

[476] See for instance the *Viking Cable* (*supra* note 54) and *European Night Services* (*supra* note 293) cases.

[477] Such as the exemptions granted under Article 81(3) EC, see above at par. 3.2. See also the various documents containing policy considerations such as the Commission Report, *supra* note 28.

Commission views the proportionality (between the requested exemption and the level of risk) as being 'decisive'.[478] I have found no indication that the domestic authorities apply such a proportionality test.

Lastly, there are some indications that the Commission will be stricter in its review in the upcoming years. See for instance Regulation 1775/2005, which states that 'the setting of fair rules for access conditions (…) can (…) be better achieved at Community level'. This shows that the Commission, while having respect for the principle of subsidiarity, seems inclined to get more involved in access issues.[479]

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[478] See p. 5 of the Interpretation Note, *supra* note 144.

[479] Recital 23 of Regulation 1775/2005 reads as follows: '(s)ince the objective of this Regulation, namely *the setting of fair rules for access conditions to natural gas transmission systems*, cannot be sufficiently achieved by the Member States and *can* therefore, by reason of the scale and effects of the action, *be better achieved at Community level*, the Community may adopt measures in accordance with the principle of subsidiarity, as set out in Article 5 of the [EC] Treaty. In accordance with the principle of proportionality, this Regulation does not go beyond what is necessary in order to achieve that objective [italics added, TvdV]'.

9. CONCLUSION

For the EU, the gas sector is, and will be, of prime importance. The European Institutions have adopted a policy to stimulate liberalisation in order to create a competitive internal gas market. This policy is considered to be vital to secure the supply of gas in the upcoming years.

Competition will only thrive if third parties can have access to the gas infrastructures. The general competition rules are able to facilitate access in several situations. In particular, they can open up markets by tackling legislation and agreements which have discriminatory effects. However, they are probably unfit to make a balanced enough appraisal between all the different interests that must be taken into account within the EC gas sector.

As a consequence, sector-specific rules were introduced. The first gas Directive attempted to improve competition in the gas sector, but could not fully open up the sector. Therefore, the second gas Directive was introduced, bringing forward regulated TPA as a key principle. It required the Member States to set up an effective access regime and to regulate access tariffs. The joint application of both general and sector-specific competition rules is capable of significantly strengthening effective access in the gas sector.

TPA brings many advantages, setting access as the standard and leaving little room for exclusivity. Notwithstanding these benefits, TPA may also have undesirable effects. In particular, it could lower incentives for financiers to invest in new gas infrastructures since it makes future revenues less certain. As a consequence, such infrastructures may not receive finance, and could perhaps not be built at all.

Article 22 of the second gas Directive aims to tackle this issue. This provision enables domestic authorities to exempt new infrastructures from TPA if a number of conditions have been met. These conditions require, *inter alia*, that the exemption must strengthen competition and the security of supply. Moreover, the project's financial risks must be so high, that the infrastructure would not be build without the exemption. According to an Interpretation Note by the Commission,[480] exemptions may only be granted in exceptional circumstances. Therefore, the conditions of Article 22 of the second gas Directive must be strictly upheld.

However, in practice, the national authorities consider the conditions to be relatively easily met. The domestic authorities seem rather lenient in their assessments of the exemption requests. They seem to directly link an increase in capacity to an enhanced security of supply, and even to an improved competition regime (albeit in the long term). The conditions are interpreted in such a way, that arguably *any* new gas infrastructure is likely to benefit from an exemption.

This approach is perhaps not all too surprising. Some conditions in the second gas Directive will by their very nature be met by a new infrastructure; especially since it will boost overall network capacity. Also, one could argue that the approach adopted

[480] See the Interpretation Note, *supra* note 144.

by the domestic authorities greatly encourages the set up of new infrastructures, which could help to achieve the challenges ahead in the gas sector.

In addition, the NRA's seem to have a presumption that capacity increases and more interconnections are beneficial for the gas sector as a whole. The same approach was used by the Commission in the context of the general competition rules; for instance in its review of the Gas Interconnector Agreement (see par. 3.2 above). Moreover, it corresponds to the Commission's policy objective of introducing more cross-border energy networks.

Moreover, the NRA's lenient stance is understandable if one considers that almost all of the exemption requests are made by new competitors. Their entry into the market should be encouraged, since it decreases the market power held by the incumbents.

Still, some aspects of the exemption orders are hardly convincing. As TPA is a principle, exemptions thereto should only be granted *if* and *insofar* they are necessary. Holding otherwise could *de facto* harm TPA's status as a legal principle when it comes to new infrastructures. Nevertheless, the NRA's do not seem to pay much regard to whether or not such a necessity requirement has been satisfied. It is uncertain if the NMa's reluctance to give a positive exemption advice in the LionGas case indicates that it may be getting more stringent in its assessments.[481]

Up to this moment, all the exemption applications have been granted by the NRA's and approved by the Commission. If these decisions can be considered representative for other future projects, TPA seems to have become the *de facto* exception rather than the principle with regard to new infrastructures. However one may value this development, it may be logic within the framework of a sector which has not fully matured yet. In the upcoming years, more facilities and interconnections are needed to create a truly European gas market and to strengthen the security of supply. If exemptions are truly indispensable to set up such infrastructures, then the principle of TPA must, in my view, yield for overriding policy interests.

In sum, the general competition and the sector-specific rules can work in tandem to establish a liberalised gas market, without losing track of major concerns such as the security of supply. However, achieving this result is anything but easy. Only time will tell if this interwoven regulatory system can succeed in striking a fair balance between all the interests at stake.

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[481] NMa decision in the LionGas case, *supra* note 406.

ANNEX I: ABBREVIATIONS

AEEG	Authorità per l'Energia Elettrica e il Gas (Italian Energy Market Regulation Authority)
AG	Advocate General
AG(2)	If preceded by a company name: Aktiengesellschaft (Public Limited Company under German Law)
BBL	Bacton Balgzand Line
Bcm	Billion cubic meters
BG	British Gas
BP	British Petroleum
B.V.	Besloten Vennootschap (Limited Company under Dutch law)
CBB	College van Beroep voor het bedrijfsleven (Dutch Administrative Court for Trade and Industry)
Cf.	*Confer* (compare)
CFI	Court of First Instance of the European Communities
CMLRev	Common Market Law Review
DG	Directorate General
DTe	Directie Toezicht Energie (Dutch Energy Market Regulation Authority)
DTI	Department of Trade and Industry (United Kingdom)
EC	European Community
EC(2)	If preceded by a number: Treaty establishing the European Community, as amended by the Nice Treaty
EC CPN	European Community Competition Policy Newsletter
ECJ	Court of Justice of the European Communities
ECR	European Court Reports
ECLR	European Competition Law Review
Ed.	Editor
EDF	Electricité de France
Eds.	Editors
EFD	Essential Facilities Doctrine
EMRA	Energy Market Regulation Authority
ERGEG	European Regulators' Group for Electricity and Gas
EU	European Union
GDF	Gaz de France
GmbH	Gesellschaft mit beschränkter Haftung (Limited Company under German law)
GTE	Gas Transmission Europe (the association of European gas network operators)
GtS	Gastransport Services (the Dutch gas transmission system operator)
GU	Gazzetta Ufficiale (The Italian Official Gazette)
GWh	Giga Watt hour
IELTR	International Energy Law and Taxation Review
IFLRev	International Financial Law Review
IGI	Interconnessione Grecia-Italia (Interconnection Greece-Italy)
IP	Intellectual Property
JERL	Journal of Energy and Natural Resources Law

JESS	Joint Energy Security of Supply Working Group (United Kingdom)
LNG	Liquefied Natural Gas
Mcm	Million cubic meters
NMa	Nederlandse Mededingingsautoriteit (Dutch competition authority)
NRA	National Regulatory Authority
nTPA	Negotiated Third Party Access
N.V.	Naamloze Vennootschap (Public Limited Company under Dutch law)
nyr	Not yet reported
OAO	Открытое Акционерное Общество (‘Open Stock Society’, Public Limited Company under Russian Law)
Ofgem	Office of Gas and Electricity Markets (UK Energy Market Regulation Authority)
OGLTR	Oil and Gas Law and Taxation Review
OUP	Oxford University Press
Par.	Paragraph
rTPA	Regulated Third Party Access
SpA	Società Per Azioni (Public Limited Company under Italian law)
TAG	Trans-Austria Gasleitung
TPA	Third Party Access
TREN	Directorate General of Transport and Energy (European Commission)
UIOLI	‘Use It Or Lose It’
UK	United Kingdom of Great Britain and Northern Ireland
ULR	Utilities Law Review
US	United States of America

ANNEX II: BIBLIOGRAPHY

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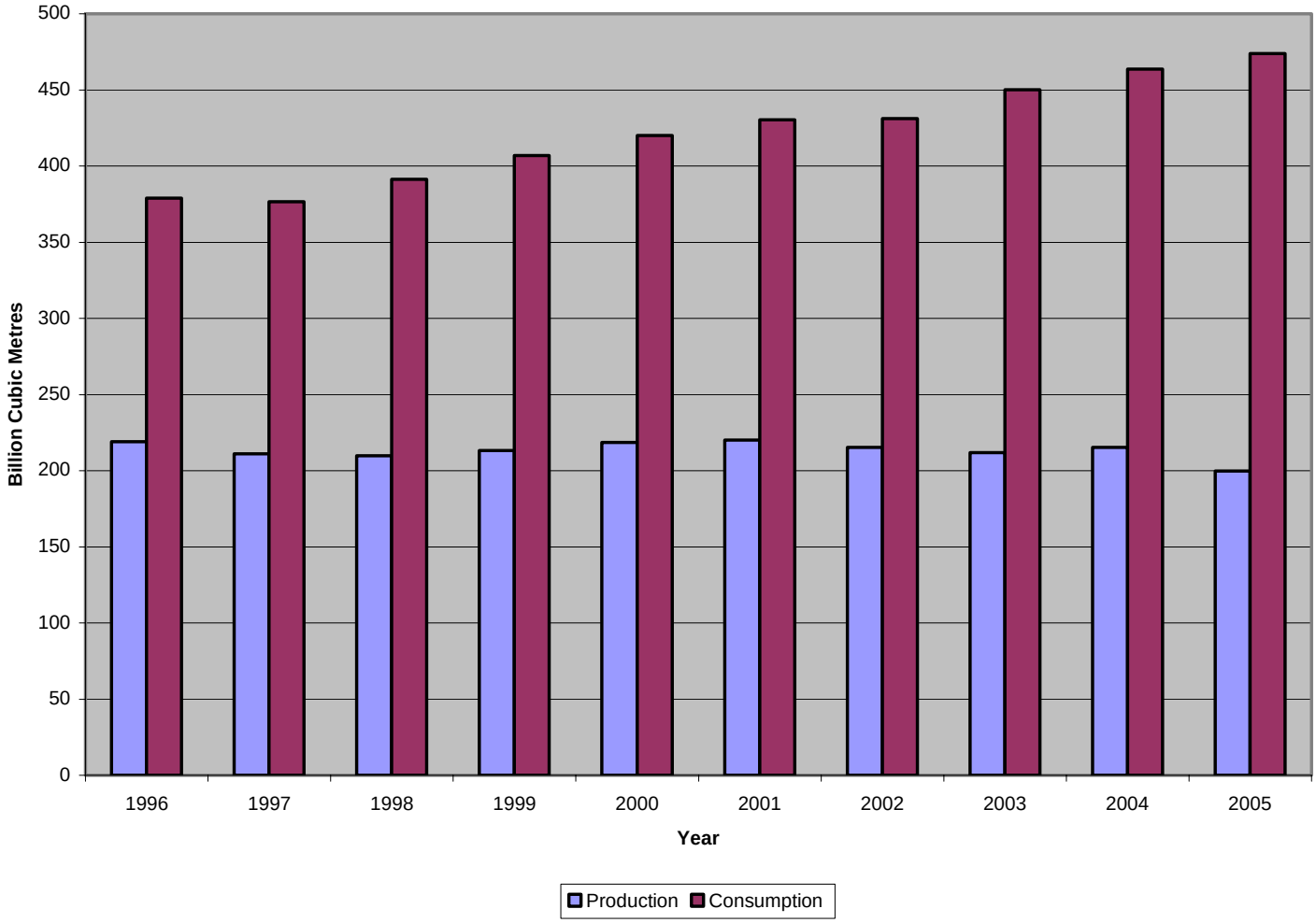
ANNEX III: GAS PRODUCTION AND CONSUMPTION

The EU-25 annual production and consumption of natural gas.



Source: Statistical Review of World Energy 2007, BP.

ANNEX IV: OVERVIEW UNDERTAKINGS REQUESTING EXEMPTION

Overview undertakings requesting an exemption from TPA

Name project	Undertaking	Subsidiary of or Joint Venture of
The United Kingdom		
BBL	Initially: Gastransport Services	Nederlandse Gasunie
	Later on: BBL Company	Nederlandse Gasunie / E.ON Ruhrgas / Fluxys BBL
South Hook	South Hook LNG Terminal Company Ltd	Qatar Petroleum / Exxon Mobile
Dragon	Dragon LNG Limited	British Gas Group / Petronas / 4Gas (subsidiary of Carlyle Group)
Grain	Grain LNG Limited	British Petroleum / Sonatrach
Caythorpe	Caythorpe Gas Storage Limited	Warwick Energy
Holford	INEOS Enterprises Limited	INEOS
WINGAS	WINGAS Storage UK Limited	ZMB Gasspeicherholding / WINGAS (Joint Venture of Wintershall / Gazprom)
The Netherlands		
BBL	Initially: Gastransport Services	Nederlandse Gasunie
	Later on: BBL Company	Nederlandse Gasunie / E.ON Ruhrgas / Fluxys BBL
Gate	Gate terminal	Koninklijke Vopak / Nederlandse Gasunie
Eemshaven	Eemshaven LNG	Essent
LionGas	LionGas BV	4Gas (subsidiary of Carlyle Group)
Italy		
Rovigo	GNL Adriatico Srl	Qatar Petroleum / ExxonMobil / Edison Gas
Brindisi	Brindisi LNG SpA	British Gas Italia
Poseidon	Poseidon Co.	Edison / DEPA

ANNEX V: OVERVIEW EXEMPTION DECISIONS

Overview exemptions to TPA granted by National Regulatory Authorities on the basis of Article 22 of Directive 2003/55/EC - July 2007

Name project	Type of project	Initial Capacity (bcm/year)	Projected capacity (bcm/year)	Exemption requested (%-years)	Exemption granted (%-years)
The United Kingdom					
BBL	Interconnection	8	17	100 % - 16 years	100 % - 16 years
South Hook	LNG terminal	10,5*	21*	100 % - 25 years	100 % - 25 years
Dragon	LNG terminal	6*	6*	100 % - 20 years	100 % - 20 years
Grain	LNG terminal	4,5*	10*	100 % - 20 (initial) / 25 (final) years	100 % - 20 (initial) / 25 (final) years
The Netherlands					
BBL	Interconnection	8	17	100 % - 16 years	100 % - 16 years
Gate	LNG terminal	8*	16*	100 % - 25 years	100 % - 20 years
Eemshaven	LNG terminal	12	12	100 % - 20 years	100 % - 20 years
LionGas	LNG terminal	9	18	100 % - 20 years	100 % - 20 years
Italy					
Brindisi	LNG terminal	8*	16*	80 % - 20 years	80 % - 20 years
Rovigo	LNG terminal	8*	8*	80 % - 25 years	80 % - 25 years
Poseidon	Interconnection	8	10	100 % - 25 years	100 % - 25 years

* Send out capacity

		Storage capacity (GWh)	Inject-ability (GWh/day)	Withdraw-ability (GWh/day)	Exemption requested (%-years)	Exemption granted (%-years)
*Caythorpe***	Gas storage facility	3000	90	120	100 % - no limit	100 % - no limit
*Holford***	Gas storage facility	1758	-***	75	100 % - no limit	100 % - no limit
WINGAS **	Gas storage facility	7650	45	85	100 % - no limit	100 % - no limit

** UK project *** Data not available