



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.9.2002
COM(2002) 488 final

2002/0219 (COD)
2002/0220 (COD)
2002/0221 (CNS)

**COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN
PARLIAMENT AND THE COUNCIL**

The internal market in energy: Coordinated measures on the security of energy supply

Proposal for a

**DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
concerning the alignment of measures with regard to security of supply for petroleum
products**

Proposal for a

**DIRECTIVE OF THE EUROPEAN PARLIAMENT AND THE COUNCIL
concerning measures to safeguard security of natural gas supply**

Proposal for a

**COUNCIL DIRECTIVE
repealing Council Directives 68/414/EEC and 98/93/EC imposing an obligation on
Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum
products, and Council Directive 73/238/EEC on measures to mitigate the effects of
difficulties in the supply of crude oil and petroleum products**

Proposal for a

**COUNCIL DECISION
repealing Council Decision 68/416/EEC on the conclusion and implementation of
individual agreements between governments relating to the obligation of Member States
to maintain minimum stocks of crude oil and/or petroleum products and Council
Decision 77/706/EEC on the setting of a Community target for a reduction in the
consumption of primary sources of energy in the event of difficulties in the supply of
crude oil and petroleum products**

(presented by the Commission)

**COMMISSION COMMUNICATION TO THE EUROPEAN PARLIAMENT AND
THE COUNCIL**

The internal market in energy: Coordinated measures on the security of energy supply

COMMISSION COMMUNICATION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

The internal market in energy: Coordinated measures on the security of energy supply

1. COMPLETION OF THE INTERNAL MARKET IN ENERGY

In accordance with Article 14 of the EC Treaty, the internal market comprises an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured. To help meet this prime objective of the Treaty of Rome, the European Community is responsible for introducing, among other things, the requirements needed to complete the internal energy market which will make it possible to gradually open up the market in order to make the energy sector more competitive. The internal market is also based on the need for solidarity between the Member States of the European Union, more especially in the essential sectors of energy supply which are gas, oil and electricity.

Achievements

Since the beginning of the 90s, the Community has adopted a series of measures in the form of directives which are helping to establish the internal market in natural gas and electricity. The achievement of this objective should make the economy of the European Union more competitive and lead to a significant reduction in consumer prices.

The process of opening up the market in natural gas and electricity to competition is governed by rules relating to access to resources and transport networks, competition and transparency which should protect the countries of the European Union against disruption of their internal supplies. This regulatory framework is essential and will make it possible to avoid crises such as that which hit California in 2000 when it experienced serious disruption of electricity supplies.

Of major importance for the proper functioning of the internal energy market is the interlinking of networks since it plays a fundamental role in the flexibility of supplies. The lack of network infrastructure, including maintenance of the quality of supplies (stability of networks) could hinder the integration of national markets and thus restrict security of supplies. On 20 December 2001, the Commission proposed a set of new measures relating to energy infrastructures aimed at optimising the use of existing gas and electricity infrastructures and encouraging the construction of new infrastructures of European interest. As stated in the conclusions of the Barcelona European Council, the existence of an adequate and effective network of energy infrastructures will ensure the proper functioning of the internal market, while guaranteeing greater security of energy supplies.

Although there is more competition in the oil market within the European Union than in the market for other energy products, further efforts will still have to be made to achieve a more open market. In the Green Paper on security of energy supply adopted by the Commission in November 2000, the Commission noted that obstacles remained on the markets downstream, more specifically distribution. Although the significant differences in prices of petroleum products between the Member States do not in themselves constitute a breach of competition rules, they nevertheless indicate that the integration of markets is still incomplete. Moreover,

surveys at Community level and at the level of the national competition authorities have been carried out and sanctions have even been imposed on certain oil companies.

The opening up of the oil market, particularly to new operators, will help to establish the conditions for healthy competition which in turn will help to ensure regular internal supplies for consumers, even if this market will remain exposed to the risks associated with increased external dependence.

An ongoing process

The numerous Community initiatives to create an internal market in gas, as well as various activities to open up the oil market, are helping to establish fair competition and to strengthen the internal security of energy supplies.

On the question of energy supply, the Green Paper on the security of energy supplies highlighted a paradox, however: at the very moment when the European Union is acquiring the most integrated internal energy market in the world, this success has not been accompanied by the necessary coordination of measures guaranteeing security of external supplies, whether oil or natural gas.

The Green Paper showed up the structural weaknesses in external energy supplies in the European Union and its vulnerabilities in geopolitical, economic and social terms. The European economy is based mainly on fossil fuels which represent four-fifths of energy consumption, and two-thirds of this is imported. This vulnerability will become more pronounced in the future with energy imports which could rise to 70% of total requirements in thirty years time, or even up to 90% for oil if nothing is done to reverse this trend.

As regards oil, the rules of the International Energy Agency (IEA) and Community legislation provide for the maintenance by States of security stocks of crude oil and petroleum products as well as possibilities of anti-crisis measures. However, these mechanisms, which were introduced in the early 70s, are no longer suited to the oil market which has undergone numerous changes as the internal market in energy has become increasingly integrated. The Community measures are characterised by a lack of solidarity between Member States which is not compatible with the objectives of an internal market, since energy crises affect all EU countries. More fundamentally, there is no Community decision-making power to dispose of oil stocks on the market. As regards the IEA, the basic elements of the 1974 Treaty are no longer applied. Other provisions have been put in place, but these require the unanimity of the 26 participating countries. The mechanisms have become obsolete in as much as they provide for joint action by all the Member States only if there is a physical disruption of oil supply. There is no legal framework for the coordination of action in the event of a threat of a physical disruption, which would increase oil prices beyond what is reasonable.

The Community legislation on oil stocks, the first directive of which dates from 1968, and the IEA set up in 1973 were an important first step in the process of better management of external energy dependency. It must however be acknowledged that these mechanisms, the underlying philosophy of which has not been subjected to detailed scrutiny for thirty years, are no longer suited to the present energy situation. They were put in place at a time when the internal market in energy was still in its infancy. At that time there was very little in the way of intra-Community electricity exchanges or interdependence of the electricity system.

Given this situation, the Commission has already announced, in its Communication on oil supplies of 4 October 2000, its intention to examine ways in which strategic oil stocks could be made more effective by placing their use on a Community footing.

The European gas industry, for its part, has so far been effective in ensuring security of supply. The fact that the gas companies were partly or wholly-owned by the public authorities and that these dominant companies controlled all infrastructures and regulated supply and demand meant that there was no need to draw up common rules to guarantee gas supplies.

In the new internal market in gas which requires the industry to restructure in order to create an integrated market in which new companies will emerge in an increasingly competitive environment, there will no longer necessarily be a single player which will assume overall responsibility for security of supply. The question is all the more urgent as dependency on gas imports will increase significantly in the decades to come. Security of supply in the gas sector therefore cannot be left entirely to the industry which is itself dependent on its external suppliers from an extremely limited number of supplier countries.

At the fifth meeting of the European forum for the regulation of the gas sector, which brought together national regulators, Member States, economic operators in the gas sector and the Commission in Madrid in February 2002, it was moreover agreed that *in the new regulatory environment for the internal gas market, which is characterised by a multitude of players and the unbundling of the activities of the integrated gas companies, security of supply can no longer be considered the responsibility of a single party. A new chain of responsibilities concerning security of supply and the planning of infrastructures between the public authorities and the various market players must therefore be established in order to guarantee certainty in this connection. Responsibilities must be assigned to the various players in a clear and appropriate manner on the basis of their role.*

It is therefore necessary to provide for harmonised measures which will guarantee unified and coordinated action with regard to the security of supply of gas, in particular measures with regard to storage and infrastructure. Stockpiling and infrastructures play an essential role in gas supplies in the European Union and in the functioning of this market, both under normal market conditions and in crises. These measures will "accompany" the process of opening up the EU market in gas in order to ensure its proper functioning.

A Community process

The European Union is making steady progress towards the completion of the internal market in energy, which will be the largest, integrated and most open regional market in the world. In this liberalised market, the European Union has an important part to play in coordinating and supporting the Member States with regard to security of supply. The task is to ensure the proper functioning of the market and in this context to guarantee a sufficiently high level of security of supply.

Measures to improve the security of supply of oil and gas will have little or no effect unless they form part of the more general framework of the internal market in energy. These measures will not have a positive impact if they are, for example, thwarted by price manipulation, or if access to the transport networks is limited. The internal market is therefore the necessary basis for measures with regard to security of energy supplies.

Conversely, it is not possible to construct an internal market in energy if this objective is not accompanied by harmonised rules on security of supplies. The power cuts which severely

affected California in 2000 clearly bear witness to this. These cuts were due not to inadequate rules on security of supply, but to a process of electricity market liberalisation which was not accompanied by adequate rules to guarantee a sufficient security of supply level. In the normal competitive environment, the (short-term) priority of companies has been to maintain or increase their stake in the Californian electricity market. In doing this, they did not make the (medium or long-term) investments which would have been necessary to guarantee a sufficient supply for all consumers.

Measures to improve oil and gas supplies must therefore be based on the proper functioning of the internal market, and the internal market in energy is itself based adequate measures to guarantee the security of supplies. It must be noted that national laws on the security of oil supplies, which are not adequately coordinated at EU level could lead - and indeed have led - to distortions in the internal market in petroleum products.

These measures with regard to security of supplies must form part of a competitive natural gas and oil market and there must be no discrimination as regards the rights and obligations of companies in the sector. The obligations regarding the security of energy supply must therefore be clearly defined, transparent, non-discriminatory and controllable. They will not go beyond what is strictly necessary to overcome potential supply difficulties. Thus, they will cause the least possible disruption in the functioning of the internal market.

There is therefore a clear need to define a **Community framework** for the implementation of measures to ensure security of external energy supplies which will place minimum restrictions on competition. These rules will clearly set out the roles and responsibilities of the various players in the oil and gas market as regards security of supplies. Any lack of clarity as regards these roles and responsibilities will increase the risk of an energy supply crisis.

According to the principle of subsidiarity, these rules will form a framework, the implementing arrangements for which should be left to the Member States to adopt. They will be implemented in close cooperation with the industry.

It is important to note that the construction of an internal market in oil cannot be considered without the development of other sources of energy, in particular the natural gas market. Oil and gas are two products which are part of the same energy market. They can also be substituted for each other and are in competition with each other as far as some uses are concerned. Furthermore, gas prices are largely indexed to oil prices. These two energy sources are therefore closely linked.

2. ENERGY DEPENDENCE IN THE EUROPEAN UNION

The energy situation in the European Union

The European economy is based mainly on fossil fuels (oil, gas, coal) almost two-thirds of which are imported. These fuels represent 80% of energy consumption in the European Union. If nothing is done, in 20 to 30 years' time, they will play an even bigger role in the European energy balance and imports will amount to 70% of overall energy needs. The Union's external energy dependence could even reach 90% for oil and 70% for gas by 2020. It should also be noted that 90% of oil is currently transported by sea.

The risks associated with the fact that the Union is, structurally, highly dependent on imported fossil fuels are further exacerbated by the political instability prevailing in many producer countries. It has been seen on a number of occasions that the events in the Middle East or

certain political crises which have destabilised the political power in place in producer countries could put the energy market under severe pressure. This pressure leads if not to the actual physical disruption of supplies, then at least to sharp fluctuations in oil prices which inevitably affect economic growth in the consumer countries.

It is important to note at this point that the objective, given a globalised economy, is not in itself to maximise energy autonomy or to minimise dependence, but to take account of the risks inherent in such dependence when they reach worrying levels.

The question of security of energy supplies is a vital one for the European Union. In spite of a lessening of the oil burden on our economies, brought about by successive crises, oil remains a vital economic component in the Member States. In 2004, the European Union will consume almost 20% of world oil production.

The situation in the transport sector is very revealing in this connection. A captive market 98% dependent on oil (which is equivalent to 67% of overall demand for oil), this sector accounts for an increasing share of energy demand. The energy intensity of the sector increased by 10% from 1985 to 1998. Growth in the transport sector is likely to continue at an annual rate of 2% over the next decade.

Gas, for its part, has become a broad spectrum energy vector penetrating all sectors of energy consumption, including electricity production and combined heat and power production but also, albeit still at an embryonic stage, transport. By 2020-2030, almost half of all electricity will be produced from natural gas. Although natural gas appears today as the diversification product which is essential for a healthy balance in energy consumption, capable of reducing CO₂ emissions, its rapid growth on certain markets such as electricity could give rise to fears of the emergence of a new structural weakness in the European Union in terms of external dependence.

Economic studies have estimated that an increase of \$10 in the price of a barrel of crude oil is likely to reduce economic growth in the industrialised countries by around 0.5%. For developing countries, such a price increase would reduce economic growth by around 0.75%. It must also be borne in mind that the impact of oil prices on economic growth is not linear: sudden unexpected and very sharp increases in prices are likely to cause much greater damage to the economy than the estimates given above. It is moreover interesting to note that since 1973 significant reductions in economic growth in the United States and Europe have all been preceded by sudden sharp increases in the price of crude oil.

Instability in energy supplies, whether it is due to market volatility, relations with supplier countries or a particular chance event, could lead to social disruption. This is likely to result in social demands, a backlash from business, even conflicts. It should be recalled that the first two oil crises contributed to a sharp increase in unemployment. In this situation, it would be impossible to attempt to construct an internal market between the economic operators whose objective is to increase the efficiency of the European economy if such a market is not based on principles which guarantee social cohesion. An example of this is the road hauliers' strike which affected many countries in Europe in the autumn 2000, following a sharp increase in oil prices. This resulted in major fiscal disruptions, insofar as Member States tried to counterbalance the effects of the energy price increases on economic sectors through uncoordinated reductions in taxation. These individual initiatives are a serious obstacle to the proper functioning of the internal market, in particular for a common and coordinated transport policy.

As stated at the Barcelona European Council, an integral part of establishing the internal market in the European Union is ensuring security of energy supplies. This objective will help to ensure, for the welfare of citizens and the proper functioning of the economy, the constant

physical availability of energy products on the market at a price which is affordable for all consumers, whether private or industrial.

The risks

In this situation of energy dependence, the European Union has to face up to two types of risk in the energy field:

- Physical risks

Permanent physical disruption of supply may result from the exhaustion and abandonment of an energy source. It is possible that in the long term the European Union will have no more significant Community resources of oil and gas at a reasonable cost. Thus, experts estimate that North Sea oil reserves should gradually run out by 2030-2050. Mention should be made in this connection of the example of coal, the production of which is gradually being abandoned by the Member States.

The European Union is also very vulnerable to a risk of temporary physical disruption of supply which may result from serious accidents affecting transport and storage infrastructures, whether within or outside the Community, which are important for the security and continuity of Community supplies. Moreover, events of, for example, a political and/or military nature in an oil production or transit region may at any time cause the temporary physical disruption of world oil supplies.

- Economic risks

An economic risk is posed by the volatility of the markets, which can be caused in particular by a threat of a physical disruption of supplies.

An analysis of recent energy market trends shows that, apart from physical disruption of supplies, there is another cause for concern: speculative movements in anticipation of a potential disruption of supplies. The general perception by operators of a risk of a potential future disruption leads to panic buying even when supply and demand are apparently in balance. The result is sharp price rises which directly affect business costs and the purchasing power of private consumers. These uncertainties in the international market are likely to jeopardise growth in the EU economy at any time, with serious consequences for employment.

During the recent period between 1998 and 2000, when there was a slight reduction in oil supplies of 3%, there was a very sharp increase in prices from \$10 a barrel up to - at certain times - \$37 a barrel. Taken over a year, such a price increase may be estimated to add some €100 billion to the oil bill.

The main risk with regard to energy today is economic. Although it cannot be totally ruled out, the physical risks of disruption of supply is only likely to come about as a result of exceptional circumstances such as major conflict in an oil- or gas-producing area. The economic risk has therefore become the real issue, since price rises have a direct effect on business costs and the purchasing power of private consumers.

3. LACK OF ADEQUATE MEANS OF ACTION

It is vital that the energy dependence of the European Union should be managed as effectively as possible since this will contribute to the construction of the internal energy market.

Where energy demand management is concerned, beyond making mere proposals to encourage or exchange good practice, the Commission has already made regulatory proposals, some of which have been adopted by the Council and the European Parliament, in particular the Directive on the production of electricity from renewable resources, the Directive on energy savings in buildings and the biofuels package. Implementing these texts will bring about a saving in terms of consumption of conventional energies of around 10% in the next few years and make it possible to limit the upward trend in the EU's energy demand as a result of increased consumption in the domestic and tertiary sector.

On the demand side, the debate on the Green Paper on security of energy supply has shown that the European Union has no scope for influencing oil and gas supply conditions. It brought out the dangers for the European Union of supply disruption and showed up the structural weaknesses of our energy supplies and their geopolitical, economic and social vulnerability. Even before the events of 11 September 2001, it highlighted the need to include questions relating to the safety of installations in the concept of security of supply.

In accordance with the position taken by the EU at the recent Johannesburg World Summit on Sustainable Development, in this context, the indigenous renewable energy production of a given Member State has a positive impact on the security of energy supply and reduces the quantity which it is obliged to hold as strategic gas or oil stocks.

Insufficient harmonisation of Community measures with regard to oil stocks

Three Community directives govern the establishment of national reserves of crude oil and petroleum products by the Member States. Member States must maintain a level of stocks equivalent to 90 days' consumption for each of the three main categories of petroleum products for energy use. Member States must also be ready to act when there is a risk of physical disruption, i.e. they must draw up action plans and set up appropriate bodies and powers enabling them to place stocks on the market and restrict consumption, guarantee supplies to priority consumers and regulate prices.

In the event of a crisis, the European Commission may, at the request of a State or on its own initiative, fix a target in terms of a reduction in consumption. However, the Commission has no powers to order stock disposal. The decision to release oil stocks is a matter for the States, although consultations are arranged at Community level for coordination purposes. Ultimately it is each individual State which will decide whether stock disposal measures should be taken. Apart from the fact that individual action by each Member State would upset the internal market, uncoordinated action would have little or no impact in view of the size of the oil market.

There is then no Community mechanism for using oil stocks which establishes solidarity between States forming part of the same internal market in the event of supply problems.

Furthermore, in most countries of the European Union - and unlike the Strategic Petroleum Reserve in the United States where stocks are held by the public authorities - the security stocks are held by the oil companies and are mixed up with their operational stocks. Only some of the Member States have set up ad hoc bodies responsible for holding all or part of their security stocks. This fragmentation of the storage arrangements affects the proper

functioning of the internal market in energy and causes distortion of competition between refiners and non-refiners which have low levels of operational stocks. In addition, the amount of oil products actually available to the Member States in the event of a crisis, i.e. which can actually be mobilised in the short term, is very uncertain since operators' security stocks are mixed up with their operational stocks. It should be noted in this respect that the stocks of the Strategic Petroleum Reserve currently amount to 545 million barrels and that the United States has decided to gradually increase their volume to 700 million barrels by 2004.

EU legislation also does not provide for harmonised rules on the use of security stocks to deal with a physical disruption of oil supply, but is an instrument for managing an existing physical shortfall which is no way intended to cope with market volatility. Volatility in the markets due in particular to the expectation of a possible physical disruption of supplies is likely to have a serious effect on the growth of EU economies.

Given the inadequacies of the Community system for the security of oil stocks compared with the reality of the energy situation and developments in the internal market in energy, it is therefore easy to understand why this system has never worked. Rules should therefore be laid down which will help to bring the national provisions closer together and which, in the event of a crisis or the threat of a crisis affecting oil supply, will ensure the solidarity and unity of action which are needed for the proper functioning of the internal market.

Inadequacy of the International Energy Agency framework

The Treaty setting up the International Energy Agency (IEA) lays down an obligation on participating States to maintain stocks equivalent to 90 days' of net imports of oil or petroleum products. It establishes a mechanism for responding to supply crises, i.e. on the one hand an obligation to reduce consumption where a certain threshold of supply disruption is exceeded and, on the other, a procedure for disposing of stocks and allocating the available oil between the participating States.

At the beginning of the '80s, the IEA had come to the view that the mechanisms of the 1974 Treaty were no longer adapted to developments on the oil market. Another crisis mechanism, the CERM (Coordinated Emergency Response Measures) was introduced by the Governing Board of the IEA to make stock disposal an easier option. However, any decision taken in relation to CERM requires unanimity of the Governing Board which is made up of representatives of the 26 participating countries, whose geographical origins and at times very different interests do not make it easy to reach a consensus (the participating countries include in particular the US, Australia, Japan and Korea.). Given the lack of clear criteria for activating this mechanism and the differences between the participating States, the risks of measures being blocked are obvious.

In fact, the CERM has been used only once, more than five months after the outbreak of the Gulf War following the invasion of Kuwait by Iraq, although oil prices had already peaked and the negative impact on the economies of the oil consumer countries had already been felt.

In addition, the IEA mechanisms link the management of the oil stocks of the European Union to that of numerous external partners (26 States) whose priorities are not necessarily the same as the EU's. Moreover, it should be pointed out that the gradual establishment of an internal energy market, as is the case between the Member States of the European Union, is a unique achievement: no other country in the IEA, including the United States, has succeeded in developing such an integrated structure.

Under the IEA Treaty as it stands, even a stock disposal measure proposed by a majority of the IEA countries - for example the European Union - could, in view of the unanimity rule governing the work of the CERM, be blocked by a single country. The mechanisms put in place within the IEA do not therefore allow the European Union, the second economic power in the world, to have its own power of decision in such a strategically important field as energy or to ensure the proper functioning of its internal market.

As with current Community legislation, the IEA mechanisms were set up only with a view to a possible physical disruption of oil supplies. The basic elements of this system, which date from 1974, were put in place to respond to measures such as the embargo imposed by OPEC on certain industrialised countries in the difficult political situation in the Middle East at the end of 1973. The circumstances today are far removed from that situation.

Lack of coordinated measures for gas supplies

Given the strategic importance that natural gas will assume in the future, an innovative approach is required insofar as there is currently no Community framework for harmonisation of the measures which will guarantee a minimum level of security of gas supplies in the European Union. It should also be pointed out in this connection that the IEA also has no specific measures to guarantee external gas supplies to participating States. 40% of EU gas imports come from three main sources of supply. Moreover, since 1995, the production of electricity from gas represents 50-60% of new investments in the production of electricity in the European Union each year. Security of gas supplies is therefore particularly important to ensure continuity of electricity production.

The European gas industry has succeeded in ensuring security of supply on a constantly expanding European gas market over the last forty years. However, the European gas market is undergoing rapid change at the moment and the role of traditional market players is also changing.

Hitherto, the work of planning and developing the gas network to achieve the objectives in terms of security - often defined by the gas industry itself - was relatively simple, given that the main suppliers possessed all the infrastructure, the data relating to supply and demand for gas, information and the other instruments necessary for a successful outcome of such planning. In addition, direct State involvement was less necessary as the national gas companies responsible for security of supply were in many cases partly or wholly State-owned.

On the new liberalised gas market, no player will henceforth necessarily assume sole responsibility for short and longer term security of gas supplies at national level because of the restructuring of the industry, the integration of national markets, the emergence of new companies and greater competition. The policies and procedures relating to security of supply therefore have to be reviewed and formalised in this new context. In a competitive market, it is not certain that gas suppliers will give a strategic priority to security of supply; competitiveness is increasingly becoming the main objective of the gas companies.

The organisation of security of gas supply can therefore no longer be entrusted solely to the industry. A new legislative framework is therefore required to ensure that all market players take basic measures to ensure that this objective is achieved.

It should be added that it is extremely important to avoid, in a rapidly changing market, any uncertainty as regards responsibility for security of supply. Any lack of clarity on this point will increase the risk of a supply crisis.

While the gas industry will have to continue to assume operational responsibility, the European Community now has a vital coordination and support role in relation to security of gas supplies. The role of the Community is to ensure the proper functioning of the internal market and give market players a clear framework within which they can interpret and manage change, while guaranteeing an adequate level of security of gas supplies.

As for oil, minimum measures are therefore needed to ensure the proper functioning of the internal market in gas. This will involve harmonised measures which will guarantee uniform and coordinated action between all Member States in the event of a supply crisis.

4. THE SOLUTION: A COMMUNITY FRAMEWORK

As the Green Paper on security of energy supply stated, the Member States are interdependent as regards both measures to combat climate change and the creation of the internal energy market. Any energy policy decision, particularly in relation to supply of oil and gas, taken by a Member State will inevitably have a knock-on effect on the functioning of the market in other Member States. Similarly, operations carried out by companies, aided by the gradual establishment of an internal energy market, are no longer limited to national territory.

Moreover, a response taken by a Member State to a change in oil and gas supply conditions without regard to the other Member States will have little or no real impact. A coordinated response by all Member States, acting in a spirit of solidarity, is the only means of finding effective solutions which will guarantee an adequate level as regards safety, security and the prevention of serious crises and accidents.

The European Union is furthermore engaged in the major political process of enlargement. Faced with this challenge, it is essential for it to take account of the proper management of one of its vital needs, namely oil and gas supplies.

Consequently, in accordance with Article 5 of the EC Treaty, the objectives of the proposed action cannot be sufficiently achieved by the Member States and can therefore, because of the scale or effects of the proposed action, be better achieved by the Community.

The Green Paper on security of energy supply has already considered various proposals in general terms:

- looking at ways of strengthening the system of oil reserves system by placing their use on a Community footing;
- the possibility of extending the oil reserves mechanism to natural gas reserves;
- the need to institute a permanent dialogue with producer countries with a view to improving price formation mechanisms, conclusion of agreements and the use of reserve stocks in the mutual interest;
- greater integration and diversification of supply networks and improved guarantees of their safety and security.

In its communication of 26 June 2002 to the European Parliament and the Council on the final report on the Green Paper on security of energy supply, the Commission indicated that geopolitical uncertainties and oil price volatility meant that thinking was needed on better organisation and coordinated use of stocks.

Objectives

The measures to be implemented to help ensure the proper functioning of the internal energy market will adopt a Community approach in order to:

- promote solidarity between the Member States of the European Union in the event of an energy crisis by putting in place predefined measures and mechanisms which will guarantee coordinated action;
- managing security of supplies by providing for adequate mechanisms to deal with physical disruption of energy supplies.
- manage the safety of supplies and infrastructures by adopting safety measures which will ensure maximum reliability of supply flows from producer countries.
- promote market stability, in consultation with producer countries, by providing for possible responses where the markets anticipate a physical disruption of supplies in order to restore the proper functioning of the market.

These objectives must be achieved within the framework of an internal energy market in which the Commission will take the necessary measures to ensure fair competition. Measures aimed at improving the supply of oil and gas will have little or no positive impact if they are thwarted by price manipulation or if access to transport networks is limited.

Measures aimed at improving the security of supplies must therefore not create any barriers to the entry of new players onto the European energy market or any additional difficulties for undertakings with small market shares. Attention will also have to be paid to ensuring that regulations introduced by the Member States guarantee fair and non-discriminatory conditions as regards storage, in particular for the construction of storage installations and access to storage capacities.

Given these objectives, and the points considered in the Green Paper on security of energy supply, a number of initiatives need to be taken at Community level.

Harmonising the organisation of oil stocks and promoting their coordinated use

1. Harmonisation of national storage systems

Some Member States have set up ad hoc bodies responsible for holding all or part of their security stocks. In others, the stocks are held by private operators.

This fragmentation of the storage mechanisms adversely affects the proper functioning of the internal market in energy. The independent distributors or importers of refined products which need only limited operational stocks consider that the obligations to hold stocks constitute a net cost that they have to bear whereas the refining companies would in any event hold stocks for operational purposes even where there is no requirement to hold security stocks. Storage obligations may therefore cause distortion of competition. To remedy this situation, all Member States will set up a public body to hold oil stocks which will own stocks

representing at least one third of the new obligations imposed. This is very partial alignment of the rules on stocks in the Member States and does not cover everything that is needed, but it will help to improve the functioning of the internal market by establishing rules which will increase competition between the economic operators. The setting up of a central body responsible for strategic stocks will release independent distributors or importers of refined products from the obligation to build up these stocks themselves. They will be able to pay a reasonable charge to the central body for it to fulfil their storage obligation for them. These conditions for healthy competition between various types of oil distributor will help to guarantee diversity of sources of supply on the market and will therefore themselves contribute to improving the supply for consumers.

It should also be noted that security stocks currently suffer from a lack of visibility, and thus of credibility. The operational stocks held by industry may be taken into account as part of the obligation to maintain minimum security stocks. Stocks held in addition to operational stocks, for the specific purposes of security of supply, are therefore very difficult to identify. Having some of these stocks held by a central body will therefore make it possible to redress the lack of visibility of security stocks, and will guarantee the effective and efficient mobilisation of these stocks in the event of a crisis.

2. Coordinated use of security stocks

Community legislation provides only for mutual consultations between technical experts from the Member States, under the aegis of the European Commission, for the purposes of releasing stocks. Each State is therefore able to dispose of stocks however it wishes.

The mechanism currently used by the IEA (the CERM) is subject to the rule of unanimity between the 26 participating countries. Furthermore, even if action is taken under the aegis of the IEA, the broad discretion left to the States as to how they can contribute to the measure means there is a flagrant lack of unity of action.

In the future, the European Community must be able to decide on a common strategy which will be adopted by all Member States to provide an effective response to a physical or economic disruption of oil supplies. This strategy will give details of the measures to be taken, their objectives, their duration and the resources that the Member States will have to provide.

In order to be effective, the action to be taken in response to a disruption of oil supplies, or a threat of a disruption which is causing volatility in the markets (economic risk), must be rapid. Therefore, if there is an imperative need arising from oil market trends, the European Commission will be empowered to urgently adopt the necessary measures, taking account of the general objectives of the mechanisms for the use of security stocks. The Commission will be assisted by a committee made up of representatives of the Member States and chaired by a Commission representative.

3. Harmonisation of intervention criteria

Current EU legislation lays down rules for the use of stocks only in the event of a physical disruption of oil supply. This provides a way of managing an existing physical shortage but cannot be used to react to volatility in the markets due to particular expectations of a physical disruption of supply.

An analysis of volatility in the markets shows that the perception by operators of a risk of a potential future disruption leads to panic buying even supply and demand seem to be in balance. Moreover, the impact of "non-commercial" operators will be to accelerate and accentuate the effects of the perception of a physical disruption on prices.

In addition to the conventional criterion for the use of stocks, namely a physical disruption of oil supply, it is therefore necessary to provide for common rules on the use of security stocks in order to react in a unified and coordinated manner in the event of an economic risk, more especially if there is a general perception of a risk of a physical disruption which is causing volatility in the markets. Action taken individually by each of the Member States would run counter to the objectives of the internal market and would also be ineffective in re-establishing smoother operation of the oil market. Common rules will help to ensure the solidarity and unity of action needed for the proper functioning of the internal market in the event of a crisis.

Any decision by the Commission to take action will be based on the convergence of a number of factors pertaining to the precise circumstances of the energy crisis. It is clear that the "price" element will be one of the essential elements when defining an economic risk situation, given that the perception of a supply disruption will have an effect on prices. In these circumstances, the potential alert threshold should be deemed to have been reached when the price of crude oil on the spot markets is such that, if the price is maintained at this level for 12 months, the external oil bill of the European Union over the following 12 months would be increased by an amount equivalent to more than half of one percent of the GDP of the European Union in the preceding year as compared with the average external oil bill over the last five years. By way of example, in the present circumstances (2002), the Community mechanisms could be implemented by the Commission if the price of a barrel of Brent goes beyond a threshold of \$30 (which corresponds to a threshold of around \$28 for the OPEC basket).

This alert threshold is a necessary, but not a sufficient, condition for action in the event of a general perception of a risk of disruption of supply: exceeding the threshold simply initiates a phase in which the Commission examines all the factors contributing to the crisis, in particular the nature, duration and scale of the factors involved. Any decision concerning the advisability of taking action will be based on the convergence of several factors which make it possible to conclude to what extent there is a threat of a disruption of supplies necessitating a reaction.

In this new situation, in which mechanisms for using security stocks will play an increasingly important role, the volume of these stocks will have to be increased. The current minimum volume of 90 days' consumption will have to be increased to 120 days so that these crisis measures can be effective and credible. These stocks will be increased gradually, taking account of the possibilities of expanding the necessary storage capacities. Average Community security stocks are currently about 114 days' consumption.

In this respect, account will also have to be taken of the situation in the candidate countries for EU membership. Under the accession negotiations, transitional periods have already been agreed with most of these countries until 31 December 2009, to enable them to gradually build up security stocks equivalent to 90 days' consumption. The Commission expects the new Member States to adhere to the principle of building up security stocks of a volume equivalent to 120 days' consumption. It nevertheless recognises that, in duly justified cases, it will be necessary to allow the gradual introduction of new provisions aimed at boosting oil stocks beyond the transitional periods already agreed upon.

Harmonising minimum measures for the security of gas supplies

Although the conditions for stocking gas are different from those for oil and petroleum products, including the technology involved, the mechanism for fixing gas prices is nevertheless index-linked to that for oil prices. The problems which arise in terms of security of supplies and the solutions to be applied are therefore similar for these two energy sources. Hence the importance of putting in place, as for oil, measures providing for a certain level of gas stocks as well as the powers to release these stocks. These new measures will be incorporated into existing Community legislation aimed at granting third parties access to gas stocks.

1. Definition of a supply policy and clarification of responsibilities

Most Member States currently do not have a very coherent approach to guaranteeing security of gas supplies in the internal market. Before any other action is taken, therefore, Member States must take the necessary steps towards defining a general policy and standards for security of gas supply. This policy, which must contribute to the proper functioning of the new open market in gas, calls for a clear definition of the roles and responsibilities of the various market players as regards security of supply.

When they formulate this general policy on security of supply, the Member States will pay the greatest possible attention to the importance of ensuring continuity of gas supplies in difficult circumstances, especially to consumers who have no alternative energy source, and the need to ensure adequate stocks of gas or alternative fuels, to diversify supplies and to establish a balance between the various sources of gas supplies.

This policy of the Member States will have to be transparent. To this end, the Member States and the Commission will draw up reports at regular intervals which will describe the mechanisms put in place for emergency situations and unexpected events to reduce the effects of any crisis on the gas market and the levels of stocks and measures taken or planned to achieve the indicative stocking targets. The Commission will also evaluate the degree of harmonisation of the measures for the security of supply and their contribution to the functioning of the internal market in gas.

2. Harmonising minimum standards for security of gas supplies

Member States will take the necessary measures to ensure that the supply to vital consumers who are not in a position to replace gas with another fuel is assured in the event of disruption of the single biggest source of supply of gas for a period of sixty days under average weather conditions. Harmonised measures will also be taken by the Member States to guarantee security of supply, in the new open gas market, in the event of extremely low temperatures.

These security of supply standards will be implemented by means of instruments that Member States will use depending on the circumstances of the supply crisis and the peculiarities of the national gas market of each Member State.

Among the measures to be implemented in response to a disruption of supply, Member States will take the necessary steps to ensure that gas stocks make at least a minimum contribution towards achieving the security of supply standards. The establishment or maintenance of a minimum level of gas stocks will take account of the geological and economic storage possibilities in the Member States, since in some Member States the geological sites available for new underground gas storage facilities are limited or non-existent.

3. Coordinated use of crisis measures - Gas stocks

Uncoordinated action by the Member States in the event of an energy crisis is likely to jeopardise the proper functioning of the internal market in gas. For the proper functioning of the internal gas market and security of supply, it is essential that Member States should act in solidarity in extraordinary supply situations. Mechanisms must therefore be put in place which will allow the coordinated implementation at Community level of measures to face up to such situations.

Depending on the gravity of the situation, the Commission will therefore have to act to ensure that the necessary measures are taken to provide specific assistance to Member States which are particularly affected by the disruption of gas supplies. In these circumstances and given the specific characteristics of the natural gas market, there is good reason to have a dual intervention mechanism.

In the event of an extraordinary gas supply situation, including a serious disruption of gas supplies from one of the main suppliers of the European Union, the Commission will be able to issue recommendations to urge Member States to take the necessary measures to provide specific assistance to the Member States particularly affected by the disruption in supplies.

If the measures taken by the Member States are inadequate in the light of the market trend or if the economic consequences of the extraordinary gas supply situation become extremely serious, the Commission will be able to take a decision requiring Member States to take specific measures to provide the necessary assistance to the Member States particularly affected by the disruption in gas supplies.

These measures, which will be the subject of either a recommendation or a decision by the Commission depending on the circumstances, may include the deblocking of gas stocks, the provision of gas pipelines to supply the gas to the regions affected or the interruption of non-essential supplies to allow redistribution of the gas and guarantee the flexibility of the system.

As with the measures to be taken in relation to security stocks of oil, the Commission will be assisted by a committee made up of representatives of the Member States.

The new Community arrangements do not at this stage, as they do for oil stocks, lay down the minimum quantities of gas stocks that Member States should hold to guarantee security of supply. Nonetheless, they do introduce quantitative requirements as regards standards of security of supply. The new Community arrangements therefore in particular require Member States to define how they will guarantee that customers who are not in a position to switch to substitute fuels will continue to be supplied for 60 days in the event of a disruption to the largest supplier on the market concerned. To meet this obligation to guarantee supply for 60 days, each Member State will have to implement a combination of measures, including the storage of gas, but also the interruption of non-essential supplies to allow redistribution of the gas and guarantee the flexibility of the system and of supply.

This combination of different measures will enable each Member State to guarantee security of gas supply equivalent to the security of oil supply to which the compulsory oil-storage measures contribute, while taking account of the intrinsic characteristics of the gas market. Not all Member States are able to build up underground stocks due to unfavourable geological conditions. Some countries do not even have appropriate gas storage sites.

However, given the importance of storage among the various measures which can be implemented, it is planned that the Member States will have to determine national indicative targets for a minimum contribution of gas stocks to the security of supply standards. These stocks may be located in the Member States or outside their territory.

It should be noted that the measures with regard to gas supply, like the oil storage obligations, do not affect any measures which may be taken with regard to the security of storage installations.

4. Supply contracts

Long-term supply contracts have played a fundamental role in the development of the European gas market. They are essential for the launch of major investment projects for the development of gas fields and long distance infrastructure projects. For consumer countries, these contracts provide an element of stability for their purchases. Long-term contracts also facilitate diversification in the medium term of gas supplies in the European Union and help to bring new sources of gas onto the market, which encourages competition on the supply side. It should therefore be ensured that an appropriate proportion of gas supplies from non-EU States is based on long-term import contracts. The Commission will monitor the trend in the Member States' gas supply structure and, where appropriate, will be able to decide upon any measures that prove to be needed.

Alongside the long-term contracts, Member States will take the necessary measures to ensure greater liquidity on the gas market and the development of transparent prices in order to promote security of supply, facilitate access to gas and provide possible outlets for companies tied by long-term contractual obligations. In this connection, a minimum proportion of new supplies of gas will have to be based on short-term "spot" contracts or on long-term contracts whose prices are geared to the spot markets in gas.

A misunderstanding arose, first of all in relations with Russia, when certain third countries apparently took the view that the European Union was no longer in favour of these long-term supply contracts. The European Commission confirmed, however, that these contracts were a necessity, as a factor of stability for both producer and consumer countries. These long-term contracts are moreover expressly recognised in Community legislation on common rules for the internal market in natural gas.

The Commission will ensure that these contracts do not create distortions of competition, whether as a result of clauses which would result in restrictive market conditions or by creating dominant market positions. It is therefore important these contracts develop in line with the new elements of the internal market for gas.

Organising an energy dialogue between producer and consumer countries

All these measures for the coordination of action on the security of oil and gas supplies are conceivable only in cooperation rather than confrontation with the producer countries. The enlarged European Union borders the main oil and gas producing areas (Russia, Caspian Sea, North Africa). This geographical benefit of enlargement will have to be taken into account when deciding where to locate oil and gas stocks. These stocks could, for example, be held in the Member States and candidate countries or equally in producer or even transit countries.

The European Community must therefore develop, institutionalise and give substance to the energy dialogue between producer and consumer countries. In this context, it will act in cooperation with the International Energy Forum (Riyadh).

An energy dialogue between producer and consumer countries will help to provide greater stability of supply. It will also enable the safety standards of the European Union to be applied to external supplies, particularly as regards the construction and operation of oil and gas infrastructures or the transport by sea of gas and oil and dangerous derivatives.

Moreover, a more intense dialogue between the European Union and the producer countries is one of the essential conditions for improving the price mechanism and the conclusion of satisfactory supply agreements. As the Green Paper on security of energy supply underlined, such a dialogue must continue whatever the state of the international economy, whether prices are rising or falling, and it must also cover the conditions for the formation and use of stocks. More specifically as regards natural gas, this consultation framework could turn into a negotiation framework in order to meet among other things the need for long-term supply contracts.

From this point of view, the dialogue between the European Union and Russia could constitute a basic model. The Paris and Brussels Summits have confirmed that its aim is to create a new energy solidarity. Thus, actions have been initiated on security of networks, the protection of investments or the identification of major projects of common interest. It may be hoped that this dialogue will enable more effective use to be made in the future of long-term intergovernmental agreements and production-sharing agreements.

Moreover, the dialogue with Russia will not hinder any dialogue with other partners of the European Union, particularly Norway, the Caspian Sea countries, the countries of the European Mediterranean region and the Middle East. Consideration must also be given to relations with OPEC, an organisation with which relations should always be maintained, even when oil prices are not abnormally high.

Acquiring technical expertise for the implementation of measures

The creation of the internal energy market is a gradual and very complex process insofar as it involves very technical rules. It is therefore important to ensure that the new legislative framework is applied effectively and uniformly by all market players under conditions which will guarantee competitiveness.

It is for this reason that the various stages of completing the internal market in gas and electricity have been accompanied by mechanisms allowing the national regulators, the Member States, the economic operators and the Commission to attend technical meetings together (Florence Forum for electricity; Madrid Forum for gas). These working meetings examine the most appropriate measures to take in order to open up the gas and electricity markets and regularly submit highly technical recommendations to the Commission.

Similarly, the new Community framework to be established to consolidate measures, as part of the process of constructing the internal market in energy, relating to security of supplies of oil and gas will require complex and technical tasks to be carried out. It will be necessary among other things to monitor trends on international oil and gas markets and assess their impact on the security and safety of supplies of oil and gas. There will have to be continuous assessment of the effectiveness of the measures taken; in this connection, the level of stocks

of oil and gas in the Member States will have to be monitored. For these tasks to be carried out, objective, reliable and comparable data will have to be available.

In the event of an energy crisis, when the European Commission decides on or recommends measures to release stocks of oil or gas, it will be necessary to assess the impact on the energy market and the economy as a whole.

It could also be mentioned that there is an increasing need to develop more reliable price indices more attuned to the realities of the market than the current ones. The Commission has already stated, in its communication of 4 October 2000 on oil supplies in the European Union, that the producer countries, market operators and the industry should be encouraged to improve price formation indicators, particularly on the basis of a global index which would reflect the whole of the market.

It therefore appears essential to create, within the Commission, a European observation system for oil and gas supply, which will gather the necessary expertise in order to respond to the highly technical issues involved in these tasks. It will provide, under the aegis of the Commission, the technical and scientific assistance and high level of expertise to assist in the correct application of Community legislation in the field of oil and gas supply.

This European observation system will be run by the Commission, which should invite to the meetings representatives of the Member States as well as representatives of the sectors concerned.

5. CONCLUSION

The European Community is gradually putting in place the conditions required for the establishment of an internal market in energy. The achievement of this objective should make the economy of the European Union more competitive and lead to a significant reduction in consumer prices. It will also help to improve internal security of energy supplies.

The completion of the internal market in energy must be accompanied by the necessary coordination of the measures which will guarantee security of external supplies of both oil and natural gas. The creation and development of an internal market in energy makes the Member States increasingly interdependent as regards the security of their supplies. Not having minimum rules on the security of supplies for all the Member States is therefore likely to adversely affect the proper functioning of the internal market in oil and gas.

The only way of guaranteeing an adequate level of safety and security of energy supplies which will contribute to the smooth functioning of the internal market in energy is to take action at Community level and globally. A coordinated and joint reaction by the States which make up the single internal market is the only effective response to an energy crisis.

The coordination of action by the Community with action by other consumer countries, including within the IEA framework, should therefore be prioritised, since action in the event of a crisis or threat of a crisis requires the deployment of means at the most global possible level.

It is therefore necessary to provide the European Union, in coordination with the International Energy Forum (Riyadh), all the consumer countries and the producer countries, with its own means of responding to energy crises. It is above all necessary to provide for means which will enable the European Union to better coordinate measures with regard to security of

supplies. These mechanisms will contribute to the construction of the internal market in energy.

This initiative, which concerns an essential feature of the functioning of our economies, should be made even more of a priority since it will be part of the process leading to the accession of new countries to the European Union which are highly dependent on energy from fossil fuels. The European Community will take account of the situation in each of the candidate countries in order to provide, if necessary, for transitional periods for some obligations.

Appropriate measures for the security of oil and gas supplies will reduce the permanent or temporary risks of physical disruption and the economic risks linked to supplies. These means of action will be implemented in cooperation with the partner producer countries as part of an energy dialogue not only with the OPEC countries but also the main partner which is Russia.

In the light of the above, the Commission proposes, on the basis of Article 95 of the EC Treaty, two legislative measures, namely:

- (1) A proposal for a Directive of the European Parliament and of the Council concerning the alignment of measures with regard to security of petroleum product supplies.
- (2) A proposal for a Directive of the European Parliament and of the Council concerning measures to safeguard security of natural gas supply.

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

concerning the alignment of measures with regard to security of supply for petroleum products

EXPLANATORY MEMORANDUM

1. COMPLETION OF THE INTERNAL MARKET IN ENERGY

1.1. Internal market in petroleum products

The market in petroleum products in the Community is more competitive than the market in other energy products. Nonetheless, a major effort still needs to be made to achieve a market in petroleum products which is genuinely open and integrated at EU level. The European Community therefore has to take the measures needed for this sector to participate effectively, together with other energy sources and more especially natural gas, in a genuine internal market in energy.

In its Communication of 4 October 2000 on oil supply and the Green Paper *Towards a European strategy for the security of energy supply* adopted in November 2000,¹ the Commission noted that the consumer prices of petroleum products before duties and taxes vary considerably from one Member State to another. It suggested the lack of competition in the downstream oil sector² in some Member States was one of the main factors which could explain such price differences. The Commission therefore indicated that it was essential to encourage a more open and competitive downstream oil structure. It noted that for this purpose it was necessary to ensure the development of a genuine internal market for refined products (in the wholesale market) to make for ready, competitive supplies to all distributors, including from refineries in other Member States.

Greater opening up of the distribution sector for petroleum products, in particular to include new operators, and the existence of a genuine internal market in refined products should help to guarantee the conditions for healthy competition. This would enable the various kinds of consumers to be supplied on the most economic terms, even if the market remained exposed to risks due to the EU's high level of external dependence.

The European Union is making steady progress towards the completion of the internal market for gas and electricity and is in the process of creating the largest integrated and most open regional market in the world. The construction of the internal market in energy cannot however be conceived without integration between all energy sources. In particular, oil and gas are two products which are part of the same market: these products can be substituted for each other and compete with each other for some uses. Gas prices are also largely indexed to oil prices. These two energy sources are closely interlinked, in particular through non-essential gas supply contracts.

1.2 The EU's external energy dependence and its consequences

As stated in the Green Paper on security of energy supply, dependence on external supplies of oil, currently 75%, is likely to exceed 85% by 2020. The risks related to EU energy supply are increased by the fact that oil production is geographically concentrated in the Persian Gulf

¹ COM(2000) 769.

² The refining and distribution of petroleum products.

region, and that this concentration is likely to increase significantly over the next few decades.³

The oil market is also highly inflexible in the short term, as regards both supply⁴ and demand.⁵ This structural character of the oil market explains the high volatility of oil prices. The slightest imbalance between supply and demand, or the expectation of such an imbalance, has a very profound impact on prices. This could be seen during the last oil crisis in 1999-2000, when marginal restrictions on supply caused crude oil prices to triple.

Any event which leads to a breakdown in supply, or which simply creates a risk of such a breakdown, is therefore likely to cause serious disruption to the European economy and to society. Even if the importance of oil to the economy has shrunk since the 1970s,⁶ any increase in oil prices always has a marked effect on the EU economy. A rise of \$10 dollars in the price per barrel increases the EU's oil bill for external supplies by about €40 billion a year. Rises in oil prices affect consumers' purchasing power and add to business costs.

It can be estimated that an increase of \$10 in the price per barrel leads to a loss of half a percentage point in terms of economic growth. However, this impact cannot be considered to be linear: sudden, unexpected and large-scale price changes are likely to damage the economy far more than this estimation would suggest. This impact also depends on the oil intensity of the economy, which varies from one Member State to another.

More generally, the predominant position of energy products, especially oil, in society means that energy dependence is a question of social equilibrium. The first two oil crises led to a sharp rise in unemployment. Upsetting the balance is therefore likely to produce a social backlash and a reaction from the business world.

1.3. Insufficient harmonisation of the mechanisms to guarantee security of supply

Current national laws with regard to the security of oil supplies are insufficiently harmonised and coordinated at EU level and can lead - and indeed have led - to distortions in the internal market in petroleum products.

Measures were introduced a long time ago by the Member States to mitigate the effects of any oil supply difficulties. They are to some extent backed up by Community legislation, which supports the building up of "security stocks" by the Member States which can be put on the market in the event of a supply crisis. Directive 68/414/EEC,⁷ as amended by Directive 98/93/EC,⁸ requires Member States to keep stocks corresponding to a minimum of 90 days'

³ Currently 30%, the share of world oil production from countries in the Persian Gulf region could rise to 40% by 2020. 65% of proven world reserves are situated in this region and 30% of the oil currently consumed in the Community comes from there (while the USA is only 14% dependent on the Gulf states).

⁴ The only significant amount of flexibility as regards supply is due to unused production capacity, most of which is situated in the Persian Gulf region.

⁵ Changes in the structure of demand (the continuing growth in the proportion accounted for by transport in oil consumption, the reduction in the proportion of oil used by industry, and the virtual disappearance of oil as a means of generating electricity) and the simultaneous reductions in the scope for substituting another fuel for oil in the short term make oil demand which is already very inelastic even more so.

⁶ The oil intensity in the EU economy, i.e. the ratio between the volume of oil consumption and Gross Domestic Product, has been halved since 1973.

⁷ OJ L 308, 23.12.1968, p. 14.

⁸ OJ L 358, 31.12.1998, p. 100.

consumption for three categories of petroleum products.⁹ Moreover, Directive 73/238/EEC¹⁰ requires the Member States to take all measures to provide the competent authorities with the powers to adopt crisis measures in the event of supply difficulties, i.e. to draw on security stocks and to restrict consumption.

It nevertheless has to be acknowledged that these directives are no longer suitable for the present internal market in energy. They were put in place at a time when the internal market in energy was in its infancy. The Community provisions in force do not guarantee sufficient harmonisation and coordination of the national measures which they back up, harmonisation and coordination nevertheless being necessary for the internal market to function properly: **it is essential that the internal market should be based on sufficiently harmonised and coordinated rules regarding security of supply.**

Two specific types of problem arise:

- those posed by the lack of harmonisation in the organisation of security stocks (see Section 2),
- those posed by the lack of harmonisation of the national laws on crisis measures and the lack of coordinated action between the Member States in event of a crisis (see Section 3).

2. STOCKHOLDING SYSTEMS

2.1. Fragmentation of the EU security stocks system

The Member States currently have maximum freedom as regards the organisation of their security stock system. As a result, the EU security stocks system is divided into fifteen different national systems which differ considerably:

- Some Member States have set up ad hoc bodies responsible for holding all or part of the security stocks; other have not. In Member States which do not have such a body, the stockholding arrangements are entrusted entirely to industry in the framework of State-imposed obligations: industrial operators in that case keep the security stocks together with their own operational stocks.¹¹
- The rules regarding the possibility for operators to fulfil their stockholding obligations by holding stocks in another Member States differ, with some Member States prohibiting this completely.

Against this background, the national provisions for the organisation of security stocks may in some cases have the effect of partitioning the markets in refined products at the national level and disadvantaging operators who are not national refiners.¹² It must be borne in mind that the independent distributors or importers of refined products need only limited operational stocks,

⁹ A similar obligation but one calculated on the basis of States' imports exists in the framework of the Treaty establishing the International Energy Agency (minimum stocks of 90 days' imports).

¹⁰ OJ L 228, 16.8.1973, p. 1.

¹¹ In a system based partially or fully on stocks held by industry, there is always confusion between operational stocks and security stocks: it is not possible to determine what level of stocks a particular operator would hold if there were no stockholding obligation.

¹² "National refiner" means an operator with a refinery in the State concerned.

whereas the refining companies would, in any event, hold significant stocks for operational purposes, even where there is no requirement to hold security stocks.

The fact that the national provisions on the organisation of security stocks may in some cases lead to national partitioning of the markets in refined products was demonstrated in the judgement of the Court of Justice of 25 October 2001 (Case C-398/98), which condemned the Greek security stocks system. According to the Court, the way in which the stockholding obligations were organised in Greece limited the ability of Greek distributors of petroleum products to obtain supplies from refineries situated in another Member State, which the Court found to be contrary to the principle of the free movement of goods.

This proposal for a Directive is not aimed at total harmonisation of the organisation of security stocks systems, but rather at aligning them by defining certain minimum requirements which must be complied with in view of the objectives of opening up the distribution sector for petroleum products and creating a genuine internal market in petroleum products.

To this end, the proposal for a Directive contains two reforms:

- an obligation on the Member States to set up a national stockholding agency,
- reform of the provisions governing the holding of security stocks in another Member State.

2.2. Creation by all Member States of a national stockholding agency

For non-refiners, the stockholding obligation is a particularly burdensome constraint and, in some cases, a barrier to entry. In many cases, the only economic solution at their disposal is to join forces with national refiners through the system of stocks "held at disposal" (the system whereby refiners accept responsibility for the stockholding obligations of other operators). The creation of a central body for strategic stockholding purposes, associated with the right for non-refiners to fulfil their stockholding obligation via this body by making a fair payment, would therefore provide a way of improving the competitive functioning of the markets in refined products by making non-refiners less dependent on arrangements with national refiners.

It should also be noted that the European security stocks are also severely lacking in visibility, this being particularly striking compared with the USA's Strategic Petroleum Reserve.¹³ It can even be said that the EU's security stocks are lacking in credibility in as much as stocks which are held in addition to operational stocks for specific security of supply purposes are very hard to identify and therefore cannot be measured. Moreover, some of the Member States have large-scale oil industry activities directed towards meeting non-national demand which could lead to the presence of particularly high operational stocks compared with domestic consumption. In this situation, the obligation to keep a volume of oil and petroleum products corresponding to 90 days' national consumption is not so relevant.

¹³ The USA does not impose any stockholding obligation on its industry, but has separately set up state-owned stocks known as the "Strategic Petroleum Reserve (SPR)". This currently consists of 545 million barrels which are kept in underground repositories (salt caverns) and which may be sold by decision of the US President. The volume of stocks held by the SPR is to be increased to 700 million barrels by 2004.

Consequently, the proposal for a Directive provides that, in each of the Member States, the ad hoc stockholding body will be responsible for covering at least one third of the security stock obligation. These bodies should themselves own the stocks and should not use systems which would allow them to resort to the industry's operational stocks. Their effective availability would then not be in any doubt and they would benefit from optimum credibility and visibility.

2.3. Holding of stocks in another Member State

Current EU legislation recognises the right of Member States to prevent security stocks from being held in other Member States. Under current EU legislation, it is also necessary for there to be intergovernmental agreements for stocks to be able to be built up in the territory of a Member State on behalf of businesses, organisations or agencies established in another Member State. In view of this, the absence of an intergovernmental agreement may constitute a *de facto* prohibition for an operator to hold stock outside the national territory. Given that there is normally a large concentration of stocks at the refinery in any petroleum products supply chain, these restrictions may disadvantage a cross-border downstream supply chain as compared with a purely national chain.

In order to guarantee the proper functioning of the internal market, the new provisions must expressly provide that the Member States must take care to ensure that the measures they put into place with regard to security of stocks do not have the effect of disadvantaging supply from refineries situated in the other Member States as compared with supply from refineries in their own territory. In practical terms, the proposal for a Directive provides that the Member States must authorise operators to fulfil their stockholding obligations using stocks held in the Member States which are their sources of supply of refined products.

Furthermore, the conclusion of intergovernmental agreements as a prerequisite to stockholding for the purposes of security of supply in another Member State is no longer acceptable in the new internal market in energy. This mechanism must be replaced by a system of surveillance in order to ensure the identification, registration and monitoring of the stocks held in the territory of a Member State on behalf of companies, organisations or agencies established in another Member State.

3. HARMONISATION AND COORDINATION OF CRISIS MEASURE ARRANGEMENTS

Current EU legislation does not guarantee unified, consolidated and coherent action between the Member States of the European Union in the event of a crisis in the oil markets. Such unity and coherence of action is however necessary to make sure that the internal market continues to operate properly in this type of situation.

Specifically, two types of problem arise:

- the existence in some Member States of legal obstacles to releasing stocks because their laws lay down excessively strict preconditions for triggering such action (point 3.1),
- the lack of an EU decision-making mechanism for deciding on unified, coherent and coordinated action at EU level (point 3.2).

3.1 Criteria for the use of security stocks

Initially, security stocks were intended to enable Member States to cope for a certain period during an oil shortage due to disruptions to supply from producer countries. They were therefore a means of last resort. The use of security stocks was also supposed to be in addition to proactive, relatively drastic reductions in consumption (e.g. "car-free Sundays").

In some Member States, the national legislation on security stocks lays down very strict conditions which must be met for the use of security stocks and which still reflect the original thinking about the use of stocks (as a means of last resort to deal with a physical shortage).

However, in view of the changes which have taken place in the oil markets,¹⁴ it may be relevant to release security stocks in other circumstances. The perception by operators that there is a risk of a future possible physical disruption of supply, without it actually needing to happen, may lead to sudden price rises on the spot markets which are extremely harmful to the economy. This type of incident was seen during the Gulf War, during which, although there was no production shortage as compared with consumption,¹⁵ prices shot up on the spot markets in view of the threat to production in Saudi Arabia. The release of oil stocks in this kind of situation would help to offset panic buying, re-establish smoother operation of the market and hence limit price volatility and its disastrous effects on the economy.

The unity and coherence of EU action in such circumstances are absolutely essential to keep the internal market functioning properly. It is therefore necessary to ensure that, in a situation in which there is no physical shortage but sharp price rises are being generated by the expectation of a risk of a physical disruption, all the Member States are able gradually to release their security stocks. This is not the case at the moment since some national arrangements are designed to operate only if there is a physical shortage and therefore lay down restrictive conditions for the release of stocks. EU legislation must therefore ensure that national arrangements are designed in such a way that stocks can be released if there is a general perception of a risk of a physical disruption which is causing a large degree of volatility. This is an essential precondition to allow for the unity and coherence of EU action and thus to keep the internal market operating smoothly.

Oil stocks will be released in two different ways if there is a perception of a risk of disruption depending on whether they are held by ad hoc stockholding bodies or by downstream oil operators in the framework of stockholding obligations.

- Releasing stocks held by an ad hoc stockholding body would mean making them available to downstream oil operators, at the market price and at a specific rate (x million barrels per day);
- Releasing stocks held by downstream oil operators as part of stockholding obligations would involve gradually reducing stockholding obligations.

The effect of releasing stocks will be similar in both cases. Downstream oil operators will be able to meet their need for "discretionary stocks", i.e. stocks which are freely available to them (the need for such discretionary stocks would be generated by the perception that there is a risk of physical disruption to supply). They will be able either to buy stocks held by the agency or keep their own security stocks which until then were "frozen" under the stockholding obligation but will then have been "released". The tendency for operators to buy

¹⁴ In particular, the central role of the spot markets in price formation: on these markets, the price of oil varies from hour to hour depending on operators' perceptions and expectations.

¹⁵ The loss of volumes from Iraq and Kuwait was made up for by using production capacity not used before, mainly in Saudi Arabia.

oil on the spot markets at any price will be curbed, and speculation about the risk of disruption to supply will be dampen. The release of stocks in anticipation of the possibility of physical disruption makes sense given that the oil market operates on the basis of expectations.

Releasing stocks obviously only makes sense if it does not alter the production policy of the producer countries in a way which would detract from the benefit of using the stocks. This is why security of stocks can never be regarded as a way of standing up to the producer countries. On the contrary, stocks should be used in a coordinated manner with the producer countries. The European Community must therefore develop, institutionalise and give substance to the energy dialogue between producer and consumer countries.

This concept for the use of stocks takes account of the changes which have taken place in the oil markets during the last 30 years. To this end, the proposal for a Directive provides that the Member States must have powers to use security stocks in two types of situation:

- a physical disruption of oil supply: this is the intervention criterion behind the original idea for the use of security stocks;
- a general perception of a risk of physical disruption. This concerns situations where operators' perception of the risk of a potential future disruption is causing unacceptable price volatility on the spot markets.

Aligning the national provisions on the basis of these principles will, in the event of a crisis, help to ensure the solidarity and unity of action needed for the proper functioning of the internal market by making sure that some Member States are not prevented from releasing stocks because of a legislative and administrative system which does not allow for it.

In this situation, with stocks being required to play a fundamental part in guaranteeing a regular oil supply at reasonable prices, the present minimum level of security stocks corresponding to 90 days' internal consumption should be gradually increased to 120 days' internal consumption. The average level of Community stocks is currently about 114 days' internal consumption. It varies from country to country between the Community minimum of 90 days' consumption and 214 days' consumption.

In this respect, account will have to be taken of the situation in the candidate countries for EU membership. Under the accession negotiations, transitional periods have already been agreed with most of these countries until 31 December 2009, to enable them to gradually build up security stocks equivalent to 90 days' consumption. The Commission expects the new Member States to adhere to the principle of building up security stocks of a volume equivalent to 120 days' consumption. It nevertheless recognises that, in duly justified cases, it will be necessary to allow the gradual introduction of new provisions aimed at boosting oil stocks beyond the transitional periods already agreed upon.

3.2. A Community intervention mechanism

No mechanism exists at the moment to enable the European Community to decide how to use the security stocks held by the Member States and to coordinate their use. Current Community legislation, which provides only for a simple procedure of mutual consultation between experts from the Member States, under the direction of the Commission, therefore does not guarantee the unity of action and solidarity between the Member States necessary for the proper functioning of the internal market in oil. Measures taken individually by each of the Member States are likely to upset the internal market.

3.2.1. Inadequacy of the International Energy Agency framework

Since the oil market operates worldwide, the European Union will always have to ensure that it works together with the other major consumer countries. The International Energy Agency (IEA), to which all Member States of the European Union and the other major consumer countries (in particular the USA, Japan, and Korea) belong, could serve as a framework for this necessary coordination. However, the existence of the IEA does not in any way obviate the need for an EU decision-making process: the specific character of the European Union and the development of the internal market make it essential to put an EU decision-making process into place.

The existing framework of the IEA also has a number of major weaknesses. Since the early 1980s, the IEA has taken the view that the crisis mechanism provided for in its 1974 founding Treaty was not properly suited to take account of changes in the oil market. The IEA Governing Board introduced another crisis mechanism, CERM (Coordinated Emergency Response Measures), to enable security stocks to be used more easily. However, unanimity of the Governing Board, made up of representatives of the 26 participating States, is needed for a CERM to be triggered, so the lack of any clear criterion for this mechanism to be deployed and the different approaches of the participating States to intervention mean there are obvious risks of blockages occurring. Furthermore, even if a CERM is triggered, **the broad discretion left to the States as to how they can make a contribution to the measure means there is a flagrant lack of unity of action.**

In view of the political nature of any oil crisis, it is important to point out that the IEA is a technical organisation and has only limited authority. The adoption of an EU decision is clearly an act whose political and legal implications go far beyond those of an IEA decision.

Nevertheless, in the event of a crisis or threat of a crisis likely to influence economic growth, priority should be given to common action involving the greatest possible number of consumer countries, including in the framework of the IEA. This will help to maximise the positive effects of Community action.

While Community action needs to be coordinated with that of the other major consumer countries, a Community decision-making process is therefore necessary to guarantee unified, coordinated and coherent action throughout the whole of the European Union so that it acts in a unified and credible manner. Both the use of security stocks and measures to reduce consumption require a Community decision-making mechanism to coordinate them. These measures cannot, in an internal market, be taken by each Member State acting independently of each other.

3.2.2. The Community mechanism proposed

The proposal for a Directive sets up a genuine decision-making mechanism under which the European Union will be able to define the action, in particular as regard the use of stocks, which it plans to take in the event of a crisis. Specifically, if the need urgently arises due to changes in the oil market, the European Commission will therefore have powers to take the emergency measures required, taking account of the general aims of the mechanisms for the use of security stocks. It will be assisted by a Committee made up of representatives of the Member States and chaired by a Commission representative.

The mechanism will be of the "regulatory procedure" type, as laid down in Article 5 of Council Decision of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission. The Commission representative will submit to the Committee a draft of the measures to be taken. The Committee will express its

opinion on the draft within a period laid down by the Chairman according to the urgency of the particular situation. If the measures proposed do not reflect the Committee's opinion, or if the Committee has not expressed an opinion, the Commission will immediately submit a proposal on the measures to be taken to the Council.

This mechanism for coordinated action will contribute to the smooth operation of the internal market in oil and will also help to make the crisis measures more effective.

3.2.3 Potential activation threshold for the mechanism

The Commission will be able to adopt the appropriate measures in the event of a general perception that supply is likely to be disrupted or if there is an actual disruption to supply.

The proposal for a Directive provides for a potential activation threshold in the event of physical disruption. Measures may be taken to draw on stocks or restrict consumption.

In the event of a general perception of a risk of disruption of supply, notably as a result of an external shock, in view of the aim of protecting economic growth, employment and the most vulnerable social and professional groups from high levels of fluctuation in oil prices, the "price" factor will be essential for defining an alert threshold which, if exceeded, will entail Community action.

This alert threshold is attained when the price of crude oil reached on the spot markets is such that, if the price stayed at that level for a period of twelve months, the European Union's external oil bill during the next twelve months would rise by the equivalent of more than half a percentage point of EU GDP for the preceding year. The reference point for calculating the scale of the increase is the average external oil bill over the last five years. By way of example, in the present situation (2002), the price of a barrel of Brent would have to exceed \$30¹⁶ for the threshold to be attained.

Exceeding this alert threshold is therefore a prerequisite for releasing stocks, but it is not sufficient in itself for taking that decision, in the event of a general perception of a risk of disruption of supply exceeding the threshold initiates a phase in which the Commission examines all the factors contributing to the crisis. Any decision about the advisability of, or need for, action will have to be taken in the light of all these factors.

4. TECHNICAL EXPERTISE FOR IMPLEMENTATION OF THE MEASURES

The creation of the internal energy market is a gradual and very complex process as it involves very technical rules. It is therefore important to ensure that the new legislative framework is applied effectively, efficiently and uniformly by all market players under conditions which will guarantee competitiveness.

The various phases of the development of the internal market for gas and electricity were therefore accompanied by measures which enabled national regulatory authorities, Member States, market operators and the Commission to be called together in the context of technical working groups. These working meetings consider what are the most appropriate measures to take to open up the gas and electricity markets and regularly submit very technical recommendations to the Commission.

¹⁶ Corresponding to an OPEC basket price of between \$28 and \$29 a barrel.

Similarly, the new EU arrangements to be put in place to harmonise the measures to safeguard oil supplies, in the context of the internal market in energy, will involve complex, technical tasks. These will in particular concern monitoring the development of international markets and assessing their impact on the safety and security of supplies. There will have to be continuous assessment of the effectiveness of the measures taken. In this context, it will be necessary to monitor the level of oil stocks held by the Member States. For these tasks to be carried out, objective, reliable and comparable data will have to be available.

Should an energy crisis occur and the European Commission takes and coordinates measures to release oil stocks, the effects of this action on the energy market and the economy as a whole will have to be considered.

It is therefore essential to create, within the Commission, a European observation system for oil and gas supply which will gather the necessary expertise in order to respond to the highly technical issues involved in these tasks. Under the Commission's direction, it will provide technical and scientific assistance and a high level of expertise to assist in the proper application of EU legislation in the field of oil and gas supply.

This European observation system will be managed by the Commission, which should invite representatives of the Member States to the meetings as well as representatives of the sectors concerned.

5. CONCLUSION

The aim of this proposal for a Directive is to encourage **greater harmonisation and coordination of national measures regarding security of oil supplies, thereby helping to ensure that the internal market functions properly**. It aims to provide the European Union with the means to act in a unified, credible manner when oil supply difficulties are disrupting, or threaten to disrupt, the functioning of the economy and society.

These measures will, in the event of a crisis, provide the solidarity and the joint Community action necessary in order to respond effectively to uncertainties in the energy market and to promote in this context the proper functioning of the internal market. They are necessary to ensure the opening up of the market in petroleum products to non-refiners, to avoid cross-border downstream supply chains from being disadvantaged as compared with purely national chains, and thus to create a genuine internal market in refined products. Article 95 of the Treaty therefore represents the appropriate legal basis for the proposal for a Directive.

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

concerning the alignment of measures with regard to security of supply for petroleum products

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 95 thereof,

Having regard to the proposal from the Commission,¹

Having regard to the opinion of the Economic and Social Committee,²

Having regard to the opinion of the Committee of the Regions,³

Acting in accordance with the procedure laid down in Article 251 of the Treaty,⁴

Whereas:

- (1) The completion of the internal energy market must be accompanied by the necessary coordination of measures to guarantee the security of the Community's external oil supplies. The internal market is based on the need for solidarity between the Member States, which can be seen more particularly in the essential energy supply sectors of oil and gas.
- (2) Crude oil and petroleum products occupy a central position in the Community's supply of energy products and play an essential part in the functioning of the economy and society, in particular in view of their role in the field of transport. Oil prices are also used as a reference for the establishment of natural gas prices.
- (3) Current national laws with regard to the security of oil supplies are insufficiently harmonised and coordinated at Community level can lead - and indeed have led - to distortions in the internal market in petroleum products. Greater harmonisation and coordination of the national measures relating to the security of oil supplies are therefore necessary to ensure the proper functioning of the internal market.

¹ OJ C [...], [...], p. [...].

² OJ C [...], [...], p. [...].

³ OJ C [...], [...], p. [...].

⁴ OJ C [...], [...], p. [...].

- (4) In order to ensure supply on the most economic terms for consumers, it is necessary to promote a more open and competitive structure in the petroleum product markets. This involves developing a genuine internal market in petroleum products which enables all distributors to be supplied on a straightforward and competitive basis, including those which are not national refiners.
- (5) The security stocks systems differ considerably from one Member State to another. The national provisions may have the effect of partitioning the petroleum products markets nationally and disadvantaging operators which are not national refiners. It is therefore necessary to take measures to align, at least partially, the stocks systems and to ensure that the organisation of these stocks does not adversely affect the proper functioning of the internal market.
- (6) For non-refiners, a stockholding obligation is a particularly burdensome constraint and, in some cases, a barrier to entry. It is therefore necessary, to ensure the opening up of the markets in petroleum products, to guarantee these operators the possibility of complying with their obligations otherwise than by themselves holding the security stocks or concluding agreements with the national refiners.
- (7) To this end also, it is appropriate to harmonise the national provisions relating to the management of stocks by setting up a public body, as exists in certain Member States, responsible for managing at least one-third of the stockholding obligations in accordance with the principles relating to the opening-up of the national market.
- (8) Since restricting provisions concerning the holding of security stocks outside of the national territory may disadvantage a cross-border petroleum products supply chain as compared with a purely national chain, it is necessary, to ensure the proper functioning of the internal market, to allow and provide a basis for stocks to be built up outside of the national territory.
- (9) As stated in the Green Paper *Towards a European strategy for security of energy supply*,⁵ the Community's external oil dependence and the geographical concentration of production capacities are substantial and are likely to increase. This situation creates major risks for the security of oil supplies.
- (10) Any difficulty which substantially reduces supplies of petroleum products or substantially increases their price is likely to cause serious damage to the Community economy. It is therefore essential to be able to make good, or at least mitigate, the damage caused by any such difficulties. To this end, it is necessary to build up security stocks which can be used in a coordinated manner in such circumstances at Community level.
- (11) Apart from the release onto the market of security stocks built up to deal with a crisis situation, the measures intended to mitigate the effects of difficulties related to the supply of crude oil and petroleum products also include measures to curb consumption. It is essential to provide for appropriate procedures and instruments to ensure the rapid, coordinated and unified implementation of these two types of measures.

⁵ COM(2000)769.

- (12) To this end, all the Member States must have the necessary powers to take the relevant measures, where appropriate and without delay, including in situations in which there is not an actual physical shortage, but sharp price rises have come about as a result of the expectation of the risk of a physical disruption.
- (13) In the event of difficulties relating to oil supply, it is necessary, in order to ensure the proper functioning of the internal market, to make sure that there is solidarity and uniformity of action in the Community, taking account of the need to coordinate such action with that of other major consumer countries.
- (14) A European observation system for oil and gas supplies should be set up within the Commission in order to assist in designing and properly applying Community legislation regarding oil supplies, monitoring the application of this legislation and helping to evaluate the effectiveness of the measures in force, as well as monitoring more closely the changes with regard to the security of oil supplies in the framework of the internal market.
- (15) The measures required for the implementation of this Directive need to be adopted in accordance with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of the implementing powers conferred on the Commission.⁶
- (16) In accordance with the principles of subsidiarity and proportionality, as referred to in Article 5 of the Treaty, the aims of the proposed action, namely the creation of a fully operational internal market in petroleum products based on free competition and security of supply for petroleum products, cannot be achieved by the Member States acting independently of each other and therefore can best be achieved at the Community level. This Directive does not go beyond what is necessary for that purpose.

HAVE ADOPTED THIS DIRECTIVE:

Article 1

The aim of this Directive is to ensure the proper functioning of the internal market in petroleum products. For this purpose, it provides for the alignment of the provisions of the Member States with regard to oil stocks and crisis measures and coordinated action between the Member States in the event of a supply crisis.

Article 2

1. Member States shall take all necessary measures to maintain at all times, subject to the provisions of Article 6, a level of stocks of petroleum products equivalent, for each of the categories of petroleum products, to at least 90 days' average daily internal consumption in the preceding calendar year.

⁶ OJ L 184, 17.7.1999, p. 23.

2. The level of minimum stocks referred to in paragraph 1 shall be increased to 120 days as soon as possible following the publication of this Directive and no later than 1 January 2007.
3. Member States shall ensure the availability and accessibility of the stocks held in accordance with paragraphs 1 and 2, in order to be able to take, without delay, appropriate measures for their use in accordance with Article 6.
4. Member States shall send the Commission, no later than one year following the entry into force of this Directive and then every six months until the level of stocks defined in paragraph 2 has been achieved, a detailed report on the measures taken or to be taken to achieve this level of stocks.
5. The stocks referred to in paragraphs 1 and 2 shall be built up and maintained by Member States within their territory or in the territory of another Member State

Article 3

1. The Member States shall set up a public oil stockholding body. They shall take all necessary measures to ensure that, as soon as possible following the entry into force of this Directive and no later than 1 January 2007, the stockholding body owns, for each of the categories of product, stocks representing at least one third of the obligations set out in Article 2(1) and (2).
2. Where a Member State imposes stockholding obligations on operators in the market, the public stockholding body shall assume the stockholding obligations of non-refiners which so wish, subject to a payment which shall not exceed the costs of the services rendered.
3. Two or more Member States may decide to use the same stockholding body or agency. In such a case, they are jointly responsible for complying with the requirements of this Directive.

Article 4

1. Member States shall ensure that fair and non-discriminatory conditions apply in their stockholding arrangements.
2. Member States shall ensure that their arrangements do not disadvantage supplies from refineries located in other Member States as compared with supplies from refineries located in their own territory. They shall in particular authorise any undertaking which has a stockholding obligation and which obtains its supplies of refined products from one or more other Member States to fulfil this obligation through stocks held in the Member States concerned.

Article 5

1. In the event of stocks being built up, for the purposes of the application of this Directive, in the territory of a Member State on behalf of undertakings, organisations or agencies established in another Member State, the Member State in the territory of

which such stocks are stored may not in any circumstances object to their being transferred to the other Member States on behalf of which the stocks are held.

2. Member States shall put in place a system of verification to ensure the identification, registration and monitoring of the stocks held in their territory on behalf of undertakings, organisations or agencies established in another Member State.

Article 6

1. Member States shall provide their competent authorities with powers to enable them to use the stocks maintained under the obligation referred to in Article 2(1) and (2) in the event of difficulties relating to the functioning of the internal market in petroleum products due to supply problems, in accordance with Articles 7 and 8.
2. Apart from the cases referred to in Articles 7 and 8, Member States shall refrain from drawing on stocks where this would have the effect of reducing them to below the minimum compulsory level, except in cases of local supply difficulties, after having informed the Commission, or to comply with their international obligations.

Article 7

1. In the event of a disruption of oil supply which may seriously disrupt the functioning of the economy and the internal market in petroleum products, the Commission may, by taking a decision in accordance with the procedure provided for in Article 9(2), require the Member States to:
 - a) make the security stocks referred to in Article 2(1) and (2) gradually available,
 - b) restrict consumption in a specific or overall manner.

The measures to be taken by the Member States must restrict competition as little as possible. The Commission shall ensure that this principle is complied with throughout the period of application of the measures.

2. The Commission may take measures of the type referred to in paragraph 1 when there is a 7% disruption of the normal level of crude oil supply at world level.
3. The Commission decision may lay down specific arrangements and conditions for the implementation of the measures to be taken by the Member States.

Article 8

1. In the event of a general perception of a risk of disruption of oil supply, notably in the context of an external shock, giving rise to a high level of volatility in the oil markets which may seriously disrupt the functioning of the economy and the internal market in petroleum products, the Commission may, by taking a decision in accordance with the procedure provided for in Article 9(2), require the Member States to make the security stocks referred to in Article 2(1) and (2) gradually available taking into account international agreements concluded by the Member States and decisions taken in the context of such agreements.

The measures to be taken by the Member States must restrict competition as little as possible. The Commission shall ensure that this principle is complied with throughout the period of application of the measures.

2. The Commission may examine the need for measures of the type referred to in paragraph 1 when the price of crude oil on the spot markets is such that, were the price maintained at that level for 12 months, the Community's external oil bill during the next 12 months would be increased by the equivalent of more than 0.5% of the European Union's gross domestic product as compared with the average external oil bill during the previous five years.
3. In the context of the examination provided for in paragraph 2, the Commission shall take account of all the elements necessary for an evaluation of the Member States' supply conditions. It shall take into consideration in particular the nature, duration and scale of the elements giving rise to the situation referred to in paragraph 1.
4. The Commission decision may lay down specific arrangements and conditions for the implementation of the measures to be taken by the Member States.

Article 9

1. The Commission shall be assisted by a Committee made up of representatives of the Member States and chaired by the Commission representative.
2. Where reference is made to this paragraph, Articles 5 and 7 of Decision 1999/468/EC shall apply, in accordance with the provisions of Article 8 thereof. The period provided for in Article 5(6) of Decision 1999/468/EC shall be one week.
3. The Committee shall adopt its internal rules of procedure.

Article 10

1. Member States shall adopt all the provisions and put in place all the mechanisms necessary to ensure the identification and supervision of stocks.

They shall determine a system of penalties applicable in case of infringements of the national provisions adopted pursuant to this Directive and shall take all necessary measures to ensure the implementation of those provisions. The penalties provided for must be effective, proportionate and dissuasive.
2. Member States shall have intervention plans which can be applied in the event of a disruption of oil supply or the general perception of a risk of disruption of oil supply which is giving rise to a high level of volatility in the oil markets. They shall designate the bodies responsible for implementing the measures to be taken pursuant to this Directive.

Article 11

1. The Commission shall take all the measures necessary for the application of this Directive. It shall in particular lay down:

- a) a definition of the categories of products referred to in Articles 2 and 3,
 - b) the arrangements for calculating internal consumption and the stockholding obligations referred to in Article 2, including taking indigenous oil production in the Member States into account in these calculations,
 - c) the arrangements for the transmission to the Commission of statistical summaries for surveillance of the Member States' implementation of the obligations under this Directive.
2. The Commission shall adopt the measures referred to in paragraph 1 in accordance with the procedure laid down in Article 9(2).

Article 12

1. Not later than 1 January 2004, the Commission shall adopt the necessary measures for setting up a European observation system for oil and gas supply to assist in preparing and ensuring the proper implementation of Community legislation in the field of oil supply, to monitor its application and to assist in evaluating the effectiveness of the measures in force and their effects on the functioning of the internal market in petroleum products. The Commission shall ensure that adequate resources are made available to permit effective monitoring of the arrangements provided for in this Directive.
2. The European observation system for oil and gas supply shall be managed by the Commission, which will invite representatives of the Member States and the sectors concerned to meetings. It shall provide the Commission with the technical assistance necessary for the formulation and evaluation of measures taken pursuant to this Directive, and shall contribute to a better understanding of the development of the internal market and the international oil markets and the factors driving these markets.
3. The European observation system for oil and gas supply shall carry out the following tasks with regard to oil:
 - (a) Monitor the functioning of the internal market and the international oil markets;
 - (b) Contribute to the setting up of a system for the physical monitoring of the infrastructures inside and outside of the Community which contribute to the security of oil supply;
 - (c) Monitor the security of oil supply and the procedures intended to guarantee security of oil supplies in crisis situations;
 - (d) Study the development of effective security measures in the oil sector;
 - (e) Monitor the level of security stocks of oil and petroleum products and the procedures for their use, and the implementation of measures to reduce consumption;
 - (f) Create objective, reliable and comparable databases to fulfil its tasks.

Article 13

Member States shall adopt the laws, regulations and administrative provisions necessary to conform with this Directive no later than 1 January 2004 and, as regards Article 2(2) and Article 3, no later than 1 January 2007. They shall forthwith inform the Commission thereof.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

Article 14

This Directive shall enter in force on the twentieth day following that of its publication in the *Official Journal of the European Communities*.

Article 15

This Directive is addressed to the Member States.

Done at Brussels, [...]

For the European Parliament
The President

For the Council
The President
[...]

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND THE COUNCIL

concerning measures to safeguard security of natural gas supply

EXPLANATORY MEMORANDUM

1. BACKGROUND

1.1. Completion of the internal market for energy

The European Union is making steady progress towards the completion of the internal market for gas and electricity. In fact, the EU is in the process of creating the largest, integrated and most open regional electricity and gas market in the world. As demonstrated by the Green Paper "Towards a European strategy for security of energy supply" (COM(2000) 769), this market integration will contribute to security of supply, provided, however, that markets are truly integrated. The European Council at Barcelona on 15-16 March 2002 therefore stressed the importance of powerful and integrated energy networks as the backbone of the internal market and an important precondition for connecting the European economies.

However, market opening and sufficient physical interconnection of markets are not in itself a guarantee of a liquid market based on secure gas supplies from both indigenous and external sources. It is therefore important that the current profound changes in the market and the transition towards a fully open internal energy market are supplemented by transparent and unambiguous new policies defining the overall framework as well as clear roles and responsibilities of the different market players with regard to security of supply within the new market context.

In order to ensure the continued well-functioning of the internal market for gas, it is equally important to ensure that appropriate measures are implemented to deal with extraordinary supply situation.

1.2. Increasing importance of gas and expected rising import dependence.

Natural gas is becoming an increasingly important source of energy in the EU's fuel mix. In 2000, natural gas accounted for approximately 24% of total EU primary energy supply compared to 16% in 1985 and less than 2% in 1960. The steady growth trend continues, even in times of low economic growth. In 2001, Western European gas consumption increased by 2.5% notably as a result of significant increase in the number of household customers and in gas consumption in power generation.

Natural gas has sustained its position as the fuel of choice in EU power generation. Since 1995, gas-fired power generation has every year represented 50-60% of new investments in EU power generation. The most remarkable development over the last decade has been the increasing share of combined-cycle gas turbines (CCGTs) due to a combination of a change in the EC stance on gas-fired power generation at the start of the 1990s, technological progress, relatively competitive gas and environmental considerations.

EU demand for gas and electricity is expected to increase considerably over the coming twenty years. Both EU gas and electricity demand is expected to increase by more than 40% before 2020 and a market share of gas in EU energy supply of up to around 30% is realistic. The key driver in gas demand growth is power generation. Two-thirds of the increase in gas demand is forecast to come from gas-fired power generation and co-generation. The increasing dependence on gas in power generation raises a number of issues with regard to the increasing interdependence between the two sectors notably with regard to security of supply.

Europe, however, is in a relatively favourable gas supply situation with significant own gas reserves and 70-80% of global gas reserves within economic reach of the European market. When implementing the EU Gas Directive later this year, Norway will become a fully integrated part of the internal gas market. Combined EU/EEA gas production is expected to increase over the coming decade based on proven and additional discovered gas reserve potential. By 2010, the internal EU/EEA gas market is expected to depend on imports for up to 25-30%. An enlarged internal market including the 10 Central and Eastern European candidate countries is expected to depend on imports for 35-40% by 2010.

Further EU/EEA gas reserves may well be mobilised before 2010, which could help further sustain EU/EEA gas production levels and hence delay a significant increase in EU/EEA gas import dependency. However, as a function of the expected rapid increase in gas demand combined with an expected gradual levelling off and decline in domestic EU/EEA gas production at some point in time, the EU/EEA is expected in the longer-term to become increasingly dependent on imported gas. Based on the current demand forecast by Eurogas and the Commission and production forecast by the International Association of Oil and Gas Producers (OGP) for EU and Norway, the level of import dependency of EU15/EEA could reach nearly 60% by 2020. For EU25/EEA, the level could reach 65% by 2020. According to recent analysis made by the OGP, these levels could, however, be lower if allowance is made for developing possible upside resource potential including "undiscovered potential" and given the right economic conditions.

On the other hand, however, the import dependency of the EU as such (i.e. without Norway) would be significantly higher and possibly as high as three-quarters by 2020 for EU15.

Import dependency varies significantly between Member States. A number of EU Member States are already completely dependent on imports while others will see their dependence rise close to 100%.

On this background, security of supply and Europe's continued ability to attract sufficient gas supply naturally becomes a priority. Security and continuity of supply is particularly crucial in the power-generating sector. Cost of failing security of supply can be very substantial to modern society as the California electricity supply crisis has borne evidence to. The cost to society of the rolling black-outs in California in January 2001 has been estimated at 42 billion USD or some 3.4% of California's GDP.

Continuity of gas supply is also essential to other consumer categories notably small customers without switching capabilities to alternative fuel such as many large industrial customer have notably with the possibility to interrupt gas supply and switch to back-up oil supply.

The Green Paper "Towards a European strategy for the security of energy supply" (COM (2000) 769) therefore suggested that in order to widen and renew policy of fuel stocks, the European Union *"could consider extending the [oil] stocks mechanism to natural gas...The Union needs to guard itself against excessive vulnerability, resulting from too great a degree of dependence"*.

In its Communication on "Security of EU Gas Supply" (COM(1999) 571 final), the Commission announced that it would report on a regular basis to the Council and the European Parliament on EU gas security issues and if and when appropriate, the Commission would *"make proposals to strengthen security of EU gas supply and further develop the common framework for security of gas supply"*.

1.3. The internal market for natural gas of the EU and security of supply

The completion of the internal market for natural gas in the European Union and ensuring security of supply are compatible objectives. It is obvious that a well functioning single market for gas relies on a sufficient level of secure gas supplies from a diversified range of supply sources. For this reason, an integral part of the creation of the EU internal gas market are measures ensuring security of gas supplies in the new market environment.

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 gas¹ has made very important contributions towards the creation of the internal market for gas. The directive already acknowledged the importance of security of supply for the internal market. Consequently, it allows Member States the possibility of imposing public service obligations on natural gas undertakings in relation to security of supply.

The creation and development of an internal market for natural gas inevitably renders Member States increasingly interdependent regarding security of supply issues. As a result, failure to adopt adequate measures in one Member State can have serious consequences regarding the operation of the internal market throughout the European Union. It is therefore essential, in order to ensure the proper functioning of the internal market, to provide for a minimum level of harmonisation regarding security of gas supply policies in each Member State, in order to avoid market distortions and ensure the well functioning of the internal market for gas on a level playing field.

Liquidity forms an indispensable ingredient of a proper functioning EU internal gas market. Measures aimed at enhancing liquidity, such as spot markets, incentives for new gas supplies from internal and external sources and non-discriminatory authorisation procedures for building storage and LNG facilities, should, among other things, be fully taken into account by security of supply policies in a competitive market environment.

2. THE EUROPEAN GAS MARKET IN TRANSITION - CLEAR SECURITY OF SUPPLY RULES ARE IMPORTANT AS AN INTEGRAL PART OF THE INTERNAL MARKET.

The European gas industry has managed security of supply in a steadily growing European gas market over the last four decades very successfully. However, the European gas market is undergoing rapid change these years and the role of traditional market actors is also changing.

Hitherto, the task of planning and developing the gas network to fulfil gas security targets (as often defined by the gas industry itself) was relatively straightforward as the dominant suppliers controlled all the infrastructure requirements, gas supply and demand side portfolio, information and other necessary instruments to conduct this planning. In addition, direct state involvement was less necessary as the national gas companies responsible for security of supply in many cases were partly or fully publicly owned. Until now, few Member States have therefore been directly involved in setting security of supply policies for natural gas.

In the new liberalised gas market, however, no single player will necessarily maintain the overall responsibility for short- and longer-term security of gas supply at national level as industry restructures, national markets integrate, new entrants emerge and competition develops. While security of gas supply forms an integral part of the internal market for gas,

¹ OJ L 204, 21.7.1998, p.1.

security of supply policies and procedures need to be reviewed and formalised in this new context, which represents different circumstances. In a competitive market, it is not evident that strategic priority will be given by gas suppliers to security of supply. The primary objective and role of gas companies is changing towards being competitive. Organising security of supply can therefore not be left to industry alone and Member States have an obligation to ensure that all market players take minimum measures with regard to security of supply. Moreover, security measures can be costly and it is perfectly feasible that certain operators could neglect these measures to reduce costs if no agreed minimum standards apply.

The adoption by Member States of measures requiring industry to meet minimum standards is therefore an important integral part of market opening. The creation of an internal market is not simply freeing customers to choice, but also ensuring that the market provides high levels of public service, foremost amongst which is security of supply. The existing Gas Directive (98/30/EC) therefore acknowledges the right of Member States to consider security of supply as a public service obligation. Security provisions are not a consequence of the creation of the internal market, but a central part of it. Without a common framework establishing harmonised minimum standards with respect to security of supply obligations, a real risk of market distortion exists.

Security of supply and competition are compatible objectives and gas security can be enhanced in the single EU gas market when properly planned for by companies in liaison with the responsible authorities. A sufficient and appropriate level of security of supply will contribute to a proper functioning of the internal market. The transition to the new market regime is obviously particularly important with regard to clearly defining the new rules and ensuring in operational terms a continued high level of security of gas supply.

Article 24 of Directive 98/30/EC concerning common rules for the internal market in natural gas allows Member States to take necessary safeguard measures in the event of a sudden crisis in the energy market. Such measures shall, however, cause the least possible disturbance to the functioning of the internal market and shall be least restrictive to competition. Measures taken shall be notified to other Member States and the Commission, which may decide that the Member State concerned must amend or abolish such measures if they distort competition or trade in a manner which is not in the common interest. It is necessary to complement these measures by establishing minimum levels of action by each Member State, which need to be compatible with the requirements of the internal market.

A clear need exists therefore to have such emergency measures defined and agreed in advance rather than Member States developing these if and when a sudden crisis arises.

The European gas industry including both GTE (the European association of transmission system operators) and Eurogas have stressed the need for the definition of clear roles and responsibilities of the individual market players with regard to security of supply². In a rapidly changing market, it is extremely important that any uncertainty with regard to security of supply responsibilities is avoided. Lack of clarity with regard to security of supply will in itself increase the risk of a supply crisis.

² GTE i.a. in "GTE Position Paper", 15 June 2001. Eurogas i.a. in "Response of Eurogas to the DG TREN Strategy Paper", 19 March 2001.

The primary responsibility for an overall definition of such clear roles and responsibilities within the new legislative, regulatory and market framework of the internal market lies with Member States.

While the operational responsibility must remain with the gas industry, Member State governments as well as the Community have therefore an important co-ordinating and supporting role to play in this respect. The role of government will be to ensure that the market is working efficiently and giving true signals to guide the participants in interpreting and managing change while maintaining the appropriate level of security of supply. The role of the Community will be to monitor implementation of the new security of supply policies and ensure their compatibility with the requirements of a well functioning internal market.

The fifth meeting held in February 2002 of the European Gas Regulatory Forum, which brings together the Commission, national regulatory authorities, Member States and all relevant gas market stakeholders agreed on a set of recommendations on "Guidelines for Good Practice" in relation to third party access services. The guidelines include some initial elements aimed at clarifying the roles and responsibilities of the main parties in gas transportation notably the transmission system operators (TSOs) and network users. In addition, the Forum agreed that³:

"Within the new regulatory and market environment of the internal market for gas characterised by a multitude of market players and unbundling of integrated gas companies, security of supply can no longer be assumed to be the responsibility of one single party.

A new chain of responsibilities with regard to security of supply and infrastructure planning between public authorities and the different market players including shippers and TSOs therefore needs to be enshrined in order to ensure certainty in this respect. Obligations must be allocated clearly to different players and appropriate to their role.

In this respect Member States will have a role in defining security of supply output standards within a public policy framework. Within this framework it may be left to the market and industry to develop the most efficient solutions to meet the agreed outputs."

However, security of gas supply is not merely a question of balancing demand and supply in a competitive market every day. It also has a long-term strategic aspect.

In view of the above and in view of the transition towards a fully operational and integrated single gas market, Member States should therefore, in function of their gas market features and structures, monitor and ensure that security of gas supply policies are adapted to the new market environment and properly translated into clear roles, operational responsibilities, security criteria and emergency procedures for all participants involved in the gas business within the new legislative framework. This is also important in order to avoid that different approaches to security of supply become a barrier to entry and cross-border trade and so impede the completion and well functioning of the internal gas market. It is equally important, however, to ensure that the new framework and procedures are implemented in a way which does not create significant difficulties for companies with small market shares or new market entrants.

³ "Conclusions of the 5th meeting of the European Gas Regulatory Forum, Madrid, 7-8 February 2002".

3. THE IMPORTANCE OF STORAGE

Gas production and long-distance transportation is capital-intensive. Due to much lower energy density for gas than, for example, for oil, the cost of gas transportation per unit of energy is much higher for gas than for oil and represents a very significant part of the total end-consumer price for gas. In practice therefore, most production from far away fields and long-distance gas transportation pipelines are operated at high utilisation rates with a relatively constant flow. As, however, demand for gas fluctuates considerably during the year, a significant difference exists between supply and demand profiles.

For optimum results, gas storage facilities (either in underground depleted fields, aquifers or salt cavities or in above-ground LNG peak shaving installations) are therefore used, preferably close to demand centres, to help balance the inevitable mismatch between supply and demand thereby reducing unit costs of gas supply. If there were no gas storage at all, both production and transportation capacity would have had to be designed to meet the peak day demand and therefore most of the time have significant over-capacity.

Underground gas storage therefore plays a key role in EU gas supply both under normal operational circumstances as well as in case of supply emergencies and there are economic and strategic reasons why gas storage should be located close to the market. Gas companies therefore seek, as far as geology and economy allows, to spread storage facilities as well as possible and to locate them as near to large demand centres as possible i.e. preferably not too far from large cities.

Underground storage therefore serves several functions including:

- strategic reserve for security of supply in case of disruption (particularly used in Member States with high dependence on non-EU gas imports);
- seasonal load balancing to match peak demand (gas is pumped into the storage during the spring and summer and typically withdrawn from October/November to February/March);
- achieving daily balance;
- arbitrage of gas prices i.e. commercial optimisation of variations in gas prices e.g. around periods of recalculation of gas prices (e.g. beginning of quarters) and more generally as a commercial tool in liberalised markets (notably in the UK). As gas prices in a competitive gas market is expected to increasingly reflect demand and supply for gas, new patterns of price variations and volatility may be expected. Under such circumstances, it should be expected that gas from storage would be released in case of high prices hence limiting volatility.
- overall system optimisation including facilitating swaps;
- transmission support such as mitigating localised capacity constraints or critical pressure thresholds.

While there may be short-term adjustments with regard to requirements for storage and the wish of market players to carry the costs of gas storage, it is generally expected that availability of storage facilities will become increasingly important over time due to growing EU gas demand and import dependency and thus the need for additional storage for security of supply reasons. Furthermore, additional need for storage will exist for load balancing and

due to increasing import dependency and relative declining flexibility from domestic production.

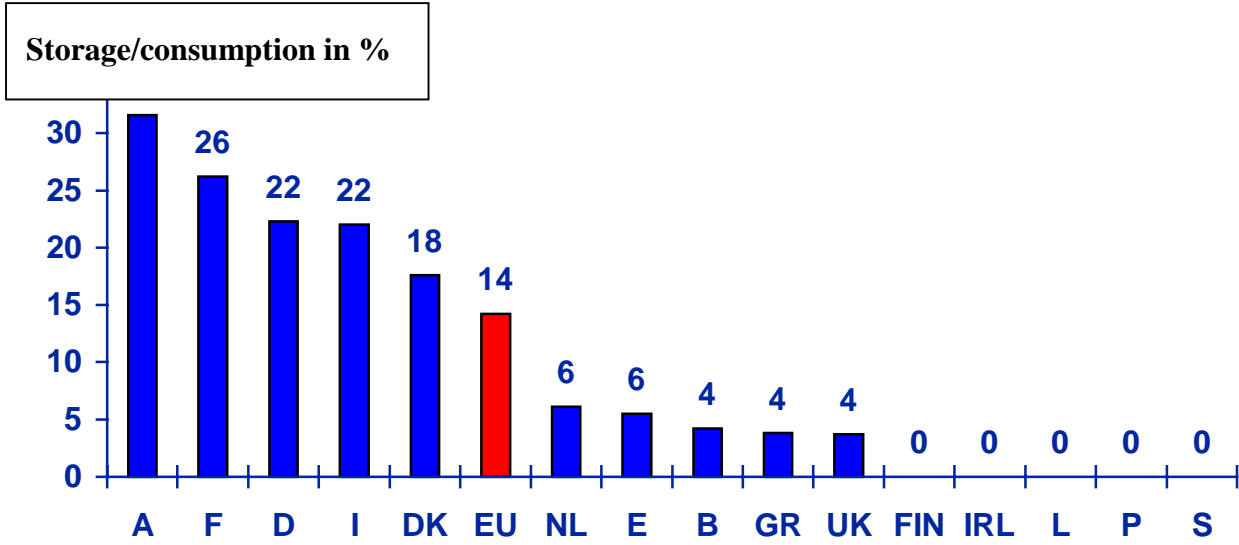
The availability of storage and equivalent alternative flexibility mechanisms as an integrated part of the overall gas supply system is crucial for an efficient operation of the gas system. Providing for non-discriminatory third party access to storage is therefore essential both for the functioning of the internal market and for security of supply reasons. In addition, based on experience from other regions of the world, it may be expected that the development of the internal market will offer new commercial opportunities to owners of storage facilities. It is therefore important that the European Union is prepared to meet the challenges, which this represents in terms of ensuring sufficient development and availability of storage.

The Community should therefore also give high priority to support the development of gas storage as appropriate under the TEN-Energy programme.

The development of a fully operational and liquid internal market for gas with spot markets gradually developing will contribute to security of supply. Security schemes and gas stock requirements at national level should be compatible with and not hamper but support the development of a competitive internal market for gas. In this respect, non-discriminatory access to storage is particularly important.

Mixed picture regarding storage requirements at Member State level

The graph below shows the storage volume in percentage of annual gas consumption.



The graph clearly illustrates the different relative importance of underground gas storage in the different Member States and the absence in some Member States of storage. On average, EU gas storage capacity is equivalent to approximately 50 days of gas consumption (or 14 % of total consumption). Austria holds storage equivalent to 115 days of average gas demand, France for 95 days, Germany and Italy for around 80 days and Denmark for around 65 days. The UK, Greece, Belgium, Spain and The Netherlands have storage equivalent to in the order of 10-20 days of average gas consumption while the remaining Member States have no storage capacity. In some Member States, the geological sites available for construction of new underground gas storage facilities are limited or non-existent. Some Member States therefore rely on storage or back-up services from other Member States. Normally it would not be optimal - but it can be necessary - to cover a storage need in a specific area through

remote storage facilities. With a view to both strengthen the internal EU solidarity and co-operation with external suppliers, there may be certain projects of common interest with regard to storage development in Europe which merit further analysis.

4. THE IMPORTANCE OF LONG-TERM CONTRACTS AND LIQUID GAS MARKETS

Long-term Take-or-Pay contracts have played a very important role for the build-up and development of the European gas market. In particular, in the past, investment in the gas supply industry has usually been underpinned by the conclusion of long-term contracts by European gas companies. Long-term contracts provide an important element of stability for external suppliers and enhance their ability to continue the development of large-scale capital-intensive gas supply projects. Long-term contracts may also facilitate the diversification in the medium term of EU's gas supply and help bring new sources of gas to the market hence enhance supply-side competition.

The Commission considers that the conditions established by the internal energy market will ensure that such contracts will continue to exist, and will continue to underpin security of supply in the internal gas market in an appropriate manner. Indeed, it is clear that EU gas undertakings, as part of their overall contract portfolio, will continue to meet gas needs through such contracts for supply in a competitive market.

Nonetheless, given the importance of long-term contracts for the security of supply of the EU gas market – such contracts are likely to remain necessary to underpin the financing of major new gas supply projects such as the Stockman field – it is appropriate to provide for a safety net, in the unlikely and unforeseeable event that insufficient long-term contracts develop. It is equally important, however, that the existence of long-term contracts does not frustrate competition either via the explicit inclusion of restrictive conditions, or by significantly foreclosing markets. Furthermore, it is important that long-term Take-or-Pay contracts evolve and adapt to the new gas market environment.

On the other hand, it is important to ensure that sufficient liquid gas supplies develop to enable the internal gas market to function properly and competitively, and also to provide the necessary conditions for gas companies to adopt a balanced contract portfolio.

This implies not only the development of gas spot markets throughout the EU – which can provide certainty that producers, suppliers or customers having sold or bought gas on a long-term basis can sell the gas, at the prevailing spot price, if they are unable to find direct outlet for the gas in the market – but equally concerns the adoption, where necessary, of gas release programmes by Member States.

Considerable progress on the development of liquid gas supplies has been made in recent years, notably in the UK and North-Western Europe where trading hubs are operating or emerging. In certain countries, gas release programmes have been implemented and have contributed to new market entry. Furthermore, action taken by the Commission under competition law in the gas sector, such as the GFU case, have further contributed to increased liquidity. The Commission is convinced that this process will, and indeed needs to, continue. Nonetheless, again a safety net needs to be provided in the event that such development do not take place.

5. EXISTING SECURITY OF SUPPLY POLICIES AT MEMBER STATE LEVEL

It is important to notice that the gas supply situation varies considerably between Member States as natural resource, geological and market circumstances differ. The supply situations of Member States vary significantly both in terms of availability of domestic gas production, the importance of gas in the overall energy balance, dependence on external gas supplies, availability of underground storage, the level of interconnection etc.

Member States and their gas industries therefore also deal with security of supply in different ways depending on their individual circumstances, market characteristics and technical options available and their relative costs.

Given these different situations, the European gas industry employs different combinations of supply-side and demand-side tools and procedures to respond to short-term security of supply difficulties. These include system and supply-side flexibility; storage and interruptible customers. The range of facilities available to gas companies allow them to ensure that gas demand and supply are matched at any given time i.e. seasonally and within-day, and that emergency situations can be dealt with.

In order to meet customer demand, the gas supply system necessarily needs to be designed to meet the combined, aggregated peak demand. Gas supply systems are often designed to meet the peak demand of the coldest day, which statistically occurs, for example, once every 20 year and the coldest winter, which statistically occurs once every 50 year.

A number of Member States and large gas companies have in some way specified conditions which need to be fulfilled in relation to security of supply or availability of storage for existing and new entrants into the market:

- In Italy, for example, new entrants importing non-EU gas into the Italian market are required to hold gas stocks equivalent to 10% of the annual supply.
- In Spain, overall gas supply dependency upon any single external supply source must not exceed 60% and there is an obligation on gas suppliers to keep gas reserves for at least 35 days of supply.
- In the UK, security of supply standards are defined to meet "1 in 20 years" peak day demand and "1 in 50 years" winter duration. Similar standards are applied in The Netherlands and France and other Member States.
- The French gas system has also been designed in order to be able to withstand (notably through strategic gas stocks) disruption of the largest source of supply for up to one year.
- In Denmark, the integrated gas company, has designed its back-up and storage capacity to be able to continue gas supplies to the non-interruptible market with no alternative fuel switching capacity in case of a disruption of one of the two offshore gas pipelines supplying gas to Denmark.

6. EFFECTIVE MECHANISMS ESSENTIAL FOR DEALING WITH EXTRAORDINARY SUPPLY SITUATIONS

While it appears that a number of Member States base their security of gas supply on a combination of extreme weather conditions and an "n-1" availability of gas supply sources i.e. that one of the range of supply sources available is disrupted, there appears to be a lack of transparency in the security of supply policies applied at national level which in many cases appear not to be sufficiently well-defined and formalised and not reflecting the market changes taking place. **Improving co-ordination at both national and EU level and improving transparency in this respect must therefore be a first priority.**

Despite the diversity in the supply situations in Member States and due to the structure of the gas supply to the EU, the main supply risks of individual Member States is often a common risk shared with other countries. The risk of disruption in gas supplies to Europe from any of the principle suppliers, for example, would have serious implications in a number of Member States. In such a situation, **only co-ordinated efforts to remedy a disruption will be sufficient. This gives a common EU dimension to measures aimed at preventing or managing a major gas supply crisis and it requires solidarity at EU level to minimise any negative impact.**

In view of the increased market integration within the internal gas market and the European inter-dependence (the "weakest link" in security terms could have an impact on security elsewhere in the internal gas market) and in order to ensure a balanced, transparent and coherent system of risk sharing, it is necessary to ensure that adequate and effective European mechanisms for safeguarding security of supply and co-ordination and intervention at EU level in case of extraordinary supply situations are adopted with a view to ensuring proper functioning of the internal market.

It is important that in pursuing this, proper account is taken of the diversity of supply situations in Member States and that the European gas industry maintains the operational responsibility for implementing the necessary measures.

With regard to gas, the proposed new Community framework pursues the same aims regarding security of supply as the proposal regarding oil stocks. Thus, it introduces strict and quantitative requirements with regard to security of supply standards, and defines the manner in which these standards must be met. In particular, it requires Member States to define and publish the manner in which they guarantee that non-interruptible customers, i.e. customers who cannot immediately switch to alternative back up fuels, are ensured continued supplies during sixty days in the event of a disruption of the largest supply source to the market in question. Similar provisions exist regarding extreme weather conditions and thus extraordinarily high demand, which require supplies to such customers to be guaranteed throughout the entire period of exceptional demand in question.

Given the considerable differences between the gas and oil markets, these measures are de facto equivalent to the obligation to maintain minimum oil stocks. However, the new framework does not envisage at this stage, as for oil stocks, the definition of minimum gas stock levels that Member States should hold in order to guarantee security of supply. This is because not all Member States have equal geological conditions for underground storage and indeed in some countries no suitable storage sites exist. Thus, each country needs to rely on a different mix of instruments to achieve the 60 day obligations and the high demand coverage requirements, based on storage (within or outside the country in question), production flexibility arrangements, linepack and other available measures.

Furthermore, whilst the different geological conditions and the significant advantages of having storage close to demand (and thus avoiding the additional costs of relying on distant storage) mean that a legally binding minimum storage requirement on a Member-State by Member-State basis would not at this stage be appropriate, storage will and must play an important role in Member States' security policies. The proposal therefore requires all Member States to publish indicative quantitative targets for the future contribution of storage in meeting their security of supply standards.

Finally, it is important to underline that, in view of the different degree of availability of storage in Member States and hence the importance of ensuring Community solidarity and co-operation across borders, non-discriminatory access to available underground storage capacity, as emphasised in the Commissions proposal of March 2001 for a Directive amending Directives 96/92/EC and 98/30/EC concerning common rules for the internal markets in electricity and natural gas, is essential.

More generally, it is absolutely indispensable that the security of supply policies to be defined and implemented by Member States are compatible with and contribute to the completion of a fully operational internal market for gas. It is particularly important that the security of supply policies are implemented in a non-discriminatory manner and in no way hamper the entrance of new market participants.

7. TECHNICAL EXPERTISE SUPPORTING THE IMPLEMENTATION OF THE MEASURES

The creation of the internal market for energy is gradual and very complex in particular in relation to the implementation of technical rules. It is therefore important to ensure that the new legislative framework is applied in an effective, efficient, non-discriminatory and homogeneous manner by all market participants under conditions, which will guarantee the competitiveness of the companies.

The various phases of the development of the internal market for gas and electricity should therefore be accompanied by measures which would allow notably to convene national regulatory authorities, Member States, market operators and the Commission in the context of technical working groups. These working group meetings should examine the most appropriate measures to be taken in order to implement the opening of the gas and electricity markets, and should regularly make technical recommendations to the Commission.

Similarly, the new Community framework, which will be created in order to enhance security of gas supply, within the context of the internal energy market, will require complex and technical tasks to be undertaken and accomplished. These will notably relate to monitoring the development of international markets and assessing their impact on safety and security of supply. The effectiveness of the measures in place will have to be continuously evaluated. In this respect, the measures aimed at guaranteeing security of gas supply including the level of gas stocks held by Member States will have to be monitored. In order to be able to carry out these tasks, objective, reliable and comparable data will be necessary.

In the event of an energy crisis, the European Commission may issue recommendations on appropriate measures to be taken by Member States or may, by decision, require Member States to take specified measures. The effects of these measures will need to be evaluated.

It therefore appears essential to create, within the Services of the Commission, a European Observation System for supply of hydrocarbons, which will gather the necessary expertise in

order to respond to the highly technical issues involved in these tasks. It will provide, under the aegis of the Commission, the technical and scientific assistance and a high level of expertise to assist in the correct application of Community legislation in the field of gas supply.

The European Observation System shall be run by the Commission, which should invite to the meetings representatives of the Member States as well as representatives of the sectors concerned.

8. CONCLUSIONS

On the basis of the foregoing, it may be concluded that security of gas supply will not diminish in strategic importance to the European Union. On the contrary. In view of the demand and supply outlook for gas for the EU and in view of the rapid ongoing change with the completion of the internal market for gas, there is a need to undertake co-ordinated action to ensure that security of gas supply is safeguarded and by this will complement other actions taken to achieve the completion of the EU internal energy market. Security of supply policies in a competitive market have to be based on clearly defined and non-discriminatory policies and operational responsibilities. Appropriate monitoring and safeguard mechanism as well as adequate emergency response measures will have to be implemented and kept under review at national and Community level.

The Commission therefore presents the following proposal for a Directive concerning measures to safeguard security of EU gas supply. These measures will ensure the proper functioning of the EU internal gas market by safeguarding security of gas supplies in a competitive market framework. In the event of a crisis, they will ensure the solidarity and the joint Community action necessary in order to respond effectively to uncertainties in the energy market and to promote in this context the proper functioning of the internal market. Article 95 of the Treaty therefore represents the appropriate legal basis for the proposal for a Directive.

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND THE COUNCIL

concerning measures to safeguard security of natural gas supply

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 95 thereof,

Having regard to the proposal from the Commission⁴,

Having regard to the opinion of the Economic and Social Committee⁵,

Having regard to the opinion of the Committee of the Regions⁶,

Acting in accordance with the procedure laid down in Article 251 of the Treaty⁷

Whereas :

- (1) 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 gas⁸ has made very important contributions towards the creation of internal market for gas. Directive 98/30/EC allows Member States the possibility of imposing public service obligations on natural gas undertakings, inter alia, in relation to security of supply;
- (2) The European Council at Barcelona agreed on a rapid adoption of the pending proposals for a completion of the internal market for gas and electricity. The completion of the internal market for gas will significantly change the market framework and must be supplemented with common rules with respect to the security of supply context and the appropriate policies required in this respect;
- (3) The guarantee of a high level of security of supply is therefore a key condition for the successful operation of the internal gas market. With a view to complete the internal market for gas and thereby ensuring a level playing field, a minimum common

⁴ OJ C [...], [...], p. [...].

⁵ OJ C [...], [...], p. [...].

⁶ OJ C [...], [...], p. [...].

⁷ OJ C [...], [...], p. [...].

⁸ OJ L 204, 21.7.1998, p.1.

approach to supply security is necessary throughout the Community in order to avoid market distortions;

- (4) Gas is becoming an increasingly important component in EU energy supply. In function of the increased importance of gas, ensuring the proper functioning of the single EU natural gas market by safeguarding security of gas supply also becomes of higher strategic importance;
- (5) A competitive single EU gas market necessitates transparent and non-discriminatory security of supply policies compatible with the requirements of such a market. Definition of clear roles and responsibilities of all market actors is therefore crucial in safeguarding the well-functioning of the internal market and security of gas supply while at the same time avoiding creating obstacles to new entry or significant difficulties for companies with small market shares;
- (6) As indicated by the Green Paper "Towards a European strategy for the security of energy supply", the European Union is expected in the longer term to become increasingly dependent on gas imported from non-EU sources of supply;
- (7) In order to meet growing demand for gas and diversify gas supplies as a condition for a competitive internal market for gas, the EU will need to mobilise significant additional volumes of gas over the coming decades much of which will have to come from distant sources and transported over long distances;
- (8) The European Union has a strong common interest with gas supplying and transit countries in ensuring continued investments in gas supply infrastructure;
- (9) Long-term contracts have played a very important role in securing gas supplies for Europe and will continue to do so. Whilst the current level of long term contracts is more than satisfactory on the Community level, it is believed that such contracts will continue to make a significant contribution to overall gas supplies as companies continue to include such contracts in their overall supply portfolio and it is appropriate to provide a safety net in this respect;
- (10) The development of liquid gas supplies in the internal market plays an important role in enabling the internal gas market to function properly and competitively. Considerable progress has been made in developing liquid trading platforms and through gas release programmes at national level. This trend is expected to continue. Nonetheless, it is appropriate to provide for a safety net in this respect;
- (11) It is important that Member States lay down an unambiguous framework which will facilitate security of supply and is conducive to investments in gas supply infrastructure. It is important to monitor that appropriate measures are taken to ensure regulatory and fiscal frameworks for exploration and production, storage and transport of natural gas which provide appropriate incentives for investment;
- (12) Domestic gas resources and measures designed to extend their availability, in a non-discriminatory manner that is compatible with the requirements of a competitive single market for natural gas and competition rules, contribute to enhancing the level of security of supply in the internal gas market.

- (13) In the interest of a well functioning internal market for gas to which secure gas supplies are crucial, the supply/demand balance in individual Member States should be monitored and appropriate action taken if security of supply is compromised on a Community level;
- (14) For the well functioning of the internal market for gas and the security of supply, solidarity between Member States in emergency supply situations is essential;
- (15) It is inherent to the creation and development of an internal market that Member States become increasingly interdependent regarding security of supply issues. Failure to adopt adequate measures in one Member State can have serious consequences regarding the operation of the internal market throughout the Community. It is therefore essential, in order to ensure the proper functioning of the internal market, to provide for a minimum level of harmonisation regarding security of gas supply policies in each Member State;
- (16) In the event of extraordinary gas supply situations, the Commission shall take appropriate action proportionate to the severity of the supply situation to ensure that the necessary measures to provide specific assistance to those Member States particularly effected by the gas supply disruption are implemented in order to safeguard, as far as possible, the continued functioning of the internal market for gas;
- (17) With a view to assist in preparing and implementing Community legislation in the field of safety and security of gas supply, to monitor its application and assist in evaluating the effectiveness of the measures in force as well as to better monitor the development of security of gas supply, a European Observation System of hydrocarbons should be established within the services of the Commission;
- (18) The necessary measures should be adopted for the implementation of this Directive in conformity with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred to the Commission;⁹
- (19) In accordance with the principles of subsidiarity and proportionality as set out in Article 5 of the Treaty, the objectives of the proposed action, namely the creation of a fully operational internal gas market, based on fair competition and secure natural gas supplies, cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale and effects of the action, be better achieved by the Community. This Directive confines itself to the minimum required in order to achieve those objectives and does not go beyond what is necessary for that purpose.

HAVE ADOPTED THIS DIRECTIVE:

Article 1

This Directive establishes measures aimed at ensuring the proper functioning of the EU internal market for gas by safeguarding security of gas supply. It establishes a common framework within which Member States shall define general, transparent and non-discriminatory security of supply policies compatible with the requirements of a competitive single EU market for gas; clarify the general roles and responsibilities of the different market

⁹ OJ L 184, 17.7.1999, p. 23

actors and implement specific non-discriminatory procedures to safeguard security of gas supply.

Article 2

For the purpose of this Directive:

1. “source of gas supply” shall mean gas supply originating from one single gas supply country;
2. “long-term gas supply contract” shall mean a gas supply contract with a duration of more than one year;
3. “new market entrants” shall mean undertakings that are not yet active in the Member State in gas supply, or have only entered the market within 5 years following the entry into force of this Directive and which have a small market share”
4. “small market share” shall mean a market share of less than 10% of the national gas market.

Article 3

1. Member States shall take the necessary measures to define the general policies for security of supply which are necessary and integral part of competitive internal natural gas market. This may include clarifying the general roles and responsibilities of the different market actors in fulfilling the security of supply standards.
2. The measures and standards to ensure security of supply in the context of the internal gas market shall be developed in accordance with paragraph 3 of this article and with article 4. The implementation of these measures and standards shall complement the completion of the internal gas market, shall be implemented in a non-discriminatory and transparent way and shall be published.
3. In developing the measures and standards referred to in paragraph 1, Member States shall take the utmost account of:
 - a) the importance of ensuring continuity of gas supplies under severe conditions notably to household customers without alternative fuel options;
 - b) the need to ensure adequate levels of gas storage or alternative back-up fuels;
 - c) the need to diversify supplies and ensure a reasonable balance between different gas supply sources;
 - d) the need to create incentives for new gas supplies from internal and external sources to the single European gas market;
 - e) the risk of the most serious system failure or of disruption of the largest single supply source and the cost related to mitigate such supply disruption;
 - f) the internal market and the possibilities for cross-border co-operation in relation to security of gas supply.

4. In developing the measures and standards referred to in paragraph 1, Member States shall also take account of the need for setting high security of supply standards for gas supplies for power generation in particular with regard to the level of interruptible demand and alternative fuel back-up capacities in this sector.
5. The security of supply policies shall be compatible with and contribute to the completion of a fully operational internal market for gas. The security of supply policies shall be implemented in a non-discriminatory manner and shall in no way hamper the entrance of new market participants.
6. In order to ensure that security of supply criteria established by Member States would not lead to a significant restriction of competition or barriers to market entry, Member States shall exempt companies with small market shares and new entrants from obligations imposed pursuant to articles 3 and 4 of this Directive.

Where Member States consider that the imposition of obligations adopted pursuant to articles 3 and 4 of this Directive would not result in a significant restriction of competition or barriers to market entry, they may apply to the Commission for authorisation to lift this exemption. The Commission shall decide on the request in conformity with article 9, paragraph 2 of this Directive.

Article 4

1. In order to fulfil the security of supply policies and achieve the standards referred to in article 3, Member States shall take the necessary measures to ensure that security of supply can be maintained to non-interruptible customers without fuel switching capabilities in case of disruption of the single largest source of gas supply during sixty days given average weather conditions.
2. Member States shall take the necessary measures to ensure that security of supply can be maintained to non-interruptible customers without fuel switching capabilities in case of extremely cold temperatures during a period of three days statistically occurring every twenty years.
3. Member States shall take the necessary measures to ensure that security of supply can be maintained to non-interruptible customers without fuel switching capabilities in case of a cold winter statistically occurring every fifty years.
4. In order to achieve these security of supply standards, Member States may use a combination of at least the following instruments:
 - a) interruptible customers
 - b) gas storage
 - c) supply flexibility
 - d) spot markets
5. Member States shall take the necessary measures to ensure that gas storage, either located within or outside the territory of the Member State, contributes to a necessary minimum degree to achieving the security of supply standards referred to in this

article in function of the geological and economical feasibility of storage within each Member State.

In this respect, Member States shall, initially not later than one year after the entry into force of this Directive and every two years thereafter, adopt and publish a report setting national indicative targets for future contribution of storage, either located within or outside the territory of the Member State, to security of supply in terms of gas storage working volume and withdrawal capacities and the percentage of gas storage capacity of gas consumption for the next ten years. The targets for future contribution of storage shall be established in accordance with the form set out in the annex to this Directive.

6. The security of supply criteria set out in this article shall be established by Member States in a manner compatible with the objectives of the internal gas market including the harmonisation of the measures implementing these criteria where economically and technically possible and appropriate. In particular, minimum storage objectives imposed on undertakings shall take account of the availability of non-discriminatory access to storage and the terms and conditions on which such access is granted by those companies that operate storage facilities.
7. When implementing security of supply standards and imposing obligations on a market participant established and registered in another Member State, Member States shall take proper account of measures already taken by the market participant in fulfilling security of supply criteria in that Member State.

Article 5

1. In the Report published by Member States pursuant to article [4a] of Directive XX/YY/EC [proposed new Directive amending Directives 96/92/EC and 98/30/EC concerning rules for the internal markets in electricity and natural gas], Member States shall, in particular, cover the following:
 - a) the competitive impact of the measures taken pursuant to articles 3 and 4 of this Directive on companies with small market shares or new market entrants and in particular the effectiveness of measures taken by Member States pursuant to article 3 paragraph 6 to redress any restriction of competition or barrier to entry to such companies resulting from these measures;
 - b) the supply/demand balance on their territory;
 - c) the level of expected future demand and available supplies;
 - d) envisaged additional capacity under planning or construction;
 - e) the emergency and contingency instruments in place to cater for a sudden crisis in the market;
 - f) the levels of stocks and the measures taken and to be taken in order to achieve the indicative storage targets and
 - g) the extent of long-term contracts concluded by companies established and registered on their territory.

In addition, Member States shall monitor that appropriate measures are taken to ensure regulatory and fiscal frameworks for exploration and production, storage, LNG and transport of natural gas which provide appropriate incentives for new investment.

2. In the Report issued by the Commission pursuant to article [28] of Directive XX/YY/EC [proposed new Directive amending Directives 96/92/EC and 98/30/EC concerning rules for the internal markets in electricity and natural gas], the Commission shall examine
 - a) issues relating to security of supply in the Community, and in particular the existing and projected balance between demand and supply including the appropriateness of incentives given to investment in new gas supply infrastructure;
 - b) the scope for harmonisation of security of supply measures aiming at better functioning of the single European gas market;
 - c) the situation with regard to stock levels in relation to the indicative storage targets;
 - d) the level of long-term contracts for gas, and the consequences in practice of this level for ensuring adequate levels of new gas supplies for the European Union in the future.

Where appropriate, this report shall include recommendations.

Article 6

1. With a view to ensure continued long-term security of gas supply for the Community and the gradual development of a more liquid internal market for gas, the Commission shall closely monitor the degree of new gas supply import contracts from non-EU countries concluded on a long-term basis as well as the existence of adequate liquid gas supplies and transparent gas price references within the Community to underpin stable long-term gas supplies. The Commission may issue Recommendations on appropriate measures to be taken by Member States in this respect. The Recommendations may only address an insufficient degree of such contracts on a Community level. Member States shall inform the Commission of the manner in which the Recommendations are implemented. In making such Recommendations, the Commission shall pay particular attention to the possible effect such measures may have on companies with small market shares and new entrants.
2. Where the measures taken by Member States in relation to the Recommendations referred to in paragraph 1 are inadequate with regard to the long-term security of gas supply, the Commission may, by Decision, in conformity with the procedure laid down in article 9, paragraph 3 require the Member States concerned to take specified measures to ensure that an appropriate minimum share of new gas supply from non-EU countries over the five years following the entry into force of this Directive is based on long-term contracts and that adequate liquid gas supplies are developing and transparent gas price references are available within the Community to underpin stable long-term gas supplies. When taking such Decisions, the Commission shall

pay particular attention to the possible effect such measures may have on companies with small market shares and new entrants.

3. The Commission shall, within five years of the entry into force of this Directive, submit a review report to the European Parliament and the Council on the experience gained from the application of this Article, so as to allow the European Parliament and the Council to consider, in due course, the need to adjust it.

Article 7

With a view to enhancing liquidity of natural gas, Member States shall take appropriate measures to ensure non-discriminatory authorisation procedures for building storage and LNG facilities and remove any obstacles for building such facilities. These procedures shall apply equally to EU natural gas undertakings as to non-EU gas suppliers.

Article 8

1. The Commission may, in conformity with the procedure laid down in article 9, paragraph 2, in the event of extraordinary gas supply situations including a major interruption of gas supplies from one of the European Union's principal gas suppliers, issue Recommendations to Member States to take the necessary measures to provide specific assistance to those Member States particularly effected by the gas supply disruption. Such measures may include, but are not limited to, the following:
 - a) release of gas stocks;
 - b) provision of pipeline capacity enabling diversion of gas supplies to affected areas;
 - c) interruption of interruptible demand to allow reallocation of gas and system flexibility.
2. Member States shall inform the Commission of their implementation of the Recommendations.
3. Where the measures taken by Member States are inadequate in the light of market developments, and/or where the economic consequences of the extraordinary gas supply situation become extremely severe, the Commission may, by Decision, in conformity with the procedure laid down in article 9, paragraph 3, require Member States to take specified measures to provide necessary assistance to those Member States particularly effected by the gas supply disruption. Such measures may include, but are not limited to, those mentioned in paragraph 1 points a), b) and c).
4. The recommendations and decisions to be taken in accordance with this article shall restrict competition as little as possible. The Commission shall ensure that this principle is complied with throughout the entire period of application of the measures.

Article 9

1. The Commission shall be assisted by a Committee of representatives of the Member States and chaired by the representative of the Commission.
2. Where reference is made to this paragraph, articles 3 and 7 of Council Decision 1999/468/EC shall apply in respect of the provisions of article 8 of that Council Decision.
3. Where reference is made to this paragraph, articles 5 and 7 of Council Decision 1999/468/EC shall apply in respect of the provisions of article 8 of that Council Decision.

The period foreseen in article 5, paragraph 6 of Council Decision 1999/468/EC shall be one week.

4. The Committee shall establish its internal rules.

Article 10

1. Not later than 1 January 2004, the Commission shall make the necessary arrangements to set up a European Observation System for supply of hydrocarbons to assist in preparing and implement Community legislation in the field of gas supply, to monitor its application and assist in evaluating the effectiveness of the measures in force and their effects on the functioning of the internal natural gas market. The Commission shall ensure that adequate resources are made available to enable the effective monitoring of measures provided for in the present Directive.
2. The European Observation System for supply of hydrocarbons shall be run by the Commission, which should invite to meetings representatives of Member States as well as representatives of sectors concerned. It shall provide the Commission with the technical assistance necessary for the formulation and evaluation of measures taken in relation to the application of the present Directive and shall contribute to a better understanding of the evolution of the internal market and the international gas market and the factors driving these markets.
3. The European Observation System for supply of hydrocarbons shall carry out, in the field of natural gas, following technical tasks:
 - a) Monitor the functioning of the internal market and the international market for gas;
 - b) Contribute to the implementation of a physical monitoring system of the internal EU and external gas infrastructures to the European Union which contribute to the security of gas supply;
 - c) Monitor gas supply and the procedures aimed at guaranteeing security of gas supply in cases of emergency;
 - d) Monitor the level of strategic gas stocks and the procedures for their use as well as the procedures applied with regard to access to storage including aspects of market dominance in relation to access to storage;

- e) Create a basis of objective, reliable and comparable data as a basis for fulfilling its tasks.

Article 11

The Commission shall closely monitor the manner in which Member States implement this Directive, and in particular the compatibility of the measures taken with regard to article 4 and their effect on the internal gas market and the development of competition within the European Union. The Commission shall closely monitor the availability of third party access to storage on non-discriminatory terms and conditions. In the light of the results of this monitoring, the Commission shall, if necessary, no later than 1 January 2004 present proposals regarding further measures to ensure effective access to storage.

Where appropriate, the Commission shall issue recommendations or make appropriate proposals.

Article 12

Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 1 January 2004. They shall forthwith inform the Commission thereof.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

Article 13

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Communities*.

Article 14

This Directive is addressed to the Member States.

Done at Brussels, [...]

For the European Parliament
The President

For the Council
The President

ANNEX

EU storage capacity - national indicative targets

The table below illustrates gas storage capacities in absolute as well as relative terms in relation to consumption.

Storage capacities at 1 January 2001.

	Working Volume (BCM)	In % of 2000 Demand	Withdrawal capacity (million m ³ /day)	2010 Target BCM Storage	2010 Target %	2010 Target Withdrawal capacity
Austria	2.295	31.6	24			
Belgium	0.675	4.2	19			
Denmark	0.810	17.6	25			
France	11.1	26.2	180			
Finland	0.0	0.0	0			
Germany	18.556	22.3	425			
Greece	0.075	3.8	5			
Ireland	0.0	0.0	0			
Italy	15.1	22.0	265			
Luxembourg	0.0	0.0	0			
Netherlands	2.5	6.1	145			
Portugal	0.0	0.0	0			
Spain	1.0	5.5	8			
Sweden	0.0	0.0	0			
UK	3.577	3.7	137			
EU-15	55.688 BCM	14.2%	1233 million m³/day			

Proposal for a

COUNCIL DIRECTIVE

repealing Council Directives 68/414/EEC and 98/93/EC imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products, and Council Directive 73/238/EEC on measures to mitigate the effects of difficulties in the supply of crude oil and petroleum products

EXPLANATORY MEMORANDUM

The Commission has put forward a proposal for a new Directive of the European Parliament and of the Council concerning the alignment of measures with regard to security of supply for petroleum products. More specifically, this proposal for a Directive provides for Member States' provisions on oil stocks and crisis measures to be more closely aligned with each other, and for coordinated action between the Member States in the event of a supply crisis.

The abovementioned proposal for a Directive is in two parts:

- The first part defines the stockholding obligations and the criteria with which the security stock systems must comply.
- The second part covers aspects relating to the adoption of measures in a crisis situation, more especially the institutional mechanism for ensuring a coordinated response from the Member States in the event of a crisis.

In this situation, existing legislation on this subject is no longer relevant. The aim of this proposal for a Directive is therefore to repeal some of the texts concerned.

Proposal for a

COUNCIL DIRECTIVE

repealing Council Directives 68/414/EEC and 98/93/EC imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products, and Council Directive 73/238/EEC on measures to mitigate the effects of difficulties in the supply of crude oil and petroleum products

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 100 thereof,

Having regard to the proposal from the Commission,¹

Having regard to the opinion of the European Parliament,²

Having regard to the opinion of the Economic and Social Committee,³

Whereas:

- (1) Directive/.../EC provides for the alignment of measures with regard to security of supply for petroleum products.
- (2) More specifically, in order to ensure the proper functioning of the internal market, Directive .../.../EC brings the provisions of the Member States with regard to petroleum stocks and crisis measures closer into line with each other and provides for coordinated action between Member States in the event of a supply crisis.
- (3) It also incorporates, in a new and coherent text, all the relevant aspects which were dealt with in particular in Council Directive 68/414/EEC of 20 December 1968 imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products,⁴ and in Council Directive 73/238/EEC of 24 July 1973 on measures to mitigate the effects of difficulties in the supply of crude oil and petroleum products.⁵
- (4) Those legislative texts are therefore now obsolete,

¹ OJ C [...], [...], p. [...].

² OJ C [...], [...], p. [...].

³ OJ C [...], [...], p. [...].

⁴ OJ L 308, 23.12.1968, p.14. Directive amended by Council Directive 98/93/EC of 14 December 1998; OJ L 358, 31.12.1998, p.100

⁵ OJ L 228, 16.8.1973, 1.

HAS ADOPTED THIS DIRECTIVE:

Article 1

Council Directive 68/414/EEC and Council Directive 98/93/EC amending Directive 68/414/EEC are hereby repealed.

Article 2

Council Directive 73/238/EEC is hereby repealed.

Article 3

This Directive shall enter in force on the twentieth day following that of its publication in the Official Journal of the European Communities.

Article 4

This Directive is addressed to the Member States.

Done at Brussels, [...]

For the Council
The President
[...]

Proposal for a

COUNCIL DECISION

repealing Council Decision 68/416/EEC on the conclusion and implementation of individual agreements between governments relating to the obligation of Member States to maintain minimum stocks of crude oil and/or petroleum products and Council Decision 77/706/EEC on the setting of a Community target for a reduction in the consumption of primary sources of energy in the event of difficulties in the supply of crude oil and petroleum products

EXPLANATORY MEMORANDUM

The Commission has put forward a proposal for a new Directive of the European Parliament and of the Council concerning the alignment of measures with regard to security of supply for petroleum products. More specifically, this proposal for a Directive provides for Member States' provisions on oil stocks and crisis measures to be more closely aligned with each other, and for coordinated action between the Member States in the event of a supply crisis.

The abovementioned proposal for a Directive consists of two parts:

- The first part defines the stockholding obligations and the criteria with which the security stock systems must comply.
- The second part covers aspects relating to the adoption of measures in a crisis situation, more especially the institutional mechanism for obtaining a coordinated response from the Member States in the event of a crisis.

In this situation, existing legislation on this subject is no longer relevant. The aim of this proposal for a Decision is therefore to repeal some of the texts concerned.

Proposal for a

COUNCIL DECISION

repealing Council Decision 68/416/EEC on the conclusion and implementation of individual agreements between governments relating to the obligation of Member States to maintain minimum stocks of crude oil and/or petroleum products and Council Decision 77/706/EEC on the setting of a Community target for a reduction in the consumption of primary sources of energy in the event of difficulties in the supply of crude oil and petroleum products

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 100 thereof,

Having regard to the proposal from the Commission,¹

Whereas :

- (1) Directive .../.../EC provides for the alignment of measures with regard to security of supply for petroleum products.
- (2) More specifically, in order to ensure the proper functioning of the internal market, Directive .../.../EC brings the provisions of the Member States with regard to petroleum stocks and crisis measures closer into line with each other and provides for coordinated action between Member States in the event of a supply crisis.
- (3) It also incorporates, in a new and coherent text, all the relevant aspects which were dealt with in particular in the Council Decision of 20 December 1968 on the conclusion and implementation of individual agreements between governments relating to the obligation of Member States to maintain minimum stocks of crude oil and/or petroleum products,² and the Council Decision 77/706/EEC of 7 November 1977 on the setting of a Community target for a reduction in the consumption of primary sources of energy in the event of difficulties in the supply of crude oil and petroleum products.³
- (4) Those legislative texts are therefore now obsolete,

¹ OJ C [...], [...], p. [...].

² OJ L 308, 23.12.1968, p.19.

³ OJ L 292, 16.11.1977, p. 9.

HAS ADOPTED THIS DECISION:

Article 1

Council Decision 68/416/EEC is hereby repealed.

Article 2

Council Decision 77/706/EEC is hereby repealed.

Article 3

This Decision is addressed to the Member States.

Done at Brussels, [...]

*For the Council
The President
[...]*

LEGISLATIVE FINANCIAL STATEMENT

Policy area(s): Energy

Activity(ies): Underpinning the security of oil and gas supply to the European Union

TITLE OF ACTION: CREATION OF AN EUROPEAN OBSERVATION SYSTEM FOR OIL AND GAS SUPPLY

1. BUDGET LINE(S) + HEADING(S)

Budget line to create:

B5-710 A “Financial Support for Energy Infrastructure – Expenditure on administrative management”

2. OVERALL FIGURES

2.1. Total allocation for action (Part B): €million for commitment 4.478 M€

2.2. Period of application:

2004 – 2009 and subs. years

(subject to renewal of the budget line concerned)

2.3. Overall multiannual estimate on expenditure: 14.022 M€

As for the years 2007 onwards, commitments and payments are subject to renewal of the TEN regulation.

a) Schedule of commitment appropriations/payment appropriations (financial intervention) (*see point 6.1.1*)

€million (to 3rd decimal place)

	2004	2005	2006	2007	2008	2009 and subs. years	Total
Commitments							
Payments							

b) Technical and administrative assistance and support expenditure(*see point 6.1.2*)

Commitments	1.474	1.721	0,761	0,411	0.111		4.478
Payments	0,338	1.136	1.721	0,761	0,411	0.111	4.478

Subtotal a+b	
--------------	--

Commitments	1.474	1.721	0,761	0,411	0.111		4.478
Payments	0,338	1.136	1.721	0,761	0,411	0.111	4.478

c) Overall financial impact of human resources and other administrative expenditure (see points 7.2 and 7.3)

Commitments/ payments	1.591	1.591	1.591	1.591	1.591	1.591	9.544
--------------------------	-------	-------	-------	-------	-------	-------	-------

Figures do not add up due to rounding

TOTAL a+b+c							
Commitments	4.655	3.312	2.352	2.002	1.702		14.022
Payments	1.929	2.727	3.312	2.352	2.002	1.702	14.022

2.4. Compatibility with the financial programming and the financial perspective

- Proposal compatible with the existing financial programming
- This proposal will entail reprogramming of the relevant heading in the financial perspective
- This may entail application of the provisions of the Interinstitutional Agreement.

2.5. Financial impact on revenue¹:

- No financial implications (involves technical aspects regarding implementation of a measure)

OR

- Financial impact – the effect on revenue is as follows:

Note: All details and observations pertaining to the method of calculating the effect on revenue should be included in a separate annex.

€million (to 1 decimal place)

		Prior to action (Year n-1)	Situation following action					
Budget line	Revenue		Year n	n+1	n+2	n+3	n+4	n+5
	a) Revenue in absolute terms							
	b) Change in Revenue	Δ						

(Please state each budget line involved, adding the appropriate number of rows to the table if there is an effect on more than one budget line)

3. BUDGET CHARACTERISTICS

Type of expenditure		New	EFTA participation	Participation applicant countries	Heading Financial Perspective
<u>Comp/</u> <u>Non-comp</u>	<u>Diff/</u> <u>Non-diff</u>	<u>YES/</u> <u>NO</u>	<u>YES/NO</u>	<u>YES/NO</u>	No

¹ For further information see a separate guidance paper

4. LEGAL BASIS

Article 95 EUT

Directive concerning the alignment of measures with regard to security of supply for petroleum products [COM(2002)488]

Directive concerning measures to safeguard security of natural gas supply [COM(2002)488]

5. DESCRIPTION AND GROUNDS

5.1. Need for Community intervention ²

5.1.1. Objectives pursued

The Green Paper “Towards a European strategy for the security of energy supply” revealed the structural weaknesses of the Communities energy supply. Growing dependency on energy imports from external suppliers entailing physical and economic risks and the forthcoming completion of the internal energy market clearly demonstrate the need to define a Community framework for the implementation of measures to ensure security of external energy supplies which will place minimum restrictions on competition. The new Community framework relating to Security of supplies of oil and gas will require complex and technical tasks to be carried out. In addition, it will necessitate very close co-operation with partner countries supplying and transiting resources to the enlarged EU. It will be necessary among other things to monitor trends on international oil and gas markets and assess their impact on the security and safety of supplies of oil, gas and strategic infrastructure. There will have to be continuous assessment of the effectiveness of the measures taken; in this connection, the level of stocks of oil and gas in the Member States will have to be monitored. For these tasks to be carried out, objective, reliable and comparable data will have to be available.

In the event of an energy crisis, when the European Communities decide on or recommend measures related to oil and gas stocks, it will be necessary to assess the impact on the energy market and the economy as a whole.

In this context, there is an increasing need to develop more reliable price indices more attuned to the realities of the market than the current ones. The Commission has already stated, in its communication of 4 October 2000 on oil supplies in the European Union, that the producer countries, market operators and the industry should be encouraged to improve price formation indicators, particularly on the basis of a global index which would reflect the whole of the market.

It therefore appears essential to create, within the Commission, a European observation system for oil and gas supply. This system will

- assist in preparing and implementing Community legislation in the field of oil and gas supply
- monitor its application and assist in evaluating the effectiveness of the measures in force and their effects on the functioning of the internal market for petroleum products, oil and natural gas.

² For further information see a separate guidance paper

5.1.2. Measures taken in connection with ex ante evaluation

a) Explain how and when the ex-ante evaluation was conducted or how the corresponding information was gathered.

In November 2000, the Commission issued a Green paper “Towards a European strategy for the security of energy supply”. The Green Paper was based on a profound analysis of the challenges, risks and needs of the European Union in terms of secure energy supplies. It identified the structural weaknesses and geopolitical, social and environmental shortcomings of the EU’s energy supply. Its publication triggered a comprehensive public debate on security of energy supplies and how to ensure it in the future. In the final report on the Green Paper, the Commission stated that energy imports would be much higher in 30 years time, amounting to 70% of total needs. The need to develop a Europe-wide security of supply concept was also highlighted. As a consequence, the Commission has developed a Community framework aiming at ensuring secure gas and oil supplies to the EU.

In addition, further input has been gathered by the Madrid Regulatory Forum, the Oil Supply Group as well as other, less formal sources from Member States and industry.

b) Describe briefly the findings and lessons learnt from the ex-ante evaluation:

In October 2000, the Commission issued a Communication on European oil supply and in November 2000, it adopted the Green Paper “Towards a European Strategy for the security of energy supply”. In February 2002, the Madrid Regulatory Forum agreed on extensive conclusions and presented a wide range of different working papers and presentations³. In these documents, among others, the following facts have been identified and highlighted:

1. The European Union will face a considerably rising dependency on oil and gas imports over the next decades; the most recent figures available to the Commission suggest a rise from 75% to 85% for oil and from 40% up to 70% for gas.
2. The volatility of oil prices, to which gas prices are still linked, does not exclusively reflect market development, but also point to political interests (OPEC) and massive speculation involved in the international oil market. Unreasonably high oil prices as a consequence of speculation caused rising inflation rates in the past with all the negative economic consequences arising from it⁴.
3. The creation of the internal energy market is very complex in particular in relation to the implementation of technical rules that are introduced as a consequence of introducing competition to the European natural gas market and in order to create and maintain a level playing field not only, but also in terms of security of supply.
4. Existing price differences in the downstream oil sector of Member States are likely to be due to a lack of competition.
5. The present security stock system in EU Member States is very fragmented: some Member States have set up ad hoc bodies responsible for holding all or part of the security stocks; others

³ see http://europa.eu.int/comm/energy/en/gas_single_market/madrid3/madrid5.html

⁴ In its Communication from October 2000, the Commission stated: “If oil prices stay at around \$30 a barrel during the rest of the year the negative effect on the price increase on growth would be 0.3% for the year 2000 and 0.5% for 2001. the increase in price would add 1% to the inflation rate.”

have not. The rules for operating the security stocks vary widely, and as a consequence, there is insufficient harmonisation of the mechanisms to guarantee security of supply.

6. The same findings apply to crisis measure arrangements currently in place in Member States.

5.1.3. Measures taken following ex post evaluation

The activities of the observatory will be subject of regular midterm reviews to identify recommendations designed to improve the performance of the Observatory.

5.2. Actions envisaged and arrangements for budget intervention

In the following, each action is specified according to the following:

- A. The target population(s) (specify number of beneficiaries if possible);*
- B. The specific objectives set for the programming period (in measurable terms);*
- C. The concrete measures to be taken to implement the action ;*
- D. The immediate outputs of each action, and their contribution to*
- E. The expected outcomes solving needs or problems*

Actions:

1. Monitoring the functioning of the internal oil and gas market and the international oil and gas market:

A. The target population(s) (specify number of beneficiaries if possible)

Commission, Member States, relevant industry and partner countries (producers, transit)

B. The specific objectives set for the programming period (in measurable terms)

1. Ensuring that Member States, the Commission and relevant decision makers in the industry and partner countries are up to date with respect to short and long term security of supply developments and risk assessments in the internal and international oil and gas market.

2. Agreements with partner countries;

C. The concrete measures to be taken to implement the action

1. Analysis of relevant economic and political developments affecting the internal and international oil and gas markets (bi-annual workshop)

2. Analysis of the impact of relevant Community legislation by evaluating public and other sources (workshops with MS and Candidate Countries, when necessary and appropriate)

3. Conduct a permanent dialogue with partner countries (roundtable every two years, supplemented by bilateral meetings)

D. The immediate outputs of each action, and their contribution to

Issue an annual report including recommendations if appropriate which identifies the development of the main political, economic and technical challenges, risks and opportunities to the EU oil and gas supply in the short and long term and the well functioning of the internal and, as far as relevant, international oil and gas markets.

E. The expected outcomes solving needs or problems

Adopt policy measures in line with the requirements of short and long term secure oil and gas supplies

2. Contribute to the implementation of a system for the physical monitoring of the oil and gas infrastructures inside and outside of the EU:

A. The target population(s) (specify number of beneficiaries if possible)

Commission, Member States, relevant industry and partner countries

B. The specific objectives set for the programming period (in measurable terms)

Develop a monitoring system for accident prevention and, if case may be, intervention, in strategic oil, gas and petroleum products infrastructure, based, among other things, on satellite communication system (Galileo)

C. The concrete measures to be taken to implement the action

1. Collect, update and analyse available information on relevant gas and oil infrastructure.

2. Launch of a technical and economic feasibility study of the design of a pan-European dispatching model for oil and gas involving a satellite based communication system (Galileo) as well as develop a computer based pan-European dispatching model for oil and gas.

4. Analysis and (as far as possible) implementation of the results of the study.

5. Launch of negotiations with partner countries on their inclusion in the monitoring system (roundtable in 2006, bilateral meetings covered by measure 1C31)

6. Elaboration of a technical and physical implementation plan of the monitoring system (experts).

D. The immediate outputs of each action, and their contribution to

1. Complete survey of relevant infrastructure inside and outside the EU.

2. Assessment of technical features and economic costs of the monitoring system.

3. Agreement with partner countries on their inclusion in the monitoring system.

4. Disposition of a technical and physical implementation plan of the monitoring system.

E. *The expected outcomes solving needs or problems*

Contribution to the implementation of the monitoring system

3. Monitor oil and gas supplies to the EU and the procedures aimed at guaranteeing the security of these supplies in emergency cases

A. *The target population(s) (specify number of beneficiaries if possible)*

Commission, Member States, relevant industry and partner countries

B. *The specific objectives set for the programming period (in measurable terms)*

1. Identification of potential challenges and development of appropriate policy measures.
2. Minimising the impact of emergency measures on the well functioning of the internal energy market.

C. *The concrete measures to be taken to implement the action*

1. Monitoring oil and gas demand and supply developments by analysing relevant information (subscription, regular workshop with Member States, industry and partner countries).

2. Monitoring the transposition and implementation of the relevant Community legislation on security of oil and gas supply (study, one follow-up meeting in 2007).

3. Investigate and evaluate Member State policies in emergency cases and analyse their impact on the internal market (study in 2004, precedent meetings with MS, then annual meetings).

4. Prepare input to Commission with a view to updating and appropriately amending security of supply legislation based on the findings from the above meetings.

5. Develop security of supply standards applicable to all Member States (study).

D. *The immediate outputs of each action, and their contribution to*

To ensure up to date measures and policies with respect to the respective supply situation.

E. *The expected outcomes solving needs or problems*

Being prepared for future challenges of secure oil and gas supplies

4. Monitor the level of oil and gas stocks as well as stocks of oil products and the procedures for their use, the implementation of measures to reduce oil and oil product consumption as well as the procedures applied with regard to access to gas storage including aspects of market dominance in relation to access to storage

A. *The target population(s) (specify number of beneficiaries if possible)*

Commission, Member States, relevant industry and partner countries

B. The specific objectives set for the programming period (in measurable terms

1. Maintaining adequate levels of oil stocks and gas storage facilities.
2. Set up of recommendations for the use of stocks.
3. Identification of means to reduce oil and oil product consumption.
4. Set up of recommendations for a code of good conduct to ensure non-discriminatory, transparent and cost-effective access to gas storage facilities.

C. The concrete measures to be taken to implement the action

- 1. Monitor and analyse stock developments including the identification of a mechanism to gather relevant data (workshops, study, follow up workshop).***
- 2. Analyse and identify appropriate stock levels against the background of specific supply situations.***
- 3. Launch a study on how to reduce oil and oil product consumption taking into account the most recent developments in the transport sector.***
- 4. Investigate TPA terms for gas storage facilities and identify best practices adapted to the respective situation (study, publication).***

D. The immediate outputs of each action, and their contribution to

1. Issuing quarterly reports on oil and gas stock developments and terms on access to storage (including tariffs).
2. Proposals for measures to reduce consumption of oil and oil products.

E. The expected outcomes solving needs or problems

1. Maintenance of adequate levels of stocks.
2. Improved third party access to gas storage also to avoid market dominance of certain players.
3. Contribution to reduced level of oil and oil product consumption.

5. Create a basis of objective, reliable and comparable data as a basis for fulfilling the above tasks

A. The target population(s) (specify number of beneficiaries if possible)

Commission, Member States, relevant industry and partner countries

B. The specific objectives set for the programming period (in measurable terms

Creation of EU data base to facilitate and enable the above actions.

C. The concrete measures to be taken to implement the action

- 1. Launch a study to identify the most appropriate design of the database.***

2. Develop a mechanism to establish the database, collect and update the relevant data.

3. Organise workshops to take account of methodological changes with respect to data acquisition and interpretation.

D. The immediate outputs of each action, and their contribution to

Identification of the most appropriate design of the database and a mechanism to collect and update the relevant data.

E. The expected outcomes solving needs or problems

Provide the relevant database for the work of the Observatory.

5.3. Methods of implementation

The European Observation System for oil and gas supply is run by the Commission and located at Commission premises. Human resources of the observation system will be gradually phased-in as from 2004, starting with around 8 people. Estimated HR needs at cruising speed, that will be reached around 2006, stand at 13 people and it is foreseen that five Commission officials (one of them will act as head of the observation system), five national experts seconded from their government and three temporary agents should contribute to the objectives of the observation system.

It is also foreseen to benefit from the expertise of third country experts, paid by their governments and without any financial implication for the Community budget.

6. FINANCIAL IMPACT

6.1. Total financial impact on Part B - (over the entire programming period)

(The method of calculating the total amounts set out in the table below must be explained by the breakdown in Table 6.2.)

6.1.1. Financial intervention

Commitments in €million (to the 3rd decimal place)

Breakdown	2004	2005	2006	2007	2008	2009 and subs. years	Total
Action 1							
Action 2							
Etc.							
TOTAL							

6.1.2. *Technical and administrative assistance, support expenditure and IT expenditure (Commitment appropriations)*

	2004	2005	2006	2007	2008	2009 and subs. years	Total
1) Technical and administrative assistance							
a) Technical assistance offices							
b) Other technical and administrative assistance: - intra muros : - extra muros :		0,1	0,3				0,4
<i>of which for construction and maintenance of computerised management systems</i>		0,1	0,3				0,4
Subtotal 1	0	0,1	0,3	0	0	0	0,4
2) Support expenditure							
a) Studies	0,275	0,885	1,310	0,650	0,300	0	3,420
b) Meetings of experts	0	0	0	0	0	0	0
c) Information and publications	0,063	0,151	0,111	0,111	0,111	0,111	0,658
Subtotal 2	0,338	1,036	1,421	0,761	0,411	0,111	4,078
TOTAL	0,338	1,136	1,721	0,761	0,411	0,111	4,478

6.2. Calculation of costs by measure envisaged in Part B (over the entire programming period)¹

(Where there is more than one action, give sufficient detail of the specific measures to be taken for each one to allow the volume and costs of the outputs to be estimated.).

For this table, please see Annex 1.

Commitments in €million (to the 3rd decimal place)

Breakdown	Type of outputs (projects, files)	Number of outputs (total for years 1...n)	Average unit cost	Total cost (total for years 1...n)
	1	2	3	4=(2X3)
<u>Action 1:</u> - Measure 1: - Measure 2 <u>Action 2</u> - Measure 1 - Measure 2 - Measure 3 Etc.				
TOTAL COST				

If necessary explain the method of calculation

7. IMPACT ON STAFF AND ADMINISTRATIVE EXPENDITURE

The needs for human and administrative resources shall be covered within the allocation granted to the managing DG in the framework of the annual allocation procedure.

7.1. Impact on human resources

Calculations are based on the cruising speed situation.

Types of post	Staff to be assigned to management of the action using existing and/or additional resources	Total	Description of tasks deriving from the action

¹ For further information see a separate guidance paper

		Number of permanent posts	Number of temporary posts		
Permanent officials or Temporary staff	A	5	3	8	
	B				
	C				
Other human resources			5 (END)	5	
Total		5	8	13	

7.2. Overall financial impact of human resources

Type of human resources	Amount €	Method of calculation *
Officials	0,54	0,108 per official
Temporary staff	0,324	0,108 per temporary agent
Other human resources END A7003 (give budget line)	0,215	0,043 per END
Total	1,079	

The amounts are total expenditure for twelve months.

7.3. Other administrative expenditure deriving from the action

Budget line (number and heading)	Amount €	Method of calculation
Overall allocation (Title A7)		
A0701 – Missions	0,1	
A07030 – Meetings	0,1	
A07031 – Compulsory committees ⁽¹⁾		
A07032 – Non-compulsory committees ⁽¹⁾		
A07040 – Conferences	0,312	
A0705 – Studies and consultations		
... Other expenditure (state which)		
Information systems (A-5001/A-4300)		
Other expenditure - Part A (state which)		
Total	0,512	

The amounts are total expenditure for twelve months.

⁽¹⁾ Specify the type of committee and the group to which it belongs.

I.	Annual total (7.2 + 7.3)	1.590.667	€
II.	Duration of action	6	Years
III.	Total cost of action (I x II)	9.544.002	€

8. FOLLOW-UP AND EVALUATION

8.1. Follow-up arrangements

The work programme of the observatory will be drawn up and approved in the framework of the normal DG TREN work programme.

8.2. Arrangements and schedule for the planned evaluation

See above.

9. ANTI-FRAUD MEASURES

The observatory will employ a number of important rules with respect to financial and administrative control, which will be adapted to features of the action concerned. These rules and procedures will be applied throughout the whole period of the actions. they concern in particular:

- before the signature of contracts: a qualitative and financial analysis of offers or proposals and, if case may be, the involvement of other services of the Commission with a view to avoid duplication of work.
- after the signature of contracts: examination of the list expenditures before payment at several levels (financial and technical); successive payments in line with progress of work; internal audit:

Action	No	Type	Type of output	Number of output	Average unit cost	Total cost
			1	2	3	Total for 4=(2X3)
Action 1		Monitoring the functioning of the internal oil and gas market and the international oil and gas market				
	1D	Annual report including recommendation	Publication	6	40000	240000
Action 2		Contribute to the implementation of a system for the physical monitoring of the oil and gas infrastructure inside and outside the EU				
	2 2C21	Dispatching model	Study	1	1800000	1800000
	2C22	Computer model	Software	1	400000	400000
	2C6	Implementation plan	Study	1	250000	250000
Action 3		Monitor oil and gas supplies to the EU and procedures aimed at guaranteeing the security of these supplies in emergency cases				
	3 3C11	Subscription and purchase of relevant material		6	15000	90000
	3C21	Transposition of relevant Community legislation	Study	1	120000	120000
	3C3	Study on emergency cases and impact on internal market	Study	1	250000	250000
	3C5	Security Standards	Study	1	250000	250000

Action 4	Monitor the level of oil and gas stocks as well as stocks of oil products and the procedures for their use, the implementation of measures to reduce oil and oil product consumption as well as the procedures applied with regard to access to gas storage including aspects of market dominance in relation to access to storage					
4C12	Identification of appropriate stock levels	Study	1	150000	150000	
4C3	Oil reduction	Study	1	200000	200000	
4C41	TPA to storage	Study	1	150000	150000	
4C42	publication of study findings	Publication	1	40000	40000	
4D1	Oil and gas stock development	Publication	11	8000	88000	
Action 5	Create a basis of objective, reliable and comparable data as a basis for fulfilling the above tasks					
5 5C1	Database design	Study	1	250000	250000	
5C2	database mechanism		5	40000	200000	
	total				4478000	

LEGISLATIVE FINANCIAL STATEMENT

Policy area(s): Energy

Activity(ies): Underpinning the security of oil and gas supply to the European Union

TITLE OF ACTION: CONVENING A COMMITTEE TO ASSIST THE COMMISSION IN CASE OF SUPPLY CRISIS (OIL)

1. BUDGET LINE(S) + HEADING(S)

Budget line: A07031, heading: Meetings and convocation in general

2. OVERALL FIGURES

2.1 Total allocation for action (Part B): €million for commitment: none

2.2 Period of application:

2004 to 2009 and subsequent years

2.3 Overall multiannual estimate on expenditure: 0,24 M€

a) Schedule of commitment appropriations/payment appropriations (financial intervention) (*see point 6.1.1*)

€million (to 3rd decimal place)

	2004	2005	2006	2007	2008	2009 and subs. years	Total
Commitments							
Payments							

b) Technical and administrative assistance and support expenditure(*see point 6.1.2*)

Commitments							
Payments							

Subtotal a+b							
Commitments							
Payments							

c) Overall financial impact of human resources and other administrative expenditure (*see points 7.2 and 7.3*)

Commitments/ payments							
--------------------------	--	--	--	--	--	--	--

TOTAL a+b+c							
Commitments	0,08	0,04	0,04	0,04	0,04	0,04	0,28
Payments	0,04	0,04	0,04	0,04	0,04	0,04	0,24

2.4 Compatibility with the financial programming and the financial perspective

- Proposal compatible with the existing financial programming
- This proposal will entail reprogramming of the relevant heading in the financial perspective
- This may entail application of the provisions of the Interinstitutional Agreement.

2.5 Financial impact on revenue¹:

- No financial implications (involves technical aspects regarding implementation of a measure)

OR

- Financial impact – the effect on revenue is as follows:

Note: All details and observations pertaining to the method of calculating the effect on revenue should be included in a separate annex.

€million (to 1 decimal place)

		Prior to action (Year n-1)	Situation following action					
Budget line	Revenue		Year n	n+1	n+2	n+3	n+4	n+5
	a) Revenue in absolute terms							
	b) Change in Revenue	Δ						

(Please state each budget line involved, adding the appropriate number of rows to the table if there is an effect on more than one budget line)

3. BUDGET CHARACTERISTICS

Type of expenditure		New	EFTA participation	Participation applicant countries	Heading Financial Perspective
<u>Comp/</u> <u>Non-comp</u>	<u>Diff/</u> <u>Non-diff</u>	<u>YES/</u> <u>NO</u>	<u>YES/NO</u>	<u>YES/NO</u>	No

¹ For further information see a separate guidance paper

4. LEGAL BASIS

Art 95 EUT

5. DESCRIPTION AND GROUNDS

5.1 Need for Community intervention ²

5.1.1 Objectives pursued

The European Union has to cope with a rising dependency on oil supply from external sources. This entails physical and economic risks, as most of the producer countries are located in politically rather unstable regions. In view of the immense importance of a secure oil supply for the European economies and societies, the Commission has proposed, as an outcome of the debate on the Green Paper “Towards a European strategy for the security of energy supply” a Community framework designed to ensure a secure supply of oil also in the future.

However, in case of emergency and /or crisis situations, it cannot be excluded that a secure oil supply is put on jeopardy due to physical interruptions and/or dramatically high prices. In order to cope efficiently and with only the least possible delay, the Commission has proposed a genuine decision-making mechanism under which the European Union will be able to define rapidly and efficiently the most appropriate response to a actual or potential threat.

This decision-making process involves Member States who will be convened in order to assist the Commission to define the most appropriate action in a given emergency or crisis situation.

5.1.2 Measures taken in connection with ex ante evaluation

In the framework of the oil crisis in autumn 2000 and while preparing the debate on the Green Paper, the Commission has carried out several in-depth analysis on crisis mechanisms currently in force (such as the IEA mechanism) and came to the conclusion that these mechanisms would be inadequate in a given crisis. These conclusions are reflected in the Green Paper and in the Communication of the Commission on oil supply³. As a result, the Commission proposes a new Community framework for security of oil and gas supplies, which foresees the above-mentioned new decision-making process.

5.1.3 Measures taken following ex post evaluation

(Where a programme is being renewed the lessons to be learned from an interim or ex post evaluation should also be described briefly.)

5.2 Actions envisaged and arrangements for budget intervention

not applicable

² For further information see a separate guidance paper

³ COM(2000)769

5.3 Methods of implementation

The Committee will be chaired by the Commission, which is assisted by representatives of Member State.

6. FINANCIAL IMPACT

6.1 Total financial impact on Part B - (over the entire programming period)

not applicable

6.1.1 Financial intervention

Commitments in €million (to the 3rd decimal place)

Breakdown	Year N	N + 1	N + 2	N + 3	N + 4	N + 5 and subs. years	Total
Action 1							
Action 2							
Etc.							
TOTAL							

6.1.2 Technical and administrative assistance, support expenditure and IT expenditure (Commitment appropriations)

	Year N	N + 1	N + 2	N + 3	N + 4	N + 5 and subs. years	Total
1) Technical and administrative assistance							
a) Technical assistance offices							
b) Other technical and administrative assistance: - intra muros : - extra muros : <i>of which for construction and maintenance of computerised management systems</i>							
Subtotal 1							
2) Support expenditure							
a) Studies							
b) Meetings of experts							
c) Information and publications							

Subtotal 2							
TOTAL							

6.2 Calculation of costs by measure envisaged in Part B (over the entire programming period)¹

not applicable

Commitments in €million (to the 3rd decimal place)

Breakdown	Type of outputs (projects, files)	Number of outputs (total for years 1...n)	Average unit cost	Total cost (total for years 1...n)
	1	2	3	4=(2X3)
<u>Action 1</u> - Measure 1 - Measure 2 <u>Action 2</u> - Measure 1 - Measure 2 - Measure 3 Etc.				
TOTAL COST				

If necessary explain the method of calculation

7. IMPACT ON STAFF AND ADMINISTRATIVE EXPENDITURE

The needs for human and administrative resources shall be covered within the allocation granted to the managing DG in the framework of the annual allocation procedure.

7.1 Impact on human resources

not applicable

Types of post	Staff to be assigned to management of the action using existing and/or additional resources		Total	Description of tasks deriving from the action
	Number of permanent posts	Number of temporary posts		
Permanent officials or Temporary staff	A B C			
Other human resources				

¹ For further information see a separate guidance paper

Total				
-------	--	--	--	--

7.2 Overall financial impact of human resources

not applicable

Type of human resources	Amount €	Method of calculation *
Officials		
Temporary staff		
Other human resources (give budget line)		
Total		

The amounts are total expenditure for twelve months.

7.3 Other administrative expenditure deriving from the action

Budget line (number and heading)	Amount €	Method of calculation
Overall allocation (Title A7)		
A0701 – Missions		
A07030 – Meetings		
A07031 – Compulsory committees ⁽¹⁾	0,04	
A07032 – Non-compulsory committees ⁽¹⁾		
A07040 – Conferences		
A0705 – Studies and consultations		
... Other expenditure (state which)		
Information systems (A-5001/A-4300)		
Other expenditure - Part A (state which)		
Total	0,04	

The amounts are total expenditure for twelve months.

⁽¹⁾ Specify the type of committee and the group to which it belongs.

I.	Annual total (7.2 + 7.3)	40 000	€
II.	Duration of action	6	Years
III.	Total cost of action (I x II)	240 000	€

8. FOLLOW-UP AND EVALUATION

8.1 Follow-up arrangements

The Commission will take care for the correct implementation of the decisions taken by the Committee. In particular, it will ensure that the internal rules of procedure are adequate and strictly followed by Committee Members.

8.2 Arrangements and schedule for the planned evaluation

If necessary and appropriate, the Commission will issue recommendation and/or proposals to streamline the work of the Committee.

9. ANTI-FRAUD MEASURES

not applicable

LEGISLATIVE FINANCIAL STATEMENT

Policy area(s): Energy

Activity(ies): Underpinning the security of oil and gas supply to the European Union

TITLE OF ACTION: CONVENING A COMMITTEE TO ASSIST THE COMMISSION IN CASE OF SUPPLY CRISIS (GAS)

1. BUDGET LINE(S) + HEADING(S)

Budget line: A07031, heading: Meetings and convocation in general

2. OVERALL FIGURES

2.1 Total allocation for action (Part B): €million for commitment: none

2.2 Period of application:

2004 to 2009 and subsequent years

2.3 Overall multiannual estimate on expenditure: 0,24 M€

a) Schedule of commitment appropriations/payment appropriations (financial intervention) (*see point 6.1.1*)

€million (to 3rd decimal place)

	2004	2005	2006	2007	2008	2009 and subs. years	Total
Commitments							
Payments							

b) Technical and administrative assistance and support expenditure(*see point 6.1.2*)

Commitments							
Payments							

Subtotal a+b							
Commitments							
Payments							

c) Overall financial impact of human resources and other administrative expenditure (*see points 7.2 and 7.3*)

Commitments/ payments							
--------------------------	--	--	--	--	--	--	--

TOTAL a+b+c							
Commitments	0,08	0,04	0,04	0,04	0,04	0,04	0,28
Payments	0,04	0,04	0,04	0,04	0,04	0,04	0,24

2.4 Compatibility with the financial programming and the financial perspective

- Proposal compatible with the existing financial programming
- This proposal will entail reprogramming of the relevant heading in the financial perspective
- This may entail application of the provisions of the Interinstitutional Agreement.

2.5 Financial impact on revenue¹:

- No financial implications (involves technical aspects regarding implementation of a measure)

OR

- Financial impact – the effect on revenue is as follows:

Note: All details and observations pertaining to the method of calculating the effect on revenue should be included in a separate annex.

€million (to 1 decimal place)

		Prior to action (Year n-1)	Situation following action					
Budget line	Revenue		Year n	n+1	n+2	n+3	n+4	n+5
	a) Revenue in absolute terms							
	b) Change in Revenue	Δ						

(Please state each budget line involved, adding the appropriate number of rows to the table if there is an effect on more than one budget line)

3. BUDGET CHARACTERISTICS

Type of expenditure		New	EFTA participation	Participation applicant countries	Heading Financial Perspective
<u>Comp/</u> <u>Non-comp</u>	<u>Diff/</u> <u>Non-diff</u>	<u>YES/</u> <u>NO</u>	<u>YES/NO</u>	<u>YES/NO</u>	No

¹ For further information see a separate guidance paper

4. LEGAL BASIS

Art 95 EUT

5. DESCRIPTION AND GROUNDS

5.1 Need for Community intervention ²

5.1.1 Objectives pursued

Despite the considerable achievements in terms of introducing competition on the European natural gas market, the gas market is still in a transitional period. The Commission has to closely follow the developments in order to help competition gaining ground. For this reason, a close co-operation between the Commission and the Member States is necessary.

In an integrated competitive internal market for gas, emergency or crisis situation of gas supplies will affect a large number of customers, who are not likely to be located within the same national boundary. In order to maintain a secure gas supply to certain customers also in crisis situations, but also to ensure the least possible disturbances of the market in such situation, a co-ordination mechanism at Community level is necessary.

For these reasons, the new Community framework for secure gas and oil supplies requests the convocation of a Committee made up of representatives of Member States and chaired by the Commission.

5.1.2 Measures taken in connection with ex ante evaluation

The analysis carried out in the Green Paper “Towards a European strategy on energy supply” demonstrated clearly that imports of natural gas will grow and come from more distant regions. The new competitive market environment introduced by liberalisation did not enable full transparency in terms of security of supply policies. For these reasons the Commission proposes a new Community framework for security of oil and gas supplies, which foresees the above-mentioned new decision-making process.

5.1.3 Measures taken following ex post evaluation

(Where a programme is being renewed the lessons to be learned from an interim or ex post evaluation should also be described briefly.)

5.2 Actions envisaged and arrangements for budget intervention

not applicable

² For further information see a separate guidance paper

5.3 Methods of implementation

The Committee will be chaired by the Commission, which is assisted by representatives of Member State.

6. FINANCIAL IMPACT

6.1 Total financial impact on Part B - (over the entire programming period)

not applicable

6.1.1 Financial intervention

Commitments in €million (to the 3rd decimal place)

Breakdown	Year N	N + 1	N + 2	N + 3	N + 4	N + 5 and subs. years	Total
Action 1							
Action 2							
Etc.							
TOTAL							

6.1.2 Technical and administrative assistance, support expenditure and IT expenditure (Commitment appropriations)

	Year N	N + 1	N + 2	N + 3	N + 4	N + 5 and subs. years	Total
1) Technical and administrative assistance							
a) Technical assistance offices							
b) Other technical and administrative assistance: - intra muros : - extra muros : <i>of which for construction and maintenance of computerised management systems</i>							
Subtotal 1							
2) Support expenditure							
a) Studies							
b) Meetings of experts							
c) Information and publications							

Subtotal 2							
TOTAL							

6.1 Calculation of costs by measure envisaged in Part B (over the entire programming period)¹

not applicable

Commitments in €million (to the 3rd decimal place)

Breakdown	Type of outputs (projects, files)	Number of outputs (total for years 1...n)	Average unit cost	Total cost (total for years 1...n)
	1	2	3	4=(2X3)
<u>Action 1</u> - Measure 1 - Measure 2 <u>Action 2</u> - Measure 1 - Measure 2 - Measure 3 Etc.				
TOTAL COST				

If necessary explain the method of calculation

7. IMPACT ON STAFF AND ADMINISTRATIVE EXPENDITURE

The needs for human and administrative resources shall be covered within the allocation granted to the managing DG in the framework of the annual allocation procedure.

7.1 Impact on human resources

not applicable

Types of post	Staff to be assigned to management of the action using existing and/or additional resources		Total	Description of tasks deriving from the action
	Number of permanent posts	Number of temporary posts		
Permanent officials or A				

¹ For further information see a separate guidance paper

Temporary staff	B				
	C				
Other human resources					
Total					

7.2 Overall financial impact of human resources

not applicable

Type of human resources	Amount €	Method of calculation *
Officials		
Temporary staff		
Other human resources (give budget line)		
Total		

The amounts are total expenditure for twelve months.

7.3 Other administrative expenditure deriving from the action

Budget line (number and heading)	Amount €	Method of calculation
Overall allocation (Title A7)		
A0701 – Missions		
A07030 – Meetings		
A07031 – Compulsory committees ⁽¹⁾	0,04	
A07032 – Non-compulsory committees ⁽¹⁾		
A07040 – Conferences		
A0705 – Studies and consultations		
... Other expenditure (state which)		
Information systems (A-5001/A-4300)		
Other expenditure - Part A (state which)		
Total	0,04	

The amounts are total expenditure for twelve months.

⁽¹⁾ Specify the type of committee and the group to which it belongs.

I.	Annual total (7.2 + 7.3)	40 000	€
II.	Duration of action	6	Years
III.	Total cost of action (I x II)	240 000	€

8. FOLLOW-UP AND EVALUATION

8.1 Follow-up arrangements

The Commission will take care for the correct implementation of the decisions taken by the Committee. In particular, it will ensure that the internal rules of procedure are adequate and strictly followed by Committee Members.

8.2 Arrangements and schedule for the planned evaluation

If necessary and appropriate, the Commission will issue recommendation and/or proposals to streamline the work of the Committee.

9. ANTI-FRAUD MEASURES

not applicable