

Open Letter

To the Minister of Economy in Germany (Mr. Müller), EU-Commission and the German Gas and Industry Associations BGW, VKU, BDI and VIK.

**Further comment on the development of the VV gas
EFET position paper – 10th April 2000**

Introduction

The European Federation of Energy Traders (EFET) was set up in 1999. The group represents over 42 large energy trading companies across the European Union. Each member company in EFET supports the principles of an open energy market, in electricity and gas, which will allow fair competition and trade of energy throughout the European Union. EFET is pleased with the process of opening the electricity market in a number of countries and the status of the gas market in the United Kingdom. Some progress appears to be made in the Netherlands gas law. Developments in Germany appear to remain slow and difficult. On 25 February 2000, EFET sent an open letter to the German Ministry of Economics and the associations negotiating the Verbaendevereinbarung for gas (the "VV gas"). This letter identified several areas where we considered drafts of the VV gas needed improvement to facilitate gas competition and to enable market based prices for the benefit of customers.

On 17 March 2000 a "Framework Agreement" ("Eckpunktepapier") for the VV gas was signed by the Associations and approved by the Ministry. EFET will highlight only some of many elements where improvement is needed and will elaborate on the Eckpunktepapier in further notices to come.

Process

Deadlines for a finalised agreement have been and gone (Autumn 1999, end of 1999 and March 2000 being just three). Now it seems that it was again not possible to agree at all on the VV gas. Rather, only the barest principles have been outlined (in the form of the "Eckpunktepapier") with discussions then continuing until the required implementation of the Gas Directive in August 2000.

These principles are not sufficient in EFET's view, with a lot of vagueness and unclarity attached to this document. If these will become reality, German customers will not participate in "competitive" gas prices – like others do!

Tariff structure

Charges are proposed to be based on a contractual path basis (so called "transaction based charging"). Several points arise here:

- For each customer that a third party wishes to supply, it is necessary to identify, several weeks or months in advance, the input and the offtake points, and all the intervening gas grids (of which there may be several).
- If such a system of charging was approved, it would mean that each transportation quote would have to be individually calculated. This will mean delays of several weeks or months to get a quote for transporting gas, thereby making it almost impossible to provide a customer with a quote for competitive supply. First experience in the market shows that the grid companies refuse to offer quotes within reasonable timeframes. EFET believes, that one week time is more than enough to provide customers with a binding offer for transport. However, it is more likely that the BundesKartellAmt will be asked to step in at a very early stage.
- It is not clear that the transportation quote will comprise the most economic tariff possible. If transportation capacity is not available on (parts of) a particular route the grid operator has to provide the customer with the cheapest alternative route.
- The route proposed by the grid operators are arbitrary in the sense that there is no definition of "import level" or "distribution level", which severely affects the pricing of transportation. This has to be solved.
- "Transaction-based" charging has already been tried in the German electricity industry. The first VV for power (the "VVI") introduced transaction-based, pancaked, charging. This agreement was quickly superseded by a second agreement (the "VVII"). Apart from a charge across a north-south German divide, the VVII is not transaction dependent, and removes the multiple charging allowed by VVI.

This evolution is consistent with the views of the European Commission that transaction-based charging is not an appropriate way of charging for transportation. The “Eckpunktepapier”, however, does not take into account these experiences from the electricity sector.

- Levels of tariffs have not been officially published for the import and regional levels. Rumour that tariffs proposed are 2 to 6 times those levels seen in comparable gas systems. Tentative analysis (by Gasunie!) shows German tariffs to be above those of Belgium, France, the Netherlands and the United Kingdom.

In sum, it seems incomprehensible that the gas industry is proposing to agree to a charging mechanism that has already been abandoned by the electricity industry and specifically criticised by the European Commission.

Gas Quality

Two main gas qualities are supplied in Germany ("L" or low cal gas and "H" or high cal gas as described in the DVG-Guideline G 260). The German grid operators import (80% of requirements) or produce (20%) various types of gas. These varying qualities are then managed, by the grid operators, to ensure that customers can receive the gas quality they need. The “Eckpunktepapier” provisions for gas quality conversion are not sufficient. New entrants can only ensure compliance with the compatibility clause as long as they input gas to the system that is exactly the same quality as that being supplied to a customer. The rules specified are much too vague, because the criteria to apply quality conversion measures are not specified. EFET is sure that this is another example of third parties being treated differently to incumbents.

Given that the grid operators have been able to take various qualities of gas for years, this appears to be wholly discriminatory. EFET fully recognises that there may be costs associated with the conversion from L-Gas to H-Gas and vice versa. However, these costs have to be reasonable and efficiently allocated, through reference to cost actually incurred. In fact, we understand that the German grid operators have in the past said that quality conversion costs were low.

Also, the European Commission has made it very clear that a properly functioning transportation regime should include quality conversion charges. EFET considers the absence of such a necessary service to be a clear breach of the Gas Directive.

Input-output Balancing

EFET welcomes that balance of inputs and offtakes will have to occur on a daily basis, with monthly accounting. EFET understands this applies to all three levels of tariffs proposed by the "Eckpunktepapier".

Provisions for hourly balancing could be required under certain circumstances; it is not clear, however, who would be in a position to demand such an hourly balancing; if at all it should be under the jurisdiction of the customer using the grid for transportation.

Summary

EFET feels the need to add its views of establishing competition in energy in the European Union to the gas market debate in Germany, since it is felt that the right developments in Germany will help the opening of the gas market in a number of countries on the European continent. As the previous paper by EFET explained, the proposed VV gas will not deliver a competitive gas market in Germany. Indeed, it seems likely that the VV gas will serve to prolong, in large part, the incumbents' positions in their home markets rather than open these markets to competition. The result will be German customers paying higher prices than necessary. We note recent announcements by Thyssengas and Stadtwerke Leipzig that they will put gas prices up due to oil indexation.

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Disclaimer

This open letter is the official point of view of EFET after a careful consultation process.
Individual members might have a different point of view.