Energy: rules for the internal market in natural gas. 'Gas Directive'

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The Commission presents it report on progress in creating the internal gas and electricity market. It states that the financial crisis of 2008 and 2009 had a direct impact on the demand for energy, causing unpredicted falls in the price of oil on the international markets. This, in turn, impacted on gas and electricity prices. A dispute between two companies outside the EU (Gazprom of Russia and Naftogaz of Ukraine) led to an unprecedented crisis in the EU's gas supply, affecting several Member States. 2009 was also an important year because the third internal energy market package was adopted on 13 July 2009.

This report discusses how these developments have affected the EU electricity and gas markets over the past year and how they are likely to affect market developments in the future.

Implementation of legislation: in June 2009, the Commission initiated infringement procedures against 25 Member States for electricity and against 21 Member States for gas. The key violations identified lack of transparency, insufficient coordination efforts by transmission system operators to make maximum interconnection capacity available, absence of regional cooperation, lack of enforcement action by the competent authorities in Member1 States and the lack of adequate dispute settlement procedures4. In October 2009, the Commission launched further infringement proceedings against two Member States; these proceedings related to gas transit and storage.

Impact of the crisis: the financial crisis had a significant impact on the internal energy market during the reporting period. Year on year, the EU-27 electricity consumption remained relatively stable, but fell by 12% and 7% in April and May, respectively. The decline in gas consumption was even more significant. Between January and March 2009, gas consumption (in EU-27) dropped by around one fourth. This drop is partly due to the interruption of gas supplies from Russia via Ukraine, but even after the crisis in March 2009 EU-27 gas consumption was still more than 16% down on the March 2008 level.

The financial crisis has had a serious impact on the internal market for energy during the reporting period:

- on the one hand, it puts pressure on planned investments – due to possible financing difficulties and uncertainties affecting the supply side – and has resulted in a fall in demand, which is more pronounced for gas than for electricity;
- on the other hand, it has created new opportunities for competition, since more gas is available at lower prices on liquid hubs;
- furthermore, the situation with excess supply in gas markets may pave the way for final consumers to see gas prices that are based on the supply and demand for gas rather than on the price of oil.

Price trends: although reduced gas and electricity consumption has had an impact on end-user prices, the fall witnessed in wholesale energy costs has not been entirely reflected in end user prices. Overall, prices in the first half of 2009 were still higher than in the first half of 2008. The trend in retail prices was quite diverse, suggesting perhaps an insufficient level of market integration at retail level.

Customer dimension: the information available for the number of consumers having switched supplier makes it difficult to gain an overall picture of the changes that have occurred across Member States. There are significant differences between the member states with more mature markets, such as the UK, which

have relatively high switching rates, and a number of others showing little or no activity. At the level of small industry and households, the reported figures suggest that electricity consumers tend to be more active than gas consumers.

National regulatory authorities: the work of national regulatory authorities tends to shift the focus towards the consumer, including the **roll-out of smart meters** as the key to smart grids in the internal energy market. This is a welcome trend for the deployment of active participation by customers in the internal energy market and increased energy efficiency and large-scale integration of renewables, as well as additional energy services, increased market transparency and easier supplier switching.

Additionally, cooperation between European power exchanges, as well as the ongoing trend of increasing trade, is a promising sign of functioning markets. However, even if there are positive signs on the retail and wholesale level, **the degree of market concentration has not changed very much**. On gas wholesale markets, the concentration remains high. In 10 Member States, the three largest wholesalers have a market share of 90% or more. In the electricity retail market, the market share of the three largest companies in the retail market as a whole was above 80% in 14 Member States.

Security of supply: a major challenge in the context of the economic crisis is to **maintain the investments in energy infrastructure**. The financial crisis risk resulting in postponed or annulled energy infrastructure investments and as a result the EU faces an increased risk of lack of or delay in construction of infrastructure to meet future supply needs. This is a particular concern in a situation where the energy sector needs to be reshaped to address the challenges of climate change and energy security. In order to help to address this risk and to help economic recovery, the EU is facilitating the financing of energy infrastructure projects via the Economic Recovery Plan. In particular, the Plan includes 2 365 billion to support a number of key electricity and gas interconnection projects. The Commission's commitment to encourage infrastructure investments will continue with the adoption, at the end of 2010, of an infrastructure package.

Internal market: the third package adopted in 2009 also provides for clearer sector specific rules and thus for incentives to invest. The Commission is preparing for the application of the third package in developing, together with ERGEG and ENTSO-E and ENTSO-G, pilot framework guidelines and codes. The Commission will assist Member States in implementing the third package and will continue to pursue the full and correct implementation of the second package, including through formal infringement procedures.

Not only investments but also the implementation of more active transmission and distribution systems in the form of smart meters and smart grids are central to the development of the internal market for energy. If needed, the Commission will not limit its action to energy regulation and will not hesitate to use its powers under competition law.