



Will the European Commission's policy hinder gas supplies to Central and Eastern European countries? OPAL case decision



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ABSTRACT

Natural gas has become one of the most important sources of energy. The liberalization of the gas sector in the last decades brought a dynamic development of the energy infrastructure in the EU. Thus it must be underlined that the liquidity of the gas market is dependent on the outside supplies. The study examines the European Commission's Policy taking into consideration specifically its decision on the exemption of OPAL gas pipeline from EU rules. The main question is what would be the long term effect of such policy. In the authors opinion there are several serious doubts whether the Commission has made an appropriate decision. The major one concentrate on the impact of the decision, which according to the Commission refers only to Germany and Czechia gas market. Nevertheless an analysis of gas flow based on the ENTSG leads to a conclusions that decision could have a substantial influence on Slovakia and Poland. If so, under the EU provisions the investment can not be excluded from the EU rules. Therefore the authors will analyze step by step the Commission decision and present its possible future impact on the internal energy market.

1. Introduction

The recent decades have brought dynamic expansion of the European Union's energy infrastructure at all levels. On one hand, this state is the result of liberalizing the energy market, which forces technological advancement, on the other hand, the policy of the EU, aimed at, i.a., supporting projects relevant to its power safety (Jones, 2010; Cherp, 2012). Some of the projects in question, such as interconnections, were deemed so important that the need of their development was regulated in the EU original law, i.e., art. 194 par. 1 letter d of the TFEU. Such an approach is in line with the internal market concept, which is intended to mitigate the barriers in the access to individual domestic markets.

The network infrastructure, necessary for the effective functioning of the power system is a special case (Diaz, 2012). It is the case especially in relation to the gas market, with its liquidity depending on the supplies from outside of the EU. However, a liberalized and competitive market is not always able to guarantee a return on investment in the infrastructure, which increases, after all, the competition and safety of the supplies (Erdmann, 2006; Spanier, 2008). We need to remember, that the mechanism adopted in EU legislation, related to the remuneration of transmission system operators, based on administratively approved tariffs, does not fully take into account the risk

associated with new investments. It results from the fact that it is hard to estimate and reflect in the tariffs, which negatively impacts new investments. As a result, there was a need to provide the investors, who decided to make infrastructural investments, with a higher and more stable source of revenues (Cameron, 2010). As a consequence, already in the second energy package, solutions were provided for, which enables the exemption of significant new infrastructure from basic market liberalization principles (Ferman, 2009). Nonetheless, in order for the applied decision to be made, it is necessary to fulfil a number of conditions, which, although have been indicated numerus clausus in the regulations governing the functioning of the natural gas internal market, in the eyes of the authors require consideration in a broader context (Jones, 2010).

The aim of this paper is an attempt to analyze and assess the decision of the European Commission (hereinafter referred to as EC) of 28th October 2016, which notifies the exemption of the Ostseepipeline-Anbindungsleitung gas pipeline (hereinafter referred to as OPAL) from the liberalization principles stipulated in the directive 2009/73/EC (EU, 2009) in light of its long-term impacts (Jansen et al., 2009). Particular attention shall be paid to the impact of the decision in question on the safety and diversification of natural gas supplies to the European Union and the competition on the natural gas internal market.

It is crucial to note that except for short popular-scientific studies,

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there is a lack of a comprehensive development in the literature, corresponding to the analysis carried out by the authors. The only scientific study of the topic includes “The Opal Exemption Decision: past, present, and the future” (Yafimava, 2017) publication prepared by Katja Yafimava. However, this publication does not take into account the analysis from the perspective of Article 36 of Directive 2009/73/EC, and due to the publication date, it does not include the relocation test of natural gas volumes after 1 January 2017.

This publication consists of four basic sections, i.e. introduction, discussion of the European Commission initial decision of 2009, the Commission decision of 2016, and conclusion. The core of this article is the third section (divided into two subsections) that includes the legal assessment of specific terms of new exclusion, especially through the prism of premises resulting from Article 26 of Directive 2009/73/EC and the impact of the new decision on relocation of gas volumes.

The basic test method adopted in this paper is the dogmatic and legal method. The primary and secondary sources of the EU law, soft law of the European Commission, but also, in a limited scope the EU case-law (Court of Justice of the European Union and the General Court) were analysed.

2. Original decision of the Commission

The commented EC decision (EU, 2009) is, in fact, an extension of the position adopted by this body in 2009. As per the adopted legislation (art. 22 par. 4 of the directive 2003/55/EC, currently 36 par. 8 of the directive 2009/73/WE), the impetus for the EC to take the position was the notification of the decision by the national regulatory body - in the discussed case, the Bundesnetzagentur (hereinafter referred to as BNetzA) of 25th February 2009 on exempting the regulated Third Party Access and tariffs in relation to the OPAL gas pipeline (Kopp, 2014). In light of the decision by the German regulatory authority,¹ the exemption included the entire transit capacity of the gas pipeline along the Greifswald (entry point) - Brandov (exit point) section, over a period of 22 years, starting from the date of its commissioning.² Ultimately, however, the Commission voiced significant concerns regarding the above-mentioned decision, indicating that in the original wording it may have adverse impact on the competition in the natural gas wholesale market (both, downstream and upstream) in the Czech Republic, inter alia, by strengthening the position of Gazprom.³ As a consequence, pursuant to art. 22 par. 4 of the directive 2003/55/WE (EU, 2003a, 2003b), the Commission called BNetzA to introduce changes limiting the possibility to reserve available throughput capacity (hereinafter referred to as capacity) at the gas pipeline exit point, i.e., in the city of Brandov, at the German - Czech border, by entities having the dominant position on the upstream and downstream natural gas market in the Czech Republic and the entities supplying natural gas to the Czech Republic. The relevant changes were made on 7th July 2009. As a consequence, the exemption of the OPAL gas pipeline from the principles provided for in the liberalization directives was conditioned on stringency in the scope of reserving the available capacity by individual entities and a program of releasing gas prices. In reality, power companies having a dominant position in the upstream segment (OAO Gazprom) and the downstream segment (RWE Transgaz) of the

natural gas wholesale market in the Czech Republic were able to jointly⁴ reserve up to 50% of the gas pipeline capacity cap at the Brandov exit point.⁵ However, this restriction was only of relative character, since it was not subject to abolition in the case of the dominants implementing a programme releasing natural gas prices (sales within the auctions) at a level of 3 bn m³ a year (which was supposed to be the minimum security for the development of competition in the Czech gas market). However, in practice, this programme was not implemented,⁶ i.e., due to the lack of an actual intent on the Gazprom and Gazprom Expert sides for such a form of sales⁷ due to the circumstance that the adopted level of 3 bn m³ did not reflect the actual market conditions⁸ (the situation on the Czech gas market changed substantially, i.e., contrary to the forecasts, natural gas demand decreased and the position of the RWE competitors on the downstream market strengthened).

In light of the above, on 12th April 2013, the interested parties, i.e., OPAL Gastransport GmbH & Co. KG, OAO Gazprom and OOO Gazprom Export filed a request to BNetzA to change the commented decision. The applicant indicated that due to the ineffectiveness of the total exemption of the OPAL gas pipeline from the obligation of third party access (Spanjer, 2008) and tariffing, the provisions restricting the possibility of using the existing infrastructure should be repealed. Following the taken actions, an agreement was concluded (First Settlement Agreement), which revised the original decision of 2009 in the scope filed by the entities initializing the review of the decision. Nonetheless, due to the extending notification procedure, the agreement expired (31st October 2014) without the EC making a formal decision.

3. Decision of the European Commission of 28th October 2016s

A successful attempt to amend the decision of 2009 was made in 2016. In May of 2016, BNetzA notified the Commission about a New Settlement Agreement. Essentially, it maintained the basic assumption set out in the first document, with the stipulation that they would remain valid until the end of July 2016 (after agreements between BNetzA and the Commission, the deadline was shifted to 31st October 2016).⁹ In this point, the authors will concentrate on presenting and assessing the legal basis for the decision and statistical data, the detailed conditions of the new exemption, including the ones from the perspective of the premises resulting to art. 36 of the directive 2009/73/EC, and the impact of the new decision on using other routes of gas transmission to the EU.

3.1. Legal basis for changing of the original decision

A fundamental procedural issue at the initial stage of the proceedings was the legal admissibility of revising the decision including the exemption of the new gas infrastructure, pursuant to art. 36 of the directive 2009/73/EC. It stems from the fact that the quoted provision does not directly refer to the possibility to amend a previously issued decision. Therefore, it seems that since the EU legislator did not

¹ In reality, these were two decisions. This article focuses solely on the decision BK7-08-009 regarding the limitation of the OPAL gas pipeline capacity, operated by OPAL Gastransport GmbH & Co. KG.

² This exemption did not include the capacity with the entry point in Greifswald and the exit point in Gross Körös, with the destination being the GASPOOL market (the regulated third party access was sustained).

³ The OAO Gazprom company, together with BASF SE, exercises ownership control over WIGA Transport Beteiligungs-GmbH & Co (remaining an 80% shareholder of the OPAL gas pipeline, 20% - E. ON Ruhrgas AG), which is in an indirect equity relationship with OPAL Gastransport GmbH & Co. KG, which is an 80% operator of the transmission system for the OPAL gas pipeline. The remaining 20% capacity operator is Lubmin-Brandov Gastransport GmbH belonging to E. ON Ruhrgas AG.

⁴ Due to binding long-term vertical contracts between Gazprom and RWE Transgaz, the possibility to reserve 50% of the capacity needs to be considered jointly.

⁵ It should be noted that natural gas transported via the OPAL gas pipeline over the section from the entry in Greifswald to the exit in Brandov remains the property of OOO Gazprom Export, which in practice, makes the 50% restriction apply only to reserving the capacity by Gazprom.

⁶ It is worth adding that the decision of 2009 did not oblige Gazprom to implement a gas release programme, as long as the 50% capacity reservation limit was respected by the entity, item 102 of the Commission decision.

⁷ Despite having expressed formal consent.

⁸ It is also worth to indicate the fact that the lack of interest in the programme resulted also from commissioning a GASPOOL hub, which enabled potential buyers from the Czech Republic access to a relatively liquid gas market.

⁹ At the same time, in agreement with the German regulatory body, the Commission extended the notification procedure, also until 31st October 2016.

introduce relevant legal solutions in this matter, the admissibility of the EC to recognize the notified decision is limited. All the more that the legislator had already had the opportunity to make relevant amendments by adopting the directive 2009/73/EC (which extended the legal solution concerning the exemption from the scope of market liberalization principles provided for in the directive 2005/55/EC). At the same time, the Commission refers to the examples, which justify the possibility of revising the decisions, which have long-term effects, i.e., in relation to concentration (EU, 2004) and antitrust proceedings (EU, 2003a, 2003b). Nonetheless, it needs to be emphasized that these circumstances were directly expressed in the sources of EU legislature - contrary to the manner in the commented case. Therefore, there is a reasonable doubt, whether such a selection of arguments was appropriate. On the other hand, as stated by the Commission, the authorization to amend a decision exempting certain entities from the obligations under EU law results from the general standards of the administrative law (item 18 of the EC decision). As a rule of thumb, the decision regarding the exemption falls within the competence of national regulatory bodies, and the possibility to revise it results from the internal legislation of a Member State (Jones, 2010; Roggenkamp et al., 2016). Thus, the Commission should have the opportunity to make a statement in a situation, in which national legislation allows for the possibility to amend a commented decision. Otherwise, it could lead to a clash with the assumptions, on which art. 36 of the directive 2009/73/EC is based, hence, making it impossible to effectively control the exemptions of new significant infrastructure by the Commission. Unquestionably however, in the absence of regulations explicitly granting the Commission with a power to amend a previous exemption decision, it is necessary for significant factor to occur, which would motivate such an action. In this case, it will be crucial to indicate that these circumstances are independent from the will of the applicant and that they significantly impact the legitimacy of exempting a given infrastructure, to an extent specified by the original decision.

3.2. New conditions of exemption

The formal decision, which notified the amendments in the scope of using the OPAL gas pipeline (in the part belonging to WIGA Transport Beteiligungs-GmbH & Co), which is operated by OPAL Gastransport GmbH & Co. KG - OGT,¹⁰ was made by the Commission on 28th October 2016 (after introducing the amendments by BNetzA). As per its content:

- 50% capacity of the OPAL gas pipeline at the entry point in Greifswald and the exit point in Brandov (limited allocation) was exempted from the third party access principle (regulated) provided for in art. 32 of the directive 2009/73/EC and the tariff regulation, referred to in art. 41 of the directive 2009/73/EC („Exempted Coupled Interconnection Capacities”),
- OGT was obliged to offer at least 10% of the so-called FZK (firm freely allocable capacities) capacities with uninterrupted access to the GASPOOL zone (in a virtual trading point), within short and medium-term auctions at a tariff price as the base („FZK Partly Regulated Decoupled Interconnection Capacities”),
- OGT was obliged to offer for auction 40% of the so-called DZK (“firm dynamically allocable capacities”) capacity, with the entry point in Greifswald and the exit point in Brandov (uninterrupted) and an interrupted access to the GASPOOL zone (virtual trading point) at a tariff price as the base (“DZK Partly Regulated Decoupled Interconnection Capacities”),
- the entities holding the dominating position on the Czech gas market and the ones, which control more than 50% of the gas at the Greifswald entry point (Gazprom, Gazprom Export, RWE, etc.) can

apply for the reservation in question, at the base price - for the FZK capacity (item 32 of the EC decision).

3.3. Exemption prerequisites pursuant to art. 36 par. 1 of the directive 2009/73/EC

Verification whether the investment increases gas supply competition, influences gas supply security or whether it does not have adverse impact on the competition and functioning of the internal gas market is of basic importance for the conformity assessment of the exemption with art. 36 par. 1 of the directive 2009/73/EC (Roggenkamp et al., 2016). As a consequence, and due to a lack of impact of the commented decision on the decision of 2009 (item 56, 57, 60 of the EC decision), the authors shall limit the analysis of the remaining exempting premises, i.e., risk level, legal separation of the infrastructure owner from the system operator, in which the infrastructure is to be constructed, or levying the infrastructure users, to the a/m circumstances.

3.3.1. Safety and competitiveness of gas supplies

First of all, we need to consider whether an investment raises supply competition and increases gas supply security. Generally, it is assumed that the premise in question should be considered in the context of the fifth premise mentioned in the catalogue art. 36 par.1 of the directive 2009/73/EC, i.e., “the exemption must not be detrimental to competition ...”. This approach is also presented by the EC, which conducts a simultaneous analysis of these conditions. In the justification, the authority indicates that, although these premises are not identical, the element connecting them is the fact that the investment must have a pro-competitive nature and provide the consumers with benefits. Adopting such a position is appropriate, although certain distinguishing features need to be pointed out. Increasing competition in gas supplies should, contrary to the adverse impact on competitiveness (which is of negative nature), be considered as a positive premise of the investment itself. In other words, the investment as such, should provide specific benefits, significant from the functional perspective of the entire internal gas market. We believe that they should not be limited only to increasing the available capacities (SEC, 2009) but also create actual conditions, which will result in more new competitors (upstream) providing (selling) natural gas appearing on the market.¹¹ To support the above cited position, it is worth to quote the definition of a “supply”, normalized in art 2 item 7 of the directive 2009/73/EC, according to which, it is “a sale, including resale, of natural gas, including LNG, to consumers”. Hence, using the linguistic interpretation, increasing competition in gas supply should, first of all, lead to new gas providers appearing on the market, compared to the state before the investment. Such approach is, however, in opposition to the fact that the raw material transmitted through the OPAL gas pipeline (at the entry point in Greifswald and the exit point in Brandov) remains the property of Gazprom Export. In light of the above, in practice, only the technical connection with the NEL gas pipeline would enable gas supplies from a source other than the gas transmitted via the Nord Stream gas pipeline (item 28 and 111 of the EC decision). As a result, it can be concluded that this investment, due to its exemption from the basic market liberalization rules would rather strengthen the position of one provider than increase competition on the market (upstream).

Nevertheless, regardless of the above, in order to meet the first condition, which justifies the exemption (pursuant to art. 36 par. 1 of the directive 2009/73/WE) it is also necessary for the investment to achieve as high supply safety as possible. The EU legislator, using the “and” nexus, indicated a need for cumulative satisfaction of both criteria. The authors believes such an approach is correct. Because, it can be assumed that together with the growth of supply competition, the

¹⁰ The EC decision *senso stricto*, refers to the reservation of the gas pipeline capacity only at the exit point in Brandov (item 32 and 99 of the EC decision).

¹¹ At the same time, it is not necessary, to determine the relevant market at this point, since the commented premise refers generally to an internal gas market as a whole.

gas supply safety increases (the more different gas providers the smaller the risk that the gas supply continuity would be endangered if the material ceased to be supplied by one of them). At the same time, it seems to us that in relation to the adverse effect on the competition, the assessment of that premise should be broader, i.e., in light of the entire EU market, and not only limit to a particular relevant market.¹² Such an approach is indicated by the lack of reference to the relevant gas market in the first premise, i.e., art. 36 par. 1 let. of the directive 2009/73/EC.

In light of recital 22 of the Preamble to the directive 2009/73/WE “The safety of energy supplies to the Community requires, in particular, the assessment (...) of the level of dependence of the Community and individual Member States on energy supplies from third countries and the approach towards the national, as well as foreign energy trade and energy investments by a given third country”. Such a position was sustained in the regulation of the European Parliament and of the Council 994/2010 (SOS) on measures ensuring safety of natural gas supplies (EU, 2010). Pursuant to recital 7 of the Preamble of the said act “Diversification of the routes and sources for supplying the EU with gas is of crucial significance for improving the safety of supplies for the entire EU as well as individual Member States. The future safety of supplies will depend on changes in the structure of fuels, development of production in the EU and in the third party countries supplying it, as well as on the investments in warehouse facilities and the diversification of routes and sources for the gas supplies within the EU and outside of it, including systems for liquefied natural gas (LNG)”. Finally, art. 3 par. 1 of the cited legal act stipulates that “The joint responsibility for the gas supply safety rests on gas companies, Member States, in particular, through their relevant bodies and the Commission, within the limits of the activity and competence of each of these entities”.

The starting point to exempt the OPAL gas pipeline from liberalization principles, on the basis of the safety premise was the fact that this investment would help increase the market liquidity and lead to the formation of a new cross-border connection between Germany and the Czech Republic. Seemingly, such an approach is in line with the catalogue of measures aimed at ensuring gas supply safety, provided for in the SOS regulation (annex II) of the 994/2010 regulation. However, the Commission, when assessing the discussed premise, seems to completely ignore the issue of diversifying gas sources and gas supply routes, as well as the potential consequences of the investments for other projects, including the ones on the list of projects, which are subject to common interest (EU, 2015). As a matter of fact, the OPAL gas pipeline is a land extension of the Nord-Stream gas pipeline, which, due to its location, is not subject to the regulations arising from the third energy package. The last circumstance makes, as previously claimed, transmitting gas via this route from a source other than under control of the Gazprom capital group, de facto, impossible. Thus, the OPAL gas pipeline is adding new capacity, at the same time (taking into account the exemption decision) resulting in the strengthening of the dependence on one gas supplier - Gazprom Export. This thesis is confirmed by statistical data, which indicate the increase of the share of natural gas imported from the Russian Federation over the years 2011–2013, i.e., from putting the Nord-Stream and OPAL gas pipeline into operation (Chart 1). As can be presumed, such a tendency would be maintained in subsequent years if not for the conflict in the Ukraine in 2014 and the associated restriction on gas supplies by Gazprom via the “Brotherhood” pipeline located in the territory of that country (Van de Graaf and Colgan, 2017). However, the Russian Federation still remains the main natural gas supplier to the European Union (Romanova, 2014; Finon and Locatelli, 2007; Siddi, 2016), and the discussed investment, in this case (i.e. Considering the fact that it was exempted from the TPA

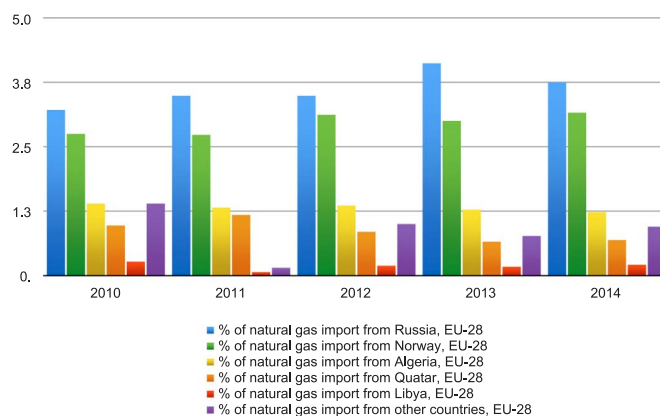


Chart 1. Natural gas importing directions to the European Union.
Source: Own elaboration on the basis of Eurostat data.

principle) strengthens the dominating position of Gazprom Export in the natural gas wholesale market, in particular, in Central and South-Eastern European countries.

Thus, the EC statements, according to which increasing the usage of the OPAL gas pipeline will increase the supply security in case of difficulties with transmitting gas via other routes, and that it will not result in the abandonment of gas transmission via the other gas pipeline in the future, seem unjustified (item 50 of the EC decision). It is enough to mention that the first monthly auctions (on the PRISMA platform)¹³ organized according to the new rules (PRISMA, 2017), which took place on 19th December 2016, resulted in the highest usage of the OPAL gas pipeline (Greifswald/OPAL - OPAL Gastransport entry) up to date, i.e., at a level from 82 to 98 mn m³/day between 1/1/2017 and 31/1/2017, compared to 58–82 mn m³/day in December 2016 (whereas from 1 to 22 December 2016, the gas transmission level was almost constant and amounted to ca. 58 mn m³/day). The gas transmission at the discussed point in the peak moment, i.e., on 10/1/2017, between 6 and 7 a.m. was 45,152,269 kW h/h, which at 45,394,745 kW h/h of the total OPAL gas pipeline capacity meant it was 99% used (ENTSO, 2017). It is worth noting that the use of the Nord Stream gas pipeline increased proportionally to the level of gas transmitted via the OPAL pipeline. It is estimated that the daily transfer along that route in the middle of January amounted to 162 mn m³, which was more than 100% of the total technical capacity of the Nord Stream gas pipeline (EEGA, 2017). As a result of the above, in January 2016 (as for the 16th of that month) 2016, gas transmission across the Ukraine, via the connection in Veľke Kapušany was lower by ca. 10 mn m³ per day, in relation to the level prior to increasing the transfer via OPAL (i.e., 23rd December 2016). At the same time, it needs to be indicated that the significant decrease of gas transfer across the Ukraine, had already been observed since 21st December 2016 (Chart 2). The daily flow of gas at the Veľke Kapušany point decreased in just 4 successive days from 162 mln m³ to 117 mln m³ (25th December 2016). At the same time at the Greifswald entry point, a significant increase of gas transmission was observed, i.e., from an average daily level of 60 mn m³ on 1–22 December to levels of 80 mn m³ per day in the last week of that month.¹⁴ While at the exit

¹² As a matter of fact, the study of potentially negative effects for competition focuses on, i.e., analysing the structure of the relevant market, effects of releasing or allocating the available capacity to third parties or, essentially, the proportionality of the applied measure, and not the assessment from the point of view of the role, which the investment will play generally, in increasing competition among gas suppliers.

¹³ At the Greifswald point, the operator, OPAL Gastransport, sold 12.66G W h/h out of the offered 15.86 GW h/h capacity for the whole month of January (Greifswald OPAL partly regulated); at the Brandov point, within two auctions, the operators, Net4Gas and OPAL Gastransport, sold 2.63 GW h/h out of the offered 5.83 GW h/h capacity for the whole month of January (Brandov OPAL bundle). In the second auction at the Brandov point, the operator, OPAL Gastransport, sold 100% of the offered 10.03 GW h/h capacity for January (Brandov OPAL partly regulated). It is worth mentioning, that the capacities sold at the Greifswald point are equal to the sum of capacities sold at Brandov, which indicates that this capacity was reserved by one entity - Gazprom (PRISMA, 2017).

¹⁴ Apart from 31st December, which was probably a consequence of Dusseldorf Higher Regional Court decision entering into force on the previous day, which temporarily halted the application of the new principles on the basis of a European Union Court of Justice

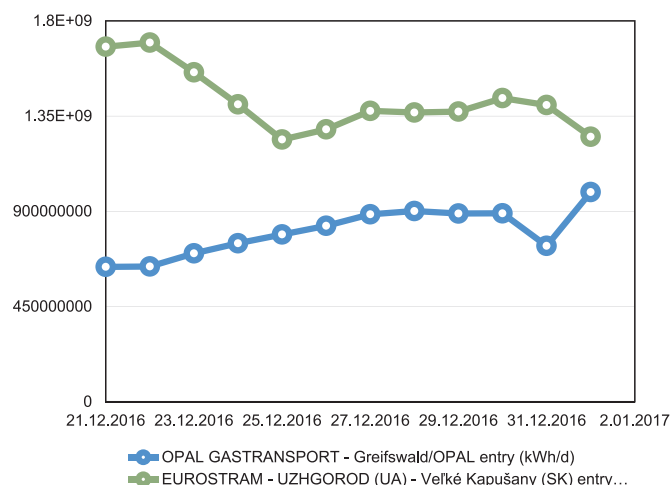


Chart 2. The comparison of gas pipeline capacity usage at selected points.

Source: Own elaboration on the basis of ENTSO data.

point, from an average level of 64.5 mn m³ on 1–22 December to almost 80 mn m³ in the last week of that month.

A change of the transmitted gas volume may also be observed at the Lanžhot point, at the border between Slovakia and the Czech Republic. A systematic decline of the gas transmitted via the route from Slovakia to the Czech Republic has been visible since 21st December 2016, including the suspension of gas transmission in that direction on 1/1/2017 (ENTSO, 2017). At the same time, an increase of gas transmission in an opposite direction than previously, i.e., from the Czech Republic to Slovakia, was noted (from a level of “0” - 1/1/2017 to almost 15.5 mn m³/day on 31/1/2017), hence strengthening the role of the Czech Republic in the transit of Russian gas. Therefore, the above indicates an attempt to change the existing gas transmission routes to the EU, which can endanger the gas supply security for Slovakia and the Ukraine (ENTSO, 2017). In addition, the case in which the commented decision shall have an adverse impact on the gas transit via the “Yamal” gas pipeline, which runs through the territory of Poland (especially, given the fact that the transit agreement expires in 2020), hence, also on the safety of gas supplies to that country, cannot be ruled out (Łoskot-Strachota, 2017).¹⁵ This is why we believe that the EC assessment should not only limit to the safety of gas supplies to Germany and the Czech Republic,¹⁶ but should also take a broader context into

(footnote continued)

decision, suspending the execution of the decision of 28th October 2016. These decisions were a result of Polskie Górnictwo Naftowe i Gazownictwo S.A., Polskie Górnictwo Naftowe i Gazownictwo Supply & Trading as well as the Polish party's challenging the EC's decision in the EU court (T-849/16R, T-883/16R, T-130/17R). In this respect, it should be emphasized that the decisions do not affect the validity of auctions, which have already taken place. At the same time, it is impossible to ignore the fact that on 21 July 2017, by decision of the EU Court, an interim relief in the form of suspension of the said decision execution was repealed. Substantiating its decision, the Court found that the plaintiff did not present serious evidence of the fact that he/she cannot “expect termination of the proceeding in terms of main complaints, without being exposed to suffering a serious and irreversible harm” (item 44). Although this decision may raise doubts, it should not be identified with the possible negative adjudication for plaintiffs. It is only provided in the subject-matter of the measure aimed at protection against potential negative effects of the EC decision, and it does not judge on the merits of the case.

¹⁵ A larger usage of the OPAL gas pipeline will enable limiting the gas transit via the “Yamal” gas pipeline across Poland. It is possible that in the case of a successful execution of the Nord Stream II project (with a planned capacity of 55 bn m³) would completely abandon using this transmission route, which raises concerns about the security of gas supplies to Poland (the possibility to fully omit Poland in gas transmission, without losses for the supplies to Western European countries).

¹⁶ In fact, amending the decision may contribute to increasing the safety of gas supplies to the Czech Republic, due to auctioning the FZK capacity (which enables gas transmission from the Gaspool market with the entry point in Brandov). Therefore, it will be theoretically possible to send gas towards the Czech Republic from other sources than the

account. Above all, it seems justified, for it to also take into account the supply safety of the States in the region, in particular, from Central Europe, i.e., Poland and Slovakia as well as the interest of the EU in general. Such an approach is substantiated by the principle of power solidarity governed by art. 194 of the Treaty on the Functioning of the European Union (Andoura, 2013). Pursuant to its content, the EU policy in the scope of power is supposed to, in a spirit of solidarity between the Member States, i.e., lead to ensuring energy supply security in the European Union. Strengthening the dependence on one gas supplier and changing the currently used transmission direction may, in turn, hinder the implementation of the above objective (Harsem and Claes, 2012). In this context, it is worth noting that due to its effect, the decision of the Commission may be a barrier for the development of regional co-operation (Jones, 2010), referred to in art. 6 of the directive 2009/73/EC, which is, in fact, a manifestation of the energy solidarity. We cannot ignore that the EU legislator indicates group of Member States in Annex IV to regulation 994/2010, including Poland and three Baltic States (Estonia, Latvia and Lithuania), Poland and Germany, the Czech Republic and Slovakia, within which the cooperation is supposed to increase their individual and common gas supply security. Although this division does not have a binding nature, the consequence of introducing the amendments to the decision of 2009 might be antagonizing the countries, concentrated in a given region. All the more, that the legislation package presented by the EC in February 2016 (which includes, i.e., new SOS regulation) for the creation of an Energy Union, provides for further strengthening of this cooperation and a transition from the national to the regional model while designing measures to protect supply security (Siddi, 2016). The superior rule of the regulation proposal (EU, 2016a, 2016b) concerning the measures ensuring the safety of natural gas supplies and repealing the regulation 994/2010, which is a part of the above mentioned package is, in fact, acting in a spirit of regional solidarity and cooperation, in order to guarantee that all Member States have sufficient tools at their disposal, which enable preparation for gas shortages and managing the effects of such a shortage caused by interruptions in the supply system or exceptionally high demand. The starting point for the EU project initiator is the obligation of the Member States to cooperate in crisis situations, within their regions (articles 6, 7 and 10 of the regulation proposal). The basis for the commented cooperation is supposed to be art. 3 par. 7 of the regulation proposal, which stipulates the criteria of regional composition (i.e., geographical proximity, interconnections, the possibility to join resources, development and market maturity, etc.) and annex I to the regulation, which contains explicit regional divisions acc. to the above-mentioned criteria. At this point, it is worth drawing attention to the fact that the Central-Eastern Region covers countries like the Czech Republic, German, Poland and Slovakia, thus, countries which directly or at least indirectly, are impacted by the amended decision in this case. From the point of view of the Commission, such a division is the best way to ensure the safety of gas supplies in an emergency situation. However, this statement seems to create confusion, since the decision increasing the available capacity of the OPAL gas pipeline, hence, impacting the change of the existing gas transmission routes leads rather to divisions fuelling mutual distrust than to an enhanced cooperation in the field of supply security.

A slightly different in the legal sense, is the situation of the safety of gas supplies to the Ukraine. Since it is not a Member of the European

(footnote continued)

material send via the Nord Stream gas pipeline. However, it is worth noting that during the first auction on the PRISMA platform, the sum of capacities sold for the Greifswald point was equal to the total capacities sold in Brandov, which in practice means that the Czech market received gas sent from the Nord Stream gas pipeline (which remains the property of Gazprom Export). As a consequence, it can be concluded that there was no interest in OPAL capacities intended for third parties, from sources other than transmitted via the Nord Stream gas pipeline, and it is not entirely clear, whether such interest will appear in the future.

Union structures, the principles presented above generally do not find direct application. The legal basis in this case is the Association Agreement between the European Union and its Member States, and the Ukraine. According to Annex XXVI to Chapter I, Title V: Economic and Sector Cooperation, the Parties of the Agreement undertake to mitigate negative effects of emergency situations,¹⁷ including all actions, which could cause negative effects for the supply of natural gas, oil or electricity between the Ukraine and the European Union or could intensify these effects (par. 14 of the Annex). Therefore, in the situation of systematic reductions of gas supplies to the Ukraine by Gazprom Export (NAFTOGAS, 2016), as well as decreasing the usage of the “Brotherhood” pipeline capacity (increasingly used as the *last resort option* in cases of peak demand for gas and no access to alternative export routes), we consider the adoption of such an approach as justified. However, it is problematic that the Agreement in question has not yet been ratified (as a result of rejecting it in a referendum, the agreement was not ratified by the Netherlands). Although, pursuant to art. 486 of the Agreement its relevant provisions temporarily apply, this undoubted circumstance may significantly impair the efficiency of used legal solutions.

3.3.2. The impact of exempting the OPAL gas pipeline on the internal gas market competition

In short, it should be considered, whether the exemption will not adversely impact the competitiveness and functioning of the internal gas market (EU, 1997). In the course of the commented case, the EC from the very start claimed that absolute exemption of the OPAL gas pipeline from the liberalization principles may have a negative impact on the competition in the Czech gas downstream market (item 69 of the EC decision). It stems from the fact that the dominating position in the market is held by RWE Transgaz (ERU, 2017), vertically associated via long-term gas supply contracts with Gazprom (until 2035) - the largest wholesale (upstream) gas provider in the Czech Republic (Chart 3)¹⁸ which shall strengthen its position as a result of increasing the capacity of the OPAL gas pipeline.

It is worth mentioning, that the EC did not agree with the position of BNetzA and other applicants that the wholesale gas supply market (both, upstream and downstream) should be considered in a broader range, i.e., at least as a market of the European Economic Area, to which the Czech providers (downstream) have free access (item 70 of the EC decision). The EC justified such a position with insufficient number and capacity of available cross-border connections (item 85 of the EC decision), long-term gas supply agreements (which distort the gas market price) or the contractual provisions introducing restrictions for cross-border competition (e.g. prohibition of reselling as to another country). Simultaneously, this body claimed that the fact of the very existence of a transmission infrastructure in this area is not sufficient to recognize it as one relevant market. In order to do that, the network infrastructure assigned to a given entry-exit zone should enable free gas flow (Dong, 2006). In practice, it means the absence of the so-called bottlenecks, which could constitute a barrier for unhindered gas transport, and in consequence, also limit competition (Gaz de France, 2006; TOTAL, 2004). Therefore, in the case in question, the EC stated that the relevant market for the determination of the dominating position at both, the upstream and downstream levels, would solely remain the national market of the Czech Republic (E.ON gas, 2010; RWE Essent, 2009; ENI, 2008).

Most of all, considering whether the effects potentially negative for the competition, resulting from amending the decision shall be

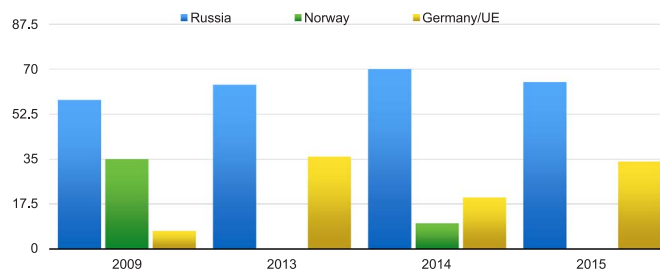


Chart 3. Natural gas importing directions to the Czech Republic.

Source: Preventive Action Plan, Ministry of Industry and Trade, 30 November 2012, p. 14/Czech National Regulatory Authority reply of 18 August 2016.

sufficiently compensated by the positive ones, is of fundamental importance to recognizing that the above premise was satisfied. Undoubtedly, the original EC decision limiting the possibilities of Gazprom (and other entities having a dominant position on the Czech market) to reserve available capacities to a max. of 50% was supposed to prevent strengthening its dominating position (on the upstream wholesale market in the Czech Republic). According to the new principles, Gazprom will have the right to participate in the auctions for the remaining capacity, under the conditions similar to the other providers. Hence, in case of lack of interest from other entities, Gazprom will be able to practically reserve the entire capacity at the exit point, i.e., in Brandov (item 99 of the EC decision), which is contrary to the original assumption and, apparently, the current EC policy towards this company.¹⁹

In order to prevent the above situation, the EC decision provides for specific compensatory measures, which are aimed at counteracting the deterioration of the competition status in a given relevant market. Above all, 10% of the capacity (3,200,000 kW h/h) being auctioned will be available in the FZK system (McDaniel and Neuhoof, 2002). It provides uninterrupted access to the GASPOOL market with an exit point in Brandov. It is insofar important as previously there were no similar solutions functioning on the OPAL gas pipeline.²⁰ The remaining capacity, i.e., 40% (12,664,532 kW h/h) will be based on the DZK mechanism (entry point in Greifswald, exit point in Brandov), which is characterized by lower flexibility and does not ensure an uninterrupted access to the GASPOOL market (item 30 of the EC decision).

An undoubted advantage of introducing auctions (Harris and Lapuerta, 2012)²¹ (short and medium-term) for FZK capacity is the fact that it enables the buyers from the Czech Republic access to a gas hub

¹⁷ An emergency situation is a situation, which causes significant disruption/physical interruption of natural gas, oil or electricity supplies between the Ukraine and the European Union - par. 2 of the Annex to the Agreement.

¹⁸ Russian Federation is the main importing direction to the Czech Republic (ca. 65% in 2015). Due to the material policy of that country, which assumes a monopoly in gas export, Gazprom is, de facto, empowered to supply gas within Europe.

¹⁹ Since September 2012 the Commission has been proceeding against Gazprom on the abuse of the dominant position in the scope of natural gas supplies to the Central and Eastern European Markets (Bulgaria, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Slovakia and Hungary). In April 2015, the Commission sent a written statement of objections, in which it expresses its initial opinion that Gazprom breaches the EU antitrust rules. The basic allegations concerned the application of territorial restrictions, unfair pricing policy and the use of package deals. In March 2017, the Commission asked the interested parties to submit their comments regarding Gazprom obligations aimed at remedying the violations in the scope of competition (European Commission - IP/15/4282, European Commission - IP/17/555).

²⁰ At the same time, it should be noted that auctions for the FZK capacity from the GASPOOL market to the Czech Republic are also offered by other operators, such as Gascade (Olbernhau gas pipeline) with the exit point in Hora Svate Saterinyi ("HSK"). On account of that, increasing the level of FZK capacity available in the auctions should contribute to the reduction in its price and make it harder for the dominants to exclude the competition from the market.

²¹ These auctions will be of short or medium-term nature, which is supposed to guarantee that the dominants will not use their advantage to strengthen their market position through long-term preclusion of access to the network infrastructure. Moreover, the implementation of the UIOLI (use it or lose it) system is expected. This system enables the entrepreneur to re-share the unused capacity to third parties. Therefore, its assumption is to counteract situations, in which the dominant would reserve a capacity larger than actually necessary.

(Stern and Rogers, 2011), with a systematically increasing liquidity (item 132 of the EC decision).²² As a result, they gain access to supply sources alternative to Gazprom. In a wider perspective, this solution increases the integration of the internal gas market, although the drawback remains that only for the German and Czech markets (Maltby, 2013). A question is whether adapting the 10% threshold for the offered capacity within the commented mechanism is sufficient. Since the product is, in fact, of pro-competitive nature, should it not prevail over the auctions based on the DZK capacity. Such an approach is, seemingly, reasonable. However, it needs to be taken into account that the FZK mechanism is much more complex than DZK. That is because it requires separate transmission networks, the simulation of environmental impact or the expansion of the existing network infrastructure (item 132 of the EC decision). Therefore, at the current market development stage, the applied measure seems commensurate with the circumstances. At the same time, it needs to be stressed that, as per EC decision, the system operator (OPAL Gastransport GmbH & Co.KG.) was obliged to increase the FZK capacity offered during the auctions (for the Brandov exit point) to a max. of 6,400,000 kW h/h²³ i.e., 40% of the entire capacity available in this mode, in a situation in which the yearly demand (for the capacity) would be equal or higher than 90% of the capacity previously offered. In such a case, the available DZK capacity volume is proportionally decreased. What is more, further increase of FZK capacity available on the auctions is expected (by a max. of 3,600,000 kW h/h), should the demand exceed the threshold of 6,400,000 kW h/h. Nonetheless, in such a situation, the sole fact of existence of a larger demand for FZK capacity is insufficient. That is because the operator is subject to the discussed obligation, provided that increasing the capacity is technically feasible, justified from the competitive perspective, and that the benefits outweigh the costs. These premises are always reviewed by the EC and it is the operator, who bears the responsibility to prove the circumstances justifying the exemption from the scope of the above obligation (art. 3 of the EC decision).

An additional protection against potential disturbance of competition is the introduction of the so-called base price during the FZK capacity auctions for the entities having a dominant position on the Czech gas market and those, which control more than 50% of the gas at the Greifswald entry point (Gazprom, Gazprom Expert, RWE, etc.). In light of the EC decision, this price may not be higher than the average price determined on the basis of the tariffs for gas transmission from the GASPOOL zone to the Czech Republic, for products comparable to the FZK mechanism, for the year in which the capacity was reserved (art. 4 of the EC decision). Although, by principle, this measure may prove to be an efficient regulatory instrument, it must be characterized by relative competitiveness in order for it to meet its function (gas upstream). It results from the fact that the applied mechanism is directed rather on counteracting the strengthening of the dominating position (in a situation, in which there is competition), than creating conditions for new entities entering the market. A confirmation of this thesis may be the first monthly auctions conducted in the new mode. As data from the PRISMA platform show, only one entity was interested in booking the capacity for the OPAL gas pipeline (PRISMA, 2017).²⁴ Because of this circumstance, both, the measure providing for the increase of the available FZK capacity, as well as the one introducing the “base price” may prove to be insufficient, if the upstream gas market is not sufficiently competitive. We believe, it is also not entirely clear, whether the “base price” is of rigid, minimum or maximum nature. Since essentially, the EC decision does not specify this issue. A certain hint in this context may be the provisions concerning the “base price” in relation to the

tariff collected by OGT from all network users.²⁵ In this case, it is the base (minimum) value, at which the FZK, as well as the DZK capacity auctions start (item 123 of the EC decision). Per analogiam, it can be assumed that the entities having a dominant position, referred to in the decision in question, may enter an auction only when the offered price is equal or higher than the “base price”, unless there is only one participating entity - the dominant. Then, the price is of rigid nature. However, the literal interpretation of art. 4 of the EC decision is confusing in this perspective. It results from the used wording, which interpreted directly states that dominants may participate in FZK capacity auctions only at the “base price” – “bid for FZK capacities only at the base price of capacity”/“Gebote für FZK-Kapazitäten auf der OPAL nur zum Basispreis dieser Kapazität abgeben können”. Hence, it lead to a conclusion that, in general, in this case we deal with a rigid price, which makes it impossible for the dominant to further participate in the auction, in a situation where the competitors offer a higher price. However, the above assumption implies a question - which entity wins an auction in a situation, in which only dominants participate (since the price is the same for them). Therefore, it seems that it would be most rational to assume that the “base price” corresponds the maximum price, within the limits, which the dominant may bid. Such an approach is indicated by the second sentence of art. 4 of the EC decision, which states that the “base price” may not be higher than the average price set on the basis of tariffs for gas transmission from the GASPOOL zone to the Czech Republic (for products comparable to the FZK mechanism, within a year in which the capacity was reserved). Hence, the entities with a dominating position may participate in the FZK capacity auctions, although only within the limits of the “base price”. A higher offer, however, should be rejected, by virtue of the law.

As EC shows, the attractiveness of FZK auctions shall be price-dependent. The basis for the determination of the initial (base) price is the tariff for the part of the OPAL gas pipeline exempted from the regulatory scope of the 2009/73/EC directive („Exempted Coupled Interconnection Capacities”). This tariff is calculated in an annual scale, on the basis of the costs of the conducted activity incurred by the operator and the revenue generated for the previous year (item 140 of the EC decision). It should be presumed that the price should be lower than the “base price” for entities having a dominant position in the Czech gas market. Otherwise, the entire purpose of the regulation in question would be completely undermined.

The above fact seems to undermine the efficiency of the instrument in question, as one mitigating the negative impact of the exemption on the competition. All the more that the FZK capacity auctions were supposed to constitute a kind of counterbalance for the ones related to DZK capacity (which shall subject Gazprom to competitive pressure to an even lesser extent). It results from the fact that although the DZK auctions ensure uninterrupted access to the OPAL pipeline at the Greifswald entry point and Brandov exit point, only gas which remains the property of Gazprom Expert may be physically sent this way due to technical reasons. It is enough to remind that due to a lack of connection between the OPAL and NEL gas pipelines, there is not technical possibility for the gas supplies along that section to be coming from a source other than the gas transmitted via the Nord Stream gas pipeline (which remains the property of Gazprom).²⁶ Thus, only the execution of an investment process, which would involve the creation of an infrastructure connecting both pipelines could bring measurable results (in the form of alternative gas providers interested in reserving the capacity in question, hence, increasing the competition pressure on Gazprom). A limit third party interest in DZK capacity should also be expected in

²² It is estimated that gas trade through the GASPOOL hub increased from 1251 TW h in 2013–1493 TW h in 2015 (GASPOOL).

²³ From a minimum level of 1,600,000 kW h/h (article 2 of the EC decision).

²⁴ The capacity auction organized in September of this year, no other entity expressed interest in using the OPAL.

²⁵ In light of the EC decision, the “base price” should be equal to the tariff set by the operator for the exempted part of the OPAL pipeline (“Exempted Coupled Interconnection Capacities”).

²⁶ Provided that the gas may partially come from another supplier, if it was purchased in the GASPOOL market. At that point, however, the physical connection will be at the Gross Körös point, via the Yamal gas pipeline.

relation to the auction concerning the gas coming from the GASPOOL zone. As previously claimed, these auctions, as opposed to FZK capacity auctions, are assigned on the “interruptible” basis. It means that an entity utilizing the assigned capacity does not guarantee that the gas will be actually delivered to the gas pipeline within the designated period, whereas the system operator does not ensure the performance of the transmission service within the designated deadline. Therefore, there is not mutual guarantee of utilizing the service within the designated deadline (Smyrgała, 2013). Therefore, this solution will be of moderate importance from the perspective of a competitive market.

4. Conclusions

There is no doubt that the formation of an internal gas market is a complex and long-lasting process. Enough to say, it has been ongoing for almost two decades now, and it seems like we need at least one more, in order to achieve full harmonization. To add to its complexity, it requires the reconciliation of different, often opposing interests. Hence, the substantial role of the EC. Within its mandate and in a spirit of the treaty's principle of solidarity, it should aim for reaching a consensus in the fields of gas supply security, and market diversification or competition, which are so crucial for the Member States. The commented decision does not seem to fully consider the above factors.

First of all, we believe it was made prematurely. At the same time, the fact that the dominants did not attempt to implement the gas release programme was not taken into account. We consider this instrument to be a more efficient measure from the point of view of competition development than the solutions adopted in the new decision. Although, contrary to the predictions, the material demand on the Czech gas market decreased, in the author's view a natural step in this situation should be striving for a proportional limitation of the scale of the condition adopted in the original decision. Lack of activity of the applicants in this scope confirms, however, that from the very beginning, their goal was to reinforce the domination on the upstream market in the Czech Republic, aimed at gaining full control over the network infrastructure in question.

Next, as a rule of thumb, although new infrastructure increases energy security, in this case it may have a negative impact on gas supplies to some countries of Central and Eastern Europe. As a result, the situation not only violates the already mentioned principle of solidarity, but also, in an extreme case, may lead to antagonizing individual countries of the region and hence, delays in the execution of the Energy Union development (Austvik, 2017). The fact that increasing the available capacity at the current market development stage shall hinder the diversification of material supplies is not without significance in this context. It results from the lack of interest in the offered third party capacities, which would enable the transmission of an even larger amount of gas from the Russian Federation to the Czech Republic and, indirectly, to Germany (via the Gazela gas pipeline). Consequently, this situation entails a real risk of change in the current natural gas supply routes to the EU through Poland and Slovakia, which is contrary to Article 36 paragraph 1 point a of Directive 2009/72/EC. It is very important because these countries largely depend on natural gas supply from the Russian Federation. Thus, the possibility of the Gazprom's resignation from the current raw material transit direction may be a political tool in the negotiations in terms of conditions related to natural gas supply to these countries. To support the above thesis, it is sufficient to recall that Gazprom repeatedly held the supplies of natural gas transported via Yamal-Europe gas pipeline to Poland and Germany, and in a situation, when the contracts for gas supplies were binding and there were no technical possibilities to provide the gas transport via other gas pipelines (which will be currently possible owing to the contested decision).

Finally, there is no certainty as to whether the EC consent for larger than previous usage of the OPAL gas pipeline would, as a matter of fact, favour an improvement of competition on the gas supply market. Quite

the opposite, its effect may be an increase of the dependence of the Czech and German consumers on Gazprom, making it difficult for the competitors to enter the market. Moreover, the fact that they will coordinate their own behaviour towards the dominant in fear of potential repressions from his side is not out of the question. Hence, although seemingly, there will be alternative downstream gas suppliers operating on the market, the freedom of their activities will be limited (Zaręba, 2016).

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