Role of gas in energy security and future energy market direction

TARK
GRUNTE
SUTKIENE

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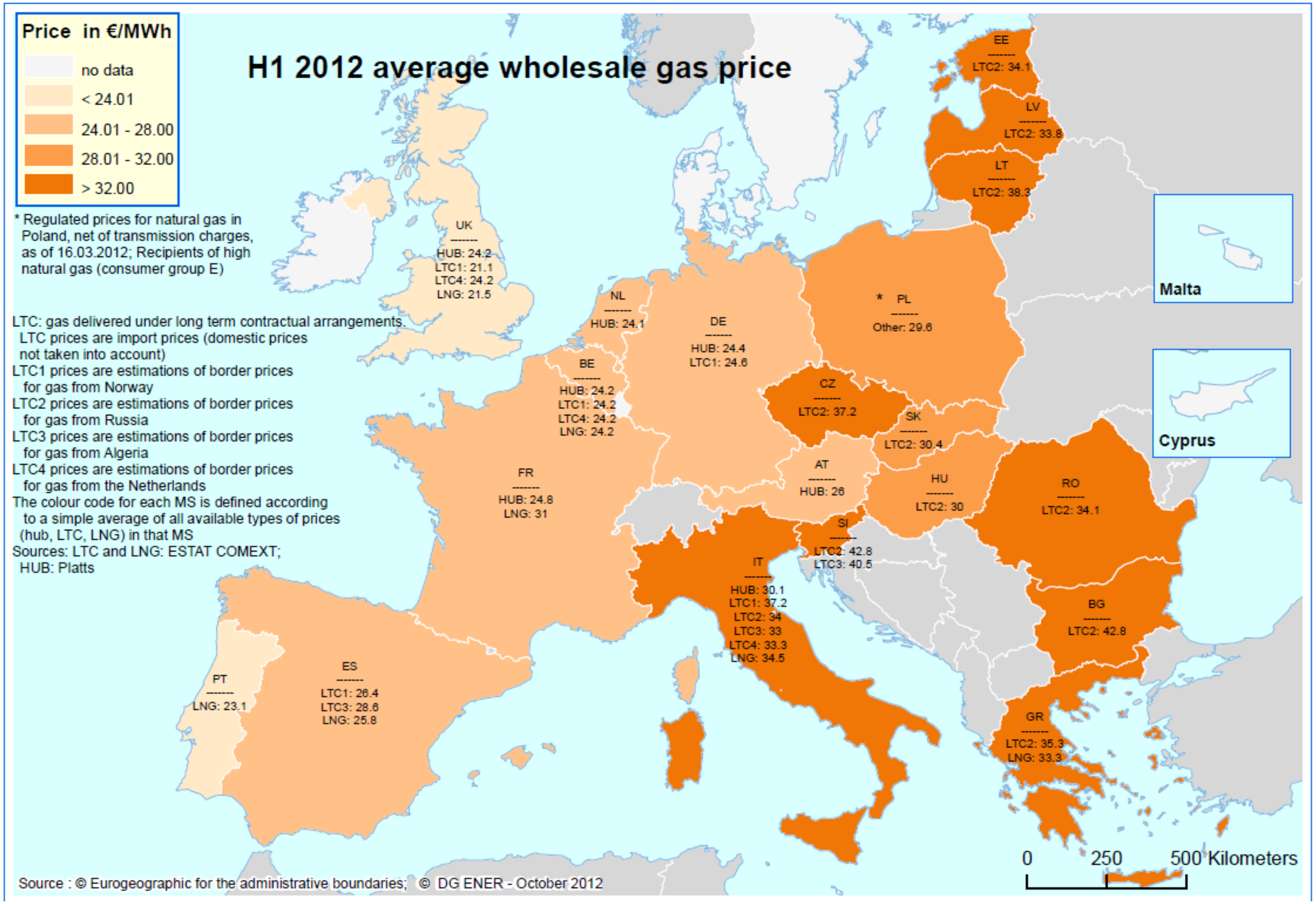
Warsaw, 19 March 2013

Agenda

- Baltic gas market overview
- 3rd energy package implementation in the Baltics
- LNG terminal and other alternatives of supply

Wholesale gas prices in Europe

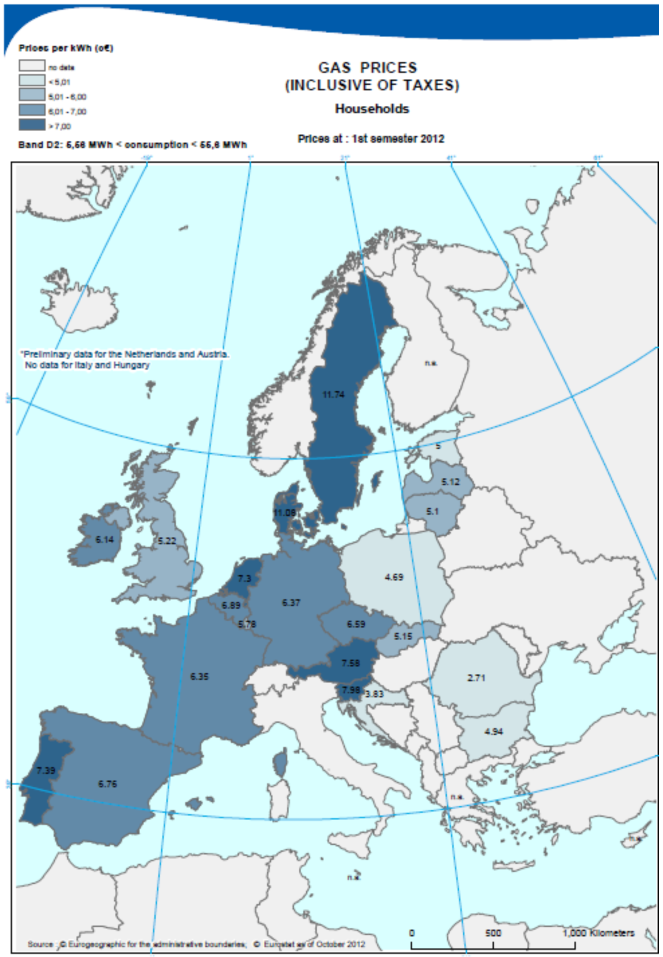


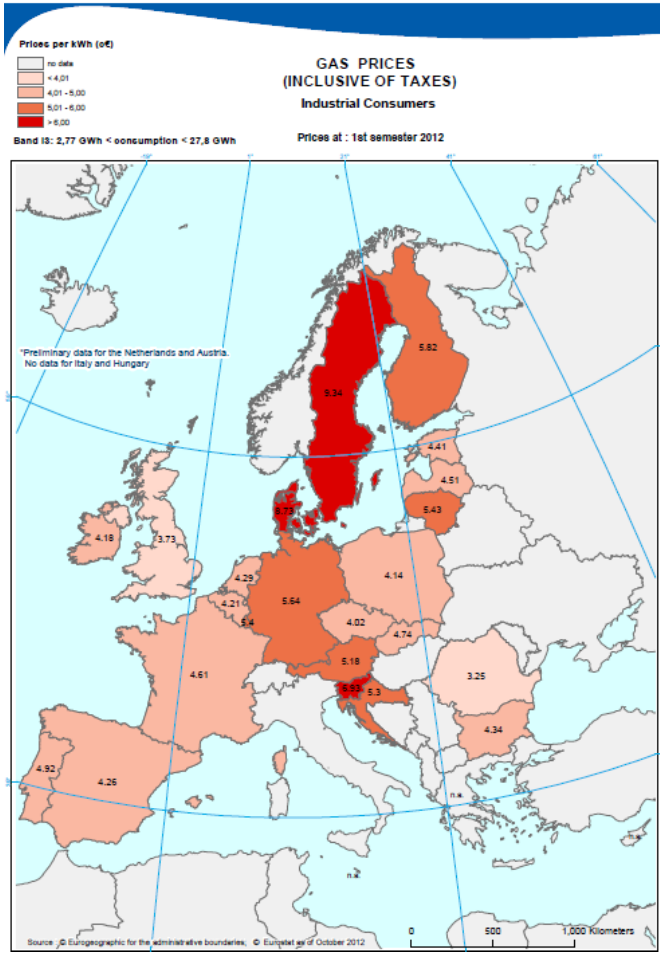
Source: DG ENERGY MARKET OBSERVATORY FOR ENERGY VOLUME 5, ISSUES 2 & 3: April 2012 – September 2012

Gas prices: households vs. industrial

Households

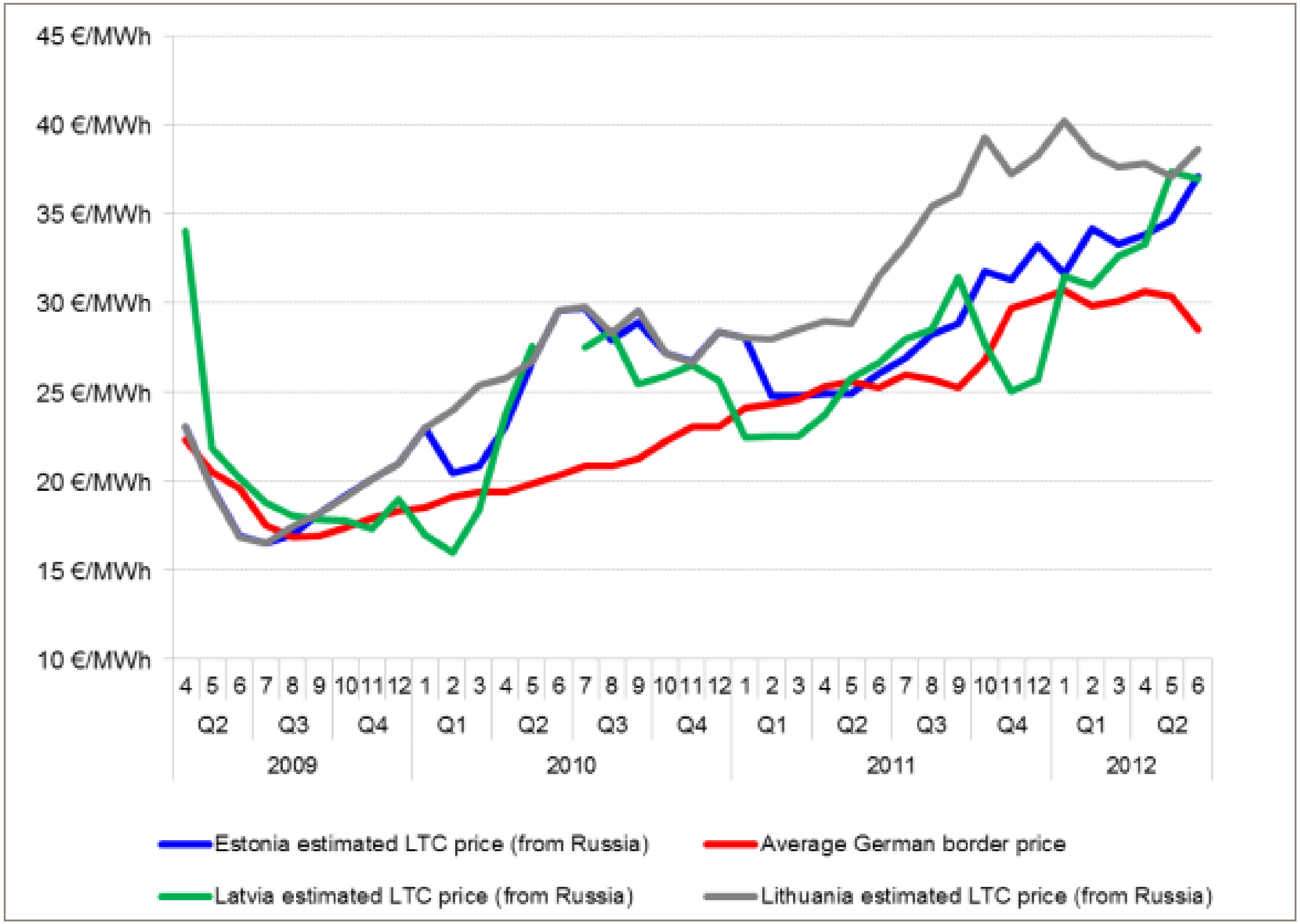
Industrial





Source: DG ENERGY MARKET OBSERVATORY FOR ENERGY VOLUME 5, ISSUES 2 & 3: April 2012 – September 2012

Baltic states: border prices



Source: DG ENERGY MARKET OBSERVATORY FOR ENERGY VOLUME 5, ISSUES 2 & 3: April 2012 – September 2012

Baltic gas market – key tendencies

- Diversification of supply sources and security of supply
- Creation of competitive market
- Strategic infrastructure developments

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Regulation of energy in EU

1996/1998

First energy package

- **Adoption of internal market general regulations in electricity and gas sectors**
- **Energy market liberalization starts**

2003

Second energy package

- **Requirement to separate activities of energy sectors – legal and functional unbundling**

2009

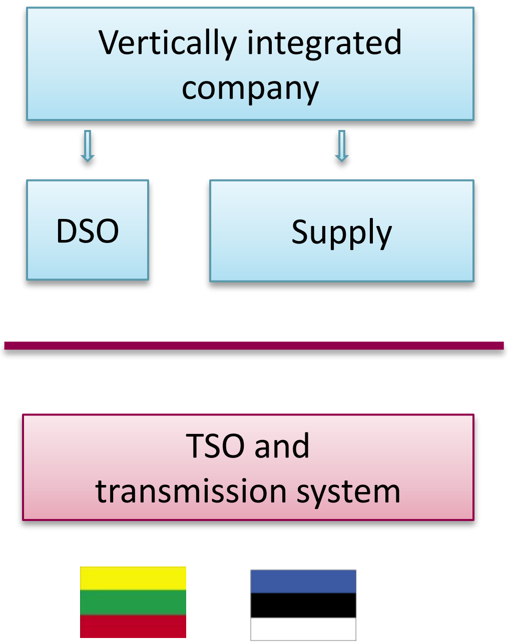
Third energy package

- **Seeking to finalize the process of energy market liberalization and to ensure open and competitive market of energy resources**

at present, there are obstacles to the sale of gas on equal terms and without discrimination (Directive 2009/73/EC)

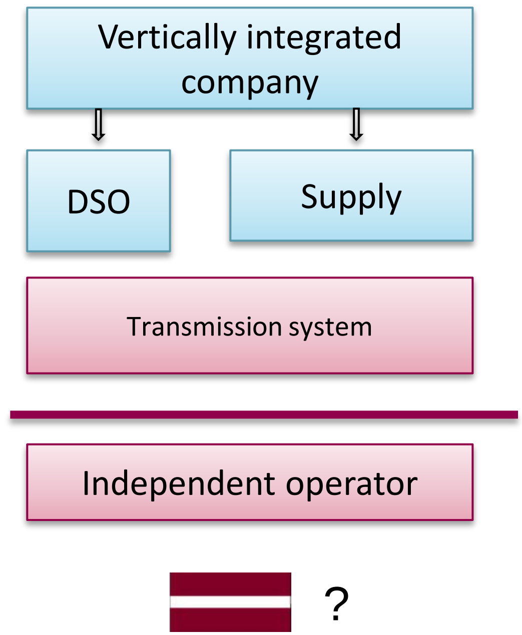
Implementation of the Directive in the Baltics

Ownership unbundling



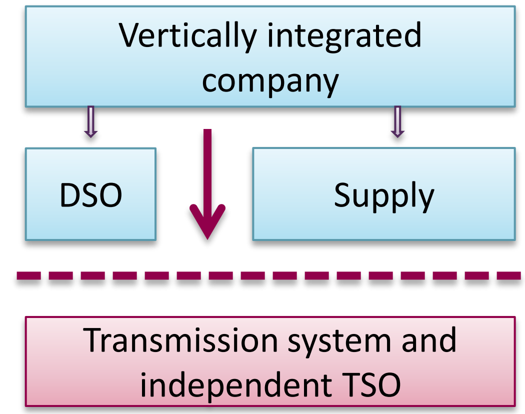
An **independent transmission system operator, that owns the system**, is established

Independent System Operator



The transmission system is owned by the vertically integrated company. **An independent operator is appointed**. **Legal means** to ensure independence of the TSO

Independent transmission operator (organizational separation)



Transmission system is owned by the vertically integrated company. An independent transmission operator is appointed within the organization of the integrated company. **Specific additional restrictions** are applied to ensure independence of the TSO

Ownership unbundling in Lithuania

Electricity sector

In 2010 the concept amendment on the Law of Electricity was approved.

Ownership and activity separation is implemented:

- Transmission activity – AB LITGRID
- Distribution activity – AB LESTO
- Production activity – AB LIETUVOS ENERGIJA

LITGRID has been delivered the electricity transmission grid.

The final step was transfer of control rights over state-owned shares in Distribution System Operator (AB LESTO) and the generation and supply company (AB LIETUVOS ENERGIJA) to the Ministry of Finance in February 2013.

Natural gas sector

A legal basis has been created whereby the vertically integrated company (AB LIETUVOS DUJOS) will be split to meet the ownership unbundling requirements

In 2011 the following legal acts were enacted:

- **Amendments to the Law on Natural Gas**;
- **The Law on Implementation of Amendments to the Law on Natural Gas**.

AB LIETUVOS DUJOS **presented the unbundling plan in May 2012**

The ownership unbundling
Is in progress.

Reorganization models

1. Procedure of control restructuring

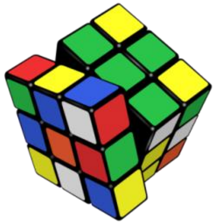
• "Volunteer restructuring" – **initiative on method** of unbundling by the vertically integrated undertaking

• The control of the company is reorganized through **transactions chosen by the company** (of transfer of property, transfer of shares, transfer of shareholder rights, shareholder agreement, increase or reduction of authorized capital, etc.)

• The process is **controlled by the National Energy Regulator** (the National Control Commission for Prices and Energy)

• **Ownership unbundling** and absence of illegal control must be assured by **31 October 2014**

• Upon completion of the procedure, a **certification is issued by the National Energy Regulator**, asserting the ownership unbundling

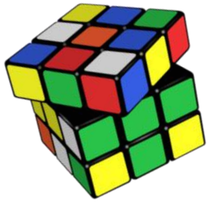


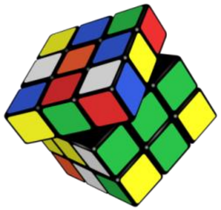
2. Reorganization procedure

• If the "volunteer restructuring" is not initiated the **Terms of Reorganization must be prepared**

• The Terms of Reorganization are analyzed by the National Energy Regulator

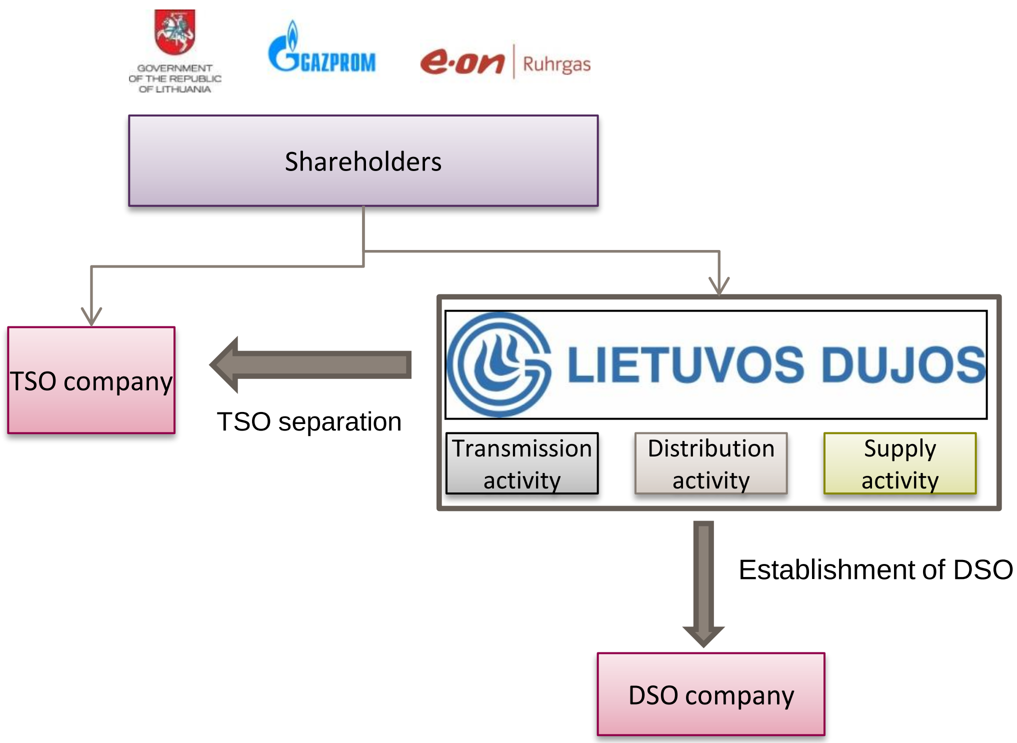
• Reorganization of the vertically integrated undertaking **in accordance with the general norms** of the Civil Code and the Law on Joint Stock Companies of the Republic of Lithuania





Reorganization plan of AB Lietuvos dujos

- **Before 31 July, 2013**
  - The legal and functional separation of TSO must be completed
  - The plan of implementation presented in May 2012
  - The Terms of Reorganization approved in January 2013
  - **Process is on track** for completion
- **Before 31 October, 2014**
  - Ownership unbundling must be finally completed
  - Control of the TSO must be transferred to complying entities

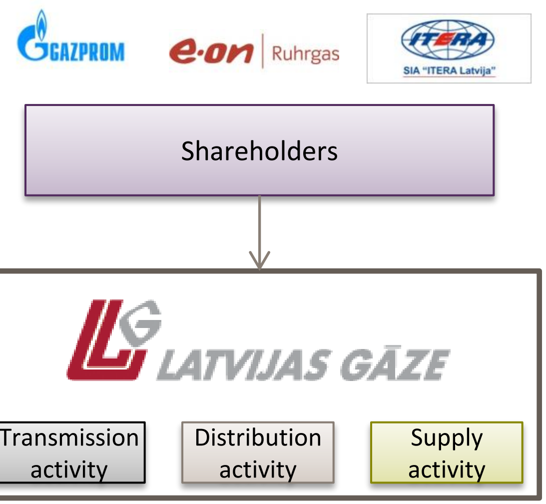


Sanctions

In case natural gas companies fail to comply with the requirements in full and on time, the National Control Commission for Prices and Energy may take a decision to issue a fine of up to ten per cent (10%) of annual income received by the violating company

Latvian model

- Latvia has **an explicit derogation from the Directive** exempting it from unbundling rules (Article 49)
- The certification of the gas TSOs has not taken place yet but the process for separating the electricity TSO has started
- The bill on gas market liberalization was planned to be approved on March 5, 2013.
- However, Saeima committee put forward a proposal to use the derogation and considerably postpone the implementation of the Directive



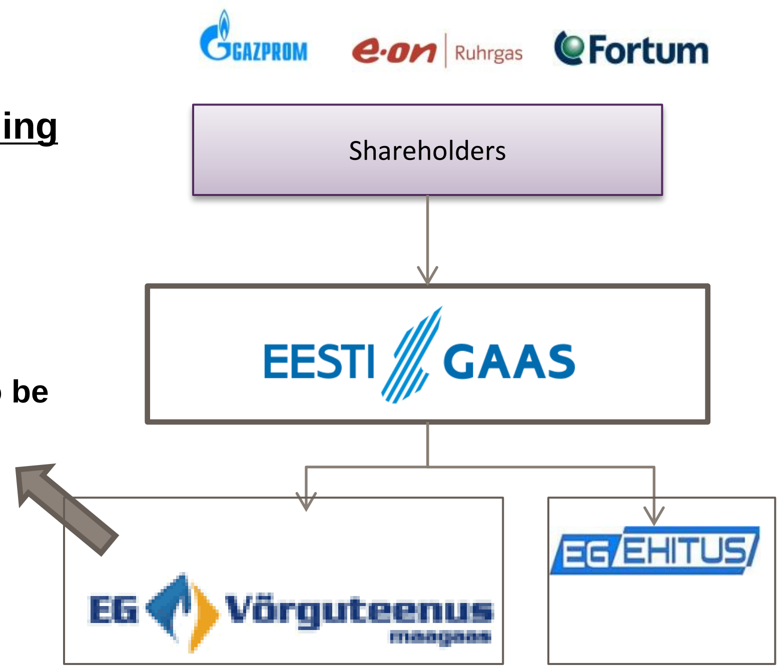
Mixed messages in the Baltics on market liberalisation
Joshua Posaner
15 March 2013 | 15:13 GMT

Two of the Baltic states have signalled very different approaches to the EU's market liberalisation strategy in recent days, with Lithuania ploughing forward with plans to unbundle its network operator but politicians in Latvia mulling over postponing its implementation, possibly as far back as 2018.

http://interfaxenergy.com/natural-gas-news-analysis/european/mixed-messages-in-the-baltics-on-market-liberalisation/

Estonian model

Under the Natural gas act of June 7, 2012, Estonia has opted for **ownership unbundling**



Ownership unbundling **to be implemented by 2015**

Prior to enactment of the unbundling requirements, **legally unbundled TSO** (**AS EG Võrguteenus**) was established and operating as of **January 1, 2006**

AS EG Ehitus was established in December 2004, separating out the construction and maintenance of gas transmission and distribution infrastructure

The Baltics after the 3rd energy package implementation

- **Issues to be considered:**
  - Lithuania is in **arbitration disputes with Gazrpom** over ownership unbundling
  - **Which Third Energy Directive model is “easier” on the market?**

__Without effective separation of networks__ from activities of production and supply (effective unbundling), there is a __risk of discrimination__ not only by operation of the network but also in the incentives for vertically integrated undertakings to __invest inadequately__ in the networks (Directive 2009/73/EC) (emphasis added)

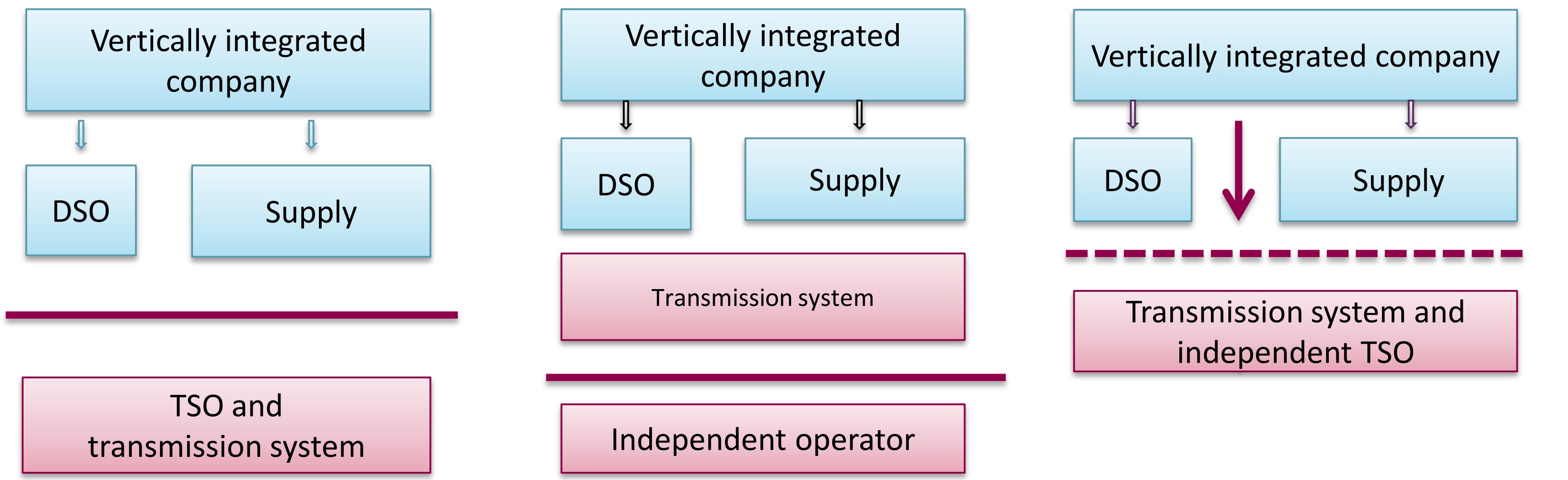
  - The Directive requires **<u>the same result to be achieved by any of the three implementation models</u>**
  - **<u>Is the “easiness” of ISO and ITO models is merely a myth?</u>**

Which one is “easier”?

Ownership unbundling

Independent System Operator

Independent transmission operator (organizational separation)



Future of the Baltic gas markets largely turns on the success of ownership unbundling

however…

- Which way will Latvia go?
- How will ownership unbundling be implemented in Estonia and Lithuania?
- How will real competition in the gas market be achieved?

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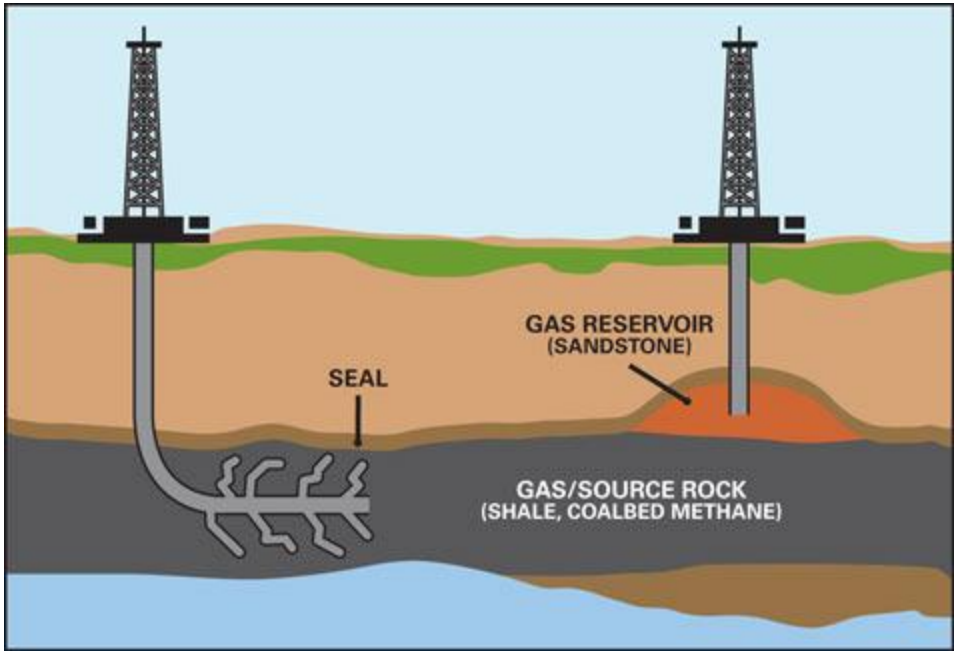
LNG terminal in Klaipeda and GIPL connection

- On land interconnector between Poland and Lithuania (GIPL) **<u>included in the BEMIP long term plan</u>**
- Studies are under way but **<u>no investment decisions were made to date</u>**
- **<u>Terms of implementation</u>** of the project to be defined

- Regional LNG terminal included in the BEMIP long term plan, however, no definitive decisions are made yet
- AB Klaipedos nafta implementing an **<u>FSRU project in Klaipeda</u>**
- The Klaipeda LNG terminal is scheduled to be **<u>fully operational in December 2014</u>**
- The **FSRU is contracted** and under construction, scheduled to be out of the shipyard by spring 2014
- The **<u>harbour dredging</u>** works for the terminal are **<u>contracted and under way</u>**
- **<u>EPC for the FSRU jetty signed</u>** on 18 March 2013
- The planned **<u>capacity of the terminal is up to 4 bcm per year</u>**

Shale gas in Lithuania

- Shale gas **reserves are forecasted** in Lithuania
- Two **tenders for shale gas exploration licenses** were announced in 2012
- At the end of 2012, the tenders were **suspended for discussion with the local community**
- Based on the current legislation, **some of the oil exploration licenses may extend to shale gas**
- Shale gas **commercial production would have a revolutionary influence** on the local gas



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