



No. 1: EU policy on improving the security of oil and gas supplies

Theo Westerwoudt, May 2003

On the 14th of May 2003 the European Union ministers of Transport and Energy will discuss, together with the European Commission, the Commission's highly controversial proposals for new directives on improving the security of energy supplies. Some parts of these proposals supposedly have already been dropped and other parts were amended in a new proposal by the Greek chairmanship, because of massive resistance from the oil and gas industry, energy consumers, Member States, members of the European Parliament Energy Committee and in some national parliaments. The Greek chairmanship will on the 14th of May in a political debate in the Council of Ministers discuss its content in an effort to reach consensus on the way forward.

The purpose of the proposals of the European Commission is to ensure the security of supply of oil, natural gas and electricity in the integrated and liberalised European energy market. At the moment, the primary energy supply of the European economy is mainly based on fossil fuels, particularly oil, gas and coal, which accounts for 80 percent of EU energy consumption. Most energy experts agree that this consumption pattern will continue in the next decades, despite the efforts by governments and market parties to replace 'the fossils' and develop a more sustainable and environmental friendly energy supply system.

Almost two thirds of the EU demand for oil and natural gas is presently imported, for a great part from producer countries where political instability prevails. According to the European Commission, the growing import vulnerability constitutes a serious risk. If no measures are implemented, imports of energy will in 20 to 30 years account for 70 percent of the total EU-consumption. Any serious disruption of supplies would cause prices to escalate and could have a serious economic and social impact.

The European Commission has therefore on 11 September 2002 adopted two Directive proposals from Commissioner Mrs Loyola de Palacio (Transport and Energy). The Commissions directives should help to improve the security of supply within the framework of the internal market for energy and promote solidarity and coordinated action between the Member States in times of crisis. In the first proposal the volume of strategic **oil** stocks is increased from the present 90 days of consumption to **120 days**. In case of a supply disruption, the new strategic stocks could be used to fend off the negative economic effects of price volatility in the market. Potentially this could be the case when the price of crude oil reaches a level of (in 2002) approximately 30 \$ per barrel.

Particularly on this particular point Mrs De Palacio's proposal has been severely criticized because this kind of market intervention is opposed by many Member States and market parties alike. Moreover, it has not been very effective in the past. Several Member States also strongly reject the somewhat critical tone in the Commissions proposal where the world wide oil crisis mechanism of the International Energy Agency is concerned.

Regarding **natural gas** (the second proposal), the proposal is that EU Member States must take measures to ensure that the supply to vital consumers who cannot replace gas with another fuel is guaranteed for **60 days** in average weather conditions when the single, most important source of gas is disrupted. In the event of extremely low temperatures other measures must be taken.

Gas stocks should at least make a minimum contribution to security of supply, although the level of these stocks should take account of the geological and economic storage possibilities in each Member State. If gas supplies are seriously interrupted, the Commission will urge Member States to assist the countries most affected and, if necessary, adopt decisions requiring Member States to take appropriate measures. These measures **may include the release of gas stocks** and the interruption of non-essential supplies. Most Member States are fiercely opposed to the latter authority of the Commission. The Dutch government has both communicated to the Council of Ministers and the national parliament that this new authority of the Commission should not be accepted because it would interfere with the sovereignty of states over national resources. Moreover, interference of the European Commission with the way gas stocks are employed could very well impede honouring existing contracts and hamper future investments of the gas industry in storage, installations and infrastructure.

The Commission underlines the importance of the availability of gas storage facilities and alternative flexibility mechanisms as "crucial for an efficient operation of the gas system", particularly with regard to improving the security of supply. The European Union should give a high priority to the development of gas storage as appropriate under the TEN-Energy programme, says the Commission in an explanatory memorandum of its proposal for a new directive.

Because of limited or non-existent geological sites suitable for underground storage facilities, some Member States rely on storage or back-up services in other Member States. With a view to both strengthening the internal EU solidarity and the cooperation with external suppliers, the Commission notes that "there may be certain projects of common interest with regard to storage development in Europe which merit further analysis".

If an important cost-effective alternative is considered for certain Member States and regions in the EU, the Commissions proposals become a lot less controversial. Gas storage can be quite expensive. Security of energy supply can in some cases be improved with oil storage and investments in dual firing installations for generating electricity and industrial purposes at much lower investment and exploitation costs than developing further gas storage capacities.

In a first informal discussion in the EU Council of energy ministers on February 22, 2003, in Tessaloniki, the Member States appeared unanimous in their rejection of the Commissions proposals. The chairmanship thereafter proposed for **oil** to modernise the existing EU oil crisis Directive that took effect in 1998 and to improve the management of oil stocks. For **gas** its proposal is to introduce minimum standards for security of supply, to legally acknowledge the importance of long-term contracts and to consider the possibility of a solidarity mechanism.

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