

# **Energy Security and Gas Supply in SE Europe: what after South Stream?**

## **(& how to bring together EU perceptions on investment regulation with *project financing* rules)**

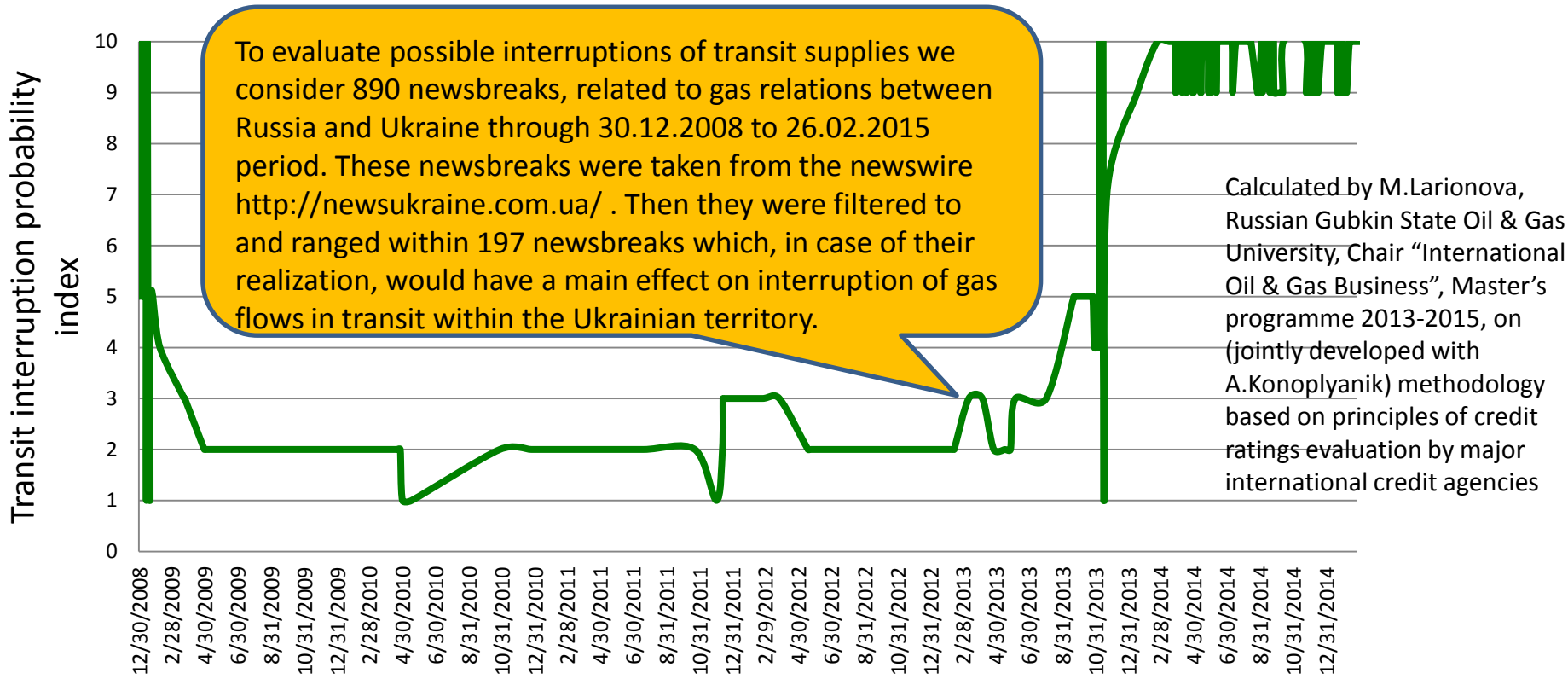
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Vienna, Austria, 12 March 2015

# Different visions on “International Energy Security” concept

- W.Churchill (1911): **IES = diversification** (“*Safety and certainty in oil, lie in variety and variety alone*”).
- G-8 Summit (SPB, 2006): **IES = SOS + SODEM + SODEL**
- (In most of?) import-dependent EU (even post-2006) **IES =:**
  - a) **either SOS only** (i.e. J.Fischer, G.Oettinger, J.M.Barroso: SODEL is NOT part of IES) – esp. in debates on South Stream,
  - b) **or diversity of counterparties within each route from each producer** (i.e. B.Devlin, EPC, 03.03.2015)
    - wrong economic perceptions ignoring *either* (a) interdependence within “Broader Energy Europe” united by fixed (immobile) capital-intensive energy infrastructure, *or* (b) sovereign right of sovereign producer/export state to define its institutional market structure
- **Russia** follows broader Churchill’s/G-8’s 2006 SPB Summit IES concept on “**multiple pipelines**” (SODEL) as **integral part of IES:**
  - => diversification of transportation routes (to diminish or escape where possible, transit risks) as a mean to improve IES, incl. SOS both for importer & exporter

# Ukraine: "transit interruption probability" index (2009–2014)

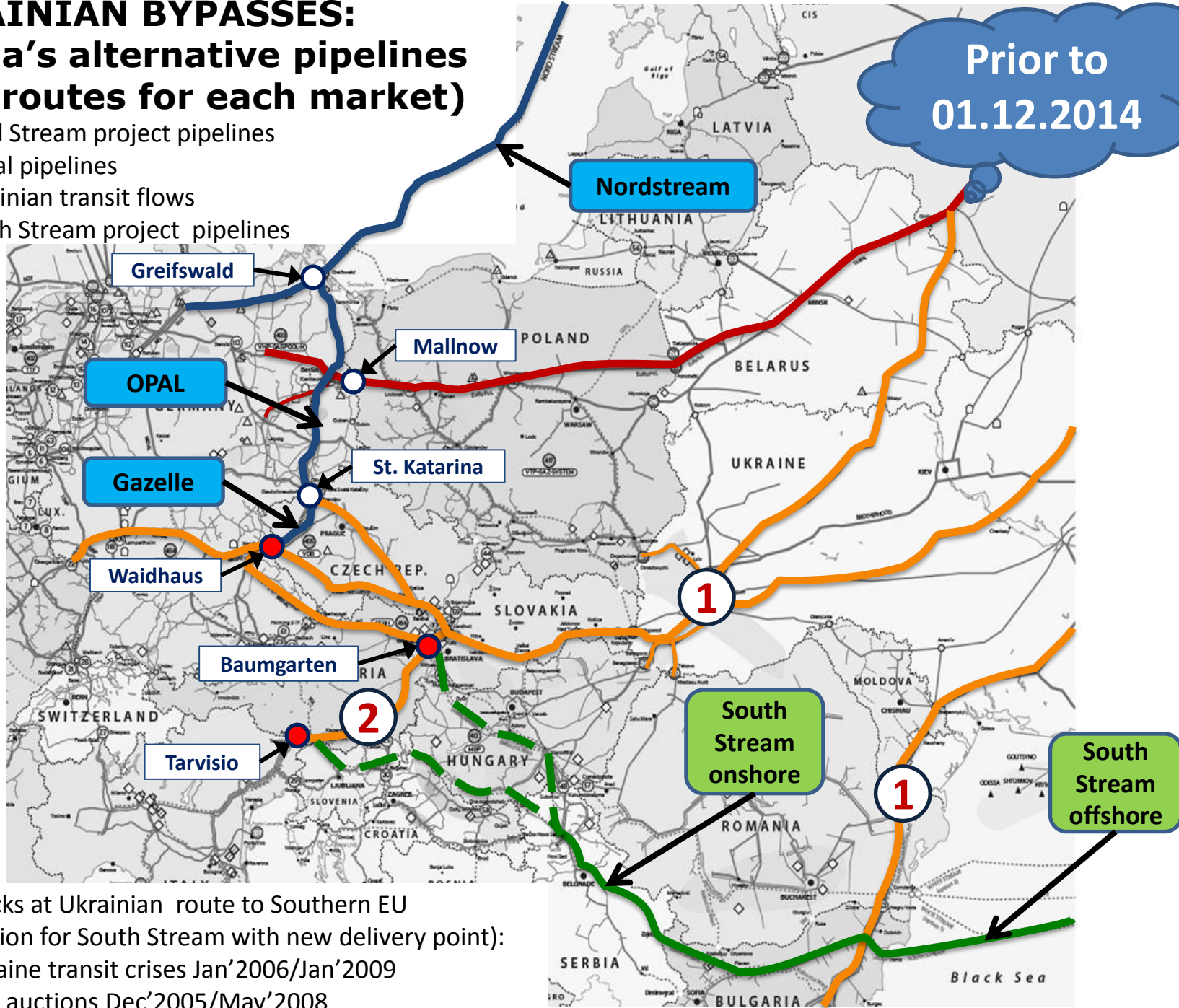


The very fact that two states cannot solve issues between them bilaterally and (at least one of them) need third party (as mediator/conciliator/arbiter) for searching temporary compromises, means a systematic mistrust => one can't leave under constant stress (uncertainty) => permanent transit risk for supplier since it is his responsibility to provide timely delivery of contracted volumes to delivery points deep inside the EU non-dependent issues with third parties => sovereign right of resource owner to evaluate such risk

# UKRAINIAN BYPASSES: Russia's alternative pipelines (two routes for each market)

- Nord Stream project pipelines
- Yamal pipelines
- Ukrainian transit flows
- South Stream project pipelines

Prior to  
01.12.2014



Bottlenecks at Ukrainian route to Southern EU  
(justification for South Stream with new delivery point):

- ① Ukraine transit crises Jan'2006/Jan'2009
- ② TAG auctions Dec'2005/May'2008



# UKRAINIAN BYPASSES: Russia's alternative pipelines (two routes for each market)

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47BCM  
at 2019:  
How to move  
from here  
acc.to  
EU  
rules?

Post  
01.12.2014

Bottlenecks at Ukrainian route to Southern EU  
(justification for South Stream with new delivery point):

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- ② TAG auctions Dec'2005/May'2008

A.Konoplyanik, IENE, Vienna, 12.03.2015

# Solution for new cross-border capacity within EU E-E zones: project financing approach (COSP, ring-fencing, ITSO, fixed tariffs till pay-back, etc.)



Parameters of new IPs/CBPs to be coordinated within chain of the zones and with supply contracts backing demand for new capacity within each zone

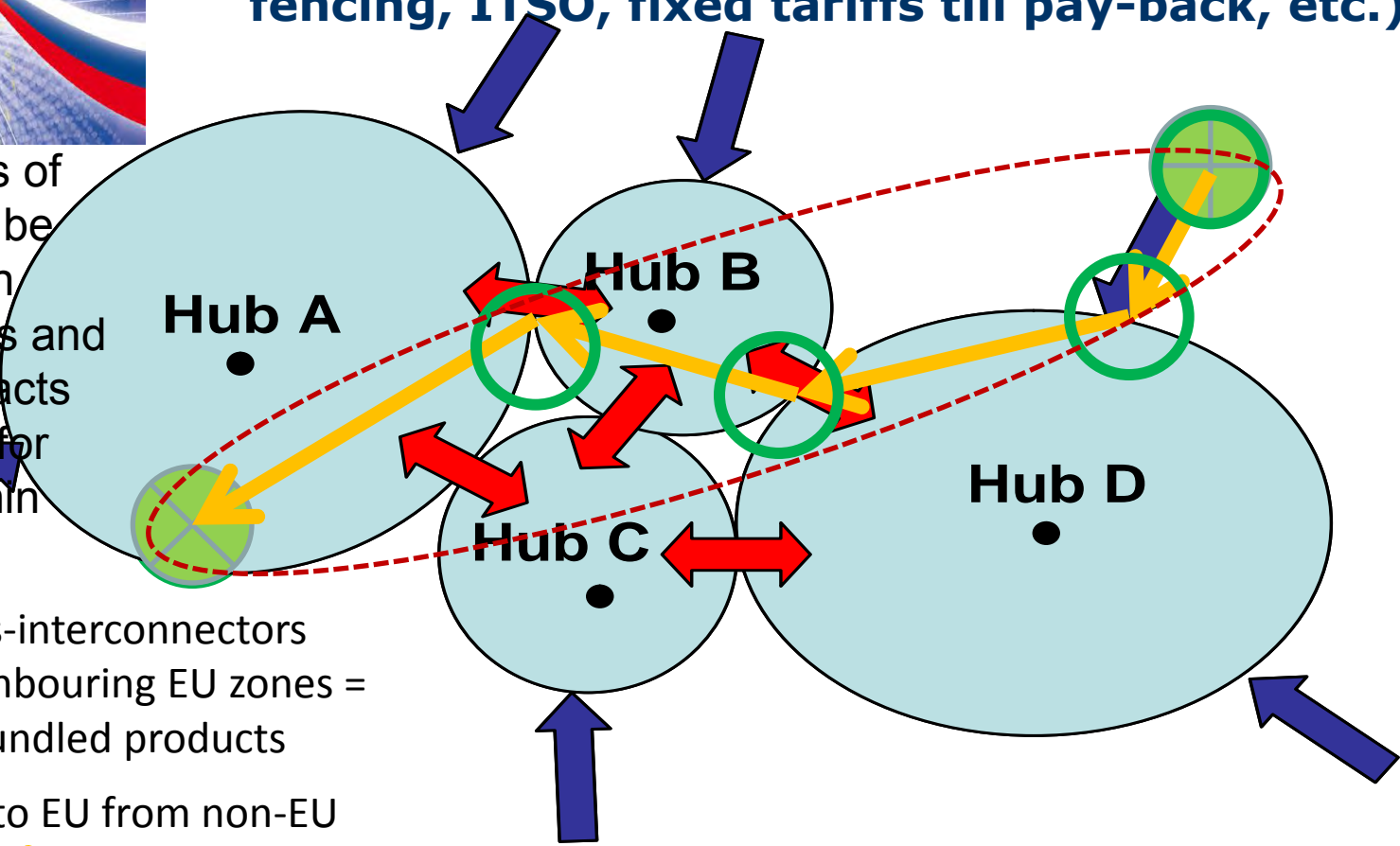
Pipelines-interconnectors between two neighbouring EU zones = single IPs with bundled products

Supplies to EU from non-EU

Non-EU producer  
Its EU customer

ITSO

**New Capacity** = multiple IPs with bundled products to be balanced, cross-border coordination of TSOs to avoid two types of contractual mismatches:  
 (1) at each IP: between term supply & transportation contract, and  
 (2) at all IPs on the route from zone to zone: between bundled products at each IP



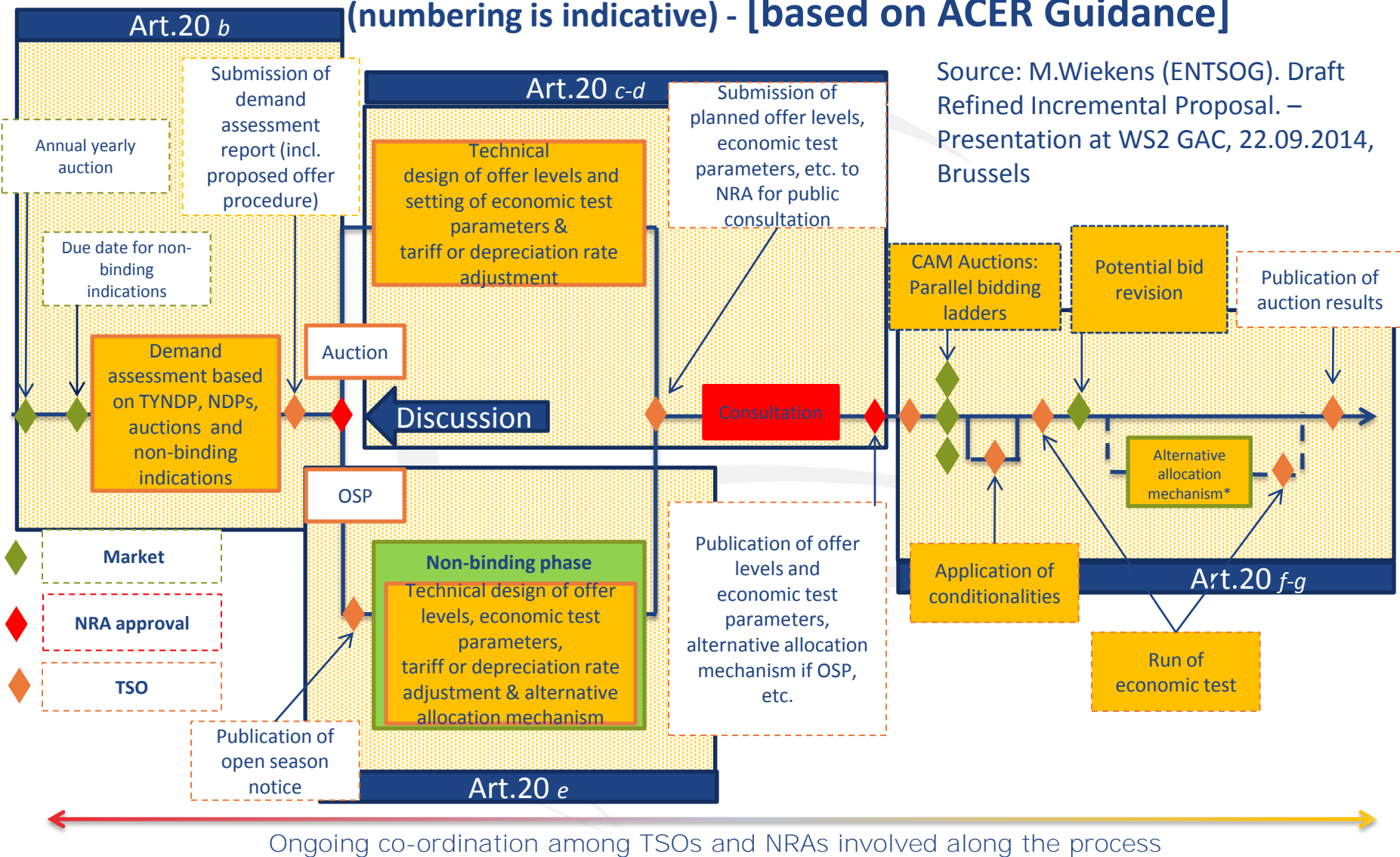
# Some key EU wrong perceptions on new capacity

Wrong perception	Why it is wrong
<p><b><u>No significant new capacity is needed in EU</u></b> since average utilization rate of existing capacity in EU appr. 70%</p>	<p>(1) Infrastructure density in CEE much lower than in NWE (40Y+ time-gap). (2) (i) New transportation routes to EU from new suppliers in South-East (Azeri, etc.), &amp; (ii) by-passes to diminish transit risk of external (Rus) supplies to EU, form new entry points to EU in SEE &amp; require new transportation routes inside EU to major EU markets</p>
<p>Risk of stable Russian gas supplies to EU via Ukraine – <b><u>to deviate from Russian gas</u></b></p>	<p>Key words for EU - “Russian gas’ (its origin, but perceived risk), while major real risk for EU – “transit via Ukraine” in result of Russia-UA disputes on supply contract to UA =&gt; major attention to new sources not to transportation risks</p>
<p><b><u>Auction as universal default procedure for capacity allocation</u></b> – for creation of <b><u>new</u></b> (not yet existing) capacity the same as in CAM NC for <b><u>existing</u></b> capacity</p>	<p>In 2009 wrong decision was taken to split preparation of CAM NC first for existing then for new capacity instead of preparation of consolidated CAM for infrastructure development. CAM NC for existing capacity first to save time &amp; report quick results in TEP implementation. Auction as MTPA for existing deficit capacity, but OSP as MTPA for non-existing new capacity</p>
<p>As if <b><u>OSP with auction</u></b> as default procedure <b><u>is financeable</u></b></p>	<p>Such OSP is non-financeable under project financing rules (segmented cross-border project, no single operator, floating tariffs, no booking guarantees, WTP as auction not NPV, cost socialization, etc.)</p>

# ENTSOE: Refining the order of articles to reflect process

(numbering is indicative) - [based on ACER Guidance]

Source: M.Wiekens (ENTSOE). Draft Refined Incremental Proposal. – Presentation at WS2 GAC, 22.09.2014, Brussels



\* An alternative allocation mechanism can only be applied in Open Season Procedures and if the default allocation mechanism prevents a positive economic test







# Turkish Stream prolongation within EU: major risks

- **Preferred option for EU** is that **Russia/Gazprom continue gas transit via Ukraine post-2019** enabling:
  - continued **financing of Ukraine** by Russia by paying transit tariffs (despite continued transit risks in unfriendly state),
  - **financing/guaranteeing pay-back of UA-EU-USA GTS consortium** acc.to UA Law 4116a (RUS participation in consortium forbidden by UA law, but **transit of RUS gas** is the **ONLY** way to make consortium financeable)
- **Two indirect ways** to implement this strategy:
  - (1) (i) slow down/prolong Amended CAM NC (Am.Reg.984) implementation till post-2019, *plus* (ii) “no go” with full utilization by Gazprom of OPAL capacity => Russia / Gazprom will have no immediate choice then to shift transit from Ukraine to another route at 2019,
  - (2) continue with Amended CAM NC (Reg.984) in its version non-financeable for cross-border new capacity (like former South & current Turkish Stream) – w/o Art.20(h)

# **Proposal: Pilot test for CAM Incremental (Amend. Reg.984/2013) for SEE “Vertical Gas Corridor”**

- “Turkish Stream” to be further prolonged within the EU towards Central Europe (hopefully before 2019):
  - non-dependent delivery points (existing vs new)
  - based on 3<sup>rd</sup> Energy Package rules (Art.13.2: TSO shall invest)
  - TSOs to effectively combine existing & new capacity
  - (i) TYNDP/PCI vs. (ii) OSP for New Cap. acc.to Am.Reg.984/2013
- 09.02.2015, Sofia: **“Vertical Gas Corridor” for SEE (03.2015)**
- **Pilot test for financeability of EU investment rules:** first implementation of Amended Reg.984/2013 (i) **without** (existing draft) & (ii) **with** (our proposal) **Art.20(h)**:
  - ACER “public consultations” ended 04.03.2015 => no result yet => then Commission to decide => time allows yet... (window of opportunities to improve procedure to become financeable)
  - Based on pilot test results, to adapt Amended Reg.984/2013 before its final approval by EU
  - => **EU (ACER/CEC/MSs => incl.SEE MSs) to decide. !!!**

# Thank you for your attention!

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