European Economic and Social Committee

TEN/126
Security of energy supply

Brussels, 26 March 2003

OPINION

of the European Economic and Social Committee

on the

Proposal for a Directive of the European Parliament and of the Council concerning the alignment of measures with regard to security of supply for petroleum products

Proposal for a Directive of the European Parliament and the Council concerning measures to safeguard security of natural gas supply

Proposal for a Council Directive repealing Council Directives 68/414/EEC and 98/93/EC imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products, and Council Directive 73/238/EEC on measures to mitigate the effects of difficulties in the supply of crude oil and petroleum products

COM(2002) 488 final - 2002/0219 (COD) - 2002/0220 (COD) - 2002/0221 (CNS)

On 15 October 2002, the Council decided to consult the European Economic and Social Committee, under Article 95 of the Treaty establishing the European Community, on the

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COM(2002) 488 final - 2002/0219 (COD) - 2002/0220 (COD) - 2002/0221 (CNS).

The Section for Transport, Energy, Infrastructure and the Information Society, which was responsible for the Committee's work on the subject, adopted its opinion on 13 March 2003. The rapporteur was **Mr Cambus**.

At its 398th plenary session, held on 26 and 27 March 2003, (meeting of 26 March), the European Economic and Social Committee adopted the following opinion with 96 votes in favour and three abstentions:

1. **Summary of the Commission's proposals**

   1. The three texts presented to the EESC follow on from the Green Paper entitled "Towards a European strategy for the security of energy supply[1]".

   2. There is a common background to the texts presented by the Commission, namely the fact that, over the next 20 years, the EU's external energy dependency could increase from 70% to 90%, in the case of oil, and from 40% to 70%, in the case of gas. Energy is a vital commodity for the economy (production and transport), whilst also providing private comfort for individuals. As most oil and gas production is based in areas of political uncertainty, security of supply with regard to both oil and gas is clearly a strategic requirement for the EU.

   3. In its communication, the Commission identifies two types of risks with regard to energy supply, namely: physical shortage caused by technical problems (loss of installations) or political difficulties (deliberate suspension of all or part of deliveries) and the spiralling of prices to levels which would place a heavy burden on the EU and would exact a heavy cost in terms of loss of growth and jobs (an increase of $10 per barrel would cut the EU's rate of growth of GDP by 0.5%) and which would also place an unbearable burden on households as final users (e.g. for heating or motor vehicle fuel).

   4. **As regards oil**, two directives[2] have already been introduced with a view to addressing security of supply in the Member States by imposing on them an obligation to maintain stocks corresponding to 90 days' consumption for three categories of petroleum products, (motor gasolines, middle distillates and heavy fuel oil), with adjusted conditions for oil-producing Member States.

1. Member States are free to implement these obligations in whatever form suits them, ranging from stockholding by private operators to stockholding by public bodies.

2. The completion of the internal energy market makes it necessary to proceed to a further stage in order to: improve competition in the refined products sector, guarantee that this market operates properly, make the EU's security stock capacity more credible and more high profile, and ensure that the action taken by Member States in the event of oil market crises is both uniform and coherent.

3. The proposals put forward with a view to achieving these objectives are as follows: the creation of a central body in each Member State to help new entrants and those not having their own installations to respect the storage obligations; the possibility of holding stocks in another Member State, so as not to place transnational operators at a disadvantage; increasing the stockholding requirement from 90 days' consumption to 120 days' consumption, with one-third of the stocks being held by the central body in order to raise the profile of the strategy for ensuring security of supply; and finally, the introduction, at EU level, of a joint regulatory framework covering the release of stocks of petroleum products and involving an appropriate decision-making process under the comitology procedure.

4. The Commission also puts forward a novel idea in respect of oil: the possibility of using strategic reserves to intervene on the market with the aim of seeking to reduce the impact of speculation on the volatility of prices for petroleum products when supply crises are anticipated.

5. **Turning to the gas sector**, the situation here is characterised by (a) a delay in opening up the internal market, even though gas is accounting for an ever larger share of the EU energy market because of, inter alia, its role in electricity generation (between 50 and 60% of electricity is generated from gas) and (b) a high level of external dependence since 40% of gas is supplied from three sources outside the EU. The International Energy Agency (IEA) has no means of intervention at its disposal in respect of gas.

    1. Before the gas sector was opened up to competition, security of supply was ensured by supply companies which enjoyed a monopoly. Once the market for gas is opened up, there will be several market players; the responsibilities of each of these players will therefore have to be redefined in order to ensure security of supply for gas users.

    2. The situation with regard to gas differs from that for oil from the point of view of the technical scope for holding stocks, which mainly depends on subterranean geology. The aim of the Commission's proposal is to extend to gas the principles set out in respect of oil but without simply transferring the same instruments. The aim is for the Member States to adopt a minimum joint approach with a view to completing and protecting the market.

3. With a view to ensuring security of gas supplies, the Commission proposes to impose an obligation on Member States to define the responsibilities of operators for ensuring the supply of gas for a period of 60 days of average consumption to customers who are not in a position to replace gas with an alternative fuel. It is, however, proposed that new entrants to the market for gas and companies with small market shares be exempted from this obligation. The Commission intends to monitor closely long-term contracts and the contribution which they make towards ensuring security of supply in the Member States.

4. In the event of crises and in order to ensure solidarity between Member States, the Commission wishes to be able to take decisions to release stocks of gas held in the Member States and actually to interrupt supplies to the interruptible market.

6. **From a general standpoint**, the proposals put forward by the Commission are based on the affirmation that, once the energy market in the EU has been opened to competition, the strategy for ensuring security of supply can no longer be pursued most effectively at the level of operators or individual Member States; this responsibility will therefore have to be assumed by the EU.

2. General comments

1. Relevance of the proposal

1. The EESC expresses its appreciation for this proposal, which follows on from the Green Paper on the security of energy supplies and carries out a thorough appraisal of the EU's security of energy supply in respect of oil and gas. After devoting ten years mainly to organising the energy market, opening to competition the monopolies which have traditionally existed in the fields of electricity and gas, and promoting renewable sources of energy, it is important that the Community now backs up this action by tackling the fundamental issues relating to the supply of these products; the EU has a structural deficit in domestic production of energy products and is therefore highly dependent on non-EU suppliers. It is important to note the major roles played by oil and gas in the EU's energy balance, particularly in transport and energy-generation (which has been responsible for a very sharp increase in the consumption of gas), and their consequent contribution to growth, employment and private comfort.

2. Subject of the proposal

1. Of the energy products imported by the EU (coal, gas, oil and uranium), oil and gas are undoubtedly those which play the most significant role in the context of the energy balance. Furthermore, they are imported from regions in the world which suffer from a lack of diversification and are exposed to political risks. In view of the

strategic importance of oil and gas, it is therefore vital to establish specific policies for these products.

2. The EESC considers that these two energy sources - natural gas and oil - give rise to fundamentally different problems; in including them in the same package of measures, we must not underestimate the impact of these differences. The first of these differences is that gas is generally speaking both a raw product and a final product at one and the same time; it has a low technological added value within the EU, whereas most oil is imported in the form of crude and subsequently processed within the EU. This explains why the price of gas has generally followed the price of oil, with the aim of enabling the full range of competing uses of these two forms of energy to be developed. This also explains the existence of "destination clauses", which are incompatible with the rules of the single market; this matter is currently being addressed in the case of new contracts. The supporters in favour of opening up the gas sector to competition hope that this will be a way of reducing, if not completely removing, the link between the prices of these two forms of energy. Furthermore, on a global level the companies producing oil and gas are frequently the same since prospecting for one of these products frequently leads to the discovery of supplies of the other.

3. The second difference relates to the structure of the market. There has long been a worldwide market for oil and it is transported from the areas of production to the areas of refining and consumption by ship rather than pipeline. This is not the case with gas. The market for gas is organised on a regional level (the EU obtains its supplies mainly from Norway, Algeria and Russia; the USA links up with Canada and Mexico to provide a market for gas; and Japan, Korea and Indonesia form a further market). The EU market has been the most stable - the American market is less stable and the Asian market is more expensive. Although this is outside the scope of this opinion, the recent events which have had such an impact on the coastlines and populations of Spain and France bolster the case for the increased use of pipelines to transport oil wherever this is technically feasible, even if it would seem to be more costly in purely economic terms.

4. The third important difference is that within the EU natural gas is generally transported to end markets by pipeline, whereas petroleum products, including LPG, are transported by pipeline from import and storage areas to refineries but are then generally transported by tankers to the final point of consumption. Any provisions which serve to shift strategic and operational stocks of refined petroleum products away from the centres of consumption will thus increase the number of transport operations by lorry.

5. The EESC therefore wishes to clearly differentiate the measures to be taken in respect of these two energy sources, even though it is desirable, as the Commission proposes, to set out common guidelines.

6. The EESC would like the proposal for a Directive to cover also the candidate states when addressing the question of security of energy supply, considering the impact on both the new Member States and the current Member States. It is important to negotiate the deadlines by which the candidate states will have to comply with the storage levels and procedures applicable to the existing Member States and to discuss the technical and economic issues with which the candidate states could be confronted in this context.

3. **Specific comments**

1. **Comments on the proposals in respect of oil**

1. The EESC endorses the proposal to oblige the Member States to set up a central security stockholding body, which is to hold stocks representing one third of the specified obligations. The EESC believes that these centralised stocks will fulfil the need to highlight the existence of the EU's strategic stocks and will help to discourage those who may be tempted to engage in price speculation. The EESC also endorses the possibility for several Member States to meet this stockholding requirement on a joint basis and for Member States to hold their mandatory stocks in another Member State. The best way to provide for this could be, in the EESC's view, to have stocks earmarked by the operator concerned or to have recourse to centralised stockholding bodies, whose establishment is proposed by the Commission. The aim is to ensure clear identification of the parties responsible for managing stocks held outside a Member State.

2. The EESC does, however, wonder - for a variety of reasons, set out below - whether it is advisable to oblige the Member States to increase their security stocks from 90 days' consumption to 120 days' consumption. Any increase in the stockholding requirement clearly provides better guarantees that crises can be overcome but these improved guarantees come with a price tag; it is essential to fully appreciate what is at stake and the likely outcome of such an increase before taking the requisite decision.

1. Member States are currently obliged by the EU (under Directives 68/414/EEC and 98/93/EC) to hold stocks of finished products (listed in three categories) corresponding to 90 days of average consumption. Under provisions established by the IAE, of which they are members, EU Member States have to hold stocks equivalent to 90 days' imports; this latter requirement generally imposes a greater obligation, particularly in view of the fact that the IAE stipulates that an allowance of 10% has to be made to cover, inter alia, bottom-of-tank stocks which cannot be used. As a result of this and in view of the additional precautions that some states may take, the actual stocks held by IEA member states are estimated by the agency to correspond, on average, to 114 days' imports, whereas the stocks held by EU Member States are estimated by the Commission to correspond

to 115 days' consumption. Nonetheless, the impact of increasing the mandatory obligation to 120 days could not be described as minimal; it would have a very onerous effect on the southern Member States, which, for reasons of climate and because of their lower heating requirements, hold stocks of the order of 90 days, whereas the reserves of some northern Member States already exceed 120 days.

2. Since the Yom Kippur War in 1973, which led to the imposition of an oil embargo by some Arab states, oil-consuming states have not had to face new physical disruptions of supply brought about by political events. The spiralling of oil prices as a result of the 1973 embargo prompted a number of reactions, in particular, the substitution of other energy sources, such as nuclear power and, to a lesser extent, renewables. This reduced the marketing outlets for oil-producing countries for many decades. Producer and consumer states consequently became aware that they had a joint interest in avoiding any drop in oil production and consumption levels. This being the case, the development of political relations conducive to good commercial cooperation seems to be an approach which should be pursued, particularly in view of the fact that the USA is in the process of refocusing its commercial relations on our side of the Atlantic and, in particular, Africa.

3. It is, however, not possible to rule out the risk of incidents being caused by, for example, terrorists, which could lead producers and consumers to reduce supplies of oil from one localised geographic area for a certain period. In such a case, it is unlikely according to experts that, if it has not been possible to find a suitable solution to the problem within the period of 90 days covered by the current level of the mandatory reserves, 30 more days will be long enough to find such a solution.

4. The economic impact of a decision to increase the level of strategic stocks to 120 days differs according to whether this involves (a) topping up existing unused physical stocks, in which case the only additional cost to be taken into account would be that of adding to the products tied up in this way or (b) increasing the actual volume of the necessary storage installations. In view of the ever growing distrust and fear felt towards all classified industrial installations, there are few areas in the EU which are prepared to accept the building or expansion of storage facilities for petroleum products, bearing in mind that "Seveso" type installations are involved here. Finally, the bill for this increase in strategic stocks is likely to have to be met by consumers; such a measure would, of course, not be very popular and nor would it be particularly conducive to maintaining growth.

3. The EESC does not agree with the line taken by the Commission towards the IEA. Since its establishment in 1973, the IEA has had the role of coordinating the reactions of member countries confronted by crises leading to a physical shortage of oil supplies in the world. The IEA has, since its establishment, adjusted its rules of operation to bring them into line with the changing background situation, with, incidentally, the participation of the EU. It was not the IEA's task to intervene when prices shot up since this is not its role.

    1. As the oil market is a worldwide market and since one third of production capacity is situated in the OPEC countries, a coordinated response has to be organised at world level if it is to be effective. The argument which holds good in the EU, to the effect that a reaction by one Member State acting alone and in opposition to the other Member States would be ineffective, is even more valid in the case of reactions at world level to serious oil supply crises. In the EESC's view it is therefore essential for the EU's strategy on security of oil supply not to be separate to that adopted by the other major consumer states; to that end the EU's strategy should be based on a close collaboration with the IEA. By speaking with one voice, EU Member States will certainly carry more weight within and in their dealings with the IEA than if they adopted a Eurocentric approach, which does not make very much sense since the oil market is a worldwide market.

4. Whilst the EESC shares the Commission's concerns over the damaging effects of sharp increases in oil prices on the EU economy and household purchasing power, it is, however, very guarded about the Commission's proposal for using strategic stocks to intervene on the market in a counter-cyclical way when the prices rise sharply. The EESC bases its standpoint on a number of arguments.

    1. Regulating oil prices is a difficult task as the price of these products has an inbuilt volatility. It is impossible to achieve a fine balance between supply and demand. Investments in exploiting oilfields are decided upon, on average, five years before production starts and on the basis of forecasts which are never strictly confirmed by the actual situation at the time in question. Subject to this technical and economic constraint, the OPEC states keep the variation in oil prices within the range of $22-28 per barrel; this appears to be the average level of prices which is acceptable to all the players involved. If the OPEC states did not take this action, price volatility would no doubt produce prices ranging from $3-60 per barrel. OPEC accounts for almost 40% of global oil production, which enables it to regulate prices in this way. The EU, for its part, accounts for only between 20% of global oil consumption; it is therefore an illusion to believe that, on the strength of a percentage of the market which is less than half of that controlled by OPEC, the EU would be capable of achieving more effective results,

possibly by acting independently of cooperation at world level through the IEA.

2. Oil prices may spiral out of control when the oil industry and consumers fear an imminent actual physical shortage, brought about by serious political or climatological factors which could come into play (such as wars, terrorist attacks or earthquakes). The reason why prices go up is because all buyers rush to increase their reserve stocks. How is it possible to imagine that, in such a situation, when all the actors involved fear the worst, the authorities in the EU could decide to oblige the Member States to release part of their strategic reserves in order to hold price levels for a brief moment, only to have to reconstitute these reserves later at a high price in order to contend with the risk of a real physical shortage? This is hardly credible.

3. There is also a practical difficulty since oil purchases are computer managed on the basis of the workload plans of refining units and price thresholds. The strategic stocks cannot be included amongst the lists of regular suppliers to be found in the management programmes; under these circumstances reserves could only be marketed using "manual" and hence onerous processes. This would fly in the face of the need for rapid intervention, designed to wrong foot the market. However, announcements of intention to place stocks on the market would not be incompatible with this requirement.

4. Finally, the decision to release strategic stocks would be a costly venture and this cost would have to be justified and endorsed by the European Parliament, as the idea of an EU body taking such a decision and then presenting the bill to the Member States would not go down well. The cost would be very high, even if we assume that only the one-third of the strategic reserve managed at a central level would be available for use in this way as this corresponds to almost one month's oil consumption in the EU and would be placed on the market probably at the equivalent to $20 per barrel, only to be renewed at a much higher price later.

5. The experience gained with the world tin market, where producer and consumer states organised the market and concluded six agreements between 1953 and 1981, demonstrates that action taken to control prices failed to produce the desired result. The theory that measures to control demand are the way to bring an influence to bear on prices has not been borne out in practice.

6. There is a kind of contradiction between, on the one hand, the EU doctrine based on the efficiency of the market in dealing with monopolies, oligopolies and administrations and, on the other hand, the readiness to give one of the EU institutions the

power to intervene on the oil market in the event of unfavourable developments.

2. **Proposals relating to gas**

1. The EESC endorses the decision to oblige Member States to introduce policies for ensuring supplies of gas in order to guarantee supplies, under difficult conditions, to customers lacking alternative fuel options (non-interruptible customers with no alternative fuel switching capacity), be such customers households or businesses. The EESC shares the Commission's view that these policies, setting out the responsibilities of the various market participants, should not stand in the way of the development of the internal market in gas, which is in the course of being completed.

2. The EESC endorses the proposed formula for assessing the obligation to ensure that security of gas supply can be maintained for a period of 60 days of average consumption, in the event of supplies being restricted.

3. The EESC understands that, given the current situation as regards the internal market for gas, the Commission does not wish to penalise unduly companies which are "new entrants" to the market or "companies with small market shares". The EESC does not however believe that consideration should consequently be given to exempting these companies on principle from the security of supply provisions to be implemented by the Member States. It should be up to the Member States to define the best way to reconcile, on the one hand, the priority which has to be attached to maintaining security of supply for customers with, on the other hand, the real opening-up of the market.

    1. Household customers and very small enterprises do not have the necessary knowledge to gauge the reliability of an offer made by a gas supplier, if the state does not require the supplier in question to assume his share of the responsibility, irrespective of how big or small he may be. Furthermore, the proposed exemption would result in a difference of treatment vis-à-vis oil suppliers which are required in the Commission's proposal to contribute to stocks - and to make payments to the central stockholding agency.

4. The EESC is pleased to note that the Commission has adopted a more realistic approach to long-term contracts, which it criticised considerably on the occasion of the opening-up of the market in gas to competition, singling out the *"take-or-pay"* clauses for special criticism. These contracts and clauses are justified on the grounds of the size of the investments required to market natural gas and the shared desire of producers, purchasers and investors to recoup and make a profit on their investments and ensure security of supply. In the EESC's view, however the Commission cannot readily oblige Member States to accept minimum requirements in long-term contracts since in

a market which is open to competition each company is free to decide how it manages its supplies.

5. The EESC endorses the proposal made by the Commission that it be authorised to put forward recommendations to Member States on the measures to be taken in the event of a disruption in supplies from a key supplier to the EU. If no effective action is taken on these recommendations, the Commission wishes to be authorised to require Member States to take action. The EESC highlights the fact that, in such a case, it would be difficult for the Commission to assess the exact nature of the constraints in connection with the use of stocks and operation of networks, particularly as regards security. Gas stocks form part of the integrated management of the gas-supply system; they cannot be arbitrarily requisitioned. Furthermore, it is not possible to hold stocks for excessively long periods without using them.

6. The EESC supports the proposal that Member States report to the Commission on their respective situations as regards supply problems and the policies which they are pursuing in order to promote security of supply.

3. Oil and gas

1. The EESC believes that, from the public standpoint, the strategy for ensuring security of energy supply has to be transparent; this transparency has been explicitly requested by consumer representatives.

2. The EESC recognises that Member States have traditionally ensured their own security of energy supply by selecting the most appropriate ways and means which best meet their political needs. Oil and gas are not the only sources of energy in the Member States; some Member States chose to invest heavily in hydroelectric and/or nuclear power. Should Member States be faced with supply crises affecting any one of the energy sources making up their overall energy-supply package, it is normal that they should be able to take into account their overall energy situation. That being the case, direct intervention by the EU should be ruled out, in accordance with the principle of subsidiarity.

    1. The role of the EU should be to (a) define common standards, as it has done in the documents under consideration; (b) ensure that the Member States apply these standards, which it is proposing to do by means of the reports to be presented by the Member States; and (c) propose coordination and solidarity instruments, particularly in respect of the management of strategic oil and gas stocks.

3. The EESC draws attention to the fact that another way of responding to the risk of oil and gas supply difficulties in the EU is for the Commission to continue its actions and incentives for promoting: diversification of energy supply sources; research in the field of non-

polluting, renewable sources of energy; and a reduction in the consumption of hydrocarbon fuels.

4. In the light of the provisions of the Treaty of Nice, the EESC considers that it should be involved in the assessment and monitoring of the policies for ensuring security of oil and gas supplies since the EESC itself comprises representatives of the various economic and social components of organised civil society and represents producers, consumers, workers and movements for the protection of the environment.

4. Conclusions

1. The EESC supports the Commission's objective of defining common guidelines for ensuring security of oil and gas supplies in the EU, following on from the Green Paper on security of energy supply and backing up the guidelines already introduced for achieving a European energy market.

2. On the subject of oil supplies, the EESC endorses the Commission's proposal to oblige the Member States to set up a central body responsible for security stocks. The intention is to give greater prominence to the holding of such stocks, ensure cost-transparency and not discriminate against companies without their own storage facilities, thereby avoiding any distortion of competition.

    1. The EESC takes a very guarded line as regards the proposal to increase the security stockholding requirement from 90 days' consumption to 120 days' consumption for all Member States, bearing in mind that, in practice, northern states need to hold larger stocks than southern states for obvious climatological reasons, as they do at present. The EESC believes that there are no compensatory benefits to justify the additional cost of such a decision.

    2. The EESC gives a similarly guarded response to the proposal to use these strategic stocks for the purpose of bringing an influence to bear on oil prices in cases where fear of a possible physical shortage leads companies to engage in precautionary purchases, thereby giving rise to panic and consequent price increases.

    3. The EESC takes the view that, in order to give it sufficient clout and prospects of success, action by the EU to manage oil supply crises should be carried out within the framework of the IEA.

3. As regards gas supplies, the EESC shares the Commission's desire to give the Member States responsibility for laying down the rules to be followed by companies in order to ensure security of supply.

    1. The EESC believes that the proposal to take appropriate steps to ensure supplies of gas equivalent to 60 days' average consumption represents an effective approach.

2. The EESC underlines the fact that the storing of gas is a very different matter from the storing of oil; the constraints and technical difficulties involved need to be appreciated when stocks have to be used in the event of supply crises.

3. The EESC notes that companies which are new entrants to the market may be exempted from the obligation to hold security stocks; it wonders what impact this measure may have and proposes that responsibility for it should lie with the Member States.

4. In the light of the EESC's own nature and role, it believes that it should be associated and involved in the monitoring and assessment of the policies for ensuring security of oil and gas supplies; such involvement would fulfil the need for transparency expressed by representatives of European consumers.

Brussels, 26 March 2003.

The President	The Secretary-General
of the	of the
European Economic and Social Committee	European Economic and Social Committee
Roger Briesch	**Patrick Venturini**

[1] COM(2000) 769 final

[2] Council Directive 68/414/EEC, of 20.12.1968 imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products and Council Directive 98/93/EC, of 14.12.1998 amending Directive 68/414/EEC imposing an obligation on Member States of the EEC to maintain minimum stocks of crude oil and/or petroleum products. The first directive imposed an obligation on Member States to keep stocks corresponding to 65 days' consumption, a figure which was subsequently increased to 90 days' consumption by the second directive.

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