GETTING THE DEAL THROUGH

Gas Regulation

in 36 jurisdictions worldwide

2011

Contributing editors:
Florence Ninane, Alexandre Ancel and Jean-Yves Ollier

Published by
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Contributing editors
Florence Ninane, Alexandre Ancel and Jean-Yves Ollier
Allen & Overy LLP

Business development managers
Alan Lee
George Ingledew
Robyn Hetherington
Dan White

Marketing managers
Ellie Notley
Sarah Walsh

Marketing assistants
Alice Hazard
William Bentley

Subscriptions manager
Nadine Radcliffe
Subscriptions@GettingTheDealThrough.com

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Adam Myers

Editorial assistant
Lydia Gerges

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Jonathan Allen

Senior subeditor
Kathryn Smuland

Subeditor
Davet Hyland

Editor-in-chief
Callum Campbell

Publisher
Richard Davey

Gas Regulation 2011
Published by
Law Business Research Ltd
87 Lancaster Road
London, W11 1QQ, UK
Tel: +44 20 7908 1188
Fax: +44 20 7229 6910

ISSN 1740-7826

Printed and distributed by
Encompass Print Solutions
Tel: 0844 2480 112

Law Business Research

Germany

Solveig Hinsch and Boris Scholtka
Scholtka & Partner Rechtsanwälte

Description of domestic sector

1 Describe the domestic natural gas sector, including the natural gas production, liquefied natural gas (LNG) storage, pipeline transportation, distribution, commodity sales and trading segments and retail sales and usage.

Germany is a rather small and mature area in terms of natural gas production. The potential for exploration is expected to be around 200 billion cubic meters (source: Federal Ministry of Economics and Technology, BMWi).

Owing to the lack of LNG terminals, Germany presently has no LNG market. The country has gas storage facilities covering about 20 per cent of its annual consumption of natural gas. The German gas transportation system is organised, as of 1 April 2011, into three 'market areas' (Net Connect Germany (NCG H and L-Gas); 'Gaspool' (H-Gas); and 'Aequamus' (L-Gas)). The market areas are managed by three individual operators (Net Connect Germany, Gaspool and Aequamus). Each market area uses multiple transportation systems owned by the former transmission system operators, such as Open Grid Europe (previously E.ON), Gasunie Deutschland (previously BEB), Thyssengas (previously RWE), Aequamus (joint venture of EWE, Erdgas Münster and Gasunie Deutschland), Wingas, Bayernets, Ontras (previously VNG) and others. The distribution market is characterised by a multi-tier structure containing some big companies at the importation level (E.ON Ruhrgas, RWE, VNG, Wingas, ExxonMobil and Shell (previously BEB)), some other companies at the regional level and approximately 720 companies operating at the local distribution level as well as a considerably growing number of independent distributors targeting end-customers nationwide. Gas trading activities have increased with the start of the German gas exchange and trading at virtual hubs but are still restricted by limited entry capacities. A number of foreign gas traders have successfully entered the market as well. Retail sales are, however, still mainly effected by regional supply companies.

2 What per centage of the country's energy needs are met directly or indirectly with natural gas and LNG? What per centages of the country's natural gas needs are met through domestic production and imported production?

Approximately 22 per cent of Germany's primary energy supply stems from natural gas (source: BMWi). Domestic production amounts to 14 per cent of total gas supply. Other imports come from mainly the Netherlands (17 per cent) and Norway (33 per cent). By far the most important source is Russia (34 per cent) (source: BMWi figures 2009).

3 What is the government's policy for the domestic natural gas sector and which bodies set it?

The implementation of the second Gas Directive 2003/55/EC accompanied the establishment of regulatory authorities – the Federal Network Agency for Electricity, Gas, Telecommunications, Mail and Railways (Bundesnetzagentur or BNetzA), and regulatory authorities on the state level. These regulatory authorities are in charge of network tariff regulation (incentive based regulation), abuse proceedings regarding network access, etc. In contrast, the Federal Cartel Office controls (only) those parts of the energy sector that are not subject to regulation, especially those areas which are considered to be fully liberalised. Recently, it alleged proceedings against some municipal utilities for abuse of a market dominant position due to certain distinctions regarding the imposition of concession fees. The Federal Cartel Office also observes the generation of power.

Regulation of natural gas production

4 What is the ownership and organisational structure for production of natural gas (other than LNG)? How does the government derive value from natural gas production?

Gas production in Germany is operated by privately owned exploration and production companies, a number of which have foreign shareholders. Apart from regular tax regulations on the consumption of natural gas, the exploration and the exploitation of natural gas are subject to special mining levies. First, the exploration of mineable resources like gas is subject to an exploration fee which is comparatively minor. Second, for the exploitation of gas the mining operator has to pay a fee which amounts to 10 per cent of the market price of the produced gas.

5 Describe the statutory and regulatory framework and any relevant authorisations applicable to natural gas exploration and production.

The Mining Law provides for a two-part regulatory framework. First, mining companies have to maintain a right to explore or exploit a mineable resource. Second, the operation of exploration or exploitation is subject to a permission by the responsible authority. The right to explore mineable resources is subject to either a permission or an authorisation; the right to exploit mineable resources is subject to an authorisation or the possession of mining property. All such licences are granted on application by the responsible authorities to a mining company.

The operation of a mining enterprise for either exploration or exploitation is subject to further permission (Rahmenbetriebsplan). This permission has to be granted if the mining company complies with all legal requirements. The Rahmenbetriebsplan usually sums up many permissions needed from other authorities. Depending on the respective state law, the regional mining authorities are responsible for all authorisations. They are part of the state administrative body. Within the scope of the permission, the mining company may decide upon the timing and quantity of gas production.

All decisions of any state authority may be challenged before the administrative courts. The respective regulation generally provides for an objection procedure within the administrative body prior to a court procedure, even though some states have recently waived such requirement. Both appeals, to the administrative body and to the administrative court, have to be filed within a period of one month after release of the respective decision. The administrative courts are independent and only bound to the law and justice. Attorneys are only requested on the second and third level of justice and may represent the plaintiff on the lower levels as well.

The transmission and distribution of natural gas requires network operation and is hence subject to regulation by either the federal or the respective state regulatory body. The decisions of the respective regulator may be challenged before the higher civil courts within one month after the release of the respective decision.

Regulation of natural gas pipeline transportation and storage

6 Describe in general the ownership of natural gas pipeline transportation, and storage infrastructure.

The German transportation system is operated in market areas by three private companies. These companies are joint ventures of the underlying transportation system operators, and considerably vary in terms of size and network dimension (see question 1). Only some big companies are involved in cross-border flows, the others are mostly active on the German market at a more regional level. Further, the market areas are operated with different gas qualities (high-calorific and low-calorific gas - see question 1). Storage facilities are still mainly operated by storage companies linked to the big transportation system operators and, to a lesser extent, by gas utilities on the distribution level (approximately 70:30 in 2009, compared to 80:20 in 2008). Germany has a storage capacity of nearly 20.4 billion cubic metres (source: Bundesnetzagentur, Monitoring Report 2010).

7 Describe the statutory and regulatory framework and any relevant authorisations applicable to the construction, ownership, operation and interconnection of natural gas transportation pipelines, and storage.

The construction, operation or modification of pipelines with a diameter of more than 300 mm – therefore basically transportation pipelines – need to run through an administrative planning procedure including an environmental assessment procedure and other administrative permissions.

Moreover, commencing network operations needs the prior approval of the competent authority at state level. Approval may only be denied if the authority finds the applicant unable to provide the personal, technical or commercial capability and reliability to ensure a network's operation in accordance with the given legal framework. For operating storage facilities, mining law has additionally to be observed.

8 How does a company obtain the land rights to construct a natural gas transportation or storage facility?

Basically, the company must obtain necessary land rights on the basis of German contract and property law. Therefore, a system operator must reach an agreement with the respective owner or beneficiary of the land. If such agreement cannot be achieved, German energy law may impose restrictions on property or may even extend to administrative expropriation. A comparable approach is provided for the construction of storage facilities pursuant to mining law for above ground facilities. Deep underground storage facilities are generally not subject to civil law property rights, however, the proprietor of a plot above such storage is not entitled to claim for the elimination of the storage.

9 How is access to the natural gas transportation system and storage facilities arranged? How are tolls and tariffs established?

Germany has regulated third-party access to the gas grid on non-discriminatory and objective conditions. The framework is provided by the Energy Industry Act, in more detail by the Gas Network Access Ordinance, and by further provisions or injunctions issued by the regulatory authorities.

Grid access is obtained on a contractual basis for feed-in (usually at the transportation level) and off-take (usually at the distribution level).

The German market is divided into market areas pursuant to the so-called Cooperation Agreement (currently still the Cooperation Agreement III, which has been implemented under surveillance of Bundesnetzagentur; the Agreement is currently being revised). Within a market area, the network user or shipper needs only an entry and an exit contract (two-contract model). Natural gas can be delivered or traded at the market area's virtual hub. The number of market areas has been significantly reduced but the ultimate task is to end up with only two different market areas by 1 August 2013. In the meantime, the industry is required to reduce the number of market areas to three, as of 1 April 2011, under the recently revised gas network access regulation.

As parts of the German transportation infrastructure run in parallel, transportation system operators (TSO) used to benefit from a legal exemption: access to their transportation system used to be subject (only) to negotiated tariffs. As of the gas year 2010/2011, due to the lack of efficient pipe-to-pipe competition, on the (long-distance) transportation level a regulated network access tariff is required by Bundesnetzagentur. The network tariffs of these companies will also be subject to an incentive-based regulation (see question 15).

At present, the Federal Network Agency is working on an innovative regime for capacity usage. Because capacities required for the entry into the German market are still short, the newly amended gas network access regulation limits the term of contracts: 65 per cent of the total capacities may be committed over a period of more than four years, and another 20 per cent for a maximal period of two years. However, existing contracts are not affected by these rules. Probably this issue will be addressed separately within the framework of the upcoming amendment of the Energy Industry Act. Capacities will be auctioned off, especially in order to strengthen the wholesale market, as of 1 October 2011.

Access to storage facilities is still subject to negotiated third-party access. With the new EU regulation on grid access (implemented by the Third Energy Package), which came into force in March 2011, the ERGEG Guidelines of Good Practice for Storage System Operators will become law.

10 Can customers, other natural gas suppliers or an authority require a pipeline or storage facilities owner or operator to expand its facilities to accommodate new customers? If so, who bears the costs of interconnection or expansion?

There is no right to demand expansion of existing facilities. However, as a general principle, the Energy Industry Act asks the network operators to keep a system in place capable of satisfying demand for transportation capacity, and thus they must expand capacity if it is economically reasonable. For determining capacity requirements, the transport system operators started to run 'open season' proceedings which have to meet certain requirements. Bundesnetzagentur is reluctant to grant exceptions to free network access under open seasons proceedings if off-takes within Germany are at issue.

Such costs have to be borne by all network users as the system operators are basically allowed to consider their expansion costs within the network access tariffs. Under the regime of regulation by incentives, distribution system operators are required to cover these costs by a blanket supplement to their revenues. Transmission system operators may apply for an additional budget. These issues are, however, highly disputed at present and the courts will have the final word. To a certain extent, network operators may ask for remuneration of the expansion costs from the person asking for interconnection. In contrast, the costs of connection to a network system have to be borne by the person asking for interconnection.

11 Describe any statutory and regulatory requirements applicable to the processing of natural gas to extract liquids and to prepare it for pipeline transportation.

No specific regulation exists. However, in accordance with general administrative law the Energy Industry Act demands facilities to be constructed and operated in a technically safe way, complying with general technical standards. These are presumed if the technical instructions and standards of the German Gas and Water Trade Association (Deutsche Vereinigung des Gas- und Wasserfaches eV) are met.

12 Describe the contractual regime for transportation and storage.

The Energy Industry Act stipulates the two-contract model (see question 9). Balancing services are provided by the market area coordinator with whom every shipper has to conclude a balancing agreement or has at least to assign a responsible balancing circle operator for their supplies by contract. The market area coordinator allocates the feed-in and off-take at the assigned entry and exit points and provides balancing services as needed. Within each market area, trading of gas between different balancing groups at a virtual hub is possible.

The relation between the network operator and the customer is addressed separately in connection agreements and in an agreement about the use of the connection facility.

Storage contracts are concluded on the basis of published standard terms and conditions.

Regulation of natural gas distribution

13 Describe in general the ownership of natural gas distribution networks.

The organisational structure for the local distribution of gas is highly fragmented. Approximately 700 different distribution system operators do exist, mainly private companies. If private utilities are owned by local municipalities, these companies are subject to public procurement law. Many municipalities aim to repurchase shares of ‘their’ local supplier or even establish a new city-owned supplier (eg, the City of Hamburg has done so).

Vertically integrated utilities with at least 100,000 customers must have their network operations from other activities unbundled as of 1 July 2007. The unbundling of information and the unbundling of accounts applies without any exemption to all gas distribution utilities.

14 Describe the statutory and regulatory structure and authorisations required to operate a distribution network. To what extent are gas distribution utilities subject to public service obligations?

Distribution network operators need approval before commencing operation (see question 7). Besides, general administrative law and all other legal requirements for undertakings have to be observed.

The distribution network operator must legally connect everyone to its low-pressure network system and thus has to maintain an appropriate and capable system to the extent that connection to the network is economically reasonable. The utility supplying the most customers connected to a distribution network has to offer basic supply tariffs applying to customers that receive gas without any specific contract.

15 How is access to the natural gas distribution grid organised? Describe any regulation of the prices for distribution services. In which circumstances can a rate or term of service be changed?

Because of the two-contract model (see question 9), the provisions for network access to transportation systems do not differ substantially from the access regime to distribution networks. The organisation of grid access is basically the same (see question 9). If a gas supplier wins a new customer, however, the new supplier may obtain the necessary off-take capacity assigned to this customer at the distribution level (the rucksack principle). The procedure of changing supplier is standardised by the regulatory authority and is therefore automated.

Distribution network access tariffs had been subject to regulatory approval based on incurred cost. From 1 January 2009 onwards, a complex system of incentive regulation provides for grid fees based on cost benchmarks. The initial regulation period lasts four years and thus ends in 2012. Any following regulation period will last five years. A subsequent change of tariffs within a regulation period is limited to statutorily defined conditions, eg, a change of tariffs owing to an approved change of fees in the upstream network.

16 May the regulator require a distributor to expand its system to accommodate new customers? May the regulator require the distributor to limit service to existing customers so that new customers can be served?

Basically, the regulator may not require a distributor to expand its system or to limit service to existing customers in favour of new entrants. The Energy Industry Act requires connection to the grid and expansion of the grid on adequate and non-discriminatory conditions. Nevertheless, the distributor must connect new customers to its system (see questions 10 and 14). Refusal is permissible only if connection or expansion would be economically unreasonable.

17 Describe the contractual regime in relation to natural gas distribution.

Applying the two-contract model there is no distinction between the contractual model of grid access to distribution networks and the gas transportation regime (see question 12).

In addition, operating a local distribution network that supplies connected consumers requires the contractual right to use the municipal property, for which the distribution system operator has to pay concession fees to the municipality.

Regulation of natural gas sales and trading

18 What is the ownership and organisational structure for the supply and trading of natural gas?

Supply of natural gas to households is mainly performed by regional suppliers, which compete to a certain extent, and also by a few larger utilities. Industrial end-users are also supplied by regional supply companies, and by supply companies on the transport and on the import level as well. Recently, a growing number of new market entrants, domestic as well as from abroad, have started to supply industrial customers as well as utilities. Gas trading in Germany is effected as over-the-counter trades between two parties and through the German Energy Exchange EEX. In the aftermath of the financial crisis, a surplus of gas in the wholesale market has led to significantly lower prices. As an effect, the still prevailing gas-oil price link has come under pressure.

19 To what extent are natural gas supply and trading activities subject to government oversight?

Gas suppliers must notify the regulator if they are supplying gas to household customers. The Energy Industry Act also requires gas suppliers to observe minimum standards for supply contracts with household customers even if they are not supplied under the basic supplier system. Gas prices are not subject to regulation but to review by the respective cartel authorities. Gas trading activities, especially if they are financially settled, may require an approval under the German Banking Act. Financial market regulation on the EU level is currently under review and may apply to gas trading.

20 How are physical and financial trades of natural gas typically completed?

Physical trades of natural gas are typically completed by an individual delivery contract. For wholesale trades most parties will use the EFET agreement. Financially settled trades are not so common in Germany. Also the gas exchange offers physically settled futures and spot trading. If financially settled contracts are to be concluded, the German master agreement or the ISDA agreement may be used.

21 Must wholesale and retail buyers of natural gas purchase a bundled product from a single provider? If not, describe the range of services and products that customers can procure from competing providers.

Wholesale and retail buyers, namely supply companies at the import or regional or local distribution level, are free to source natural gas from different suppliers and to conclude separate contracts for supply and transportation.

Regulation of LNG

22 What is the ownership and organisational structure for LNG, including liquefaction and export facilities and receiving and regasification facilities?

For the time being, there is no LNG terminal in Germany. In 2005, E.ON Ruhrgas planned an LNG terminal in Wilhelmshaven for regasification with an annual capacity of 10 billion cubic metres; however, it stated that there were not enough shippers interested to book firm capacities, abandoning the project to develop an LNG facility in Rotterdam instead.

23 Describe the regulatory framework and any relevant authorisations required to build and operate LNG facilities.

The building and operating of LNG facilities requires an approval according to general administrative law from the respective authorities including pollution control, environmental protection, planning and building regulations. There is no separate permission required under energy law for LNG facilities.

24 Describe any regulation of the prices and terms of service in the LNG sector.

If existing, an LNG facility in Germany would probably be considered as being an essential facility.

Mergers and competition

25 Which government body may prevent or punish anti-competitive or manipulative practices in the natural gas sector?

Anti-competitive practices in the supply of natural gas are subject to German cartel law. Therefore, the Federal Cartel Office or, if the anti-competitive behaviour is limited to a region, the respective cartel offices at the regional state level, are responsible for foreclosure. As far as anti-competitive behaviour is related to network access, Bundesnetzagentur or its regional counterparts are exclusively responsible.

26 What substantive standards does that government body apply to determine whether conduct is anti-competitive or manipulative?

The Federal Cartel Office or other cartel offices apply the standards of German as well as European cartel law. In 2007, a new article was introduced in the German cartel law to ease proceedings of the cartel offices against abusive behaviour in the energy sector; subsequently, numerous cases have been initiated and all cases of the Federal Cartel Office have been settled. This new article is applicable only until 31 December 2012. Bundesnetzagentur and its regional counterparts apply the Energy Industry Act, which sets forth a standard that is similar to the standards of cartel law. Also, compliance with the federal regulations on network access and tariffs is required.

27 What authority does the government body have to preclude or remedy anti-competitive or manipulative practices?

It is at the discretion of the competent cartel offices to open a proceeding and start investigations. If the authority finds the gas utility abusing its dominant position, it can issue a cease-and-desist order. It may also impose a fine for certain infringements.

In general, the same applies for the Energy Industry Act and the authority of the regulator. Besides their ex-ante activities, they supervise adequate and non-discriminatory network access on an ex-post basis. Further, the Energy Industry Act provides a specific proceeding that generally must be completed within two months of a complaint.

28 Does any government body have authority to approve or disapprove mergers or other changes in control over businesses in the sector or acquisition of production, transportation or distribution assets?

German merger control is applied by the Federal Cartel Office. If the conditions of the European Merger Control Regulation are met, European merger control is exercised by the EU Commission. No sector-specific provisions exist. According to German law, a merger must be notified prior to execution if the combined worldwide turnover of the companies involved exceeds 500 million and if at least one of the concerned companies has a turnover exceeding 25 million within Germany. Moreover, merger control is not applicable if the conditions of a statutory de minimis rule are met.

The Federal Cartel Office must decide within one month of submission of a complete notification whether a detailed investigation is necessary because of competition concerns. If so, the Federal Cartel Office must decide within another four months about its further findings. Extensions are possible.

29 In the purchase of a regulated gas utility, are there any restrictions on the inclusion of the purchase cost in the price of services?

Purchase investments are not susceptible to be recognised as costs for network access tariff regulation purposes. Return on equity for new investments is capped at 9.29 per cent before tax and 7.56 per cent before tax for existing facilities.

30 Are there any restrictions on the acquisition of shares in gas utilities? Do any corporate governance regulations or rules regarding the transfer of assets apply to gas utilities?

No sector-specific rules apply.

Update and trends

The four market areas will be reduced to two in 2013.
Gas transportation capacities will be auctioned off and capacity agreements will be limited in duration.

International

31 Are there any special requirements or limitations on foreign companies acquiring interests in any part of the natural gas sector?

The general legal framework applies to them as well as to any domestic company. However, the German parliament has adopted an amendment to the Foreign Trade Act that allows for the government to interdict acquisitions by non-EU investors if they endanger public safety.

32 To what extent is regulatory policy affected by treaties or other multinational agreements?

EU legislation was decisive for the recent developments in the natural gas sector, since the whole regulatory system is based upon EU directives. Beyond these structural aspects, coordination takes place on a regulatory level, for example at the Madrid Forum. The EU has implemented a Third Energy Package in 2009. The implementation in Germany is not expected before autumn 2011 and may be delayed until 2012.

33 What rules apply to cross-border sales or deliveries of natural gas?

The Energy Industry Act provides for a comprehensive framework for gas trade to be as liberalised as possible. Cross-border network access is subject to EC Regulation 1775/2005. This regulation ensures non-discriminatory network access.

Transactions between affiliates

34 What restrictions exist on transactions between a natural gas utility and its affiliates?

Because of the obligatory unbundling of information, a network operator must preserve commercially sensible information even within its own, associated or affiliated companies. Even if not subjected to unbundling in functional terms because of the statutory exemption (see question 13), this provision must be considered in any transactions with affiliates. Besides, every transaction must be carried out in a non-discriminatory manner.

35 Who enforces the affiliate restrictions and what are the sanctions for non-compliance?

The monitoring of the unbundling regime as well as the enforcement of non-discrimination is performed by the regulatory authorities. For violations of the unbundling regime, the regulatory authorities are able to issue an administrative injunction. If the injunction is not observed, the company will be fined. Furthermore, the regulatory authorities enforce proceedings against abusive behaviour. Moreover, the Energy Industry Act sets forth an additional application procedure, and non-compliance may be challenged before civil courts.

SCHOLTKA & PARTNER
Rechtsanwälte

Solveig Hinsch	**hinsch@scholtka-partner.de**
Boris Scholtka	**scholtka@scholtka-partner.de**
Guido Brucker	**brucker@scholtka-partner.de**

Meinekestraße 4
10719 Berlin
Germany

Tel: +49 30 50 96 95 0
Fax: +49 30 50 96 95 77
www.scholtka-partner.de

ISSN 1740-7826