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COMMENTS ON NATURAL GAS MARKET CONCEPT DESIGN

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DATA

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ACRONYMS

EFET	European Federation of Energy Traders
MoESD	Ministry of Economy and Sustainable Development of Georgia
GoG	Government of Georgia
GOGC	Georgian Oil and Gas Corporation
ITO	Independent Transmission Operator
SSO	Storage System Operator
UGS	Underground Gas Storage
USAID	United States Agency for International Development
VTP	Virtual Trading Point

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INTRODUCTION

A Natural Gas Market Concept Design shall set out conceptual directions and principles of the natural gas market development to further facilitate sector improvements and enhance market security, efficiency and competition.

The way the Natural Gas Market Concept Design (Concept Design) is drafted and structured, USAID Energy Program thinks the document by its nature is vague and does not really provide the necessary structure and “legal and organizational preconditions” of the Natural Gas Market of Georgia as defined under Chapter I. In addition, USAID Energy Program realizes the unique characteristic of any natural gas market and finds the current Concept Design not tailored to the Natural gas market of Georgia and its further development.

USAID Energy Program has reviewed the Natural Gas Market Concept Design drafted by the Energy Secretariat and provides the bellow organized comments.

MAIN IDENTIFIED ISSUES

1. Under the draft Law, after its adoption, the Concept Design shall be adopted by the Government of Georgia (GoG) for “general guidance for the organisation and functioning of the natural gas market in Georgia. The general guidance shall define the structure of the natural gas market and shall provide general outline of the rights and obligations of market participants to extent where it is essential to define the general essence of the market structure”. Such general guidance for the defined sector is determined under a primary legislation and serves as the basis for specific sector related laws. The Energy Law defines the organization of the market, functions of the entities and related obligatory provisions. Therefore, the necessity and the role of adopting Concept Design for the natural gas market in Georgia is not well justified.
2. Repetition with slight changes in methodology (as provided in the table below): Much of the first section of the Concept Design (Articles 1, 2, 4, 5, and 6) is repetition of language from the Draft Energy Law and from the Grid Code, with some significant changes in terminology. Article 6 of the Concept Design changes the description of the components of the wholesale natural gas market used in Article 136.3 of the Draft Energy Law by substituting the term "organized natural gas market" for the term "day-ahead natural gas market." The Draft Energy Law mentions a gas exchange, in Article 25, which deals with regional and international cooperation. Since the Draft Energy Law is undergoing amendments, this clarification should be made in the Law to avoid confusion.
3. Contrary to Market-Based Principles: Language in the Concept Design appears contradictory to the market-based principles. For example, the convoluted description of market-based trade in Article 18.3 says that all conditions in natural gas sale and purchase contracts are to be freely negotiated "except in the case and to the extent where mandatory requirements for the form *and or content of the contract are stipulated in the Market Rules.*" But the Concept Design itself does not mandate any form or content so leaves open what mandatory terms will be required, essentially vitiating the whole idea of freely negotiated agreements. Similarly, Article 18.4 says long term contracts are not be prevented "in so far as such contracts *comply with the competition rules stipulated in applicable laws as required by Energy Community Law.*" Again there is no reference to specific prohibitions which makes it impossible to know what will be banned and when; effectively casting such uncertainties on long term contracts that might be prohibited.
4. The Concept Design does not provide the Unbundling of network activities as a main component of the natural gas market development and part of the market concept.
5. The Concept Design does not outline the Underground Gas Storage (UGS) facility as part of the considered design.
6. The Concept Design does not include the creation of the Storage System Operator (SSO) as well.
7. The Concept Design considers “the day-ahead natural gas market (natural gas exchange) and the organized natural gas balancing and ancillary services market, *i.e.* not later than by 1 January 2023”. The Concept Design rather outlines all possible markets that can be implemented starting from the so-called day-ahead, then defining a clear guidance for opening and structuring the sector.
8. The Concept Design goes beyond the confines of the Draft Energy Law and makes substantive changes which need to be reflected in the Law. Some examples: (1) New definitions that create new concepts not mentioned in the Law; (2) Including a “Mandatory sale” in the Concept Design should also consider such provision included in the Energy Law; (this may be a reasonable proposal to introduce liquidity into the exchange but it is not based on the Law and may violate sanctity of contracts since several agreements between Gazprom and Georgian Oil and Gas Corporation (GOGC) extend beyond 2023); (3) Article 21.2 of the Concept Design stipulates that the day ahead market will be organized by the "natural gas market operator"; Article 50.2(6) of the Law makes the Independent Transmission Operator (ITO) responsible for setting up the trading platform.
9. The Concept Design lacks clarity: (i) There are numerous references to "transitory period" but no definition of this period, either when it starts or when it ends. There are many different dates in the Law for implementing provisions related to gas (Articles 172, 175, 181) and it is unclear to which of these the term "transitory period" applies; (2) Article 7.2 refers to "special regulatory regime" which

is a term not defined and not used anywhere in the Law; (3) Article 12.5 uses the term "special purpose public service obligation" which is not defined and not used in the Law.

10. The Concept Design fails to address the items listed in Article 139 of the Draft Energy Law (such as specifying the products to be sold in the gas market/gas exchange).
11. In addition, the Concept Design repeatedly states a "competitive" natural gas market and does not really provide any clear definition of such for Georgia's natural gas market, taking into account the existing exemptions associated with the cross-border pipelines.
12. Furthermore, the bellow table considers additional comments of USAID Energy Program in relation to various articles of the Concept Design.

COMMENTS ON NATURAL GAS MARKET CONCEPT DESIGN

Text of Concept Design	Suggested modification or comment
<p>Article 27. Procurement of gas for balancing and operational gas Balancing group responsible parties, before establishment of the natural gas exchange, shall strive to sell or procure natural gas based on bilateral contractual relations with other natural gas market participants as necessary to avoid or minimise imbalances in their natural gas portfolio. Sale and purchase of natural gas for this purpose shall be carried out in line with Articles 15–19 hereof.</p>	<p>Missing definition of balancing group responsible parties Under “Use of terms”.</p>
<p>Article 3. Use of terms “trading platform” shall mean a natural gas exchange or another virtual place, as referred to in this Market Design, established for trade in natural gas or natural gas derivatives which is administered by a designated operator in accordance with applicable legal acts.</p>	<p>A trading platform is a place for physical and/or financial natural gas transactions. It should not be identified as “another virtual place or a natural gas exchange”.</p>
<p>Article 3. Use of terms “Virtual Trading Point” (VTP) shall mean a virtual point in the domestic natural gas transmission system of Georgia, as determined under the Natural Gas Transmission Network Code, at which the trade in natural gas takes effect on the wholesale natural gas market and which is the single point for all transfers of natural gas ownership in the Georgian balancing zone.</p>	<p>The Network Code defines “Virtual Delivery Point” instead of “VTP”. As such defined, the VTP shall be a point (not virtual but rather virtual balancing) in the transmission system.</p>
<p>Article 24. Mandatory sale of imported natural gas 1. In order to enhance the competition in and liquidity of the natural gas market, natural gas imported and injected to the domestic natural gas system of Georgia shall be mandatorily sold on the natural gas exchange in the following percentage: a) from [1 January 2023] not less than [50%] of imported and injected natural gas; b) from [1 January 2024] not less than [75%] of imported and injected natural gas; and c) from [1 January 2025] not less than [100%] of imported and injected natural gas.</p>	<p>The Concept Design defines the so-called “Mandatory sale” which is in fact already well-established terminology and program by European Federation of Energy Traders (EFET): Gas release program. These items are not described in the Draft Energy Law but only in the Concept Design.</p>
<p>Article 24. Mandatory sale of imported natural gas Natural gas market participants may be exempted from the obligation for mandatory sale of imported natural gas on the natural gas exchange only in case and to the extent where such exemption is granted by the GoG as justified as a public service obligation in accordance with the Law of Georgia “On Energy”. In any case, such exemption may apply for not more than [33%] of natural gas imported to Georgia on quarterly basis.</p>	<p>Undefined justification for the exemption.</p>
<p>Page 13 footnote: the day-ahead natural gas market (natural gas exchange)</p>	<p>A natural gas exchange can include various contracts with duration from within day, through day-ahead and up to years. It is not correct to use the term “natural gas exchange” as substitute for day-ahead market.</p>
<p>Chapter VI. Day-ahead natural gas market</p>	<p>The best international practices consider natural gas hubs/exchanges, with offered trades and duration of contracts as general organization of the market. Day-ahead is type of duration of contracts along with week-ahead, month ahead, etc. Text on day-ahead market defines a market within the day-ahead only. In the natural gas sector this is misleading and not well-defined term.</p>
<p>Article 24. Mandatory sale of imported natural gas Mandatory sale of imported natural gas on the natural gas exchange shall be organised, monitored and reported to the Commission and to the Ministry of Economy and Sustainable</p>	<p>The role of the MoESD is not clear in the mandatory sale process of imported gas.</p>

<p>Development of Georgia (MoESD) by the natural gas market operator under the terms and conditions stipulated in the Market Rules.</p>	
<p>Article 24. Mandatory sale of imported natural gas Requirements for mandatory sale of imported natural gas on the natural gas exchange shall also apply for natural gas volumes injected to the natural gas storage facility which are further on withdrawn and used for sale in Georgia</p>	<p>Natural gas stored for security of supply reasons may not be required for the so-called mandatory sale.</p>
<p>Article 28. Organised natural gas balancing and ancillary services market System operators shall have no functions with regard to the operation and/or administration of the organised natural gas balancing and ancillary services and shall be deemed as participants thereof within the scope defined in the Market Rules. The system operator may not engage in any other natural gas market or trading activity.</p>	<p>Under Article 28, the provision states: "Terms and conditions for trade by system operators on the organised natural gas balancing and ancillary services market shall be regulated." This is in contradiction with this provision.</p>
<p>Article 28. Organised natural gas balancing and ancillary services market System operators shall be eligible to procure gas for balancing and operational gas on the organised natural gas balancing and ancillary services market as necessary to perform their respective transmission and/or distribution related functions. This shall be without prejudice to the right of the transmission system operator to procure gas for balancing based on bilateral contracts pursuant to Article 27 hereof in cases where short-term standardised products on the organised natural gas balancing and ancillary services market will not or are not likely to provide the response necessary to keep the transmission network within its operational limits or in the absence of liquidity of trade on the organised natural gas balancing and ancillary services market. Terms and conditions for trade by system operators on the organised natural gas balancing and ancillary services market shall be regulated by the applicable Network Code and the Market Rules.</p>	<p>This item should be revised and re-written for better understanding.</p>

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