

Roadmap on regional gas market integration between Estonia, Finland, Latvia and Lithuania

20 April 2020

INTRODUCTION

The Regional Gas Market integration process started as a political process in which the Baltic States' Prime Ministers endorsed, in December 2015 in Riga, the Regional Gas Market Development Action Plan and invited Finland to take part in this process. The objective is to establish a merged, regional gas market in Estonia, Finland, Latvia and Lithuania, encompassing all four Member States, with the objective to improve market liquidity, integration and competition, ensuring affordable gas prices and high quality service, thus being attractive for existing and new market participants. In its' National Energy and Climate Strategy of 2016 the Government of Finland also endorsed an objective for the Finnish energy policy to create a common regional gas market with the Baltic States.

Market integration is an opportunity for the Baltic States and Finland to make the best use of the existing and future infrastructure such as gas storage facilities, LNG terminals, the Balticconnector and the Gas Interconnection Poland–Lithuania (GIPL). It is also a chance to increase competition to the benefit of the end-consumers in the region by attracting suppliers which otherwise will not come as the separate markets are relatively small.

The Baltic Energy Market Interconnection Plan (BEMIP) Action Plan includes a precise task for the preparation of a regional gas market model in the Baltic States and interconnected gas market with Finland. With the establishment of the Regional Gas Market Coordination Group¹ (RGMCG) to facilitate the development of the functioning regional gas market in the East Baltic region the countries have committed to jointly cooperate moving towards development of a regional gas market.

This is the general political will, expressed by all transmission system operators (TSOs), national regulatory authorities (NRAs) and Ministries (thereafter: parties) of all four countries. The commitment towards the successful realisation and functioning of the market merger for all the four Member States was reconfirmed at the BEMIP High Level Group plenary meeting.

STATE OF PLAY AND GENERAL PRINCIPLES

During 2018, a lot of effort was put for the development of a tariff model and inter-TSO compensation (ITC) mechanism for the common Baltic-Finnish market, resulting in stepwise integration approach agreed by RGMCG. In October 2018 three TSOs (Latvian, Estonian and Finnish) signed a Memorandum of Understanding (MoU) which sets out the principles of an ITC mechanism and establishment of single balancing zone and other principles relating to TSO cooperation. The TSOs of Finland, Estonia and Latvia (FinEstLat) signed the ITC mechanism agreement on the 14 February 2019.

¹ https://www.acer.europa.eu/en/Gas/Regional_%20Initiatives/Pages/BALTIC-RGMCG.aspx

In turn, NRAs of Finland, Estonia and Latvia (FinEstLat) on November 14, 2018 signed the MoU to facilitate cooperation and coordination between the NRAs in order to create in good time the FinEstLat market which provides for the possibility for other NRAs to join as well as agreed on a single entry-exit system encompassing all the participating states and establishing the same entry tariff on each entry point to the single entry-exit system. Further, Estonia and Latvia – from the beginning of 2020, have formed a common balancing zone. Finland remains as a separate balancing area but is a part of the common entry tariff area with Estonia and Latvia. The Lithuanian TSO, despite their active participation in market merger planning and ITC mechanism discussions did not sign the MoU nor the ITC mechanism agreement due to a lack of agreement on the compensation mechanism between the TSOs. Thus, Lithuania remains as a fully separate entry-exit system.

Since the conclusion of the ITC mechanism agreement, all parties from the four countries together with the Commission, have worked closely to find a solution which would enable the creation of a common regional gas market consisting of all four Member States.

The present contribution sets out a process with concrete milestones to be achieved in order to pave the way to the regional gas market integration model agreeable to all the four Member States and potentially open to other Member States to join.

The attempts to create a common regional gas market (so-called “gas market merger”) are of a pioneering nature and may result to a first four-country wide cross-border gas market merger in the EU.

However, the deeper the level of integration sought, the more attention should be paid to a regionally effective market design and the level of harmonisation required to deliver this. In order to steer this integration process, this Roadmap defines the general principles of the future regional gas market merger between four countries as follows. A regional gas market merger or any other, intermediate, form of regional integration of the gas markets shall fulfil *inter alia* the following general principles:

- be beneficial for the liquidity of the (merged) market;
- be as transparent as possible ensuring that all relevant parties have access to the information relevant for them (aggregating confidential information if need be, in agreement with the market participants);
- contribute to the security of supply in the region and be compliant with the relevant provisions of the EU law²;
- be based on necessary analysis of impacts as described below in the Action Plan;
- be broadly consulted with both market participants and adjacent Member States;
- should not adversely affect cross-border gas flows and trade with the adjacent Member States. To this extent firm cross-border capacity shall not significantly fall and the entry tariff to the merged market and exit tariff from the merged market shall not significantly increase;
- be in line with EU law;

² See for instance article 6 of Gas SoS Regulation 2017/1938 (the so-called “supply standard”, which concerns the obligation to ensure the supply of gas to the protected customers under a set of demanding conditions).

- be economically beneficial for all participating Member States.

The Commission and possibly Agency for the Cooperation of Energy Regulators (ACER) could participate in the work on a case-by-case basis. The Commission could bring an external view and facilitate the implementation of solutions. Similarly, the Commission could, by following carefully the gas markets integration process of the Baltic States and Finland (merger project) advances, identify the areas that could later constitute as building blocks for similar arrangements in other areas.

MERGER PROJECT ACTION PLAN AND TIMELINE

Key actions taken towards a market integration between the Baltic States and Finland include the following work streams and key milestones:

Action	Schedule	Responsibility
1. TARIFFS AND 4-COUNTRY ITC MECHANISM - TOWARDS A JOINT TARIFF AREA BETWEEN ESTONIA, FINLAND, LATVIA AND LITHUANIA		Coordination: RGMCG with assistance by the Commission and ACER if needed
External analysis (contractor) to support ITC-design and coordinated position on tariffs ³ : <ul style="list-style-type: none"> - Analysis of impacts on removal of entry and exit tariffs on the Latvia-Lithuania border and on the wholesale market: impacts on the wholesale gas prices (including related impact on end-consumers), trading efficiency and market participants businesses and any other relevant wholesale market metrics in, Estonia, Finland, Latvia and Lithuania - Analysis of entry-points tariff harmonization and effects of possible discounts at entry points from EU Member States (LNG, GIPL) 	Q1-Q2/2020	All TSO (Scope approved by all RGMCG members)
Design of an ITC mechanism solution	Q3/2020	All TSOs
Public consultation of ITC mechanism solution	Q4/2020	NRAs and Ministries (subject to national legislation)
Joint position on ITC mechanism solution and tariff setting principles	Q4/2020 – Q1/2021	NRAs joint decision; to be followed by the national decision of each

³ Quantification, including methodology where applicable, and monetisation of these effects should be reflected. The currency used should be EURO.

			NRA implementing joint decision, if necessary. This might be merged into one decision together with joint decision on tariff setting principles.
	ITC mechanism agreement	Q4/2020 - Q1/2021	All TSOs
	Consultation of the proposed tariff methodology and tariffs based on TAR NC	Q1/2021	NRAs
	ACER's opinion on tariff methodology based on TAR NC	Q2/2021	ACER
	Approval of tariff methodology	Q4/2021	NRAs
	Harmonised Tariff Applications for 2022	Q1/2022	All TSOs (to NRAs)
	Approval of tariffs for 2022	Q2/2022	NRAs joint decision; to be followed by national decision implementing joint decision, if necessary. Joint decision may reflect the differences in the national tariffs if this is the outcome of the tariff discussions.
	Tariff area FIN-EST-LAT-LIT in operation	2022 (precise date depending on the chosen tariff period) ⁴	TSOs and NRAs
	2. FURTHER INTEGRATION: TOWARDS DEEPER MARKET INTEGRATION BETWEEN ESTONIA, FINLAND, LATVIA AND LITHUANIA		Coordination: RGMCG with assistance by the Commission and ACER if needed
	Experience sharing on the functioning of ESTLAT common balancing zone and Balticconnector commissioning	Q1-Q3/2020	TSOs and NRAs

⁴ Based on TAR NC tariffs shall be published one month before the yearly auction.

<p>Operational balancing regime analysis, including, but not limited to⁵ :</p> <ul style="list-style-type: none"> - Investigating potential bottlenecks on Kiemenai interconnection point on Lithuanian-Latvian border and the effects of the additional capacity constraints in setting up a common balancing zone - Investigating potential bottlenecks on Balticconnector interconnection point and the effects of the additional capacity constraints in setting up a common balancing zone 	Q2-Q3/2020	Scope to be approved by all RGMCG members
IT-systems and commercial operating models common balancing zone: key options identified	Q2-Q3/2020	RGMCG
Common network and balancing rules: key open issues identified	Q3/2020	RGMCG
<p>Design of scenarios and analysis for further integration options:</p> <ul style="list-style-type: none"> - Scen. 1. Joint tariff and balancing zone FIN-EST-LAT- LIT 2022 - Scen. 2. Joint tariff and balancing zone FIN-EST-LAT 2022 - Scen 3. Joint Tariff area FIN-EST-LAT-LIT 2022, joint balancing area FIN-EST-LAT 2022 as an intermediary towards joint balancing for FIN-EST-LAT-LIT in 2024 after ELLI project completion - Scen 4. Joint Tariff area FIN-EST-LAT-LIT 2022, joint balancing for FIN-EST-LAT-LIT in 2024 after ELLI project completion without Finland joining the balancing area in 2022 - Scen 5. Possible other identified in process of analysis and based on ITC-negotiations 	Q1-Q3/2020	RGMCG
Proposal on the way forward on integration model based on analysis	Q3-Q4/2020	RGMCG
<p>3. UPDATE OF THE ROADMAP FOR THE NEXT STEPS OF INTEGRATION (BASED ON THE INTEGRATION MODEL CHOSEN AND RESULTS OF ITC-NEGOTIATIONS) AND GOVERNANCE OF THE INTEGRATED MARKET:</p> <ul style="list-style-type: none"> - updated Roadmap - regulatory oversight of the merged/integrated market (NRAs market oversight and decisions, 	Q4/2020-Q1/2021	Proposed by RGMCG to BEMIP Senior Officials level for endorsement with the assistance by the Commission and ACER if needed

⁵ Quantification, including methodology where applicable, and monetisation of these effects should be reflected. The currency used should be EURO.

market-based balancing and capacity contracts arrangements)		
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GOVERNANCE

The merger project is coordinated by RGMCG and managed by mutual agreement of the four TSOs/ key gas infrastructure operators, NRAs and Ministries. RGMCG consists a representation of NRAs, Ministries and TSOs/key gas infrastructure operators.

The RGMCG will report to the BEMIP Senior Officials level on progress following the above action plan and request its involvement while the consensus cannot be reached on the RGMCG level. BEMIP Senior Officials meeting, for the purpose of this Roadmap, consists of Senior Officials from NRAs, Ministries and TSOs/key gas infrastructure operators from Estonia, Finland, Latvia and Lithuania. The Commission acts as a facilitator. ACER may be invited to join when necessary.

The decision on the way forward of the integration model shall be endorsed at the political level (BEMIP Senior Officials) based on a RGMCG proposal assuming that it will be an agreement reached among all parties on the ITC mechanism.

The RGMCG shall present a proposal for a market integration model including the milestones and the updated version of this Roadmap. The milestones should be detailed, and express relevant measures taken in relation to capacity contracts, market-based balancing and wholesale market integration. Necessary decisions shall be taken in consensus by all parties. In case of disagreement or difficulties, the diverging views shall be noted. This Roadmap shall be updated along the entire regional integration process, if needed, towards the final regional set-up.

The proposal towards the regional market integration will need to ensure the effective regulatory oversight and specify the necessary legally binding decisions to be taken by the NRAs and the governments and a timing for these decisions. In particular it will specify the instances where the NRAs will be taking joint opinions or decisions. It should also specify the necessary changes in the legislation in the four Member States. The Commission should be involved in particular to ensure maximisation of cross-border trade and to address the potential negative impacts on the adjacent Member States, if any.