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COMMISSION OPINION

of 17.10.2014

**correcting Opinion C(2014) 5483 final of 28 July 2014 pursuant to Article 3(1) of
Regulation (EC) No 715/2009 and Article 10(6) and 11(6) of
Directive 2009/73/EC - Greece - Certification of DESFA**

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I. PROCEDURE

On 29 May 2014 the Commission received a notification from the Greek national regulatory authority, RAE, of a draft decision on the certification of the Hellenic Gas Transmission System Operator S.A. (hereafter, "DESFA").

Pursuant to Article 10 and 11 Directive 2009/73/EC¹ (hereafter "Gas Directive") and Article 3 Regulation (EC) No 715/2009² (hereafter "Gas Regulation") the Commission is required to examine the notified draft decision and deliver an opinion to the relevant national regulatory authority.

On 28 July 2014 the Commission adopted its opinion.³ This correcting opinion corrects the opinion of 28 July 2014 which, due to a procedural error, contained non-final drafting in a limited number of paragraphs. Since none of the corrections affect the initial opinion in a substantive manner, the correcting opinion has retroactive effect in amending the opinion of 28 July 2014 which will continue to apply as of that date.

II. DESCRIPTION OF THE NOTIFIED DRAFT DECISION

DESFA is the only gas transmission system operator for gas in Greece. It owns and operates the national natural gas transmission system, including its interconnections with Turkey and Bulgaria, and the LNG terminal at Revithoussa. DESFA was established in 2007 as a subsidiary of the state-controlled vertically integrated gas undertaking DEPA S.A. (hereafter, "DEPA").

In the context of the restructuring plan for Greece, the Hellenic Republic Asset Development Fund (hereafter, "HRADF") commenced, in February 2012, a privatization process for the DEPA group. HRADF retained the State Oil Company of the Azerbaijan Republic (hereafter, "SOCAR"), an undertaking established in Azerbaijan and controlled by the Republic of Azerbaijan as the preferred bidder for DESFA. SOCAR will acquire 66% and thereby sole control of DESFA subsequent to the closing of the share purchase agreement ("SPA"). The remaining 34% will continue to be held by the Hellenic Republic.

On 9 December 2013, RAE was officially informed by DESFA of the imminent change in control. In January 2014 DESFA submitted to RAE its application, which was later

¹ Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, OJ L 211/94 of 14.8.2009.

² Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005, OJ L 211/36 of 14.8.2009.

³ C(2014)5483 *final*

complemented with additional information, for certification under the Independent Transmission Operator model (hereafter, "ITO") justifying its compliance with the ITO-provisions and with the criteria related to Article 65 of the Greek Energy Law 4001/2011 which transposes Article 11 of the Gas Directive and which relates to the certification of TSOs controlled by a person from a third country.

RAE has analysed whether and to what extent DESFA complies with the unbundling rules of the ITO-model as well as with the criteria related to the certification of TSOs controlled by a person from a third country, as laid down in the Greek legislation transposing the Gas Directive. In its preliminary decision, RAE concludes that DESFA complies with these requirements and that certification can thus be granted. On this basis RAE submitted its preliminary decision on 29 May 2014 to the Commission requesting an opinion.

III. COMMENTS

On the basis of the present notification the Commission has the following comments on the draft decision.

1. The choice of the ITO-model

According to Article 9(8) Gas Directive, the ITO model may be applied in cases where, on 3 September 2009, the transmission system belonged to a vertically integrated undertaking (hereafter, "VIU"). The Commission agrees with RAE that in the present case the choice for the ITO model is legitimate, considering that the transmission system concerned did belong to a VIU on the relevant date.

Whereas DESFA, prior to its partial privatization, belonged to the vertically integrated undertaking DEPA, RAE has carried out an additional assessment to ensure not only the independence from its new controlling shareholder, SOCAR, but also from its previous owner. The assessment includes *inter alia* the independence of personnel and management, the separation of IT-systems and the sharing of premises. The Commission agrees with RAE that, given the important position of DEPA in the Greek gas market, the complete separation of DESFA from DEPA is an important element to ensure that DESFA can carry out its tasks independently from any supply or generation related interests.

2. Sufficient resources

According to Article 17(1)(b) and (c) Gas Directive the ITO shall employ all personnel necessary for the activity of gas transmission including tasks related to the operation, maintenance and development of the network and the performance of all corporate tasks. In addition, the TSO shall not be able to lease personnel or procure services from the vertically integrated undertaking.

In the context of RAE's preliminary assessment of the separation of DESFA from DEPA, a study has been carried out in 2013 - before the change of ownership - into the compliance of DESFA with the requirements of Article 17(1)(b) and (c) Gas Directive in which it was concluded that a relatively large proportion of the necessary human resources are ensured through outsourcing, including a number of critical positions in the TSO. The Commission notes that whilst the high degree of outsourcing may be explained in the specific context of the austerity measures related to state-owned undertakings in Greece, it is important in ensuring a high degree of independence, that following the change of control over DESFA the situation is corrected as soon as reasonably possible. The Commission recommends RAE to closely cooperate with DESFA and its owners to develop a plan aimed at reducing the leasing of personnel.

3. Services related to the Trans-Adriatic Pipeline

Article 17(1)(c) Gas Directive allows in specific circumstances for the provision of services by the ITO to other parts of the VIU, in particular if there is no discrimination of other system users, if there is no restriction of competition in production or supply and if the regulatory authority has approved the provision of the services concerned. In this context it is relevant to assess the services that DESFA intends to carry out for TAP AG, a consortium of companies promoting the Trans-Adriatic Pipeline (hereafter, "TAP") that will run through Greece bringing Azeri gas to the European market, but that will also connect DESFA's network to the Albanian and Italian grids and reinforce its interconnections with Turkey. DESFA has signed a cooperation agreement with TAP AG in which SOCAR is one of the participants, owning 20% of its shares.

In its preliminary decision, RAE argues that since SOCAR is not a controlling shareholder in TAP AG, the latter is not part of the VIU and that thus the cooperation agreement falls outside the scope of the certification procedure. Whilst the Commission agrees that it is not an obstacle for the certification of DESFA that the services concerned comply with the criteria of Article 17(1)(c) Gas Directive, the Commission nevertheless encourages RAE to ensure that DESFA, in carrying out the services for TAP AG both during and after the construction phase of the TAP, does not discriminate in favour of TAP AG and to the detriment of other network users. This could for instance take the form of prioritization of investments related to TAP or preferential financial treatment for TAP AG, which can be avoided by an appropriate degree of regulatory oversight.

4. Application of Article 11 – Certification in relation to third countries

Article 11 Gas Directive determines that where certification is requested by a TSO that is controlled by a person from a third country, the regulatory authority shall refuse certification if it has not been demonstrated that the entity concerned complies with the requirements of Article 9 and that the granting the certification would not put at risk the security of supply of the Member State and the Community. In considering the latter question, three relevant aspects need to be taken into account. Firstly, the rights and obligations of the Community vis-à-vis the third country arising under international law, including any agreement concluded with one or more third countries to which the Community is a party and which addresses the issues of security of supply. Secondly, the rights and obligations of the Member State with respect to that third country arising under agreements concluded with it, insofar as these are in compliance with Community law. And thirdly other specific facts and circumstances of the case and the third country concerned.

As SOCAR, with its participation of 66% of the shares will, after completion of the transaction, control DESFA, RAE has carried out this assessment.

RAE brings forward a number of arguments to underline its conclusion that SOCAR's control over DESFA does not put at risk the security of supply of Greece or the EU. The assessment relies strongly on the argument that the volumes of Azeri gas delivered to Greece and the EU are small, especially in comparison to Russian volumes. This argument is not fully convincing, given that the share of Azeri gas in the Greek market today already amounts to ~18% and that significant additional volumes might flow to Greece and the wider region in the near future, notably after the development of the Southern Corridor. The Commission is of the opinion that such volumes are not irrelevant from a security of supply perspective. The Commission also takes the view that the position of SOCAR not only in the future but already today is of significance to the assessment of Greece's and the wider region's security of supply situation, particularly in view of its participations in the Shah Deniz II field and in the TANAP pipeline. Furthermore the Commission observes that risks regarding security of

supply can also concern non-Azeri gas supplies, as SOCAR could use its control over DESFA's network to foreclose gas supplies from other sources.

A second pillar of RAE's assessment concerns the argument that an increase in Azeri gas supplies will actually improve the security of supply situation in Greece and the wider region given that it will reduce the dependence on gas from a single source, in this case, Russia. This assessment is correct and the Commission strongly supports the development of the Southern Gas Corridor. Under Article 11 Gas Directive however the question to be answered is whether the acquisition of control over DESFA by SOCAR raises security of supply concerns, against the background of Azeri gas supplies to Greece and the Community.

In that context, the Commission deems it necessary to take into account the strategic position and function of the DESFA network, which constitutes an entry gate of gas from multiple sources to Greece and the EU. It includes for the time being the sole entry point of Azeri gas to Greece and the EU. In the future, the role of the DESFA network for the transmission of gas from different, competing, sources to other EU Member States and Members of the Energy Community surrounding Greece will further increase when additional planned interconnections, for example with Bulgaria, are developed. In this respect, the DESFA network plays a strategic role for the security of supply to Greece and the EU. Precisely because of the presence of this variety of suppliers and the DESFA network's location on the crossing of various supply routes, it will be important to ensure that the fact that the network is in the hands of a vertically intergated state-owned company from a third country that is one of the main supply sources does not put at risk the independent operation of the transmission system and development of the network for all possible supply routes. The need to secure the independent operation and development of the DESFA network is further exacerbated by the fact that SOCAR has a participation in TAP, a planned pipeline that will be connected to the DESFA network.

RAE argues that the independent operation of DESFA is already sufficiently secured by the fact that DESFA complies with the EU unbundling framework, in casu with the regular ITO-rules. The Commission agrees that EU unbundling rules provide for a framework to prevent vertically integrated EU companies from abusing their control over the network to their own benefit. For instance, with regard to investments, RAE has the duty to require DESFA to carry out certain investments if these are not executed in line with the ten-year network development plan. RAE should in such case either require DESFA to execute the investment, organise a tender procedure open to any investor or oblige DESFA to accept a capital increase to finance the necessary investments (Article 22(7)(a to c) Gas Directive).

However, the Commission underlines that the EU legislator has clearly established the security of supply assessment in Article 11 as an *additional test* to that of Article 9 Gas Directive (unbundling rules). Recital (22) Gas Directive indicates that "[...] *Persons from third countries should [...] only be allowed to control a transmission system or a transmission system operator if they comply with the requirements of effective separation that apply inside the Community. Without prejudice to the international obligations of the Community, the Community considers that the gas transmission system sector is of high importance to the Community and therefore additional safeguards are necessary regarding the preservation of the security of supply of energy to the Community to avoid any threats to public order and public security in the Community and the welfare of the citizens of the Union. [...]*" (emphasis added).

Such additional safeguards are needed as there are material differences between a person from a third country controlling a transmission sytem operator and a person from an EU Member State controlling a transmission system operator. While EU Member States cannot undermine

the application and enforcement of EU Regulation, including the Gas Directive, in view of their Treaty obligations, third countries are not bound by such obligations. In addition, investigation and enforcement of EU Regulation is also more difficult vis-à-vis companies located in third countries. However, the applicability and enforceability of EU Regulation should be fully ensured in all cases and regardless as to whether the owner of an EU transmission network is an EU or a non-EU person. Additional measures may thus be required. In the case at hand, the Commission is of the view that at least the following potential risks should have been assessed:

1. The risk of governmental acts by the Republic of Azerbaijan or acts by SOCAR and companies affiliated to them that render it impossible or more difficult (such as by creating legal uncertainty or conflicts of law between Azeri and EU legislation) for SOCAR or DESFA to comply with EU energy law, other relevant EU law or Treaty obligations. This includes in particular acts that would impair the development of DESFA's network, such as not providing DESFA with the appropriate financial resources to carry-out necessary investment projects, notably those contained in DESFA's ten-year network development plan, including those concerning the Revithoussa LNG terminal and the future interconnections with the TAP, in accordance with Article 22 Gas Directive;
2. The risk that the Republic of Azerbaijan could exercise its ownership rights in SOCAR in a manner that could result in SOCAR or DESFA acting contrary to EU energy law, other relevant EU law or Treaty obligations, including the exercise of investigative powers and enforcement action;
3. The risk of acts by the Republic of Azerbaijan, SOCAR and/or companies affiliated to them that directly or indirectly sanction the enforcement of EU law against SOCAR or DESFA, including by measures regarding the supply of natural gas to the EU or the terms and conditions of such supplies.

The Commission notes that these risks have not been integrated by RAE in its assessment of risks related to SOCAR's acquisition of control over DESFA.

Finally, the Commission notes that Article 11 explicitly prescribes that RAE should have taken into account in its assessment the rights and obligations of Greece and of the Community with respect to the Republic of Azerbaijan arising under international law, including intergovernmental agreements addressing the issue of security of supply. In addition, Recital (22) of the Gas Directive mentions that in that context *'the treatment of both domestic and foreign trade and investment in energy in a particular third country'* needs to be assessed. These considerations should have been taken into account in RAE's assessment.

On the basis of the above the Commission concludes that RAE's assessment contains shortcomings and that it has not been demonstrated convincingly that no risk to security of supply stems from SOCAR's acquisition of sole control over DESFA. Especially in view of the important position of the DESFA network in the context of the region's security of supply, in view of the fact that control is carried out by a vertically integrated state-owned company from a third country that is an important supplier of gas to Greece and, on the basis of further planned investments, to the EU and, finally, in view the fact that the unbundling rules and other regulatory provisions do not, by themselves, provide sufficient guarantees in the absence of additional safeguards such as an intergovernmental agreement addressing security of supply, the Commission is of the opinion that additional safeguards are necessary to effectively address the abovementioned concerns.

The Commission therefore takes the view that certification should only be granted once it has been established that RAE has the power to suspend, on its own initiative or upon request of the Commission, all voting rights attached to the shares that SOCAR holds in DESFA should SOCAR and/or the Republic of Azerbaijan take a decision or action that negatively affects the security of supply of Greece and/or the European Union.

More in particular, the suspension - which would ensure that the regulator has equivalent enforcement powers vis à vis all operators - should be triggered by the following decisions or actions:

1. Governmental acts by the Republic of Azerbaijan or acts by SOCAR and companies affiliated to them that render it impossible or difficult (such as by creating legal uncertainty or conflicts of law between Azeri and EU legislation) for SOCAR or DESFA to comply with EU or Greek energy law, other relevant EU law or Treaty obligations. These include in particular acts that would impair the development of DESFA's network, such as not providing DESFA with the appropriate financial resources to carry-out necessary investment projects, notably those contained in DESFA's ten-year network development plan, including those concerning the Revithoussa LNG terminal and the future interconnections with the TAP, in accordance with Article 22 Gas Directive;
2. The exercise by the Republic of Azerbaijan of its ownership rights in SOCAR resulting in SOCAR or DESFA acting in a material manner contrary to EU or Greek energy law, other relevant EU law or Treaty obligations, including the exercise of investigative powers and enforcement action, where other regulatory measures are not effective to ensure compliance;
3. Acts by the Republic of Azerbaijan, SOCAR and companies affiliated to them that directly or indirectly sanction the enforcement of EU and Greek law against SOCAR or DESFA, including by measures regarding the supply of natural gas to the EU or the terms and conditions of such supplies.

Before suspending the voting rights of SOCAR in DESFA in accordance with the above, RAE is requested to consult the Commission. SOCAR's procedural rights, including the right to be heard, should be respected.

The suspension of voting rights should not be lifted before legally binding measures, including, if required, legally binding measures under international public law, have entered into force that fully eliminate the risks that have given rise to the suspension of SOCAR's voting rights.

Furthermore, the Commission takes the view that no later than 3 months after granting the certification the Member State should grant RAE the right to apply more stringent measures in case the suspension of SOCAR's voting rights has not resulted in the elimination of the decision or action by SOCAR and/or the Republic of Azerbaijan that negatively affect security of supply.

The Commission should be consulted on the legislative measures to be adopted by the Member State to ensure the implementation of the above mentioned more stringent measures.

IV. CONCLUSION

Pursuant to Article 3 Gas Regulation, RAE shall take utmost account of the above comments of the Commission when taking its final decision regarding the certification of DESFA, and when it does so, shall communicate this decision to the Commission.

The Commission's position on this particular notification is limited to the application of Gas Directive and without prejudice to any position it may take vis-à-vis national regulatory authorities on any other notified draft measures concerning certification, or vis-à-vis national authorities responsible for the transposition of EU legislation, on the compatibility of any national implementing measure with EU law. The Commission's opinion is notably without prejudice to Commission procedures under European competition law.

The Commission will publish this document on its website. The Commission does not consider the information contained therein to be confidential. RAE is invited to inform the Commission within five working days following receipt whether it considers that, in accordance with EU and national rules on business confidentiality, this document contains confidential information which it wishes to have deleted prior to such publication. Reasons for such a request should be given.

Done at Brussels, 17.10.2014

For the Commission
Simm KALLAS
Vice-President

