

ENERGY AGENCY
OF THE REPUBLIC OF SERBIA
Number: 40/2018-D-03/62a
Date: 5 March 2019
Belgrade, Terazije 5

The Council of the Energy Agency of the Republic of Serbia, acting upon the request of GASTRANS d.o.o. Novi Sad, with its business seat at Novi Sad, Narodnog fronta 12, dated 2 February 2018, acting through attorneys Jelena Gazivoda and Nikola Đorđević, lawyers from Belgrade, by which it requested an exemption of GASTRANS d.o.o. from the ownership unbundling obligation and an exemption of future interconnector for natural gas from the obligation to apply third party access rules and regulated prices, pursuant to Article 51 paragraph 2 item 3), article 288. paragraph 19, in relation to paragraph 14. of this article, and Article 39 paragraph 1 of the Energy Law ("Official Gazette of the Republic of Serbia", no. 145/14 and 95/2018-other law) and Article 136 of the Law on General Administrative Procedure ("Official Gazette of the Republic of Serbia", No. 18/16 and 95/2018-authentic interpretation), having obtained an opinion of the Ministry of Mining and Energy of the Republic of Serbia pursuant to Article 288 paragraph 3 of the Energy Law, and the opinion obtained from the Energy Community Secretariat referred to in Article 288 paragraph 12 of the Energy Law, at the 6th extraordinary session held on 5 March 2019, renders the following

Decision
on the exemption of the new interconnector for natural gas

Item 1

IT IS APPROVED TO GASTRANS d.o.o. Novi Sad, with its business seat at Novi Sad, Narodnog fronta 12, company number 20785683, TIN 107350223 (hereinafter referred to as: "**GASTRANS d.o.o.**"), an exemption in respect of the future gas interconnector, described in Item 2 of the disposition of this Decision, from the application of third party access rules (general rules for capacity allocation and general terms and conditions for natural gas transmission), and regulated prices under Article 283 paragraph 1 of the Energy Law (hereinafter referred to as: "**the Law**"), and the exemption from the implementation of ownership unbundling requirements under Article 224 of the Law, as further determined in Items 3-24 of the disposition of this Decision (hereinafter referred to as: "**the Scope of the exemption**").

IT IS APPROVED THAT the exemption referred to in paragraph 1 above shall apply for a period of 20 years, from the date of the start of the commercial operation of the future gas interconnector (hereinafter referred to as: "**the Duration of the exemption**").

Item 2

The approval referred to in Item 1 of the disposition of this Decision refers to the entire future gas interconnector for the transmission of natural gas, with a technical annual capacity of 13.88 bcm (billion cubic metres annually) in accordance with expected technical design (hereinafter referred to as: "**maximum technical annual capacity**"), passing through the territory of the Republic of Serbia in the length of about 400 km and crossing the state border of the Republic of Serbia, to connect with adjacent transmission systems in the Republic of Bulgaria and Hungary, including related equipment for its connection (hereinafter referred to as: "**the New Interconnector**").

The New Interconnector has one (1) entry point – entry point "Zaječar" where the New Interconnector is connected with the adjacent transmission system in the Republic of Bulgaria operated by the transmission system operator BULGARTRANGAZ EAD, and four (4) exit points, being:

1) exit "Horgoš" – exit point where the New Interconnector is connected with the adjacent transmission system in Hungary operated by the transmission system operator FGSZ, and

2) exit "Paraćin", exit "Pančevo" and exit "Gospodinci" – all three points where the New Interconnector is connected with the transmission system operated by the transmission system operator in the Republic of Serbia.

This Decision shall also apply in the case GASTRANS d.o.o. changes the maximum technical capacity of the New Interconnector and adjusts the technical design in accordance with item 13, paragraph 3 of the disposition of this Decision.

Exemption from the obligation of ownership unbundling of operator

Item 3

IT IS APPROVED TO GASTRANS d.o.o. that it remains under the control of one or more companies or be part of a group of companies that are under the control of one or more companies which are conducting the activity of natural gas production or supply, so that by this Decision GASTRANS d.o.o. is exempted from the ownership unbundling requirements under Article 224 paragraph 2 and Article 225 paragraph 1 items 1)-4) of the Law, in the manner that:

- 1) a company may, directly or indirectly, exercise control over a company performing the activity of natural gas production or supply, and simultaneously, directly or indirectly, exercise control or have any right over GASTRANS d.o.o.;
- 2) a company may, directly or indirectly, exercise control over GASTRANS d.o.o. and simultaneously, directly or indirectly, exercise control or have any right over an undertaking performing the activity of natural gas production or supply;
- 3) a company may appoint members of any board or bodies, including persons legally representing GASTRANS d.o.o. and simultaneously, directly or indirectly, exercise control or have any right over an undertaking performing the activity of natural gas production or supply, and
- 4) members of the board or bodies, including persons legally representing the company performing the activity of natural gas production or supply can simultaneously be members of the board or bodies or person legally representing GASTRANS d.o.o.

Item 4

GASTRANS d.o.o. is OBLIGED to permanently protect the confidentiality of commercially sensitive information of system user and apply the measures securing that the commercially sensitive information, particularly as regards the required and agreed capacities and nominations of system users, are not disclosed in a discriminatory manner to the ultimate owners of GASTRANS d.o.o. and their subsidiaries performing the activity of natural gas production or supply (hereinafter referred to as: “**Related Parties**”) or other companies performing the activity of natural gas production or supply.

GASTRANS d.o.o. IS OBLIGED to, to the extent it would not conflict with the exemption approved by this Decision, at the latest by the date of the start of commercial operation of the New Interconnector, and for the Duration of the exemption to:

- 1) independently conduct business operations and operate the New Interconnector and be organized separately from the Related Parties;
- 2) possess the necessary financial, material and technical means for the performance of activities of transmission and operation of transmission system, including independent information systems, equipment, devices and information protection systems from access of Related Parties, as well as has separate and different premises from the Related Parties;
- 3) have a sufficient number of employees who independently perform legal, economic, technical and other duties, as well as duties related to information technology;
- 4) implement the Compliance Program (hereinafter referred to as: “**the Program**”) and the recommendations of the compliance officer;

- 5) secure that the compliance officer performs the duty of monitoring Program implementation separately and independently from GASTRANS d.o.o. and Related Parties.

Item 5

GASTRANS d.o.o. IS OBLIGED to:

- 1) adopt the Program with the consent of the Energy Agency of the Republic of Serbia (hereinafter referred to as: **“the Agency”**);
- 2) adopt the act on the conditions for appointing of the compliance officer, with the consent of the Agency,
- 3) appoint compliance officer, with prior consent of the Agency.

IT IS REQUESTED FROM GASTRANS d.o.o. that it, prior to dissemination of the binding invitation for allocation of long-term capacity pursuant to Decision on the manner of allocation and mechanisms for management of the transport capacities of the company GASTRANS d.o.o. number 40/2018-D-03/42, adopted by the Council of the Energy Agency at its session held on 3 September 2018 and its amendments and supplements (hereinafter referred to as: **“the Decision on allocation”**):

1) adopt the Program and act on conditions for appointing the compliance officer with the consent of the Agency and obtain prior approval of the Agency for appointing the compliance officer referred to in paragraph 1 of this item of the disposition of this Decision.

2) appoint an *ad hoc* body to receive objections from bidders on the results of the allocation of capacity that has been exempted from the third party access requirements. Such body shall consist of three members who are not appointed persons in the management bodies and do not have professional responsibility in either (a) any of the companies that are the ultimate owners of GASTRANS d.o.o., or (b) subsidiaries of those companies from mentioned point (a) performing activities of natural gas production or supply.

Item 6

GASTRANS d.o.o. IS OBLIGED to determine in the Program:

- 1) measures to prevent discriminatory treatment of GASTRANS d.o.o. against service users, taking into account the Scope of the exemption;
- 2) measures that provide permanent protection against discriminatory access to commercially sensitive data of service users and prevention of disclosure of these unaggregated information to Related parties;
- 3) authorisations of the compliance officer, particularly:
 - right and obligation to attend meetings of all management bodies which are deciding on the issues that are subject of its monitoring and to be timely informed of the agenda and materials which shall be considered;
 - the right to access services, premises, documentation, information and other systems for the purpose of controlling the implementation of the Program and its objectives, without prior notice;
 - monitoring the method of realisation of the gas transportation agreements, especially with regard to the non-discriminatory application of congestion management mechanisms, calculation of the price of system access under the agreements on provision of long-term and short-term natural gas transmission services, regularity and non-discriminatory determination of the user's imbalance and the method of determining the imbalance prices;
 - monitoring the adequacy of the technical means and resources necessary for the independent performance of the activities of transmission and operation of the transmission system;
 - monitoring of the non-discrimination and adequacy of the performance of work by employees in the performance of technical, economic-financial, legal and IT works in accordance with the conditions under the Program;
- 4) the obligation of the compliance officer to monitor the Program implementation, to submit an annual report to the Agency on the undertaken measures for the implementation of the Program, to inform the

Agency on any significant breach of the provisions of the Program and submit other related information at the request of the Agency;

- 5) the obligation of the compliance officer to submit a report on implementation of the Program to the managing body with the recommendation for its application;
- 6) the conditions under which Related Parties may provide services to GASTRANS d.o.o., apart from the activities related to the crediting and realisation of the construction and maintenance of the New Interconnector.

Item 7

GASTRANS d.o.o. is OBLIGED to determine in the act on conditions of appointment of the compliance officer, in accordance with this Decision:

- 1) the conditions for appointing the compliance officer and the conditions for ensuring its independence, which implies that it cannot be appointed or have professional responsibility, interest or share in the Related Party, directly or indirectly, nor that it has had such an engagement, interest or responsibility, directly or indirectly, in previous 3 years;
- 2) the term of the mandate and the conditions for dismissing the compliance officer, whereby it can be dismissed only with prior consent or at the request of the Agency, if it was not professional or independent in performing its authorities.

Exemption from the third party access

Item 8

IT IS APPROVED TO GASTRANS d.o.o. a partial exemption of the New Interconnector from the obligation to apply the principles of the third party access specified in the Article 283, paragraph 1 of the Law, so that GASTRANS d.o.o. has the right to allocate a part of the capacity of the New Interconnector on the long-term basis in a scope and in the manner determined in items 9, 10 and 11 of the disposition of this Decision.

The manner of the allocation of capacities exempted by this Decision from the obligation to apply third party access rules is obligatory for GASTRANS d.o.o. also in the case, when following enactment of this Decision, GASTRANS d.o.o. changes maximum technical capacity and adjusts technical design of the New Interconnector.

GASTRANS d.o.o. IS OBLIGED to allocate the capacities of the New Interconnector referred to in items 9, 10 and 11 of the disposition of this Decision, which are exempted from the obligation to apply the third party access rules, as a one-stage procedure conducted within a period determined by it in the invitation for submission of binding bids in accordance with the Decision on allocation.

Allocation of capacities exempted from the application of third-party access rules

Item 9

IT IS APPROVED TO GASTRANS d.o.o. to allocate a part of capacities of the New Interconnector in priority to companies "Gazprom export LLC" and JP Srbijagas (hereinafter referred as: "**EPA Parties**") for contracting of long-term gas transmission services for a period not exceeding the Duration of the exemption, whereby the volume of the capacity for which it is permitted to be allocated in priority cannot be higher than:

- 1) 70% of the technical capacity at entry point "Zaječar" for a period not exceeding 20 years;

- 2) 55% of the technical capacity at “Paraćin”, “Pančevo” and “Gospodinci” exit points for a period not exceeding 20 years; and
- 3) 75% of the technical capacity at exit point “Horgoš” for a period not exceeding 18 years.

Priority allocation of capacities to EPA Parties is made at entry point “Zaječar” and exit points:

- 1) in accordance with overall economic value of their binding bids (calculated on the basis of duration of service, amount of the capacity and tariff) at the entry point “Zaječar”, if the total required capacities from their binding bids exceed the permitted volume of the technical capacity referred to in paragraph 1 of this item;
- 2) through full acceptance of bids for priority allocation of capacities, if the total required capacities are smaller or equal to the permitted volume of capacity referred to in paragraph 1 of this item, determined at the entry point and each exit point.

GASTRANS d.o.o. IS OBLIGED to, in case of a part of capacities remaining unallocated for reasons referred to in paragraph 2, subitem 2) of this item, allocate such unallocated capacity together with the capacities referred to in item 10, paragraph 2 of the disposition of this Decision.

Item 10

IT IS APPROVED TO GASTRANS d.o.o. to allocate a part of capacities of the New Interconnector to all third parties which are not Related Parties and which submit binding bids in accordance with the Decision on allocation for the conclusion of the contract on the provision of long-term gas transmission services for a period not exceeding the Duration of the exemption.

GASTRANS d.o.o. IS OBLIGED to, in accordance with the rules on allocation of capacities and criteria for ranking of binding bids under items 5, 7 and 8 of the Decision on allocation, allocate to the third parties referred to in paragraph 1 hereof at least:

- 1) 20% of the technical capacity at the entry point of “Zaječar”, for a period not exceeding 20 years;
- 2) 35% at the exit point “Paraćin”, “Pančevo”, “Gospodinci”, for a period not exceeding 20 years, and
- 3) 15% at the exit point of “Horgoš” (“Kiškundorožma”), for a period not exceeding 18 years,

whereby it is obliged to increase all the capacities referred to in the sub-items 1) -3) of this item for the capacities that remained unallocated at the entry point and the exit points after allocation to the EPA Parties, pursuant to item 9, paragraph 3 of the disposition of this Decision.

GASTRANS d.o.o. shall be obliged, on the basis of the list of ranking of binding bids drawn up in accordance with item 8 of the Decision on allocation, to allocate the total available capacities under paragraph 2 of this item to the ranked bids of those bidders who have requested a capacity that is of the same volume in each gas year, provided that they have requested transport services for a period of 20 years, that is 18 years at the “Horgoš” exit point.

Item 11

IT IS APPROVED TO GASTRANS d.o.o., in the event that part of the capacity remains unallocated after allocation in accordance with items 9 and 10 of the disposition of this Decision, to allocate all unallocated capacity to the bidders that submitted the binding bids (including EPA Parties and Related parties), on the basis of the list of ranking of binding bids drawn up in accordance with item 8 of the Decision on allocation.

The allocation of capacities referred to in paragraph 1 of this item shall be carried out if GASTRANS d.o.o. assesses that it is economically justified.

Allocation of capacities non- exempted from the application of third-party access rules

Item 12

GASTRANS d.o.o. is OBLIGED to, without prejudice to the right to decrease technical capacity in accordance with item 2 of disposition of this Decision, offer for allocation short-term capacities of the New Interconnector in the volume of at least 10% of the technical capacity of the entry point and each individual exit point, which includes capacity previously allocated but freed up due to expiration of the gas transportation agreement concluded in accordance with items 9, 10 and 11 of disposition of this Decision.

The capacities referred to in paragraph 1 hereof shall be offered and allocated to all interested parties during the Duration of exemption in accordance with the applicable rules of regulated third party access, for the purpose of concluding short-term natural gas transmission services for the duration of the gas quarter, gas month, gas day and intra gas day.

GASTRANS d.o.o. IS OBLIGED starting from the day of commencement of the operation of the New Interconnector, to offer and allocate the capacity referred to in paragraph 1 hereof through the operating platform, applying the auction method in which the initial price for the capacity is determined in the amount corresponding to the applicable annual tariff applied at the time of allocation at the point of entry, i.e. individual exit point, and which it has formed in accordance with the methodology it adopts for determining the price of long-term access to the New Interconnector and by application of the coefficients and seasonal factors set out in Decision 2018/07/of the Permanent High Level Group of the Energy Community (PHLG EnC) in the part by which the Energy Community adapts Chapter III of Regulation (EU) No. 2017/460 establishing a network code on harmonised transmission tariff structures for gas.

GASTRANS d.o.o. IS OBLIGED to, in accordance with the rules of regulated third party access, prior to the start of the operation of the New Interconnector, adopt the network code regulating in detail the method of allocating the capacity via auctions and the conditions for using the operating platform it selects, bearing in mind the platforms used by the adjacent transmission system operators to whose expanded infrastructure it plans to connect the New Interconnector, for the purpose of allocating the capacity in accordance with the rules set out in Decision 2018/06/Permanent High Level Group of the Energy Community (PHLG EnC) in the part adapting Regulation (EU) No. 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems and in accordance with the Decision 2018/07/Permanent High Level Group of the Energy Community (PHLG EnC) in the part adapting Regulation (EU) No. 2017/460 establishing a network code on harmonised transmission tariff structures for gas,

Item 13

The capacities referred to in item 12 of the disposition of this Decision shall be allocated successively for the whole Duration of the exemption in accordance with the applicable rules of regulated third party access, whereby the first capacity allocation shall be implemented starting from the first year in which the operation of the New Interconnector starts.

GASTRANS d.o.o. IS OBLIGED to determine the timing of auctions in accordance with the auction schedule set forth in Decision 2018/06/Permanent High Level Group of the Energy Community (PHLG EnC) in the part adapting Regulation (EU) No. 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems.

GASTRANS d.o.o. is entitled to reduce the maximum technical capacity of the New Interconnector if, after the implementation of the allocation of capacity in accordance with items 9, 10 and 11 of the disposition of this Decision, it contracts less than 90% of the maximum technical capacity of the New Interconnector, but it shall in the event of reducing the maximum technical capacity of the project during the Duration of the exemption permanently offer to all interested persons at least 10% of this reduced maximum technical capacity in accordance with item 12 of the disposition of this Decision.

GASTRANS d.o.o. shall endeavour, in cooperation with adjacent transmission system operators, to offer short-term capacities for allocation as bundled products.

Item 14

GASTRANS d.o.o. IS OBLIGED to, starting from the day of commencement of operation of the New Interconnector, and during the Duration of exemption, offer for allocation reverse (commercial) capacities on interruptible basis, for the direction from Hungary to Serbia at the exit point "Horgoš", for the direction from Serbia to Bulgaria at the exit points "Gospodinci", "Pančevo" and "Paraćin" and at the entry point "Zaječar" in accordance with the rules under item 12 of the disposition of this Decision, whereby the initial auction price for the annual reverse (commercial) capacity on interruptible basis shall not exceed 47.5 % of the amount of the applicable annual tariff for the exempted long-term capacity it applies at these points at the moment of capacity allocation, and which it has determined in accordance with the methodology. The initial auction price for the reverse (commercial) capacity on interruptible basis for the gas quarter, gas month and gas day shall not be higher than 47.5 % of the amount of the applicable tariff, which it applies as the initial price for the auction for the gas quarter, gas month and gas day at these points for the physical direction of flow of natural gas.

GASTRANS d.o.o. IS OBLIGED to examine every two years the interest of the market for the use of additional capacities in the directions of the physical and reverse flow of natural gas supply, and if the obtained results show the economic justification of the investment, it shall build additional capacities in accordance with the demand of the natural gas market. Additional capacities will be allocated in accordance with the rules of regulated third party access from item 12, paragraph 3 of the disposition of this Decision.

GASTRANS d.o.o. IS OBLIGED to, in the event of an emergency, provide a physical flow of natural gas in direction from Serbia to Bulgaria in accordance with the procedure and rules set out by the applicable law including principles of transparency, non-discrimination and fair compensation.

Item 15

IT IS APPROVED TO GASTRANS d.o.o. the right to be exempted from the application of the third party access rules on the part of the capacity of the New Interconnector which it allocates in accordance with items 9, 10 and 11 of the disposition of this Decision, which implies:

- 1) exemption from the obligation to apply non-discriminatory access to the transmission system referred to in Article 247, point 7) of the Law and Article 248, paragraph 1, item 12) of the Law, so that the allocations of capacities is in accordance with the rules under items 9, 10 and 11 of the disposition of this Decision shall not be deemed as discriminatory treatment of users in exercising the right to access to the system,
- 2) exemption from the obligation to publish the methodology which GASTRANS d.o.o. adopts based on the approval of the Agency for determining the prices for calculation of long-term natural gas transmission services under items 9, 10 and 11 of the disposition of this Decision, as well as the exemption from the obligation to publish the cost structure, the individual amounts of the tariffs and the manner of their harmonization as determined by this methodology, so that non-publication thereof shall not be deemed as a breach of Article 248, paragraph 1, items 13) and 15) and Article 254 paragraph 1 items 17) and 18) of the Law, whereby GASTRANS d.o.o. shall be obliged to publish the initial prices for the capacity it allocates in accordance with the third-party access rules via auctions it implements in accordance with item 12 of disposition of this Decision;
- 3) exemption from the obligation to keep records set out in Article 248, paragraph 1, item 17) of the Law;
- 4) exemption from the obligation to apply the prescribed balancing rules for the transmission system referred to in Article 248, paragraph 1, point 8), 254, paragraph 1, point 16, 293 and 296 of the Law, if GASTRANS d.o.o. assesses the application of different rules during the Duration of the exemption as more favourable, such as the contracting of the operational balancing of the system in the agreement on natural gas transmission and/or the network code and the determination of the imbalance charge;

- 5) to contract access to the New Interconnector on the basis of a contract on access (gas transportation agreement) containing the elements prescribed by Article 284 of the Law and the network code referred to in Article 254 of the Law, and in relation to Article 53, paragraph 1, item 4) of the Law, so that GASTRANS d.o.o. is entitled to conclude gas transportation agreements in accordance with this Decision, subject to the approval of the Agency for the model of this agreement.

IT IS APPROVED TO GASTRANS d.o.o the right to an exemption from the application of the third party access rules on the part of the capacity of the New Interconnector which it allocates in accordance with items 9,10 and 11 of the disposition of this Decision, so that it includes the exemption from the obligation to apply the following obligations and principles if they, on the basis of change of regulation in the Republic of Serbia, become obligatory during the Duration of exemption , as follows:

- 1) the obligation to designate the long-term capacity of the New Interconnector as standard firm capacity products and the application of general or harmonized rules, methodologies or algorithms for the allocation of such products, as well as the standardization of allocation or auction frequencies;
- 2) the requirement to bundle long-term capacity;
- 3) the obligation to implement the rules, methodologies or algorithms for the allocation or auction of an interruptible capacity, harmonized minimum interruption lead times, coordination of interruption processes and the conditions and grounds for interruption;
- 4) the obligation to implement standardized rules on third party trade nominations;
- 5) the obligation to implement standardized rules on daily imbalance price formulation or determination and quantity calculation;
- 6) the obligation to implement requirements of, and principles for neutrality of cash flows for system balancing actions;
- 7) the obligation to implement standardized rules of credit risk management for taking or procuring balancing actions;
- 8) the obligation to implement requirements to conduct a cost benefit analysis assessment for balancing actions taken, and
- 9) the obligation in relation to regulation and standardization of rules on linepack flexibility services and on interim measures.

Item 16

GASTRANS d.o.o. IS OBLIGED TO, prior to allocation of capacity in accordance with items 9, 10 and 11 of the disposition of this Decision, determine the model of the agreement on the long-term natural gas transmission which shall be approved by the Agency, as well as prior to the commencement of the operation of the New Interconnector, adopt the network code, with the approval of the Agency regulating in detail the manner of performance of natural gas transmission services, taking into account the Scope of the exemption granted by this Decision.

The model of the agreement and the network code referred to in paragraph 1 shall mandatorily contain:

- 1) right of the user to the "secondary trade" of capacities (the assignment of long-term and short-term transmission agreements to third parties, as well as the right of the system user to amend the agreement for the purpose of assigning a part of the capacity in favour of the third party or another system user);
- 2) right of GASTRANS d.o.o. to, with the written consent of the users of the capacity, offer and contract with market participants a part or all of the long-term capacity of such user, in its own name and for its own account, in accordance with the applicable regulations governing capacity management mechanisms for the period of a gas month, gas quarter or gas year, with the obligation of GASTRANS d.o.o. in that case to reduce the agreed compensation to the system user, in the manner and at the prices determined by the regulations;
- 3) the obligation of GASTRANS d.o.o. to offer all contracted long-term and short-term capacities that the system users have not nominated within the prescribed deadline, for allocation to all interested entities at least a day ahead on an interruptible basis, as well as the obligation to, in case it is established in the

annual report of the Energy Community Secretariat that there was contractual congestion in the previous year, apply the rules set forth in Decision 2018/01/Permanent High Level Group of the Energy Community (PHLG EnC) in the part adapting Annex 1 to Regulation (EU) No. 715/2009 on conditions for access to the natural gas transmission networks, as amended by European Commission Decision 2012/490;

- 4) transparent and non-discriminatory rules for the nomination of quantities, acceptance and change of nominations (re-nominations), in accordance with the regulations;
- 5) the right of GASTRANS d.o.o. to limit the scope of nominated quantities for transmission in case of overload or system jeopardizing;
- 6) the right of GASTRANS d.o.o. to limit the provision of services on the basis of application of measures established in accordance with the applicable regulations in case of a system disruption or the occurrence of natural gas shortages and in emergency cases;
- 7) the obligation of GASTRANS d.o.o. to exchange data with adjacent operators and conclude interconnection agreements, as well as the obligation to perform the flow control, measurement of natural gas quality, harmonization of allocated quantities, application of prescribed units for measurement of delivered natural gas, odorization, submission of information on measured quantities to users and system operators to which it is connected, in accordance with the applicable regulations governing the operation of the transmission system and the obligations of the transmission system operator;
- 8) the obligation to cooperate with the adjacent operators to which systems the New interconnector is connected,
- 9) the obligation to comply with the transparency rules, except in the part specified in item 15 paragraph 1, sub-item 2) of the disposition of this Decision,
- 10) the obligation to keep records of concluded agreements on transmission and transactions of users of the system which it is obliged to submit at the request of the Agency for the purpose of performing tasks within its competence.

GASTRANS d.o.o. shall, starting from the transmission commencement date, apply the network code for the purpose of realization of the gas transmission agreements concluded in accordance with the items 9-12 of the disposition of this Decision to the extent that the application of these rules is not in conflict with the exemption granted by this Decision.

Exemption from the application of regulated prices

Item 17

IT IS APPROVED TO GASTRANS d.o.o. the exemption from the obligation to determine regulated prices for transmission system access in accordance with Article 283 paragraph 1 of the Law, and Article 50 paragraph 1 item 6) and Article 248 paragraph 1 item 10) of the Law.

GASTRANS d.o.o. shall form the prices for the calculation of costs of long-term access to the New Interconnector which are expressed in tariffs, in line with the methodology based on principles defined under item 18 of the disposition of this Decision and which is adopted with the consent of the Agency.

IT IS APPROVED TO GASTRANS d.o.o. the exemption of long-term capacities allocated in accordance with items 9,10 and 11 of the enacting terms of this Decision, from the application of the following obligations and principles, if they, on the basis of change of regulation in the Republic of Serbia become obligatory during the Duration of the exemption:

- 1) application of the standardized rules on cost allocation assessment;
- 2) set alternative price methodologies and their application to entry point and exit points;
- 3) application of the standardized rules on reserve price calculation;
- 4) application of the standardized rules on reconciliation of tariff revenues;

- 5) application of the standardized rules on pricing of bundled capacity;
- 6) application of the standardized rules on pricing at a virtual point;
- 7) application of the standardized rules on tariff clearing price calculation;
- 8) requirements to consult with the network users and adjoining network operators on tariff setting, and
- 9) application of the standardized rules on pricing of the incremental capacity.

Item 18

The tariffs for long-term contracted capacities of the New Interconnector (Tariffs) shall be transparent, non-discriminatory and equal for all users of the exempted capacities, with the goal of securing the covering of the costs of efficient operation and objective investment risks, and shall be formed for each gas year and expressed in €/kWh/h/a.

GASTRANS d.o.o. shall use nominal flat Tariffs starting from the gas year in which the exit point Horgoš is fully operational for the entire gas year and thereafter.

The Tariffs shall be formed by allocating the necessary income to contracted long-term firm capacities at the entry point and exit points during the Duration of the exemption, so that the same weight shall be applied at distribution, namely 0.5 at the entry and 0.5 at all exits, and all exits intended for delivery to end users of natural gas in the Republic of Serbia shall be treated as a single (virtual) exit point, which ensures a uniform Tariff for all exits in the Republic of Serbia.

The necessary income for all years during which the exit point Horgoš is fully operational for the entire gas year is defined as the sum of operational costs, maintenance costs, costs for compensation of natural gas loss, depreciation costs and necessary return on CAPEX. The necessary income shall be decreased by all income from sale of capacities that have not been contracted as long-term firm capacities, or have been contracted but are not being used, and shall be adjusted by a correction element.

The tariff may be increased or decreased in accordance with the methodology.

The depreciation costs referring to transmission assets of natural gas shall be calculated using pro rata method over 40 years.

The necessary income for the first gas year of operation and gas years before exit point Horgoš is fully operational for the entire the gas year, shall not include depreciation costs and necessary return on CAPEX.

Tariffs for the respective entry or exit points shall be determined as a quotient of the part of the necessary income distributed to that entry or exit point and contracted capacities. Allocation of the necessary income between exit points shall be carried out depending on capacity and transport distance from entry to exit points. For the gas years after the first gas year of operation, until exit point Horgoš becomes fully operational for the entire gas year, the tariffs shall be determined based on the ratio between the Tariffs for the first gas year of operation and the projected Tariffs for the gas year in which exit point Horgoš is fully operational for the entire gas year, and respective average growth rates in that period. In the event that the exit point Horgoš becomes operational partway through the gas year in which it starts operating, the tariff for that exit point shall be determined by multiplying the exit tariff for Serbia in the gas year preceding the full exploitation of capacity with the estimated ratio of the tariff for the exit point Horgoš, divided by the tariff for exit points in Serbia in the subsequent gas year.

Tariffs for each gas year shall be determined in the above described manner and shall be adjusted annually by way of a correction element adjusting the necessary income by the amount of deviation of the actual realized necessary income calculated in accordance with the tariff methodology in the previous year for the estimated necessary income.

The correction element shall not be calculated before the year in which exit point Horgoš is fully operational for the entire the year.

GASTRANS d.o.o. shall, no later than 60 days before the beginning of the transmission service and before the annual adjustments, form the Tariffs for the long-term firm and reverse capacity in accordance with this Decision, based on the relevant data and documentation on current elements of the necessary income and data on contracted capacities and distance between the entry and exit points.

GASTRANS d.o.o. shall be obliged to submit the following economic and financial data and documentation to the Agency by the following deadlines:

- 1) Tariff calculation, data and documentation reflecting the current elements of the necessary income, and calculation of the correction element for the previous year, no later than 90 days before the tariffs enter into force,
- 2) Other data and documentation within the deadline specified in the act regulating the manner, procedure and deadlines for book keeping records, separating accounts by business activities and submitting data and documentation for the purpose of regulation.

Other obligations

Item 19

GASTRANS d.o.o. IS OBLIGED to, during the Duration of the exemption, foresee in its network code a virtual point for the place of natural gas handover where natural gas trade is performed between market participants, including the trade of the quantities contracted on the organized market of the independent market operator in the Republic of Serbia.

During the Duration of the exemption, GASTRANS d.o.o shall, on the request of the Agency, in accordance with the applicable law provide requested data for performing the Agency's competences including the data required for the monitoring of the competition on the gas market of the Republic of Serbia.

Item 20

All the rights determined by this Decision are granted under the condition that GASTRANS d.o.o. shall be the owner of the New Interconnector with described characteristics, that it independently manages New Interconnector and protects the confidentiality of data on system users, and that it operates independently and is separated, in terms of organization, from Related Parties, as well that it performs other obligations determined by this Decision.

Item 21

GASTRANS d.o.o. may propose amendments to the Program, gas transmission agreement, network code and methodology, on which it shall notify a compliance officer. Compliance officer shall evaluate compliance of the proposal with the Scope of exemption and inform the Agency about its evaluation within five working days from the date of receipt of the proposal, and it shall forward to the Agency its evaluation with a proposal for amendments. Taking into account an evaluation of the compliance officer, the Agency shall check compliance of the amendments with the Scope of exemption and, in the case of compliance, it will give its approval within five working days from the date of receipt of the proposal. If granting an approval is denied, the Agency will give reasons for not granting its approval, whereby an approval may not be unreasonably withheld. If the Agency does not provide the response within five working days, it will be deemed to have agreed with proposed amendments.

This item shall be without prejudice to the right of users to accept proposed amendments of the gas transmission agreement and network code in accordance with procedure set out in the gas transmission agreement and network code.

Tariffs adjustment pursuant to item 18 of the disposition of this Decision is not subject to approval of the Agency.

Item 22

Change of regulations governing the conditions for ownership unbundling, for third party access, terms and conditions for natural gas transmission services, the method of determining the prices for access to the natural gas transmission system, the manner of managing the transmission system in order to perform long-term transmission services in the exempted capacity and manner of organizing of a system operator is without the effect to the scope and the manner of exercise of the rights granted to the GASTRANS d.o.o. by this Act and the rights and obligations of users of long-term natural gas transmission services that GASTRANS d.o.o. contracted in the Duration of the exemption, in accordance with the Scope of exemption approved by this Act.

Item 23

This Decision shall become valid from the date of rendering thereof and shall cease 20 years starting from the commercial operations date of New Interconnector.

All rights granted with this Decision shall cease if GASTRANS d.o.o. does not commence the construction works in relation to the New Interconnector within two years of the date this Decision becomes final and does not put the New Interconnect into operation within five years of the date this Decision becomes final, or if it ceases to permanently fulfil conditions determined by this Decision during its validity.

Item 24

GASTRANS d.o.o. IS OBLIGED, prior to the commercial operation date, to obtain Agency's act on certification which shall be issued and valid under proviso GASTRANS d.o.o. meets conditions set forth in this Decision, whereby, the Agency shall in the prescribed certification procedure consider the conditions referred to in Art. 224, 225, paragraphs 1)-4), Article 245 and Article 246 of the Law as fulfilled.

GASTRANS d.o.o. IS OBLIGED, during the Duration of the exemption, to report in writing to the Agency any change of importance for the assessment of the fulfilment of the conditions under which the exemption is granted, no later than 15 days after its occurrence.

Item 25

IT IS ADOPTED the request of GASTRANS d.o.o. to protect the confidentiality of commercial and other confidential business data and it is ordered that the protected version of this Decision, which does not include commercial and other confidential business data, is published in the Official Gazette of the Republic of Serbia and on website of the Agency together with the opinion of the Ministry of Mining and Energy and opinion of the Energy Community Secretariat.

Item 26

The amount of RSD 12,110 being administrative fee for issuance of the act on exemption for new infrastructure in natural gas industry and the amount of RSD 121,100 being administrative fee for the act on exemption have been collected pursuant to the Law on state administrative fees, tariff number 140.

Item 27

Once this Decision becomes final, the Decision on exemption of the New Interconnector for natural gas No. 40/2018-D-03/46, adopted by the Council of the Energy Agency of the Republic of Serbia at the 2nd Extraordinary Session held on 1 October 2018, shall cease to apply.

Explanation

GASTRANS d.o.o. Novi Sad, with business seat in Novi Sad, Narodnog fronta 12, company number 20785683 TIN 107350223, filed on February 2 2018, through attorneys Jelena Gazivoda and Nikola Đorđević, lawyers from Belgrade, a request for exemption of GASTRANS d.o.o. from the obligation of ownership unbundling referred to in Article 224 of the Law and for full exemption (100%) of the future gas interconnector from third party access and the application of regulated prices referred to in Article 283 paragraph 1 of the Law, for a period of 25 years.

This request was submitted to the Energy Agency of the Republic of Serbia in accordance with Article 288 paragraph 1 of the Energy Law (hereinafter referred to as: "**the Law**") which implements into the legal system of the Republic of Serbia the international obligations of the Republic of Serbia as accepted by Decision 2011/02/MC-EnC of the Energy Community Ministerial Council (hereinafter referred to as: "**Implementing Decision**"). By the Implementing Decision the Energy Community of South Eastern Europe has adapted Article 36(1) of Directive 2009/73/EC of the European Parliament and of the Council concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (hereinafter referred to as: "**Gas Directive**"), which specifies the conditions and manner of

approving the right to third party exemption on natural gas infrastructure. The Implementing Decision was issued by the Ministerial Council of the Energy Community pursuant to the Law on ratification of the Treaty establishing the Energy Community between the European Community and the Republic of Albania, Bosnia and Herzegovina, the Republic of Croatia, the former Yugoslav Republic of Macedonia, the Republic of Montenegro, Romania, the Republic of Serbia and the United Nations Interim Administration Mission in Kosovo in accordance with United Nations Security Council Resolution 1244 ("Official Gazette of the Republic of Serbia", no. 62/2006).

Article 51 paragraph 2 item 3) of the Law regulates the authority of the Agency to issue an act on exemption referred to in Article 288 of the Law.

Article 288 paragraph 1 of the Law stipulates that new gas infrastructure, i.e. interconnectors and storage facilities, may, upon request, be exempted from the application of Article 224 of the Law (obligation of ownership unbundling) and right to access (under Article 283 paragraph 1 of the Law) under the following conditions:

- 1) the investment into the new infrastructure facility must enhance competition in gas supply and enhance security of supply;
- 2) the level of risk attached to investing into new infrastructure facility must be such that the investment will not take place unless an exemption is granted;
- 3) the new infrastructure facilities must be owned by a natural or legal person operating in a different business entity separate from the system operators in whose systems that new infrastructure will be built;
- 4) charges for use of the infrastructure facility must be levied on the users of that infrastructure; and
- 5) the exemption must not be detrimental to competition, to the effective functioning of the internal market in natural gas, or to the efficient functioning of the regulated system to which the infrastructure is connected.

Article 288, paragraph 3 of the Law stipulates that the act on exemption shall be issued by the Agency upon obtaining the opinion of the Ministry which shall be published in the "Official Gazette of the Republic of Serbia".

Article 288, paragraph 4 stipulates that the act on exemption may include the whole new infrastructure or its parts, existing infrastructure with an increased or modified capacity.

Article 288, paragraph 6 of the Law stipulates that when deciding on the request for exemption the Agency shall consider non-discriminatory access to new infrastructure; duration of exemption; access to new facilities to be constructed; planned infrastructure exploitation period; and national specificities that are applicable in the specific case.

Article 288, paragraph 7 of the Law stipulates that prior to passing the act on exemption, the Agency shall decide on the rules on allocation of capacity and mechanisms for management of capacity.

Article 288, paragraph 9 of the Law stipulates that the act on exemption may be issued upon an exchange of opinions with adjacent operators.

Article 288, paragraph 10 of the Law stipulates that the Agency shall, without delay, submit the decision on exemption and a copy of the request for exemption to the competent authority, in accordance with the obligations arising from confirmed international agreements (to the Energy Community Secretariat in accordance with the Treaty establishing the Energy Community).

Article 288, paragraph 13 of the Law stipulates that the competent authority, in accordance with the obligations arising from confirmed international agreements, may issue a decision requiring the Agency to amend or withdraw the act on exemption.

Article 288, paragraph 13 of the Law stipulates that in case that the competent authority issues the decision under Paragraph 12 of this Article, the Agency shall take this decision into account to the greatest possible extent.

Article 288, paragraph 14 of the Law stipulates that where the final decision of the Agency diverges from the opinion of the competent authority, the Agency shall provide and publish, together with that decision, the reasoning underlying its decision.

I. Content of the request for exemption, procedure preceding the issuing of the act on exemption referred to in Article 288 paragraph 3 of the Law (Act on Exemption of the Energy Agency of the Republic of Serbia no. 40/2018-D-03/46 dated 1 October 2018)

In its request for exemption submitted to this Agency on 2 February 2018 (hereinafter referred to as: "**Initial request**"), GASTRANS d.o.o. requested exemption from:

- (1) the obligation of applying rules on ownership unbundling of the system operator pursuant to Article 224 of the Law (implementing Article 9 of the Gas Directive on the basis of the Implementing Decision);
- (2) the obligation of applying rules on third party access to the new interconnector which it plans to construct for the purpose of transporting natural gas (which includes the obligation of applying prescribed conditions for transmission of natural gas) and the obligation of applying regulated natural gas transmission tariffs pursuant to Article 283 paragraph 1 of the Law (implementing Article 32 of the Gas Directive on the basis of the Implementing Decision);

In the Initial Request GASTRANS d.o.o. requested that the Agency approve the right to exemption in a scope which grants:

- (a) exemption of GASTRANS d.o.o. from the obligation of applying methodology adopted by the Agency and the obligation of forming its tariffs for access to the transmission system on the basis of these methodologies with the approval of the Agency (corresponding to the scope of exemption referred to in Article 41 paragraph 8 of the Gas Directive, applied by the Energy Community on the basis of the Implementing Decision), and in connection therewith approval of the right of GASTRANS d.o.o. to independently adopt methodology by which it shall determine the manner of forming prices for access to the natural gas transmission system and methodology for determining costs of connecting to the transmission system, including the right to independently determine imbalance fees (price for providing balancing services) and price for access to cross-border infrastructure (corresponding to exemption from Article 41 paragraph 6 of the Gas Directive, applied by the Energy Community on the basis of the Implementing Decision);
- (b) exemption from the obligation of applying prescribed conditions for providing the service of transport of natural gas, including applying regulated transmission tariffs and Agency methodologies (corresponding to exemption from Article 41 paragraph 10 of the Gas Directive, applied by the Energy Community on the basis of the Implementing Decision);
- (c) exemption from the obligation of applying Regulation (EC) 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) 1775/2005 (hereinafter referred to as: "**Gas Access Regulation**") as implemented into the Law by the Republic of Serbia on the basis of the Implementing Decision, to the new infrastructure.

In the attachment to its Initial Request, in accordance with Article 288 of the Law and Article 3 of the Rules of Procedure on conditions for exemption, content of request for exemption and content of act on exemption ("Official Gazette of the Republic of Serbia", no. 11/2018)- hereinafter referred to as the "**Rules of Procedure**", GASTRANS d.o.o. submitted the following: 1) corporate data on structure of ownership with a list of energy undertakings in the Republic of Serbia related to GASTRANS d.o.o., 2) an overview of the current state of development of the natural gas sector in the Republic of Serbia, 3) details of the Project and an assessment of compliance of the Project with the strategic goals of the Republic of Serbia and legal grounds for submission of the Initial Request, 4) an excerpt on registration of GASTRANS d.o.o., issued by the Business Registers Agency on 31 January 2018, a power of attorney for Jelena Gazivoda and Nikola Đorđević from Belgrade dated 31 January 2018, and 5) a letter from [.....]

In the Initial request, GASTRANS d.o.o. emphasizes that:

- it is conducting an economic and technical feasibility study for the construction of a new natural gas transmission pipeline which will run through the Republic of Serbia (hereinafter referred to as: "the **Project**") and connect to the Hungarian and Bulgarian national transmission systems (hereinafter referred to as: "**NTS**"), which presumes (according to preliminary estimations) a maximum annual flow rate of thirteen point eighty eight billion (13,880,000,000) m³ at the Entry point; the Initial Request specifies that [.....];

- the realization of investment in the new infrastructure is possible only if the Agency grants full exemption for a period of 25 years from the obligation of ownership unbundling stipulated under Article 224 of the Law and exemption

from third party access and exemption from the obligation of application of regulated prices under Article 283 paragraph 1 of the Law;

- the Project is in alignment with the strategic goals and priority actions set out in the Energy Sector Development Strategy of the Republic of Serbia until 2025, with projections until 2030 ("Official Gazette of the Republic of Serbia", no. 101/2015, hereinafter referred to as: the "**Strategy**") since, if constructed, the pipeline would provide for a new direction of supply and for the establishment of interconnections with Bulgarian and Hungarian NTS;

- the Project fulfils the requirements of the Strategy, does not conflict with the other projects envisaged by the Program for Realization of the Energy Sector Development Strategy of the Republic of Serbia until 2025, with projections until 2030, for the period 2017-2023 ("Official Gazette of the Republic of Serbia", no. 104/2017, hereinafter referred to as: the "**Program**"), and represents a unique opportunity to connect the Serbian NTS with the Bulgarian NTS and Hungarian NTS via one pipeline, wherefore it represents a project of interest for the Republic of Serbia in securing its natural gas supply, thus providing benefits for the users of natural gas and providing for the development of the natural gas market in the Republic of Serbia;

- the realization of the new infrastructure would have beneficial effects on the natural gas market in the Republic of Serbia which lacks additional transmission capacities, since 80% of the total demand for natural gas in the Republic of Serbia is provided by imports, through the only interconnection at the Horgoš location (operated by JP Srbijagas Novi Sad), and that, according to the data and projections that GASTRANS d.o.o. has at its disposal, increase of the demand for natural gas is expected, which must be secured from imports as domestic gas production is constantly decreasing, as well as that in the Republic of Serbia at this time no projects are being realized by the competent operators nor third parties relating to investing in alternative routes or sources of supply, wherefore GASTRANS d.o.o. emphasizes that, due to such situation in the natural gas sector in the Republic of Serbia, it would be interested in constructing and, as owner, operating the new infrastructure, provided that the Agency grants the exemption on the basis of the submitted request;

- the realization of the Project will benefit the Republic of Serbia in terms of: development of the domestic natural gas market; guaranteeing long-term security and stability of natural gas supply; connecting the natural gas transmission system of the Republic of Serbia with the Bulgarian NTS and the Hungarian NTS; diversifying sources and streams/directions of supply; obtaining a modern transmission system of natural gas; (.....); and ensuring the capacity to meet increased demand for natural gas in the Republic of Serbia, as well as additional benefits for the Republic of Serbia in terms of increase of public revenues of the Republic of Serbia through the natural gas transmission fees, the engagement of domestic man-power in the implementation of the Project and the reduction of the unemployment rate in the Republic of Serbia;

- adjacent transmission system operators in the neighboring countries - BULGARTRANGAZ EAD and FGSZ - are planning to upgrade the existing natural gas transmission system by constructing additional sections of new pipelines in the Republic of Bulgaria and Hungary to which GASTRANS d.o.o. could connect its new infrastructure, in which case the implementation of the Project would enable connection of the natural gas market in the Republic of Serbia with the Bulgarian and Hungarian natural gas markets, and, at the same time, be the first interconnection connecting the gas markets of these two EU countries, via the route of the gas pipeline in the Republic of Serbia.

In the Initial Request, GASTRANS d.o.o. described the new infrastructure facility as a gas interconnector whose planned route through the territory of the Republic of Serbia is about 400 km long, that the route plans one entry point near the city of Zaječar, three exit points in the territory of Republic of Serbia (Paraćin, Pančevo, Gospođinci), and a fourth exit point in the vicinity of inhabited place Horgoš, i.e. that this pipeline is planned to cross the state border of the Republic of Serbia in order to connect to the future pipelines to be constructed by the adjacent system operators in Hungary and the Republic of Bulgaria. In the Initial Request GASTRANS d.o.o. further stated that preliminary discussions with the adjacent system operators BULGARTRANGASZ EAD and FGSZ have been commenced for the purpose of harmonization of the technical characteristics of the pipelines and the requirements at the point of connection, which, according to the preliminary agreements, envision a projected pressure at the entry and the exit points of 7.4 MPa, maximum allowed operational pressure of 6.6 MPa, and maximum annual flow rate of the interconnector of 13.8 billion m³ of natural gas.

The Initial request also contained a separate request of GASTRANS d.o.o. that the Agency determine the manner and conditions for collecting non-binding bids in order to determine decisive facts about the overall needs of

participants on the market for using the new infrastructure. The Initial request also contained the request of GASTRANS d.o.o. for protection of confidential information in accordance with Article 57, paragraph 7 of the Law.

Acting upon the submitted request the Agency took into consideration:

- that Article 288 paragraph 1 of the Law prescribes that new gas infrastructure, i.e. interconnectors and storage facilities, may, upon request, be exempted from the application of Article 224 of the Law (obligation of ownership unbundling) and right to access (Article 283 paragraph 1 of the Law) under the conditions specified in items 1)-5) of this Article, which include the condition that the new infrastructure must be owned by a natural or legal person operating in a different business entity separate from the system operators in whose systems that new infrastructure will be built (item 3) of paragraph 1 of this Article);

- that Article 2 item 25) of the Law defines "interconnector" as an electricity transmission line, gas pipeline, oil pipeline or product pipeline that crosses the border between countries for the purpose of connecting their systems, as well as the equipment that is used for connecting the energy systems.

- that Article 2 item 46) of the Law defines "new infrastructure facility" as a facility not constructed by the date of entering of the Law into force.

Acting upon the Initial Request of GASTRANS d.o.o., the Agency has determined that GASTRANS d.o.o. is registered for conducting the business activity of pipeline transmission and is not a system operator operating in the market of the Republic of Serbia, but that GASTRANS is a separate legal entity which plans to build a new gas infrastructure provided that the exemption is granted, and to acquire ownership of the new infrastructure on the basis of the construction thereof, in order to operate said infrastructure as a transmission system operator, separately from other transmission system operators in the Republic of Serbia, which is a condition prescribed in Article 288 paragraph 1 Item 3) of the Law, on the basis of which the legitimation/right to participate in respective proceedings of the applicant submitting the request in the exemption procedure is established.

As the Initial Request specifies that construction of the gas interconnector is planned from the entry point at the border with the Republic of Bulgaria near the town of Zaječar, so that the route passes through the territory of the Republic of Serbia in the length of about 400 km, and that the planned final exit/delivery point is at a location planned to probably be across the state border with the Republic of Hungary, the Agency has established that exemption is requested for a facility that will be constructed in full from the entry point to the final exit point, which makes this facility a new infrastructure facility in accordance with Article 288 paragraph 1 and Article 2 item 46) of the Law.

Taking into account the characteristics and description of the new infrastructure facility as described in the Initial Request, the Agency has established that the request is permissible because it is submitted for a natural gas transmission facility whose technical capacity is of significant volume, and whose route is planned to cross the state border of the Republic of Serbia in order to connect to the adjacent transmission systems, wherefore in the opinion of the Agency this important gas infrastructure meets the prescribed requirements that qualify it as a gas interconnector for which exemption may be granted in accordance with Article 288 paragraph 1 and Article 2 item 25) of the Law. The Agency took into consideration the fact that the Project as described in the Initial Request does not define the exact points and locations of connection to adjacent systems, and that the requesting party stated that the point of connection would be defined during the harmonization of the Project characteristics with the adjacent system operators to whose systems this interconnector is planned to be connected.

Given that the requesting party has in the Initial Request demonstrated the probability that the Project plans for the New Interconnector to cross the state border of the Republic of Serbia in order to connect to the adjacent transmission systems in Hungary and the Republic of Bulgaria, the Agency has established that GASTRANS d.o.o. and other interested parties have not submitted to the Hungarian regulatory authority (hereinafter referred to as: "**Hungarian NRA**") or to the regulatory authority of the Republic of Bulgaria (hereinafter referred to as: "**Bulgarian NRA**") requests for exemption of the part of the New Interconnector to be constructed in Hungary and/or the Republic of Bulgaria, based on which it has established that it is the authority with sole competence to decide on this request, without the obligation of issuing a joint decision with the neighboring regulatory authorities, but just with the right to exchange opinions with the neighboring countries, i.e. the national regulatory authorities which would be impacted by the new infrastructure constructed under the condition that the exemption is granted (Article 288 paragraph 9 of the Law).

Since in the Initial Request the party separately requested that the Agency determine the manner and conditions for collecting non-binding bids in order to determine decisive facts about the overall needs of participants on the market for using the new infrastructure, in connection with this request the Agency took into consideration the contents of the attached Letter from supplier [...dated 26 May 2017] by which, in the opinion of the Agency, the requesting party demonstrated the probability of the existence of interest in use of the new infrastructure. Acting upon this request, in accordance with its powers under Article 288 paragraph 7 of the Law, in accordance with the best regulatory practices of the association of regulatory bodies of the European Union, the Agency has decided to determine the manner of allocation of capacity and mechanisms for managing capacities so that it shall first, in accordance with the request of the requesting party, determine the manner of conducting a non-binding phase of testing the interest of the market in using the new infrastructure. Taking into account the proof of existence of expressed interest of the said supplier, in accordance with the request of the requesting party, and with its powers under Article 288 paragraph 7 of the Law, the Agency has adopted a Decision on the Manner and Deadlines for Market Test for use of the Future Infrastructure Facility of the company GASTRANS d.o.o. (hereinafter referred to as: "**Decision on Market Test**").

The Decision on Market Test as under Article 288 paragraph 7 of the law determines the obligation of GASTRANS d.o.o. to enable, in a transparent and non-discriminatory way, all participants in the natural gas market to submit non-binding bids for their desired capacity in the New Interconnector, which it plans to construct, by the deadline that GASTRANS d.o.o. shall specify in the public invitation to bid, so that based on the interest expressed in the non-binding bids GASTRANS d.o.o. can determine whether, and to which extent, there is market interest in using the new infrastructure, depending on which it shall decide whether it will still request exemption if the market interest is insufficient to enable financial viability and recovery of the investment in the Project, which shall also impact the decision on this administrative matter. In this decision the Agency has obliged GASTRANS d.o.o. to enable bidders to specify in their non-binding bids any additional requests relating to the number of delivery points, routes and flows of transport, etc. so as to determine the true needs of the market which the new infrastructure should meet to the greatest possible extent, and so that based on the obtained Market Test results a decision can be made on the scope of exemption, having in mind this proof as decisive facts of importance for assessing the fulfillment of the conditions specified in Article 288 paragraph 1 items 1)-5) of the Law.

The Agency has determined that after obtaining the Market Test results, if the party still wishes to request exemption, a decision shall also be made on the procedure of collecting binding bids for allocation of capacity and mechanisms for managing capacities.

Acting in accordance with the Agency's Decision on Market Test, GASTRANS d.o.o. announced on 5 March 2018 a Public Invitation for submission of non-binding bids for booking capacity in the "Official Gazette of the Republic of Serbia" No. 16/2018, in international media and on its website. By this Public Invitation, GASTRANS d.o.o. invited all Serbian entrepreneurs and Serbian and foreign legal entities, including shareholders of GASTRANS d.o.o. and their subsidiaries and related parties, as well as adjacent transmission system operators to submit non-binding bids without discrimination and to indicate the scope of their interest in use of the new infrastructure. A total of six bidders responded to the Public Invitation by the deadline, and four more after expiration of the deadline for submission of bids, wherefore on 30 April 2018 GASTRANS d.o.o. submitted a Report on the Market Test results to the Agency, accompanied by the bids of the interested bidders.

After evaluating the Market Tests results according to the scope of the capacity requested by the market participants in their non-binding bids for use of transmission services, on 29 June 2018 GASTRANS d.o.o. submitted to the Agency, through its above specified attorneys, an addendum to the request for exemption (hereinafter referred to as: "**Addendum**") by which it partially supplemented and amended the Initial Request.

In the Addendum GASTRANS d.o.o., acting in accordance with Article 3, paragraph 1 item 2) of the Rules of Procedure, which sets out the proof to be attached to the request for exemption, more closely defined the scope and duration of the requested exemption, specifying that it was requesting the Agency to approve:

1. exemption for a period of 20 years (instead of 25 years as requested in the Initial Request);
2. exemption of the full capacity of the new infrastructure (entire new infrastructure facility (100%)) from:

a) the obligation to organize in accordance with Article 224 paragraph 2 of the Law (with reference to Article 225 paragraph 1 items 1), 2), 3) and 4) of the Law) transposing Article 9 of the Gas Directive into the legal system of the Republic of Serbia on the basis of the Implementing Decision (scope of obligations detailed and elaborated in Section 6.3 of the Addendum);

b) the obligation to provide non-discriminatory access to the system, in respect of which GASTRANS d.o.o. is requesting full exemption, or partial exemption in the case of change of the maximum technical capacity of the Project or key technical characteristics of the Project (scope of obligations detailed and elaborated in Section 6.1 of the Addendum);

c) the obligation to apply regulated prices, in respect of which GASTRANS d.o.o. is requesting full exemption (scope of obligations detailed and elaborated in Section 6.2 of the Addendum).

The exemption of the new infrastructure requested by the Addendum, from third party access and from the obligation to apply the rules on regulated access to the transmission system (transposed Article 32 of the Implementing Decision), includes:

- the right of GASTRANS d.o.o. to have its methodologies for calculating the price for access and the costs of connecting to the system, to independently determine the imbalance fees (providing balancing services) as well as fee for access to cross-border infrastructure, so that they are not subject to the Agency's evaluation or approval (corresponds to exemption from Article 41 paragraph 6 of the Gas Directive), i.e. the right to form tariffs, adopt methodologies and form imbalance fees which will not be subject to the Agency's approval (corresponds to exemption from Article 41 paragraph 8 of the Gas Directive),
- the right to independently determine the requirements for operating and for transmission of gas, including amounts of tariffs and determining of methodologies, which will not be subject to the Agency's evaluation or approval, while the Agency shall ensure that the requirements are proportionate and are applied in a non-discriminatory manner (corresponds to exemption from Article 41 paragraph 10 of the Gas Directive); and
- the right for the Gas Access Regulation (as implemented into the Energy Community on the basis of the Implementing Decision) to not be applicable to the Project (which is in line with Article 30 item b) of the Gas Access Regulation, as implemented into the Energy Community on the basis of the Implementing Decision).

The party more closely defined the requested exemption from third party access requesting that 100% of the capacities of the entire facility be exempt, while the right to priority booking of 88% of the available capacity be reserved for the investor companies of the Project (i.e. GAZPROM and JP Srbijagas Novi Sad (hereinafter referred to as: **"SRBIJAGAS"**) and their respective subsidiaries), while the remaining 12% of the available capacity should be allocated on a long-term basis to all interested third parties who have submitted a non-binding bid (expressed interest in use of the capacity in the non-binding market test stage). In its reasoning for the request for exemption of 88% of the planned technical capacity of the New Interconnector in favor of GASPROМ and SRBIJAGAS and their subsidiaries, GASTRANS d.o.o. argues that it will not be possible to secure financing for the Project if a percentage less than 88% is approved, considering that the total demand of third parties who submitted non-binding bids under the GASTRANS d.o.o. Public Invitation dated 5 March 2018 is [...]), which is insufficient for the realization of the planned investment. GASTRANS d.o.o. justifies these statements by presenting different scenarios of utilization of the technical capacity of the gas pipeline, pointing out that the total expressed demand of third parties in the market test stage as specified in the non-binding bids for use of capacities is doubled at the exit points from the Republic of Serbia, i.e. that third parties requested capacities that are significantly higher than the actual and future demands of domestic consumption in the Republic of Serbia, indicating that, if third parties submit binding bids for booking of capacities at those exists, the volume of the actually required capacities would be significantly lower. From all of the above GASTRANS d.o.o. concludes that the investment in the New Interconnector would not be justified if the companies in whose ownership structure GASTRANS d.o.o. is were not granted the right to 88% of the technical capacity, which is the only volume that can ensure a positive investment decision for the construction of a New Interconnector.

In the Addendum GASTRANS d.o.o. also requested exemption from obligations directly connected with third party access under Article 283 paragraph 1 of the Law and exemption from ownership unbundling under Article 224 of the Law, as follows:

- the obligation to apply the rules for third party access referred to in Articles 228, 247, 248, 249, 283, 284 and 285 of the Law (which articles, according to the harmonization table¹, transpose Article 14 of the Gas Access Regulation);
- the obligation to apply capacity allocation and congestion management principles referred to in Articles 254 and 286 of the Law (which articles, according to the harmonization table, transpose Article 16 of the Gas Access Regulation);
- the obligation of transparency referred to in Articles 247-249 of the Law (which articles, according to the harmonization table, transpose Article 18 of the Gas Access Regulation);
- the obligation of record keeping referred to in Articles 248 paragraph 1 item 17) and 291 paragraph 4 of the Law (which articles, according to the harmonization table, transpose Article 20 of the Gas Access Regulation);
- the obligation to apply balancing rules referred to in Articles 248, 254, and 293-296 of the Law, (which articles, according to the harmonization table, transpose Article 21 of the Gas Access Regulation);
- the obligation to apply rules on trading of capacity rights referred to in Article 254 paragraph 1 item 8) of the Law (which article, according to the harmonization table, transposes Article 22 of the Gas Access Regulation);
- the obligation to obtain approval for the general terms and conditions for the provision of services referred to in Article 283 paragraph 1 and in particular Article 53 paragraph 1 item 4) and Article 56 paragraph 1 item 2) of the Law (which articles, according to the harmonization table, transpose Article 41 (6) (b) and (10) of the Gas Directive);
- the obligation to obtain the approval of the Agency for tariffs and methodologies referred to in Article 92 paragraph 1 of the Law, in connection with Article 50 paragraph 1 item 6) of the Law (which articles, according to the harmonization table, transpose Article 41 (6), (8) and (10) of the Gas Directive);
- the obligation to apply tariffs determined in the manner referred to in Article 50 paragraph 1 items 6-8) of the Law (which article, according to the harmonization table, transposes Article 13 of the Gas Access Regulation);
- all future obligations arising from the relevant articles of the network codes governing balancing, capacity allocation, interoperability, which GASTRANS d.o.o. considers to be contrary to the exemption if it is approved, and for which it seeks that they not be applicable, having in mind that similar regulations on these issues may become part of the legal system of the Republic of Serbia during the exemption period.

In the Addendum the requesting party confirmed the request for approving exemption from the obligation of ownership unbundling.

The following proof was attached to the Addendum in accordance with Article 3 of the Rules of Procedure:

- 1) information on changes to the structure of ownership, proving that in the meanwhile GAZPROM TRANSGAZ KRASNODAR has become a shareholder of South Stream Serbia AG Switzerland (hereinafter referred to as: "**SOUTH STREAM SERBIA AG**") instead of OAO GASPROM a.d. (hereinafter referred to as "**GASPROM**");
- 2) additional data and information on the Project (explanation that the facility meets the requirements for a new interconnector as specified in the Law and the Gas Directive and the Implementing Decision, market analysis data, the Market Study and results of the market test, as well as a statement on the requested scope of exemption with an explanation and analysis of the facts confirming fulfillment of the criteria specified in Article 288 paragraph 1 items 1)-5) of the Law.

The Addendum also included the following proof in the form of separate schedules:

- 1) Schedule 1 - Feasibility Study prepared by Društvo za poslovno savetovanje BDO Business Advisory DOO, Beograd (Stari grad), Knez Mihailova 10, 11000 Beograd, in accordance with Article 3, paragraph 1 item 5) sub-item (1) of the Rules of Procedure; 2) Schedule 2 - Tariff Methodology prepared by GASTRANS d.o.o.; 3) Schedule 3 - Compliance Program prepared by GASTRANS d.o.o. providing information relating to the requested exemption from the ownership unbundling requirements set out in Articles 224 and 225 of the Law; 4) Schedule 4 – Market Study report, prepared by BluBerries GmbH, Stetten 4, 83123 Amerang Germany, proving fulfillment of the conditions specified in Article 288, paragraph 1 items 1) and 5) of the Law, and also providing information relating to proving

¹ The form of the statement on harmonization of legislation with the EU legislation, accompanying the proposal of the Law submitted to the National Assembly of the Republic of Serbia for adoption, available at: http://www.parlament.gov.rs/upload/archive/files/cir/pdf/predlozi_zakona/4678-14.pdf

fulfillment of other conditions specified in Article 288 paragraph 1 of the Law; 5) Schedule 5 – Licenses, permits and consents, proving fulfillment of the conditions specified in Article 288, paragraph 1 item 2) of the Law, and also providing information relating to proving fulfillment of other conditions specified in Article 288 paragraph 1 of the Law; 6) Schedule 6 - Rules of Procedure for the binding phase of allocation of capacity prepared by GASTRANS d.o.o., containing the capacity allocation method; and 7) Schedule 7 - excerpts from the corporate registry for South Stream Serbia AG, GAZPROM TRANSGAZ KRASNODAR, GAZPROM, and GAZPROM EXPORT and from the register of shares for South Stream Serbia AG as at 30 May 2018, showing the change of the shareholder i.e. GAZPROM TRANSGAZ KRASNODAR substituting GAZPROM.

By a letter dated 4 July 2018 the Agency requested that GASTRANS d.o.o. submit: the articles of association and incorporation act of South Stream AG Switzerland; a translation into English of an excerpt from the commercial register for GAZPROM TRANSGAZ KRASNODAR; a translation into English of an excerpt from the commercial register for GAZPROM; data pursuant to which the feasibility study was prepared; economical and financial data; information on whether the adjacent transmission system operators have expressed their respective standings on the Rulebook on capacity allocation for the binding phase, which GASTRANS d.o.o. sent to BULGARTRANGAZ EAD and FGSZ, which proof is necessary for the requirements of the further conducting of the procedure before the Energy Community Secretariat in accordance with Article 288 of the Law. On 3 August 2018 GASTRANS d.o.o. submitted the requested documentation.

On 10 August 2018 GASTRANS d.o.o. submitted to the Agency an elaborate report on the necessity for exemption regarding the risks connected to the investment. On 27 September 2018 GASTRANS d.o.o. submitted an amended Schedule 1 (Feasibility Study) and Schedule 2 (Tariff Methodology).

Article 288 paragraph 3 of the Law stipulates that the act on exemption shall be issued by the Agency upon obtaining the opinion of the Ministry which shall be published in the "Official Gazette of the Republic of Serbia".

The Agency obtained the opinion of the Ministry of Mining and Energy as referred to in Article 288 paragraph 3 of the Law, which this Ministry provided by letter no. 312-01-00677/2018-05 as of 18 July 2018, in which opinion the Ministry concludes: "that the realization of the described project will contribute to the fulfillment of the strategic goals of the Republic of Serbia in the domain of natural gas and that its exemption, in accordance with the conditions specified in Article 288 of the Energy Law will enhance the security of natural gas supply of the Republic of Serbia, increase energy safety and safety of pipeline transmission of gaseous hydrocarbons, and be a significant contribution to more efficient and more ecologically friendly use of energy."

Article 288 paragraph 7 of the Law stipulates that the Agency, before rendering the act on exemption, shall decide on the rules and mechanisms for the management and allocation of capacities.

Article 288 paragraph 6 of the Law stipulates that when deciding on a request for exemption, the Agency shall, inter alia, consider non-discriminatory access to the new infrastructure.

With the Addendum, GASTRANS d.o.o. submitted a proposal of the volume and manner of allocation of capacity, proposing the following:

- the technical capacity of the Project pipeline (TCPP) represents the sum of the minimum required shareholder capacity (MRSC) and third party capacity (TPC) allocated in the binding phase of the Market Test;
- 88% is the minimum required capacity that needs to be allocated to the shareholders being the ultimate owners of the company and their subsidiaries, in order to enable financing of the Project,
- third party capacity (TPC) up to 12% is to be allocated in the following manner - third party capacity (TPC) represents the sum of third party capacities allocated in the binding phase of the Market Test (ATPC) and third party capacities unallocated in the binding phase of the Market Test (UTPC);
- UTPC also represents the remaining available third party capacity to be available to the shareholders or their related parties for subsequent booking in priority over third party transmission system users, which together with MRSC represents shareholder priority capacity. UTPC not booked by the shareholders or their related parties is third party capacity to be allocated after the commercial operation date (COD);

In addition to the Report on the Market Test results dated 30 April 2018, GASTRANS d.o.o. has also provided in the Addendum an analysis of the Market Test results, which are presented in the section "*Exemption from third party access*".

Since the requesting party specified in the Addendum that, according to the results of the conducted market test, the interest expressed by third parties (entities not being Related Parties, i.e. the ultimate owners of GASTRANS and their subsidiaries) is not such as to enable GASTRANS d.o.o. to construct the New Interconnector (the demand of third parties is only [.....] of the technical capacity), GASTRANS has assessed that without allocation of capacity to Related Parties, construction of the New Interconnector would not be financially or economically feasible.

After analyzing the Market Test results and the opinions of the neighboring NRAs, the Council of the Agency, acting in accordance with Article 288 paragraph 7 of the Law, before deciding on the request for exemption, has adopted a Decision on the manner of allocation and mechanisms for management of the transport capacities of the company GASTRANS d.o.o. number 40/2018-D-03/42, dated 3 September 2018 (hereinafter referred to as: "**Decision on allocation**"), by which it has partially accepted the proposal on the manner of allocation of capacities. By this Decision the Agency has obliged GASTRANS to allocate capacities to third parties in the binding phase, whereas all specified allocation rules may be applied if they are not in contravention of the act on exemption at the time of application.

II. Content of the Act on Exemption no. 40/2018-D-03/46 dated 1 October 2018 adopted by the Energy Agency of the Republic of Serbia in accordance with Article 288 paragraph 3 of the Law (hereinafter referred to as: Preliminary Act) and justification of the fulfillment of the specified conditions for approving exemption under Article 288 paragraph 1 items 1)-5) of the Law

Acting in accordance with the Initial Request and the Addendum (hereinafter referred to as: "**Request for Exemption**") submitted to the Agency in Serbian and in English, the Agency has analyzed the fulfillment of the specified criteria under Article 288 paragraph 1 items 1)-5) and determined in this procedure that all the specified criteria without which a positive decision on the request for exemption cannot be reached have been fulfilled.

Analyzing the decisive facts the Council of the Agency, acting in accordance with Article 288 paragraph 3 of the Law, adopted a Decision on exemption of the New Interconnector for natural gas No. 40/2018-D-03/46 dated 1 October 2018, which was published in the "Official Gazette of the Republic of Serbia" no. 74/2018), the adoption of which preceded the adoption of this Act (hereinafter referred to as: "**Preliminary Act**").

II. 1 Content of the disposition of the Preliminary Act

In the disposition of the Preliminary Act the Agency approved exemption from the obligation of ownership unbundling, the obligation of application of third party access rules (obligation of application of specified rules for natural gas transmission), and the obligation of application of regulated prices, for a period of 20 years. In the disposition of the Preliminary Act the Agency specified that:

1. it approves exemption from the obligation of ownership unbundling, so that GASTRANS d.o.o. can remain under the control of one or more companies or be part of a group of companies that are under the control of one or more companies which are conducting the activity of natural gas production or supply, and that GASTRANS d.o.o. is exempted from the ownership unbundling requirements under Article 224 paragraph 2 and Article 225 paragraph 1 items 1)-4) of the Law.

The disposition of the Preliminary Act obliges GASTRANS d.o.o. to protect the confidentiality of commercially sensitive information from access and discriminatory disclosure to the Related Parties of GASTRANS d.o.o., to which end GASTRANS d.o.o. is obliged to adopt and implement a Compliance Program and to have its enforcement

monitored by a compliance officer, while adoption of the Program, determining the conditions for appointing of the compliance officer and appointment of the compliance officer require the prior consent of the Agency.

At the same time, GASTRANS d.o.o. is obliged to independently conduct business operations and be organized separately from the Related Parties, along with other measures ensuring non-discriminatory operation of GASTRANS d.o.o. as a system operator approved exemption from ownership unbundling requirements.

2. it approves exemption from the obligation to apply rules on third party access, so that GASTRANS d.o.o. has the right to allocate and contract up to 88% of the maximum technical annual capacity of the New Interconnector (hereinafter referred to as: "Priority Capacity"), for a period not exceeding the duration of the exemption, to the companies Gazprom export LLC and JP Srbijagas (hereinafter referred to as "EPA Parties"), whereas the remaining 12% of the maximum technical annual capacity of the New Interconnector may be allocated in accordance with the Decision on allocation of capacities and contracted to third parties other than the EPA Parties that submitted non-binding bids upon Public Invitation of GASTRANS d.o.o. dated 5 March 2018, for a period not exceeding the duration of the exemption.

In the Preliminary Act the Agency approved that if in any year demand for the long-term capacity is lower than the technical capacity at the entry point or exit points (in accordance with the expected technical design of the project of the New Interconnector), GASTRANS d.o.o. may adjust expected technical design and technical capacity of the New Interconnector as close as possible to the technical design required to meet all allocated long-term capacities and short-term capacities, so that the capacity allocated as long-term capacity shall amount to 90% of the capacity of the New Interconnector and the remaining 10% of the capacity of the New Interconnector shall be allocated as short-term capacity of the New Interconnector on a non-discriminatory basis, whereby capacity of the New Interconnector in sum shall not exceed the maximum technical annual capacity. GASTRANS d.o.o. shall base this technical design and technical capacity adjustment of the New Interconnector on the results of the binding phase of the Market Test, considering offers for capacities requested for periods shorter than duration of exemption. At the same time, the Agency approved that if GASTRANS d.o.o. does not adjust the technical design and technical capacity, GASTRANS d.o.o. shall:

- 1) in case part of the 88% of the maximum technical annual capacity remains unallocated to EPA Parties on a long-term basis, offer this unallocated capacity on a short-term basis, provided that EPA parties have priority in booking; and
- 2) in case part of the 12% of the maximum technical annual capacity offered to third parties remains unallocated, offer this unallocated capacity as short-term capacity, on a non-discriminatory basis.

Furthermore, unless otherwise agreed with adjacent TSOs, short term capacity shall be allocated applying the auction method, for the entire duration of the exemption. The reserve (initial) price at the auction shall be determined according to the applicable tariffs for the exempted long term capacity of the New Interconnector at the entry and exit points, which prices shall be determined in accordance with the GASTRANS d.o.o.'s methodology determining the prices of long-term natural gas transmission services.

GASTRANS d.o.o. is instructed to, at least every six years, or at any time as GASTRANS d.o.o. deems necessary, verify the interest of the market for expansion of capacity of the New Interconnector and, provided that this is economically justified, prepare an investment plan and submit such investment plan to the Agency for approval pursuant to the Article 250 of the Law.

3. it approves exemption from the obligation to apply regulated prices, with the obligation of GASTRANS to ensure that:

- The tariffs for long-term contracted capacities of the New Interconnector (Tariffs) shall be transparent, non-discriminatory and equal for all users of the exempted capacities, with the goal of securing the covering of the costs of efficient operation and objective investment risks, and shall be formed for each year and expressed in €/kWh/h/a.

- GASTRANS d.o.o. shall apply nominal flat Tariffs starting from the year in which exit Horgoš is fully operational for the entire year and thereafter.

- The Tariffs shall be formed by allocating the necessary income to contracted long-term firm capacities at the entry and exits during the exemption period, so that the same weight shall be applied at distribution, namely 0.5 at the entry and 0.5 at all exits, and all exits intended for delivery to end users of natural gas in the Republic of Serbia shall be treated as one (virtual) exit, which ensures a uniform Tariff for all exits in the Republic of Serbia.

- The necessary income for all years during which exit Horgoš is fully operational for the entire gas year is defined as the sum of operational costs, maintenance costs, costs for compensation of natural gas loss, depreciation costs and necessary return on CAPEX. The necessary income shall be decreased by all income from sale of capacities that have not been contracted as long-term firm capacities, or have been contracted but are not being used, and shall be adjusted by a correction element.

- The Tariff may be amended in accordance with the methodology.

- The depreciation cost referring to transmission assets of natural gas shall be calculated using pro rata method over 40 years.

- The necessary income for the first year of operation and the years before exit Horgoš is fully operational for the entire year shall not include depreciation costs and necessary return on CAPEX.

- The Tariffs for the respective entry and exit points shall be determined as the quotient of the part of the necessary income distributed to that entry or exit point and contracted capacities. Allocation of the necessary income between exit points shall be carried out depending on capacity and transport distance from entry to exit points. For the years after the first year of operation until exit Horgoš becomes fully operational for the entire year, the Tariffs shall be determined based on the ratio between the Tariffs for the first year of operation and the projected Tariffs for the first year in which exit Horgoš is fully operational for the entire year and the respective average growth rates in that period. In the event that exit Horgoš becomes operational partway through the year in which it starts operating, the tariff for that exit shall be determined by multiplying the exit tariff for Serbia in the year preceding the full exploitation of capacity with the estimated ratio of the tariff for the exit towards Hungary divided by the tariff for exits in Serbia in the subsequent year.

- The Tariffs for long-term contracted reverse capacity (virtual reverse flow) shall be 90% of the relevant Tariff for long-term firm capacity.

- The Tariffs for each gas year shall be determined in the above described manner, and shall be adjusted annually by way of a correction element adjusting the necessary income by the amount of deviation of the actual realized necessary income calculated in accordance with the methodology in the previous year from the estimated necessary income. The correction element shall not be calculated before the year in which exit Horgoš is fully operational for the entire year.

- GASTRANS d.o.o. shall, no later than 60 days before the beginning of the transmission service and before annual adjustments, form the Tariffs for the long-term firm and reverse capacity in accordance with this Act, based on the relevant data and documentation on current elements of the necessary income and data on contracted capacities and distance between the entry and exit points.

- GASTRANS d.o.o. shall be obliged to submit economic and financial data and documentation to the Agency by the following deadlines:

- Tariff calculation, data and documentation reflecting the current elements of the necessary income, and calculation of the correction element for the previous year, no later than 90 days before the tariffs enter into force.

- Other data and documentation within the deadline specified in the act regulating the manner, procedure and deadlines for bookkeeping records, separating accounts by business activities and submitting data and documentation for the purpose of regulation.

In addition to the above, the Agency also approved exemption from certain obligations accepted by the Republic of Serbia on the day of adopting Decision 2018/07/ of the Permanent High Level Group of the Energy Community (PHLG EnC) in the part in which the Energy Community adapts Chapter III of Commission Regulation (EU) 2017/460

establishing a network code on harmonized transmission tariff structures for gas, which the Republic of Serbia has accepted to implement so that it shall become part of the legal system of the Republic of Serbia, the application of which shall not be compatible with the approved exemption.

Finally, the Agency has obliged GASTRANS to obtain certification before the start of commercial operation, whereby the conditions under Articles 224 and 244-246 of the Law shall be considered fulfilled.

II. 2. Justification of fulfillment of prescribed conditions for approving exemption under Article 288 paragraph 1 items 1)-5) of the Law

Article 288, paragraph 13 of the Law stipulates that the competent authority, in accordance with the obligations arising from confirmed international agreements, may issue a decision requiring the Agency to amend or withdraw the act on exemption.

Article 288, paragraph 13 of the Law stipulates that in case that the competent authority issues the decision under Paragraph 12 of this Article, the Agency shall take this decision into account to the greatest possible extent.

Article 288, paragraph 14 of the Law stipulates that where the final decision of the Agency diverges from the opinion of the competent authority, the Agency shall provide and publish, together with that decision, the reasoning underlying its decision.

1. *The Agency has established that GASTRANS d.o.o. has legitimation/right to participate in respective proceedings in this matter, considering the fact that it is not a transmission system operator in the Republic of Serbia, and that it plans to build an interconnector and to acquire ownership of the interconnector on the basis of the construction thereof, in order to operate said new interconnector as an independent natural gas transmission system operator, which is a condition for approving exemption prescribed in Article 288 paragraph 1 Item 3) of the Law. Since for this reason in the part of the Request for Exemption from the obligation of ownership unbundling the requesting party requested not to be exempted from the application of Article 224 paragraph 1 of the Law which stipulates the obligation of the system operator to be the owner of the transmission system, which corresponds to the content of Article 288 paragraph 1 point 3) of the Law, the disposition of this Act therefore does not approve exemption from the obligation of application of Article 224 paragraph 1 of the Law which regulates the obligation of the operator to be the owner of the transmission system.*

2. *The Agency has determined that the Request for Exemption is permissible considering that:*

A. *The Project pipeline is an important gas infrastructure constructed in full as a new infrastructure within the meaning of Article 288 paragraph 1 and Article 2 item 46) of the Law, for which the Law permits exemption. This is due to the fact that the new pipeline is planned to pass through the territory of the Republic of Serbia in the length of about 400 km and cross the state border of the Republic of Serbia, so that the entry point is at the interconnection with the transmission system of the Republic of Bulgaria, and the final exit point at the location of Horgoš, so that the pipeline crosses the state border of the Republic of Serbia with Hungary, in order to connect to the adjacent system operators in the Republic of Bulgaria (operated by BULGARTRANGASZ EAD) and in Hungary (operated by FGSZ), from where it is possible to supply the Hungarian and/or neighboring Central European markets, connecting the entry points of the Project pipeline to the capacities planned to be built by BULGARTRANGASZ EAD for delivery to the market of the Republic of Serbia. The Agency has taken into account that the described technical characteristics of the Project pipeline in the Request for Exemption are preliminary, because the front-end engineering and design (FEED) is not yet complete, wherefore the final technical parameters shall be known at a later date.*

B. *The Project pipeline is a gas interconnector within the meaning of Article 2 item 25) of the Law, which defines the term "interconnector" as an electricity transmission line, gas pipeline, oil pipeline or product pipeline that crosses the border between countries for the purpose of connecting their systems, as well as the equipment that is used for connecting the energy systems.*

In determining that the Project pipeline is an interconnector the Agency took into account the following:

1) Article 2(17) of the Gas Directive which defines an interconnector as "a transmission line which crosses or spans a border between (EU) Member States for the sole purpose of connecting the national transmission systems of those Member States", and

2) Article 2(17) of the Implementing Decision by which the Energy Community Ministerial Council adapted the term "interconnector" for the requirements of the Energy Community so that it means "a transmission line which crosses or spans a border between Contracting Parties for the sole purpose of connecting the national transmission systems of those Contracting Parties", (thereby excluding those transmission lines that cross the border between a Contracting Party and an EU Member State, having in mind Article 2(17) of the Gas Directive).

3) There are differences in the characteristics of transmission lines that "cross" a border and that "span" a border (the term "interconnector" in the Gas Directive and the Implementing Decision) is more precise than the term "interconnector" in Article 2 item 25) of the Law, which specifies that the transmission line crosses the border between states for the purpose of connecting to neighboring systems.

In this regard, the Agency has determined that the New Interconnector fulfills the conditions specified in Article 2 item 25) of the Law to be qualified as a gas interconnector, although Article 2(17) of the Gas Directive of the EU and the Implementing Decision of the Energy Community do not treat as an interconnector a pipeline crossing the border between a Contracting Party and an EU Member State, whereas the Implementing Decision transposing Article 2(17) of the Gas Directive into the Energy Community is contrary to Article 2 item 25) of the Law).

However, having in mind that:

- The opinion of the Ministerial Council of the Energy Community dated 23 September 2014 no. 2014/01/MC specifies in Article 2 that "pipelines crossing the border between Contracting Parties and EU Member States shall be treated in the same way as those crossing the border between Contracting Parties, and all provisions regarding flow, export, import, transactions, capacity and infrastructure shall apply to them", which has been confirmed by the European Commission in its Recommendation dated 29 October 2014.

- In practice the Energy Community approved an exemption for the interconnector in the TAP Project², and the European Commission for the interconnector "Nabucco Project", in which it specified that any other treatment would be discriminatory and that designating these pipelines as interconnectors is in accordance with the goals of the Energy Community because they ensure connecting of markets even when crossing the border between a Contracting Party (or Third Party) and EU Member States.

- According to its technical characteristics the Project pipeline is not contrary to existing pipelines with similar characteristics that have been exempt in the EU and the Energy Community (exemption of BBL - pipeline passes across water between Member States, connecting beach to beach; Gazelle, OPAL, SK-HU Interconnector - pipeline crosses one Member State and reaches over short distance into another Member State; TAP - pipeline passes across water, starting in the territory of one Member State, spans a Contracting Party and another Member State and reaches into a Third Country; and Nabucco - pipeline crosses multiple Member States and reaches into a Third Country). Based on the aforesaid, the Agency has found that the routing of the Project pipeline resembles the routing of Gazelle, OPAL and the SK-HU Interconnector. In the case of OPAL, the majority of the pipeline passes through the German territory and reaches over the border with the Czech Republic, connecting with the Czech NTS 300 meters from the border, which is the case with the Project of GASTRANS d.o.o. as well.

- The procedure of harmonization of technical characteristics and the exact location at the point of connection is in progress, and has not been completed.

The Agency, applying Article 2 item 25) of the Law (transposing Article 2(17) of Directive 2009/73/EC, without discrimination), has approved exemption of the Project because it has found that the prescribed conditions have been fulfilled and that approving this pipeline as a new gas interconnector is not in contravention of the practice of the EU and the Energy Community.

3. The Agency took into account the Opinion of the Ministry of Mining and Energy of the Republic of Serbia before issuing the act on exemption (Article 288 paragraph 3 of the Law)

² item 25 and 26 of the Opinion ECS 1/2013 on exemption on TAP interconnector from the requirements in compliance with directive 2009/73 approved by Albanian regulatory energy authority (ERE)

Article 288, paragraph 3 of the Law stipulates that the act on exemption shall be issued by the Agency upon obtaining the opinion of the Ministry in charge of energy matters. Acting in accordance with Article 288 paragraph 3 of the Law, the Agency requested by letter dated 11 July 2018 the opinion of the Ministry of Mining and Energy, prior to issuing the act on exemption (Preliminary Act).

The Ministry of Mining and Energy by its letter no. 312-01-00677/2018-05 dated 18 July 2018 submitted the requested opinion to the Agency, notifying it that construction of the new interconnector would enhance the security of supply of natural gas in the Republic of Serbia. This opinion is provided in full, and reads as follows:

"Article 7 paragraph 2 of the Law on Ministries ("Official Gazette of the Republic of Serbia", no. 44/14, 14/15, 54/15, 96/15 - other Law and 62/17) stipulates that the Ministry of Mining and Energy, among other matters, performs state administration affairs relating to: energy policy and energy development planning, energy balance of the Republic of Serbia, gas economy strategy and energy security policy, development of annual and medium term energy security programs and provision of material and other conditions for the realization of these programs. The Energy Policy of the Republic of Serbia was established by the Energy Development Strategy.

The Energy Development Strategy as the strategic priorities of the energy sector development of the Republic of Serbia, for the mentioned period, defines: ensuring energy security, development of the energy market and transition to a sustainable energy.

The strategic goals of the Republic of Serbia in the field of natural gas are: ensuring safe supply of the domestic natural gas market, establishment of domestic and regional natural gas market and diversification of sources and directions of natural gas supply achieved through the following strategic directions of operation: country research for the purpose of finding new natural gas deposits, use of natural gas as a replacement for the consumption of electricity for heat needs, use for combined production of electricity and heat in the industry and bigger cities, participation in international projects of natural gas transmission; and regional connectivity.

The Republic of Serbia's natural gas market is supplied from domestic sources and mainly from imports. Annual energy needs, i.e. energy products expressed at the monthly level, which it is necessary to provide for the reliable, safe and quality supply of end customers, while observing the needs for rational consumption of energy and energy products, sources of providing the necessary quantities of energy, i.e. energy products, as well as the required level of supplies and spare capacities of energy, facilities for safe supply of customers with energy and energy products are determined by the Energy Balance of the Republic of Serbia. The total amount of natural gas needed for consumption in 2018, planned by the Energy Balance of the Republic of Serbia for 2018 ("Official Gazette of the Republic of Serbia", no. 119/2017) is 2,483.074 million m³ of which 18% shall be provided from domestic production and 82% from imports.

The projection of natural gas consumption has a long-term growth trend, with an expected consumption of about 4,000 million m³ by 2030.

The natural gas transmission system of the Republic of Serbia has two interconnections with other gas pipelines, one entry point at the border with Hungary (Kishkundozhma) and one exit point at the border with Bosnia and Herzegovina.

The total length of the natural gas transmission system in the Republic of Serbia is about 2460 km, of which 95% is owned by SRBIJAGAS, while the remaining 5% is owned by PREDUZEĆE ZA IZGRADNJU GASOVODNOG SISTEMA, TRANSPORT I PROMET PRIRODNOG GASA YUGOROSGAZ a.d. BEOGRAD (in English: Company for the construction of gas pipelines, transmission and natural gas distribution Yugorosgaz a.d. Belgrade) (hereinafter referred to as: "**Yugorosgaz**").

The activity of transmission and management of the natural gas transmission system in the Republic of Serbia is performed by two transmission system operators: SRBIJAGAS and DRUŠTVO SA OGRANIČENOM ODGOVORNOŠĆU YUGOROSGAZ-TRANSPORT NIŠ (hereinafter referred to as: "**Yugorosgaz-Transport**"). The harmonization of the business operations and organization of these undertakings is in progress in accordance with the provisions of the Law.

In addition to the abovementioned, participants in the natural gas market are the following energy entities: 65 natural gas suppliers, 33 natural gas public suppliers, 33 distribution system operators, one natural gas storage operator and around 270,000 end customers.

For the gas sector of the Republic of Serbia, the realization of a gas pipeline would be of great importance, which would enable a new direction of natural gas supply and which would improve the security of supply of natural gas in the entire region in the future period. The realization of interconnections with countries in the region and the construction of a new direction of natural gas supply would enable more significant use of natural gas, as well as its use for combined heat and power generation and use in the traffic sector (compressed natural gas)."

In accordance with the above, the opinion of the Ministry is that realization of the described project will contribute to the fulfillment of the strategic goals of the Republic of Serbia in the domain of natural gas and that its exemption, in accordance with the conditions specified in Article 288 of the Energy Law will enhance the security of natural gas supply of the Republic of Serbia, increase energy safety and safety of pipeline transmission of gaseous hydrocarbons, and be a significant contribution to more efficient and more ecologically friendly use of energy."

4. The Agency exchanged opinions with the neighboring NRAs before deciding on the request for exemption (Article 288 paragraph 9 of the Law)

Article 288 paragraph 9 of the Law stipulates that act on exemption may be issued after exchanging opinions with the other countries on which the construction of the infrastructure has an impact, or with the competent regulatory bodies of such countries.

The Agency acted in accordance with Article 288 paragraph 9 of the Law by its letter no. 40/2018-D- 03/25 dated 13 July 2018 and in attachment thereto forwarded to the Bulgarian NRA and Hungarian NRA the Proposal of the act which GASTRANS submitted in attachment to the Addendum, detailing the ratio and manner of allocation of capacities in the binding phase. By this letter the Agency requested that the neighboring regulatory authorities provide their statements relating to the acceptability of the proposed method of allocation requested by GASTRANS, and provide the Agency with their opinions on the impact of the new infrastructure on their natural gas markets.

[.....]

5. The Agency examined the fulfillment of the prescribed criteria for approving exemption stipulated in Article 288 item 1)-5) of the Law

Article 288 paragraph 1 of the Law prescribes that new gas infrastructure facilities, i.e. interconnectors and storage facilities, may, upon request, be exempted from the application of Article 224 of the Law (obligation of ownership unbundling) and right to access to the system at regulated prices specified in Article 283 paragraph 1 of the Law, under the following conditions:

- 1) the investment into the new infrastructure facility must enhance competition in gas supply and enhance security of supply;
- 2) the level of risk attached to investing into new infrastructure facility must be such that the investment will not take place unless an exemption is granted;
- 3) the new infrastructure facility must be owned by a natural or legal person operating in a different business entity separated from the system operators in whose systems that new infrastructure will be built;
- 4) charges for use of the infrastructure facility must be levied on the users of that infrastructure; and
- 5) the exemption must not be detrimental to competition, to the effective functioning of the internal market in natural gas, or to the efficient functioning of the regulated system to which the infrastructure is connected.

Analyzing the conditions specified in Article 288 paragraph 1 items 1)-5) of the Law, the Agency determined that:

1) The investment in the new infrastructure facility enhances competition on market and security of supply

1a) Assessing the criterion of enhancement of security of supply

The Agency obtained the opinion of the Ministry of Mining and Energy, as mentioned above, which indicates that the New Interconnector would enhance the security of supply in the Republic of Serbia.

At the same time the Agency examined the statements of the requesting party relating to fulfillment of the criterion of enhancement of security of supply based on the data submitted in attachment to the Addendum: Analysis of the natural gas market, point 5.1. of the Addendum (*Overview of the Serbian natural gas market*), in which GASTRANS d.o.o. provided data, assessments and explanations for:

1. The current and forecast balance between supply and consumption of natural gas, including the percentage of supplies of the relevant market expected to be covered by the Project, as described in detail in Chapter E of the Market Study (Schedule 4 to the Addendum), developed by BLUBERRIES GmbH for GASTRANS d.o.o.

2. Confirmation of the Project capacity based on the balance between supply and consumption of natural gas and assessing the capacity of existing supply routes including information on how the Project provides the requested capacities required for the national and regional markets it intends to supply.

3. Natural gas sources and information on agreements on supply or long-term transmission of natural gas. This criterion is less relevant if the capacities are allocated short-term, and considering that in the non-binding phase of the Market Test, [.....], it is stated that it can be expected that part of the capacity of the New Interconnector which will be allocated on a short-term basis will enable transporting natural gas from other sources that are not currently available, but shall be available in the future.

In order to assess the fulfillment of this criterion, the Agency applied the criteria which the Energy Community recommends and uses in exemption procedures, when assessing the fulfillment of the condition relating to enhancing the security of supply³. These criteria and results were detailed by the Agency in the reasoning of the disposition of the Preliminary Act, pointing out that the Project fulfills all the prescribed criteria as detailed below:

Criterion 1 – whether the project contributes to diversification of the supply of the relevant market, in particular allowing the transport of natural gas from a new source of supply or simply by opening a new supply route from an existing supply source

The Agency has assessed that the New Interconnector enables transmission of natural gas from a new supply source and opens a new supply route from the existing supply source. Although one of the primary sources for natural gas is Russian natural gas, a wide range of alternative sources could, in the opinion of the Agency, potentially supply gas (through the Bulgarian interconnection with Romania, Turkey, and Greece), subject to the realization of some project currently under consideration.⁴ These include: (1) Azerbaijani natural gas, via Turkey, Greece, Bulgaria, (2) gas from Romania (being a substantial natural gas producer in the region); and (3) LNG import terminals in Greece and Turkey which offer access to international natural gas, such as, for example, LNG from Qatar, USA, and Russia. The Agency believes that this criterion is fulfilled because the Project as a new infrastructure enhances the security of supply since it contributes to diversification not only of supply routes for the relevant market, but potentially to diversification of supply sources as well.

Criterion 2 – whether the project contributes to achieving security of supply to households

The Agency had determined that the New Interconnector in accordance with EU Recommendation 2004/67/EC replaced in 2010 by Regulation (EU) No 994/2010, and then by Regulation 2017/1938, ensures the infrastructure standard in case of interruption of the single largest gas infrastructure. This standard is determined to assess whether in the event of a disruption of the single largest gas infrastructure, the technical capacity of the remaining infrastructure is able to satisfy total gas demand during a day of exceptionally high gas demand occurring with a statistical probability of once in 20 years.

The infrastructure standard is fulfilled when the condition that $N-1 (\%) \geq 100\%$ is satisfied.

The analysis shows that:

- Construction of the New Interconnector significantly increases fulfillment of the infrastructure standard in the Republic of Serbia from 33.8% to 114%.

³ Commission staff working paper – New infrastructure exemptions 06 May 2009

⁴ For more detailed exposition of alternative sources, please see the Market Study of BLUBERRIES section E(i),

- Construction of pipelines in Turkey and Bulgaria which are necessary for delivery of natural gas to the New Interconnector significantly increases fulfillment of the infrastructure standard in the Republic of Bulgaria from 62.8% to 175.6%.
- Construction of the New Interconnector increases fulfillment of the infrastructure standard in Hungary from 124.5% to 151%.

Accordingly, the Agency believes it is clear that the construction of the New Interconnector will significantly improve the achievement of security of supply to households not only in the Republic of Serbia, but also in the Republic of Bulgaria and Hungary, as presented below.

For the purpose of the analysis the Agency has presented the following proof:

$$N-1 (\%) \text{ is calculated as follows: } N-1(\%) = \frac{E_{pm} + P_m + S_m - I_m}{D_{max}} * 100$$

where:

E_{pm} (in million m^3/d) – means the sum of the technical capacity of all entry points from another transmission system capable of supplying gas to the relevant geographic area;

P_m (in million m^3/d)- means the maximal technical natural gas production capability which can be delivered to the entry points to the transmission system;

S_m (in million m^3/d)– means the maximal technical withdrawal capacity which can be delivered to the entry points to the transmission system from the underground gas storage facility;

I_m (in million m^3/d) – means the technical capacity of the largest entry point to the transmission system;

D_{max} (in million m^3/d) – means the total daily gas demand during a day of exceptionally high gas demand occurring with a statistical probability of once in 20 years.

N-1 standard in the Republic of Serbia

In EU countries where transmission pipelines are also used for transit to other countries, there are two ways to calculate fulfillment of the infrastructure standard. The first calculates the entire capacity at the border entry point from another country as entry capacity. The second decreases the capacity at the border entry point by the contracted capacity at the transmission system exit for transit requirements. Applying the second approach, it is possible for the infrastructure standard not to be fulfilled, even though it was fulfilled when applying the first approach. For examining the fulfillment of the N-1 standard in the Republic of Serbia the first approach will be applied, since the same way of calculating the N-1 standard was applied for the Republic of Bulgaria and Hungary.

The capacity values in the Republic of Serbia in 2017 were as follows:

E_{pm} – Entry point Horgoš / Kiskundorozsma 13 million m^3/d ;

P_m - natural gas production 1.5 million m^3/d ;

S_m - PSG Banatski Dvor 5.2 million m^3/d ;

I_m - Entry point Horgoš / Kiskundorozsma 13 million m^3/d

D_{max} –17.274 million m^3/d (estimate based on air temperature and consumption on 9 February 2012).

$$N-1(\%) = \frac{13 + 1.5 + 5.2 - 13}{17.274} * 100$$

$N-1(\%) = 38.8\%$ - the infrastructure standard is not fulfilled

Constructing the New Interconnector will increase the capacities at the entry points into the Republic of Serbia by 38.0 million Sm³/d.

$$N - 1(\%) = \frac{38 + 13 + 1.5 + 5.2 - 38}{17.274} * 100$$

$N - 1(\%) = 114.0 \%$ - the infrastructure standard is fulfilled

In the Addendum GASTRANS d.o.o. did not specify the reverse capacity of the New Interconnector at the exit Horgoš. Existence of reverse capacity at the exit Horgoš would certainly contribute to the further increase of fulfillment of the infrastructure standard. Construction of the New Interconnector will increase the value of fulfillment of the infrastructure standard from 38.8% to 114.0%. Before the start of commercial operation of the New Interconnector at 100% of the planned capacity, GASTRANS d.o.o. and the transmission system operator in Hungary need to jointly define the reverse flow capacity of the New Interconnector at the exit Horgoš.

The Report on the role of gas storage in internal market and in ensuring security of supply⁵ contains calculations of the N-1 standard for all EU countries, including Hungary and the Republic of Bulgaria.

N-1 standard in the Republic of Bulgaria

Table A.4.2. of the Report on the role of gas storage in internal market and in ensuring security of supply shows the following data for the Republic of Bulgaria:

Epm1 – entry point from Romania 20.3 million m³/d;

Epm2 – entry point from Greece (reverse flow capacity) 3.5 million m³/d;

Epm3 – entry point from interconnector Romania-Bulgaria 1.4 million m³/d;

Pm - natural gas production 2.2 million m³/d;

Sm - underground storage 4.2 million m³/d;

Im - Entry point from Romania 20.3 million m³/d;

Dmax - 18 million m³/d.

$$N - 1(\%) = \frac{20.3 + 3.5 + 1.4 + 2.2 + 4.2 - 20.3}{18} * 100$$

$N - 1(\%) = 62.8 \%$ - the infrastructure standard is not fulfilled

The pipeline that will be constructed in the Republic of Bulgaria will be connected with the New Interconnector in the Republic of Serbia, and by one branch of the pipeline with TurkStream in Turkey as well. The capacity of one branch of the TurkStream pipeline, based on the information from the GAZPROM official website, is 17.75 billion m³ per year, or 43.1 million m³/d. Including the capacity of this entry point into the N-1 formula produces a new value for the N-1 standard:

$$N - 1(\%) = \frac{43.1 + 20.3 + 3.5 + 1.4 + 2.2 + 4.2 - 43.1}{18} * 100$$

$N - 1(\%) = 175.6 \%$ - the infrastructure standard is fulfilled

5 - <https://ec.europa.eu/energy/sites/ener/files/documents/REPORT-Gas>

In the Addendum to the Request for Exemption GASTRANS d.o.o. did not specify the reverse capacity of the New Interconnector at the entry point. Existence of reverse capacity at the entry point would contribute to the further increase of fulfillment of the infrastructure standard for the Republic of Bulgaria, so before the start of commercial operation of the New Interconnector at 100% of the planned capacity, GASTRANS d.o.o. and the transmission system operator in the Republic of Bulgaria should jointly define the reverse flow capacity of the New Interconnector at the entry point.

N-1 standard in Hungary

Table A.9.4. of the Report on the role of gas storage in internal market and in ensuring security of supply shows the following data for Hungary:

Epm1 – entry point from the Ukraine 56.3 million m³/d;

Epm2 – entry point from Austria 14.4 million m³/d;

Epm3 – entry point from Slovakia 12.0 million m³/d;

Epm4 – entry point from Romania 4.8 million m³/d;

Epm4 – entry point from Croatia 19.2 million m³/d;

Pm - natural gas production 6.9 million m³/d;

Sm - underground storage 72.8 million m³/d;

Im - entry point from the Ukraine 56.3 million m³/d;

Dmax - 104.5 million m³/d.

$$N - 1(\%) = \frac{56.3 + 14.4 + 12 + 4.8 + 19.2 + 6.9 + 72.8 - 56.3}{104.5} * 100$$

N – 1(%) = 124.5 % - the infrastructure standard is fulfilled

Construction of the New Interconnector secures a new entry for Hungary, with capacity of 27.6 million m³/d.

Including this entry point into the N-1 formula produces a new value for the N-1 standard.

$$N - 1(\%) = \frac{56.3 + 14.4 + 12 + 4.8 + 19.2 + 27.6 + 6.9 + 72.8 - 56.3}{104.5} * 100$$

N – 1(%) = 151.0 % - the infrastructure standard is fulfilled

The Agency's analysis shows that by application of the formula for determining the infrastructure standard, construction of the New Interconnector significantly increases fulfillment of the infrastructure standard in the Republic of Serbia from 33.8% to 114%, in the Republic of Bulgaria from 62.8% to 175.6%, and in Hungary from 124.5% to 151%, wherefore the Agency has assessed that based on the above, it has been established that the New Interconnector will improve the security of supply to households in the Republic of Serbia, Republic of Bulgaria and Hungary.

Criterion 3 - Security of supply is increasing if new infrastructure allows the flexibility of natural gas sources on the market. The flexibility of natural gas sources on the market is realized through enabling the import of natural gas from several sources and allowing part of the capacities to be contracted in the short-term

The analysis shows that construction of the New Interconnector will enable, for the natural gas market in the Republic of Serbia, but also for the South-East Europe (SEE) region, the import of natural gas from other sources as well, as

compared to import from the Russian Federation (the closest other source is natural gas from the Black Sea, which has proven reserves, and on the basis of which Romania is planned to become a natural gas exporter in 2022), having in mind that the capacity of the pipeline connecting the Romanian and Bulgarian transmission systems exceeds 20 million m³/d. The second additional source is natural gas from Azerbaijan from the Shah Deniz 2 gas field. Natural gas from this gas field is planned to be transported via the TAP pipeline from 1 January 2020, from Turkey through Greece, Albania to Italy. Natural gas from the Shah Deniz 2 gas field could be transported to the New Interconnector by route Turkey, Bulgaria, when transport of natural gas from Turkey towards the Republic of Bulgaria is enabled, or by route Turkey, Greece, the Republic of Bulgaria when the IGB interconnector is constructed. The third additional source of natural gas is natural gas from LNG terminals in Turkey and Greece. Natural gas from various countries can be regasified in the LNG terminals. Natural gas from the LNG terminals in Turkey would be transported to the New Interconnector by route Turkey, the Republic of Bulgaria, and from the LNG terminals in Greece by way of the IGB interconnector. Potential natural gas sources also include natural gas from Iraq, Iran, and the Mediterranean Sea, when the transport infrastructure is constructed. Therefore it is concluded that this criterion is fulfilled, because the New Interconnector will enable new supply routes but also the possibility of supply of gas from other sources (diversification of supply of the natural gas market in the Republic of Serbia and in South-East Europe).

Criterion 4 – The larger the project compared to the size of the market, the greater the security of supply

The Agency considered the fact that natural gas consumption in the Republic of Serbia and Bosnia and Herzegovina in 2017 amounted to 2.805 billion m³, while import amounted to 2.448 billion m³, and that the capacity of the exit points of the New Interconnector enables delivery of [.....]. Since natural gas consumption in Hungary in 2016 amounted to 9.745 billion m³, while import amounted to 7.951 billion m³, and the capacity of the exit point of the New Interconnector towards Hungary enables delivery of [.....], the Agency has assessed that the New Interconnector has a sufficient capacity relative to the natural gas market in the Republic of Serbia and South-East Europe to increase the security of supply.

Based on the above, the Agency considers that the New Interconnector increases the security of supply of natural gas in the Republic of Serbia and the SEE region, given that it fulfills all four criteria for increasing the security of supply as defined by the EU Commission.

1b) Increasing market competitiveness

The Agency has based its assessment of the fulfillment of this criterion on the content of the Market Study analyzing the Serbian natural gas market and the natural gas market in the region of South-East Europe, submitted by GASTRANS d.o.o. as Schedule 4 of the Addendum.

In the Market Study analyzing the impact of construction of the New Interconnector on the Serbian natural gas market and on the natural gas market in the region of South-East Europe, the requesting party specifies that construction of the New Interconnector will increase competition on the natural gas market in the Republic of Serbia in two ways. Firstly, by increasing the capacities for importing natural gas; the increased possibility of supply will in turn increase demand for natural gas, because increased possibility of supply creates conditions conducive to lowering the price of natural gas, solely based on the increased liquidity of the market, regardless of the structure of the natural gas market in the Republic of Serbia. Secondly, the New Interconnector will have a positive effect on competition on the Serbian natural gas market because it is expected to enable restriction of the prices set by Gazprom Export, if they are higher than the prices of natural gas of other suppliers with access to the Serbian natural gas market.

The Study specifies that the New Interconnector will increase the competitiveness of the natural gas market in the Republic of Serbia, because according to the conclusions of this Study: 1) it opens new routes for transporting natural gas in the opposite direction (south-north) from the existing routes for transport of natural gas (north-south) in the Republic of Serbia and the SEE region; 2) it enables import of natural gas into the Republic of Serbia and Hungary from sources that were previously unavailable, such as natural gas from Romania, natural gas from Azerbaijan, natural gas from LNG terminals in Greece and Turkey, and potentially other sources as well; 3) it increases the liquidity of the only relatively liquid gas hub in the region - Baumgarten in Austria; and 4) it enables the importing of natural gas from

Central Europe into the Republic of Bulgaria via the reverse flow of the New Interconnector. The requesting party states that all the factors listed above will together facilitate reduction of natural gas prices both in the Republic of Serbia and the region, and an increase in the consumption of natural gas as a result of inter-fuel substitution.

The Study further proves that the New Interconnector will promote inter-fuel competition, because the Republic of Serbia, and the region at large has potential for natural gas to substitute other less environmentally friendly fossil fuels such as oil and coal, and this potential, combined with increased supply and lower prices, should enable natural gas to gain new market share and engage in other markets that were previously unavailable due to either price or availability factors, wherefore the Market Study concludes that the New Interconnector will increase competition on the Serbian natural gas market and the natural gas market in the region of South-East Europe.

The Agency's analysis of the natural gas market in the Republic of Serbia and the SEE region

Natural gas sources

The only countries in Europe in which natural gas production exceeded natural gas consumption in 2017 were Norway, the Netherlands and Denmark. Because of decreased natural gas production, Denmark⁶ will become a net importer of natural gas as from 2020, as potentially will the Netherlands⁷ as from 2022 due to a decrease in the production of natural gas from the Groningen gas field. It is economically justified for natural gas to be sold as closely as possible to the place of production, so natural gas from Norway, the Netherlands and Denmark was primarily sold in the markets of Northern and Western Europe. The countries of South-East Europe, including the Republic of Serbia, could not and cannot in future count on the natural gas produced in those three countries. Given that in almost all countries in North, West, Central, South and South-East Europe natural gas production is less than their natural gas consumption, GAZPROM OAO has emerged as the dominant supplier of natural gas to the countries of South-East Europe. In the region of South-East Europe, apart from natural gas from the Russian Federation, natural gas can be obtained from other sources as well, so a potentially cost-effective source of natural gas in the Republic of Serbia, as well as in the region of South-East Europe, is natural gas from Romania. Another potential source of natural gas in the Republic of Serbia and in the SEE region is natural gas from Azerbaijan, when physical transport of that natural gas to the Republic of Bulgaria is enabled from Turkey or from Greece. Finally, another source of natural gas could be natural gas from the LNG regasification terminals in Greece and Turkey. The closest LNG terminal is in Greece, near Athens. LNG terminals in Europe for the most part have the role of enabling delivery of natural gas from sources that cannot be connected to the European system by pipeline. However, commercially speaking, natural gas from the LNG terminals is usually more expensive than natural gas transported by way of gas pipelines. Hypothetical sources of natural gas in the Republic of Serbia and the SEE region are natural gas from Iraq, Iran and the Mediterranean Sea. The downside of these sources is the length of the transport route for natural gas from Iraq and Iran. For natural gas from the Mediterranean Sea, from the territorial waters of Israel, Egypt and other countries, the problem lies in the lack of infrastructure, while the costs of building pipelines would be high.

Structure of the natural gas market in the Republic of Serbia

The ultimate shareholders of GASTRANS d.o.o. and their affiliates hold a dominant position in the Republic of Serbia. Import of natural gas into the Republic of Serbia is predominantly, and in some years 100% from Gazprom Export, while GAZPROM is through Gazprom Neft the majority shareholder of NIS, the sole producer of natural gas in the Republic of Serbia. SRBIJAGAS occupies a dominant position in the activities of wholesale of natural gas, transport

6 - <https://www.valuewalk.com/2017/01/denmark-natural-gas/>

7 - <https://www.woodmac.com/press-releases/groningen-gas-production-cap/>

of natural gas, distribution of natural gas and retail sale of natural gas. Gazprom Export and SRBIJAGAS are the owners of the only natural gas storage facility in the Republic of Serbia.

Assessing the increase of market competitiveness

In order to assess whether the Project for which exemption is being requested increases competitiveness of the natural gas market, the Agency emphasizes that it had in mind the criteria which the Energy Community uses in determining whether granting an exemption for new infrastructure is justified and the requirement for the proponent of a project and/or national regulator to submit:

- Structure of ownership for the project – (In the Request for Exemption, GASTRANS d.o.o. submitted the structure of ownership of GASTRANS d.o.o., the management bodies of the companies in the shareholders' structure of GASTRANS d.o.o., as well as the members of the management bodies of those companies, as well as all necessary data defined in the Rulebook on Conditions for Exemption, Content of the Request for Exemption and Content of the Exemption Act ("Official Gazette of the Republic of Serbia", No. 11/2018, dated 9 February 2018)).

- The opinion of the project proponent on how the exemption will affect the relevant market. As Schedule 4 of the Addendum, GASTRANS d.o.o. submitted a Market Study prepared for GASTRANS d.o.o. by BLUBERRIES GmbH. In this Study Chapter E Serbian Natural Gas Market, in the part relating to competition, defines the impact of the New Interconnector on the Serbian natural gas market, while Chapter F Impact of the Project on Competition and Gasification in the Region defines the impact of the New Interconnector on the natural gas market in the region of South-East Europe, which comprises 9 countries.

In summary, the Market Study concluded that the New Interconnector would promote competition through a downward pressure on prices within both the Serbian domestic and regional market, wherefore approving the exemption cannot alter this decisive fact.

1. Market structure for each of these markets, including a description of the relevant market conditions and defining the market shares of companies being ultimate shareholders of GASTRANS d.o.o. and their affiliates

In the Addendum, namely point 5.1 Overview of the Serbian natural gas market and point 5.1.4 Overview of the natural gas market of South-East Europe, GASTRANS d.o.o. provided an overview of the natural gas market, as well as in point 7.1 Increase of Competitiveness on Natural Gas Markets and Security of Supply. Moreover, in Chapter E Serbian Natural Gas Market of the Market Study, GASTRANS d.o.o. provided the following: structure of the market of natural gas transmission in the Republic of Serbia, with lengths of the transmission systems of TSOs SRBIJAGAS and Yugorosgaz-transport, structure of the market of natural gas distribution with the total number of connections and total length of the distribution network in the Republic of Serbia and the number of connections and length of the distribution network of distributor SRBIJAGAS. There is one producer of natural gas in the Republic of Serbia, the majority owner of which is a daughter company of one of GASTRANS d.o.o. ultimate shareholders, and one underground gas storage facility. GASTRANS d.o.o. ultimate shareholders are the owners of this underground gas storage facility, directly or indirectly. The entire imports for 2017 were realized by SRBIJAGAS, and its share in the natural gas retail market amounted to 87%.

2. The manner in which the capacities will be allocated and the results of the market test conducted by GASTRANS d.o.o.

In the Addendum GASTRANS d.o.o. submitted the results of the non-binding Market Test for use of the New Interconnector. As Schedule 6 of the Addendum, GASTRANS d.o.o. submitted a Proposal of the document proposing the manner of allocation of capacities in the binding Market Test phase, which the Agency accepted only in part when it determined the manner of allocation in its Capacity Allocation Decision dated 3 September 2018.

3. Assessment of the anticipated impacts of the project on the markets impacted by the project

In the Market Study, in Chapter E Serbian Natural Gas Market, GASTRANS d.o.o. concluded that the New Interconnector will have a positive effect on the Serbian natural gas market, and in Chapter F Impact of the Project on Competition and Gasification in the Region that the New Interconnector will have a positive effect on the natural gas market in the region of South-East Europe. The Market Study concluded that the impact would be one of increased competition within the natural gas market and between various types of fuel in the region and in the Republic of Serbia, partially realised through lower prices for natural gas. Assessment of the expected impacts on the natural gas market in the Republic of Serbia and in the region of South-East Europe was performed by the Agency through an assessment of the criteria of the EU Commission for increasing competition and through the conditions it imposes for the New Interconnector.

4. Measures that will prevent third parties not having access to capacities

In the Addendum, in point 6.1.1. Exemption from Third-Party Access and the Rulebook for Binding Allocation of Capacities, comprising Schedule 6 of the Addendum, GASTRANS d.o.o. proposed a manner of allocating the capacities of the New Interconnector. GASTRANS d.o.o. proposes that 88% of the capacities be offered for long-term allocation to the ultimate shareholders of GASTRANS d.o.o. and their affiliates, and that the remaining 12% of capacities be allocated on a long-term basis to third parties. If third party interest in long-term contracting of capacities does not cover the 12%, the unallocated capacities will first be offered to the ultimate shareholders of GASTRANS d.o.o. and their affiliates, and failing their interest, will be left for allocation for periods of time shorter than one year, in accordance with NC CAM, once the New Interconnector starts its commercial operation. The Agency considers that the said principles are unacceptable and specifies the rules for allocation as explained in detail in the section Exemption from rules of third party access.

5. Measures that will facilitate secondary capacity trade

GASTRANS d.o.o. has proposed that congestion management provisions be applicable for third-party capacities, but not for the capacities of the ultimate shareholders of GASTRANS d.o.o. and their affiliates. Congestion management provisions motivate capacity owners to trade capacities on the secondary market if they are not using them. The Agency considers that the said measures are insufficient and specifies that the congestion management UIOLI mechanism for a day ahead shall be applied to third-party capacities, but also to the capacities of ultimate shareholders of GASTRANS d.o.o. and their affiliates, which will facilitate the development of secondary trade of the capacities of the New Interconnector. This means that GASTRANS d.o.o. will be obliged in case of contractual congestion of capacities to offer all capacities for which no nomination for their use has been sent a day ahead to all interested parties on an interruptible basis. If a transmission system user that has contracted firm capacity nominates such capacity (the precise hour by which nominations are to be submitted shall be specified in the network code), the transmission system operator will return such capacity to the user with firm capacity.

Potential conditions that may be imposed on the New Interconnector

In order to assess whether a gas pipeline for which exemption is being requested increases competitiveness, the EU Commission has defined Criteria for determining whether granting exemption to new infrastructure is justified, the fulfillment of which is to be assessed by national regulators.

Requirement of testing the interest of the market and meeting the expressed demand for capacities to the greatest extent, and defining the minimal size of the infrastructure in order to avoid large charges for its use in case of insufficient utilization of capacities. The Agency rendered a Decision on Market Test, based on which GASTRANS d.o.o. organized a non-binding Market Test examining the interest in the use of the New Interconnector. In the Addendum GASTRANS d.o.o. defined the required capacity of the New Interconnector in accordance with the results of the non-binding allocation of capacities in order to avoid capacity congestion.

The Agency rendered a Capacity Allocation Decision, based on which GASTRANS d.o.o. will allocate capacities during the binding phase of the Market Test examining the interest in the use of the New Interconnector.

- Defining the maximum percentage of capacities that may be allocated to companies with a significant share on the relevant market. This condition may be combined with the requirement of freeing a part of the capacities or the relevant quantities of natural gas that exceed the defined maximum percentage.

By this Act the Agency has determined the maximum percentage of 88% of capacities of the New Interconnector which may be contracted by Gazprom Export and SRBIJAGAS, in order to ensure that the financing of the pipeline is not jeopardized. At the same time this restriction of the possible allocation of capacities to Gazprom Export and SRBIJAGAS should also ensure that market participants that do not have a dominant position can, either through long-term or possibly through short-term allocation, secure their share in the market, *i.e.* it should restrict the dominant position of certain participants.

- Defining the decision on exemption is valid only if the operation of the project commences within a specific timeframe. This avoids "congestion of exemptions" which could lead to the blocking of a location or route for competitive projects.

In accordance with Article 288 paragraph 18 of the Law, the Opinion of the Energy Community Secretariat on the act on exemption shall expire two years from the date of its rendering, if construction of the infrastructure has not started, or five years from the date of its rendering, if the infrastructure has not been deployed, unless the Energy Community Secretariat decides that the delay is caused by circumstances outside of the control of the party being granted the exemption. This Act also defines that the exemption shall expire two years from the date of passing the final Act, if construction of the infrastructure has not started, or five years from the date of the final Act if construction of the infrastructure has not been completed.

- Requirement to reserve capacities for short-term contracts that will enable development of the spot market. It may be considered that the amount of capacities to be reserved for short-term capacities is not determined in advance as a percentage of the technical capacity of the pipeline, but is ideally based on the relevant interest in short-term capacities determined in assessing the market requirements. It should be borne in mind that offering capacities for short periods of time has a strong impact on the financing structure of the project, because it decreases the predictability of long-term income. Therefore the national regulators should take this effect into consideration when assessing the project risk.

Since the non-binding Market Test examining interest in the capacities of the New Interconnector showed that for a significant number of the years for which exemption is being requested interest in capacities at the exit Horgoš was expressed only by [Gazprom Export LLC] and there are no interested third parties, the situation could arise where realization of the New Interconnector is not cost-effective. Namely, based on experiences with other exemptions, interest of third parties in using a pipeline is significantly lower in the case of binding allocations than of non-binding allocations. Therefore, it is to be expected that not all capacities of the New Interconnector will be contracted on a long-term basis, wherefore they will be offered as short-term capacities. Based on the non-binding Market Test, it is expected that in certain years there will be more than 10% of capacities available for short-term contracting. With the aim of securing predictability of long-term income and thus access to the capacities of the New Interconnector for ultimate shareholders of GASTRANS d.o.o. and their affiliates and third parties maximally in accordance with their respective requirements for long-term capacities, the Agency has specified by this Act that, in case of insufficient interest in long-term contracting of capacities which is economically justified, GASTRANS d.o.o. may change the technical design of the New Interconnector. In that case, apart from all required long-term capacities, the capacity of the New Interconnector must also ensure 10% of capacities for short-term allocation to all interested parties.

- Requirements relating to the structure of ownership, distribution of voting rights of the corporative entity managing the company granted exemption, including agreements between the company owners, requirements relating to independence of the management, core financial and contractual relations and flow of information

GASTRANS d.o.o. submitted the structure of ownership of GASTRANS d.o.o., as well as the management bodies of the companies that are shareholder and ultimate shareholders of GASTRANS d.o.o. GASTRANS d.o.o. submitted a Compliance Program (program for non-discriminatory conduct), as well as the obligation of appointing a compliance officer.

- Requirement of organizing the sale of part of the natural gas delivered to the natural gas market in the Republic of Serbia through the new infrastructure to third parties

The Agency believes that this restriction is not necessary, since a restriction has been set for the maximum amount of capacity for import of natural gas into the Republic of Serbia to the ultimate shareholders of GASTRANS d.o.o. and their affiliates, and a part of the capacity will be available for short-term contracting, which creates the necessary conditions for companies that are not ultimate shareholders of GASTRANS d.o.o. and their affiliates to import natural gas for the requirements of the natural gas market in the Republic of Serbia under market conditions.

- Limiting the exemption to part of the capacity of the proposed investment

By this Act the Agency has limited the amount of capacities available to ultimate shareholders of GASTRANS d.o.o. and their affiliates for priority long-term contracting.

The Agency's conclusion with regard to enhancement of competition by the New Interconnector and appropriate conditions to apply

For the reasons described above, the Agency considers that the New Interconnector has the potential to enhance competition in the supply of natural gas in the Republic of Serbia and the SEE region. Competition should contribute to lowering of prices and an increase of natural gas consumption — which is associated with some substitution of other fuels with natural gas. The Agency has determined that the New Interconnector, whose physical direction of transmission is south-north, can transport natural gas from new sources which could be economically justified for the Republic of Serbia and the SEE region.

The results of the non-binding Market test show that interest has been expressed by third parties in using the New Interconnector, but that this interest is insufficient for the construction of the New Interconnector without participation of the companies being the ultimate shareholders of GASTRANS d.o.o. The companies being the ultimate shareholders of GASTRANS d.o.o. hold a dominant position on the natural gas market in the Republic of Serbia, however the Agency has determined that the New Interconnector will nonetheless increase the competitiveness of the natural gas market under the following conditions:

Company shareholders and their affiliates Gazprom Export and SRBIJAGAS are entitled to priority long-term contracting of no more than 88% of the capacities of the New Interconnector, that is to say, GASTRANS d.o.o. is obliged to offer to third parties for long-term contracting no less than 12% of the capacities of the New Interconnector. GASTRANS d.o.o. must set aside all capacities of the New Interconnector that have not been contracted as long-term capacities for short-term allocation of capacities.

If the economic and financial analyses demonstrate that changing the technical design of the pipeline is justified, the new capacity of the pipeline must ensure the capacity for all requested long-term capacities and that 10% of the capacity of the New Interconnector is left over for short-term allocation to all interested parties.

Applying these criteria as described in the reasoning for the disposition of the Preliminary Act, the Agency has established that the New Interconnector has the potential to enhance competition in the supply of natural gas in the Republic of Serbia and the SEE region. Competition would contribute to lowering of prices which would in turn cause an increase of natural gas consumption, and therefore substitution of other fuels with natural gas. The Agency has determined that the New Interconnector, whose physical direction of transmission is south-north, can transport natural gas from new sources which could be economically justified for the Republic of Serbia and the SEE region.

As the results of the non-binding Market test have shown that interest has been expressed by third parties in using the New Interconnector, but that this interest is insufficient for the construction of the New Interconnector without

participation of the companies being the ultimate shareholders of GASTRANS d.o.o. The companies being the ultimate shareholders of GASTRANS d.o.o. hold a dominant position on the natural gas market in the Republic of Serbia; the Agency has determined that the New Interconnector would nonetheless increase the competitiveness of the natural gas market, provided the following conditions specified in the disposition of the Preliminary Act were fulfilled:

- Company shareholders and their affiliates Gazprom Export and SRBIJAGAS are entitled to priority long-term contracting of no more than 88% of the capacities of the New Interconnector, that is to say, GASTRANS d.o.o. is obliged to offer to third parties for long-term contracting no less than 12% of the capacities of the New Interconnector.
- GASTRANS d.o.o. must set aside all capacities of the New Interconnector that have not been contracted as long-term capacities for short-term allocation of capacities.
- If the economic and financial analyses of the feasibility of the Project demonstrate that changing the technical design of the pipeline is justified, the new capacity of the pipeline must ensure the capacity for all requested long-term capacities and that 10% of the capacity is left over for short-term allocation to all interested parties.

2. Is the risk of investing in the new interconnector such that the investment will not take place if exemption is not granted

Article 288 paragraph 1 item 2 of the Law requires "that the risk attached to the investment in the new infrastructure facilities is such that the investment would not take place unless an exemption is granted".

Article 3 of the Rulebook on Conditions for Exemption, Content of the Request for Exemption and Content of the Exemption Act ("Official Gazette of Republic of Serbia" no. 11/2018) specifies that the request for exemption shall, *inter alia*, include the following:

- technical and economic documentation: analyses or feasibility studies relating to construction of the infrastructure (paragraph 1, item 5), sub-item (1)) and an analysis of fulfillment of the prescribed conditions set forth in Article 288 of the Law and Article 2 of the Rulebook based on the data on the infrastructure project and the results of the Market Test examining interest in use of the infrastructure (paragraph 1, item 5), sub-item (3));
- proposal for the manner of forming access prices to the system and adjusting the prices during the period for which the exemption is requested if the request seeks exemption from the obligation of applying regulated access prices as referred to in Article 283 paragraph 1 of the Law.

Article 5 of the Rulebook specifies that the analysis referred to in Article 3, paragraph 1, item 5), sub-item (3) of the Rulebook, which confirms fulfillment of the conditions set forth in Article 288 of the Law and Article 2 of the Rulebook, shall, *inter alia*, include the following:

- an analysis of the risk of investing in the infrastructure which the applicant submitting the request is basing on data concerning the estimated time for construction of new or expansion or alteration of the existing infrastructure, estimated value of investments in the infrastructure, probability of recovery of the investment in the event that exemption is not granted, analyzing in particular the risk of lack of use of the infrastructure and the risk of change of volume of costs and income, and the risk of competition if the construction of infrastructure of similar volume is planned or in progress, in which case the risk can be assessed by benchmarking against the risk of constructing the infrastructure in the surroundings which is, by nature and volume, comparable to the infrastructure to which the request pertains and the results relating to the scope of market interest in use of the infrastructure which justify the requested exemption (paragraph 1 item 3)); and
- the data used to prepare the proposal for the manner of forming access prices for users of the infrastructure referred to in Article 3 paragraph 1 item 6) of the Rulebook.

GASTRANS d.o.o. has emphasized several key risks which prevent realization of the construction in case of application of regulated conditions for access to the system and regulated prices. It has specifically pointed out that it would not have the right to manage the system upon construction of the pipeline as ISO/ITO, as well as if ownership unbundling is carried out. It also specifies that GASTRANS d.o.o. would not be able to attract enough equity and enough third party financing to construct the New Interconnector, and therefore points out that the exemption from third party access rules would enable it to grant priority use of the New Interconnector to interested and creditworthy users of the future transmission system since overrun costs in constructing the facility cannot be recovered under the tariff

calculation methodology for access to the transmission system which was issued by the Agency and is applied by the existing transmission system operators.

The Addendum also contains a table and analysis of other exemption decisions in regard to this condition, benchmarking the risk attached to the construction of the New Interconnector with the risks existing in those other cases (*i.e.* Opal, Gazelle, Slovakian-Hungarian interconnector, BBL, TAP) where exemption was granted by the relevant national regulatory authorities. The purpose of such benchmarking is to show these risks increase in accordance with the length of the pipeline, the overall project costs, the nature of the terrain, the particularities of the jurisdiction and the number of shareholders able to provide equity for the project, and to show that the construction of the New Interconnector and realization of the Project is equally risky, if not more risky, than in those projects which have already received an exemption.

The economic and financial documents and data which GASTRANS d.o.o. submits together with the request for exemption are analyses or feasibility studies relating to construction of the infrastructure. They should contain: 1) data on the estimated time for construction of the new infrastructure, 2) data on the estimated value of investments in the new infrastructure, and 3) data on the probability of recovery of the investment in the event that an exemption is not granted, analyzing in particular the risk of lack of use of the new infrastructure and the risk of change of volume of costs and income, as well as a proposal for the manner of forming access prices to the transmission system and adjusting the prices during the period for which the exemption is requested.

In that context GASTRANS d.o.o. submitted an elaborate report on the necessity of exemption with regard to the risks relating to the investment, particularly in the context of examining the bankability of the Project and its financial viability, as well as other requested documents on the basis of which the Agency has assessed the fulfillment of this condition.

In assessing the fulfillment of this condition, the Agency has especially taken into consideration the particularities of the market of the Republic of Serbia which is in line with Article 288 paragraph 6 item 5 of the Law. Such national particularities, according to GASTRANS d.o.o. view, are:

- in the Republic of Serbia so far, no project has been realized with the project company attracting [EUR 300 million];

- no Serbian private company without support from strong and creditworthy shareholders could obtain financing for transmission system projects of such magnitude;

- construction and operation of the pipelines is not one of the eligible projects, for which investment incentives can be obtained pursuant to the Law on investments (Official Gazette of the Republic of Serbia no. 89/2015) and Rules of Procedure on conditions and manner of attracting direct investments (Official Gazette of the Republic of Serbia no. 18/2018). Therefore, the Project risks cannot be mitigated by procuring investment incentives from the Republic of Serbia;

- the construction of the New Interconnector is not partially financed by grant support from third countries or EU that could contribute to the reduction of risks; and

- apart from two projects realized in the last fifteen years, specifically the construction of a gas pipeline between natural gas storage Banatski Dvor and Gospodinci (with an investment of approx. EUR 11 million) and the construction of a crossing under the River Danube (approx. 13 years ago with an investment value of approx. EUR 3 million), the Serbian gas transmission sector has had no significant investments since the 1990's. In effect, the market is stagnant and there are no investments to facilitate infrastructure development.

Based on a review of the submitted documentation, it has been determined that [.....

:

No.	Description of datum/indicator	Value
1.	Estimated value of investment (in 000 EUR)	
1.1.	Estimated value of investment in construction of infrastructure (in 000 EUR)	
1.2.	Estimated value of first filling with gas (in 000 EUR)	
2.	Residual project value (in 000 EUR)	

3.	Sources of funding for the investment (in 000 EUR)	
4.	Planned period of use of the infrastructure (number of years)	
No.	Investment criteria	According to the Feasibility Study
1.	Net present value (in 000 EUR)	
2.	Internal rate of return (in %)	
3.	Payback period (number of years)	
4.	Discount rate (in %)	
5.	Discounted payback period (number of years)	

.....]

a) Analysis of other economic and financial risks of investing in the infrastructure (Article 5 item 3) of the Rulebook)

The Agency has also assessed, based on the data presented in the request, that the expressed interest of third parties in using the services of the New Interconnector, being only around [...%], in a year of maximum third party demand, confirms that providing the service under regulated conditions, given the limited expressed interest, would be insufficient for realization of the Project. Therefore, it has assessed that the Request for Exemption is founded, since the Project will not be realized if its investors (the companies being suppliers and producers of natural gas which are part of the ownership structure that includes GASTRANS d.o.o.) are not entitled to certain guaranteed long-term use of the capacities of the New Interconnector. Furthermore, in the Request for Exemption, GASTRANS d.o.o identifies the risk that potential overrun of the costs of the Project cannot be recovered by the methodology for calculating tariffs for the national transmission system managed by the current transmission system operators as a particular risk of investment in the New Interconnector. Although the methodology for forming the prices for access to the natural gas transmission system which is applied in the Republic of Serbia ensures the covering of all justified operating costs and a certain yield on efficiently invested funds into conducting the business activity of natural gas transmission, the Agency has assessed that it should be borne in mind that applying the current methodology would not be able to ensure stability of income over a long period of time, which is the basic presumption in order for someone to invest. GASTRANS d.o.o. has stated that the methodology for forming prices for access to the natural gas transmission system has changed several times over the previous period which is true, and it is realistic to expect changes to the methodology in the future period as well, due to the planned harmonization with EU regulations (among other changes, it is possible that the price regulation method will change from the "Internal rate of return" method to incentive methods).

The Agency, recognizing the fact that the possibility of change of the methodology in the coming period cannot be excluded, and the fact that it is not possible to determine tariffs over a longer period of time (which would decrease the risk of insufficient use of capacities and the risk of change in income), which are indeed the basic criteria for assessing the risk of realizing an investment, has established during the procedure that the Project is high risk and that its realization is not be possible unless exemption is granted.

b) Request for exemption from applying regulated prices

Analyzing the request for exemption of the New Interconnector in the part where GASTRANS d.o.o. requests exemption from the application of regulated prices, and considering that the basic principles of such a manner of determining prices require that they must be formed in a clear and non-discriminatory manner for long-term booking of capacity, which presumes defining the manner for determining the necessary income which should be recovered through the tariffs, and the conditions for future correction of such tariffs. Independent setting of prices must be such that all future deviations of projected from realized costs, such as investment costs, operating costs, crediting costs and the like, are subject to review each year and, as needed, for the amount and direction of their correction, a new tariff may be formed, but so that it is fixed for a period of one year.

Recognizing the specificities of the Project and the schedule for its construction and activation of individual sections, the tariffs and the manner for determining the tariffs for the period before the New Interconnector achieves full utilization of capacities have been separately defined. Due to the risk that the proposed manner of forming the tariffs, in this case could have the consequent of jumps in the tariffs over the observed period of time, in order to avoid this, a special manner for determining the tariffs has been envisaged, which should ensure linear and gradual achievement of the tariffs in the years when there will be full utilization of capacities.

c) Analysis of the justification of the requested duration of the exemption

Article 288 paragraph 6 of the Law specifies the obligation of the Agency when deciding on a request for exemption to, *inter alia*, consider the duration of exemption and the planned period of use of the infrastructure.

In the Addendum, GASTRANS d.o.o. reduced the period of exemption to 20 years. The Agency believes that exemption for a period of 20 years enables bankability of the Project, given the periods of payback of the borrowed funding, creates the necessary conditions for securing funding for construction and successful operation of the GASTRANS d.o.o. pipeline, *i.e.* secures the necessary time that enables the net income to cover all investments.

This is indicated by the results shown in the Feasibility Study for the Project. In the part relating to the investment criteria, two payback periods are shown. One is the actual payback period (Simple Year Payback) of 16 years, while the other is the dynamic discounted payback period which is 27 years. The first, simple year payback, is a statistical indicator, because it does not take into account the value of money over time. Thus, this approach to calculation of the payback period, due to its simplicity, is used in practice mainly in the case of smaller or one-time investments with a short payback period. Given the size of this Project, its periods of time in terms of both investment and duration, the more appropriate criterion for assessing the length of the exemption period would be the discounted payback period. Since the duration of the exemption must be equal to or less than the payback period for the investment, taking into account that the discounted payback period is 27 years, exemption from the obligation of applying regulated prices in the duration of 20 years is in accordance with this request.

Based on all of the above, and on the fact that allocation of up to 20 years exists in European Union regulations and practice as well, the Agency has assessed that the long-term allocation of capacities for a period of 20 years is acceptable, taking into account the positive opinion of the Energy Community Secretariat for the TAP pipeline project for allocation of capacities and full exemption for 25 years.

Based on the data and documentation submitted by GASTRANS d.o.o., the planned period of use of the relevant infrastructure is 40 years. The useful lifetime of the relevant infrastructure is in accordance with the Decision on the Manner, Procedure and Deadlines for Bookkeeping Records, Separating Accounts by Activities and Delivering Data and Documents for Regulation Purposes ("Official Gazette of Republic of Serbia", No. 65/14).

Based on the above, the Agency has assessed that the request for exemption from the application of regulated prices for the duration of 20 years is justified, that GASTRANS d.o.o. is obliged to form the prices in the manner set out in item 18 of this Act, including the manner and deadlines for adjusting tariffs which will be formed in accordance with the methodology adopted during the exemption period, and to submit a tariff calculation and data and relevant documentation documenting the current elements of necessary income and calculation of the correction element for the previous year to the Agency no later than 90 days before the start of application thereof, together with the data and documentation, applying *mutatis mutandis* the act regulating the manner, procedure and deadlines for bookkeeping records, separating accounts by activities and delivering data and documents for regulation purposes. Taking into consideration exemption decisions⁸ rendered so far, and weighting the arguments in the context of national particularities, the Agency has concluded that this condition is fulfilled.

3. That the new interconnector must be owned by a legal or natural person operating as a different legal entity separated from the operator of the system within which the new infrastructure facility will be constructed

⁸ Joint Opinion in TAP case, in Section 3.3 provides the following - "clearly, the size of the TAP project, especially compared to the national markets of Greece and Albania, is such that volume or other risks cannot be borne by the users of the national gas systems *i.e.* under a regulated TPA regime, without undermining the viability of the corresponding national systems."

In its Request for Exemption, GASTRANS d.o.o. specifies that upon construction of the New Interconnector, and subject to approval of the exemption, it intends to conduct the business activity of natural gas transmission and manage the New Interconnector as Transmission System Operator.

Based on a review of the Request for Exemption and the submitted evidence, it has been determined that the New Interconnector will be constructed by GASTRANS d.o.o., which is a separate legal entity and is not a system operator. Moreover, the Agency has determined that GASTRANS d.o.o. will construct the new infrastructure facility using its own funds and that, based on such construction, it will acquire ownership rights over the New Interconnector, on which it will conduct the business activity of natural gas transmission.

4. Charges must be levied on users of the new interconnector

In the Exemption Request, GASTRANS d.o.o. states that after the construction of the new connector and subject to approval of the exemption, it intends to form the prices for transmission services in line with the proposed methodology and the approved exemption from the obligation of applying regulated prices.

Having reviewed the received documentation, the Agency established that the charges for using the new interconnector will be levied on users of the new infrastructure and that the amount of these charges will be determined and levied on the users by GASTRANS d.o.o. in order to collect them in its own name and for its own account.

5. The exemption must not be detrimental to competition or the effective functioning of the internal market in natural gas, or the efficient functioning of the regulated system to which the new interconnector is connected

In reaching its conclusion on the Exemption Request, the Agency took into account the criteria the European Commission recommended to apply in this procedure, namely:

Criterion 1 - the exemption must not be detrimental to competition;

Criterion 2 - the construction of the exempted infrastructure will not be detrimental to the effective functioning of the market, and

Criterion 3 - the construction of the exempted infrastructure will not lead to higher tariffs of regulated systems

Criterion 1 - The Agency assessed that the construction of the New Interconnector will enable to increase the pressure in the southern part of the existing transmission system in the Republic of Serbia and thereby to construct new gas pipelines not only in this region of the Republic of Serbia, but also in neighbouring countries, which was not feasible so far due to the low pressures in the Serbian transmission system. The Agency assessed that the construction of the New Interconnector will have a positive impact on the regulated transmission system of the Republic of Serbia given the fact that it will enable natural gas imports to the Republic of Serbia from two directions and thereby increase the import capacities at the entry points, thus, creating the conditions for increase of competition for importing natural gas and the functioning of the overall market. Furthermore, the Agency assessed that the construction of the New Interconnector will have a positive impact on the Hungarian regulated transmission system, as well as on the natural gas market in Hungary and regions of Southeast and Central Europe. Having considered all of the above, it is assessed that the approval of the exemption will not be detrimental to competition.

Criterion 2 - The Agency assessed that the construction of the New Interconnector will not lead to congestions in the connected transmission systems, nor it will have negative impacts on the effective functioning of the market, which is to be confirmed by the transparent operating conditions and capacity management for the New Interconnector. As GASTRANS d.o.o. harmonised both the technical capacities at the interconnection points with the transmission systems in the Republic of Bulgaria, the Republic of Serbia and Hungary and the minimum operating pressures at the interconnection points, the Agency assessed that the construction of the New Interconnector will not cause congestions in the connected transmission systems, nor it will have negative impacts on the effective functioning of the market.

Criterion 3 - Analysis of impacts of the construction of the New Interconnector on the transmission tariffs of the transmission systems falls within the competence of the national regulatory authorities of the Republic of Bulgaria

and Hungary. In the non-binding phase of the natural gas market test for the construction of the New Interconnector, a strong interest was expressed for contracting long-term capacities at the entry point from the Republic of Bulgaria, and the same interest exists in the Bulgarian transmission system for the transport towards the Republic of Serbia. Therefore, it is expected that the income to be gained by transporting natural gas through the Republic of Serbia (Turkey-Serbia direction) will be sufficient to cover the costs of expanding the transmission system in the Republic of Bulgaria, and, hence, no higher tariffs are expected. In the non-binding phase of the natural gas market test for the construction of the New Interconnector, an interest was expressed in contracting long-term capacities at the exit point of Hungary, and the same interest exists at the entry point to the Hungarian transmission system from the Republic of Serbia, therefore, it is expected that the income to be generated from transporting natural gas from the Republic of Serbia to the Hungarian transmission system will be sufficient to cover the costs of expanding the Hungarian transmission system and, hence, no higher tariffs are expected.

Considering all of the above, the Agency assessed that:

- all three exit points of the New Interconnector for Serbia are close to the existing transmission system in the Republic of Serbia and connecting of the New Interconnector with the existing transmission system in the Republic of Serbia will not lead to higher tariffs for using the existing transmission system in the Republic of Serbia, and
- the construction of the New Interconnector with the designed utilisation period will not lead to higher tariffs of regulated systems, but rather to their decrease due to the competitive pressure.

Based on the above, the Agency concluded that the exemption of the new interconnector does not prevent competition, effective functioning of the natural gas internal market and efficient operation of regulated systems to which the future gas pipeline will be connected, given the fact that it meets all the criteria.

Assessment of the fulfilment of conditions for granting an exemption from the obligation of ownership unbundling

GASTRANS d.o.o. requested an exemption from the obligation of ownership unbundling prescribed under Article 224, paragraph 2 and Article 225 of the Law.

Having reviewed the documents enclosed with the request, it was established that GASTRANS d.o.o. is a single member company established under the laws of the Republic of Serbia for pipeline transmission as a core activity, that its sole member is South Stream AG, a joint stock company established under the laws of Switzerland, with a head office in Switzerland, Canton of Zug and that the shareholders of South Stream AG are TRANSGAZ KRASNODAR with 51 % of the shares and JP Srbijagas with 49% of the shares in South Stream AG.

Both companies, GASTRANS d.o.o. and South Stream AG, are founded with the aim of developing, financing, constructing, operating and maintaining the sections of the South Stream gas pipeline that will be constructed in the Republic of Serbia for the purpose of transporting and supplying natural gas to the Republic of Serbia.

In terms of the law, JP Srbijagas is a vertically integrated company established to engage in natural gas transmission and operation of natural gas transmission systems, natural gas storage and management of natural gas storages, distribution and operation of natural gas distribution systems, natural gas supply, public natural gas supply, combined electricity and heat generation, exploration and production of natural gas with the possibility of conducting these activities through subsidiaries. Even though JP Srbijagas established the subsidiaries to conduct natural gas transmission and distribution activities, all these activities are still being conducted by JP Srbijagas, which is 100% owned by the Republic of Serbia. The majority shareholder of South Stream AG is GAZPROM TRANSGAS KRASNODAR established to engage in natural gas pipeline transmission activity as its core activity. GAZPROM TRANSGAS KRASNODAR is 100% owned by GAZPROM, a vertically integrated company registered for oil and natural gas production activities, production of gas condensate, gas distribution through a distribution system, gas supply, non-specialised trade, pipeline gas transmission and transmission of products obtained by their processing. GAZPROM subsidiaries, GAZPROM EXPORT and GAZPROM Schweiz, are engaged in foreign trade and export of natural gas. GAZPROM and Centrex Europe Energy&Gas AG as its subsidiary are the majority owners of Yugorosgaz, in which JP Srbijagas holds 25% of ownership, which is established to engage in natural gas supply, public supply and distribution

of natural gas, and which 100% subsidiary Yugorosgaz Transport d.o.o. conducts the transport activity. In addition, GAZPROM EXPORT owns 51% of shares of Banatski dvor d.o.o., which is established for natural gas storage and in which the remaining 49% of shares is held by JP Srbijagas.

Article 222 of the Law stipulates that the activity of natural gas transport and natural gas transmission system management shall be performed by a natural gas transport system operator, with rights and obligations stipulated by this Law.

Article 224, paragraph 1 of the Law prescribes that the transmission system operator shall be the owner of the transmission system.

Article 224, paragraph 2 of the Law stipulates that a transmission system operator shall be an independent legal entity that is not a part of a vertically integrated company and is independent in performing energy-related activities of natural gas production and supply.

Having reviewed the Exemption Request, it was established that GASTRANS d.o.o. does not request an exemption from the obligation of applying the provisions of Article 224, paragraph 1 of the Law, but as underlined therein, its intention is to acquire ownership by constructing, which is, after all, a condition to grant the exemption prescribed under Article 288, paragraph 1, item 3) of the Law.

In its Exemption Request, GASTRANS d.o.o. limits the scope of exemption from ownership unbundling exclusively to the obligations under Article 224, paragraph 2 of the Law, which stipulates that a transmission system operator shall be an independent legal entity that is not a part of a vertically integrated company and is independent in performing energy-related activities of natural gas production and supply.

In its request, GASTRANS d.o.o. points out that the requested exemption under Article 224, paragraph 2 of the Law also implies an exemption from the provisions regulating the manner of achieving independence of a system operator under Article 225 of the Law.

In order to ensure a non-discrimination of the transmission system users, the Law establishes a condition of ownership unbundling, which implies that a legal entity may not directly or indirectly exercise control over another legal entity engaged in the natural gas production and supply and at the same time exercise control over a transmission system operator and this condition of ownership unbundling also applies in the case of an inverse structure.

In the Exemption Request, GASTRANS d.o.o. noted that the Project would not be implemented without financial commitments - through capacity bookings and equity commitments - of companies exercising control over GASTRANS d.o.o. and its subsidiaries engaged in the natural gas production and supply, indicating that GASTRANS d.o.o. is in the same situation as TAP, Nabucco pipeline, SK-HU interconnector or ICGB interconnector, all of which were granted a full exemption from the obligation of ownership unbundling.

It is assessed that if the exemption request from Article 224, paragraph 2 of the Law would not be accepted, GASTRANS d.o.o., in accordance with the regulations governing the manner of ownership unbundling of transmission system operators under Article 224 of the Law, would be only entitled to construct the New Interconnector as any other investor in accordance with the law, but not to engage in the natural gas transmission and operation of the New Interconnector, as the application of Article 224 would either force GASTRANS d.o.o. to transfer its ownership over the New Interconnector to a third party or to transfer a majority share of GASTRANS d.o.o., whereby the entity must not be a natural gas producer or supplier, but an independent and autonomous entity within the meaning of Article 224, paragraph 2 of the Law. Therefore, the Agency concludes that GASTRANS' inability to manage gas pipeline in the case that the exemption is not granted and the risk of uncertainty GASTRANS would face in this case confirm that investments would not be made if the exemption was not granted and for this reason the Agency is of the view that the request for exemption from the obligation of applying ownership unbundling rules under Article 224, paragraph 2 and Article 225 of the Law is legitimate.

The ownership unbundling conditions under Article 225 of the Law also stipulate that a legal entity exercising control over a system operator shall not be entitled to appoint the members of a supervisory board or other management bodies or legal representatives of a transmission system operator and simultaneously exercise control over an entity engaged in the natural gas production and supply. Moreover, it requires that the same person is not entitled to be a member of a supervisory board or other management bodies or a legal representative of a transmission system operator or an entity engaged in the natural gas production and supply.

The Agency noted that in relation to the Albanian section of the TAP pipeline, TAP AG was fully exempted from clauses (c) and (d) under Article 9 (1) of the Gas Directive, but that the Energy Community imposed the following requirements: 1) Members of the management bodies and executive management of TAP AG shall not take part in any corporate structure of the shareholders of TAP AG responsible for day-to-day natural gas production and supply; 2) evidence that the professional interests of persons responsible for the management of TAP AG is taken into account in a manner that ensures that they are capable of acting independently, and 3) providing evidence that the transmission system operator will have a compliance program in place, which is adequately monitored by a compliance officer employed by the pipeline operator itself.

With a view to granting the exemption from Article 225 of the Law (transposing clauses (c) and (d) of Article 9 (1) of the Gas Directive), GASTRANS d.o.o. enclosed a draft Program in the Addendum. The Agency is of the view that the adoption of a Compliance Program is a mandatory condition to ensure non-discrimination and confidentiality under Article 225 of the Law (transposing clauses (c) and (d) of Article 9 (1) of the Gas Directive), particularly taking into account the scope of the granted exemption from the third party access and capacity allocation mechanisms set out in the disposition of this Act and the Capacity Allocation Decision.

As the ownership unbundling exemption under Article 224, paragraph 2 and Article 225 of the Law cannot be granted without imposing appropriate commitments that regulate confidentiality of commercially sensitive information and non-discriminatory treatment of system users, GASTRANS d.o.o. proposed:

1. To have a compliance program (Appendix 4 of the Addendum) monitored by a compliance officer independent of the shareholders of GASTRANS d.o.o in order to ensure that commercially sensitive data about transmissions system users available to GASTRANS d.o.o. and/or its employees are not made available to entities performing the energy activities of natural gas production or supply;

2. Starting from commercial operation date, GASTRANS d.o.o. to have sufficient human, technical, physical and financial resources to operate the pipeline independently on a day to day basis;

3. from the start of operations, GASTRANS d.o.o. to have a corporate governance structure in place that will adequately consider professional interests of any person involved in the day to day management of GASTRANS d.o.o. and in the day to day management of a business segment of gas supply or production of a shareholder to avoid discrimination between the transmission system users, etc.

GASTRANS d.o.o. notes that these commitments as a whole would ensure: 1) security/storing of commercially sensitive information and the independence of the management of GASTRANS d.o.o. in relation to the day to day operation of the New Interconnector and the non-discrimination in relation to shareholder affiliated transmission system users of GASTRANS d.o.o. and third party transmission system users in relation to capacity allocation and transportation services; 2) implementation of the Project and construction of the New Interconnector by having creditworthy shareholders able to provide sufficient equity and sufficient security for the lenders to make the Project financeable as well as sufficient volume of long term capacity to be booked to enable the debt finance of the Project; and 3) compliance with the general principles and practice of the national regulators and Energy Community Secretariat so far.

The Agency indicates that the Law provides for three models of organization of transmission system operators - unbundled transmission system operators (Articles 224 and 225 of the Law), independent system operators (Articles 227 - 231 of the Law) and independent transmission operators (Articles 232 - 238 of the Law) and the conditions to be imposed on an applicant when granting an exemption from the obligation of ownership unbundling are not provided in the Law. The Gas Directive also does not prescribe particular conditions or models in this regard.

Taking into account a decision-making practise of the European Commission, the Energy Community Secretariat and national regulatory authorities, where circumstances are comparable, in its request, GASTRANS d.o.o. indicated that there is no a single model or generally accepted requirements that in the context of an exemption may be considered to constitute alternative unbundling model, which the Agency confirmed by reviewing the decisions in relation to TAP, Nabucco, Gazelle and SK-HU Interconnector, in which no consistent set of requirements that have been applied to alternative unbundling models was identified.

As the Agency assesses the adequacy of the request and determines the scope of exemption according to the specific circumstances, the Agency grants the exemption from the obligation of ownership unbundling by imposing additional obligations aimed at ensuring a non-discriminatory access to and use of the system and confidential treatment of information of system users.

Given the manner of capacity allocation set out by the Capacity Allocation Decision, which assumes that all the capacities will be allocated on a long-term basis in line with the Capacity Allocation Decision, the Agency considers that proposal of GASTRANS d.o.o. to adopt the compliance program and to appoint a compliance officer is justified and sufficient to ensure non-discriminatory access and confidential treatment of information. However, the draft Program that GASTRANS d.o.o. enclosed with the Addendum must be supplemented as provided in the disposition of this Act both in terms of the content of the Program, and the requirement for the appointment of a compliance officer. In granting the exemption from the obligation of ownership unbundling, the Agency provides necessary authorisations for compliance officer and requirements for its appointment in order to allow it to act independently when implementing the Compliance Program not only for the duration of the exemption but also before conducting the binding phase pursuant to the Capacity Allocation Decision. Therefore, the Agency decided to oblige GASTRANS d.o.o. to appoint an ad hoc body consisted of independent members to decide upon complaints of the participants in the binding phase (Item 4) and thus ensure a non-discriminatory access and confidential treatment of information.

The Agency also imposed a restriction in Item 4 of the disposition of this Act that the commercially sensitive information held by GASTRANS d.o.o. or its employees cannot be made available to undertakings performing activities of the natural gas production or supply. This prohibition is based on Article 225 paragraph 5 of the Law and it is imposed by the Agency as additional manner of protection of confidentiality of information. In case that some of the New Interconnector capacities remain unallocated on a long-term basis (meaning that unallocated capacities will be allocated on a short-term basis in line with Item 8 of the disposition of this Act), the Agency agrees to use a third party capacity allocation platform to allocate GASTRANS d.o.o. capacities.

In its Exemption Request, GASTRANS d.o.o. submitted evidence that once operational, it will have all necessary resources, including human, technical, physical and financial to effectively operate the New Interconnector on a day to day basis without relying on resources of its shareholders. However, the Agency considers that, in order to give full effect to the confidentiality, transparency and non-discrimination commitments, GASTRANS d.o.o. is obliged to have separate and different premises from its related parties; independently operate the transmission system and independently operate and be organisationally separated from its related parties; and implement recommendations of the compliance officer.

Considering the compliance program proposed by GASTRANS d.o.o. in the Addendum and the additional requirements set by Agency in Items 3 - 7 of the disposition of this Act, the Agency is of the view that the effect of these commitments corresponds to the conditions set by the Energy Community in relation to the Albanian section of the TAP pipeline and that on this basis, an exemption from Article 225 of the Law (transposing clauses (c) and (d) under Article 9 (1) of the Gas Directive is proportionate and justified.

As Article 245 of the Law in connection with Articles 240, 241 and 246 of the Law, transposing Article 11 of the Gas Directive (Certification Relating to Third Countries) stipulates that the Agency, in case of certification of a transmission system operator controlled by a party or parties from a third country or third countries, must refuse certification if it has not been demonstrated that the transmission system operator complies with the applicable unbundling requirements (Article 11 (3)(a) of the Gas Directive), and that granting the certification would not put at risk the security of supply of the Contracting Party and the Energy Community (Article 11 (3)(b) of the Gas Directive), therefore, the application of these articles would require to refuse certification as the New Interconnector is to be constructed by GASTRANS d.o.o., a company controlled by GAZPROM being a party from a third country for the purposes of the Articles 245 and 246 of the Law (transposing Article 11 of the Gas Directive) and for this reason, the Agency decided to grant GASTRANS d.o.o. the exemption from the obligation of ownership unbundling in this segment, given the fact the competent authorities and the Agency confirmed that the impact of the New Interconnector on the Republic of Serbia and neighbouring countries is such that it will promote the security of supply.

In order to monitor the compliance with these conditions for the exemption period, the Agency obliged GASTRANS to conduct certification once the New Interconnector is constructed, whereby during the certification of GASTRANS d.o.o. as a transmission system operator that will be controlled by a party from the third country, the fulfilment of the prescribed conditions of ownership unbundling and security of supply by system operators in relation to third countries under Articles 224, 225, 245 and 246 of the Law will not be assessed, given the fact that the Agency hereby determined, with previous obtaining of the opinion of the competent ministry that the security of supply is not compromised and that the Agency grants the exemption from the application of the rules for ownership unbundling.

Assessment of the fulfilment of the conditions to exempt the New Interconnector from third party access

GASTRANS d.o.o. requested the exemption from the rules on non-discriminatory access to the system pursuant to the Article 283 paragraph 1 of the Law and proposed allocation mechanism as follows.

In the Addendum, GASTRANS d.o.o. proposed to split the capacity in the manner described in this explanation under Item 5. Rules and mechanisms for management and allocation of capacities as precondition for rendering the act on exemption.

GASTRANS d.o.o. argued that the principles and steps stated in the draft Capacity Allocation Rules for the Binding Phase enclosed with the Addendum, reflect the results of the Market Test demonstrating that third party transmission system users' interest in the Project pipeline in the New Interconnector is not such that it would enable GASTRANS d.o.o. to construct the New Interconnector.

[In the non-binding phase of the market test,.....]

The Market test results demonstrate that third party transmission system users' non-binding bids together amount only to [.....billion m3] in a year with maximum capacity requests, being around [...%] of the maximum annual technical capacity of the New Interconnector, what clearly demonstrates that without the support of shareholders/shareholders' affiliated transmission system users and allocation of respective quantity to shareholders/shareholder affiliates, the construction of the New Interconnector would not be financially and economically feasible.

Therefore, giving full consideration to the results of the Market test, opinions of the neighbouring national regulatory authorities, conditions for the exemption set out in Article 288 paragraph 1 items 1-5) of the Law and Article 288 paragraph 6 of the Law (non-discriminatory access to new infrastructure, exemption period, access to new facilities to be constructed, planned period of use of infrastructure and national specificities applicable in the specific case) the Agency:

1. adopted the request of GASTRANS d.o.o. that 88% of the technical design of the New Interconnector is allocated in priority to GAZPROM EXPORT LLC and SRBIJAGAS, as the Agency considers that GASTRANS d.o.o. has substantiated its request in this respect by the Addendum and Appendices thereto;

2. adopted the request of GASTRANS d.o.o. that 12 % of the technical design of the New Interconnector is allocated to third parties, as nominal interest of third parties also includes possible double booking as presented in the analysis of the Market test results and the Agency agrees with the reasoning of GASTRANS d.o.o. that the nominal bookings significantly exceed the real demand in the Republic of Serbia and Bosnia and Herzegovina;

3. refused to adopt the request of GASTRANS d.o.o. that the capacity allocation includes step 3 and step 4, as the Agency agrees with the views of neighbouring national regulatory authorities that these steps may limit the third party access, which could hamper competition on the Serbian market and to unjustly limit the access to the New Interconnector;

4. introduced the rule that, if in any year demand for the long-term capacity is lower than the technical capacity at the entry point or exit points (in accordance with the expected technical design of the project of the New Interconnector), GASTRANS d.o.o. may adjust expected technical design and technical capacity of the New Interconnector as close as possible to the technical design required to meet all allocated long-term capacities and short-term capacities, so that the capacity allocated as a long-term capacity shall amount to 90% of the capacity of the New Interconnector and remaining 10% of the capacity of the New Interconnector shall be allocated as the short-term capacity of the New Interconnector on a non-discriminatory basis whereby capacity of the New Interconnector in sum shall not exceed maximum technical annual capacity. Technical design and technical capacity adjustment of the New Interconnector GASTRANS d.o.o. shall base on the results of the binding phase of the market test, and consider offers for capacities requested for periods shorter than the exemption period.

The Agency decided to determine the described scope of third party access exemption because the market test results show that there is an interest of the users for the whole technical capacity of the New Interconnector. When the market shows the interest for the long-term allocation, it would not be justifiable, according to the opinion of Agency, that the allocation rules limit the possibility of the interested parties to book such capacity on a long-term basis. The Agency assessed that in the case of a failure to book a major part of the technical capacity on a long-term basis,

GASTRANS d.o.o. shall be entitled to adjust the technical design and technical capacity of the New Interconnector (to decrease technical capacity), as close as possible to the technical design required to meet all allocated long-term capacities and short-term capacities, so that the capacity allocated as long-term capacity shall amount to 90% of the capacity of the New Interconnector and remaining 10% of the capacity of the New Interconnector shall be allocated as the short-term capacity of the New Interconnector on a non-discriminatory basis.

The Agency assessed that in this manner the tariff and consequently the price of natural gas for end users in the Republic of Serbia should be reduced as the transmission system users would not be obliged to pay the tariff for the cost of construction of the technical capacities that the market will not be using.

The Agency introduces an obligation for GASTRANS d.o.o to, at least every six years or at its discretion, if GASTRANS d.o.o. deems it necessary, verify the interest of the market for investments in the New Interconnector and, provided that such investment is economically justified, to make the investment plan and submit such investment plan to the Agency for the approval pursuant to the Article 250 of the Law. This obligation is introduced taking into account that GASTRANS d.o.o. will construct completely new infrastructure, that majority of the capacity of the New Infrastructure will be allocated on a long-term basis pursuant to this Act and the Capacity Allocation Decision while 10% of the capacity will be allocated on a short-term basis in a non-discriminatory manner (depending on whether there will be the decrease of the technical capacity or not), and that the capacity expansion is not possible without the previous increase in capacities on the upstream system, so that there will be no further investments in the New Infrastructure over certain period of time.

The Agency agrees that GASTRANS d.o.o. should also be, as the consequence of exemption from third party access, exempted from the obligation to:

1) grant the third party access in accordance with the Article 228 of the Law so that GASTRANS d.o.o. is entitled to allocate the capacity of the New Interconnector and to contract the transmission service in accordance with item 8 of the disposition of this Act;

2) provide a non-discriminatory access to the transmission system set out in Article 247 of the Law, so that GASTRANS d.o.o. is entitled to grant an access to the New Interconnector in accordance with item 8 of the disposition of this Act;

3) refrain from discriminating potential users or group of users of New Interconnector including entities related to GASTRANS d.o.o from Article 248 paragraph 1 item 12) of the Law, so that GASTRANS d.o.o. is entitled to grant an access to the New Interconnector in accordance with item 8 of of the disposition of this Act;

4) regulate in the network code the manner of capacity allocation and congestion management mechanisms in accordance with Article 254 paragraph 1 items 7) and 8) of the Law, so that network code regulates these matters in compliance with this Act;

5) publish methodology regulating the method of price determination for the calculation of long-term natural gas transmission services, including the publication of cost structure, the amounts of the tariff and the manner of their harmonization in accordance with Article 248 paragraph 1 items 13) and 15) and Article 254 paragraph 1, items 17) and 18) of the Law, except from publishing reserve (initial) price for short term capacities;

6) keep records set out in Article 248 paragraph 1 item 17) of the Law;

7) apply the balancing rules, as regulated in Article 248 paragraph 1 item 8), Article 254 paragraph 1, item 16), Articles 293 and 296 of the Law, so that GASTRANS d.o.o. is entitled to establish and enter into operator balancing agreements and to stipulate in the gas transmission agreements and network code provisions which may deviate from the balancing rules governed by applicable law, and

8) contract the access to the New Interconnector on the basis of the agreement on access (gas transmission agreement) which contain elements prescribed by the Article 284 of the Law and network code under Article 254 in relation to Article 53 paragraph 1 item 4) of the Law, so that GASTRANS d.o.o. is entitled to execute the gas transmission agreements, and to enact the network code complying with this Act, which shall be subject to approval of the Agency.

The exemption from the above cited provisions of the Law derives as a consequence of exemption of GASTRANS d.o.o. granted under this Act, argumentum a contrario, rejection of the exemption from the obligations set out under cited articles would limit the granted exemption from third party access.

On the other hand, the Agency considers that GASTRANS d.o.o. should not be exempted from:

Article 249 of the Law as this Article regulates the prohibition of the transmission system operator to trade with natural gas for the purpose of securing necessary quantities of natural gas for the operation of the pipeline and not to transparency rules so the Agency rejects the request of GASTRANS d.o.o. to be exempted from the Article 249 of the Law; and

- Article 285 of the Law as this Article regulates the right of transmission system operator to refuse access to the system, and not obligation to offer access to the system, so the Agency rejects the request of GASTRANS d.o.o. to be exempted from the Article 285 of the Law.

Although the Agency accepts the exemption from third party access pursuant to Article 283 paragraph 1 of the Law in respect to terms and conditions of the natural gas transmission services as explained above, such exemption is granted with the obligation of GASTRANS d.o.o. to realize the terms of the agreement on long-term natural gas transmission in long-term capacity (model of the agreement), and a network code, in accordance with the Scope of the exemption granted under this Act and with the application of the following requirements:

1) right of the user to the "secondary trade" of capacities (the assignment of long-term and short-term transmission agreements to third parties, as well as the right to amend the long-term agreement in favour of the third party);

2) right of GASTRANS d.o.o. to, with the written consent of the users of the long-term capacity, offer and contract part or all of the long-term capacity of such user, in its own name and for its own account, to market participants in accordance with the applicable regulations governing capacity management mechanisms for the period of the gas month, gas quarter or gas year, with the obligation of GASTRANS d.o.o. to reduce the agreed compensation to the user who gave the consent, in the manner and at the prices determined by the applicable regulations;

3) obligation to regulate transparent and non-discriminatory rules for the announcement of quantities, acceptance and change of announcements (renominations), in accordance with the regulations;

4) to limit the scope of announced (nominated) quantities for transmission in case of overload, system jeopardizing;

5) to limit the provision of services on the basis of application of measures established in accordance with the applicable regulations in case of a system disruption or the occurrence of natural gas shortages and in emergency cases;

6) obligations of data exchange with adjacent operators, execution of interconnection agreements, performance of flow control, measurement of natural gas quality, harmonization of quantities and allocation, application of prescribed units for measurement of delivered gas, odorization, submission of information on measured quantities to users and system operators to which is connected in accordance with the applicable regulations governing the operation of the transmission system and the obligations of the transmission system operator;

7) cooperation with the adjacent operators to which systems New interconnector is connected; and

8) compliance with the transparency rules, except in the part specified in item 9 paragraph 1, point 5) of the disposition of this Act.

The Agency notes that the network code shall also be applicable to a short-term capacity offered by GASTRANS d.o.o. in accordance with this Act and the agreement on short-term natural gas transmission shall be based on the principles of the agreement on long-term natural gas transmission applicable as well as that GASTRANS d.o.o. shall also keep records of transactions and submit data on request to the Agency for the purpose of performing tasks within its competence.

These requirements are imposed by the Agency in order to enable non-discriminatory treatment of the users of the New Interconnector (save to the extent arising from the Scope of Exemption granted by this Act) and secondary trade with the capacities, as well as regular operation of the New Interconnector and cooperation with adjacent system operators.

In the Request for Exemption, GASTRANS d.o.o. explicitly made reference to the following legislation currently in force in the European Union but which are expected to be transposed in the legislation of the Republic of Serbia or become directly binding: 1. Commission Regulation (EU) No 312/2014 of 26 March 2014 establishing a Network Code on Gas Balancing of Transmission Networks (hereinafter **NC BAL**) 2. Commission Regulation (EU) No 2015/703 establishing a network code on interoperability and data exchange rules (hereinafter **NC IDE**); 3. Commission Regulation (EU) No 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems (hereinafter **NC CAM**); and 4. Commission Regulation (EU) No 2017/460 establishing a network code on

harmonized transmission tariff structures for gas (hereinafter **NC TAR**); - NC BAL, NC TAR, NC IDE and NC CAM hereinafter collectively referred as the **EU Network Codes**

With regard to the Request, the Agency notes that the EU Network Codes contain provisions on their applicability to non-exempted capacities in major new infrastructures which have received exemption from Article 32 of the Gas Directive, which is why, according to the understanding of the Agency, it is grounded to grant the exemption from the application of these Network Codes on exempted capacities once and if they are transposed to the legislation of the RS: Therefore, the Agency accepts the argumentation of GASTRANS d.o.o that certain provisions of the EU Network Codes should be applicable to GASTRANS d.o.o and to the New Interconnector, taking into account that by this Act the Agency has accepted GASTRANS d.o.o's request to exempt 100% of capacities.

GASTRANS d.o.o requested that the following articles are not applicable to it and to the New Interconnector:

1) The rules on the allocation of firm capacity products (annual, quarterly, monthly, daily) as currently stipulated in Articles 8 – 18 of NC CAM.

2) The rules on bundled capacity as currently stipulated in Articles 19 - 21 of the NC CAM.

3) The rules on incremental capacity as currently stipulated in Articles 22 – 30 of the NC CAM.

4) The rules on third party trade nomination as currently stipulated in Article 4, Articles 20-22, Articles 29-30, Article 31, Article 38, Article 43 and Article 44 of the NC BAL.

The application of the above rules would restrict GASTRANS' ability to determine appropriate project finance provisions in the gas transmission agreement terms and conditions in order to promote project bankability. Accordingly, the Agency in the Preliminary Act sets out the obligations and principles prescribed by EU Network Codes which will not be applicable to GASTRANS d.o.o and the New Interconnector. However, the Agency assesses the request of GASTRANS d.o.o. to be exempted from the rules on interim measures in the absence of the short-term liquidity under Art. 47-50 of the NC BAL as groundless as the Agency believes that these rules do not interfere with the scope of the exemption granted by this Act, so that these articles of NC BAL shall be applicable once they become legislation of the Republic of Serbia.

The Agency assessed the request of GASTRANS d.o.o. as groundless to be exempted from the provisions for which the Agency requires to be applicable to GASTRANS d.o.o. once and if they become part of the legislation of the Republic of Serbia, as follows:

1) Rules on corporate principles as currently stipulated in Articles 4-7 of NC CAM-a;

2) rules on interconnection agreement as currently stipulated in Articles 3-5 of NC IDE;

3) rules on flow control as currently stipulated in Article 6 of NC IDE;

4) rules on gas quantity and gas quality measurement as currently stipulated in Article 7 of NC IDE;

5) rules on matching process as currently stipulated in Article 8 of NC IDE;

6) rules on allocation of gas quantities as currently stipulated in Article 9 of NC IDE;

7) rules on exceptional events as currently stipulated in Article 10 of NC IDE;

8) rules on disputes as currently stipulated in Article 11 of NC IDE;

9) rules on the amendment of interconnection agreement as currently stipulated in Article 12 of NC IDE;

10) rules on sets of units for data exchange and data publication as currently stipulated in Articles 13 and 14 of NC IDE;

11) rules on gas quality and odorization as currently stipulated in Articles 15-19 of NC IDE;

12) rules on data exchange as currently stipulated in Articles 20-24 of NC IDE;

13) rules on trade nominations and allocation as currently stipulated in Article 5 of NC BAL;

14) rules on nominations and renominations as currently stipulated in Articles 12-18 of NC BAL;

15) rules on within day obligations as currently stipulated in Articles 24-28 of NC BAL; and

16) rules on information provision (general, inputs and offtakes) as currently stipulated in Articles 32-37 of NC BAL.

Assessment of the fulfilment of conditions for the exemption from regulated prices

GASTRANS d.o.o. requested for the New Interconnector to be exempted from the application of regulated tariffs pursuant to the Article 283 paragraph 1 of the Law, and in connection with Article 50 paragraph 1 item 6) of the Law, as well as to Articles 90, 92 and 248 paragraph 1 item 10) of the Law GASTRANS requests to apply the

methodology it enclosed as a draft methodology in the Addendum. The Tariff Methodology is based on that the existing regulated tariff prescribed by the methodologies adopted by the Agency to determine the system access price is not sufficient to allow for the adequate recover of investment cost associated with the New Infrastructure and the regulated tariff is subject to change which makes it difficult to plan the income necessary to ensure Project financing. In the Addendum, GASTRANS d.o.o. stressed that the regulated tariff is designed to cover the operating cost of existing infrastructure but is limited in the ability to recover investment costs. The Agency agrees with the reasoning put forward by GASTRANS d.o.o. that the regulated tariff methodology cannot provide the return of investments in the New Interconnector.

The Agency notes that its methodology is designed so to recover certain necessary income through the applicable tariff in a certain year. The methodology stipulates as its guiding principles that the tariff is to be based on transparency and non-discrimination and any adjustment of the tariff is to be made in line with the prescribed procedure and with the approval of the Agency in order to ensure a non-discriminatory application of the tariff on all transmissions system users for the relevant entry and exit.

As the tariff is calculated for long term product on an annual basis, a year, as stipulated in the methodology, is defined as a period of 365 or 366 days for the first year from the start of operation and then for subsequent years as a period of 365 or 366 days following the end of previous year. The Agency requested to specify the year in line with financial or gas year, but it conceded to GASTRANS d.o.o. request to maintain the current structure of the year due to uncertainties around the start of the New Interconnector.

Regarding the definition and derivation of the necessary income, the Agency requested, and GASTRANS d.o.o. agreed to determine the cost factors within this definition in order to promote transparency and allow clear supervision of the formation of the necessary income, which will be the subject of consideration and will constitute a correction mechanism for the previous year when the estimated necessary income is larger than the actual necessary income (i.e. the payments acquired by the application of the tariff resulted in an over-recovery), all with a view to returning this excess to the transmission system users through lower tariffs in the subsequent years. Accordingly the methodology proposed by GASTRANS d.o.o. defines the necessary income for all years during which exit Horgoš is fully operational for the entire year as the sum of operational costs, maintenance costs, costs for compensation of natural gas loss, depreciation costs, and necessary return on CAPEX. The necessary income shall be decreased by all income from sale of capacities that have not been contracted as long-term firm capacities, or have been contracted but are not being used, and shall be adjusted by a correction element (reflecting the difference between actual and estimated necessary income in the previous year). In line with the Tariff methodology, the decrease of the tariff should occur as a principle rule, while the decision whether to increase the tariff or not rests with GASTRANS d.o.o.

The Agency requested that this needs to be supplemented by a clear definition of necessary return of CAPEX that allows for and guarantees sufficient return on shareholder capital investment as well as interest and principal payment of debt associated with the construction of New Interconnector. The Agency agreed with the proposal of GASTRANS d.o.o. that in the years in which exit Horgoš is not fully operational (which is a major source of outlet capacity and thus the largest tariff income), the necessary income would be inadequate as it would result in significant fluctuation in tariffs. The Agency supports the proposal of Gastrans that the necessary income for the first year of operation and the years before exit Horgoš is fully operational for the entire year shall not include depreciation costs and necessary return on CAPEX and that the tariffs for the respective entry and exit points shall be determined as the quotient of the part of the necessary income distributed to that entry or exit point and assigned capacities.

Distribution of the necessary income between exit points shall be carried out depending on capacity and transport distance from entry to exit points. For the years after the first year of operation until exit Horgoš becomes fully operational for the entire year, the tariffs shall be determined based on the ratio between the tariffs for the first year of operation and the projected tariffs for the year in which exit Horgoš is fully operational for the entire year and the respective compound annual growth rates in that period. In the event that the exit Horgoš becomes operational partway through the year in which it starts operating, the tariff for that exit shall be determined by multiplying the exit tariff for

the Republic of Serbia in the year preceding the full exploitation of capacity with the estimated ratio of the tariff for the exit towards Hungary divided by the tariff for exits in the Republic of Serbia in the subsequent year.

The methodology of GASTRANS d.o.o. stipulates to calculate the tariff by splitting the recovery of the necessary income between entry and exit using a factor 60% via entry and 40% via exits. However, the Agency does not agree with the splits as this, from the Agency's view, constitutes cross subsidization of capacity of exit Horgoš by the exits into the Serbian market and thus the Agency prescribed the splits to be 50% via entry and 50% via exits.

The tariff for reverse flow is set as 90% of the relevant tariff for direct flow and the reverse flow will be offered to system users on interruptible basis, so it is reasonable to have a discount to an uninterruptible flow tariff. Since the market test showed the interest in long term capacity for the whole period of the requested exemption at significant volumes, the probability for interruption is very low. Having considered the above and taking into account the existing practice on the international market, the tariff for virtual reverse flow amounts to 90 % of the tariff for physical flow in the point between the two transmission system operators in Germany (GRT Gaz Deutschland GmbH, Gasunie, Deutschland Transport Service Fee). The Agency assessed that the level of 90% of tariff for reverse flow seems to be reasonable.

The methodology of GASTRANS d.o.o. proposes to calculate the tariffs for an entry point based on the contracted capacity in line with NC TAR Article 5 paragraph 1 subparagraph a.ii and consequently, expresses the tariff for the transmission system users' booked entry capacity in €/kWh/h/a. The tariffs for the exits are based on forecasted contracted capacity and distance in line with NC TAR Article 5 paragraph 1 subparagraph a.iv where exits to the Serbian market are clustered into one homogenous exit group. The tariff for the transmission system users' booked exit capacity is expressed in €/kWh/h/a.

The Agency accepts this particular approach to the calculation of the entry and exit tariff as it is non-discriminatory and transparent, and allocates the cost through elements determining the relative cost of using entry and respective exits.

The methodology recognizes that the tariff, while calculated pursuant to the above described manner, will need to be adjusted annually by way of a correction element and with more accurate forecast for the cost that is applicable in the relevant year. The Agency agrees with the necessity to assure the adequacy of the recovery of necessary income and thus the amount of tariffs.

The Agency requires from the requesting party to include stakeholder consultations, such that the adjustment process is transparent and allows for adequate monitoring of compliance by the Agency. Accordingly, the Agency stipulates that the adjustment mechanisms shall be regulated so that GASTRANS d.o.o. forms the new tariff in accordance with the manner set out above and inform transmissions system users no later than 60 days before the tariff is to become applicable, as well as, submit the tariff calculation and all relevant information to the Agency in sufficient time prior to the 60 days deadline above to allow the Agency adequate time to verify the calculation and data and thus validity of the adjustment of the tariffs.

The Agency took into consideration the proposed tariff methodology and the arguments made by GASTRANS d.o.o. and pursuant to Article 288 accepts the request by GASTRANS d.o.o. to be exempted from the application of regulated tariffs pursuant to Article 283 paragraph 1 of the Law, in relation to Article 50 paragraph 1 items 6-8) of the Law, as well as to Articles 90, 92 and 248 paragraph 1 item 10) of the Law and apply the above stipulated tariff methodology subject to conditions set forth in this Act. The Agency agrees to have an alternative tariff methodology but has opted to regulate the principles pursuant to which GASTRANS tariff methodology should be prepared.

The Agency assesses that there is a justified need to assure that the proposed tariff methodology is and remains transparent and non-discriminatory as well as distributes the cost in such a manner to minimize cross subsidization and limit market distortion, while allowing for adequate return on investment.

In the Request for Exemption GASTRANS d.o.o. pointed out the NC TAR, which is currently in force in the European Union, has not yet become part of the legislation of the Republic of Serbia. NC TAR regulates in detail different aspects of tariffs.

The Agency recognizes that NC TAR adopted in the Energy Community should start applying in the Republic of Serbia in the course of the Duration of the Exemption. In order to fully determine the regulated price exemption regime, and for transparency, compliance and predictability reasons, the Agency believes that the above-stated aspects need to be regulated by this Act, rather than being left for future regulation, once NC TAR become applicable in the Republic of Serbia. Namely, NC TAR contains provision on its applicability to non-exempted part of major new infrastructures which have received exemption pursuant to Article 36 of the Gas Directive. In cases where the specific nature of interconnectors has been acknowledged at European level by an exemption in accordance with Article 36 of the Gas Directive or by other means, the national regulatory authorities should have the power to grant derogation from requirements of this Regulation, which would jeopardize the efficient operation of such interconnectors. As already explained, the Agency agrees that certain provisions of the NC TAR should not apply to GASTRANS d.o.o once when this regulation becomes part of the legislation of the Republic of Serbia.

GASTRANS d.o.o requested that Articles 5, 6-8, 10, 11, 14-16, 17-20, 21-24, 26-33 of NC TAR are not applicable to it and to the New Interconnector (standardized rules on cost allocation assessment, establishing alternative price methodologies and their application to entry point and exit points, standardized rules on reserve price calculation, standardized rules on reconciliation of tariff revenue, standardized rules on pricing of bundled capacity, standardized rules on pricing at virtual point, standardized rules on tariff clearing price calculation, standardized rules on payable price calculation, requirements to consult with network users and adjoining network operators on tariff setting, standardized rules on publication requirements, and standardized rules on pricing of the incremental capacity).

The Agency analysed these arguments and concluded that the following obligations and principles shall not be applicable to GASTRANS d.o.o. if these regulations become applicable in the Republic of Serbia during the exemption period as they are not tailored to the right of the exemption from the regulated price that is granted to allow the project implementation.

The Agency took into account the incompatibility of NC TAR with the needs of the New Interconnector. NC TAR was developed for valuation of existing capacity and short term allocations up to one year. To finance the New Interconnector, it is needed to provide a tariff that is both long-term and capable of taking into consideration construction costs, overrun costs, adjustment etc., and it would not be appropriate for these principles to be applicable in the case of the New Interconnector. Therefore, a common, suitable, set of principles is needed and as NC TAR has not been yet implemented in Serbia, the retroactive application of its rules is not possible. Instead, the Agency instructed to include, to a greatest possible extent, the principles and objective of NC TAR during the methodology and tariff model harmonisation procedure for the purpose of determining the tariff. The Agency also notes that a number of other pipelines have obtained exemptions from NC TAR for similar reasons.

The Agency refuses to accept the request of GASTRANS d.o.o. for exemption from the standardized rules on payable price calculation, which rules are stipulated in the Article 24 of the NC TAR and the standardized rules on publication requirements, which rules are currently stipulated in Articles 29-32 of NC TAR, as the Agency believes that these rules does not interfere with the scope of the granted exemption.

By the Preliminary Act the Agency also decided on the following matters:

- if GASTRANS d.o.o. changes the key technical parameters of the New Interconnector, it is obliged to inform the Agency about the final technical design, and that rights and obligations set out in this Act shall remain in force.
- all rights determined by this Act are granted on the basis that GASTRANS d.o.o. shall be the owner of the New Interconnector and manage the New Interconnection as a system operator in accordance with this Act.
- during the 20-year exemption period, in line with the legal certainty principles, the regulations on ownership unbundling and manner of organizing system operators, third party access, general conditions for natural gas transmission services, methods for determining prices for access to the natural gas transmission system and manner

of managing the transmission system will not affect the scope and manner of exercising the rights granted to GASTRANS d.o.o.

Pursuant to Article 141 paragraph 3 of the Law on General Administrative Procedure prescribing that the administrative act must contain the decision on the costs of the procedure, the Agency decided on the costs and declares that on July 4, 2018, GASTRANS d.o.o. paid the amount RSD 12,110 as an administrative fee for filing the exemption request for the new infrastructure in the natural gas industry and the amount RSD 121,100 as a prescribed administrative fee for issuing the act on exemption in accordance with the Law on public administrative fees ("Official Gazette of the Republic of Serbia", no. 43/2003, 51/2003 -correction, 61/2005, 101/2005 – state law, 5/2009, 54/2009, 50/2011, 70/2011 – adjusted RSD amounts, 55/2012 - adjusted RSD amounts, 93/2012, 47/2013 - adjusted RSD amounts, 65/2013 – state law, 57/2014 - adjusted RSD amounts, 45/2015 - adjusted RSD amounts, 83/2015, 112/2015, 50/2016 - adjusted RSD amounts, 61/2017 - adjusted RSD amounts, 113/2017, 3/2018 - correction and 50/2018 - adjusted RSD amounts).

Based on the above, the Agency concluded that the conditions prescribed under Article 288 paragraph 1 of the Law are fulfilled to grant the exemption upon the applicant's request and the Council of Energy Agency of the Republic of Serbia on the 2nd extraordinary session held on October 1st, 2018, in accordance with the article 136 of the Law on General Administrative Procedure rendered the Preliminary Act by which it decided upon the request as given in the disposition of the Preliminary Act.

v) Procedure following the adoption of the Preliminary Act

Having adopted the Preliminary act, the Agency submitted a copy of the Exemption Request and supporting evidence to the competent authority – Energy Community Secretariat pursuant to Article 288 paragraph 10 of the Law.

Article 288 paragraph 10 of the same Law stipulates that the Agency will immediately submit the Exemption Act and copy of the Exemption Request to the competent authority in line with the obligations arising from the international agreements (to the Energy Community Secretariat pursuant to the Energy Community Treaty).

Article 288 paragraph 12 of the Law prescribes that within a period of 2 months from the day following the receipt of information under paragraph 10 hereof, the competent authority may, in line with the obligations arising from the international agreements, adopt the decision requiring the Agency to amend or withdraw the Exemption Act.

Article 288 paragraph 13 of the Law prescribes that in case that the competent authority issues the decision under paragraph 12 of this Article, the Agency shall take the utmost account of such decision.

Article 288 paragraph 14 of the Law prescribes that when the final decision of the Agency differs from the opinion of the competent authority, the Agency shall provide and publish, along with its decision, an explanation of the decision.

Article 288 paragraph 15 of the Law prescribes that the deadline under Paragraph 12 of this Article may be extended for an additional period of two months if the competent authority, in accordance with the obligations arising from confirmed international agreements, requires additional information, and the extension shall commence after the day of receipt of complete information.

Acting upon the request of the Energy Community Secretariat to provide additional information pursuant to Article 288 paragraphs 15 of the Law and no later than December 2nd, 2019, the Agency provided additional information requested by the Secretariat within the prescribed period for the purpose of preparing the opinion under Article 288 paragraphs 12-14 of the Law.

The Energy Community Secretariat, as a competent body in line with the obligations arising from the international agreements, has on February 2nd, 2019 delivered to the Agency the Opinion 1/19 as of February 1st, 2019, assessing the content of the Preliminary Act. The Secretariat's Opinion was delivered to the Agency in accordance with Article 288 paragraph 12 of the Law given that the Energy Community Secretariat notified the Agency in its opinion that it refuses to accept the exemption of the New Interconnection from third party access, unless the Agency, in its final decision, does not ensure that the exemption is granted with the provision of conditions and safeguards to a full extent as determined in Items 174-200 of this Opinion.

III. ENERGY COMMUNITY SECRETARIAT OPINION 1/2019

on the exemption of the Gastrans natural gas pipeline project from certain requirements under Directive 2009/73/EC by the Energy Agency of the Republic of Serbia

1. Procedure

1. On 1 October 2018, the Energy Community Secretariat ("the Secretariat") was notified by the Energy Agency of the Republic of Serbia ("AERS") of the latter's Decision No. 40/2018-D-03/46 of 1 October 2018 concerning an exemption granted to Gastrans d.o.o. Novi Sad ("Gastrans") from the requirements of Articles 9(1), 32, 41(6), (8) and (10) of Directive 2009/73/EC¹ ("the Decision").

2. Based on Article 288 of the Energy Law of the Republic of Serbia ("the Serbian Energy Law")², which transposes Article 36 of Directive 2009/73/EC, the Decision exempts the Gastrans natural gas pipeline project ("the Project"), as described in Section 2 of this Opinion, from certain requirements under Directive 2009/73/EC regarding ownership unbundling of the natural gas transmission system operator, third-party access to the natural gas transmission system, and regulated setting of natural gas transmission tariffs. The scope of the exemption, its respective effects and compliance with Article 36 of Directive 2009/73/EC are the subject of this Opinion.

3. Pursuant to Article 36(9) of Directive 2009/73/EC, "*within a period of two months from the day following the receipt of a notification, the Secretariat may issue an opinion inviting the regulatory authority to amend or withdraw the decision to grant an exemption. That two-month period may be extended by an additional period of two months where further information is sought by the Secretariat. That additional period shall begin on the day following the receipt of the complete information*". In a letter dated 20 November 2018, the Secretariat submitted to AERS a set of clarification questions concerning the Decision and the Project. By consequence, the deadline for submitting the Secretariat's Opinion was extended by an additional period of two months. AERS' response to the Secretariat's questions was provided by letter dated 3 December 2018.

4. In the course of the procedure, several meetings were held between the Secretariat and AERS concerning the Decision. On several occasions, the Secretariat met representatives of Gastrans presenting the Project. Further, the Secretariat organised a public consultation between 24 October 2018 and 9 November 2018, inviting interested parties to provide their observations on the Decision. During the public consultation, comments from ENGIE, *Ukrtransgaz*, and the Embassy of the United States of America in Austria were received. Additional information received from AERS and Gastrans as well as observations provided by other interested parties were also considered by the Secretariat and, to the extent necessary, reflected in this Opinion.

5. According to the third subparagraph of Article 36(9) of Directive 2009/73/EC, "*the notifying bodies shall take the utmost account of a Secretariat opinion that recommends to amend or withdraw the exemption decision. Where the final decision diverges from the Secretariat's opinion, the regulatory authority concerned shall provide and publish, together with that decision, the reasoning underlying its decision. Diverging decisions shall be included in the agenda of the first meeting of the Ministerial Council following the date of the decision, for information and discussion*".

1 Directive 2009/73/EC of the European Parliament and of the Council of 13.07.2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC as adopted and adapted by Decision 2011/02/MC-EnC of the Ministerial Council of the Energy Community of 6.10.2011.
2 Official Gazette No 145/2014.

2. Description of the Project

6. According to the Decision, the Project consists of a future natural gas transmission pipeline which is planned to pass through the territory of Serbia in the approximate length of 400 km, and to connect the Serbian natural gas transmission system with those of Bulgaria and Hungary, including four metering stations and one compressor station to be built on the territory of Serbia. The projected technical capacity of the new pipeline is 13.88 bcm annually ("bcm/a").

7. The new pipeline is supposed to enter the territory of Serbia at Zaječar, where it should connect to the Bulgarian gas transmission system operated by Bulgartransgaz EAD ("Bulgartransgaz"). Four exit points are envisaged, i.e. one exit point at Horgoš connecting the new pipeline with the Hungarian gas transmission system operated by FGSZ Zrt. ("FGSZ"), and three exit points – Paraćin, Pančevo and Gospođinci – connecting the pipeline with the existing Serbian gas transmission system, operated by JP Srbijagas Novi Sad ("Srbijagas"). (....). According to the Decision, the technical parameters of the Project may still be adjusted, including the routing of the new pipeline as well as the locations of the entry/exit points.

8. The schedule presented by Gastrans foresees the completion of construction activities to enable the start of the pipeline's commercial operation ("COD") on..... The date for reaching its full transportation capacity is envisaged for.....).

9. The promoter of the Project envisaged as a future operator of the new pipeline is Gastrans, the successor of South Stream d.o.o. Novi Sad which was originally founded on 30 April 2012 for the construction of the Serbian branch of the South Stream pipeline project. The original South Stream project was based on intergovernmental agreements between the Russian Federation and the countries through which the pipeline was supposed to pass. It was abandoned after the Secretariat and the European Commission had raised concerns regarding the compliance with the *acquis communautaire*.

10. The company was re-established on 26 January 2018, and the company's name was changed to Gastrans as of 1 February 2018. Gastrans is fully owned by South Stream Serbia AG, which is registered in Switzerland and owned by PJSC Gazprom Transgaz Krasnodar (51%), a subsidiary of the Russian natural gas holding PJSC Gazprom ("Gazprom"), and Srbijagas (49%). Gastrans has two appointed directors: Mr. Dusan Bajatovic (also the General Director of Srbijagas) and a representative of Gazprom, who remained in their respective positions following the re-establishment of the company in January 2018.

11. Both Gazprom and Srbijagas, the ultimate shareholders of Gastrans, are dominant players on the Russian and Serbian gas markets respectively and Gazprom being dominant on both markets. Gazprom possesses more than (72%) of Russia's proven natural gas reserves and accounts for (...%) of the national natural gas output. The company's corporate group dominates domestic transmission, distribution and supply, and it owns the Unified Gas Supply System (UGSS), which is an exclusive route for export of piped natural gas, *inter alia*, to Europe³. Srbijagas, a 100% state-owned Serbian natural gas incumbent, is engaged in gas transmission, distribution and supply activities and dominates the market both at wholesale and retail levels.⁴ The position of Gastrans' ultimate shareholders on the relevant markets, and the impact of the Project on these markets is further considered in Section 4.2.1 of this Opinion.

3 Energy and Natural Resources Global Guide: Oil and gas regulation in the Russian Federation, Practical Law by Thomson Reuters, 01.05.2018; <http://www.gazprom.com/about/>.

12. The Project aims at transporting natural gas from Turkey (using capacities of the so-called TurkStream pipeline⁵) and Bulgaria, where a new pipeline is to be built. Downstream of the Serbian gas system, the gas transmitted through the pipeline is to be transported to Hungary. The Project was triggered by the interest of (.....)

13. As part of a natural gas corridor from the Russian Federation to Central Europe, the Project essentially envisages the flow of natural gas from the Bulgarian to Serbian and further downstream to the Hungarian natural gas systems. In addition to the Project located in Serbia, the natural gas transmission system operators in the neighbouring countries – Bulgartransgaz and FGSZ – are expected to complement their respective existing natural gas transmission systems by new sections to which Gastrans could connect its pipeline upstream and downstream. However, neither of the two transmission system operators has requested or plans to request an exemption similar to the one requested by Gastrans.

14. On 2 February 2018, Gastrans submitted to AERS an initial request for an exemption (“the Initial Exemption Request”). Based on AERS’ decision⁷ Gastrans proceeded with the market test for the use of the new infrastructure in the form of collecting non-binding bids from market participants. The market test for the Project was carried out by Gastrans in the period between 5 March 2018 and 30 April 2018.

15. By the deadline for registration set in Gastrans’ public invitation, i.e. by 5 April 2018, six participants had registered for participation in the market test. Another four entities submitted information about their interest in capacity of the new pipeline after the deadline or without complete registration. The Secretariat analysed the bids based on an aggregated information provided by Gastrans in the addendum to the Initial Exemption Request (“the Amended Exemption Request”) as submitted to AERS on 29 June 2018.⁸ The Secretariat’s findings are provided in Section 4.2.1(a) (i) of this Opinion.

16. In the Amended Exemption Request, and based on the results of the market test, Gastrans requested an exemption from the obligations under the Serbian Energy Law to unbundle the company as future transmission system operator of the new pipeline, to grant third-party access for 88% of the new pipeline’s technical capacity,⁹ and to apply regulated tariffs for the transmission of natural gas in the corresponding volumes. The exemption was requested for a period of 20 years from the pipeline’s COD.¹⁰

4 Energy Community Secretariat, Annual Implementation Report 2017 (01.09.2018), p. 162-163.

5 TurkStream is a natural gas pipeline project directly connecting, through its offshore segment under the Black Sea, the Russian and Turkish natural gas systems. The pipeline has two lines with a total capacity of 31.5 bcm annually. The offshore part of the pipeline being complete in November 2018, it is expected to become operational by the end of 2019. The TurkStream project is implemented by South Stream Transport B.V., a subsidiary of Gazprom.

6 6 Cf. Gazprom Export, letter to Gastrans, Srbijagas and the latter’s subsidiary Transportgas Srbija d.o.o. Novi Sad (“Transportgas Srbija”) dated 26.05.2017.

7 AERS Decision No 40/2018-D-03/1 of 09.02.2018.

8 Section 5.2 of the Amended Exemption Request.

9 Instead of a full capacity (100%) exemption as requested by Gastrans in the Initial Exemption Request. Cf. Section 6.1 of the Amended Exemption Request.

10 Instead of a period of 25 years as requested by Gastrans in the Initial Exemption Request.

3. The Decision

17. In its Decision, AERS decided to grant “to GASTRANS d.o.o. Novi Sad [...] an exemption in respect of the future gas interconnector, described in Item 2 of the disposition of this Act, from the application of third party access rules (general rules for capacity allocation and terms and conditions for natural gas transmission services), and regulated prices under Article 283 paragraph 1 of the Energy Law (hereinafter referred to as: “Law”) and the exemption from the implementation of ownership unbundling requirements under Article 224 of the Law, as further determined in Items 3-17 of the disposition of this Act.”

18. The Decision thus exempts the Project, and in particular the operation and use of the new pipeline within the territory of Serbia, for a period of 20 years from the new pipeline’s COD from: (i) the unbundling of the pipeline’s system operator; (ii) regulated third-party access to 88% of the pipeline’s capacity; and (iii) setting of regulated tariffs for the transmission of natural gas through the new pipeline. The exemption is subject to Gastrans’ compliance with conditions set by AERS as further assessed in this Opinion.

19. Firstly, the Decision exempts Gastrans, as the future transmission system operator in charge of the new pipeline, from the mandatory obligation to unbundle from any other activities and interests in the energy sector pursuant to Article 9 of Directive 2009/73/EC. This exemption means that Gastrans may remain under the control of one or more vertically integrated companies engaged in the production and/or supply of natural gas besides transmission. For this exemption to be effective, the Decision establishes a number of mandatory conditions to be met by Gastrans, including the adoption of a compliance program, the appointment of an independent compliance officer and the designation of an ad hoc body to solve complaints regarding capacity allocation in the new pipeline, possession of all assets necessary to perform the transmission activity, having an independent staff, separate premises, and operating independently from related companies. The Decision also specifies AERS’ monitoring rights concerning Gastrans’ independent conduct. By this exemption, the unbundling regime enshrined in Article 9 of Directive 2009/73/EC is replaced with a set of tailor-made requirements to be complied with by Gastrans during the entire exemption period.¹¹

20. Secondly, the Decision exempts the new pipeline from unrestricted third-party access to its natural gas transmission capacities in accordance with Article 32 of Directive 2009/73/EC based on an objective and non-discriminatory capacity allocation procedure. In particular, Gastrans is allowed to allocate and contract up to 88% of the maximum technical capacity of the new pipeline exclusively for the benefit of its ultimate shareholders – Gazprom and Srbijagas. The remaining 12% of the maximum technical annual capacity of the new pipeline may be allocated and contracted to companies other than Gazprom and Srbijagas provided they had submitted non-binding bids in the market test.¹² In other words, this exemption makes available up to 88% of the new pipeline’s capacities for exclusive use by Gazprom and/or Srbijagas, whereas the rest of capacities can be made available only to those other companies which participated in the market test. Thus the entire capacity of the new pipeline is exempted from third-party access for 20 years. The Decision provides, however, that in case the long term capacity demand for Gastrans is smaller than the nominal technical capacity of the new pipeline, a residual 10% of its technical capacity is set aside for short term bookings.

21. Thirdly, the Decision exempts Gastrans from the obligation to apply regulated tariffs for the transmission of natural gas through the new pipeline and related services as required under Articles 41(6), (8) and (10) of Directive 2009/73/EC. Instead, Gastrans is required to set network tariffs under its approved methodology and in accordance with the conditions established in the Decision. Tariff- setting by Gastrans will be subject to AERS’ supervision.¹²

¹¹ The Decision, items 3, 4, 5, 6 and 7 and chapter 6.5, p. 57-63.

¹² The Decision, items 11 and 12 and chapter 6.5, p. 72-77.

22. The exemption is granted under the condition that Gastrans becomes the owner of the new pipeline, once it is constructed, and manages it as a transmission system operator. The Decision will lose its validity if Gastrans does

not start constructing the new pipeline within two years from the date of the AERS' final act on exemption and/or does not commence the new pipeline's operation within five years from the date of AERS' final act on exemption.

23. It is envisaged in the Decision that Gastrans' compliance with all mandatory requirements set therein will be assessed through the certification procedure to be conducted under the terms and conditions stipulated in the Energy Law pursuant to Articles 10 and 11 of Directive 2009/73/EC.

4. The Secretariat's assessment of the conditions for an exemption

24. In the following, the Secretariat, gives its Opinion on the compliance of the AERS Decision with the conditions for an exemption listed in Article 36(1) of Directive 2009/73/EC.

4.1. Major new gas infrastructure, i.e. interconnectors, LNG and storage facilities (Article 36(1) Directive 2009/73/EC)

25. Article 36(1) of Directive 2009/73/EC limits the scope of projects which may benefit from an exemption from certain provisions of the Directive to major new gas infrastructure which, in the case of a pipeline project such as Gastrans, needs to qualify as an interconnector. By contrast, pipelines not qualifying as interconnectors are not eligible for an exemption.

26. Pursuant to Article 2(17) of Directive 2009/73/EC, an interconnector is defined as "a transmission line which crosses or spans a border between Member States for the sole purpose of connecting the national transmission systems of those Member States". When incorporating the Directive in the Energy Community, the Ministerial Council adapted that provision as follows: "'interconnector' means a transmission line which crosses or spans a border between Contracting Parties for the sole purpose of connecting the national transmission systems of those Contracting Parties" (emphasis added). Article 2(25) of the Serbian Energy Law defines an interconnector as "... a natural gas pipeline ... that crosses the borders between the states for the purpose of connecting their systems, as well as equipment that is used for connection of the energy systems".

4.1.1. The existence of an "interconnector"

27. As regards the qualification of the Gastrans project as an interconnector within the meaning of Article 36(1) of Directive 2009/73/EC, the Decision is based on the assumption that the pipeline to be built by Gastrans will connect to the Hungarian and Bulgarian national transmission systems following a "border to border" design, with exit and entry points "to be situated on the Serbian-Hungarian border and the Serbian-Bulgarian border".¹³ For the purpose of connecting to Gastrans, both the Bulgarian and the Hungarian system operators are expected to build new gas pipelines. The upstream connection with Bulgaria is envisaged near Zajecar (Serbia) and the downstream interconnection at the border station with Hungary near Horgos (Serbia)¹⁴ According to the Amended Exemption Request, "the exact location of the entry point at the Bulgarian-Serbian border and the exit point Horgos at the Hungarian-Serbian border are still being confirmed. In both cases, the exact location will be agreed with the adjoining transmission system operators FGSZ and Bulgartransgaz, whereby in any case one of the connections will be on the territory of the Republic of Serbia and the another one on the territory of Bulgaria/Hungary."¹⁵ In a response to the Secretariat's questions of 20 November 2018, AERS

13 Information provided by AERS by letter dated 16.03.2018.

14 Initial Exemption Request p. 1, 10, 16; Amended Exemption Request, p. 12.

15 Amended Exemption Request, p. 12.

essentially confirms that the exact location of the interconnection points is still unclear.

28. The uncertainty as to whether and where the Project will be interconnected with the Bulgarian and Hungarian transmission systems calls for a verification as to whether the Gastrans project constitutes an interconnector within the meaning of Article 36 of Directive 2009/73/EC.

29. At the outset, the Secretariat recalls that the notion of an interconnector must be interpreted strictly, as Article 36 of Directive 2009/73/EC is an exception to the general rules of the internal market, and the legislator of the Third Package did not intend to exempt purely domestic infrastructure.¹⁶ The notion of an interconnector as defined by Article 2(17) of Directive 2009/73/EC ultimately requires a pipeline to cross a border.¹⁷

30. As requests for exemptions are typically made during the planning stage of a pipeline project, it is in principle appropriate to consider the design pursued by the project developer for the determination of the notion of an interconnector. The definition in Article 2(17) of Directive 2009/73/EC also refers to the "purpose" of a transmission pipeline¹⁸. (.....)

31. That said, Article 2(17) of Directive 2009/73/EC is based on a technical, not an economic notion of interdependence. The mere commercial interest of shareholders and shippers in transit of gas across borders does not suffice to for the infrastructure to be qualified as an interconnector.

32. At the project stage, the Secretariat thus deems an objective likelihood for the future creation of physical interconnections necessary. Otherwise, an exemption under Article 36 of Directive 2009/73/EC could ultimately depend on wishful thinking of a project promoter. This is of particularly importance in a case, as the one under scrutiny, where the national regulatory authorities of the neighbouring countries to which the infrastructure to be exempted is supposed to connect, have not received corresponding exemption requests.

33. Instead, the regulatory authorities of Hungary and Bulgaria, in their responses to a letter by AERS of 17 July 2018, expressed concern as regards an exemption granted to the Project in Serbia. The Hungarian Energy and Public Utility Regulatory Authority ("MEKH")¹⁹ raised concerns that an exemption granted to Gastrans would frustrate a harmonized incremental capacity procedure based on Commission Regulation (EU) 2017/459 ("the CAM Network Code")²⁰ across all three jurisdictions. Similarly, the Energy and Water Regulatory Commission of Bulgaria ("EWRC") called for a "single regulatory regime" based on the CAM Network Code and identified a risk that "along the pipeline route in the Bulgaria-Serbia-Hungary corridor a different regulatory regime with regard to TPA will be applied". EWRC concluded that an exemption from third-party access rules as requested by Gastrans "would have a negative effect on the development of trade, competition and market integration within the regional market".²¹

16 Cf Commission Decision C(2011)3424 of 20.05.2011 on the exemption of the Gazelle interconnector, paragraph 22.

17 Cf Commission Decision C(2011)3424 of 20.05.2011 on the exemption of the Gazelle interconnector, paragraph 20; Commission Decision C(2015) 1852 of 17.03.2015 on the exemption of the Trans Adriatic Pipeline, paragraph 54.

18 Cf Commission Decision C(2013) 6159 of 17.09.2013 on the exemption of the SK-HU interconnector, paragraph 54.

19 Letter dated 26.07.2018.

20 Regulation 2017/459 of 16.03.2017 establishing a network code on capacity allocation mechanisms in gas transmission systems; adopted for the Energy Community Contracting Parties by Decision 2018/06/PHLG-EnC.

21 Letter dated 15.08.2018.

34. Beyond regulatory concerns in the jurisdictions up- and downstream of Serbia, by the time of issuing the Decision, also the transmissions system operators had not yet taken any final investment decision (“FID”) as to whether or not to build the infrastructure required for connecting with the Project with their respective systems. Moreover, Joint Development Agreements with the neighbouring transmission system operators have still not been concluded as envisaged by Gastrans.²²

35. As regards a potential interconnection with Bulgartransgaz of Bulgaria, an “expansion of the gas transmission network of Bulgartransgaz in the section from the Bulgarian-Turkish to the Bulgarian- Serbian border” is listed as a key project in the company’s Ten-Year Network Development Plan (TYNDP) 2018-2027²³. At the time of issuing the present Opinion, Bulgartransgaz, on the basis of the CAM Network Code, conducted an economic test for incremental capacity for a maximum of 20 years.²⁴ As a result of the final phase of the test, Bulgartransgaz announced on 31 January 2019 that binding offers had been submitted by three shippers for 100% of the offered 11.2 bcm/a long-term capacity. On 21 December 2018, Bulgartransgaz also initiated a tender for the equipment and construction works for a 474.7 km of new pipeline which follows the route previously envisaged for South Stream and runs from Provadia to the Bulgarian-Serbian border,²⁵ where it is expected to cross the border south of the border control point Vrashka Chuka.²⁶ The Secretariat considers that the successful conclusion of the economic test and the procurement activities of Bulgartransgaz demonstrate a sufficiently concrete indication for a future interconnector with the Project.

36. As regards the interconnection with FGSZ of Hungary, project(s) for building new infrastructure and/or upgrading the existing elements of the Hungarian transmission system related to accommodating gas flows from the Project are in a more preliminary phase at the time of issuing the present Opinion. MEKH decided not to include the project connecting to Gastrans in the Hungarian TYNDP due to the uncertainty in the development of the upstream section of the project and indicated that it may be subject to further examinations.²⁷ Yet AERS bases its Decision on the presumption that the final exit point of the Gastrans pipeline will be within the existing metering station Kiskundorozsma,²⁸ on the territory of Hungary. Kiskundorozsma is also the interconnection point between the existing systems of FGSZ and Srbijagas.²⁹ There are currently still several options of linking the Hungarian transmission system to the Project that significantly differ in terms of entry and compressor capacity, new pipeline length, capital expenditure need etc. A decision between the three options and an FID can only be taken once a binding economic test as part of the incremental capacity process under the CAM Network Code has been carried out to identify the precise capacity demand.

37. The uncertainties related to the potential downstream interconnection aside, the Secretariat, based on the developments in Bulgaria, sees a sufficient degree of probability at this point in time for the Project to develop into an interconnector within the meaning of Article 36 of Directive 2009/73/EC.

²² AERS, reply to the Secretariat’s questions.

²³ РЕШЕНИЕ № ДППМ - 1 от 25.07.2018 г – http://www.dker.bg/uploads/reshenia/2018/res_dprm-1_18.pdf.

²⁴ https://bulgartransgaz.bg/en/news/bulgartransgaz_ead_announced_the_procedure_for_construction_of_a_stage_of_the_expansion_of_the_gas_t-437-c15.html.

²⁵ http://tenders.bulgartransgaz.bg/bg/competitions/izgrajdane_na_obekt_razshirenje_na_gazoprenosnata_infrastruktura_na_bulgartransgaz_ead_paralelno_n-424-c1-1.html.

²⁶ According to the Technical Specification included in the tender documents, “the point of crossing the Bulgarian-Serbian border is in the WGS84 system with the following coordinates: B= 43°50’25,9199”; L= 22°22’30,4357”.

²⁷ MEKH Resolution No 9050 /2018 - http://www.mekh.hu/download/2/63/60000/9050_%202018.pdf.

²⁸ Amended Exemption Request, p. 12.

²⁹ ENTSOG, Capacity Map 2018.

4.1.2. Interconnectors between Contracting Parties and Member States

38. The present case also raises the question of whether a pipeline crossing a border between a Contracting Party (Serbia) and one or more Member States of the European Union (Bulgaria and Hungary) qualifies as an interconnector.

39. The definition of an “interconnector” in Article 2(17) of Directive 2009/73/EC, as applicable in the European Union, and as applicable in the Energy Community differs. The former applies only to interconnectors between EU Member States whereas the latter applies only to interconnectors between Energy Community Contracting Parties. Interconnections between a Contracting Party and EU Member States fall outside the scope of either definition.³⁰ At the time of issuing this Opinion, the resulting legal gap is subject to negotiations for amendments to the Treaty establishing the Energy Community. That gap cannot be closed by recurring to national legislation.

40. The fact that the Serbian Energy Law in its Article 2(25) transposes Article 36 of Directive 2009/73/EC in a neutral manner which refers to “States” rather than “EU Member States” or “Contracting Parties” is immaterial for the present assessment. The exclusive benchmark for the Secretariat’s assessment is Energy Community law, i.e. Article 36 of Directive 2009/73/EC, as adopted and adapted by the Ministerial Council. For the same reason, the fact that from an EU law perspective, the Gastrans project might be considered “spanning” two borders of EU Member States by crossing a non-EU Member State, Serbia,³¹ is immaterial. Finally, whether or not the regulatory authorities of Bulgaria and Hungary have taken a decision to apply the CAM Network Code to interconnection points from and to Contracting Parties under Article 1(2) of the CAM Network Code is also of no relevance for the purpose of the present assessment.

41. It is on account of primary Energy Community law, and in particular Articles 7 (prohibition of discrimination) and 41 (free movement of energy) of the Treaty establishing the Energy Community (“the Treaty”), that the Secretariat ultimately supports the view that the Project is to be considered an interconnector within the meaning of Article 36 of Directive 2009/73/EC, as adopted and adapted by the Ministerial Council.

42. On 23 September 2014, the Ministerial Council adopted Interpretation No. 2014/01/MC-EnC under Article 94 of the Treaty (“the Interpretation”). Article 1 of the Interpretation determines that “*in any legal act of the Energy Community incorporating European Union legislation, any reference to [...] c. existing or new gas and electricity infrastructure (including interconnections and interconnectors) crossing borders, zones, entry-exit or control areas between Parties and integrating the Contracting Party/Contracting Parties with the EU internal energy market, shall be treated in the same way and be subject to the same provisions as the respective [...] infrastructure between Contracting Parties under Energy Community law.*”

43. The recitals of Interpretation No 2014/01/MC-EnC recall that the Treaty requires equal treatment for any energy infrastructure located within the Energy Community, by “stressing that the different treatment of interconnections, cross-border flows, transactions or network capacities, depending on whether the border to be crossed is situated between two Member States of the European Union, two Contracting Parties or an EU Member State and a Contracting Party, frustrates the very idea of a single regulatory space for Network Energy and leads to barriers of trade.”

44. According to Item VIII.4. of the Rules of Procedure of the Ministerial Council, to which the recitals of Interpretation No 2014/01 /MC-EnC refer, an Interpretation is binding on the Parties and the institutions under the Treaty.³² The Interpretation thus requires the authorities of Serbia – a Party to the Energy

³⁰ Cf Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 25.

³¹ The provision reads: “This Regulation shall apply to interconnection points. It may also apply to entry points from and exit points to third countries, subject to the decision of the relevant national regulatory authority.”

³² Unless and until the EU judiciary rules otherwise, cf. Article 94 of the Treaty.

Community - as well as the Secretariat - an institution of the Energy Community - to treat a gas pipeline crossing a border between Serbia and Bulgaria or Hungary - such as Gastrans - in the same manner as it would treat a gas pipeline connecting Serbia with another Contracting Party, e.g. with Bosnia and Herzegovina. As the latter constellation would be considered an interconnector within the meaning of Article 36 of Directive 2009/73/EC, treating the former not as an interconnector would amount to discrimination and hence run counter to the Treaty establishing the Energy Community, as interpreted by the Ministerial Council.

45. While the principle of non-discrimination and its Interpretation by the Ministerial Council are crucial for the establishment of an interconnector within the meaning of Article 2(17) of Directive 2009/73/EC, the same principle requires the operators of infrastructure crossing the borders between Contracting Parties and EU Member States to ensure equal treatment on their respective segments. While the Secretariat does not call into question the legitimacy of requesting an exemption in one jurisdiction only, it also concurs with the regulatory authorities of Bulgaria and Hungary that an exemption granted for a part of a continuous pipeline supposed to connect Contracting Parties and Member States risks creating different conditions for access and capacity allocation on different segments of the pipeline. The Ministerial Council's Interpretation aims to avoid such a situation. Eligibility of the Project for an exemption and applying the same conditions for the non-exempted part of the Project as hypothetically applicable between two EU Member States or two Contracting Parties are in fact two sides of the same medal. Important basic elements for such harmonization are the Network Codes, including the CAM Network Code which, since 29 November 2018, is applicable in the Energy Community following the European Union.³³ The other Network Codes are either already applicable in the Energy Community,³⁴ or are expected to become applicable very soon.

46. On this basis, AERS is requested to ensure that the Network Codes, to the extent applicable in the Energy Community, apply to the non-exempted part of the Project's capacity on all interconnection points.

Conclusion

47. The Project is a major infrastructure with a length of some 400 km and a total investment of over (.....) It will be capable of transporting 13.88 bcm/a gas towards Serbia. Its transport capacity, once built, will have made up around 72% of the overall gas import capacity of the country.

48. Based on the above, the Secretariat concludes that the Project may be regarded as an interconnector within the meaning of Article 36 of Directive 2009/73/EC. At the same time, the Interpretation on which this conclusion relies requires that the non-exempted part of the Project is fully subjected to the *acquis communautaire* applicable to the Project during the exemption period.

4.2. Investment must enhance competition in gas supply and enhance security of supply (Article 36(1)(a) Directive 2009/73/EC)

4.2.1. Effect on competition

49. Article 36 of Directive 2009/73/EC requires that (i) the investment enhances competition in gas supply and (ii) the exemption is not detrimental to competition. While these two requirements are not identical, these regulations they imply that the project must be pro-competitive and thus create benefits for consumers.

³³ Regulation (EU) 2017/459 was adopted and adapted by Decision 2018/06/PHLG-EnC on 28.11.2018. According to Article 3 of the Decision, the scope of the Regulation determined in Article 2(1) of Regulation (EU) 2017/459 is limited to interconnection points between Contracting Parties. While this follows the same logic as the adaptation of Article 2(17) of Directive 2009/73/EC, Article 2(1) of Regulation (EU) 2017/459 further provides for the possibility of the Regulation to be applied "to entry points from and exit points to third countries, subject to the decision of the relevant national regulatory authority."

³⁴ Namely Regulation 703/2015 establishing a network code on interoperability and data exchange; amendment to Annex I of Regulation 715/2009 as amended by Commission Decision 2012/490 and 2015/71; and Regulation 2017/460 establishing a network code on harmonized transmission tariff structures for gas.

50. In its review of the structure of the natural gas market in Serbia, AERS notes a high level of concentration and concludes that the “ultimate shareholders of GASTRANS d.o.o. and their affiliates hold a dominant position in all segments of the natural gas market in the Republic of Serbia”. AERS examines the impact of the Project on “the increase of market competitiveness” in Serbia and the South East Europe region by predominantly referring to the arguments in Gastrans’ Initial and Amended Exemption Requests, including a Market Study. On this basis, AERS concludes that the Project “has the potential to enhance competition in the supply of natural gas in the Republic of Serbia and the SEE region” and that it “can transport natural gas from new sources”.

51. In particular, AERS argues that enabling imports of natural gas into Serbia from two directions and increasing import capacities at the entry points, the Project will create the necessary conditions for competition for importing natural gas and have positive effects on the functioning of the natural gas market in Serbia. It argues that apart from Russian gas imported by Gazprom as the dominant supplier of natural gas to the countries of South East Europe, a “potentially cost-effective source of natural gas in the Republic of Serbia, as well as in the region of South-East Europe, is natural gas from Romania”, as well as from Azerbaijan. Furthermore, LNG from Greece and Turkey are listed as potential sources, and gas from Iraq, Iran and the Mediterranean Sea are identified as hypothetical alternative sources. Moreover, AERS maintains that the construction of an entry point into the Hungarian transmission system from Serbia will enable importing of natural gas from various sources which would have a positive effect on competition on the Hungarian natural gas market. It also assumes that gas could be transported from Hungary to the connected countries in Central Europe because the capacity of the new interconnector at the border between Serbia and Hungary would be greater than the demand for imports in Hungary. Finally, AERS argues that the Project, as part of a new transmission route for gas from Turkey through Bulgaria and Serbia to Hungary, will enable imports of natural gas from various sources. AERS concludes that the Project has the potential to enhance competition in the supply of natural gas in Serbia and the South-East Europe (“SEE”) region under the conditions referred to above.

52. At the outset, the Secretariat recalls that when assessing whether the Project is pro-competitive, the question whether the investment leads to the creation or strengthening of a dominant market position needs to be considered.³⁸ A dominant position is “a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers”.³⁹ The existence of a dominant position can only be assessed in connection with a definition of the relevant markets⁴⁰

53. The relevant market is established by the combination of the product and geographic markets. A relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products’ characteristics, their prices and their intended use.⁴¹ The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas.⁴²

35 To analyse this requirement, it is necessary to analyse and measure potential positive and negative effects of the project on competition.

36 Only if the positive effects of the investment outweigh the negative effects, the exemption may be granted under Article 36 of Directive 2009/73/EC.³⁷

35 Cf Commission Staff Working Paper on Article 22 of Directive 2003/55/EC concerning common rules for the internal market in natural gas and Article 7 of Regulation (EC) No 1228/2003 on conditions for access to the network of cross-border exchanges in electricity – “New Infrastructure Exemptions” (“Commission Staff Working Paper”), paragraph 30; Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018.

36 Commission Staff Working Paper, paragraph 31.

37 Cf Commission Decision C(2011)3424 of 20.05.2011 on the exemption of the Gazelle interconnector, paragraph 27.

38 Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018. paragraph 64.

39 ECJ 27/76, United Brands, ECLI:EU:C:1978:22, paragraph 65; 85/76, Hoffmann-La Roche, ECLI:EU:C:1979:36, paragraph 38.

40 Commission Staff Working Paper, paragraph 36.

41 Commission Notice on the definition of relevant market for the purposes of Community competition law, [1997]C372/5, para. 7.

42 Commission Notice on the definition of relevant market for the purposes of Community competition law, [1997] C 372/5, para. 8

a. *Effect on competition in Serbia*

54. Natural gas is the third most used primary energy source in Serbia, after coal and oil. Gross domestic consumption in 2017 amounted to 2.66 bcm/a, which was 11.94% higher compared to 2016. The domestic production covered 18.4% of gas demand in 2017, while the rest was secured by imports from the Russian Federation under a long-term contract. There were no imports from other sources or other contracts.

55. The gas transmission system in Serbia currently has one entry point at the Hungarian border (Kiskundorozsma-Horgoš) with the annual technical capacity of (approx. 4.55 bcm/a) and one exit point on the border with Bosnia and Herzegovina (Zvornik). Both points are connected to the Srbijagas transmission system. In 2016, the utilisation rate of the entry firm capacity amounted to an average of 42.6%, varying according to seasons. The natural gas transmission services are performed by two transmission system operators: Srbijagas which operates 95% of the gas transmission network and Yugorosgaz-Transport which operates the remaining 5% of the network in south-east Serbia. Neither operator complies with the unbundling requirements under the Third Energy Package.

i. *Development, production and upstream gas supply*

56. The European Commission has defined a single product market for development, production and upstream supply of natural gas to large importers/wholesalers⁴³ With respect to the geographic market, the market can be defined as national from a supply side perspective, due to limited interconnection infrastructure or lack of available cross-border capacities.⁴⁴

57. The current Serbian development, production and upstream gas supply market is highly concentrated, with two players active on this market: Gazprom Export and Naftna Industrija Srbije a.d. Novi Sad ("NIS").

58. Gazprom Export exports gas via an intermediary, vertically integrated company Yugorosgaz, under long-term contracts to Srbijagas, the dominant player downstream. The ultimate owners of Yugorasgaz are Gazprom PJSC (75%) and Srbijagas (25%). The long-term gas supply contract between Yugorosgaz and Gazprom Export runs until 2021. It envisages deliveries of 1.5 bcm/a until 2018, i.e. 2 bcm/a starting from 2018.⁴⁵ The data taken from the 2017 Report of AERS show that the volumes actually supplied under the long-term contract may be even higher.

59. NIS is the only producer of natural gas in Serbia. The total annual production which was delivered to the transmission and distribution system in 2016 amounted to 399 mcm. A total of 44% of this quantity was sold to other suppliers and 56% was spent by NIS to cover its own demand.⁴⁶ NIS is majority owned by Gazprom Neft⁴⁷ (56.15%), while 29.87% are held by the Republic of Serbia, i.e. the sole shareholder of Srbijagas.⁴⁸ For the purpose of assessing the structure of the market and competition within this market, the fact that NIS is effectively under the control of Gazprom as its majority shareholder needs to be taken into account.⁴⁹

60. Based on the figures included in the 2017 Report of AERS,⁵⁰ the Secretariat agrees with AERS' finding that Gazprom has a dominant position on the Serbian development, production and upstream gas supply market: The market share of Gazprom Export amounts to approx. 80%, whereas the remaining approx. 20% are held by NIS which due to its shareholder structure is again controlled by Gazprom. It follows that companies under the control of Gazprom effectively enjoy a monopoly on the Serbian market for development, production and upstream gas supply.

43 COMP/M.6910 Gazprom/Wintershall Target Companies, of 03.12.2013, paragraph 83; COMP/M.6801 Rosneft/TNK-BP, of 08.03.2013, COMP/M.5585 Centrica/Venture Production of 21.08.2009; COMP/M.4545 Statoil/Hydro of 03.05.2007.

44 COMP/M.6801 Rosneft/TNK-BP of 13.04.2013, paragraph 12; COMP.39.315 ENI of 29.09.2010, paragraph 28; COMP/M.4545 Statoil/Hydro of 12.06.2007, para. 13-16; COMP/M.3696 E.ON/ Mol of 16.09.2006, paragraph 131; COMP/M.3440 ENI/EDP/GDP of 19.11.2005, para. 25-28.

45 <http://www.gazprom.com/press/news/2017/december/article388143/>; <http://www.gazprom.com/press/news/2018/october/article461916/>

	2015 million m ³	% of total	2016 million m ³	% of total	2017 million m ³	% of total
Total volume	2,172		2,206		2,560	
Local production	432	19.89%	399	18.09%	377	14.73%
Import from Russian Federation via long-term contract	1,733	79.79%	1,807	81.91%	2,183	85.27%
Import from other sources	7		-		-	
Total volume supplied by undertakings ultimately controlled by Gazprom	2,165	99.68%	2,206	100%	2,560	100%

61. While generally speaking, investment in infrastructure may provide an opportunity for market entrance of new market players or for a change in market shares of already active market players, this is almost certainly not to be the case on the Serbian market in view of its shareholding structure controlled by Gazprom (51%) and Srbijagas (49%).

62. Firstly, since Gazprom enjoys a monopoly on the Serbian market for development, production and natural gas supply, the Project creates the risk of foreclosure of access to the upstream market. Gazprom will be able to block delivery of gas to any downstream competitor and with Gazprom controlling 51% of Gastrans it will also have an incentive to deny competitors access to the pipeline. For this reason, the Secretariat does not share AERS expectation that the Project may be used to ship gas from other sources than the Russian Federation. Apart from the theoretical availability of such alternative gas sources, these sources should also effectively be available to competitors of the monopoly for them to enter and compete on the Serbian market. Given the structure of the market monopolized by the exclusive exporter of Russian gas, there is no commercial interest in the Project being made available for other sources of supply. The Secretariat further elaborates on that in the context of security of supply (below at point 4.2.2)

63. Secondly, since the second shareholder, Srbijagas, is dominant on the markets for downstream wholesale supply, retail supply, transmission and distribution, the Project also creates the risk of foreclosure of the downstream markets, as will be shown below under iii). As Gastrans is owned by undertakings with exorbitant market power on all levels of the Serbian gas market, the assumption that Project developed by these undertakings will enhance competition on the Serbian gas markets cannot be substantiated.

64. The Secretariat further notes that the majority of the annual gas supplies to Serbia are fixed on the long-term to Gazprom. Based on the agreement concluded between the governments of Serbia and Russia, Gazprom and Yugorosgaz signed a long-term contract for natural gas supply to Serbia until the end of 2021 for an annual supply of (... bcm/a) until 2018, i.e. (... bcm/a) from 2018-2021. The foreclosure of the upstream and downstream markets through the Project makes the prolongation of the long-term supply contract with Gazprom the most likely option. The prolongation of the long-term supply contract will in turn further reinforce the foreclosure of the market by stabilizing the supply market structure for another significant number of years. The effect of the Project and the long-term contract mutually reinforce each other, effectively perpetuating the market position of Gazprom, and of Srbijagas.

46 AERS Annual Report 2016, p. 57.

47 The largest shareholder of Gazprom Neft PJSC is Gazprom PJSC (95.68%); the remaining shares are in free float.

48 <https://www.nis.eu/en/about-us/company-information>.

49 Control means the possibility to exercise decisive influence on an undertaking, meaning the power to determine the strategic commercial decisions of the other undertaking. This power is typically achieved by owning a majority of the shares. See European Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings (2008/C 95/01), paragraphs 18-34.

50 Available at <https://www.aers.rs/Files/Izvestaji/Godisnji/Izvestaj%20Agencije%202017.pdf>.

65. Hence, the Project is not expected to make new capacity effectively available to new market entrants and/or competitors but will strengthen the market position of its owners and further foreclose the markets.

66. The effect of the Project on competition is further and significantly exacerbated by the impact of the exemption. The Third Energy Package envisages third-party access as a crucial element for ensuring equal access to energy infrastructure and as the main instrument for opening the market to competition. However, the Decision exempts the Project from Article 32 of Directive 2009/73/EC, i.e. third-party access. According to the Decision, Gastrans has the right to allocate and contract up to 88% of the maximum technical annual capacity to Gazprom and Srbijagas, thereby exempting it from third-party access for a duration of 20 years.

67. Moreover, according to the Decision, the remaining 12% may be allocated and contracted to companies other than Gazprom and Srbijagas only if they submitted non-binding bids in the market test. Due to this caveat of participation in the non-binding market test, also for these 12%, there is no third-party access, but access is reserved to the companies having indicated interest earlier on. The Secretariat has analysed the submitted bids for the non-binding phase of the market test:(.

Years	Estimation of total consumption in Serbia ⁵¹	Exit capacity via Gastrans	Interest expressed in non-binding market test (in bcm)				
			Exit capacity via Gastrans	by Srbijagas	by NIS	by undertakings ultimately controlled by Gazprom or	by others
2017	
2020							
2021							
2022							
2023							

51 Feasibility Study of the Project.

2024							
2025							
2026							
2027							
2028							
2029							
2030							
2031							
2032							
2033							
2034							
2035							
2036							
2037							
2038							

2039							
2040							

).

68. Two out of four shippers that submitted bids for gas transportation to the Serbian market are shareholders of Gastrans (i.e. Srbijagas and Gazprom), while one shipper is owned by a company holding a dominant position on the Serbian market (i.e. NIS). Together, these three shippers showed interest which represents about 170% of the designed exit capacity of the Project to Serbia.⁵² By contrast, the only shipper which does not have direct links to any of the companies holding a dominant position on the Serbian market submitted bids for only 3% of the design exit capacity of the Project to Serbia, which corresponds to 4% of the forecasted Serbian demand until 2024.

69. The European Commission established a general rule under which “an exemption is not granted to a new piece of infrastructure that is likely to have a significant amount of its capacity allocated to any dominant player in one of the markets affected”.⁵³ Where access to the infrastructure is restricted, this will restrict competition, in particular, if the new capacity is not available to new market entrants and/or competitors of the dominant undertaking. If, on the contrary, the new capacity is only available to the already dominant market player, the Project will strengthen its market position and further foreclose the market. Therefore, the European Commission only accepted allocation to any dominant market player at a maximum of 50%⁵⁴ or even 40%.⁵⁵

70. The data of the non-binding phase of the market test shows that not only 88% but even more capacity could be allocated to market players ultimately controlled by the dominant companies on the Serbian market. A significant part of the capacity will thus be allocated to dominant or monopolistic undertakings for a significant period of time, while the remaining capacity is also not open for any third party but only to the limited pool of market participants which have indicated interest in the non-binding market test. Therefore, the effect of such exemption is to eliminate any competitive constraints which could have hypothetically been created by a Project open to third-party access.

71. The Project, subject to the exemption granted by the Decision, does not open the market for new competitors but effectively forecloses the market to the advantage of the already dominant market player. The Project significantly impedes effective competition by helping the monopoly Gazprom to eliminate the possibility of rival firms to compete or enter the market. On account of its exclusive right to book up to 88% of the capacity on Gastrans. Potential market entrants are not, neither individually or in the aggregate, in a position to exercise any competitive pressure on Gazprom and constrain its behavior on the market.

72. Therefore, the Project as exempted from third party access does not only have likely anti-competitive effects, but effectively cancels out any potential pro-competitive effects that new infrastructure may have in principle. The Secretariat came to the conclusion that the Project and the exemption conditions granted by AERS in the Decision do not enhance competition in the Serbian market for development, production and supply, but on the contrary, strengthen the market position of the dominant undertaking Gazprom.

⁵² This booking level represents more than 200% of the forecasted Serbian consumption until 2024 and more than 180% of the forecasted Serbian consumption until 2029. If the Serbian gas consumption increased to the levels currently expected in the Feasibility Study of the applicant, the bookings of the above-mentioned companies would still represent more than 150% of that increased consumption from 2030.

⁵³ Cf Commission Decision C (2009) 3037 of 24.04.2009 on the exemption of the Nabucco interconnector (BG), paragraph 31; Commission Decision D(2008) 142 of 08.02.2008 on the exemption of the Nabucco interconnector (AT), paragraph 55.

ii. Storage

73. The market for the storage of natural gas constitutes a separate product market. 56 The geographic scope of the market for the storage of natural gas is either national or regional.⁵⁷

74. In Serbia, there is only one storage, Natural Gas Underground Storage Banatski Dvor, LLC (“Banatski Dvor”), founded and owned by Srbijagas (49%) and Gazprom Germania⁵⁸ (51%). The currently available capacity amounts to 450 mcm while the designed withdrawal capacity amounts to 5 mcm/d. The bidirectional gas pipeline Gaspodinci – Banatski Dvor connects the underground gas storage with the transmission system of Srbijagas.

75. According to the Decision, 88% of the capacity of the Project will be reserved for Gazprom and Srbijagas, i.e. the shareholders of Banatski Dvor. As a consequence, the Decision allocates a significant part of the capacity not only to the company dominant on the Serbian market for development, production and upstream supply of gas, but also to the same companies enjoying a monopoly on the Serbian gas storage market. The exemption granted by the Decision therefore leads to the companies which will reinforce their quasi-exclusive access to the Serbian downstream market to be in the position and to have an incentive to utilize the storage facility for their own interests on the highest possible level, thereby foreclosing competitors from the storage market.

76. The European Commission has identified a distinct product market for the downstream wholesale supply of gas which encompasses sales by shippers or suppliers with an upstream gas supply contract (as well as those with domestic production),⁵⁹ to retailers and other wholesalers.⁶⁰ In terms of geography, the European Commission has generally considered downstream wholesale gas supply markets to be delineated along existing (regional) grid areas, by market area or at a national level.⁶¹

77. As rightly pointed out by AERS, Srbijagas is dominant on the Serbian market for downstream wholesale supply of gas. In particular, on this market, only two market players – NIS and Srbijagas – are active. In 2016, Srbijagas was also appointed as the public supplier and supplier of the last resort of final customers, putting it in a legal monopoly with regard to these customers. The market shares of Srbijagas in the last three years clearly indicate its dominant market position:⁶²

(...)

Srbijagas in million m3	% of total	NIS in million m3	% of total	Srbijagas in million m3
2015
2016				
2017				

....).

54 Cf Commission Decision C (2009) 3037 of 24.04.2009 on the exemption of the Nabucco interconnector (BG).

55 Cf Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018.

56 COMP/M.5549 EDF/Segebel of 12.11.2009, paragraph 167-168; COMP/M.3696 E.ON/MOL of 21.12.2005, paragraph 99; COMP/M.3410 Total/Gas de France of 08.10.2004.

57 COMP/M.3696 E.ON/MOL of 21.12.2005, paragraph 130.

58 Gazprom Germania is fully owned by Gazprom Export, a 100%-subsidiary of Gazprom.

iii. Downstream wholesale gas supply and retail supply

78. Besides the downstream wholesale supply of gas market, the European Commission further distinguishes between: i) retail supply of gas to gas-powered electricity producers, ii) retail supply of gas to large industrial customers, iii) retail supply to small industrial and commercial customers and iv) retail supply to households.⁶³ It considers that the geographic scope of retail markets is general national in scope.⁶⁴

79. Also in this regard, the Secretariat confirms AERS' finding that Srbijagas is dominant on the Serbian retail supply market, accounting for some 79% of total natural gas sales in 2016.⁶⁵ The remainder consists of other suppliers, such as public supplier DP Novi Sad (3%) and NIS (2.5%), whereas all others have even lower market shares.

80. As has been explained above, the Project will not enable market entrance of new competitors and/or a change in market shares of already active market players, because Gazprom and Srbijagas as the shareholders of Gastrans have strong market positions on all levels of the Serbian gas markets and an incentive to foreclose the market to their own advantage. The Project also creates the risk of further foreclosure of the downstream markets. Being in a dominant position on the wholesale supply market, Srbijagas will be in the position to foreclose any potential competitor downstream.

81. Furthermore, since the Decision effectively reserves 88% or more of the capacity of the Project for Gazprom and Srbijagas, a significant amount of its capacity is allocated to undertakings dominant on different segments of the Serbian gas market. In particular with regard to Srbijagas, this will put Srbijagas as shareholder of the Project in the position to foreclose the downstream and retail supply markets for other (potential) market participants. The Decision would perpetuate the current lack of competition by effectively prescribing quasi-exclusive access to the Project for an already dominant undertaking.

82. With a 49%-share in Gastrans, Srbijagas also has an incentive to foreclose access to the infrastructure serving the downstream wholesale and retail markets. Srbijagas is not only dominant on the downstream wholesale and retail markets, but also directly controls 95% of the gas transmission system in Serbia, and Yugorosgaz-Transport (ultimately held by Gazprom) the remaining 5%. Srbijagas also controls (...%) of the gas distribution system in the country. The company continues to perform transmission (and distribution) of natural gas in breach of the unbundling provisions of the Third Energy Package, and does not separate control over transmission and supply activities. Its lack of unbundling in line with the Third Energy Package has already led to a Decision establishing a serious and persistent breach of Energy Community law by the Ministerial Council.⁶⁶

59 COMP/M.7228 Centrica/Bord Gais Energy of 13.06.2014.

60 COMP/M7936 Petrol/Geoplin of 10.03.2017, paragraph 17; COMP/M.6984 EPH/Stredoslovenska Energetika, of 20.11.2013.

61 COMP/M7936 Petrol/Geoplin of 10.03.2017, paragraph 18; COMP/M.6984 EPH/Stredoslovenska Energetika of 20.11.2013; COMP/M. 5802 RWE Energy/Mitgas of 17.06.2010; COMP/M.5467 RWE/Essent of 23.06.2009; COMP/M.5220 ENI/DISTRIGAZ of 15.10.2008.

62 With regard to market shares, the European Court of Justice has found that very large market shares are in themselves, and save in exceptional circumstances, evidence of the existence of a dominant market position, Case 85/76, Hoffmann-La Roche, ECLI:EU:C:1979:36, paragraph 39 et seqq. That is the situation where there is a market share of 50%, Case C-62/86, AKZO, ECLI:EU:C:1991:286, paragraph 60.

63 COMP/M.8701 Edison/GNVI of 05.02.2018; COMP/M.8358 Macquarie/National Grid/Gas Distribution Business of National Grid of 16.03.2017, paragraph 18; COMP/M7936 Petrol/Geoplin of 10.03.2017, paragraph 25; COMP/M.7602 Deutsche Telekom Group/Met Holding/JV of 19.08.2015, paragraph 10; COMP/M.5740 Gazprom/A2A/JV of 16.06.2010.

64 COMP/M.8358 Macquarie/National Grid/Gas Distribution Business of National Grid of 16.03.2017, paragraph 18; COMP/M7936 Petrol/Geoplin of 10.03.2017, paragraph 26; COMP/M.6068 ENI/ACEGASAPS/JV of 11.04.2011; COMP/M.5740 Gazprom/A2A/JV of 16.06.2010; COMP/M.3230 Statoil/BP/Sonatrach/In Salah JV of 19.12.2003.

65 AERS Annual Report 2016, p. 77.

83. Moreover, Srbijagas effectively prevents competitors to enter the Serbian market via the interconnection point Kiskundorozsma-Horgoš but uses the interconnection capacity exclusively for its own (and Gazprom's) deliveries. The Secretariat has initiated an infringement procedure. An increase of capacity to Serbia on account of granting third-party access at the Kiskundorozsma- Horgoš interconnection point would not constitute a pro-competitive effect attributable to the Project, but would simply restore compliance with Energy Community law.

84. The Secretariat thus concludes that, by reserving 88% or more of the capacity for Gazprom and Srbijagas, the Project and the exemption granted to it effectively ensures foreclosure not only of the upstream market on which Gazprom holds a dominant position, but also of the downstream wholesale and retail markets on which Srbijagas is dominant and can leverage its dominance across markets. Therefore, the Secretariat comes to the conclusion that the Project and the exemption conditions granted by AERS do not increase competition in the Serbian markets, but on the contrary, significantly strengthen the dominance of the existing market players.

b. Effect on competition in Hungary

85. In 2017, the Hungarian natural gas demand amounted to approx. 9.5 bcm/a.⁶⁷ Domestic production met less than 20% of the total consumption and most (95%) of the remainder was effectively imported from the Russian Federation. The majority of imports – including the volumes transited to Serbia – amounted to 13.4 bcm in 2018 and entered Hungary from Ukraine through the interconnection point Beregovo.⁶⁸ Another important entry point is from Austria at Mosonmagyaróvár through which 6.8 bcm were imported in 2018. In addition, gas can be transported to Hungary from Slovakia, and it is expected to become possible to import gas from Romania and Croatia in the course of 2019.

86. The Hungarian market for development, production and upstream gas supply already shows a high level of concentration. Between 1995 and 2015, a long-term gas supply contract with Gazprom was the cornerstone of gas supplies to Hungary providing at maximum 9.5 bcm/a of supplies⁶⁹. Currently, the long-term contract continues to be extended on a short-term basis, most recently until the year 2020. ⁷⁰ According to this agreement, Panrusgaz,⁷¹ as the Hungarian partner, imported 4.9 bcm in 2016, i.e. 5.1 bcm⁷² in 2017 to Hungary, the latter representing half of the total annual gas demand.

87. On the market for downstream wholesale supply, approx. 90 companies have a license to trade gas in Hungary. The state-owned Hungarian Gas Trade Ltd, who has an obligation to supply gas at regulated prices to universal service providers upon request, has a market share of over 60%. Due to the number of competitors on the market, there is a certain degree of competition; however since around 20 traders source their gas from Gazprom (as is Panrusgaz), the market cannot be considered to be fully competitive.

88. The Project foresees an exit capacity of 10 bcm/a reaching Hungary.⁷³ According to the demand assessment by ENTSOG in its latest TYNDP,⁷⁴ the forecasted Hungarian demand by 2030 is expected between 7.6 - 9 bcm/a; no market expansion is anticipated. This indicates that the planned exit capacity from the Project is capable to comfortably cover the entire Hungarian gas demand

66 Cf Case ECS-9/13S, Reasoned Request, paragraph 48. In particular, the obligation to implement the requirement of legal unbundling of Srbijagas from other activities not related to transmission is not fulfilled. Furthermore, the obligation to ensure the independence of Yugorosgaz-Transport in terms of organization and decision-making from other activities not relating to transmission is not fulfilled. Moreover, the obligation to ensure the independence of the two TSOs in terms of its organization and decision-making from other activities not relating to transmission is not fulfilled.

67 BP Statistical Review of World Energy 2018 - <https://www.bp.com/content/dam/bp/en/corporate/pdf/energy-economics/statistical-review/bp-stats-review-2018-full-report.pdf>

68 These figures include also those quantities, which are sold from Hungary to Ukraine.

69 Report on the activities of the Hungarian Energy and Public Utility Regulatory Authority in 2013, p. 59.

89. The Project, subject to the exemption granted by the Decision, in particular the allocation of 88% or even more of the capacity to undertakings which are ultimately controlled by Gazprom could lead to a scenario where both of the major entry points into Hungary (Beregovo⁷⁵ and Kiskundorozsma- Horgoš) are controlled by Gazprom which is already in a dominant position on the Hungarian market for the development, production and upstream wholesale gas supply (with a market share between 50% and 80%). The additional capacity foreseen by the Project to reach Hungary and the very limited allocation of capacity to third parties effectively would strengthen Gazprom's position on the upstream market by increasing its market share and thereby enabling it to foreclose the downstream markets to any potential competitor. Whereas the competition on the downstream wholesale supply market is already limited due to the exclusively Russian supply of gas, the Decision would promulgate this market concentration and further limit competition.

c. *Effect on competition in Bosnia and Herzegovina*

90. Natural gas can currently enter Bosnia and Herzegovina only via one cross-border entry point from the domestic gas transmission system of Serbia. The capacity of this point is used by BH-Gas d.o.o. Sarajevo and Gazprom Export.

91. Since the Project does not provide for a connection to Bosnia and Herzegovina, nor for any capacity destined for this market, the Project does not directly impact competition on the Bosnian gas markets. The Project might have certain pro-competitive effects only if due to the Serbian capacity of the Project, new supply could reach the Bosnian market. However, such pro-competitive effects will not materialize in case significant parts of the capacity are, as envisaged by the Decision, allocated to the undertakings dominant on the Serbian and Bosnian gas markets.

d. *Effect on competition in Bulgaria*

92. The Bulgarian gas transmission network contains two co-existing systems i.e. the national gas transmission network and the gas transmission network for transit transmission. The latter is used for the transmission of Russian natural gas to Turkey, Greece and the former Yugoslav Republic of Macedonia and has a technical capacity of 17.8 bcm/a. The transit system is technically and commercially interconnected with the national gas transmission network, although only to a very limited extent. The capacity of entry into the national system is 0.3 bcm/a, whereas entry into the transit system is 0.6 bcm/a. The Project is planned to connect to a newly-built pipeline section on the territory of Bulgaria, which is expected to have only one connection to the domestic Bulgarian network.

93. The vast majority of Bulgaria's approx. 3.5 bcm/a gas demand is met via imports, which are procured dominantly by the state-owned Bulgargaz. A long-term supply contract, between Bulgargaz and Gazprom Export covers the supply of (...bcm/a) between 2013 and 2022,⁷⁶ which indicates that Gazprom is a dominant player on the market for the Bulgarian market for the development, production and upstream supply of gas.

⁷⁰ <http://kremlin.ru/events/president/news/58586>

⁷¹ Owned by Gazprom Export, E.ON Ruhrgas International AG and Centrex Hungaria Zrt.

⁷² <http://www.panrusgaz.hu/en/ker.htm>

⁷³ Blueberries, Market Study for the Project.

⁷⁴ <https://www.entsog.eu/tyndp#entsog-ten-year-network-development-plan-2020>

⁷⁵ Currently Ukrtransgaz is unable to carry out all the TSO functions vis-à-vis FGSZ at the Beregovo interconnection point in the direction Ukraine-Hungary. The reason for this barrier derives from the contractual provisions between Naftogaz and Gazprom [<http://www.naftogaz.com/www/3/nakweben.nsf/0/AE96AA9D16162AA9C2257E5B004AB86D?OpenDocument&Highlight=0,FGSZ>].

94. The main players on the Bulgarian gas market are grouped into a 100% state owned conglomerate, the Bulgarian Energy Holding (“BEH”). Both Bulgargaz and the transmission system operator Bulgartransgaz are part of BEH. As a result of an investigation opened in July 2013, the European Commission found that the “BEH group holds dominant positions both in the gas infrastructure markets and in the gas supply markets in Bulgaria”.⁷⁷ In 2017, 99.5% of the total downstream wholesale market was covered by Bulgargaz at regulated prices, while 0.5% was supplied by other traders at negotiated prices. This indeed indicates an extreme level of market concentration on the downstream wholesale market with Bulgargaz enjoying a quasi-monopoly.

95. As Bulgaria is in the upstream direction of the Project, the Secretariat does not consider that the Project and the exemption from third-party access for the flows in the default south-north flow direction have a direct impact on the Bulgarian gas markets. Only in case of reverse flow, gas may be traded freely from Central-Eastern Europe to Bulgaria. This would constitute an alternative gas supply, putting competitive pressure on the currently dominant upstream gas supplier Gazprom. Furthermore, such trade could also serve an opportunity for arbitrage between the CEE and SEE markets and thus facilitate market integration, enabling a potential Bulgarian gas hub to be integrated, liquid and mature.

Conclusion

96. The Secretariat concludes that due to the dominant position of the shareholders of the Project on different levels of the Serbian gas market, the Project is not expected to make new capacity effectively available to new market entrants and/or competitors but will strengthen the market position of its owners and further foreclose the markets. Furthermore, the exemption from third-party access and therefore exclusive allocation of 88% or more of the capacity will further restrict competition, in particular because the new capacity is not available to new market entrants and/or competitors of the dominant undertakings but only to the already dominant market players themselves. Therefore, the Secretariat comes to the conclusion that the Project and the exemption conditions granted by AERS in the Decision do not enhance competition neither on the Serbian, nor the Hungarian and Bulgarian markets, but on the contrary, strengthen the market position of the dominant undertaking Gazprom and Srbijagas.

97. The Secretariat therefore concludes that the Project does not enhance competition, but that the exemption granted by the Decision is detrimental to competition. Under these conditions, an exemption cannot be granted and would violate Article 36 of Directive 2009/73/EC.

98. Apart from the necessity to establish compliance with Energy Community law regarding the unbundling of Srbijagas and the capacity allocation at the interconnection point Kiskundorozsma- Horgoš, the Secretariat deems it indispensable to amend the conditions regarding exemption from third-party access by significantly lowering the percentage of capacity which is allocated exclusively to Gazprom and Srbijagas, to a level that allows competitors to enter and compete on the respective markets. The remaining capacity must be allocated in a competitive manner, in accordance with the *acquis communautaire*. Furthermore, in order to open the market for potential competitors of the dominant firms, the Secretariat insists on additional liquidity measures whereby the dominant companies must offer gas on the Serbian market in order to stimulate the emergence of at least some degree of competition on highly concentrated markets.

4.2.2. Impact on security of supply

99. Article 36 of Directive 2009/73/EC requires that gas infrastructure must enhance security of supply as a precondition to be granted with an exemption. For this it needs to be assessed whether and to what extent the Project enhances the security of supply in Serbia and the neighbouring markets in South East Europe.

100. In the Decision, AERS concludes that the Project “increases the security of supply of natural gas in the Republic of Serbia and the SEE region”.⁷⁸

101. At the outset, the Secretariat notes that in general, an investment which provides a new route to the Serbian and other markets in South East Europe,⁷⁹ and connects new sources of upstream gas from new suppliers, will normally increase the security of supply of those markets. Yet, the impact of security of supply has to be assessed on a case-by-case basis.⁸⁰

a. New supply route to Serbia, Bosnia and Herzegovina, Hungary and Bulgaria

102. In general, the Secretariat agrees that the Project constitutes a new supply route to Serbia, Hungary and indirectly to Bosnia and Herzegovina and enhances the security of supply of those markets.

103. Currently, all natural gas imports to Serbia (and Bosnia-Herzegovina) enter Serbia through the Kiskundorozsma-Horgoš interconnection point on the Hungarian-Serbian border. The maximum import daily capacity for both Serbia and Bosnia and Herzegovina at the Kiskundorozsma entry point is 540,000 m³/h or 13 mcm/d, out of which 11 mcm/d is booked for Serbia.⁸¹ Serbia's peak consumption of 17.274 mcm/d is covered from imports through that interconnection point, the underground gas storage site at Banatski Dvor (maximum withdrawal rate 5 mcm/d),⁸² and the maximum domestic production of 1.2 mcm/d. The historical supply peak through Kiskundorozsma is at 11.3 mcm/d in the winter months for both Serbia and Bosnia and Herzegovina combined.⁸³

104. Hence the current Serbian peak demand can be satisfied with the use of all available sources, but may reach a capacity limit should the demand further increase. The Project is expected to add a total entry capacity of (34.4 bcm/d) (13.88 bcm/a) at the border between Bulgaria and Serbia, of which a capacity of more than 10 mcm/d⁸⁴ (3.8bcm/a) can exit to the Serbian system. The Project will likely increase the resilience of the Serbian system, in particular in situations where the entry capacity to Serbia from the Kiskundorozsma-Horgoš interconnection point reaches its limits.⁸⁵

105. AERS also concludes that the Project will increase the N-1 standard for Serbia, which foresees that in the event of a disruption of the single largest gas infrastructure element the capacity of the remaining infrastructure is still able to satisfy peak gas demand⁸⁶. The N-1 standard is deemed fulfilled if it is higher than 100%. The Project would increase Serbia's N-1 standard from existing 38% to 114%.⁸⁷

76 <http://www.gazpromexport.ru/en/partners/bulgaria/>.

77 http://europa.eu/rapid/press-release_IP-18-6846_en.htm.

78 The Decision has reached its conclusion on enhancement of security of supply based on assessment of the four criteria as defined by the Commission Staff Working Paper.

79 For the purpose of the security of supply assessment, the term "SEE market" includes Serbia, Bulgaria, Hungary and Bosnia and Herzegovina.

80 Cf Commission Decision C(2015) 1852 of 17.03.2015 on the exemption of the Trans Adriatic Pipeline, paragraph 59; Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018. paragraph 38; Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 43.

81 AERS, Annual Report 2017.

82 The Serbian storage facility Banatski Dvor has a capacity of 460 mcm working level with maximum injection and withdrawal rates which stand at 2.7 and 5 mcm/day.

83 AERS, Annual Report 2017.

84 Calculated by the Secretariat based on the annual capacity.

85 Cf Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 89.

86 As defined by Article 5 of Regulation (EU) 2017/1938.

87 AERS Decision p 36-37.

106. At the same time, the Secretariat recalls that Srbijagas has committed to, and the Government has supported, building other interconnectors with adjacent transmission system operators which are expected to become operational in the course of the next years. The most mature of this is the Bulgarian-Serbian interconnector (IBS). Once built, that interconnector would increase Serbia's N-1 standard to approx. 65%. Moreover, Srbijagas is in negotiations with Transgaz of Romania for an interconnector Arad-Mokrin. This interconnector would increase Serbia's N-1 standard to 50.5%. While the parallel development of these projects which Srbijagas has committed to construct in the coming years do not eliminate the impact of the Project on improving the infrastructure security standard in Serbia, they show that Serbia's security of supply in terms of route diversification is likely to improve anyhow.

107. As regards Bosnia and Herzegovina, the entry point at the existing Serbian transmission system in Zvornik has a capacity of 2 mcm/d.⁸⁸ The Project will not affect that capacity and thus does not affect the N-1 standard of Bosnia and Herzegovina.

108. As regards Hungary, the Decision argues that the Project will enhance the N-1 infrastructure standard from 124.5% to 151%. While the Secretariat generally agrees that this is the case, it is to be noted that the Project's impact on Hungary's N-1 standard is not of the same importance as in the case of Serbia, since the N-1 standard is already fulfilled by Hungary at present.

109. As regards Bulgaria, AERS claims that the Project will improve the N-1 infrastructure standard from 62.8% to 175.6%. The Secretariat disagrees with this conclusion. The Bulgarian N-1 standard will be increased by the Project only under the assumption that firm physical reverse flows from Serbia to Bulgaria are possible. Under the conditions imposed by AERS, however, the Project represents a plain exit point from Bulgaria because only transit towards Serbia and further to Hungary is envisaged. Physical reverse flow is mentioned only as noncommittal possibility without any requirements or concrete time period for implementation. (.....)⁸⁹ Without further specification it cannot be concluded that Bulgaria's N-1 standard will improve on account of the Project. In case physical reverse flow on the Project were ensured, it would indeed constitute another route of supply to Bulgaria and increase N-1 standard by adding a new entry point to the Bulgarian system.

110. The Secretariat concludes that the Project may be considered improving the N-1 standard in Serbia and Hungary, and thus contributes to route diversification, an element for security of supply within the meaning of Article 36 of Directive 2009/73/EC.

111. Besides, the Secretariat notes that natural gas is currently imported to the countries in Central and South East Europe on the basis of transit through Ukraine. The current transit contract between Gazprom and the gas incumbent of Ukraine expires by the end of 2019. Whether and to what extent it will be replaced by a new transit contract is currently subject to negotiations. The state of these negotiations entails a degree of uncertainty. In this situation, the Secretariat was made aware by the system operators and authorities of Serbia and Hungary of the increased importance of the Project for their security of supply. The Project's capacity of approximately 14 bcm/a will not allow for a full replacement of the Ukrainian route, which transported 93.5 bcm of Russian gas in 2017.⁹⁰ Yet it would enable the supply of natural gas to Serbia in case that the transit capacities through Ukraine are interrupted or diminished. Although Hungary is much better interconnected with its neighbours, the Project will enable another supply route at a capacity comparable to the current Hungarian market of around 10 bcm/a.

⁸⁸ <https://ots-test.srbijagas.com/frontend/ulizl.php>.

⁸⁹ Annex of the FEED contract for Gastrans.

b. New supply sources

112. The Decision states that the new interconnector will also permit the flow of existing and new sources of natural gas from south to north.

113. As regards the Project's impact on security of supply by opening new sources from new suppliers to Serbia, however, the Secretariat notes that apart from the theoretical availability of such sources, these must be realistically available to the Serbian market. (...)

114. By contrast, the likelihood of bringing gas from new supply sources to Serbia and the SEE region through the other planned interconnectors (Bulgaria-Serbia and Romania-Serbia) is much higher.

115. The existence of long-term contracts between Gazprom and Srbijagas (via Yugorosgaz) covering the entire demand for imports in Serbia also underpins that only Russian gas would be transported on the Project to Serbia, which hence is not likely to result in source diversification. Rather, the Project could either turn into a partial substitute of the existing route of Russian gas to Europe via Ukraine, or serve as incremental capacity for bringing additional quantities of Russian gas to Europe.

116. In order to improve the security of supply beyond the mere N-1 infrastructure standard⁹² the Secretariat requests to by default set aside short-term capacities to third parties in line with what was reasoned above from a perspective of effective competition. The current Decision provides that 12% of the Project's capacity is non-exempted, although even this portion of the pipeline is set aside for participants in the non-binding market test for long-term booking. This is, in the Secretariat's view, not enough to enable short-term flexibility for new sources which may come upstream later, through the interconnector Greece-Bulgaria for instance and its opening to Azeri and LNG supplies via Greece, or from new production sources in the Black Sea. The region has been historically supplied only with Russian gas, and the Project, which continues this trend, should offer at least a part of its capacities available to take advantage of this opportunity and realize its potential for security of supply even more. This would also enable flexibility to contract gas sources on a short term basis also in cases of emergency.

90 Cf Commission Decision C (2016) 6950 of 28.10.2016 on the exemption of the OPAL interconnector, paragraph 50.

91 Cf chapter 4.2.1.

92 The Staff Working Paper emphasis to a certain extent the flexibility of sources though linked somewhat to an emergency: "The more flexibility of supply an infrastructure project adds for bringing additional gas to a market in case of an emergency, the more it enhances security of supply".

c. Reverse flow and incremental capacity

117. The Secretariat recalls that the Decision does not exempt the Project from any current or future pieces of the *acquis communautaire* related to security of gas supply⁹³. The *acquis* at present consists of Directive 2004/67/EC in the Contracting Parties to the Energy Community, and of Regulation (EU) 2017/1938 of the European Parliament and of the Council⁹⁴ in the European Union. The incorporation into Energy Community law of Regulation (EU) 2017/1938 and its preceding Regulation (EU) 994/2010 has long been discussed in the Energy Community institutions, and is envisaged still for 2019. Once adopted, it will be applicable to the new interconnector and its operators. It follows from point 4.1.2 above and from the Interpretation referred to there, that for all aspects not subject to an exemption, AERS must ensure homogeneity and compliance with current and future pan-European standards.

118. According to Article 5(4) of Regulation (EU) 2017/1938, all cross-border interconnections must be physically bi-directional at all times. The Decision should ensure Gastrans enables permanent physical reverse flow capacities.

(.....) The Secretariat requests AERS to ensure that the Decision requires Gastrans to enable adequate capacity of physical reverse flow from Hungary to Serbia (and further to Bulgaria) for emergency operations, in the same manner as any infrastructure project subject to Regulation (EU) 2017/1938 in the European Union would.

119. Moreover, the Decision currently includes only a general request⁹⁵ to Gastrans to examine the interest of the market for capacity expansion (including reverse flows) every six years. This is three times less the typical frequency of market demand testing envisaged by Article 26 of the CAM Network Code. AERS does not give reasons for such unusual long intervals. The Secretariat requests AERS to amend its Decision by obliging Gastrans to identify the demand for incremental capacity through regular binding market tests which will be performed every second year, and consequently build incremental capacity, unless it shows that expansion is not economically viable. Expansion capacity (as well as any remaining unused initial capacity) must be made available to the market under the non-exempted regime.

Conclusion

120. The Secretariat concurs with AERS that the Project will enhance security of supply of natural gas in Serbia and to the SEE region, albeit only by opening a new transportation route and not by providing access to new sources of gas.

121. Based on the above, the Secretariat requests AERS to ensure full compliance of the entire Project (regardless of the exemption) with Article 5 of Regulation (EU) 2017/1938. The Secretariat also requests AERS to apply Article 26 of the CAM Network Code for non-exempted capacities.

4.3. The level of risk attached to the investment must be such that the investment would not take place unless an exemption was granted (Article 36(1)(b) Directive 2009/73/EC)

122. Article 36(1)(b) of Directive 2009/73/EC requires an analysis of whether the Project would not take place without granting the exemptions for ownership unbundling, third party access and application of regulated prices, in the scope and manner granted by the Decision.

123. At the outset, the Secretariat recalls that an exemption under Article 36 of Directive 2009/73/EC is a risk mitigation measure to be tailored to the specific risk profile of major new infrastructure projects. For this purpose, the risks incurred by the Project need to be identified. Any exemption granted must be proportionate compared to the risk it is expected to mitigate.

124. Based on the documents provided by the company and its own analysis, AERS concludes that the investment would not take place unless the exemption in the form provided by the Decision is granted. In the Decision, AERS accepts the following risks and their justification: (i) the size of the project; (ii) very limited possibilities for financing the project of that size by existing TSOs; (iii) the small number of shareholders; (iv) limited interest of third-party users of the system.

⁹³ Cf Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018, paragraph 39; Commission Decision C(2015) 1852 of 17.03.2015 on the exemption of the Trans Adriatic Pipeline, paragraph 60.

⁹⁴ Regulation (EU) 2017/1938 of the European Parliament and of the Council of 25 October 2017 concerning measures to safeguard the security of gas supply and repealing Regulation (EU) No 994/2010.

⁹⁵ Cf Item 8 of the Decision: "GASTRANS d.o.o shall at least every six years, or may at its discretion, if GASTRANS d.o.o deems it necessary, at any time verify the interest of the market for investments in the New interconnector and, provided that such investment is economically justified, make the investment plan and submit such investment plan to the Agency for the approval pursuant to Article 250 of the Law".

125. The Secretariat generally agrees that the investment in the Project, with an expected CAPEX of around (), is of a high magnitude. The Secretariat also notes that the equity- debt ratio for financing the Project is assumed to be %
-%.

126. The Secretariat further notes that the cost-benefit analysis carried out in the feasibility report, which was submitted together with the exemption request, is based on one single scenario, namely on the assumption that 88% of the total capacity is utilized on Exits Paraćin, Pančevo and Gospođinci from (.....) and on exit point Horgoš from (.....). This scenario models only the “exemption granted” scenario when the shareholders of Gastrans reserve capacity in the extent allowed by the Decision.⁹⁶

127. A state-of-the-art cost-benefit analysis for projects of such an investment size would have required a sensitivity analysis⁹⁷, along with a scenario analysis as a basis for a proper risk assessment. This would have allowed defining the most pertinent risks for the Project’s financing.⁹⁸ Identifying the most sensitive variables would have been the precondition to come up with appropriate risk mitigation strategies.⁹⁹ Such an assessment is usually required by financial institutions. This type of assessment is missing from the feasibility study and the cost-benefit analysis where a single assessment scenario is presented without any sensitivity analysis or alternative scenario analysis. Hence it is difficult to conclude whether the current level of exemption granted addresses the identified risks proportionately.

128. In the feasibility study, no analysis has been carried out to compare the financial feasibility of the project under the regulated and the exempted regime. The Secretariat however notes that the currently applicable regulated transmission tariff methodology in Serbia would result in high tariffs in the first years of operation, until higher utilization of the pipeline is reached, thus risking lower capacity bookings. The Secretariat recognizes the fact that the tariffication methodology as proposed by Gastrans, addresses this issue and avoids tariff fluctuations. Nevertheless, there are regulatory measures, such as smoothing of revenues/tariffs over the years, to mitigate the risk of lower bookings due to higher tariffs in the first few years within the regulated regime. Consequently, such regulatory measures could lower the risk.

129. The Secretariat considers the following risks brought forward by Gastrans as relevant for the present assessment:

- (i) The size of the project (in terms of the value of investment (.....mil.), length, capacity) compared to the size of the natural gas market of Serbia;
- (ii) Existing transmission system operator(s), or Gastrans as an unbundled entity, would not be able to attract equity and third party financing to construct infrastructure;
- (iii) Existing transmission system operators are not in the position to construct the project due to insufficient human and logistical resources;
- (iv) Small number of shareholders among which to spread the project risk;
- (v) Investment incentives (i.e. direct state funds, tax break) cannot be obtained from the Republic of Serbia¹⁰⁰ for the project, and it cannot (partially) be financed by grant support from international financial institutions, including the European Union.

96 Schedule 1 - GASTRANS d.o.o. Novi Sad Feasibility Study on Construction of the Energy Infrastructure, June 2018, pg. 23 Main assumptions 3 and pg. 6 Under point 3

97 Guide to Cost-Benefit Analysis of Investment Projects, 1.2 Definitions and scope of ‘major projects’ Assessment, Directorate-General for Regional and Urban policy, December 2014.

98 In the sense of the “critical variables of the project [which] have the largest impact on the project’s financial and/or economic performance”, cf. Guide to Cost-Benefit Analysis of Investment Projects, 2.9 Risk Assessment, Directorate-General for Regional and Urban policy, December 2014.

99 Commission Staff Working Paper, paragraph 45.

130. The Secretariat notes that Article 36(1)(b) of Directive 2009/73/EC addresses investment and financing risks, but not risks of a general nature such as delayed land rights and permits or regulatory and legal risks which cannot be mitigated by an exemption. Project management risks attributable to interface risk with contractors and connecting to downstream and upstream systems should be mitigated with insurance policies, appropriate project design and planning, but not via exemptions.

131. In general terms, the Secretariat does not support the argument that an investment needs to be protected from future changes in third party access regulation.¹⁰¹ Activities of a commercial character are by nature susceptible to legislative development and possible changes of the legal framework. The competence of any legislature to develop and adjust primary and secondary legislation to economic, market and policy considerations would be unduly and unrealistically limited by requiring absolutely no changes in the legal framework for 20 years.¹⁰²

132. Equally, the risk to find creditworthy shippers is addressed through the binding capacity allocation conditions/market testing conditions and via the binding contract, but not through an exemption.

133. The Secretariat notes that the potential cost overruns can be recovered through the regulated tariff regime, namely via the correction element¹⁰³ that recovers all efficiently incurred and justified cost overruns in the following tariff/regulatory period. Also, AERS stated that the currently applicable methodology ensured covering of all justified costs and yields on investments. Thus, the Secretariat considers that this claimed risk is not relevant for the exemption.

134. Moreover, the size of the Serbian market as a demand risk is not the relevant benchmark for the risk assessment, as the Project's goal is not only to supply Serbia and Bosnia and Herzegovina, but to transit majority of gas volumes (approx. (%) of the planned technical capacity) to Hungary and its neighbouring countries.

135. As regards the Project's investment and financing risk, the Secretariat notes that the cost of debt assumed for the Project amounted to ...%.¹⁰⁴ This is low given that the project is realized in Serbia and the current risk-free rate of Serbia, is 4.2%¹⁰⁵, even if it aims to supply markets beyond Serbia. The low cost of debt assumed is the reason for the Project's low weighted average capital cost (WACC).¹⁰⁶ The low WACC assumption, in turn, results in a relatively low internal rate of return (IRR) of ...%.¹⁰⁷

136. The financing of such a significant project inevitably requires a blend of financing instruments. Among others, these can feature: (i) sovereign grants, loans and guarantees, thus decreasing the financial exposure; (ii) International Financial Institutions (IFIs) project financing or state financing to be sub- lent to a special purpose vehicle/project company typically with very competitive conditions; (iii) Export Credit Agency (ECA) financing; (iv) commercial and syndicate loans from the financial market; (v) project bonds; (vi) corporate financing, shareholder (recourse, limited- or non-recourse or subordinated) loans; (vii) completion support/shareholder guarantee to decrease risk exposure of other financiers; (viii) and shareholder equity to limit financial gearing.

137. The assumed low cost of debt would be achievable through a significant share of project financing from IFIs, blended with sovereign guarantees, loans or decreased exposure via national or international grants. The Secretariat agrees with AERS that these options are not realistic to support finance of the Project in its current design. Rather, the Project will need to involve commercial bank/syndicate loans within the financing portfolio, due to the size of the financing needs.

100 Funds available according to Rules of Procedure on conditions and manner of attracting the direct investments (Official Gazette of the Republic of Serbia No 18/2018).

101 Commission Staff Working Paper, paragraph 17.

102 Cf Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 65.

103 Cf Methodology for Setting Natural Gas Transmission Use-of-System Charges (Official Gazette of the Republic of Serbia No. 93/2012).

138. A possible way to achieve such favourable financing conditions would be through significant corporate financing by the shareholders. Corporate financing may take the form of shareholder loans, special project bonds¹⁰⁸, limited/non-recourse debt or completion support/shareholder guarantees. In all these cases, if the debt is owned/financing is provided by the ultimate shareholder, the risks are not attributable to the Project itself, but to the risk profile of the entire undertaking providing the corporate financing. Such a financing structure would indeed significantly decrease the investment and financial risks of the Project, and may enable achieving the envisaged cost of debt.

Against this background, the Secretariat concludes that the alleged risk related to the limited number of shareholders in particular cannot substantiate the exemption, as the Project's ultimate majority shareholder is a diversified, integrated gas export company, namely Gazprom, with the current capital investments in the value of around EUR 15.7 billion and financial investment in the value of around EUR 38.5 billion, out of which approx. EUR 2.1 billion is long term loans provided to companies.¹⁰⁹

This means that the project is part of a diversified risk portfolio. Furthermore, the majority shareholder is in the position to provide favourable corporate and project financing to the shareholders of Gastrans or the project company directly via its financial affiliates, which further decreases the financial risk.

139. The Secretariat acknowledges that the exemption, and in particular certain aspects thereof, has a significant role for enabling the targeted low cost of debt, especially due to the necessary involvement of commercial/syndicate loans. Without the exemption on ownership unbundling, Gazprom could not be engaged as majority shareholder in the Project.

140. The Secretariat recalls its findings above that the Project, in its current design, will strengthen the shareholders in their monopolistic positions on the relevant markets. This lowers the risk of the investment and thus reduces the need for an exemption.¹¹⁰ The exemptions from third-party access and regulated tariffs, as granted by AERS under the current conditions are not proportionate compared to the risks incurred.

141. Taking into consideration the results of the non-binding market test, it is also reasonable to assume that third-party bookings will materialize, which will increase the Net Present Value and the IRR, and decrease the payback period. In the absence of the sensitivity analysis in the feasibility study, the Secretariat cannot determine the magnitude of the improvement in the financial key performance indicators (KPIs) and thus reduction in financial risks, as a result of an extra unit of third party booking on any of the Entry or Exit points.

104 Schedule 1 - GASTRANS d.o.o. Novi Sad Feasibility Study on Construction of the Energy Infrastructure, June 2018, pg. 24: "cost of debt is 2.5% (information provided by the Company Management)".

105 <https://www.ekapija.com/en/news/1872406/yield-on-15-year-government-bonds-remains-at-42and>

<http://www.icbbg.rs/eng/berza/sno.php?ID=241>, also presented in the feasibility study submitted by Gastrans. The risk-free interest rate is based on the 15 years T bond issue of the Republic of Serbia of 06.09.2018 as retrieved on 14.01.2019.

106 Where debt is assumed to be ...% in the capital structure and because the cost of equity (...%) has been set at%.

107 Schedule 1 - GASTRANS d.o.o. - Feasibility Study on Construction of the Energy Infrastructure, June 2018, pg. 26

108 In the special case when the parent company buys the bond.

109 Gazprom PJSC Annual Report 2017 - Balance Sheet as of 31 December 2017.

Conclusion

142. Based on the above, the Secretariat acknowledges the need for long-term financial stability and predictability for financing a project involving high investment costs. In this respect, the Secretariat understands the project promoters' argument that this requires a certain share of the capacity exempted from the application of regulated prices and a certain amount of capacity reserved for use by the investors only.¹¹¹

143. The Secretariat furthermore accepts the conclusion of AERS that the exemption from the obligation of ownership unbundling of Gastrans as the Project's transmission system operator is justified based on the investment risk attached to the Project in its current design. The exemption from ownership unbundling may be considered a proportionate measure to mitigate risks caused by the size of the project and the targeted costs of debt, which requires the shareholder's involvement in equity and debt financing.

144. On the other hand, the Secretariat considers the conclusions of AERS concerning the exemption from third-party access and the application of regulated prices under its current conditions of 88% of capacity exempted not proportionate in view of the risks incurred.

145. The low cost of debt targeted by the Project enables lower tariffs (everything else left unchanged). If these lower tariffs are not accessible through third party access to every shipper on all interconnection points, it further enhances the dominant position of the shareholders. For this reason, the exemption conditions of the Decision are not proportionate compared to the recognized risks.

146. In order to mitigate the risk of attracting finance, not all the currently exempted capacity on the Serbian and Hungarian Exit points and the Serbian Entry point would need to be exempted from third-party access and regulated prices, as the Project's financial viability, together with anticipated third party bookings, will not be jeopardized. The Secretariat recalls that an increase in the share of non-exempted capacities is also indispensable to make capacity accessible for potential new market entrants for the Serbian and regional gas markets.

147. The scenario used for the financial cost-benefit analysis can be considered as conservative for the investor, as no third party booking has been assumed. The Project has been evaluated as financially viable in this conservative scenario by the shareholders and AERS. However the Secretariat observes that any third party booking will further increase the financial viability of the project. Therefore, there is room for competition enhancement without jeopardizing the financial viability of the Project.

4.4. The infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose system that infrastructure will be built (Article 36(1)(c) of Directive 2009/73/EC)

148. Article 36(1)(c) of Directive 2009/73/EC requires for the major new gas infrastructure requested for exemption to "be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that infrastructure will be built".

149. In this respect, the Decision confirms that the new pipeline will be constructed by Gastrans, which is not an operator of any other segment of the Serbian natural gas system. AERS further relies on the commitment of Gastrans to acquire ownership rights over the new pipeline once it is constructed, to manage and operate the pipeline, and to carry out the activity of the transmission of natural gas through the pipeline. The Decision is made subject to a condition that Gastrans becomes the owner of the new pipeline and manages it as a system operator in accordance with the Decision.

150. The Secretariat considers it sufficiently established that Gastrans, at least in terms of its legal form, is separate from the transmission system operators in charge of any other segment of the Serbian natural gas transmission system, namely Srbijagas¹¹² and Yugarosgaz Transport¹¹³. Moreover, the Secretariat has no reason to doubt the company's intention to acquire the ownership over the pipeline once it is constructed, and to be designated as a natural gas transmission system operator for carrying out the transmission of natural gas through the pipeline as confirmed by AERS.

4.5. Charges must be levied on users of that infrastructure (Article 36(1)(d) Directive 2009/73/EC)

151. Article 36(1)(d) of Directive 2009/73/EC requires that the charges for using the major new gas infrastructure requested for exemption "must be levied on users of that infrastructure".

152. According to the Decision, the tariffs for long-term contracted capacities on the Project will be imposed on all users of the exempted capacities. These tariffs will be calculated in line with the tariff methodology to be developed by Gastrans in accordance with the principles established by the Decision.

153. Having in mind that the Project's shareholders are vertically integrated undertakings active also in the supply of natural gas, it is of utmost importance that the transport charges are not excessive to deter third-party access (of non- shareholders)¹¹⁴ and that there is no abuse of a dominant position of shareholders in the respective markets. Therefore the Secretariat deems it important that the tariff methodology determined by Gastrans is approved by AERS before entering into force and that AERS is empowered to regularly monitor whether Gastrans complies with the approved methodology i.e. whether the tariffs are calculated according to the approved methodology.¹¹⁵

154. Provided that the Decision is amended in the abovementioned manner, the Secretariat confirms that the criterion established by Article 36(1)(d) of Directive 2009/73/EC is fulfilled.

4.6. The exemption must not be detrimental to competition or the effective functioning of the internal market in natural gas, or the efficient functioning of the regulated system to which the infrastructure is connected (Article 36(1)(e) Directive 2009/73/EC)

4.6.1. The exemption must not be detrimental to competition

155. On the basis of its assessment under point 4.2.1 above, the Secretariat comes to the conclusion that the exemption is detrimental to competition.

4.6.2. The exemption must not be detrimental to the effective functioning of the internal market

156. The effective functioning of the internal market may be affected where an exemption impedes the overall optimization of the functioning of markets connected to the Project or creates barriers to free movement of gas, such as congestion.¹¹⁶ The Decision excludes any such effects.

¹¹⁰ Commission Staff Working Document, paragraph 46.

¹¹¹ Cf Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 66.

¹¹² As explained above, Srbijagas continues to carry out the activities of the natural gas transmission system operator, covering 95% of the natural gas transmission network of the Republic of Serbia, pursuant to Article 421 of the Energy Law, which authorises such activity before certification of the newly designated transmission system operator.

¹¹³ License No 0219/13-LG-TSU issued by AERS on 28.08.2013 for the period of 10 years.

¹¹⁴ Commission Staff Working Paper, paragraph 57.

¹¹⁵ Also in the case of increase or decrease of tariffs according to the tariff methodology.

¹¹⁶ Commission Staff Working Paper, paragraph 61.

¹¹⁷ The Decision, page 56.

157. The Decision further assumes positive effects of the Project on the functioning of the internal market. From a technical point of view, AERS envisages that the Project's higher pressure level compared to the one of the existing gas transmission system of Serbia will avoid congestion. AERS also refers to the envisaged operation agreement between the Project and the Serbian transmission system.¹¹⁷ Moreover, AERS assessment is based on the assumption that common technical interoperability standards will apply at interconnection points.¹¹⁸

158. There is no reason to assume that the Project will create barriers in terms of compatibility with technical and (inter-)operational standards with the gas systems of Serbia, Hungary and Bulgaria to which it aims to connect. Technical harmonisation is probably just a function of the project promoters' interest to physically reach the markets targeted by the Project.

159. However, Article 36(1)(e) of Directive 2009/73/EC refers to the effect of the exemption and not the technical parameters of the Project. In this respect, the Decision analyses only the positive impact of selected elements of the exemption, namely the availability of short-term capacities and the applicability of congestion management at the interconnection points to Serbia, Hungary and Bulgaria which is supposed to avoid congestion.¹¹⁹ Yet, the impact of the exemption on the effective functioning of the internal market is not only a question of whether congestion can be minimized. The Decision does not elaborate on potential other negative impacts of an exemption to the creation of an integrated internal gas market and the free flow of gas across borders. In this respect, the Secretariat recalls that Article 2 of the Treaty establishing the Energy Community tasks the Parties to the Treaty to "create a single regulatory space for trade in gas" and "to develop gas and electricity market competition on a broader scale".

160. In principle, a new interconnection between gas markets is able to develop positive effects on the development of competition, increase liquidity and facilitate the flow of gas between these markets, i.e. in the present case Hungary and Bulgaria.¹²⁰

161. Under the exemption granted by the Decision, however, the potential of those effects to materialize is not likely. With a large part not being open to third parties, the strengthening of the dominant positions of the Project's shareholders on the relevant capacity and commodity markets, the systematic elimination of incentives for enhancement of competition, the scope of the exemption rather undermines the effective functioning of the internal market and the free movement of gas and cross-border trade¹²¹

162. The availability of short-term capacities and the application of congestion management procedures at the interconnection points between Serbia and Hungary, in itself, is not sufficiently able to lift these negative effects for Hungary.¹²²

163. With regards to Hungary, the Secretariat further notes the potential risk of the capacity market (and thus the commodity market) becoming further foreclosed. This concern is reflected in Decision 1858/2017 of MEKH. The exemption, in the manner and form granted by the Decision, is likely to have negative effects on the effective functioning of the Hungarian market. Additional conditions are necessary to ensure access to capacity by third parties.

118 I.e. the rules of Regulation 703/2015 establishing a network code on interoperability and data exchanges; the Regulation has been incorporated into the Energy Community acquis communautaire Decision 2018/02/PHLG-EnC of the Permanent High Level Group of 12.01.2018 with a deadline for implementation and transposition of 01.10. 2018.

119 The Decision, page 56.

120 Secretariat Opinion 1/2013 on the exemption of the Trans Adriatic Pipeline interconnector, paragraph 105; Commission Decision D(2008) 142 of 08.02.2008 on the exemption of the Nabucco interconnector, paragraph 55; Commission Decision on the exemption of the interconnector Greece-Bulgaria, C(2018)5058 of 25.07.2018. paragraph 151.

121 Commission Decision of 9.12.2016 on the exemption for an electricity interconnector between Italy and France, paragraph 72.

122 See further paragraph 109 of the Opinion.

164 .Moreover, for the assessment of the impact of the exemption on the functioning of the internal market, also the likely effects on present or future infrastructure projects should be taken into account. This requires that repercussions that the exemption may have on other projects, whether regulated, exempted or submitted for exemption, need to be considered.¹²³ In particular, the exemption may have a detrimental effect on the economic viability of a similar infrastructure planned in parallel to the Project.¹²⁴

165. In the view of the Secretariat it is relevant to analyse this aspect specifically with regard to the planned interconnector between Serbia and Bulgaria (IBS) as the most mature one affecting the markets of Serbia, Bulgaria and Hungary.¹²⁵ The interconnector will make available capacities for the transport of (...to ...)bcm/a of gas from Bulgaria to Serbia and ... bcm/a from Serbia to Bulgaria on the basis of unlimited third party access. According to the above, IBS is capable of positively affecting competition, increasing liquidity and facilitating the flow of gas between gas markets. As elaborated above, the Project and its exemption, on the other hand, entail market foreclosure and are detrimental to competition. At the same time, its capacity is much larger than IBS'. Under these circumstances, there is a risk that IBS may not be realized on the account of the Project. Given this risk, the Project should allow at least a comparable level of freely accessible gas volumes for supply to the Serbian market and physical reverse flows to Bulgaria in the case of an emergency.

166. The Secretariat concludes that the exemption, as granted by the Decision, is detrimental to the effective functioning of the internal market, unless significantly modified.

4.6.3. The exemption must not be detrimental to the effective functioning of the regulated system to which the infrastructure is connected

167. This criterion requires an assessment of how the exemption influences the costs of operating the regulated system to which the Project will be connected. A negative impact on the effective functioning of the regulated system occurs if the Project, as exempted by AERS, would lead to substantially higher network tariffs in any of the connected regulated gas systems of Serbia, Bulgaria or Hungary. This could be the case if the realization of the Project require the expansion or reinforcement of the existing regulated infrastructure.¹²⁶

168. The Decision concludes that the exemption will not have an impact on the tariffs of the regulated systems of Serbia, Hungary and Bulgaria and will thus not be detrimental to the effective functioning of the regulated systems. AERS argues that the high level of interest expressed in the non-binding phase of the Project's market test for long-term capacities at the entry point to Serbia from Bulgaria and further on at the interconnection point to Hungary suggests that the income to be gained from allocation of the new capacities in Bulgaria and Hungary for the benefit of Gastrans will out-weight the related costs of system expansion in those countries.

¹²³ Commission Staff Working Paper, paragraphs 60 and 63.

¹²⁴ cf. Commission Decision C(2011)3424 of 20.05.2011 on the exemption of the Gazelle interconnector, paragraph 63.

¹²⁵ The project forms part of the EU's Projects of Common Interest and should allow for the transfer of between 1 and 1.8 billion cubic meters of natural gas annually from Bulgaria to Serbia and 0.15 billion cubic meters from Serbia to Bulgaria. On the Serbian side the project would connect to the existing Serbian gas transmission system. The European Commission contributes to the Serbian side of the project with a Pre-Accession grant of EUR 49.6 million. See: https://ec.europa.eu/info/news/eu-investment-gas-interconnection-between-bulgaria-and-serbia-enhance-energy-security-region-2018-may-17_en.

¹²⁶ cf. Commission Staff Working Paper, paragraph 62.

169. In the view of the Secretariat, this assessment is reasonable for the case of Serbia. The Project will not increase the regulated asset base and thus the tariffs of the regulated gas transmission system in Serbia. Given that the Project will largely be exempted, the regulated system and Serbian customers are shielded from the risk to reimburse the costs of an underuse of the system via the regulated tariffs.¹²⁷

170. The Secretariat also has no reason to challenge the assumption of a neutral impact of the exemption on the regulated system of Bulgaria.

171. However, the Secretariat has concerns as regards the impact of the Project, as exempted, on the regulated system of Hungary. Namely, the consultation documentation related to the TYNDP of the Hungarian gas transmission system operator FGSZ¹²⁸ suggests an impact of the Project on increasing the regulated transmission tariffs in Hungary. However, the precise dimension of such effect remains subject to the final decision on the technical approach for linking the Hungarian transmission system to the Project, which has still not been decided upon (as discussed at point 4.1.1 above).

172. Until FGSZ has taken a decision as to whether and how incremental capacity will be built, it is difficult to evaluate the impact of the Project on tariffs and the possible increase resulting from the Project's interconnection with Hungary. In this situation, the Secretariat cannot fully subscribe to the conclusions of the Decision with respect to the impact on the effective functioning of the regulated system to which the Project is connected.

4.7. Others (Article 36(6) Directive 2009/73/EC)

173. Article 36(6) of Directive 2009/73/EC also requires that the regulatory authority concerned decides upon the rules and mechanisms for management and allocation of capacity before an exemption is granted. The Secretariat deems that this requirement was fulfilled by AERS in its decision published on 12 February 2018.

5. The Secretariat's Opinion

174. It follows from the assessment of the criteria in Article 36(1) of Directive 2009/73/EC and their application to the Project by AERS, that the Decision fails to meet all the conditions required by that provision. The list of conditions in Article 36 (1) of Directive 2009/73/EC is of a cumulative nature. If one condition is not fulfilled, the Project cannot be exempted. In this respect, the Secretariat recalls that in particular the detrimental impact of the Project, as exempted by the Decision, on competition in the relevant markets but also the level of risk is such that it does not justify an exemption under Article 36(1) of Directive 2009/73/EC.

175. The Secretariat finds it imperative that an exemption is not granted to the Project, unless the following safeguards and remedies are introduced in their entirety, and their implementation is ensured and monitored by AERS. AERS shall ensure that in the case of non-compliance with these safeguards and remedies the exemption shall lose its effect.

127 cf. Commission Staff Working Paper, paragraph 62; Secretariat Decision 1/2013 on the Trans Adriatic Pipeline interconnector; Commission Decision C(2011)3424 of 20.05.2011 on the exemption of the Gazelle interconnector, paragraph 66; Commission Decision D(2008) 142 of 08.02.2008 on the exemption of the Nabucco interconnector, paragraph 55.

128 https://fgsz.hu/file/documents/1/1158/tyndp_18122018_hu.pdf.

176. The Secretariat stresses that the required safeguards are applicable and shall be implemented in full regardless of any potential changes in the technical capacity by the Project.

177. Therefore, if AERS decides to uphold its decision to grant an exemption to the Project, the Secretariat requests that the following safeguards and remedies are included in AERS' final Decision.

On the sales, bookings and allocation of capacities on the interconnection point Bulgaria-Serbia at Zaječar

178. The exemption shall allow, for a period not exceeding 20 years from COD, Gastrans to sell and allocate a maximum of ..% of the total technical annual capacity of the interconnection point on the Serbian/Bulgarian border to the companies Gazprom Export and Srbijagas ("exempted capacity"). In the case of over-booking of the exempted capacity, the bookings made by Gazprom Export and Srbijagas shall be reduced on a pro rata basis. In the case of under-booking of the exempted capacity, the remaining available capacity shall be considered as non-exempted long-term capacity and shall be sold and allocated according to the rules in the following paragraph.

179. A minimum of ...% of Gastrans' total technical annual capacity of the interconnection point on the Serbian/Bulgarian border ("long-term non-exempted capacity") shall be sold and allocated to interested system users via auctions on an annual yearly basis organized on a capacity booking platform pursuant to Article 37 of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the long-term non-exempted capacity products are offered on the same platform used in the neighbouring EU Member States i.e. Bulgaria and Hungary. The auctions for the long-term non-exempted capacity shall be performed in two phases: Phase 1 of the auction shall be open to all interested system users excluding the shareholders of Gastrans and any affiliates. The capacity offered in Phase 1 of the auction shall comprise of yearly products with a duration of not more than 20 years. The reserve price in Phase 1 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity. Phase 2 of the auction shall be open to all interested system users. The capacity offered shall comprise of yearly products for no longer than the upcoming 3 years. The reserve price in Phase 2 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity.

180. A minimum of ...% of Gastrans' total technical annual capacity of the interconnection point on the Serbian/Bulgarian border ("short-term non-exempted capacity") shall be sold and allocated via auctions organized on a capacity booking platform pursuant to Article 37 of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the short-term non-exempted capacity products are offered on the same platform used in the neighbouring EU Member States i.e. in Bulgaria and Hungary. The auction shall be open to all interested system users. The capacity offered shall comprise of quarterly, monthly, daily and within-day products. The reserve price for all short-term products at the auction shall be calculated pursuant to Chapter III of Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a network code on harmonised transmission tariff structures for gas ("TAR Network Code").

On the sales, bookings and allocation of capacities on the Gastrans interconnection point Serbia- Hungary

181. The exemption shall allow, for a period not exceeding 20 years from COD, Gastrans to sell and allocate a maximum of ...% of the total technical annual capacity of the interconnection point on the Serbian/Hungarian border to Gazprom Export and Srbijagas ("exempted capacity"). In the case of over-booking of the exempted capacity, the bookings made by Gazprom Export and Srbijagas shall be reduced on a pro rata basis. In the case of under-booking of the exempted capacity, the remaining available capacity shall be

considered as non-exempted long-term capacity and shall be sold and allocated according to the rules in the following paragraph.

182. A minimum of ...% of Gastrans' total technical annual capacity of the interconnection point on the Serbian/Hungarian border ("long-term non-exempted capacity") shall be sold and allocated to interested system users via auctions on an annual yearly basis organized on a capacity booking platform pursuant to Article 37 of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the long-term non-exempted capacity are offered on the same platform used in the neighbouring EU Member States i.e. Bulgaria and Hungary. The auctions for the long-term non-exempted capacity shall be performed in two phases: Phase 1 of the auction shall be open to all interested system users excluding the shareholders of Gastrans and any affiliates. The capacity offered in Phase 1 of the auction shall comprise of yearly products with a duration of not more than 20 years. The reserve price in Phase 1 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity. Phase 2 of the auction shall be open to all interested system users. The capacity offered shall comprise of yearly products for no longer than the upcoming 3 years. The reserve price in Phase 2 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity.

183. A minimum of ...% of Gastrans' total technical annual capacity of the interconnection point on the Serbian/Hungarian border ("short-term non-exempted capacity") shall be sold and allocated via auctions organized on a capacity booking platform pursuant to Article 37 of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the short-term non-exempted capacity are offered on the same platform used in the neighbouring EU Member States i.e. in Bulgaria and Hungary. The auction shall be open to all interested system users. The capacity offered shall comprise of quarterly, monthly, daily and within-day products. The reserve price for all short-term products at the auction shall be calculated pursuant to Chapter III of the TAR Network Code.

On the sales, bookings and allocation of capacities on the exit points into the domestic gas transmission system of Serbia at Paraćin, Pančevo and Gospođinci

184. The exemption shall allow, for a period not exceeding 20 years from COD, Gastrans to sell and allocate a maximum of ...% of the total aggregated technical annual capacity of the three exit points to the system operated by Srbijagas to Gazprom Export and Srbijagas ("exempted capacity"). In the case of over-booking of the exempted capacity, the bookings made by Gazprom Export and Srbijagas shall be reduced on a pro rata basis. In the case of under-booking of the exempted capacity, the remaining available capacity shall be considered as non-exempted long-term capacity and shall be sold and allocated according to the rules in the following paragraph.

185. A minimum of ...% of Gastrans' total aggregated technical annual capacity of the three exit points to the system operated by Srbijagas ("long-term non-exempted capacity") shall be sold and allocated to interested system users via auctions on an annual yearly basis organized on a capacity booking platform pursuant to Article 37(1) of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the long-term non-exempted capacity are offered on the same platform used in the neighbouring EU Member States i.e. Bulgaria and Hungary. The auctions for the long-term non-exempted capacity shall be performed in two phases: Phase 1 of the auction shall be open to all interested system users excluding the shareholders of Gastrans and any affiliates. The capacity offered in Phase 1 of the auction shall comprise of yearly products with a duration of not more than 20 years. The reserve price in Phase 1 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity. Phase 2 of the auction shall be open to all interested system users. The capacity offered shall comprise of yearly products for no longer than the upcoming 3 years. The reserve price in Phase 2 of the auction shall be equal to the tariff applicable to the shareholders of Gastrans for using the exempted capacity.

186. A minimum of ...% of Gastrans' total aggregated technical annual capacity of the three exit points to the system operated by Srbijagas ("short-term non-exempted capacity") shall be sold and allocated via auctions organized on a capacity booking platform pursuant to Article 37 of the CAM Network Code. In order to facilitate a smooth implementation, the Secretariat suggests that the short-term non-exempted capacity are offered on the same platform used in the neighbouring EU Member States i.e. in Bulgaria and Hungary. The auction shall be open to all interested system users. The capacity offered shall comprise of quarterly, monthly, daily and within-day products. The capacity offered shall comprise of quarterly, monthly, daily and within-day products. The reserve price for all short-term products at the auction shall be calculated pursuant to Chapter III of the TAR Network Code.

Liquidity measure for the gas market in Serbia

187. As from COD, the shareholders of Gastrans and their affiliates shall be obliged to offer each quarter a volume equivalent to 30% of the volume of their total natural gas sales in the corresponding quarter of the previous year in Serbia – regardless of the point of entry into the Serbian domestic transmission system – on an independent organized market place e.g. SEEPEX. The delivery point of the offered gas shall be the Virtual Trading Point (VTP) in Serbia. The offer price shall not be higher than the price defined in the long-term contract of the entity. In the absence of demand from third parties, the offered volumes shall remain in the ownership of the undertaking which offered it.

188. At the end of each quarter the shareholders of Gastrans shall submit a report to AERS about the volumes of natural gas sold by them and their affiliates in Serbia and the volumes of gas they offered on the organized market place.

189. AERS shall monitor the compliance of the shareholders' obligation under the previous two paragraphs, and shall ensure that all interested parties have free and non-discriminatory access to the services and to the gas offered on the organized market place. AERS shall publish annual reports on the liquidity of the gas market in Serbia.

190. In case third parties not related to either shareholders of Gastrans and their affiliates reach a combined share in the volume of total annual natural gas sales in Serbia of ...% or more, the application of the Liquidity Measure may be suspended in the following year.

191. Not later than five years as from COD, AERS and the Secretariat shall review whether the liquidity measure has contributed to the enhancement of competition on the natural gas market in Serbia and, as the case may be, propose changes respecting the general scope of the exemption.

Other measures related to the enhancement of competition and avoiding conflicts of interest

192. Before COD, Gastrans' shareholder Srbijagas shall ensure that its subsidiary Transportgas Srbija is unbundled, and unconditionally certified by AERS, taking into account the Opinion of the Secretariat, as the transmission system operator of the gas transmission system currently operated by Srbijagas.

193. The tariff methodology determined by Gastrans shall be approved by AERS before entering into force. AERS shall regularly monitor whether Gastrans complies with the approved methodology i.e. whether the tariffs are calculated according to the approved methodology.

For the enhancement of security of supply of natural gas in Serbia

194. Gastrans shall ensure that physical reverse flows for emergency operations are enabled from Serbia to Bulgaria.

Additional safeguards for the effective functioning of the internal market in natural gas and the efficient functioning of the regulated system to which the infrastructure is connected

195. To the extent not conflicting the exemption, the Energy Community acquis communautaire shall apply in its entirety to the non-exempted part of the Project as from the date of expiry of the respective transposition deadlines.

196. AERS shall ensure that the capacities on interconnection points are offered as bundled products in line with Articles 19-21 of the CAM Network Code.

197. AERS shall ensure that congestion management rules (Use-It-Or-Lose-It or Use-It-Or-Sell-It) shall be fully applied on both the exempted and non-exempted capacities of Gastrans.– AERS shall ensure that Gastrans offers non-nominated day-ahead capacities firm (UIOLI) and provides the relevant rules immediately for the approval of AERS.

198. AERS shall ensure that interruptible capacity (i.e. backhaul) is made available on the Gastrans pipeline in the direction from Hungary to Serbia and from Serbia to Bulgaria at a close-to-zero tariff from the start of commercial operations. AERS shall ensure that all relevant elements of the Energy Community acquis enabling counter nominations and the provision of interruptible capacities in the reverse direction on the pipeline for all shippers are applied by Gastrans. AERS shall closely work with the national regulatory authorities of Bulgaria and Hungary to ensure that the relevant interruptible capacity matching the offer on the Gastrans pipeline can be booked and nominated in their jurisdictions and regulatory systems as well.

199. Gastrans shall identify the demand for incremental capacity in both forward and reverse directions on the pipeline through regular binding market tests which will be performed every second year, and consequently build incremental capacity, unless it shows that expansion is not economically viable. The newly built incremental capacity shall be offered and allocated via auctions of long-term and short-term capacity products on a capacity booking platform pursuant to Article 37 of the CAM Network Code. The auctions shall be open for all interested parties.

200. Gastrans shall ensure and AERS shall monitor that Gastrans operates independently from its shareholders. Gastrans shall preserve the confidentiality of commercially sensitive information and shall guarantee that no information related inter alia to the booking, nomination and allocation of capacities is disclosed in a discriminatory manner to the advantage of its shareholders and affiliates.

Vienna, 1 February 2019

Janez Kopač Director, m.p.
Deputy Director/Legal Counsel, m.p.

IV. Party's views on the draft final decision

Upon receiving this opinion, the Agency invited the requesting party to submit to the Agency within 8 days its views on the conditions of exemption provided by the Secretariat in its opinion and under which conditions the Agency is obliged to base its final decision on exemption to the maximum extent possible. Acting upon the invitation sent by the Agency to the proxies of the party by a letter dated 7.2.2019, in accordance with Articles 11 and 106. of the Law on General Administrative Procedure, GASTRANS d-.o.o. submitted its views through the proxy by an act dated 22 February 2019, in which it mainly disputes the content of the opinion of the Secretariat in the part referring to the points 178-192 and 198 of the Secretariat's opinion.

In its statement, Gastrans requested that the provisions under points 1,2,3,4,5,6,7,12,13,14,15,16 and 17 of the Preliminary Decision enacting terms remain unchanged, and in regard to the points 8, 9, 10 and 11 that the Agency

adopts the following requirements as it considers that the implementation of the conditions from the Secretariat's opinion would be unjustified, for the following reasons:

- in point 179 of the Opinion the Secretariat requests that capacities shall be made available to all interested system users in Phase 1 of the capacity allocation, excluding the shareholders/members of Gastrans d.o.o. and their affiliates

- that Gastrans d.o.o. understands that "all interested system users" means the companies that have expressed interest in using the new interconnector during the non-binding phase,

- that there was an objective reason justifying 88% of capacity for priority allocation at all entry and exit points, as well as that exempted capacities will be allocated in practice in equal percentage at all entry and exit points;

- that the percentage of priority capacity was derived from the amount of long-term capacity commitments required to achieve an economically viable tariff and obtain third party debt financing sufficient for the shareholders/members to be able to commit to their equity contributions and to implement the project even in the case that there is not third party interest.

The requesting party points out that the Secretariat in its opinion requires a change in the percentage of priority capacities in terms of downsizing at the points of entry and exit, for which the Secretariat did not provide an explanation of how the required percentage of capacity was determined, and in the absence of an adequate explanation, it is impossible to understand why the percentages at the entry point from Bulgaria and at the exit point to Hungary would be different. Gastrans also points out to the contradiction that the volumes of natural gas which the Secretariat requires to be made available to the market and the success of the implementation of this measure is determined on the basis of 20% of the market share in Serbia, while the exit capacity into the Serbian system, which is allocated in priority to shareholders/members is limited to 55%, instead of 80%. The Opinion also points out not considering how the respective percentages would be viewed from the perspective of ensuring the bankability of the project, as the key criteria for the initial sizing of the capacity, as well as in the cases where there may not be any significant initial demand for long term capacity by third parties. The decision would in theory make it possible that up to 45% of the exit capacity to the Serbian market may remain uncommitted or may only be committed on the basis of a three year commitment. Applying common requirements for acquiring the financing for gas pipelines of this nature, Gastrans points out that such an arrangement would not be bankable and would not realise the equity investment by the shareholders/members.

Regarding the request of the Secretariat about the allocation of capacity at the interconnection point between Bulgaria and Serbia, Gastrans d.o.o. and its shareholders/members accept the proposed percentage of priority capacity for shareholders/members, and long-term non-exempt capacity, as well as 10% short-term non-exempt capacity only if the key bankability requirements underpinning the original technical sizing can still be met in some other form. The same is true in respect of implementation of auctions in phases relating to the long-term non-exempt capacity. Gastrans d.o.o. notes that, when determining access based on different allocation percentages for different entry/exit points, an absolute limit on the percentage of shareholder/member capacity is not proposed, and this deviates from the approach in other decisions on exemption. Taking this approach has helped alleviate the significant deviation from 88% - 12% principle. This is only if there is a prospect of them being able to acquire significant capacities within the all-market-participant auction rounds (if needed) as, in doing so, the New Interconnector would be able to ensure a similar level of bookings being realised as in the case of 88% - 12% model, which they consider to be crucial for acquiring the financing for the New Interconnector and for the maintenance of a commercially sustainable level of tariffs. Gastrans d.o.o. concludes that in the absence of a significant interest in capacities in phase 1 of the auction, it would not be appropriate to allocate capacities at this stage because this would result in an uneconomical design of the gas pipeline and lead to higher tariffs. Therefore Gastrans d.o.o. proposes that, in the event less than 90% of the long-term non-exempt capacity is subject to successful bids, (which would equate to a similar financing base case as for the originally proposed 88% capacity for which the shareholders/members of the company Gastrans d.o.o. expressed a willingness to contractually commit) the first phase auction should not result in capacity allocation and instead all capacity should roll forward for allocation in the second phase.

Gastrans d.o.o. disputes the requirement that the capacities offered under the second phase will "consist of annual products for a period not exceeding the next 3 years" as proposed by the EnCS, noting that the EnCS did not provide any justification as to the reason for determining the time limit of 3 years, nor the reasoning whether such a restriction is consistent with previously approved exemption cases, or whether it reflects the current or possible future

level of market development. The analysis carried out by Gastrans d.o.o. clearly shows that, if the capacities were allocated only on this basis, the level of booked capacities in that category would be only 30%, which is assessed as insufficient for the financial institutions that would secure the financing of the project and, if implemented, this will lead to the project becoming unbankable for financing, that is, the project will cease to fulfil the requirements of bankability, which can result in the withdrawal from the project. Also, they point out that this will increase the tariff levels and make an economical supply of gas unviable both for Gastrans d.o.o. shareholders/company members and its competitors alike. In addition, they consider it unnecessary for the EnCS to request that third parties that are competitors to members/shareholders may book capacities only for shorter periods in comparison with shareholders/members, if their interest in the non-binding phase of market research studies leads to the conclusion that they are interested in long-term capacities of between 10 and 20 years, and not 3 years as the EnCS proposes, and for which no third party has expressed any interest. Instead, Gastrans d.o.o. proposes that long-term annual capacities under the second phase of the auctions which are not subject to the exemption shall be for a period of 20 years for purely commercial reasons, since otherwise the project would not be realized.

Also, Gastrans d.o.o. believes it is important for it to be able to elect which capacity allocation platform it uses to conduct the auction phases. The comment of EnCS in paragraph 185 of the Opinion suggests that the long-term entry capacities are offered on the same platform used in the neighbouring member states (i.e. RBP), but if Gastrans d.o.o. was bound to a particular platform by the explicit requirement contained in the regulatory decision, this would diminish its impact in negotiations with companies that provide capacity-allocation services through the platform and would almost certainly lead to cost increases, as well as that there are other justified reasons to consider other potential providers of these services, such as PRISMA, or even the possibility that Gastrans d.o.o. develops its own platform .

Regarding the imposed liquidity measure for the gas market in Serbia, Gastrans d.o.o. considers the legality of such a measure as questionable, as well as its effectiveness and appropriateness, since the points 187 to 191 of the Opinion of EnCS do not introduce measures for Gastrans d.o.o but for the ultimate owners and all their subsidiaries that carry out the activity of production and supply of natural gas. According to Article 95 of the Law on General Administrative Procedure and Art. 48 to 60 of the Energy Law, according to substantive regulations, AERS would have no basis to determine any measure such as the liquidity measure proposed in the Opinion, but only in accordance with Article 57 paragraph 3 of the Energy Law, to examine the circumstances, data and the exchanged information, including those concerning the functioning of the natural gas market, and to decide on the implementation of measures to promote effective competition and to ensure the normal functioning of the market, to cooperate with the competent competition authority, which means that AERS can not make decisions solely on the basis of the proposal of the measure stated in the Opinion, but such a measure should be the subject of a special procedure and a decision taking into account the Opinion and which should be in accordance with all other conditions of this process, in order to determine a reasonable measure in accordance with Article 57. Therefore, taking into account the above mentioned arguments, Gastrans d.o.o. considers that the implementation of the liquidity measure would be unreasonable, unjustified and unenforceable within the framework set out in the Final Exemption Act. Gastrans also points out that such measures, according to recent findings of the World Trade Organization Panel in the process of dispute settlement, the Russian Federation / European Union and its Member States - Certain measures related to the energy sector (WT/DS 476/R), the ruling found that different additional conditions for limitation of capacity booking in relation to the optional gas release programmes i.e. the capacities for the purpose of making it available to the market are not in accordance with Article XI: 1 of the General Agreement on Tariffs and Trade of 1994 (GATT), and that the liquidation measure proposed by the Opinion has the same disadvantage (it is contrary to GATT), which can only be fully established after a clear definition of the liquidity measure.

Gastrans d.o.o. considers that the recommendation from the Opinion regarding the price of the released gas volume for the purpose of making it available to the market is not clear, in case this recommendation means that the gas volumes in question should be sold at the purchase price paid for the gas by the shareholders/members, therefore such a provision of the Opinion would be unlawful. Gastrans d.o.o. has no information that such measures have ever been implemented in the scope of the exemption procedure or even as a result of test procedures related to the protection of competition or the granting of a concentration. Even in cases where the gas release programs for the purposes of its placing on the market were established, gas was offered on the market through auctions. In Gastrans d.o.o.' view this is likely to be tantamount to an expropriatory measure and, as a result, the proposal made in the Opinion would have the same effect as the expropriatory measure, which is also contrary to the human right to own

property under Article 58 of the Constitution of the Republic of Serbia. Article 58 of the Constitution of the Republic of Serbia stipulates that the right to own property may be revoked or restricted only in public interest established by the law and with compensation which can not be less than market value. The law may only restrict the manner of using the property. This approach to pricing the gas considers that it will not be viable due to obligations under bilateral investment treaties and the WTO. The Republic of Serbia is currently in the process of joining the World Trade Organization and consequently already has an obligation to comply with the rules of the World Trade Organization, and that the non-acceptance of the requirement from the Opinion would be in accordance with the international obligations of the Republic of Serbia towards the Russian Federation and Switzerland. GAZPROM in the statement indicates that, in cooperation with the competent authorities, AERS should ensure that its decision is harmonized with the Agreement between the Federal Government of the Federal Republic of Yugoslavia and the Government of the Russian Federation on Mutual Investment Promotion and Protection dated 10.10.1995 and the Agreement between the Government of the Republic of Serbia and the Government of the Russian Federation on the Deliveries of Natural Gas from the Russian Federation to the Republic of Serbia dated 13.10.2012. Finally, Gastrans d.o.o. notes that the sale of gas on the Serbian market represents the activity for which it is required to obtain the license in accordance with Articles 19 and 22. of the Law, and that it seems that it would be illegal to impose obligations on companies in regards to the sale of gas if they do not hold or have the legal possibility to hold the adequate license.

In the statement Gastrans also indicates that the level of detail of the liquidity measure extends well beyond previous practice of implementation of equivalent economic measures that were proposed in other projects. For example, the gas release programme for the purpose of its placement on the market that was implemented in the case of TAP was subject to the possibility of a temporary derogation granted by the national regulatory authority, in consultation with the national competition authority. It seems that EnCS has not provided the regulatory authorities of Serbia the same opportunity to determine if under local circumstances there are reasons which might affect or prevent the implementation of the liquidity measure in Serbia from time to time.

Gastrans d.o.o. also believes that the proposed volume of gas release programs for the purpose of making it available to the market is not proportionate and goes significantly beyond what has been seen in practice so far. Gastrans d.o.o. indicates that a number of gas exemptions programs for the purposes of making it available to the market have been determined by the European Commission and the relevant regulatory bodies in the Member States, either as part of the procedures for deciding on notifications of concentration or as part of the liberalization process of the energy market. These programs were restricted to a period of less than 10 years and were related to about 15% of the relevant gas consumption or even a lower percentage. For example, a decision by the European Commission M.3868-DONG/Elsam/Energi E2 concerning the establishment of a gas release program for the purpose of its market availability in the amount of about 10% of the total consumption in Denmark - which is 3 times less than the measure envisaged in the Opinion, whereas the duration of this measure in the case of Denmark was limited to a period of up to 6 years. Other cases include the European Commission's decision of 21 Dec. 2005 in the case of M.3696-E.ON/MOL regarding the determination of the gas release measure for the purpose of making it available to the market in connection with a transaction involving the acquiring of a number of MOL subsidiaries in Hungarian market E.ON; the measure set by the Spanish Ministry of Economy on 29 June, 2010. Decision RCL 2001/1644 concerning the measure of gas release for the purpose of making it available to the market operated by Sagane S.A.A. in terms of 25% of the contracted volumes of gas from the Maghreb gas pipeline in the period from 2001 to 2003; communication of the Energy Regulation Commission in regards to the establishment of the gas release program for the purpose of making it available to the market in France from 15 April 2004, setting up the measure of gas release for the purpose of making it available to the market directed against market participants in the southern and southeastern regions of France for a period of 3 years; the decision of the Italian electricity and gas company, decision ARG/gas 114/09, establishing the gas release program for the purpose of making it available to the market, operated by Eni for the period from October 2009 to March 2010; press release department for loyalty commerce in regards to the agreement of the Department of loyalty commerce with British Gas dated March 11, 1992 in respect of an obligation assumed by British Gas which includes the obligation to release at least 500,000,000 tons of gas per year in the period 1992/1993 to 1994/1995 and 200,000,000 therms during 1995/1996; Order of the Cartel Department of the Higher Court in Vienna of 18 October 2002 in which a joint venture company was registered between the national oil and gas company OMV and regional gas suppliers, which order also includes, inter alia, the obligation to release gas in the amount of 250,000,000 m3 for the period from 2003 to 2008 through auctions.

The Opinion defines the requirement in respect of 30% of the volume of natural gas sales, which significantly exceeds the previous decisions mentioned above for the purpose of comparison without giving any reason for determining such percentage, which is contrary to the European Commission's decision-making process, which includes a detailed assessment of the effects of the gas release program for the purpose of making it available to the market, in order to conclude that such a program is proportionate to achieve the intended purpose (such a detailed assessment usually takes into account the effects to different levels in the supply chain, at the higher-levels and lower levels of supply). The lack of such a detailed assessment leads to arbitrary decision-making that is not based on actual effects in the relevant market, which ultimately calls into question the effectiveness of the proposed program of gas release for the purpose of making it available to the market. All of the above examples clearly show that the Opinion deviates to a great extent from previous practice on a similar issue. Such deviation was also established in regards to the identity of the entities towards which this measure was directed. In particular, all gas release programs for the purpose of making it available to the market have been established as a measure towards a national supplier that is lower in the supply chain rather than to its supplier higher in the supply chain, as the Opinion refers to herein. Therefore, not only is the effectiveness of this measure problematic, especially considering that there is not one such example in the previous practice, but this measure is at the same time a discriminatory measure against Gazprom.

The liquidity measure is also subject to a number of requirements, including sales platforms, a gas delivery site, a restriction of the price at which the exempt gas shall be placed on the market (which in its nature is a measure having the effect of an expropriation measure); condition that the volumes offered remain in the possession of the bidders in the event that they are not used (which, as argued above, is an unreasonable and excessive cost burden/commercial risks that are transferred to market participants on behalf of the opening of the market); the tasks of quarterly reporting that represent an unreasonably high administrative burden, proposed by an incoherent and non-commercial-oriented administrative body, regardless of the pressure that such reporting obligations have on market participants. Therefore, Gastrans assesses that these conditions together exceed the effects of the so far imposed measures of this type. Gastrans d.o.o. questions whether such an approach is justified, or whether it represents regulation for regulation's sake. Gastrans points out that there are more practical liquidity measures to be considered which are not addressed in the Opinion (the mechanisms on which the measure is based would require extensive discussion and engagement of gas exchanges, EnCS and others in order to determine the appropriate commercial and regulatory structure for the implementation of such arrangement), and that the company Gastrans d.o.o. should be enabled to develop a potentially appropriate structure over a specific period of time, and then make a proposal to AERS. Also, Gastrans d.o.o. considers it disproportionate that 30% of the volume of gas subject to liquidity measure is calculated on the basis of the market share of shareholders/members. Taking into account all of the above, both in terms of the legality and the legal nature of the liquidity measure, Gastrans d.o.o. points out that the Agency should not impose the measure of liquidity from the Opinion.

Gastrans d.o.o. notes that, at paragraph 196 of the Opinion, it is proposed that AERS should ensure that the capacities on interconnection points are offered as bundled capacity in line with Articles 19-21 of NC CAM. Gastrans d.o.o. and its shareholders/members, accept this request.

Concerning point 192 of the Opinion regarding the requirement of ownership unbundling and unconditional certification of the company Transportgas Srbija, Gastrans d.o.o. considers that the present request is legally and procedurally unfounded in the exemption decision because the Exemption Act is passed by AERS in accordance with the Law on General Administrative Procedure, which makes it an administrative act that resolves on a particular request by direct application of the law in the relevant field, and determines the rights and obligations of the party in the administrative procedure, and that this request will impose an impossible obligation on the regulator, contrary to the applicable law, to oblige at least two different entities (regardless of the fact that they are affiliate companies) in regards to two different obligations (which are the subject of two separate procedures (exemption procedure or certification procedure)) before the same body (AERS), regulated by different procedures (certification procedure regulated by Articles 239-241 of the Energy Law while the exemption procedure is regulated by Article 288 of the Energy Law), different requirements with regard to proving different conditions and with different legal and operational consequences of the two regulatory processes. Gastrans points out that the recognition of the notion of various procedures in the Serbian Energy Law was also recognized in the previous EnCS decisions relating to Serbian entities performing activities in the energy sector, which led to different (unrelated) decisions of the EnCS in each individual procedure, by which EnCS has shown that it recognizes the notion of different procedures, and that AERS should consider as much

as possible the statement and act in accordance with the laws of the Republic of Serbia and its competencies in certain procedures.

Gastrans points out that point 197 of the Opinion on how to manage congestions (the principle of Use-It-Or-Lose-It) or Use-It-Or-Sell-It)) can be interpreted in different ways, while the application of this principle Use-It-Or-Lose-It should be provided on an interruptible day-ahead basis. Gastrans d.o.o. also notes that, in accordance with the paragraph 199 of the Opinion, it accepts that the process of market test on interest for incremental capacity is carried out every two years (and not every 6 years in accordance with the Preliminary Exemption Act), and that the distribution of newly built capacities is carried out through the capacity allocation platforms in accordance with Article 37 of the NC CAM. In this regard, Gastrans d.o.o. requests clarification in regards to the provisions relating to the application of the acquis referred to in paragraph 195 of the Opinion as well as with regard to the application of Articles 19-21 of the NC CAM which it accepts to apply only in the period following the commissioning of the gas pipeline. Gastrans d.o.o. which is necessary that AERS additionally clarifies when rendering its final decision. Also, the contents of paragraph 198 of the Opinion addressing counter-nominations and the provision of interruptible capacity in the reverse direction are, in general, acceptable, however that this will not be feasible after the date of commissioning of the gas pipeline, but as of the moment when it becomes "reasonably feasible".

Since EnCS is of the view that reverse capacity should be made available at close to zero cost. Gastrans d.o.o. does not believe that this requirement creates a level playing field and would aid overall supply competition in an objective and non-discriminatory manner. Gastrans believes that this will rather serve the purpose of selling the gas available on the Hungarian market on the Serbian or Bulgarian markets without transmission costs, which would put the gas suppliers in the Serbian and Bulgarian markets in a much more unfavourable position, so the payment of the tariff for reverse transmission would enable the reduction of total tariffs and thus have a greater impact on the economic supply of individual gas markets. Gastrans d.o.o. remains at the position that the tariff for reverse capacity is set at 90% of the tariff for uninterruptible capacity in the original direction Bulgaria-Hungary and that such a proposal is reasonable.

As regards paragraph 200 of the Opinion, Gastrans d.o.o. believes that the duty on AERS to ensure that Gastrans d.o.o. operates independently from its shareholders would be appropriate, subject to the inclusion of the caveat that this is the case to the extent that doing so "would not conflict with the scope of the exemption".

As regards Item 8, Gastrans d.o.o.

-Requests that AERS retains priority allocation to the EPA Parties as defined in the Preliminary Exemption Act;

-Requests that AERS clarifies within the Final Exemption Act that the percentages for priority allocation to the EPA Parties do not result in the long-term capacity for other parties that are non-EPA Parties being fully subject to the Energy Community acquis communautaire, without having regard to the scope of the exemption;

-Requests that the percentages of the EPA Parties' capacity and all interested parties' capacity be determined on the basis of the maximum technical annual capacity at the entry point and the exit points as set out in the Preliminary Exemption Act, equalling:

-38.0 million m³ at 20 degrees Celsius / day / year for the Entry Point Kirevo/Zaječar;

-11.94 million m³ at 20 degrees Celsius / day / year for the Exit Point Serbia.

-26.06 million m³ at 20 degrees Celsius / day / year for the Exit Point Horgoš/Kiskundorozsma; and

-Also requests that:

1. Up to 70% of the maximum technical annual capacity for the entry point Kirevo/Zaječar, 55% at the exits in Serbia and 75% at Horgoš can be allocated in priority to the EPA Parties for the contract durations of 20 years;

2. The remaining 20% of the maximum technical annual capacity at the Zaječar exit, i.e. 35% at the exits in Serbia and 15% at the Horgoš exit, can be allocated to all interested parties for the contract durations of 20 years in the next 2 phases, so that in Phase 1 Gastrans d.o.o. may set the bid level in accordance with the alternative allocation principles under the NC CAM and that the EPA Parties do not participate in Phase 1;

- Requests that any overbooking be resolved by ranking the bids according to their commercial value (volume and duration);

- Requests that if bid levels are not reached in Phase 1, third-party bids be automatically transferred to Phase 2, where only bids in the duration of 20 years will be accepted and where the EPA Parties may make bids, that any overbooking be resolved by using the same method as in Phase 1, that Phase 1 and Phase 2 be organised by Gastrans

d.o.o. based on its Rulebook drawn up in accordance with the Final Exemption Act and to the extent applicable under the Allocation Rules, taking into account our comments on Section 8, and that if 90% of the maximum technical annual capacity is not reached in priority allocation of capacity to the EPA Parties and two phases for interested parties combined, Gastrans d.o.o. be entitled to reduce the capacity in accordance with the principles in the Preliminary Exemption Act;

- Requests that all remaining capacity be allocated as short-term capacity in the form of quarterly, monthly, daily and within-day products, in accordance with the Energy Law implementing the NC CAM;

- Requests that after the commencement of the operation of the New Interconnector, short-term capacity be offered as bundled capacity provided that the operator and the regulator of the adjacent transmission system have passed all the necessary decisions facilitating this;

- Requests that Gastrans d.o.o. be entitled to freely choose the allocation platform through which it will allocate short-term products.

Requests that in respect of the Exit Point Serbia:

- Requests that, to avoid any doubt, AERS includes a confirmation in Item 9 of the Preliminary Exemption Act that the Energy Community acquis communautaire shall apply to the capacity not allocated to the EPA Parties as of the date of expiry of the respective transposition deadlines insofar as such application is not contrary to the scope of the exemption granted by the Final Exemption Act, while all other elements in Item 9 of the Preliminary Exemption Act should remain unchanged.

- Requests, with regard to Item 11 of the Preliminary Exemption Action, that AERS should reconfirm the merits of the decision in Item 11 with the right to check tariff calculations, data and documentation. AERS may supplement Item 11 by adding that AERS shall regularly monitor whether Gastrans d.o.o. complies with the approved methodology, notably whether the tariffs are calculated according to the approved methodology. Gastrans d.o.o. requests that all other elements of Item 11 of the Preliminary Exemption Act should remain unchanged.

As regards the Transportgas Srbija ownership unbundling requirements, Gastrans d.o.o. requests that AERS should specify that the issue is subject to a separate procedure before AERS and that it is to be settled under the separate procedure. In respect of Item 198 of the Opinion, Gastrans d.o.o. requests that AERS should appropriately address the proposals in the Opinion in terms of facilitating counter nominations and cooperation of the national authorities. Finally, Gastrans d.o.o. highlights the need for bringing into line the capacity allocation rules in the Decision, the Preliminary Exemption Act and the Opinion.

Complying with Article 288 paragraph 3 of the Law, the Agency requested in the official letter dated 5 February 2019 that the Ministry of Mining and Energy submit a statement or deliver an opinion concerning the Final Exemption Act.

Acting upon this request, the Ministry of Mining and Energy submitted the official letter No. 011-00-18/2019-01 dated 25 February 2019 to the Agency, noting that the Ministry delivered its opinion by virtue of the Act dated 18 July 2019 published in the 'Official Gazette of the Republic of Serbia' No. 74/18 dated 5 October 2018 together with the Preliminary Act.

V. Explanation of the Disposition of the Act

The Agency has determined the scope and duration of the exemption as well as the conditions under which the exemption is granted, having assessed in a procedure preceding the rendering of this act that the New Interconnector project fulfils the criteria and requirements of the exemption as set out in Article 288 paragraph 1 items 1) - 5) of the Law.

The assessment of the fulfilment of the prescribed requirements for granting the exemption from the third-party access rule, the application of regulated prices and the ownership unbundling obligation under Article 288 paragraph 1 items 1) - 5) of the Law was fully specified by the Agency in Item III of the explanation of the disposition hereof, where the Agency presented in detail the criteria and decisive facts for granting the request per each of the requirements under this Article of the Law, also contained in the explanation of the disposition of the Preliminary Act.

In this item of the explanation of the disposition hereof, the Agency only confirms and refers to all previously determined facts, which, as assessed by the Agency, confirm that the future gas pipeline project fulfils the prescribed requirements that qualify it as a new gas interconnector since it provides cross-border interconnection of adjacent transmission systems, as well as the following prescribed criteria:

- 1) Investment in the New Interconnector enhances competition in the market and the security of supply,
- 2) The risk attached to the investment in the New Interconnector is such that the investment would not take place unless an exemption was granted to GASTRANS d.o.o.,
- 3) The New Interconnector project will be owned by GASTRANS d.o.o. as a legal person operating separately from the existing system operators in the territory of the Republic of Serbia where the new infrastructure will be built,
- 4) Charges will be levied on users of the New Interconnector, and
- 5) The exemption of the New Interconnector will not prevent competition in the natural gas market or have an adverse impact on the efficient functioning of the regulated systems to which it is planned to be connected.

Complying with Article 288 paragraph 13 of the Law and in view of its competences as set out under the Law, the Agency acknowledged the Opinion of the Energy Community Secretariat and its explanations concerning this part to the largest extent possible in the disposition hereof. The following requirements of the Secretariat were implemented in the disposition hereof as specified below.

The Agency accepted the requested percentages for capacity allocation under Items 178-186 of the Opinion of the Energy Community Secretariat and accordingly determined in Item 9 paragraph 1 of the disposition hereof that the EPA Parties (JP SRBIJAGAS Novi Sad and Gazprom Export) may be allocated in priority no more than:

- 70% of the maximum technical capacity at the entry point Zaječar,
- 55% of the maximum technical capacity at the exit points of Paraćin, Pančevo and Gospođinci, and
- 75% of the maximum technical capacity at the exit point Horgoš,

while third parties may be allocated at this entry point and all exit points:

- 20% of the maximum technical capacity - Zaječar, 35% of the maximum technical capacity - Paraćin, Pančevo and Gospođinci, and 15% of the maximum technical capacity - Horgoš, provided that a minimum of 10% of the maximum technical capacity must be reserved for short-term allocation.

Item 176 of the Opinion of the Energy Community Secretariat stipulates that the granted exemption and safeguards must remain unchanged even in the case that GASTRANS decides to change the technical capacity of the project. Item 13 paragraph 3 of the disposition hereof specifies that long-term capacity may not exceed 90% of the maximum technical capacity of the project, i.e. that short-term capacity may not be less than 10% of the maximum technical capacity, which corresponds to the requirement in Items 180, 183 and 186 of the Opinion of the Energy Community Secretariat. The Agency stipulated in Item 13. 3. of the disposition of the Act that the capacity ratio must remain unchanged even in the case of a change in the technical design or technical capacity of the project.

In Item 12 of the disposition hereof, the Agency specified that the non-exempted part of the capacity is subject to the binding rules of regulated third-party access that GASTRANS will lay down in the rules governing the operation of the transmission system in accordance with the Law before the commencement of the operation of the New Interconnector, the content of which rules must correspond to the content of the binding Decision of the Energy Community accepting the obligation to implement the Network Code on Capacity Allocation in Transmission Systems (Decision 2018/06 PHLG) and the Network Code on Transmission Tariff Structures (2018/07/ PHLG), as set out in Items 12 and 13 of the disposition hereof.

Furthermore, in compliance with the Opinion of the Energy Community Secretariat, the Agency also stipulated that auction calendars shall be brought into line and that capacity shall be offered at interconnection points as bundled products and in cooperation with the adjacent transmission system operators through the selected operating platform.

The Agency additionally specified all its competences of monitoring the acts adopted by GASTRANS d.o.o. - adopting network code, price determination methodologies, Compliance Program, an act on requirements for appointing a compliance officer and an act to appoint a candidate by GASTRANS d.o.o. so as to ensure that they can be adopted and amended only with the consent of the Agency.

At the same time, the Agency accepted the Opinion of the Energy Community Secretariat that the validity of the exemption be conditional on permanent fulfilment of all conditions set out in the disposition hereof, to ensure that all conditions will be fulfilled for the entire duration of the exemption. To that end, the Agency specified in the disposition

hereof that failure to fulfil these conditions will affect the outcome of the certification procedure and the validity of this Act, which is to be in effect for 20 years as of the commencement of the operation of the gas pipeline (the Duration of the Exemption).

The Agency also accepted the requirement contained in the Opinion of the Energy Community Secretariat to facilitate reverse flow from Serbia to Bulgaria in case that the security of supply is at risk, as well as to have the reverse commercial capacity at the exit point Horgoš available from the commencement of the operation of the gas pipeline (Item 14 of the disposition hereof).

In the same Item of the disposition hereof, the Agency fully accepted the explanation of the Energy Community Secretariat as to the obligation of GASTRANS d.o.o. to permanently offer all short-term capacity in accordance with the third-party access rules for the entire duration of the exemption.

Moreover, the Agency accepted the Energy Community Secretariat's requirement that GASTRANS should undertake to test market interest in using additional capacity, in full compliance with the rules in the Energy Community's Decision 2018/06 PHLG adapting Article 37 of the CAM Network Code.

With respect to the other stipulations in the Opinion of the Secretariat, the Agency notes that it accepts them in part for the following reasons:

Article 288 paragraph 14 of the Law stipulates that when a final decision of the Agency departs from the opinion of a competent body, the Agency will provide and publish along with its decision the underlying explanation for its decision.

Despite accepting the New Interconnector capacity allocation percentages proposed by the Energy Community Secretariat, the Agency finds it appropriate to introduce minor modifications concerning the capacity allocation conditions to ensure that the construction of the New Interconnector is realised.

The first modification concerns the method of long-term capacity allocation to third parties (non-EPA Parties). The Energy Community Secretariat indicates that the long-term capacity allocation is to be organised by auction on the operating platform in which all interested parties may participate with the exception of Gazprom Export LLC and JP Srbijagas Novi Gas and their related parties.

The Agency assessed that the long-term capacity is to be allocated by applying the 'willingness to pay' principle instead of an auction and that only the parties having submitted a non-binding bid for capacities and having been registered with GASTRANS d.o.o. may take part in the binding phase of the long-term capacity allocation.

The Agency made this modification in view of the following:

1) The 'Open Season' procedure has been a common way of testing market interest in gas pipeline - interconnector capacity and allocating capacity in the EU states in the region in the last few years. The 'Open Season' procedure has been applied in the case of the Hungary-Slovakia, Hungary-Austria, Hungary-Romania, Hungary-Croatia and Greece-Bulgaria interconnectors. If capacity requests are higher than the capacity offered within an 'Open Season' procedure, capacity is allocated according to the 'willingness to pay' principle and not by auction;

2) The alternative capacity allocation procedure, defined in the NC CAM, also makes it possible to allocate capacity according to the 'willingness to pay' principle and not by auction. The alternative capacity allocation procedure and the 'willingness to pay' principle were used in the capacity allocation for incremental capacity between Hungary, Slovakia and Austria and also in the Bulgartransgaz capacity allocation for the interconnection point Bulgaria-Serbia in 2018 and 2019;

3) Binding capacity requests for the interconnection point Bulgaria-Serbia with Bulgartransgaz were lower than the capacity offered. GASTRANS d.o.o. plans to offer the same capacity for the interconnection point Bulgaria-Serbia on the Serbian side. If the capacity requests for the interconnection point Bulgaria-Serbia on the Serbian side are lower than the capacity offered, as was the case with Bulgartransgaz, which is only logical, all binding capacity requests will be met. In that case, all requested capacity will be contracted, so it is completely irrelevant whether the allocation method when the requests are higher than the capacity offered involves the 'willingness to pay' principle or auction;

4) GASTRANS d.o.o. is still a project company that does not have an operating capacity allocation platform. It is not logical, there is not enough time for GASTRANS d.o.o. to purchase or borrow the service of using an operating platform for the allocation of long-term capacity, and has not been common practice for the transmission system

operators in the neighbouring EU states to do so, either. In the event of construction of the gas pipeline, this act imposes an obligation on GASTRANS d.o.o. to purchase an operating platform and allocate capacity by auction. It is emphasised that an auction would not make sense at the moment given the fact that capacity allocation on the upstream gas pipeline in Bulgaria had already finished before this Act was adopted;

5) GASTRANS d.o.o. will organise the testing of market interest in the gas pipeline capacity and capacity allocation in two phases - non-binding and binding, which is in accordance with the 'Open Season' procedure. On 5 March 2018, GASTRANS d.o.o. issued an invitation to all interested parties to submit non-binding bids for capacity in the 'Official Gazette of the Republic of Serbia' No. 16/2018, on the website of GASTRANS d.o.o. and in the magazine 'World Pipelines'. Non-binding bids were submitted by 10 companies. All interested parties were able to take part in the non-binding phase and considerable interest was shown in the gas pipeline capacity and the gas pipeline exits to Serbia and to Hungary. Therefore, any interested parties that took part in the non-binding phase and that registered with GASTRANS d.o.o. may take part in the binding phase, and

6) Given that the Bulgartransgaz capacity allocation is finished, it is logical that the parties that took part in the Bulgartransgaz capacity allocation or the parties having in place a contract for the purchase of natural gas on the Bulgarian-Serbian border from the parties to whom the Bulgartransgaz capacity at the Bulgarian-Serbian border were allocated take part in the binding phase of GASTRANS d.o.o. capacity allocation.

The Agency is of the opinion that capacity allocation in Phase 2 should be for the entire duration of the exemption, instead of for a period of 3 years, as proposed by the Energy Community Secretariat - the Agency assessed that in this phase it is possible to request capacity for periods shorter than the exemption and finds that GASTRANS d.o.o. may reduce the gas pipeline capacity if interest in long-term capacity is under 90% of the maximum technical capacity, the gas pipeline capacity being such as to allow that minimum 10% of the maximum technical capacity be offered for allocation at auctions as short-term capacity, that GASTRANS d.o.o. base the adjusting of the technical design and the technical capacity of the New Interconnector on the results of the binding phase of the market test, taking into account bids for a period shorter than the duration of the exemption.

The Agency made this modification in view of the following:

1) The Agency accepted the maximum percentages of the capacity that may be allocated in priority to the EPA Parties as referred to in the Opinion of the Energy Community Secretariat. However, if third parties do not show interest in a long-term booking of the gas pipeline capacity, or if the interest is very low, only about 70% of the maximum technical capacity of the gas pipeline will be booked on the long-term basis following Phase 1.

2) A long-term booking of capacity of 55% of the maximum technical capacity of the gas pipeline for exits to Serbia would significantly increase tariffs for the use of the gas pipeline for exits to Serbia that should be paid by final customers in Serbia.

3) A long-term booking of capacity of 75% of the maximum technical capacity of the gas pipeline for the exit to Hungary would increase the tariffs for the use of the gas pipeline for the exit to Hungary, which could make the gas pipeline non-competitive compared to other gas pipelines by which natural gas may be delivered to Hungary. It may be concluded that a long-term booking of capacity of 70% of the maximum technical capacity of the gas pipeline at the entry point and 55% and 75% of the maximum technical capacity of the gas pipeline at the exit points cannot ensure the bankability of the project, which may put the implementation of the project at risk, as assessed by the Agency. One should also take into account that the construction of the GASTRANS d.o.o. gas pipeline is a commercial project without substantial EU and budget funding, in contrast to the projects of the Greece-Bulgaria interconnector and the LNG Terminal Krk, where EU funding and Bulgaria and Croatia budget funding will cover a substantial part of the investment. It is therefore necessary to facilitate, within Phase 2, long-term allocation of capacity not allocated to third parties in Phase 1 in order to increase the utilisation of the gas pipeline and, by extension, ensure the bankability of the project.

4) The Agency assessed that minimum 10% of the maximum technical capacity of the gas pipeline at the entry point and at the exit points must be available for short-term capacity contracting. In 'Open Season' procedures, it is common to leave 10% of the maximum technical capacity of the gas pipeline for short-term contracting, while 90% of the maximum technical capacity is allocated on the long-term basis.

5) The alternative capacity allocation procedure, defined in the NC CAM, also makes it possible to allocate 90% of the maximum technical capacity on the long-term basis and 10% on the short-term basis.

The Agency accepted the position of the Energy Community Secretariat that interruptible backhaul capacity be available as of the commencement of the operation of the New Interconnector.

In Item 6.7.5. of its Statement, GASTRANS d.o.o. finds it not viable for the interruptible backhaul capacity to be available as of the commencement of the operation of the New Interconnector, proposing that the obligation be imposed "as soon as reasonably practicable". In Item 6.7.6. of its Statement, GASTRANS d.o.o. finds that close-to-zero tariffs for the interruptible backhaul from Hungary to Serbia and from Serbia to Bulgaria will result in the natural gas available in the Hungarian market being sold in the Serbian or Bulgarian market without transmission costs, which would put gas shippers in the Serbian and Bulgarian market at a much greater disadvantage. Paying a backhaul transmission tariff would make it possible to reduce overall tariffs for the use of the New Interconnector. GASTRANS d.o.o. remains of the opinion that the backhaul capacity tariff should be set in the value of 90% of the tariff for the firm capacity in the direction of the physical flow of natural gas.

The Agency notes that the Network Code on Harmonised Transmission Tariff Structures for Gas (Regulation (EU) No. 2017/460) did not stipulate the method of calculation or the permitted range for the percentage to be used to calculate interruptible backhaul tariffs. The assessments of the percentage to be used to calculate backhaul tariffs contained in the Opinion of the Energy Community Secretariat and the Statement of GASTRANS d.o.o. are completely opposite, so the Agency used the methods of comparison to evaluate the solutions applied by the transmission system operators with which the New Interconnector is to connect and whose system characteristics and gas markets resemble the Serbian market.

As specified on the Bulgartransgaz website, interruptible capacity tariffs in the direction of the physical flow of natural gas amount to 90% of firm capacity tariffs, but interruptible backhaul tariffs are not specified. Based on the information on the FGSZ website, this transmission system operator does not offer interruptible backhaul capacity for the physical flow of natural gas either in the direction Ukraine-Hungary, Hungary-Ukraine, Hungary-Romania, Romania-Hungary, Hungary-Croatia, Croatia-Hungary or Hungary-Serbia. FGSZ has interruptible backhaul capacity tariffs for:

- 1) Domestic exits and they amount to 189.4 % of tariffs for the physical flow of natural gas;
- 2) Natural gas production entries and they amount to 52.8 % of tariffs for the physical flow of natural gas;
- 3) Interconnection with Austria, where backhaul tariffs amount to 513.39 HUF/kWh/h/per year, which amounts to 47.5% of the tariff for the physical flow of natural gas in the direction Austria-Hungary, which is 1080.48 HUF/kWh/h/per year.

FGSZ has an approach of not facilitating interruptible backhaul at interconnection points where physical flow in both directions but not simultaneously is possible. The physical flow of natural gas from Hungary to Serbia is possible at the interconnection point of Horgoš, while the construction of the New Interconnector will make the flow of natural gas from Serbia to Hungary possible. If one were to adopt the FGSZ approach, it would not be necessary to introduce interruptible backhaul for the New Interconnector at the interconnection point of Horgoš.

Taking all the above into account, the Agency establishes that interruptible backhaul capacity tariffs at all entry/exit points of the New Interconnector amount to 47.5% of the tariffs for the physical flow of natural gas in the direction from Hungary to Serbia and from Serbia to Bulgaria.

Items 187-188 of the Opinion of the Secretariat stipulate that as from COD, the shareholders of Gastrans and their affiliates shall be obliged to offer each quarter a volume equivalent to 30% of the volume of their total natural gas sales in the corresponding quarter of the previous year in Serbia - regardless of the point of entry into the Serbian domestic transmission system - in an independent organised market place e.g. SEEPEX. The delivery point of the offered gas shall be the Virtual Trading Point (VTP) in Serbia. The Energy Community Secretariat also notes in this opinion that the affiliates' offer price of natural gas shall not be higher than the price defined in the long-term contract. In the absence of demand from third parties, the offered volumes shall remain in the ownership of the undertaking which offered it. In addition, it is stipulated that at the end of each quarter the shareholders of GASTRANS d.o.o. shall submit a report to AERS about the volumes of natural gas sold by them and their affiliates in Serbia and the volumes of gas they offered in the organised market place.

The Agency understands that this market liquidity measure is an issue that may be decided by the Republic of Serbia authorities in charge of protection of competition in the market, given that Article 57 paragraphs 3 and 4 of the Law authorises the Agency to examine the circumstances, collect information about the functioning of the market and decide on the enhancement of effective competition only in cooperation with the authority in charge of competition and the authorities in charge of financial market oversight.

Apart from the Agency's lack of competence under the substantive legislation (the Energy Law) with regard to performing duties and imposing safeguards to establish the liquidity of market and the protection of competition, which duties fall outside its scope of work being an energy regulator, the Agency emphasises that in an administrative matter such as granting an exemption this procedure is instituted following a request of a party (GASTRANS d.o.o.) and a decision on this request is taken in accordance with the substantive legislation and the Law on General Administrative Procedure. In this respect, the Agency was mindful of the fact that there are no grounds in the substantive legislation or in procedural law allowing it to impose special measures on the entities that are not parties to the procedure in which the administrative matter of granting an exemption is being decided. As the Agency's competences with respect to the protection of competition and the protection of liquidity of an unregulated and free market in natural gas are limited and conditional on its cooperation with the competent competition protection and financial market oversight authorities, the Agency, acknowledging the assessments of the Energy Community Secretariat, shall, complying with the Energy Law, provide the guarantees in this procedure that will make it possible for the competitors in the market to have a non-discriminatory approach to the New Interconnector but also the conditions ensuring that the new system operator operates and engages in its core activity according to the principles of non-discrimination, which will also have an indirect effect on providing the necessary prerequisites for enhancing competition in the free market in natural gas.

As the Agency, under Article 57 paragraph 3 of the Energy Law decides on the implementation of required and appropriate measures for enhancing effective competition in cooperation with the authorities in charge of competition and financial market oversight (Article 57 paragraph 4 of the Law), the actions taken by this Agency are conditional on cooperation with the Commission for the Protection of Competition. In view of the fact that the Agency's prescribed competences are not sufficient to allow it to impose safeguards on the entities operating in the free market as well as that under procedural law there are no grounds for the Agency to impose measures on the entities that are not parties to this administrative procedure, the Agency does not specify herein the safeguards as stipulated by the Energy Community Secretariat concerning the protection of competition and the liquidity of market (within the meaning of the obligation of the Affiliates to sell natural gas in the organised market place in a volume equivalent to 30% of the volume of their total natural gas sales in the previous year) as it would thereby exceed its statutory competences. Given that the protection of competition in the market falls within the scope of work of the Commission for the Protection of Competition, under a special law and under Article 57 paragraph 4 of the Law, this Act is therefore also submitted to the Commission for the Protection of Competition for information and further competent action, with which Commission the Agency will cooperate within its competences as referred to in Article 57 paragraphs 3 and 4 of the Law.

It is emphasised that regulators impose measures for the protection of market liquidity on the entities that are active in the market and that are holders of a natural gas supply licence. However, Gazprom Export, being a subsidiary of the ultimate owner, does not have a subsidiary in the Republic of Serbia at the moment or a natural gas supply licence, nor does it operate in the gas market of the Republic of Serbia at the moment.

In accordance with Article 57 paragraphs 3 and 4 of the Law, the Agency complied with the requirements of the Energy Community Secretariat to impose the market liquidity measure within its competences when in Item 19 of the disposition of the Exemption Act the Agency imposed an obligation on GASTRANS d.o.o. for the duration of the exemption in the network code to determine a virtual point for the place of natural gas handover where natural gas trade shall be done between market participants, including the trade of the volumes contracted in the organised market of the independent market operator in the Republic of Serbia. In paragraph 2 of this Item of the disposition, the Agency imposed an obligation on GASTRANS d.o.o. to provide, for the duration of the exemption, on the request of the Agency,

in accordance with the applicable law, requested data for the purpose of performing the Agency's competences, including the data required for the monitoring of competition in the gas market of the Republic of Serbia.

In view of the fact that there are no grounds under procedural law for the Agency to set out in this administrative decision the obligation of legal and functional unbundling of the system operator Transportgas Srbija d.o.o. from the vertically integrated company JP Srbijagas Novi Sad as these two entities are not parties to the procedure, this explanation merely reflects that the statutory obligation of legal and functional unbundling of this system operator from JP Srbijagas Novi Sad is set out in the Energy Law as well as a deadline for discharging it, including the obligation of Transportgas Srbija d.o.o. to get certified as a system operator following the unbundling. As the statutory obligation of legal and functional unbundling of Transportgas Srbija from JP Srbijagas as a vertically integrated company as referred to in Article 224 of the Law and this operator's certification obligation were not discharged even after the expiry of the statutory deadline, the Agency states in this procedure that the obligation is set out under the Law and that this statutory obligation shall be discharged directly by the public company, while the application of the Energy Law in this respect shall be ensured by the Government of the Republic of Serbia, with the monitoring of the competent ministry. For this reason, the Agency understands that in accordance with the Opinion of the Energy Community Secretariat this public company and the competent authorities of the Republic of Serbia will take all necessary measures to ensure that the obligations set out by the Law are discharged, which would also ensure the implementation of the measures in the Opinion of the Energy Community Secretariat concerning the legal and functional unbundling of Transportgas Srbija d.o.o., before the commencement of the operation of the New Interconnector.

Based on the above, acting upon the submitted request in accordance with the competences under Article 288 paragraph 14 of the Energy Law, it has been determined that the conditions have been met to grant an exemption from Article 288 paragraph 1 of the Law, so the Council of the Energy Agency of the Republic of Serbia, under the provision of Article 136 of the Law on General Administrative Procedure, decided as stated in the disposition hereof at the 6th extraordinary session of 5 March 2019.

Legal Remedy:

This Act is final in the administrative procedure and an administrative lawsuit may be brought against it by filing a clawsuits with the Administrative Court of Serbia within 30 days of receiving the Act. The lawsuits shall be filed with the court in person or by mail in two copies.

Distribution List:

- Proxies of GASTRANS d.o.o. Novi Sad,
Jelena Gazivoda and Nikola Đorđević, attorneys-at-law from Belgrade
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CHAIRMAN OF THE COUNCIL

L.S.

Dejan Popović (p.m.)