

ENERGY AGENCY
OF REPUBLIC OF SERBIA
No: 40/2018-D-03
Date: October 1st, 2018
Belgrade, Terazije 5/V

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 the attorney Jelena Gazivoda and Nikola Đorđević, being 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 288 paragraph 3 and Article 51 paragraph 2 item 3) and Article 39 paragraph 1 of the Energy law ("Official Gazette of the Republic of Serbia", No. 145/14), Article 136 of the Law on General Administrative Procedure ("Official Gazette of the Republic of Serbia", No. 18/16), having obtained an opinion of the Ministry of Mining and Energy of the Republic of Serbia pursuant to Article 288 paragraph 3 of the Law, and before obtaining the opinion of the Energy Community Secretariat referred to in Article 288 paragraph 12 of the Law on 2nd, extraordinary session held on October 1st, 2018, renders the following decision

ACT
on 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 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 (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 Act refers to entire future gas interconnector for the transmission of natural gas with a technical capacity of 13.88 bcm annually in accordance with expected technical design of the future gas interconnector (hereinafter referred to as: “**maximum technical annual capacity**”), which may have a lower capacity according to conditions defined in below Item 8, 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 transmission systems in the Republic of Bulgaria and Hungary, including related equipment for connection with the adjacent systems (hereinafter referred to as: “**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:

- 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 Act shall apply also in the case GASTRANS d.o.o. changes key technical parameters of the New Interconnector, on which changes GASTRANS d.o.o shall inform Agency.

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 production or natural gas supply, so 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, 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 production or supply of natural gas;

3) a company may appoint members of any board or bodies legally representing GASTRANS d.o.o. and simultaneously, directly or indirectly, to exercise control or have any right over an undertaking performing the activity of production or supply of natural gas, and

4) a member of the board or bodies legally representing the company or any related company performing the activity of production or supply of natural gas can simultaneously be a member of the board or bodies legally representing GASTRANS d.o.o.

Commercially sensitive information held by GASTRANS d.o.o., or by its staff cannot be made available to undertakings performing the activity of production and supply.

Item 4

IT IS REQUESTED FROM GASTRANS d.o.o. that it, prior to announcement of the 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-Д-03/42 dated 3. September 2018 (hereinafter referred to as: **“the Decision”**):

1) adopts the compliance program approved by the Agency;

2) submit to the Agency for approval the proposal for appointment of a compliance officer being either personal or legal entity;

3) appoint an *ad hoc* body to receive objections from bidders that relate to 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 natural gas supply (hereinafter collectively referred to as: **“Related parties”**).

Item 5

IT IS REQUESTED FROM GASTRANS d.o.o. to determine in its compliance program (hereinafter referred to as: **“the Compliance program”**):

1) measures to prevent discriminatory treatment of GASTRANS d.o.o. against service users, taking into account the Scope of exemption;

2) measures that provide permanent protection against access to commercially sensitive data of users of all services and protection of disclosure of these unaggregated data to Related parties;

3) the authorization of the compliance officer, particularly:

- rights and obligations 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 Compliance program and its objectives, without prior notice;
- monitoring the method of realization 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 transport and management of the transmission system;
- monitoring of the non-discrimination and adequacy of the performance of work by employees in the performance of economic, financial, legal and technical works in accordance with the conditions under the Compliance program;

4) the obligation of the compliance officer to submit an annual report to the Agency on the undertaken measures for the implementation of the Compliance program and significant breaches of the Compliance program in this period;

5) submission of annual reports of the compliance officer on monitoring of implementation of the Compliance program to all managing bodies with the recommendation for its application, and

6) the conditions under which Related parties may provide services to GASTRANS d.o.o., apart from the activities related to the crediting and realization of the construction and maintenance of the New Interconnector.

Item 6

GASTRANS d.o.o. IS OBLIGED TO prior the announcement of the invitation for the capacity allocation pursuant to the Decision and during the exemption:

1) determine more closely the conditions for appointing of 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 parties, directly or indirectly, nor that it has such an appointment, interest or responsibility, directly or indirectly, in previous 3 years;

- 2) determine 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;
- 3) to submit to the Agency for approval, acts with the conditions from sub-point 1) and 2), at the latest with the proposal for appointment of compliance officer, and
- 4) appoint a compliance officer, provided that for the proposal of its appointment, GASTRANS d.o.o. has obtained the prior approval of the Agency.

Item 7

GASTRANS d.o.o. IS OBLIGED TO, at latest from the date of the start of commercial operations of the New Interconnector, and for the Duration of the exemption to:

- 1) possess the necessary financial, material and technical means for the performance of transmission activities, including independent information systems, equipment, premises, information protection systems from the Related Parties;
- 2) have a sufficient number of employees who independently perform legal, economic, technical and other duties, as well as duties related to information technology;
- 3) have separate and different premises from the Related Parties;
- 4) implement recommendations of the compliance officer, and
- 5) to the extent it wouldn't conflict with the Scope of exemption, to independently conduct business operations and to operate the New Interconnector and be organized separately from the Related Parties.

Exemption from the third party access

Item 8

IT IS APPROVED TO GASTRANS d.o.o. the exemption from the obligation to apply the principles of the third party access specified in the Article 283 paragraph 1 of the Law, so that the capacity of the New Interconnector is allocated in accordance with this Item 8.

The capacity of the New Interconnector shall be allocated in accordance with this Act and the Decision.

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: "**Priority Capacity**"), for a period not exceeding the Duration of the exemption, to the companies Gazprom export LLC and JP Srbijagas (hereinafter: "**EPA Parties**").

Up to the remaining 12 % of the maximum technical annual capacity of the New Interconnector may be allocated in accordance with the Decision, and contracted to companies other than the EPA Parties that submitted non-binding bids upon Public invitation of GASTRANS d.o.o. dated March 5, 2018, for a period not exceeding the Duration of the exemption.

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 remaining 10% of the capacity of the New Interconnector shall be allocated as the short-term capacity of the New Interconnector on 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 Duration of exemption.

If GASTRANS d.o.o. does not adjust the technical design and technical capacity:

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

Unless otherwise agreed with adjacent TSOs, allocation of short term capacity shall be conducted by applying the auction method, for the entire Duration of the exemption. The reserve (initial) price at the auction is determined according to the applicable tariffs for the exempted long term capacity of the New Interconnector at the entry and exits, which prices are determined in accordance with the GASTRANS d.o.o.'s methodology determining the prices of long-term natural gas transmission services in accordance with Item 12 of disposition of this Act.

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 the Article 250 of the Law.

Item 9

IT IS APPROVED TO GASTRANS d.o.o. the exemption from the obligation to:

- 1) approve 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 transportation service in accordance with item 8 of disposition of this Act;
- 2) procure non-discriminatory access to the transportation system determined by Article 247 of the Law, so that GASTRANS d.o.o. is entitled to procure access to the New Interconnector in accordance with item 8 of 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 procure access to the New Interconnector in accordance with item 8 of 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 will regulate 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 item 13) and 15) and Article 254 paragraph 1 item 17) and item 18) of the Law, except from publishing reserve (initial) price for short term capacity;
- 6) keep records set out in Article 248 paragraph 1 item 17) of the Law;
- 7) apply the balancing rules, as implemented 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 transportation 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 transportation agreement) which contain elements prescribed by the Article 284 of the Law and network code in relation to Article 53 paragraph 1 item 4) of the Law, so that GASTRANS d.o.o. is entitled to execute the gas transportation agreements, and to enact the network code complying with this Act, which shall be subject to approval of the Agency.

It is approved to GASTRANS d.o.o. the exemption from the application of the following prescribed obligations and principles resulting from the change in law in the Republic of Serbia, within the Duration of the exemption:

- 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 requirement to conduct in regular intervals market demand assessments and design phases for incremental capacity in the New Interconnector or to develop project proposals for incremental capacity projects;
- 4) 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;
- 5) obligation to implement standardized rules on third party trade nominations;
- 6) obligation to implement standardized rules on daily imbalance price formulation or determination and quantity calculation;
- 7) obligation to implement requirements of, and principles for neutrality of cash flows for system balancing actions;
- 8) obligation to implement standardized rules on credit risk management for taking or procuring balancing actions;
- 9) obligation to implement requirements to conduct a cost benefit analysis assessment for balancing actions taken, and
- 10) obligations in relation to the regulation and standardization of rules on linepack flexibility services and on interim measures.

Item 10

GASTRANS d.o.o. IS OBLIGED TO determine the terms of the long-term natural gas transmission (model of the agreement), and a network code, in accordance with the Scope of the exemption granted under this Act and which contain the following:

- 1) right of the user to the "secondary trade" of capacities (the assignment of long-term and short-term transmission agreements to third party, as well as the right to amend the long-term agreement in favor 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, three gas months 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) right to limit the scope of announced quantities for transmission in case of overload, system jeopardizing;
- 5) right 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) obligation 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) obligation to cooperate with the adjacent operators to which systems New interconnector is connected;
- 8) obligation to comply with the transparency rules, except in the part specified in item 9 paragraph 1, point 5) of disposition of this Act.

GASTRANS d.o.o. shall apply equally the network code for the purpose of realization of the long term and short term gas transportation agreement in accordance with the above item 8 of disposition of this Act.

The agreement on short-term natural gas transmission shall be based on the principles of the agreement on long-term natural gas transmission applicable after the commercial operation date.

In case of contractual congestion, GASTRANS d.o.o. is obliged to offer unused capacity day ahead on an interruptible basis.

GASTRANS d.o.o. IS OBLIGED TO keep records of transactions and submit data on request to the Agency for the purpose of performing tasks within its competence.

Exemption from the application of regulated prices

Item 11

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, and Article 50 paragraph 1 item 6) and Article 248 paragraph 1 item 10) of the Law.

GASTRANS d.o.o. shall determine the prices for access to the transportation system which are expressed in tariffs, in line with the Tariff methodology set out by GASTRANS d.o.o. in accordance with the principles set out in Item 12 of this Act.

It is approved to GASTRANS d.o.o. the exemption from the application of the following prescribed obligations and principles resulting from the change in law in the Republic of Serbia within 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 revenue ;
- 5) application of the standardized rules on pricing of bundled capacity;
- 6) application of the standardized rules on pricing at virtual point;
- 7) application of the standardized rules on tariff clearing price calculation;
- 8) requirements to consult with network users and adjoining network operators on tariff setting,
and
- 9) application of the standardized rules on pricing of the incremental capacity.

Item 12

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 use 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 Tariffs for all exits in the Republic of Serbia.

The necessary income for all years during which exit Horgoš is fully operational for the entire 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 increase or decrease according to Tariff 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 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 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 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 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 manner, procedure and deadlines for bookkeeping records, separating accounts by business activities and submitting data and documentation for the purpose of regulation.

Item 13

All rights determined by this Act are granted under the condition 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.

Item 14

GASTRANS d.o.o. may propose amendments of the Compliance program, gas transmission agreement, network code and Tariff methodology by notification to the compliance officer. The compliance officer shall evaluate the amendments to determine compliance thereof with the Scope of Exemption and shall notify the Agency of its evaluation within 5 working days of receipt of the proposal of the amendments and forwards to the Agency proposal of amendments. The Agency, taking into account the compliance officer's evaluation, shall check the compliance of the amendments with the Scope of Exemption. In case of compliance the Agency shall approve the amendments within 5 working days of receipt of the proposed amendments.

In case the Agency rejects proposed amendments the reasons shall be substantiated, whereby the approval shall not be unreasonably withheld. If the Agency does not provide the response within 5 working days, the approval is deemed provided.

Tariffs adjustment pursuant to item 12 of disposition of this Act, is not subject to approval of the Agency.

Item 15

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 16

All rights determined in this Act shall cease if GASTRANS d.o.o. does not commence construction works in relation to the New Interconnector within 2 years of the date of the final act on exemption in respect of the New Interconnector, and does not put the New Interconnector into operation within 5 years of the date of the final act on exemption.

Item 17

In the procedure of certification of GASTRANS d.o.o. which the Agency shall conduct before the start of operation of the New Interconnector, the Agency shall assess the fulfilment of conditions set out in this Act, during which procedure the conditions from Article 224, 225, 245 and 246 of the Law shall be considered as fulfilled.

Item 18

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 protected version of this Act, which does not include commercial and other confidential business data, as well as opinion of the Ministry of Mining and Energy, shall be published in the "Official Gazette of the Republic of Serbia" and on website of the Agency.

Item 19

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 b].

Item 20

This Act together with other documents stipulated by Article 288 paragraph 10 of the Law shall be submitted to the Secretariat of the Energy Community which is to provide its opinion, after which Agency shall adopt its final decision on GASTRANS d.o.o. exemption request.

Explanation

GASTRANS d.o.o. Novi Sad, with a business seat in Novi Sad, Narodnog fronta 12, company number 20785683 TIN 107350223, filed on February 2 2018, through the attorneys Jelena Gazivoda and Nikola Đorđević, lawyers from Belgrade, request for exemption of GASTRANS d.o.o. from the obligation of ownership unbundling referred to in Article 224 of the Law and for the exemption 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, detailed as follows:

In accordance with Article 288 paragraph 1 of the Law implementing Article 36(1) of Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (hereinafter referred to as: "**Gas Directive**") as implemented into the Energy Community by Decision 2011/02/MC-EnC (hereinafter referred to as: "**Implementing Decision**"), GASTRANS d.o.o. has requested full (100%) exemption for the period of 25 years, from:

- (i) the obligation to unbundle the transmission system owner pursuant to Article 224 of the Law implementing Article 9 of the Gas Directive as implemented into the Energy Community by the Implementing Decision;
- (ii) the obligation to offer access to the transmission system to third parties pursuant to Article 283 paragraph 1 of the Law implementing Article 32 of the Gas Directive as implemented into the Energy Community by the Implementing Decision which also assumes that:
 - a. the obligation to have its methodologies to calculate or establish the terms and conditions to (i) the connection and access to national networks, (ii) the provision of balancing services, and (iii) access to cross-border infrastructures shall not be subject to the fixing or approval by the Agency, which corresponds to the exemption from the Article 41 paragraph 6 of the Gas Directive as implemented into the Energy Community by the Implementing Decision;
 - b. the obligation to have its tariffs or methodologies and the balancing service shall not be subject to the fixing or approval by the Agency, which corresponds to the exemption from the Article 41 paragraph 8 of the Gas Directive as implemented into the Energy Community by the Implementing Decision;
 - c. the obligation to have its terms and conditions, which include tariffs and methodologies, shall not be subject to modification by the Agency, to ensure that they are proportionate and applied in a non-discriminatory manner if deemed necessary by the Agency, which corresponds to the exemption

from the Article 41 paragraph 10 of the Gas Directive as implemented into the Energy Community by the Implementing Decision; and

d. the 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 Energy Community by the Implementing Decision shall not be applicable to the Project, which is in line with the Article 30 item (b) of such Regulation as implemented into the Energy Community by the Implementing Decision .

In the initial request for exemption dated 2 February 2018 (hereinafter referred to as: “**Initial request**”), GASTRANS d.o.o. provided its corporate data including shareholders structure, and the list of other energy undertakings in the Republic of Serbia related to GASTRANS d.o.o. It also provided an overview the current development of the natural gas sector in the Republic of Serbia, the project details and GASTRANS d.o.o. view on compliance thereof with the strategic goals of the Republic of Serbia and legal grounds for submission of the Initial request.

The Initial request contains a separate request of GASTRANS d.o.o. that the Agency determines 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 contains the request of GASTRANS d.o.o. for the protection of confidential information in line with Article 57, paragraph 7 of the Law.

Attached to the Initial request, GASTRANS d.o.o. enclosed an excerpt on the registration of GASTRANS d.o.o., issued by the Business Register Agency on 31 January 2018, the power of attorney for Jelena Gazivoda and Nikola Đorđević from Belgrade dated 31 January 2018 and [...¹.]

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 pipeline which will run through the Republic of Serbia and connect to the Hungarian and Bulgarian national transmission systems (the Project);
- the envisioned Project assumes the construction of the new gas pipeline infrastructure on the territory of the Republic of Serbia for the purpose of transmission of natural gas from the entry point to the exit points, with a design pressure of 7,4 MPa and maximum allowed operating pressure (MAOP) of 6,6 MPa on the borders, which assumes (preliminary estimations) maximum annual flow of thirteen point eighty eight billion (13,880,000,000) m³ on entry point. [...];
- the realization of investment in the new infrastructure is possible only if the Agency grants the full exemption for a period of 25 years from ownership unbundling requirements 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;

¹ text in brackets containing commercially sensitive data erased

- the Project is in alignment with the strategic goals and priority actions set out in the Strategy of the development of energy sector 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**”) as, if constructed, the pipeline would provide for a new direction of supply and for the establishment of interconnections with Bulgarian and Hungarian national transmission systems (NTS);
- the Project (i) fulfils the requirements of the Strategy, (ii) does not conflict with the other projects envisaged by the Program of realization of the Strategy of development of energy sector 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 (iii) represents a unique opportunity to connect the Serbian NTS with the Bulgarian NTS and Hungarian NTS via one pipeline. As such, 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), according to the data and projection that GASTRANS d.o.o. has at its disposal, the increase of demand for natural gas is expected, which must be secured from imports as domestic gas production is constantly decreasing. Pointing out that in the Republic of Serbia at this time projects are not realized by the competent operators nor third parties are interested in investing in alternative routes or sources of supply, GASTRANS d.o.o. in the request emphasizes that, due to the such state of natural gas sector in the Republic of Serbia, it would be interested in the construction and, as owner, operation of 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 specifically as follows: (i) the development of domestic natural gas market, (ii) the guarantee of long-term security and the stability of natural gas supply, (iii) the connection of the natural gas transmission system of the Republic of Serbia with the Bulgarian NTS and the Hungarian NTS, (iv) the diversification of sources and streams/directions of supply, (v) the obtaining of modern transmission system of natural gas, (vi) the possibility of having reverse flow on the new transmission system of natural gas; and (vii) ensuring the capacity to meet increased demand for natural gas in the Republic of Serbia. In addition, supplementary benefits for the Republic of Serbia are the 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;
- the transport system operators in the neighboring countries - BULGARTRANGAZ EAD and FGSZ - are planning to upgrade the existing natural gas transportation system by the construction of new sections 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 GASTRANS d.o.o. project would enable the connection of the natural gas market in the Republic of Serbia with the Bulgarian market and with the Hungarian market, and, at the same time, be the first interconnection connecting the gas markets of the two countries of the EU, Hungary and the Republic of Bulgaria, via the route of the gas pipeline in the Republic of Serbia.

In the Initial request, GASTRANS d.o.o. has described a new infrastructure facility as a gas interconnector whose route over the territory of the Republic of Serbia is about 400 km, and which crosses the state border of the Republic of Serbia and has the entry point near the city of Zaječar, three exit points on the territory of Republic of Serbia (Paraćin, Pančevo, Gospođinci), and the fourth exit point, across the border with the Republic Hungary (Horgoš). GASTRANS d.o.o. furthermore stated, that this gas pipeline interconnector shall cross the state border of Republic of Serbia to connect to the future gas pipelines to be built by the neighboring operators of Hungary and the Republic of Bulgaria.

GASTRANS d.o.o. has also stated that the preliminary discussions with the neighboring operators BULGARTRANGASZ EAD and FGSZ started with 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, implies the projected pressure at the entry and the exit points of 7.4 MPa, the maximum allowed operational pressure of 6.6 MPa, and the maximum annual flow of the interconnector of 13.8 billion m³ of natural gas.

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 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 (under Article 283 paragraph 1 of the Law) under the following conditions:

- 1) the investment must enhance competition in gas supply and enhance security of supply;
- 2) the level of risk attached to the investment must be such that the investment would not take place unless an exemption was granted;
- 3) 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 systems that infrastructure will be built;
- 4) charges must be levied on users of that infrastructure; and
- 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 infrastructure is connected.

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

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

Acting upon the Initial request and GASTRANS d.o.o.'s separate request seeking the Agency to determine the manner and conditions for collecting non-binding bids, the Agency has determined that GASTRANS d.o.o. is entitled to submit a request for an exemption because it is not a system operator but a separate legal entity, separated from the system operators operating on the territory of the Republic of Serbia, where the GASTRANS d.o.o. plans to build a new infrastructure. This is a condition prescribed in Article 288 paragraph 1 Item 3) of the Law, on the basis of which the active legitimacy of GASTRANS d.o.o. is established.

The Agency has also determined, taking into account the characteristics and given the description of the new infrastructure facility from the submitted request, that the request for exemption of the described infrastructure is formally allowed because:

- the request is submitted for the new infrastructure that GASTRANS d.o.o. plans to completely build from the entry point to the final exit point, which makes this facility a completely new infrastructure facility for which it is permitted to request an exemption, in the accordance with the Article 288 paragraph 1 in relation to Article 2 item 46) of the Law,
- it is planned that the future gas pipeline of the described route through the Republic of Serbia simultaneously crosses the state border of the Republic of Serbia with the aim of a cross-border connection with the neighboring transmission systems in Hungary and the Republic of Bulgaria, on which basis the new infrastructure facility for which the request for an exemption is submitted, is an interconnector in accordance with the Article 2 item 25) of the Law for which new gas pipeline facility it is allowed to request an exemption in accordance with Article 288 paragraph 1 of the Law,
- at the same time, the Agency determined that GASTRANS d.o.o. filed a request for exemption for the described interconnector to the Agency, that for a part of the gas pipeline that crosses the border of Republic of Serbia neither GASTRANS d.o.o. nor other legal entity submitted nor intends to submit the request for exemption to the Energy and Public Utility Authority of Hungary (hereinafter referred to as: "**Hungarian NRA**") or Energy and Water Regulatory Commission of the Republic of Bulgaria (hereinafter referred to as: "**Bulgarian NRA**"), and that, in this particular case, the Agency is competent to decide upon the submitted request.

Taking into account the determined facts listed above, and as GASTRANS d.o.o. has, by the submitted letter [...], made the existence of an interest in the use of services on the new interconnector probable, the Agency, on 9 February 2018, in accordance with the best practices of the regulatory bodies of the European Union, adopted the Decision on the manner and deadlines for Market test for use of the future infrastructure facility of the company GASTRANS (hereinafter referred to as: "**the Decision on Market test**"). The Decision on Market test regulates the procedure and deadlines for the Market test for the use of the new infrastructure and the obligation to apply non-discriminatory and transparent rules for the collection of non-binding bids for the use of new capacities, which provide the opportunity for all market participants to specify the desired capacity by submitting the non-binding bids and also to highlight possible additional requests regarding the location, number of entry or exit (delivery points) or transmission direction.

By rendering the Decision on Market test, the Agency adopted the request of GASTRANS d.o.o. from the Initial request for the determination of the rules for the collection of non-binding bids in order to provide evidence confirming the decisive facts about the scope of market interest in the use of the future gas infrastructure, and without which evidences is not possible to decide on the merit of the request for exemption.

Decision on Market test imposed an obligation on GASTRANS d.o.o. to report to the Agency, upon completion of the Market test, on the volume of interest and specific requests of the bidders, and to submit all non-binding bids for inspection as evidence confirming the existence and volume of market interest in the use of the new infrastructure, and on the basis of the obtained results in the Market test to notify the Agency whether it still remains with the submitted request for exemption of 2 February 2018.

In accordance with the Decision on Market test, GASTRANS d.o.o. announced on 5 March 2018 the Public invitation for submission of non-binding bids for booking of 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, as well as TSOs, shareholders of GASTRANS d.o.o. and their subsidiaries and affiliates to submit non-binding bids. Upon Public Invitation, a total of six bidders responded within a deadline, and four more after the expiration of the deadline for submission of bids. GASTRANS d.o.o. informed the Agency about it in its Report on the results of the Market test, which was submitted to the Agency on 30 April 2018 and accompanied with the bids confirming the scope of the expressed interest of the market for the use of the transmission capacities of the New Interconnector.

Evaluating the results obtained by the Market test, GASTRANS d.o.o. has on 29 June 2018 submitted to the Agency, through its attorneys, an addendum of the request for exemption (hereinafter referred to as: "**Addendum**") specifying that the Initial request and the Addendum represent a unified request for the exemption (hereinafter referred to as: "**Request for Exemption**").

In the Addendum GASTRANS d.o.o.:

A) acting in accordance with Article 3, paragraph 1 item point 2) of the Rules of Procedure on conditions for exemption, content of request for exemption and content of an act on exemption ("Official Gazette of the Republic of Serbia", no. 11/2018 dated 9 February 2018, hereinafter referred to as the "**Rules of Procedure**"), as well as in accordance with the Decision on Market test, specified the request for exemption in respect to the scope of exemption, so that it required exemption from:

1. the obligation to organize in accordance with Article 224 paragraph 2 of the Law *i.e.* the obligation to unbundle the transmission system owner pursuant to Article 224 of the Law (with the reference to Article 225 paragraph 1 items 1), 2), 3) and 4) of the Law) implementing Article 9 of the Gas Directive as implemented into the Energy Community by Implementing Decision, in respect of which GASTRANS d.o.o. required a full exemption, as detailed and elaborated in Section 6.3 of the Addendum;
2. the obligation to provide non-discriminatory access to the system, in respect of which GASTRANS d.o.o. required a part exemption as detailed and elaborated in Section 6.1 of the Addendum; and

3. the obligation to apply regulated prices, in respect of which GASTRANS d.o.o. required a full exemption, as detailed and elaborated in Section 6.2 of the Addendum.

Both points 2. and 3. above being in accordance with Article 283, paragraph 1 of the Law *i.e.* the obligation to offer access to the transmission system to third parties pursuant to Article 283 paragraph 1 of the Law implementing Article 32 of the Gas Directive which also assumes that:

- the obligation to have its methodologies to calculate or establish the terms and conditions to (i) the connection and access to national networks, (ii) the provision of balancing services, and (iii) access to cross-border infrastructures shall not be subject to the fixing or approval by the Agency, which corresponds to the exemption from the Article 41 paragraph 6 of the Gas Directive;
- the obligation to have its tariffs or methodologies and the balancing service shall not be subject to the fixing or approval by the Agency, which corresponds to the exemption from the Article 41, paragraph 8 of the Gas Directive;
- the obligation to have its terms and conditions, which include tariffs and methodologies, shall not be subject to modification by the Agency (*i.e.* whereby the Agency, would ensure that such terms and conditions are proportionate and applied in a non-discriminatory manner if deemed necessary by the Agency), which corresponds to the exemption from the Article 41 paragraph 10 of the Gas Directive; and
- the Gas Access Regulation, as implemented into the Energy Community by Implementing Decision shall not be applicable to the Project, which is in line with the Article 30 item b) of such Regulation, as implemented into the Energy Community by the Implementing Decision.

B) acting in accordance with Article 3, paragraph 1 item 3) of the Rules of Procedure, as well as in line with the Decision on Market test, specified the Request for Exemption in respect to the scale of exemption, so that it required that each exemption requested in the above paragraph A) is to relate to the whole new infrastructure *i.e.* the entire New Interconnector and all capacities thereof.

C) acting in accordance with Article 3, paragraph 1 point 4) of the Rules of Procedure, as well as in line with the Decision on Market test, amended the Request for Exemption in respect to the duration of exemption, so that it required that the duration of each exemption requested in the above paragraphs is to be for a period of 20 years from the start of operations of the New Interconnector, instead of a period of 25 years as provided in the Initial request.

The Addendum also contained additional data in accordance with Article 3 of the Rules of Procedure, including information on the change of the ownership structure, so that GAZPROM TRANSGAZ KRASNODAR has become a direct shareholder of South Stream Serbia AG Switzerland (hereinafter referred to as: **“SOUTH STREAM AG”**) instead of PAO GAZPROM (hereinafter referred to as: **“GAZPROM”**).

The Addendum provided additional details on the Project, elaboration that the Project pipeline qualifies as new interconnector (under Law, the Gas Directive and the Implementing Decision), the market overview, the market study and the market test results, the scope of exemption sought and justification on the fulfillment of the criteria stipulated in Article 288 paragraph 1 points 1)-5) of the Law.

In the Addendum, GASTRANS d.o.o. specified the requested exemption from third party access under Article 283 paragraph 1 of the Law so that the right to a priority booking of 88% of the available capacity is 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), arguing that this is a necessary condition without which it is not possible to secure the financing of the Project. The remaining 12% of the available capacity may be allocated to all third parties who have submitted a non-binding bid.

In the Addendum, GASTRANS d.o.o. states that the requested exemption of 88% of the envisaged technical capacities of the New Interconnector will be allocated to GAZPROM and SRBIJAGAS and their respective subsidiaries as this is a necessary condition without which GASTRANS d.o.o. cannot provide project financing. This request is reasoned by GASTRANS d.o.o. claiming 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 about [...] in a year of a maximum demand, which is insufficient for the realization of the planned investment. GASTRANS d.o.o. justifies the request for 88% capacity by different scenarios of utilization of the technical capacity of the gas pipeline, but also by the fact that the stated demand is non-binding, that non-binding bids for the use of transmission services to the place of delivery to buyers in the Republic of Serbia are duplicated, significantly higher than the real and future demand and needs of the market in the Republic of Serbia, and that in the case of submitting binding bids for booking of the capacities at the exits from which the Republic of Serbia market would be supplied, the volume of the required capacities was significantly lower, indicating that the investment in the New Interconnector would not be justified if the companies in whose ownership structure GASTRANS d.o.o. is would not have the right to 88% capacity, which is the volume that provides for a positive investment decision for the construction of a New Interconnector.

Explaining further different capacity utilization scenarios, GASTRANS d.o.o. remained with the Initial request, in which it requested an exemption from the obligation to apply regulated prices, as it indicates that this is a condition without which it is not possible to recover the investment and realize the necessary income during the exemption period.

In addition to the aforementioned, GASTRANS d.o.o. argued that the requested exemption requires the exemption from other articles of the Law correlating with the exemption from third party access and regulated under Article 283 paragraph 1 of the Law and the exemption from ownership unbundling under Article 224 of the Law, so that the Agency by the act on exemption should also exempt GASTRANS d.o.o. from:

- the obligation to apply minimum requirements for third party access referred to in Article 228, 247, 248, 249, 283, 284 and 285 of the Law, which articles, according to the harmonization table², transpose Article 14 of the Gas Access Regulation,
- the obligation to apply capacity allocation and congestion management principles from Articles 254 and 286 of the Law, which articles, according to the harmonization table, transpose Article 16 of the Gas Access Regulation,
- the obligation to apply rules of transparency from Articles 247-249 of the Law which articles, according to the harmonization table, transpose Article 18 of the Gas Access Regulation,
- the obligation to apply rules of record keeping from the 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 from the Articles 248, 254, and Article 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 from the Article 254 paragraph 1 item 7) of the Law, which articles, according to the harmonization table, transpose Article 22 of the Gas Access Regulation,
- obligation to obtain approval for the general terms and conditions for the provision of services referred to in Article 283 paragraph 1 as well as Articles 48-57 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 Articles 41 (6) (b) and (10) of the Gas Directive,
- the obligation to obtain the approval of the Agency on tariffs and methodologies referred to in Article 92 paragraph 1 of the Law, and in relation to Article 50 paragraph 1 item 6) of the Law, which articles, according to the harmonization table, transpose Articles 41 (6), (8) and (10) of the Gas Directive,
- the obligation to apply tariffs from Article 50 paragraph 1 item 6-8), which article, according to the harmonization table, transpose Article 13 of the Gas Access Regulation,
- all future obligations arising from the relevant articles of the network codes for balancing, capacity allocation, interoperability, which GASTRANS d.o.o. considers to be contrary to the exemption right and for which it seeks guarantees that they will not be applied during the exemption period, for which duration these and other regulations may become part of the legal system of the Republic of Serbia.

The Addendum included the following schedules:

² The form of the statement on the harmonization of legislation with the EU legislation, accompanying the proposal of the Law submitted to the Parliament of the Republic of Serbia to the adoption, available at: http://www.parlament.gov.rs/upload/archive/files/cir/pdf/predlozi_zakona/4678-14.pdf

- 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) point (1) of the Rules of Procedure;
- Schedule 2 - Tariff Methodology prepared by GASTRANS d.o.o.;
- Schedule 3 - Compliance program prepared by GASTRANS d.o.o. providing information related to the requested exemption from the ownership unbundling requirements set out in the Articles 224 and 225 of the Law;
- Schedule 4 - Market Study report, prepared by BluBerries GmbH, Stetten 4, 83123 Amerang Germany, supporting justification for conditions prescribed in the Article 288, paragraph 1 items 1) and 5) of the Law, but also providing information related to justification of other conditions prescribed in the Article 288 paragraph 1 of the Law;
- Schedule 5 - Licenses and consents, supporting justification for condition prescribed in the Article 288, paragraph 1 item 2) of the Law, but also providing information related to justification of other conditions prescribed in the Article 288 paragraph 1 of the Law;
- 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
- Schedule 7 - Corporate registry excerpts for South Stream Serbia AG, GAZPROM TRANSGAZ KRASNODAR, GAZPROM, and GAZPROM EXPORT LLC and the register of shares of South Stream Serbia AG as of 30 May 2018, showing the change of the shareholder i.e. GAZPROM TRANSGAZ KRASNODAR substituting GAZPROM.

After the review of the submitted Request for Exemption and accompanying documentation, the Agency has requested by the letter dated 4 July 2018 from GASTRANS d.o.o. to submit the following documentation: i) statute and incorporation act of South Stream AG Switzerland, (ii) translation in the English language of an excerpt from the commercial register for GAZPROM TRANSGAZ KRASNODAR, (iii) translation in the English language of an excerpt from the commercial register for GAZPROM, (iv) data pursuant the which the feasibility study has been prepared, (v) economical-financial data, (vi) information on whether the adjacent transmission system operators have expressed their respective standing on the Rulebook on capacity allocation for the binding phase, which GASTRANS d.o.o. sent to BULGARTRANSGAZ EAD and FGSZ.

On 3 August 2018, GASTRANS d.o.o. submitted the requested documentation. On 10 August 2018 GASTRANS d.o.o. submitted to the Agency elaboration of the necessity of the exemption regarding the risks connected to the investment. On 27. September 2018 GASTRANS d.o.o. submitted amended Schedule 1 (feasibility study) and Schedule 2 (tariff methodology).

Both Initial request and the Addendum are submitted in the Serbian language and in the English language, for the purposes of further proceedings before the Secretariat of the Energy Community, in accordance with Article 288 of the Law.

Based on the analysis of the content of the Initial request, the Addendum and all Schedules, the Agency has determined the following:

1. Existence of active legitimacy of GASTRANS d.o.o.

By the Addendum GASTRANS d.o.o. has amended the Initial request by, *inter alia*, specifying that it will be the owner of the Project pipeline and that it therefore does not seek the exemption from Article 224 paragraph 1 of the Law.

Bearing in mind this new fact, the Agency has reassessed active legitimacy of GASTRANS d.o.o., which was determined on the basis of information from the Initial request and before rendering the Decision on Market test, and it has reconfirmed that GASTRANS d.o.o. has active legitimacy to submit the request for exemption.

2. Eligibility and allowance of the Request for Exemption

During assessment of the eligibility of the Request for Exemption, the Agency considered the Project description and qualification of the Project pipeline as new interconnector, evaluating the following:

A Project pipeline as new infrastructure

In addition to details on the Project pipeline, provided in the Initial request, GASTRANS d.o.o., in the Addendum, has provided certain additional information on the Project pipeline. Based on this information, the Agency has determined that the planned infrastructure has the characteristics of new infrastructure, whereby it has taken into consideration the fact that technical characteristics of the Project pipeline are still preliminary as the front-end engineering and design (FEED) is still ongoing so that the final technical parameters of the New Interconnector will be known only at the later stage.

The Project pipeline as a new interconnector is about 400 km long, its route crosses the territory of the Republic of Serbia in the length of about 400 km, it will cross the Republic of Serbia state border, so that the entry point to the interconnector is on the border between the Republic of Serbia with the Republic of Bulgaria and the exit point of the Project pipeline shall cross the Republic of Serbia border with Hungary. The Project pipeline is to be connected to the adjacent natural gas transmission system in Republic Bulgaria, which is operated by BULGARTRANGAZ EAD, and the adjacent natural gas transmission system in Hungary, which is operated by FGSZ.

As stated in the Request for Exemption, GASTRANS d.o.o. plans to provide the transmission services not only to suppliers in order to supply the Republic of Serbia's market, but also for the transmission of natural gas and further supplies outside the territory of the Republic of Serbia (so that a part of the quantities will be delivered across the Republic of Serbia border with Hungary, where there will be a connection point of the Project pipeline with the neighboring FGSZ system, wherefrom it is possible to supply Hungarian and/or neighboring markets of Central Europe).

The Project envisages a connection of the entry point of the Project pipeline to the incremental capacity that shall be constructed by BUGLARTRANGAZ EAD in the direction towards the territory of the Republic of Serbia, while the final exit point of the Project pipeline shall be connected to the incremental capacity that shall be built by FGSZ for the connection to the Project pipeline.

In accordance with the letters from Hungarian NRA and Bulgarian NRA, in order to ensure optimal functioning of the new infrastructure of the territory of the Republic of Bulgaria, the Republic of Serbia and Hungary it is recommended to work out a single regulatory regime that will be close to the provisions on incremental capacity described in European Commission Regulation (EU) 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems (hereinafter referred to as: “**NC CAM**”).

It is planned that the Project pipeline will have one metering station on the territory of one of the neighboring countries, and according to the preliminary agreement with FGSZ the location of that metering station should be located near the town of Kishkundorozhma, in Hungary.

The Project envisages that additional three exits shall be built on the planned route through the Republic of Serbia at the locations of the cities of Paraćin, Pančevo and the town of Gospođinci, from which the Serbian market would be supplied. This would allow some of the quantities delivered to these exits to be delivered through the transmission system of SRBIJAGAS *i.e.* Transportgas Srbija d.o.o., to the market of Bosnia and Herzegovina.

By reviewing the Request for Exemption and the Feasibility Study, the Agency has determined that the operating pressure of the interconnector is 7.4 MPa, and the maximum allowable operating pressure of 6.6 MPa, which provides for a maximum annual flow of 13.88 billion m³ of natural gas, whereby the deadline for the start of the operational work of the pipeline is [...].

The Project pipeline of the GASTRANS d.o.o. is described as a facility that by its capacity provides sufficient quantities of natural gas that will contribute to the development of gas infrastructure in the Republic of Serbia and create conditions for the development of the natural gas market in Republic of Serbia but also the development of gas markets in the region countries where need for gasification exists, because a significant percentage of the population, including the Republic of Serbia, have no access to natural gas nor the possibility to supply with natural gas.

In the Feasibility Study and the Request for Exemption, it is pointed out that the connection of the Project pipeline to the transmission system in the Republic Bulgaria would provide not only an alternative route of natural gas supply to the Republic of Serbia, but also a diversification of the supply sources in the Republic of Serbia, bearing in mind that the transmission system BUGARTRANSGAZ EAD transports natural gas coming from several different sources, including natural gas from the LNG terminal, and that, in the case of the construction of an IGB interconnector (Bulgaria-Greece) GASTRANS d.o.o. could also supply natural gas to the market of the Republic of Serbia, which, via the TAP interconnector, are delivered from Shah Deniz 2 gas fields. Bearing in mind the above, it follows from the request that the Project pipeline would enable not only an alternative route of Republic of Serbia market supply, but also contribute to the diversification of the sources of supply of the market of the Republic of Serbia with natural gas from other sources.

The Project envisages the construction of the pipeline in sections, as follows: Section 1 - from the Bulgarian-Serbian border to Žabari (150 km), Section 2 - from Žabari to Kovin (48 km), Section 3 - from Kovin to Gospođinci (112 km), and Section 4 - from Gospođinci to the Serbian-Hungarian border (location Horgoš) (92 km).

The Project involves the construction of a total of 4 main metering regulation stations (MMRS) near Zaječar, Paraćin, Žabalj and Pančevo, and compressor station CS 1 is Section 5 at the location of Velika Plana.

[.....]

The holder of the Project, GASTRANS d.o.o., plans to own the described pipeline in order to perform the activity of natural gas transmission and operation of the transmission system, including its development and maintenance.

B Project pipeline as interconnector

As mentioned above, Article 288 paragraph 1 of the Law prescribes that the exemption is granted for new facilities of the gas pipeline system - interconnectors and natural gas storage facilities.

As mentioned above, Article 2 item 25) of the Law defines interconnector as electricity transmission line, natural gas pipeline, oil pipeline that crosses the border between the states for the purpose of connecting of their systems, as well as the equipment that is used for connection of energy systems.

It follows from the above provisions of the Law that a gas pipeline crossing the border between the Republic of Serbia and any other state is considered an interconnector if such a crossing is aimed at interconnecting gas pipelines, and that the integral part of the interconnector is also equipment used for their connection.

Based on the review of the Request for Exemption and the submitted evidence, GASTRANS d.o.o. plans to build a completely new infrastructure as described in subsection A above (*Project pipeline as new infrastructure*). The Project pipeline, according to the Agency, qualifies as a new infrastructure, having in mind that it shall be entirely constructed as a new infrastructure within the meaning of Article 2 item 46) and Article 288 paragraph 1 of the Law.

In assessing the Project pipeline as an interconnector, the Agency took into account the provisions of Article 2 of the Gas Directive defining an interconnector as a transmission line which crosses or spans a border between Member States (EU) for the sole purpose of connecting the national transmission systems of those Member States, including equipment for their connection.

The Agency also took into account that the Ministerial Council of the Energy Community passed the Implementing Decision by which the Ministerial Council of the Energy Community defined the concept of interconnectors as a pipeline that crosses or spans the borders between the two Contracting parties to connect their systems, including equipment for their connection.

Therefore, as specified by GASTRANS d.o.o. there are differences in defining term interconnector in the Gas Directive, Implementing Decision and Law:

- pursuant to Article 2 paragraph 1 item 25 of the Law, it is a "[...] pipeline [...] that crosses the border between the states for the purpose of connecting of their systems, as well as the equipment that is used for connection of energy systems";

- pursuant to Article 2 item 17 of the Gas Directive, it is 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*"; and
- pursuant to Article 2 item 17 of the Implemented Gas Directive, it is 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*".

The Agency has considered the submissions made by GASTRANS d.o.o. against the previous practice of the European Commission and the Energy Community which have qualified as interconnector different pipelines as follows:

- BBL - pipeline passes across water between Member States, connecting beach to beach.
- Gazelle, OPAL, SK-HU Interconnector - pipeline traverses one Member State and reaches over short distance into another Member State.
- TAP - pipeline passes across water from a Member State, spans a Contracting Party and a Member State and reaches into a Third Country.
- Nabucco - pipeline traverses multiple Member States and reaches into a Third Country.

In that sense the Agency agrees with GASTRANS d.o.o. 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. This is a clear example of a transmission line "crossing" the border with the neighboring country.

In addition, the Agency understands Article 2 item 17 of the Gas Directive in a manner that the Project pipeline would qualify as interconnector under that provision as the Project pipeline spans a border between the Republic of Bulgaria and Hungary.

The Agency took into account the evaluations of the Energy Community made in the exemption procedure (TAP Project³) and the European Commission practice (Nabucco Project) in which gas pipelines are considered as interconnectors even when crossing the border between the Contracting Party (or Third Party) and EU Member States. In those cases it was decided that the interconnector exists if the pipeline connects the borders (at least) of two Member States, whether on that occasion the border of a non-EU country is crossed⁴. Such decisions created the precedents for all future cases under the Gas Directive and the Implementing Decision. Therefore, the Agency concludes that the Project pipeline qualifies as the New Interconnector pursuant to the Implementing Decision as well.

³ 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)

⁴ item 55 of decision of commission as of 16 May 2013 on exemption of Trans Adriatic Pipeline on requirements related to third party access, regulation of prices and ownership unbundling set out in articles 9, 32, 41 (6), 41 (8) and 41 (10) of Gas Directive 2009/73/EC

In any case, the fact that European Union regulations and the decisions of the Energy Community do not treat as an interconnectors only those gas pipelines crossing the border between the Contracting party and the EU Member State, according to the Agency's assessment, is without prejudice to the eligibility of the Request for Exemption, given the obligation of the Agency to perform the work from its scope in accordance with the Law, by which the Republic of Serbia has implemented accepted obligations, which it recognizes as interconnectors and those gas pipelines crossing the border between Republic of Serbia (as the Contracting party) and any neighboring state (regardless of whether they are the Contracting party or a member of the EU).

By the Law, the Republic of Serbia has implemented in its legal system the Gas Directive in a manner that is non-discriminatory and equally treats all gas pipelines regardless of the border crossing, if the purpose of crossing the border is to interconnect the neighboring gas pipelines for the transmission of natural gas. Therefore, according to the Agency's assessment, the Project pipeline has the capacity of a new interconnector because its construction would achieve the purpose of cross-border connection of gas pipelines, which is the goal of both the European Union and the Energy Community. The Agency also estimates that the treatment of the Project pipeline as an interconnector is not contrary to the objectives of the Energy Community Treaty (Article 2), having in mind the opinion of the Ministerial Council of the Energy Community of 23 September 2014 on the application of the decisions of the Energy Community confirming that the gas pipelines crossing the border between the Contracting parties and EU Member States shall be treated on the same way as those crossing the border between the Contracting parties and to apply on them all provisions regarding flow, export, import, transactions, capacity and infrastructure, which opinion and the position with the same content and identical reach has been confirmed by the European Commission in its Recommendation of 29 October 2014.

Also, the Agency estimates that the circumstance that the Request for Exemption was submitted only to this Agency, as the competent regulatory body in the Republic of Serbia, has no impact to the status of the Project as an interconnector, having in mind the exclusive competence for deciding on exemption has a regulatory body on which territory is predominant part of the gas pipeline⁵ and when only a small part of the pipeline crossed the border and territory of the neighboring state.

In this regard, the Agency notes that the Request for Exemption made by GASTRANS d.o.o. in respect of the approach taken by other interconnector projects and the relevant regulatory authorities, which demonstrates that a number of interconnectors have only be regulated by one national regulator.

GASTRANS d.o.o. submitted Request for Exemption only to Agency, notwithstanding the fact that pipeline reaches into territory of other country, having in mind that this approach was applied to other similar interconnectors, when act on exemption was rendered by only one NRA.

3. Opinion of the Ministry of Mining and Energy as precondition for rendering the act on exemption

⁵ Exemption of interconnector Gazelle, exemption of interconnector Opal and interconnector crossing the border of Slovakia and Hungary

Article 288, paragraph 3 of the Law stipulates that the act on exemption shall be issued by the Agency upon the opinion of the Ministry competent for energy.

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.

Ministry of Mining and Energy, from the aspect of its competence, with its letter no. 312-01-00677/2018-05 as of 18 July 2018, submitted the requested opinion with the following content, which 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 others, performs state administration affairs related 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 program. The Energy Policy of the Republic of Serbia was established by the Strategy.

The Strategy as the strategic priorities of the energy sector development of the Republic of Serbia, for the mentioned period, defines: providing of 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 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 is necessary to provide for the reliable, safe and quality supply of end customers, while respecting the needs for rational consumption 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 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 2483,074 million m³ and 18% from domestic production and 82% from imports shall be provided. The projection of natural gas consumption has a long-term growth trend, with an expected consumption of about 4000 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 on the border with Bosnia and Herzegovina. The total length of natural gas transmission system in the Republic of Serbia is about 2460 km, out 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 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 the region countries 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).

4. Opinions of the neighboring NRA as precondition for rendering the act on exemption

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.

Since the Request for Exemption is considered as allowed in respect of the infrastructure facility and GASTRANS d.o.o. has specified the scope and duration of the required exemption in the Addendum, the Agency acted in accordance with Article 288 paragraph 9 of the Law by its letter no. 40/2018-D-03/25 of 13 July 2018 and forwarded the Proposal of the Rulebook on the binding phase to the Bulgarian NRA and Hungarian NRA, requesting from them to, on the basis of insight of the submitted Proposal of the Rulebook on the manner of capacity allocation and details of the requested scope of the exemption, send to the Agency their respective opinion on the impact of the new infrastructure on their natural gas markets.

[...]

5. Rules and mechanisms for management and allocation of capacities as precondition for rendering the act on exemption

Article 288 paragraph 7 of the Law prescribes that the Agency, before rendering the act on exemption, shall decide on the rules and mechanisms for the management and allocation of capacities, and Article 288 paragraph 6 of the Law stipulates that when deciding on the Request for Exemption, the Agency shall consider non-discriminatory access to the new infrastructure, exemption period, access to the new facilities to be constructed, planned period of the use of the infrastructure and the national specificities applicable in the specific case.

In the Addendum, GASTRANS d.o.o. proposed to split the capacity in the following manner:

- technical capacity of the Project pipeline (TCPP) represents the sum of a minimum required shareholder capacity allocated in the binding phase of the Market Test (MRSC) and third party capacity (TPC);
- third party capacity (TPC) is split in the following manner - third party capacity (TPC) represents the sum of a third party capacity allocated in the binding phase in the Market Test (ATPC) and third party capacity unallocated in the binding phase in the Market Test (UTPC);
- UTPC also represents the remaining available third party capacity to be available to the shareholders or their affiliates for a subsequent booking in priority to third party transmission system users, which together with MRSC represents shareholder priority capacity. UTPC not booked by the shareholders or their affiliates is the third party capacity to be allocated following commercial operation date (COD);
- the minimum required shareholder capacity is the capacity determined by GASTRANS d.o.o. as required to be allocated in priority to shareholders or to affiliates of shareholders in order to finance the Project, which GASTRANS d.o.o. determines as 88% of technically available capacity.

These principles have been further developed in the Rules of Procedure for the Binding phase of allocation of capacity (Schedule 6) providing the steps in the allocation of capacities in the binding phase as follows:

Step 1: Allocation of capacities to shareholders' affiliates (SHA)

- (i) if the sum of SHA Binding Bids is lower than the minimum requirements for SHA capacity in order to take a final investment decision in relation to the Project (i.e. SHA Minimum Capacity), then all SHA Bidders are allocated in accordance with their respective Binding Bids and the difference between SHA Minimum Capacity and SHA allocated Binding Bids is SHA retained capacity;
- (ii) if the sum of SHA Binding Bids is equal to SHA Minimum Capacity, then all SHA Bidders are allocated in accordance with their respective Binding Bids;
- (iii) if the sum of SHA Binding Bids is higher than SHA Minimum Capacity then:
 - (1) SHA shall agree on adjusting of their respective Binding Bids, so that the sum of all SHA Binding Bids is less or equal to SHA Minimum Capacity; or
 - (2) if SHA do not agree on adjusting their respective Binding Bids, the SHA Binding Bids shall be provisionally pro-rated to the level of SHA Minimum Capacity ("Pro-rated SHA Binding Bid") and the difference between a SHA Binding Bid and its Pro-rated SH(A) Binding Bid will, at the election of each pro-rated SHA, be increased up to the SH(A)'s Binding Bid if there is an additional capacity available after the step 3 allocation of TP Binding Bids within any

requirement of the GASTRANS d.o.o. exemption for capacity available only to TPs (i.e. TP Only Capacity).

Step 2: Allocation of capacities to third party ("TP")

- (i) if the sum of TP Binding Bids is lower than or equal to TP Only Capacity, then all TP Bidders are allocated in accordance with their respective Binding Bids;
- (ii) if the sum of TP Binding Bids is higher than TP Only Capacity then TP Binding Bids are provisionally pro-rated to the level of TP Only Capacity ("Pro-rated TP Binding Bid") and the difference between a TP Binding Bid and its Pro-rated TP Binding Bid will, at the election of each pro-rated TP, be increased up to the TP's Binding Bid if there is additional GASTRANS d.o.o. capacity unallocated after the step 3 allocation.

Step 3: Increase of Pro-rated SHA Binding Bids, further SHA allocation, and increase of Pro-rated TP Binding Bids

- (i) if after the allocation of TP capacity within TP Only Capacity there is unallocated GASTRANS d.o.o. capacity remaining:
 - (1) first, a pro-rated SHA will, at its election, have its Pro-rated SHA Binding Bid increased pro-rata to other Pro-rated SHAs which exercised their election right, up to the SHA 's Binding Bid;
 - (2) second, SHA may, upon decision by the Sponsors, place Binding Bids and be allocated with capacity in such amounts as the Sponsors decides as required to enable the Sponsors to take the financial investment decision for the Project;
 - (3) third, a pro-rated TP will, at its election, have its Pro-rated TP Binding Bid increased pro-rata to other Pro-rated TPs which exercised their election right, up to the TP's Binding Bid.

Step 4: Any remaining available capacity shall be made available after the Scheduled Commercial Operations Date as short term capacity, i.e. with a duration of up to one (1) year.

GASTRANS d.o.o. argued that the above principles and allocation steps reflect the results of the Market Test demonstrating that third party transmission system users' interest in the New Interconnector is not such that it would enable GASTRANS d.o.o. to construct the New Interconnector. Namely, third party transmission system users' non-binding bids together amount only to [...], in the year of maximum demand, of the technical capacity of the New Interconnector, what clearly demonstrates that without the support of shareholders/shareholders' affiliated transmission system users and allocation of respective capacities to shareholders/shareholder affiliates, the construction of the New Interconnector would not be financially and economically feasible.

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

The Agency has analyzed the allocation principles and steps, the results of the Market test and the opinions of the neighboring NRAs and has decided to adopt the Decision on the manner of allocation and mechanisms for management of the transport capacities of the company GASTRANS d.o.o number 40/2018-Д-03/42 dated 3 September 2018 (hereinafter referred to as: "**Capacity allocation decision**") by which it has not entirely accepted the proposal of GASTRANS d.o.o. The reasons for not acceptance of relevant parts is detailed in the section "*Exemption from third party access*" below. Generally, the Agency has not followed entirely the proposal of GASTRANS d.o.o. for the allocation of the capacity, but required amendments to be made in relation to allocation for third parties, and the availability of short-term capacity.

The Agency is of the view that the Capacity allocation decision meets the concerns of the Bulgarian NRA and the Hungarian NRA and that it reflects good practice when benchmarked against the allocation procedures applied for other interconnectors.

The Agency can understand the principle assertion made by GASTRANS d.o.o. that it needs to be considered whether long-term capacity or short term capacity are more likely to establish competition in the market. The Request for Exemption of GASTRANS d.o.o. and the allocation rules proposed by it would suggest that its interpretation of the outcome of the non-binding bids is that long-term booked capacities would support competition more than short-term capacities and that consequently the booking of long-term capacities should take preference over the short-term capacity until the commercial operations date. Also GASTRANS d.o.o.'s Request for Exemption suggests that a *pro-rata* allocation would support greater competition by allowing more third parties to be allocated with capacity, even if this would not lead to allocation for all requested capacity.

Whilst the Agency agrees that there are bid scenarios in which this conclusion and the respective allocation principles submitted by GASTRANS d.o.o. would be justified, having regard to the outcome of the demand assessments by the neighbouring TSOs and its analysis of the likelihood of the non-binding bids being repeated in the binding phase, the Agency requires an adjustment of the allocation principles so that some capacities are retained for the short term market if the demand for long-term capacities in the binding phase would be less than the planned maximum capacity of the Project pipeline.

The Agency believes that the proposed split between long-term capacity and short term capacity for allocation after the commercial operation date provides a reasonable split that still allows third parties which have not been allocated with capacity during the first allocation to arrange for supply and transportation from the commercial operations date.

The Agency is of the view that as a consequence of the construction of the New Interconnector, certain existing capacities between the Hungarian system and the Serbian system may also become available for short term capacity bookings. In this regard, it is justified to consider only a smaller amount of short-term capacity as a requirement for the New Interconnector, as the combined effect of short term capacity expected to become available on the existing network as well as capacities retained on the New Interconnector for short term allocation would exceed 10% of the combined capacity.

In relation to available short term capacity, it is also necessary to consider not only relative percentages but also absolute numbers of the capacity being available for short term bookings. Here, the Agency observes that with a planned maximum technical annual capacity of 13.88 bcm, the New Interconnector exceeds in absolute numbers significantly the capacity of other interconnectors or recent incremental capacity projects in the Southern Gas corridor, so that even a percentage below 10% on the New Interconnector exceeds in absolute terms the capacity reserved for short term services on other interconnectors and incremental capacity projects.

At the same time, the Agency considers that it is necessary to introduce a rule that would ensure short term capacity being retained by GASTRANS d.o.o. in case the binding phase of the Market test does not reflect booking long-term capacity from non-binding bids. In this case, a short-term capacity will ensure that parties that may have expressed an interest in the non-binding phase but have for commercial reasons not decided to bid in the binding phase have another opportunity to book capacities nearer to the commercial operations date.

Having in mind the demands for capacities in non-binding phase of the market test, which are published by the neighboring TSOs in Republic of Bulgaria and Hungary, which are almost identical to the bids submitted to GASTRANS d.o.o. the Agency assessed that bundling of capacity is not necessary.

The Agency notes that the bundling of cross-border capacities has not been necessary to achieve matching bids between an exempted section of TAP and the incremental capacity required on the Italian system operated by SNAM. In addition, the bidder comments in the non-binding phase of Market test conducted by GASTRANS d.o.o. and the demand assessments conducted by neighboring TSOs has not indicated a need to bundle capacity that would not be achieved by conditional bids in the incremental capacity process or the binding phase of GASTRANS d.o.o.

6. Assessment of fulfillment of five conditions

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

- 1) the investment must enhance competition in gas supply and enhance security of supply;
- 2) the level of risk attached to the investment must be such that the investment would not take place unless an exemption was granted;
- 3) 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 systems that infrastructure will be built;
- 4) charges must be levied on users of that infrastructure; and

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 infrastructure is connected.

Estimating the conditions prescribed in Article 288 paragraph 1 items 1)-5) of the Law, the Agency has determined that:

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

1a) Enhancement of security of supply

GASTRANS d.o.o. analysis on the security of supply

The natural gas market in Serbia is described in the Addendum in point 5.1. (*Overview of the Serbian natural gas market*). In its points 5.11 to 5.13 the detailed data. for 2017 on the following matters was provided: domestic production of natural gas, natural gas quantities sold by the ten largest natural gas suppliers to the final customers, details on natural gas transport systems in the Republic of Serbia with the length of the gas pipeline, capacity utilization on interconnectors with the transmission systems of Hungary and Bosnia and Herzegovina, and the volume of natural gas quantities transported. In the point 5.1.4. of the Addendum the review of the natural gas market in South East Europe is given.

- 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

The current and forecasted balance between the supply and consumption of natural gas in the Republic of Serbia is described in detail in Chapter E of the Market Study (Schedule 4 to the Addendum), developed by BLUBERRIES GmbH for GASTRANS d.o.o. The Market Study contains data on the realized consumption of natural gas in the Republic of Serbia and natural gas production in the Republic of Serbia in the period from 1996 to 2016, as well as the forecast of natural gas consumption in the Republic of Serbia for the period up to 2030, as well as the forecast of natural gas production in the Republic of Serbia for the period until 2030. The study predicts that the demand for natural gas imports in the Republic of Serbia will increase from 84% in 2017 to 95% in 2030, partly due to a decrease in natural gas production, and partly due to increased consumption. The study also includes the participation of natural gas in gross energy consumption in the Republic of Serbia, as well as the structure of natural gas consumption by sectors. There were no changes in total consumption of natural gas in the Republic of Serbia between 2011 and 2016, but consumptions in sectors and changes in sectors in 2011 and 2016 were given, as well as the reasons for changes in consumption across sectors such as air temperature and change in gross domestic product.

The current balance between supply and consumption of natural gas in the region of Southeast Europe is described in the Market study in chapter F, where is presented in total the realized consumption of natural gas and the production of natural gas in the region of Southeast Europe in the period from 1996 until 2016. It is pointed out that more than half of the natural gas market in the region of Southeast Europe is Romania. From 2011 to 2016, there was a decrease in both consumption and production of natural gas in the region of Southeast Europe. All countries in the region are importers of

natural gas. Observing the whole region, the dependence on natural gas imports is around 40%, but if Romania and Croatia with the largest natural gas production are excluded, the dependence of other countries on imports is 75% higher.

Overall the study concludes that the New Interconnector supports security of energy supply in the Republic of Serbia and the region through (i) the promotion of an alternative mode of transportation for existing gas sources, (ii) opening the possibility of new sources of gas; and (iii) enhances security through the promotion of inter fuel substitution.

- 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 that the Project provides effective requests for capacities to the national and regional markets it intends to supply

The planned maximum quantities of natural gas that can be transported annually through the New Interconnector amounts to [...] for exit to Hungary and [...] for exits to the Republic of Serbia, or [...] for entrance from the Republic of Bulgaria.

In the non-binding phase of Market test, the demand for capacities towards Hungary was made by [...]. The maximum annual quantities that occur in the years in which exist demands of all [...]. According to the data from Hungarian NRA, gross natural gas consumption in Hungary amounted to 9.745 billion m³ in 2017, and imports amounted to 7.951 billion m³. The New Interconnector allows the delivery of natural gas to Hungary, which is higher than the total import in Hungary in 2016 by 26.8%, i.e. than the total consumption in Hungary in 2016 by 3.5%. The planned capacity of the New Interconnector at the Hungary exit can meet the overall natural gas demand in Hungary. Taking into account that the transmission systems in Hungary are connected with the transmission systems of Ukraine, Romania, Croatia, Austria and Slovakia and that the reverse flow is already enabled or will be realized on all interconnectors, the planned capacity of the New Interconnector at the Hungary exit shall enable the natural gas supply to the other countries in the regions of Southeast and Central Europe.

In the non-binding phase of Market test, demand for capacities at the exits towards the Republic of Serbia that would be used for supplying Bosnia and Herzegovina was expressed by [...]. The maximum annual quantities in the years in which exist the requests of all [...]. In 2017, gross natural gas consumption in the Republic of Serbia and Bosnia and Herzegovina amounted to 2.805 billion m³, out of which the imported quantities for covering this consumption amounted to 2,448 billion m³. The envisaged capacities of the New Interconnector at the exits for Serbia are [...] than the maximum required, but the requests for capacities are considerably higher than the needs of the natural gas market in the Republic of Serbia and Bosnia and Herzegovina, which means that GASTRANS d.o.o. has submitted request for capacity planned to supply the same customers in these markets, so it is a realistic expectation that at the binding phase some of the companies shall withdraw their requests. The New Interconnector allows the deliverance of natural gas for the Republic of Serbia and Bosnia and Herzegovina, which is [...], or [...] which means that the planned capacity of the New Interconnector at the exits for the Republic of Serbia can meet the current and future needs for natural gas in the Republic of Serbia and Bosnia and Herzegovina.

- Natural gas sources and, if possible, information on supply agreements or transmission capacities contracted when a long-term capacity allocation is performed. This requirement is less relevant if the capacities are allocated short-term.

This requirement is also considered in the light of the availability of capacities that shall be short-term allocated during the operation of the pipeline for the period less than a year and is less relevant if the capacities are short-term allocated. In the non-binding phase of Market test, [.....]. Taking into account the requests for capacities expressed in the non-binding phase, it is expected that part of the capacity of the New Interconnector shall be short-term allocated so that there will be the possibility of transporting natural gas from sources that are not currently available, but shall be available in the future.

Opinion of the Ministry of Mining and Energy

It is clear from the Ministry of Mining and Energy's opinion, referred to above, that the Ministry's analysis has concluded that the New Interconnector will enhance the security of supply in the Republic of Serbia.

The analysis of the Agency

In reaching this conclusion, the Agency particularly emphasizes that it had in mind the criteria that the Energy Community uses in assessing the fulfillment of the conditions relating to the security of supply in the exemption procedure⁶ being:

Criterion 1 - If it contributes to the 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;

Criterion 2 - If it contributes to achieving security of supply to households;

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;

Criterion 4 - The more bigger the project than the size of the market, the better for the security of supply.

Criterion 1 - Contributions to diversification of supply of the relevant market, namely transporting natural gas from a new supply source or opening a new supply route from an existing supply source.

Currently the only direction for importing natural gas into the Republic of Serbia is from Hungary. The entire quantity of natural gas imported into the Republic of Serbia during 2017 was imported from the Russian Federation through the Ukraine and Hungary.

⁶ [Commission staff working paper – New infrastructure exemptions 06 May 2009](#)

It can therefore be concluded that at this time natural gas for the Republic of Serbia is imported from the Russian Federation, along the shortest transport route. However, restrictions or interruptions of transport of natural gas along this transport route seriously jeopardize supply of natural gas to the Republic of Serbia. The interruption of transport in the territory of the Ukraine in 2009 caused serious economic consequences to natural gas consumers in the Republic of Serbia, and a humanitarian disaster was narrowly avoided in those towns in the Republic of Serbia where heating plants cannot replace natural gas with other energy sources. Those heating plants were very nearly left without natural gas which would have shut down the district heating systems in a large number of towns in the Republic of Serbia during winter months.

Because of all of the above, another supply direction and other sources for importing natural gas are a must for the security of supply in the Republic of Serbia.

[...]

The New Interconnector enables transmission of natural gas from a new supply source and opens a new supply route from the existing supply source. More specifically, although one of the primary sources for natural gas is likely to be Russian natural gas, a wide range of alternative sources could potentially use the GASTRANS d.o.o. pipeline through Bulgarian interconnection with Romania, Turkey, and Greece—subject to the realization of some project currently under consideration.⁷ 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.

Therefore, the Agency believes that the criterion of the EU Commission that new infrastructure increases security of supply because it contributes to diversification of sources and supply routes for the relevant market, particularly by enabling transmission of natural gas from new supply sources and opening new supply routes from an existing supply source, has been fulfilled.

Criterion 2 - Contribution to achieving the security of supply to households

Criteria as to whether the new infrastructure increases the security of supply in accordance with EU Recommendation 2004/67/EC replaced in 2010 by Regulation (EU) No 994/2010, and then by Regulation 2017/1938. These Regulations, apart from security of supplying specific consumer groups, also define the infrastructure standard for the security of supply. The infrastructure standard defines that each country shall ensure that the necessary measures are taken so that 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.

Fulfilling the infrastructure standard, that is, the N-1 standard, is one of the specified conditions for security of supply.

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

⁷ For more detailed exposition of alternative sources, please see the Market Study of BLUBERRIES section E(i),

The analysis shows that:

- Construction of the New Interconnector significantly increases fulfillment of the infrastructure standard in the Republic of Serbia from 38.8% to 114%.
- Construction of pipelines in Turkey and the Republic of 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.

N-1 (%) is calculated as follows:

$$N - 1(\%) = \frac{Epm + Pm + Sm - Im}{Dmax} * 100$$

where:

Epm (in million m³/d) – means the sum of the technical capacity of all border entry points capable of supplying gas to the calculated geographic area

Pm (in million m³/d)- means the maximal technical natural gas production capability which can be delivered to the entry points in the calculated geographic area;

Sm (n million m³/d)– means the maximal technical withdrawal capacity which can be delivered to the entry points to the transmission system;

Im (n million m³/d) – means the technical capacity of the largest entry point to the transmission system;

Dmax (n million m³/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:

Epm – Entry point Horgoš / Kiskundorozsma 13 million m³/d;

Pm - natural gas production 1.5 million m³/d;

Sm - PSG Banatski Dvor 5.2 million m³/d;

Im - Entry point Horgoš / Kiskundorozsma 13 million m³/d

Dmax –17.274 million m³/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 the 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 transport 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 supply⁸ 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;

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

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

In the Addendum 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 transport 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

Criterion 3 - Enabling flexibility of natural gas sources on the market through enabling the import of natural gas from several sources and enabling part of the capacities to be contracted on a short-term basis.

Interested users of the New Interconnector that are not GASTRANS d.o.o. ultimate shareholders and their affiliates will be able to contract the New Interconnector capacities, subject to the Capacity allocation decision. 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. 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, the Republic of 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.

The New Interconnector will enable different sources of natural gas on the natural gas market in the Republic of Serbia and South-East Europe through long-term and short-term allocation of part of the technical capacities of the pipeline to third parties, and this will serve to better achieve the security of supply both in the Republic of Serbia and the SEE region.

Criterion 4 - The larger the Project compared to the size of the market, the better for the security of supply.

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. The capacity of the exit points of the New Interconnector enables delivery of [...].

Natural gas consumption in Hungary in 2016 amounted to 9.745 billion m³, while import amounted to 7.951 billion m³. The capacity of the exit point of the New Interconnector towards Hungary enables delivery of [.....].

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.

The Agency's conclusion with regard to fulfillment of prescribed conditions on enhancement of the security of supply

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

GASTRANS d.o.o. analysis of the natural gas market in the Republic of Serbia and the SEE region

As Schedule 4 of the Addendum, GASTRANS d.o.o. submitted a 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 authors of the study believe that construction of the New Interconnector will increase competition on the natural gas market in the Republic of Serbia in two ways.

The first way is by increasing the capacities for importing natural gas. Increasing demand for natural gas through increased possibility of supply will lower the price of natural gas, regardless of the structure of the natural gas market, because increased market liquidity will cause the prices to drop. This is because in any economic model, upward stimulation of demand as a reaction to increased liquidity is accompanied by lower prices. If the prices are not lowered, there will be no increase in demand for natural gas, and the additional supply caused by increasing the capacity for importing natural gas will not be realized. This is supplemented by an analysis which, from a top down approach, looks at the cost of supply and shows that the New Interconnector offers the cheapest supply route and it is there likely that prices would fall as a result of its development.

The other way in which the New Interconnector will have a positive effect on competition on the Serbian natural gas market is the price at which the natural gas will be sold. The New Interconnector will enable third-party access which will restrict the prices at which Gazprom Export LLC will sell natural gas

in the Republic of Serbia. Because, if Gazprom Export's prices are higher than the prices of natural gas of other suppliers with access to the Serbian natural gas market, the quantities of third-party natural gas would increase, lowering the prices of natural gas sold in the Republic of Serbia.

The authors of the study consider that the New Interconnector, together with third-party access, will act as an economic force that pushes the market to act more as competitive market through establishing a price ceiling for the current natural gas suppliers in the natural gas market in the Republic of Serbia. This is in accordance with the results of the non-binding Market test which disclosed a marginal third-party interest in the capacities of the New Interconnector. The interest level essentially shows interest in the situation of arbitrary participation of third parties in the natural gas market in the Republic of Serbia, as well as for transit requirements.

The study further suggests that the New Interconnector will promote inter-fuel competition. That is, the Republic of Serbia, and the region at large, has potential for natural gas to substitute other fuels, including other less environmentally friendly fossil fuels such as oil and coal. This potential, combined with more supply and lower prices, should create an increased opportunity for natural gas to gain new market share and engage in other markets that were previously unavailable due to either price or availability factors.

The conclusion of the Market Study is that the New Interconnector will cumulatively increase the competitiveness of the natural gas market in the Republic of Serbia and the SEE region in several ways:

- by opening 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;
- by enabling the 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;
- by increasing the liquidity of the only relatively liquid gas hub in the region - Baumgarten in Austria;
- by enabling the importing of natural gas from Central Europe into the Republic of Bulgaria via the reverse flow of the New Interconnector.

Together, the factors listed above will facilitate: (i) the reduction of natural gas prices both in the Republic of Serbia and the region, and (ii) an increase in the consumption of natural gas as a result of, amongst other reasons, inter-fuel substitution.

The Agency 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, Denmark⁹ will become a net importer of natural gas as from 2020, as potentially will the Netherlands¹⁰

9 - <https://www.valuwalk.com/2017/01/denmark-natural-gas/>

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 the above, as well as that in almost all countries in Central, South and South-East Europe natural gas production is less than their natural gas consumption, GAZPROM 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.

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.

Further sources of natural gas include natural gas from the LNG regasification terminals in Greece and Turkey. The closest LNG terminal is in Greece, near Athens. The LNG terminals in Europe for the most part have the role of enabling delivery of natural gas from sources that cannot reasonably 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 current lack of infrastructure, while the costs of building pipelines would be high.

Structure of the natural gas market in the Republic of Serbia

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. Import of natural gas into the Republic of Serbia is predominantly, and in some years 100% from Gazprom Export LLC, 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 of natural gas, distribution of natural gas and retail sale of natural gas. Gazprom Export LLC 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 increases competitiveness of the natural gas market, the Agency particularly emphasizes that it had in mind the criteria the Energy Community uses in determining whether there is a justification of granting an exemption to new infrastructure and the

requirement for the proponent of a project and/or national regulator to submit certain information requirements.

- 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 will promote competition through a downward pressure on prices within both the Serbian domestic and regional market - and that the exemption requested will not alter this fact.

- 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 a total number of connections and total length of the distribution network in the Republic of Serbia and a 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%.

- 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 the Rules of Procedure for the binding Market test phase in which it provided a proposal for allocation of capacities.

The Agency rendered the Capacity allocation decision on 3 September 2018, defining the principles for allocation of capacities. This Act and the Capacity allocation decision define the principles and procedure for allocation of capacities of the New Interconnector which GASTRANS d.o.o. should apply in the allocation of capacities after submission of binding requests for capacities of the New Interconnector.

- Assessment of the anticipated impacts of the project on the markets impacted by the project

As already specified, in the Market Study, 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. In summary, the Market Study concluded that the impact would be one of increased competition within the natural gas and between fuels 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.

- 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 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 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 third party access.

- 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 notification for their use has been sent a day ahead to all interested parties on an interruptible basis. However, if the transmission system user, which has contracted firm capacity, (the precise hour by which nomination could be done shall be specified in the network code), nominates such capacity, the transmission system operator will return capacity to user with firm capacity.

Potential conditions that may be imposed on the New Interconnector

In order to ensure that a gas pipeline for which exemption is being requested increases competitiveness, the EU Commission in its Criteria for determining whether there is a justification of granting exemption to new infrastructure has defined which conditions national regulators may impose:

- Requirement of testing the interest of the market and satisfying the interest expressed in the capacities as far as possible, 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. GASTRANS d.o.o. defined the 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 the 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 LLC 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 LLC 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, except if 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, and 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 [...] 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. However, 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, 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 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 and the Capacity allocation decision the Agency has limited the amount of capacities available to ultimate shareholders of GASTRANS d.o.o. for priority long-term contracting, which limitation allows for the development and implementation of the Project.

The Agency's conclusion with regard to the 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 lower prices and an increase of natural gas consumption—associated with some fuel substitution.

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 ultimate shareholders of GASTRANS d.o.o. The companies being 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 if the following conditions are applied:

- Gazprom Export LLC 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 New Interconnector is justified, the new capacity of the New Interconnector 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.

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, point 5), sub-point (1)) and an analysis of fulfillment of the specified 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, point 5), sub-point (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, point 5), sub-point (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 the 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 point 3));

- 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 point 6) of the Rulebook.

GASTRANS d.o.o. has emphasized several key risks which prevent realization of the construction within the regulated system, *i.e.* without the exemption from the ownership unbundling, third party access and regulated tariff requirements. It has specifically pointed out that existing ISO/ITO operators are not in a position to construct the pipeline as well as that GASTRANS d.o.o. as unbundled entity could not be able to attract enough equity and enough third party financing to construct the New Interconnector.

GASTRANS d.o.o. also pointed out that the exemption from third party access rules would enable it to prioritize the use of the New Interconnector by more credit worthy transmission system users as well as that potential overrun costs are not possible to be recovered under the tariff calculation methodology for the national transmission system operated by the existing transmission system operators.

The Addendum further contained the 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 the exemption has been granted by the relevant national regulatory authorities. The purpose of such benchmarking was to show that investment risks increase in accordance with the length of the pipeline, the overall project costs, the nature of terrain, the jurisdictional charges and the number of shareholders able to provide the equity. It was also 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 should be submitted together with a request for exemption are the analyses or feasibility studies relating to construction of the infrastructure. They should contain: 1) data on the estimated time for the construction of the new infrastructure, 2) data on the estimated value of investments in the new infrastructure, 3) data on the probability of recovery of the investments 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 a feasibility study 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 basis of which the Agency has assessed the fulfillment of this condition.

In assessing fulfillment of this condition, the Agency has especially taken into consideration the peculiarities of the market of the Republic of Serbia which is in line with point 5 of article 288 paragraph 6 of the Law. Such national peculiarities, 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 [...] equity from the market;
- 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 the direct investments (Official Gazette of the Republic of Serbia no. 18/2018). Therefore, the Project risks could not 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;
- apart from two projects realized in the last fifteen years, specifically the construction of gas pipeline between natural gas storage Banatski Dvor and Gospođinci (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 1990s. In effect, the market is stagnant and there is no investment 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 point 3) of the Rulebook)

In the Request for Exemption GASTRANS d.o.o. specifies certain economic and financial risks of investing in the infrastructure, which, from the viewpoint of the Agency, can be considered objective, and which can be accepted:

- Size of the project. The value of investment in the construction of the Project and the physical characteristics of the Project (length, capacity, etc.) are of extremely high volume given the size of Republic of Serbia's natural gas market, which consequently carries significant risks and investments that cannot solely be borne by the users of the domestic natural gas transmission systems.

- Very limited possibilities for financing a project of this size by the existing TSOs in the Republic of Serbia. Bearing in mind the long-term financial standing and capacities of the domestic TSOs, including human and logistical resources, the assessment that their possibilities for financing a project of this size are very limited is objective. The same assessment relates to possibilities regarding state aids and subventions from third countries (including the EU).
- Small number of shareholders (or shareholders' affiliates/related parties) of GASTRANS d.o.o. between which the economic and financial risks of the investment can be distributed. Namely, GASTRANS d.o.o. has only one direct shareholder and two ultimate shareholders, which hinders the possibilities for obtaining capital and decreases the options for dispersing risk.
- Limited interest of third-party users of the system. Success of the Project, measured by the desired return on the investment and its security which are a prerequisite for securing funding for the Project, is significantly conditional upon the existence of long-term transport agreements for a major part of the New Interconnector's capacities. The long-term financial stability and predictability of the Project are essential for financing of a project of this size.

The Agency has also assessed that the expressed interest of third parties in using the services of the New Interconnector, being around only [...], confirms that providing the service under regulated conditions, given the limited expressed interest, would be insufficient for realization of the Project. Therefore, it has been 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 some guaranteed long-term use of the capacities of the New Interconnector.

Furthermore, in the Request for Exemption, GASTRANS d.o.o identified the risk that exceeding 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, 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.

Moreover, GASTRANS d.o.o.'s statement that the methodology for forming prices for access to the natural gas transmission system has changed several times over the previous period 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).

Recognizing the fact, as stated, that this is a high-risk Project, and that the present methodology, apart from not excluding the possibility of change in the coming period, does not provide for the option of determining tariffs over a longer period of time, which impacts the risk of insufficient use of capacities and change in income, which are indeed the basic criteria relating to the risk of realizing an investment, we believe that this will not be possible unless exemption is granted.

b) Request for exemption from applying regulated prices

Starting from the above stated reasons, the Act on Exemption also provides for exemption from applying regulated prices. Taking that requirements into consideration, this Act defines the basic principles on which the future manner of forming prices for access to the transmission system should be based. The basic goals in defining these principles were based on the need for the future manner of forming prices to ensure a clear and non-discriminatory approach to determine the tariffs for the long term booked capacity. This includes precisely and unambiguously determined formula for determining the necessary income which should be recovered through the tariffs. Moreover, this includes a clearly determined procedures and processes on the basis of which future corrections of tariffs can be derived. This means that all future deviations of projected from realized costs, such as investment costs, operating costs, crediting costs and the like, will be reviewed each year and, as needed, for the amount and direction of their correction, a new tariff will be formed which would be fixed for a period of one year. This also includes deadlines, necessary documentation that needs to be submitted to the Agency for verification whether the future tariffs have been formed in accordance with the methodology. Non-discrimination means that no transport system user may be in a privileged position with regard to the tariffs.

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 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 complete 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 life 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 the item 12 of this Act, including the manner and deadline for adjusting tariffs which will be formed in accordance with the methodology adopted within the Duration of exemption, 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.

Therefore, having assessed the overall facts and data provided by the GASTRANS d.o.o., taking into consideration exemption decisions¹¹ rendered so far, and weighting the arguments in the context of national peculiarities, 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 separate from the operator of the system within which the new infrastructure facility will be constructed

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

¹¹ 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."

will acquire ownership rights over the New Interconnector, on which it will conduct the business activity of natural gas transmission.

4. That the users of the new interconnector bear the costs of use of the facility

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 form the prices for the transmission services in accordance with the proposed tariff methodology and the approved exemption from the obligation of applying regulated prices.

By reviewing the submitted documents, the Agency has determined that the users of the New Interconnector will bear the costs of use of services on the New Interconnector, and that the amount of such costs will be determined and charged to the users by GASTRANS d.o.o., in its own name and on its own behalf.

5. That the exemption does not prevent competition, efficient functioning of the internal natural gas market and efficient operation of the regulated systems to which the new interconnector is connected

In reaching its conclusion on this requirement, the Agency particularly emphasizes that it has had in mind the criteria the European Commission uses in assessing the fulfillment of the following criteria:

Criterion 1 - That the exemption will not be detrimental to competition;

Criterion 2 - That the construction of the exempt infrastructure will not have a negative effect on the effective functioning of the market; and

Criterion 3 - That the construction of the exempt infrastructure will not result in increasing the tariffs of regulated systems.

Criterion 1 - That the exemption will not be detrimental on competition:

The criterion requiring that the exemption will not have a negative effect on competition has a different approach from effects the New Interconnector has on competition (*i.e.* section 1 b)), because the focus is not on the specific effects of the investment, but on the potential negative effects of the exemption itself. It is necessary to determine whether the exemption could have negative effects on the competitive structure of the market through granting powers to market participants that would allow them to exercise market influences they may not otherwise.

The New Interconnector is part of a new direction for transmission of natural gas from Turkey, through the Republic of Bulgaria and the Republic of Serbia to Hungary. A proportion of the gas from this source could be transported from Hungary to the countries with which it is connected, given that the capacity of the New Interconnector at the border between the Republic of Serbia and Hungary will be greater than the requirements for imported gas in Hungary. The New Interconnector will be a new infrastructure facility of a new transmission system operator, while in the Republic of Bulgaria and Hungary the existing regulated transmission systems will be expanded.

The expansion of the transmission system in the Republic of Bulgaria means the construction of infrastructure that will enable significant capacity for import of natural gas from Turkey, as well as the construction of an interconnector between the Republic of Bulgaria and the Republic of Serbia. The construction of an entry point into the Bulgarian transmission system from Turkey will enable importing of natural gas from various sources, which will have a positive effect on competition on the Bulgarian natural gas market. The IGB interconnector, for which an exemption procedure has been initiated, should connect the transmission systems of the Republic of Greece and the Republic of Bulgaria. The planned capacity of the IGB interconnector is 3 billion m³ a year, but the binding allocation of capacity has been unsuccessful several times due to insufficient commercial interest. The construction of the New Interconnector will increase the natural gas market for placement of natural gas from the IGB interconnector to include the Republic of Serbia, Hungary and other countries connected to the Hungarian transmission system, which could have a positive effect on the utilization of this interconnector and on increasing competition.

It is assessed that the construction of the New Interconnector will have a positive effect on the regulated transmission system in the Republic of Bulgaria, on the IGB interconnector and on the Bulgarian natural gas market. The same is true of the natural gas market and system in Turkey. The positive effect largely derives from the fact that these projects are complementary and this is a synergy that the competitive nature of the markets and transmission systems in those states can be expected to embrace.

The Serbian transmission system is linear with radial development of the system from north to south, which makes it extremely sensitive in terms of reliability and ensuring security of supply, because any upstream interruption of supply could cause disruptions in delivery at the exit points from the transmission system downstream from the point of interruption. The New Interconnector will enable increased reliability of the Serbian transmission system. The sought exemption should not limit this effect as it permits the flow of both existing and new sources from south to north.

The New Interconnector will have three exit points towards the existing transmission system in the Republic of Serbia. Increasing the number of entry points for importing natural gas into the Republic of Serbia from the current one to four will have a positive effect in a number of ways. Since the working pressure in the New Interconnector will be higher than in the existing transmission system, it will increase the working pressure in the existing transmission system in the Republic of Serbia. The first exit point from the New Interconnector will enable increased working pressure in the south part of the existing transmission system in the Republic of Serbia and solve the problem of large drops in pressure in the system during the winter period from north to south, because now all entry points to the Serbian transmission system are in the northern part. Increasing the pressure in the southern part of the existing transmission system in the Republic of Serbia will enable construction of new pipelines both in that part of the Republic of Serbia, but also construction of an interconnector with neighboring countries which was not possible so far because of the low pressure in the Serbian transmission system.

The Agency has assessed that construction of the New Interconnector will have a positive effect on the regulated transmission system in the Republic of Serbia. Enabling importing of natural gas into the Republic of Serbia from two directions and increasing the import capacities at the entry points will create the necessary conditions for competition for importing natural gas and will have positive effects on the functioning of the natural gas market in the Republic of Serbia.

Expanding the transmission system in Hungary means the construction of infrastructure that will enable significant capacity for import of natural gas from the direction of the Republic of Serbia. Reverse flow of natural gas will be enabled at the point of interconnection between the Republic of Serbia and Hungary. The construction of an entry point into the Hungarian transmission system from the Republic of Serbia will enable importing of natural gas from various sources, which will have a positive effect on competition on the Hungarian natural gas market. Since the capacities for importing natural gas from the direction of the Republic of Serbia are greater than the requirement for import of natural gas for Hungary, and since there are other entries into the Hungarian transmission system, it is to be expected that part of the quantities of natural gas imported into Hungary from the direction of the Republic of Serbia will be transported to other countries, *i.e.* that there will be positive effects on the functioning of the natural gas market in South-East Europe but also in Central Europe.

The Agency has assessed that the construction of the New Interconnector will have a positive effect on the regulated transmission system in Hungary, as well as on the natural gas market in Hungary and the regions of South-East and Central Europe.

The Agency considers that, were the exemption requested to be approved, the benefits described above would not be of detrimental effect to competition as a result.

Criterion 2 - Construction of the exempt infrastructure will not have a negative effect on the effective functioning of the market

To confirm compliance with this criterion it is necessary to prove that optimization of the operation of the New Interconnector will not cause congestion in connected transmission systems. This scenario is achieved by setting the conditions for transparency and capacity management for the New Interconnector.

When determining the capacity of the New Interconnector, GASTRANS d.o.o. harmonized capacities at the interconnection points with the transmission systems in the Republic of Bulgaria, the Republic of Serbia and Hungary, that is, the capacity at the exit point from the Bulgarian transmission system towards the New Interconnector is equal to the capacity of the entry point of the New Interconnector. The capacity at the exit point from the New Interconnector towards the Hungarian transmission system is equal to the capacity of the entry point of the Hungarian transmission system from the Republic of Serbia. The minimum working pressures at the interconnection points have also been harmonized.

GASTRANS d.o.o. has accepted to apply at the interconnection points the network code provisions (binding for TSOs in EU countries) that relate to the operational cooperation between the connected transmission system operators.

The New Interconnector will have a higher working pressure than the current transmission system in the Republic of Serbia. Therefore, the New Interconnector cannot cause congestion. An agreement on the operating regime of and between the two transmission systems will harmonize the operation of the New Interconnector and the current transmission system in the Republic of Serbia.

Harmonizing the procedure for short-term allocation of capacities and the procedure for congestion management between the New Interconnector and the connected transmission systems will avoid capacity congestion at the interconnection points between the New Interconnector and the

connected transmission systems and will have a positive effect on the efficient functioning of the market.

The construction of the New Interconnector will not cause congestion in the connected transmission systems, so it will not have a negative effect on the efficient functioning of the market.

Criterion 3 - Construction of the exempt infrastructure will not result in increasing the tariffs of regulated systems

Analysis of the impact of the construction of the New Interconnector on the transmission tariffs for the transmission systems in the Republic of Bulgaria and Hungary falls within the competence of the national regulators of the Republic of Bulgaria and Hungary. Below is the information relating to the interest in use of the capacities and necessary investments relating to interconnectors with these two transmission systems that the Agency currently has at its disposal.

Since, during the non-binding phase of the Market test examining the natural gas market relating to the construction of the New Interconnector, great interest was expressed in contracting of long-term capacities at the entry point from the Republic of Bulgaria, this same interest exists in the Bulgarian transmission system for the transport towards the Republic of Serbia. The income from transporting natural gas from Turkey towards the Republic of Serbia is expected to be just enough to cover the costs of expanding the transmission system in the Republic of Bulgaria, and thus is not expected to increase the tariff.

Conversely, since, during the non-binding phase of the Market test examining the natural gas market relating to the construction of the New Interconnector great interest was expressed in contracting long-term capacities at the exit point towards Hungary, this same interest exists at the entry into the Hungarian transmission system from the Republic of Serbia. The income from transporting natural gas from the direction of the Republic of Serbia through the Hungarian transmission system is expected to be just enough to cover the costs of expanding the transmission system in Hungary, and thus is not expected to increase the tariff.

The New Interconnector is planned to be connected to the existing transmission system in the Republic of Serbia at three points. All of these three exit points which are part of the New Interconnector are very close to the existing transmission system in the Republic of Serbia, so, given minimal investment required, connecting the New Interconnector with the existing transmission system in the Republic of Serbia will not cause increase of the tariffs for use of the existing transmission system in the Republic of Serbia.

The construction of the New Interconnector, with its projected utilization period, will not result in an increase of the tariffs of the regulated systems. Quite to the contrary, it is likely to lead to their decrease by applying competitive pressure.

Based on all of the above, the Agency has assessed that exemption of the New Interconnector will not prevent competition, efficient functioning of the internal natural gas market or efficient operation of the regulated systems with which the future pipeline will be connected, since it fulfills all of the criteria.

Exemption from the obligation of ownership unbundling

GASTRANS d.o.o. has requested exemption from the obligation of ownership unbundling specified in Article 224 paragraph 2 and Article 225 of the Law.

Based on review of the documentation submitted with the Request for Exemption, it has been determined that GASTRANS d.o.o. is a one member/shareholder company, founded under the regulations of the Republic of Serbia to conduct the activity of pipeline transport as its core business activity, that its sole member/shareholder is joint-stock company South Stream AG, founded under the regulations of Switzerland, with seat in Switzerland, Canton Zug, and that the shareholders of South Stream AG are GAZPROM TRANSPORT KRASNODAR with 51% of shares and SRBIJAGAS, with 49% of the shares in South Stream AG.

Both companies, GASTRANS d.o.o. and South Stream AG, were founded for the activities of development, financing, construction, exploitation and maintenance of the section of the South Stream pipeline which will be constructed in the Republic of Serbia for transport through and delivery of gas to the Republic of Serbia.

SRBIJAGAS is a vertically integrated company in the sense of the Law, founded to conduct the business activity of transporting and managing a transmission system for natural gas, storage and managing a natural gas storage, distribution and managing a distribution system for natural gas, supply of natural gas, public supply of natural gas, heat and power cogeneration, exploration and production of natural gas, which activities it may also conduct through subsidiaries. Although SRBIJAGAS has founded subsidiaries for the business activities of transmission and distribution of natural gas, all the above activities are still conducted by SRBIJAGAS which is 100% owned by the Republic of Serbia.

The majority shareholder of South Stream AG is GAZPROM TRANSPORT KRASNODAR which was founded to conduct the business activity of pipeline transport of natural gas, as its core business activity.

GAZPROM TRANSPORT KRASNODAR is 100% owned by GAZPROM, a vertically integrated company registered for the activities of production of oil and natural gas, production of gas condensate, distribution of gas through a distribution system, supply of gas, non-specialized trade, transport of gas via pipeline and products derived by their processing.

GAZPROM subsidiaries GAZPROM EXPORT and GAZPROM Schweiz conduct the activity of foreign trade and export of natural gas.

GAZPROM and its subsidiary Centrex Europe Energy&Gas AG are the majority owners of Yugorosgaz, in which SRBIJAGAS holds 25% ownership, which was founded for the business activities of supply, public supply and distribution of natural gas, and which 100% subsidiary Yugorosgaz Transport conducts the activity of transport.

Also, GAZPROM EXPORT owns a 51% shareholding in Banatski Dvor d.o.o., which was founded for storage of natural gas, and in which the remaining 49% of shares is held by SRBIJAGAS.

Article 222 of the Law specifies that the activity of transporting natural gas and operation a transmission system for natural gas is conducted by a transmission system operator, with the rights and obligations determined by the Law.

Article 224 paragraph 1 of the Law specifies that a transmission system operator must be the owner of the transmission system.

Article 224 paragraph 2 of the Law specifies that a transmission system operator must be separate legal entity which is not part of a vertically integrated undertaking and which is independent from the conducting of the energy activities of production and supply of natural gas.

By reviewing the content of the Request for Exemption it was determined that GASTRANS d.o.o. is not requesting exemption from the obligation of applying the provisions of Article 224 paragraph 1 of the Law, as it pointed out therein its intent to acquire ownership by construction, which is indeed a condition for granting an exemption specified in Article 288 paragraph 1 item 3) of the Law.

In the Request for Exemption GASTRANS d.o.o. restricted the requested exemption from ownership unbundling solely to the obligation of applying Article 224 paragraph 2 of the Law, which specifies that a transmission system operator must be a separate legal entity which is not part of a vertically integrated undertaking and which is independent from the conducting of the energy activities of production and supply of natural gas.

Since the manner of achieving independence of a system operator is regulated in detail by Article 225 of the Law, in its Request for Exemption, GASTRANS d.o.o. points out that the exemption from the obligation of applying Article 224 paragraph 2 of the Law also presumes the exemption from the provisions regulating the manner of achieving independence of a system operator specified in Article 225 of the Law.

To ensure non-discrimination of system users, ownership unbundling requires that a legal entity may not directly or indirectly exercise control over another legal entity engaged in the production or supply of gas and at the same time directly or indirectly exercise control over a transmission system operator. Ownership unbundling exists in case of the inversion of this structure, *i.e.* when is requested nonexistence of the direct or indirect control over a transmission system operator together with the direct or indirect control over a legal entity engaged in production or supply of natural gas.

GASTRANS d.o.o. has demonstrated that the Project could not be implemented without the financial commitment - through capacity bookings and equity commitments - of shareholders that do exercise control over legal entities engaged in production or supply of natural gas. It is therefore necessary to fully exempted GASTRANS d.o.o. from these requirements. In this regard, GASTRANS d.o.o. is in the same situation as TAP, the Nabucco pipeline, the SK-HU Interconnector, or the ICGB Interconnector, all of which have been or are granted full exemption from this requirement.

Furthermore, without the request for exemption from Article 224 paragraph 2 of the Law being accepted by the Agency, the construction of the New Interconnector and its operation would be disassociated one from another. In such circumstances, GASTRANS d.o.o. would have the right to implement a part of the Project (*i.e.* to construct the New Interconnector), but not to perform the other part (*i.e.* to conduct the business activity of transport of natural gas and management of the New

Interconnector). GASTRANS d.o.o. would either be forced to transfer its ownership over the New Interconnector, or the majority share in GASTRANS d.o.o. would be transferred, to a third party (that is independent and separate in the sense of Article 224 paragraph 2 of the Law) immediately after completion of the construction. This obligation to transfer would go against the main Project parameters and would therefore result in GASTRANS d.o.o. not being able to realize the investment in the New Interconnector.

The Agency is also of the view that an exemption from this requirement should be supplemented by a methodology for shareholder capacity allocation and third party capacity allocation, as regulated in the Capacity allocation decision. This will help to ensure that production or supply related interests cannot impact the capacity allocation of GASTRANS d.o.o. and lead to discrimination, because GASTRANS d.o.o. will have to follow a regulated process which, in the view of the Agency, would result in a non-discriminatory treatment of all system users. In this regard, the requirements imposed by the Agency would go beyond the requirements set by other national regulatory agencies and the Energy Community in the case of TAP project, where the "ad-hoc ITO" conditions relating to capacity allocation were limited to requiring that all financial supervision rights were charged to a decision making body which can independently make decisions with significant impact on the value of the shareholders assets, such as the allocation of capacity on the pipeline, and that this body cannot interfere with the day-to-day activities of the company or the operation of the pipeline.

The ownership unbundling conditions under the Law also require that a legal entity is not entitled to appoint members of a board of or a body representing a transmission system operator and at the same time to directly or indirectly exercise control over an entity engaged in the supply or production of natural gas. Moreover, it requires that the same person is not entitled to be a member of a board or a body legally representing the transmission system operator or an entity performing the functions of supply or production.

The Agency is of the view that the purpose of these requirements is not to limit the GASTRANS d.o.o. shareholder or other related party control by way of appointing members in boards. Otherwise, the obligation under the Law implementing limb (b) of Article 9 (1) of the Gas Directive would be redundant, as control rights would always be exercised through decision making in corporate bodies. Rather, the purpose of this clause is to ensure that confidentiality of third party system users' information is sufficiently safeguarded and that generally dealings of the transmission system operator are conducted on a level playing field and representatives of an entity engaged in supply or production do not draw an unfair advantage from the participation in the board meetings or other representative functions.

The Agency noted that in relation to the Albanian section of the TAP pipeline, TAP AG was fully exempted from limbs (c) and (d) from Article 9 (1) of the Gas Directive, but that the Energy Community imposed the following requirements:

- the top and executive management of TAP AG will not participate in any company structures of the shareholders of TAP AG responsible for the day to day production and supply of gas;
- evidence that the professional interests of persons responsible for the management of TAP AG are taken into account in a manner that ensures that they are capable of acting independently; and

- 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.

In lieu of exemption from Article 225 of the Law (transposing limbs (c) and (d) from Article 9 (1) of the Gas Directive), GASTRANS d.o.o. submitted in the Addendum a proposal of compliance program. The Agency considers that in the context of an exempted infrastructure, the compliance program is the principle tool to ensure the confidentiality and level playing field objectives of Article 225 of the Law (transposing limbs (c) and (d) from Article 9 (1) of the Gas Directive), especially taking into account the scope of exemption regarding third party access and capacity allocation mechanisms set out by this Act and the Capacity allocation decision.

However, although the exemption from ownership unbundling under Articles 224 paragraph 2 and Article 225 of the Law is granted to GASTRANS d.o.o., such exemption cannot be granted without imposing appropriate commitments that primarily regulate the issues of confidentiality and non-discrimination.

GASTRANS d.o.o. proposed the following commitments:

- 1) GASTRANS d.o.o. to have a compliance program, in the form appended in Schedule 4 of the Addendum, monitored by a compliance officer independent of the shareholders of GASTRANS d.o.o. This, according to GASTRANS d.o.o., will ensure that commercially sensitive data about transmissions system users that is available to GASTRANS d.o.o. and/or its employees is not made available to entities performing the energy activities of natural gas production or supply;
- 2) GASTRANS d.o.o. to allocate capacity which has not been booked during the first capacity allocation resulting from the binding phase of the Market Test and which is not exempted from third party access in accordance with the procedures of the NC CAM as may be adopted in the Republic of Serbia;
- 3) GASTRANS d.o.o. to apply to the first capacity allocation resulting from the binding phase of the Market Test and subsequent capacity allocation a tariff and tariff adjustment model, using the tariff methodology, in the form appended in Schedule 2 of the Addendum;
- 4) at the start of the commercial operation, GASTRANS d.o.o. to have sufficient human, technical, physical and financial resources to operate the pipeline independently on a day to day basis;
- 5) during the construction phase of the project, and as required during the operational period, GASTRANS d.o.o. to establish and maintain a corporate decision-making body at its level or level of its sole shareholder that will exercise shareholder financial supervision rights with material impact on the value of the project's assets which will not exceed the scope set out in the current corporate documents of the GASTRANS d.o.o. and SOUTH STREAM AG; and

- 6) 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 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.

These commitments as a whole, in view of GASTRANS d.o.o., will ensure:

- 1) security 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 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 long term capacity to be book to enable the debt finance of the Project;
- 3) compliance with the general principles and practice of the national regulators and Energy Community Secretariat so far.

The Law provides for three models of organization of transmission system operators - unbundled transmission system operators (Articles 224 and 225), independent system operators (Articles 227 - 231) and independent transmission operators (Articles 232 - 238).

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. Rather, the unbundling structure in the case of an exempted new gas infrastructure should turn on the circumstances, structure and requirements of the individual case. More broadly, however, the structures and requirements can draw on decision practice of the European Commission, the Energy Community Secretariat and national regulatory authorities where circumstances are comparable. The Agency agrees with GASTRANS d.o.o. that there is not one model or consistent set of requirements in the context of an exemption and an alternative unbundling model. Reviewing the decisions in relation to TAP, Nabucco, Gazelle and SK-HU Interconnector, it is difficult to establish a consistent set of requirements that have been applied to alternative unbundling models.

The Agency also considers that unbundling requirements do not perform an isolated function, but seek to supplement other obligations of a transmission system operator to ensure non-discriminatory access to and use of transmission services and confidential treatment of information of system users.

Given the scope of the granted exemption in respect to third party access and the manner of capacity allocation set out by this Act and Capacity allocation decision, which assumes that all the

capacities will be allocated on long-term basis in the procedure govern by the Capacity allocation decision and monitored by the Agency pursuant thereto, the Agency considers that proposal of the GASTRANS d.o.o. to adopt the compliance program and to appoint a compliance officer is justified and sufficient to ensure nondiscriminatory access and confidential treatment of information in the proposed manner. In that respect, the Agency has compared and benchmarked the scope of the compliance program GASTRANS d.o.o. submitted in the Addendum against those of other exempted infrastructures and found it on par or exceeding commitments on a comparative basis.

By obliging GASTRANS d.o.o. to adopt the compliance program (Item 4 of the Act), by setting out at the same time requirements the compliance program must be complied with (Item 5 of the Act), by obliging GASTRANS d.o.o. to appoint a compliance officer (Items 4 and 6 of the Act), by setting out at the same time its authorities and conditions for the appointment in order to ensure that the compliance officer acts independently of shareholders when implementing the compliance program (Items 5 and 6 of the Act), all of it before conducting the binding phase pursuant to the Capacity allocation decision, as well as by obliging GASTRANS d.o.o. to appoint *ad hoc* body consisted of independent members to decide upon complaints of the participants in the binding phase (Item 4 of the Act), the Agency aims to ensure nondiscriminatory access and confidential treatment of information.

Equally, in case that some of the New Interconnector capacities remain unallocated on the long-term basis, which presumes that unallocated capacities will be allocated in short-term basis in line with Item 8 of this Act, outsourcing the capacity allocation function to allocation platform, can equally achieve the objective of non-discriminatory allocation of capacity, even if the new gas infrastructure is owned by shareholders that operated in the area of supply and or production of natural gas.

The Agency has also imposed restriction in Item 3 of the Act that the commercially sensitive information held by GASTRANS d.o.o. or its staff cannot be made available to undertakings performing any of the activity of 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.

Furthermore, GASTRANS d.o.o. has submitted in the Request for Exemption 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 its shareholders for these resources. However, the Agency considered that, in order to give full effect to the confidentiality, transparency and non-discrimination commitments made under the compliance program, GASTRANS d.o.o. should also be required to:

- have separate and different premises from its related parties;
- operate, from a legal and organizational perspective, separately from its related parties; and
- implement recommendations of the compliance officer.

These requirements have been reflected in Item 7 of the Act.

Having regard to the compliance program proposed by GASTRANS d.o.o. as part of its submission and the additional requirements set by Agency in Items 3 - 7, the Agency is of the view that the effect of these equal or exceed the conditions set by the Energy Community relation to the Albanian part of the TAP pipeline and that on this basis an exemption Article 225 of the Law representing limbs (c) and (d) from Article 9 (1) of the Gas Directive is proportionate and justified.

Finally, the Agency recognizes that, in case of certification of a TSO which is controlled by a person or persons from a third country or third countries, Article 245 of the Law in connection with Articles 240, 241 and 246 of the Law, transposing Article 11 (Certification Relating to Third Countries) of the Gas Directive, apply. Under this provision, the regulatory authority must refuse certification if it has not been demonstrated that the entity concerned 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).

The New Interconnector will be developed by GASTRANS d.o.o., a company controlled by Gazprom being a person from a third country for the purposes of the Articles 245 and 256 of the Law (transposing the Article 11 of the Gas Directive). This Act has granted the exemption of GASTRANS d.o.o. from the obligation of ownership unbundling. At the same time this Act has already considered the impact of the New Interconnector in relation to security of supply in the context of both the Republic of Serbia and its neighboring states and such assessment has clearly shown that the New Interconnector will promote security of supply.

GASTRANS d.o.o. will have to go through a process of certification when the New Interconnector is constructed. In relation to that, it have been assessed that in the process of certification of GASTRANS d.o.o. as the transmission system operator controlled by third country entity, the Agency shall not consider again the fulfilment of prescribed conditions of ownership unbundling and of the security of supply in relation to third countries from Articles 224, 225, 245 and 246 of the Law, as the Agency has determined by this Act, with previous obtaining of the opinion of the ministry in charge, that those conditions are fulfilled.

Exemption from third party access

GASTRANS d.o.o. has 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 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 allocation steps stated in the proposal of the Rules of Procedure for the Binding phase of allocation of capacity appended to 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.

[.....]

The Market test results demonstrate that third party transmission system users' non-binding bids together amount only to [...] in a year with maximum capacity requests, being around [...] of 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 neighboring NRAs, 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 has:

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 Schedules 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. not adopted 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 neighboring NRA 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 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 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 Duration of exemption.

The subject rule is introduced by the Agency from the following reasons. The Market test results showed that there is interest of the users for almost 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 long-term basis.

If, however, less than whole technical capacity is allocated on the long-term basis due to the lack of interest of the market participants on binding basis (as compared to non-binding basis) such remaining capacity should be allocated on short term basis.

In addition to that, in order to deal with the scenario when larger part of technical capacity is not booked on the long-term basis, the Agency has introduced the possibility for GASTRANS d.o.o. 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 non-discriminatory basis.

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 has also introduced the obligation of 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. In introducing such obligation, the Agency has taken into account that GASTRANS d.o.o. will construct completely new infrastructure, that majority of the capacity of the New Interconnector be allocated on long-term basis pursuant to this Act and the Capacity allocation decision while 10% of the capacity will be allocated on short-term basis in 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.

In addition to the Article 283 paragraph 1 of the Law, GASTRANS d.o.o. specified other provisions of the Law from the application of which it should also be exempted as a consequence of third party access, being Articles 48-57 (in particular Article 53 paragraph 1 item 4 and Article 56 paragraph 1 item 2), 228, 247, 248, 249, 254, 284, 285, 286, 291, 293 and 296 of the Law. The request by GASTRANS d.o.o. to be exempted from the cited provisions of the Law derives from the harmonization table being Appendix to the proposal of the Law, which table contains the breakdown of harmonization of particular articles of the proposal of the Law with articles of relevant EU legislation.

The Agency has assessed the request for exemption from third party access under Article 283 paragraph 1 of the Law, has adopted the request of GASTRANS d.o.o. to be exempted from third party access, and has, as detailed above, partially adopted capacity allocation mechanism proposed by GASTRANS d.o.o. Having in mind the scope of granted exemption and allocation mechanisms set out by this Act, 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:

- approve 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 transportation service in accordance with item 8 of disposition of this Act;

- procure non-discriminatory access to the transportation system determined by Article 247 of the Law, so that GASTRANS d.o.o. is entitled to procure access to the New Interconnector in accordance with item 8 of disposition of this Act;
- 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 procure access to the New Interconnector in accordance with item 8 of disposition of this Act;
- 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 will regulate these matters in compliance with this Act;
- 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 item 13) and 15) and Article 254 paragraph 1 item 17) and item 18) of the Law, except from publishing reserve (initial) price for short term capacity;
- keep records set out in Article 248 paragraph 1 item 17) of the Law;
- apply the balancing rules, as implemented 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 transportation agreements and network code provisions which may deviate from the balancing rules governed by applicable law, and
- contract the access to the New Interconnector on the basis of the agreement on access (gas transportation agreement) which contain elements prescribed by the Article 284 of the Law and network code in relation to Article 53 paragraph 1 item 4) of the Law, so that GASTRANS d.o.o. is entitled to execute the gas transportation 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 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 also in respect to terms and conditions of the for 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 party, as well as the right to amend the long-term agreement in favor 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, three gas months 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;
- 8) compliance with the transparency rules, except in the part specified in item 9 paragraph 1, point 5) of disposition of this Act.

The network code shall also be applicable to short-term capacity offered by GASTRANS d.o.o. in accordance with this Act. The agreement on short-term natural gas transmission shall be based on the principles of the agreement on long-term natural gas transmission applicable after the commercial operation date.

GASTRANS d.o.o. is also obliged to 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 addition to the above, 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 is not yet part of the legislation of the Republic of Serbia:

- 1) Commission Regulation (EU) No 312/2014 of 26 March 2014 establishing a Network Code on Gas Balancing of Transmission Networks (*NC BAL*);
- 2) Commission Regulation (EU) 2015/703 establishing a network code on interoperability and data exchange rules (implemented into the Energy Community by virtue of Decision 2018/02/PHLG-EnC, *NC IDE*);
- 3) Commission Regulation (EU) 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems (*NC CAM*); and
- 4) Commission Regulation (EU) 2017/460 establishing a network code on harmonized transmission tariff structures for gas (*NC TAR*).

NC BAL, NC IDE, NC TAR and NC CAM shall hereafter be referred to as the "EU Network Codes".

The EU Network Codes regulate in detail different aspects of third party access and tariffs but do not currently form part of the Serbian legal system. However, the Agency recognizes that, in the future, EU Network Codes may become implemented in the Energy Community and subsequently in the Republic of Serbia. The Agency is of the view that the subject matter of the EU Network Codes should be addressed by this decision rather than their treatment being subject to future implementing acts applicable in the Energy Community and/or the Republic of Serbia. Taking this approach will provide an appropriate level of regulatory certainty to GASTRANS d.o.o. and in so doing facilitate the efficient development of the New Interconnector against a known baseline. The Agency also believes that addressing these issues now is appropriate in the context of good governance, due process and transparency as to the basis on which the decision was made and what it contained. This is also beneficial for all parties interested in services of natural gas transmission i.e. future transmission system users of the New Interconnector.

The EU Network Codes contain provision on their applicability to non-exempted capacities in major new infrastructures which have received exemption from Article 32 of the Gas Directive. These provisions, according to the understanding of the Agency, mean that EU Network Codes should not apply at all to exempted capacities.

However, GASTRANS d.o.o. has presented a detailed overview setting out its view of the provisions of the EU Network Codes which:

- should not apply to GASTRANS d.o.o. and the New Interconnector as a consequence of scope of exemption requested by GASTRANS d.o.o.; and
- should apply to GASTRANS d.o.o. and the New Interconnector on the basis of them not conflicting to the scope of the exemption requested by GASTRANS d.o.o.

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, once when the

Republic of Serbia transposes said regulations, especially 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 has 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, as currently stipulated in Articles 8 – 18 of NC CAM in relation to shareholder priority capacity for the first allocation in the binding phase of the Market Test as well as for the Duration of the exemption.

The Capacity allocation decision issued by the Agency provides for a system of capacity allocation to Gastrans shareholders and their affiliates that ensures the commitment of those entities to the financing of the New Interconnector which would not otherwise be forthcoming. As the rules on the allocation of firm capacity products in the NC CAM diverge from the system of allocation set out in the Capacity Allocation Decision referred to above, it is necessary to provide an exemption from the requirements of NC CAM Articles 8 -18.

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

NC CAM does not currently apply to interconnection points that are between an EU Member State and a third country or a member of the Energy Community and an EU Member State. In addition, due to the different allocation processes, NC CAM does not provide or assume that exempted and incremental capacities are bundled. The alignment with the adjoining system operators and their respective national regulatory authorities is ongoing, all to ensure that, despite different allocations methods under the exemption (to be applied to GASTRANS) and the incremental capacity process (to be applied the adjoining system operators), the objectives of unbundling gas capacity are respected, i.e. that shareholder affiliated and third party transmission system users are in a position to book similar capacity on both sides of an interconnection point.

- 3) The rules on incremental capacity as currently stipulated in Articles 22 – 30 of NC CAM for Priority Capacity allocated post commercial operation date.

New infrastructure can be developed either as incremental capacity or as exempted new infrastructure under EU law. The New Interconnector has been granted an exemption as new infrastructure and therefore the provisions on incremental capacity naturally do not apply. It is therefore appropriate to grant an exemption in respect of these provisions.

- 4) The rules on third party trade nomination as currently stipulated in Article 4 of the NC BAL.

The New Interconnector is subject to the Capacity Allocation Decision and this regulates the allocation of short term capacity. Therefore, the provisions of NC CAM relating to interruptible short term capacity naturally do not apply. It is therefore appropriate to grant an exemption in respect of these provisions. In addition the reverse-flow aspect of the New Interconnector has not been confirmed; therefore, to the extent that the New Interconnector does not incorporate such technical features, it would be inappropriate for provisions of the NC CAM governing these activities to apply.

- 5) The rules on daily imbalance price and quantity calculation as currently stipulated in Article 20 – 22 of NC BAL.

In the absence of an exemption from this provision, GASTRANS' ability to determine appropriate project finance provisions in the gas transportation agreement terms and conditions would be restricted, thereby materially impacting the project bankability.

- 6) The rules on neutrality of cash flows as currently stipulated in Article 29 and Article 30 of NC BAL.

The application of the neutrality of cash flow provision would not be consistent with the proposed tariff model and the exemption. It would also not be consistent with the likely security package to be proposed by lenders. It would therefore be necessary to deviate from the provision to ensure the overall bankability of the gas transportation agreement. However, consultation with the Agency, transmission system users and the adjoining system operators is required in order to ensure that deviations are kept to a minimum whilst ensuring bankability of the project documentation.

- 7) The rules on credit risk management as currently stipulated in Article 31 of NC BAL.

The Agency understands that the debt-financing of the project will result in a special security package being arranged in relation to the gas transportation agreements as documents securing GASTRANS' main revenue scheme. An enhanced package will be required from shareholder affiliated transmission system users as well as third party transmission system users. This security package will in part go beyond and deviate from the credit risk management provisions of the network code. Therefore, for reasons of bankability, it is required to exempt the project fully from this provision.

- 8) The rules on cost benefit analysis assessment as currently stipulated in Article 38 of NC BAL.

The Agency notes that GASTRANS is willing to reflect the objectives of this Article at an in-principle level in its overall obligations under the gas transportation agreement. However, the Agency agrees that cost benefit analysis assessment is not consistent with the scope of the exemption in relation to the non-regulation of terms and conditions and tariffs.

- 9) The rules on linepack flexibility service as currently stipulated in Article 43 and 44 of NC BAL.

For transit pipelines like this Project is, it is not expected that balancing is going to be an issue in case of Operational Balancing Agreement. Consequently there is not going to be a need for flexibility service.

The above said restrict GASTRANS' ability to determine appropriate project finance provisions in the gas transportation agreement terms and conditions in order to promote project bankability.

Accordingly, the Agency in item 9, paragraph 2 of the disposition of this 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 has not accepted the request of GASTRANS d.o.o. for exemption from the rules on interim measures in the absence of the short-term liquidity, which rules are stipulated in the Articles 47-50 of the NC BAL 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 when they become legislation of the Republic of Serbia.

The Agency understands that, according to position of GASTRANS d.o.o., the following articles may be applicable to GASTRANS d.o.o and New Interconnector, once when they become legislation of the Republic of Serbia:

- 1) rules on principles on corporation as currently stipulated in Articles 4-7 of NC CAM;
- 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 notification 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.

In making its assessment, the Agency assessed the arguments raised by GASTRANS d.o.o. and determined that the scope of exemption from the application of the network codes is tailored to those aspects that are necessary for the purpose of exemption from third party access regulation, which, in turn, is necessary the purpose of the project implementation, so that the exemption from third party access requirements granted by this decision would not be complete (or otherwise would or could be limited) without an exemption from the application of the mentioned aspects of the EU Network Codes, once they become applicable in the Republic of Serbia. The Agency considers the arguments raised by GASTRANS d.o.o. to be well founded and finds no reason to refuse to grant or limit the exemption requested from the application of the relevant parts of the mentioned network codes (save in respect of Articles 47 - 50 of NC BAL which, as described above, has been rejected).

Exemption from regulated prices

GASTRANS d.o.o. has requested for the New Interconnector to be exempted from the application of regulated tariffs pursuant to the Article 283 paragraph 1 of the Law, which article is in

relation to 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.

Instead GASTRANS d.o.o. has applied to use an alternative tariff methodology. The decision to request the exemption and instead to use an alternative is based on that the existing regulated tariff on the one hand is not sufficient to allow for the adequate recover of investment cost associated with new infrastructure and on the other hand because regulated tariff is subject to change which makes it difficult for investment planning and the acquisition of necessary debt financing. Regarding the former, it should be stressed that the regulated tariff is designed to cover the operating cost of existing infrastructure but is limited in the guarantee and ability to recover investment cost associated with new infrastructure. The Agency agrees with the reasoning brought forward by GASTRANS d.o.o. why the regulated tariff methodology is not adequate for the New Interconnector.

The methodology in principle is designed to recover a certain needed 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. The Agency recognizes and welcomes that the methodology follows the principles of transparency and non-discrimination. Any adjustment of the Tariff methodology is performed through engagement and communication with the Agency. The methodology envisages that the tariff is applied non-discriminatory to all transmissions system users for the relevant entry and exits.

The tariff pursuant to capacity allocation is calculated for long term product on 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 a period of 365 or 366 days following the end of previous year. While the Agency requested initially the possibility to specify the year in line with financial or natural gas year, the Agency conceded to GASTRANS d.o.o. request to maintain the current structure of the year on the grounds of alignment between various associated part of the exemption and due to uncertainty 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, for an extensive elaboration of the cost factors within this definition in order to promote transparency and allow clear supervision of the formation of the necessary income. Moreover, given that for a specific year the necessary income will need to consider in many cases forecast, that the necessary income shall factor in a correction mechanism for the previous year that in the event that GASTRANS d.o.o. estimated necessary income is larger than the actual necessary income, i.e. the tariff resulted in over recovery, that this excess shall be given back to the transmission system users through lower tariffs the subsequent years, and vice versa. Accordingly the methodology in accordance with Agency's stipulation defines the necessary income for all years during which exit Horgoš is fully operational for the entire year to be the sum of operational costs, maintenance costs, costs for compensation of natural gas loss, depreciation costs, and necessary return on CAPEX. Moreover, 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 that reflects the difference between actual and estimated necessary income in the previous year.

Following 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 and GASTRANS d.o.o. agreed that this needs to be supplemented by a clear definition of the necessary return on 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.

However, the Agency recognizes in line with GASTRANS d.o.o. standing that in the years in which exit Horgoš is not fully online which is a major source of capacity and thus tariff income, that the above process for the assignment of necessary income is inadequate as it would result in significant fluctuation in tariffs. Accordingly, GASTRANS d.o.o. suggested in alignment with the Agency 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.

GASTRANS d.o.o.'s methodology envisages 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 relevant tariff for direct flow. Reverse flow would be offered to system users on interruptible basis, so it is reasonable to have a discount to a direct 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 said the above and taking into account the existing practice on European market, level of 90% seems to be reasonable.

Subsequently, the methodology calculates the tariff to be recovered via entry capacity based on contracted capacity in line with NC TAR Article 5 Paragraph 1 Subparagraph a.ii and consequently expresses the tariff due from 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 due from 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, while assigning the cost pursuant to 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 this necessity to assure the accuracy and adequacy of the recovery of necessary income and thus tariff as a matter of fairness for and between GASTRANS d.o.o. and transmission system users. Nonetheless, the Agency requires and GASTRANS d.o.o. agrees that a clear definition of the process, including time horizons need to be clarified as well as include stakeholder consultation, 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 written such that GASTRANS d.o.o. form 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 has taken 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. That is, the Agency agree to have an alternative tariff methodology but has opted to regulate the principles pursuant to which GASTRANS tariff methodology should be prepared. This decision largely reflects 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 addition to the above and as already explained in detail, in the Request for Exemption GASTRANS d.o.o. has pointed out the NC TAR which is currently in force in the European Union but which is not yet part of the legislation of the Republic of Serbia. NC TAR regulates in detail different aspects of tariffs.

The Agency recognizes that NC TAR may become implemented in the Energy Community and therefore start applying in the Republic of Serbia in the course of the Duration of the Exemption. For the purpose of full regulation of the exemption from regulated prices, as well as transparency, due process and predictability reasons, the Agency believes that the above-stated aspects need to be regulated by this decision, rather than being left for future regulation by the Agency, once NC TAR become applicable in the Republic of Serbia.

Namely, NC TAR contain 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, national regulatory authorities should have the power to grant a derogation from requirements of this Regulation which would jeopardize the efficient operation of such interconnectors. As already explained above, 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 has requested that the following articles of NC TAR are not applicable to it and to the New Interconnector:

- 1) standardized rules on cost allocation assessment, which rules are currently stipulated in Article 5 of NC TAR;
- 2) the setting of alternative price methodologies and their application to entry point and exit points, which rules are currently stipulated in Articles 6-8 and 10 and 11 of NC TAR;
- 3) standardized rules on reserve price calculation, which rules are currently stipulated in Articles 14-16 of NC TAR;
- 4) standardized rules on reconciliation of tariff revenue, which rules are currently stipulated in Articles 17-20 of NC TAR;
- 5) standardized rules on pricing of bundled capacity, which rules are currently stipulated in Article 21 of NC TAR;
- 6) standardized rules on pricing at virtual point, which rules are currently stipulated in Article 22 of NC TAR;
- 7) standardized rules on tariff clearing price calculation, which rules are currently stipulated in Article 23 of NC TAR;
- 8) standardized rules on payable price calculation, which rules are currently stipulated in Article 24 of NC TAR;
- 9) requirements to consult with network users and adjoining network operators on tariff setting, which rules are currently stipulated in Articles 26-28 of NC TAR;
- 10) standardized rules on publication requirements, which rules are currently stipulated in Articles 29-32 of NC TAR; and
- 11) standardized rules on pricing of the incremental capacity, which rules are currently stipulated in Article 33 of NC TAR.

The Agency analyzed these statements and concluded that the following obligations and principles shall not be applicable to GASTRANS d.o.o. to the extent they are or became applicable in the Republic of Serbia within the Duration of exemption as the scope of exemption from the application of regulated prices is tailored to those aspects that are necessary for the purpose of exemption from the regulated prices, which, in turn, is necessary the purpose of the project implementation:

- 1) standardized rules on cost allocation assessment, which rules are currently stipulated in Article 5 of NC TAR;
- 2) the setting of alternative price methodologies and their application to entry point and exit points, which rules are currently stipulated in Articles 6-8 and 10 and 11 of NC TAR;
- 3) standardized rules on reserve price calculation, which rules are currently stipulated in Article s14-16 of NC TAR;
- 4) standardized rules on reconciliation of tariff revenue, which rules are currently stipulated in Articles 17-20 of NC TAR ;
- 5) standardized rules on pricing of bundled capacity, which rules are currently stipulated in Article 21 of NC TAR;
- 6) standardized rules on pricing at virtual point, which rules are currently stipulated in Article 22 of NC TAR;
- 7) standardized rules on tariff clearing price calculation, which rules are currently stipulated in Article 23 of NC TAR;

- 8) requirements to consult with network users and adjoining network operators on tariff setting, which rules are currently stipulated in Articles 26-28 of NC TAR; and
- 9) standardized rules on pricing of the incremental capacity, which rules are currently stipulated in Article 33 of NC TAR.

The rationale for the Agency's approach to these issues is due to the fundamental incompatibility between NC TAR and 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 a tariff is needed that is both long term and capable of taking into consideration construction costs, overrun costs, adjustment etc. It would not be appropriate for these principles to be applicable in the case of the New Interconnector or even for them to apply to one of shareholder held capacity and third party held capacity but not the other. A common, suitable, set of principles is needed. The NC TAR is not yet applicable in Serbia in any case and retrospective application of its detailed principles could easily impact the finance-ability of the New Interconnector long after its financial underpinnings have been agreed and settled with equity and debt funders. This would be inappropriate. Instead, a methodology and an associated tariff model has been established and agreed with the Agency. This regime takes into consideration the high-level principles and objectives of NC TAR when setting the tariff principles contained within it. The Agency also notes that a number of other pipelines have obtained exemptions from NC TAR for similar reasons.

The Agency has not accepted 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 exemption granted by this Act.

In respect to the granted exemption, the Agency has also decided on the following matters:

As FEED of the pipeline is still in the course, the Agency has stipulated in item 2 paragraph 3 of disposition of this Act that in case GASTRANS d.o.o. changes 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.

As GASTRANS d.o.o. has not requested exemption from the obligation to be the owner of the New Interconnector pursuant to Article 224 paragraph 1 of the Law, the Agency has stipulated that 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.

As the Agency has granted the exemption for a period of 20 years and for the purpose of providing legal certainty over that period, the Agency has stipulated that 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 GASTRANS d.o.o. as 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.

As the Article 288 paragraph 18 of the Law prescribes that the opinion of the Energy Community is time limited and as the condition for rendering the final decision on exemption by the Agency is obtaining of the opinion of the Energy Community, the Agency has stipulated that all rights determined in this Act shall cease if GASTRANS d.o.o. does not commence construction works in relation to the New Interconnector within 2 years of the date of the final act in respect of the New Interconnector, and does not put the New Interconnector into operation within 5 years of the date of the final act.

As the Agency is obliged pursuant to Article 57, paragraph 7 of the Law to protect commercial and other confidential business data of the parties in the proceedings and as the Article 288 paragraph 3 of the Law prescribes that the act on exemption and the opinion of the Ministry of Mining and Energy shall be published in the "Official Gazette of the Republic of Serbia", the Agency has adopted the request of GASTRANS d.o.o. to protect commercial and other confidential business data from the Request for Exemption and stipulated that protected version of this Act, which does not include commercial and other confidential business data, and the opinion of the Ministry of Mining and Energy shall be published in the "Official Gazette of the Republic of Serbia" and on website of the Agency.

As the Article 141 paragraph 3 of the Law on general administrative procedure prescribes that administrative resolution must contain the decision on costs of the proceedings, the Agency has decided on the costs declaring at the same time that GASTRANS d.o.o. has on 4 July paid 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, all in line with the Law on public administrative fees ("Official Gazette of the Republic of Serbia", no. 43/2003, 51/2003 - correction, 61/2005, 101/2005 - other 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 - other 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).

As the Article 288 paragraph 10 of the Law prescribes that the act on exemption shall be submitted to the Secretariat of the Energy Community, the Agency has decided that this Act, together with other documents stipulated by Article 288 paragraph 10 of the Law, shall be submitted to the Secretariat of the Energy Community.

On the basis of stated above, it is determined that applicant' request fulfils conditions for exemption prescribed in article 288. paragraph 1. of the Law, so the Council of Energy Agency of the Republic of Serbia on 2nd extraordinary session held on October 1st, 2018, in accordance with the article 136. of Law on Administrative procedure has decided as it is determined in the disposition of this Act.

PRESIDENT OF THE COUNCIL
(L.S)
Dejan Popović (M.P)

To:

- GASTRANS d.o.o, acting through the attorney Jelena Gazivoda and Nikola Đorđević, being lawyers from Belgrade,
- Ministry of Energy and Mining
- Energy Community Secretariat, Austria, Vienna
- Archive