

15 August 2011

AMENDMENTS TO THE ELECTRICITY MARKET LICENSING REGULATION

This article provides information regarding the recent amendments to the Electricity Market Licensing Regulation¹ (the “Licensing Regulation”). The amendments were published in the Official Gazette and became effective on 11 August 2011² (the “Amending Regulation”).

I. EXECUTIVE SUMMARY

The main amendments introduced by the Amending Regulation can be summarized as follows:

- Prior to the Amending Regulation, publicly listed companies were not permitted to transfer their licenses to its fully-owned subsidiaries. The Amending Regulation, however, permits the publicly listed companies to transfer their generation and auto production licenses to its fully-owned subsidiaries upon an approval of the Board of the Energy Market Regulatory Authority (“EMRA”).
- Prior to the Amending Regulation, all share transfers under Article 47 of the Licensing Regulation were subject to the approval of the Board of EMRA. Following the Amending Regulation, the EMRA Board will approve the share transfers only for the legal entities whose tariffs are subject to regulation by EMRA (i.e., transmission, distribution, retail sale to non-eligible consumers and public wholesale activities), whereas the remaining share transfers will be evaluated and approved by the relevant department of EMRA rather than the Board.
- The definition of renewable energy resources under the Licensing Regulation has been amended and is now more consistent with the definition under the Renewable Energy Law No. 5346 (the “Renewable Energy Law”)³, except for the hydroelectric generation facilities with pumped storage, which are not expressly covered by the Renewable Energy Law. Certain provisions of the Renewable Energy Law have also been incorporated in the Licensing Regulation to ensure consistency.
- Generation facilities based on renewable energy resources now have priority over generation facilities based on domestic natural resources in terms of connection to the

¹ Published in the Official Gazette No. 24836, dated 4 August 2002.

² Published in the Official Gazette No. 28022, dated 11 August 2011.

³ Published in the Official Gazette No. 25819 dated 18 May 2005.

system. Prior to the Amending Regulation, there was no order of priority between the two.

- Prior to the Amending Regulation, generation, auto producer or auto producer group license holders who generate electricity based on renewable energy resources were permitted to purchase electrical energy from private sector wholesale companies on the condition that such amounts did not exceed the annual average generation amount of the facility stated in its license. Pursuant to the Amending Regulation, such amounts shall not exceed the difference between the annual generation amount that the facility can generate based on its current installed capacity and the actual generation amount in a calendar year.
- Generation license holders now have the right to establish (additional) generation facilities based on renewable energy resources at the same project site in order to meet the internal electricity consumption needs of the generation facility with the conditions set forth in the Amending Regulation. Such an opportunity did not exist in the prior Licensing Regulation.
- Solar power plants are now subject to the same criteria as wind power projects in terms of connection to the system. Pursuant to the Amending Regulation, the public electricity transmission company (“TEİİAŞ”) and/or the relevant distribution company shall not issue an affirmative opinion for the connection of a solar power plant to the system in a case where a connection point exists that is more appropriate and causes less system loss when compared to the demanded connection point.
- The Amending Regulation sets an installed capacity upper limit of 50 MW for each solar power plant application.

II. ANALYSIS

A. Transfer of Generation Licenses in Publicly Listed Companies

In accordance with the Licensing Regulation, the transfer of licenses is prohibited with certain exceptions (such as demerger, spin-off or step-in rights). Prior to the Amending Regulation, the Licensing Regulation did not include any provision in relation to the transfer of licenses held by publicly listed companies. Pursuant to the Amending Regulation, a generation or auto producer license of a publicly listed company may be transferred to another legal entity, 100% of the share capital of which is held by that publicly listed company, provided that the approval of the Board of EMRA is obtained. In such case, a new license as the successor of the previous license will be granted to the legal entity.

B. EMRA Approval on Share Transfers

Prior to the Amending Regulation, any approval on share transfers within the scope of Article 47 of the Licensing Regulation came under the authority of EMRA’ Board. The Amending Regulation makes a more clear distinction with respect to the approving authority on share transfers. Under the new provisions, the EMRA Board will approve the share transfers only for the legal entities whose tariffs are subject to regulation by EMRA (i.e., transmission,

distribution, retail sale to non-eligible consumers and public wholesale activities) whereas the remaining share transfers will be evaluated and approved by the relevant Department of EMRA.

C. Renewable Energy Resources

The Amending Regulation changes the scope and definition of renewable energy projects. The purpose of this amendment is to harmonize the definition of renewable energy resources with that of the Renewable Energy Law, and to ensure consistency. Pursuant to the Amending Regulation, generation facilities based on hydrogen energy are no longer encompassed by the scope of the Renewable Energy Law but stream energy has been added. Furthermore, prior to the Amending Regulation, only river and arc-type hydroelectric generation facilities with an installed capacity of 50 MW and less would qualify as generation facilities based on renewable resources. Now, pursuant to the Amending Regulation, the installed capacity threshold has been removed. In addition, prior to the Amending Regulation, hydroelectric generation facilities with a reservoir volume of less than a hundred million cubic meters or with a reservoir area of less than fifteen square kilometers would have fallen within this scope, whereas under the Amending Regulation, hydroelectric generation facilities with a reservoir area of less than fifteen square kilometers or with pumped storage qualify as renewable energy resource projects. However, please also note that hydroelectric generation facilities with pumped storage, which are currently encompassed by the Licensing Regulation via the Amending Regulation, are not defined by the Renewable Energy Law. Finally, all references to “biogas” in the Licensing Regulation have been amended to “gas that is produced from biomass (including landfill gas)”.

Another important change introduced by the Amending Regulation relates to the order of priority with regards to connection to the system. Prior to the Amending Regulation, the Licensing Regulation stated that generation facilities based on domestic natural resources and renewable energy sources would have priority in connection to the system without granting any priority between the two, which could lead to conflicts. However, the Amending Regulation clarifies this point by stating that generation facilities based on renewable energy resources will have priority over generation facilities based on domestic natural resources.

The Amending Regulation brings a number of additional provisions with respect to generation and auto producer licenses, which are summarized as follows:

- The maximum annual generation amount that a facility can generate based on its current installed capacity shall be incorporated into generation or auto producer licenses based on renewable energy resources as its annual generation amount. Such amount shall be considered as the annual average electricity generation amount. The licenses of the license holders, who apply to amend licenses in line with this provision, shall be amended accordingly within three months.
- Generation or auto producer license holders who generate electricity based on renewable energy resources may establish additional capacity provided that they stay within the site specified in their licenses, and that the power supplied to the system during operation does not exceed the installed capacity described in their licenses. This was in fact an existing provision of the Renewable Energy Law. However, the

Licensing Regulation further states that it is mandatory to amend the license for installed capacity prior to the temporary acceptance of the additional facility.

- Prior to the Amending Regulation, generation, auto producer or auto producer group license holders who generate electricity based on renewable energy resources were allowed to purchase electrical energy from private sector wholesale companies on the condition that amounts did not exceed the annual average generation amount of the facility stated in its license. Pursuant to the Amending Regulation, such amount shall not exceed the difference between the annual generation amount that the facility can generate based on its current installed capacity and the actual generation amount in a calendar year.
- All generation license holders (rather than only renewable energy companies) are now permitted to establish (additional) generation facilities based on renewable energy resources on the same project site in order to meet the internal electricity consumption needs of the generation facility provided that: (i) the additional facility shall lead to increase in productivity or shall be designed as part of the generation process, (ii) TEİAŞ and/or the distribution company shall issue an affirmative opinion for connection of the facility to the system, (iii) the generation amount shall not exceed the internal needs, and (iv) the facility shall be incorporated into the generation license.
- Lastly, in the event that forests and lands under private ownership of the Treasury, or under the control or disposal of the State, are utilized by the power plants generating electricity from renewable energy resources, which will be commissioned by 31 December 2012, 85% discount shall be applicable on permit fees, leases, easement rights and usage right amounts for the facility, connection roads and transmission lines for the first 10 (ten) year of investment and operation period. This incentive, in fact, had already been introduced by the Renewable Energy Law and is now included in the Licensing Regulation as well.

D. Solar Energy

Following the enforcement of the Solar Energy Regulation⁴, the Amending Regulation also incorporates new provisions relating to solar power plants. The regime brought by the Amending Regulation for solar power plants is very similar to that of wind farms in terms of right of access to the system under Article 38 of the Licensing Regulation. Accordingly, TEİAŞ and/or the relevant distribution companies shall not issue an affirmative opinion for the connection of a solar power plant to the system in a case where there is a connection point that is more appropriate and causes less system loss when compared to the demanded connection point. In such a case, the license application shall be rejected and the request of the license applicant legal entity for establishing a special direct line shall not be considered.

Additionally, pursuant to the Amending Regulation, the installed capacity of an application for a solar power plant shall not exceed 50 MW. Furthermore, as also contained in the

⁴ Regulation on the Electricity Generation Facilities based on Solar Energy, published in the Official Gazette No. 27969 dated 19 June 2011.

Renewable Energy Law, the total installed capacity of solar power plants holding renewable energy resource certificates, which will connect to the transmission system until 31 December 2013, shall not exceed 600 MW.

E. Research and Development Activities

The Amending Regulation sets forth provisions regarding the establishment of generation facilities within the scope of research and development activities. Pursuant to the Amending Regulation, generation activities for research and development activities shall be permitted by EMRA provided that: (i) TEİAŞ and/or the relevant distribution company give an affirmative opinion for the connection point, (ii) the electricity generated from the facility shall not be traded, (iii) the installed capacity of the facility shall not exceed 10 MW, and (iv) the legal entity shall agree that it will take necessary measures to avoid any negative impact on the grid and will indemnify EMRA for any damages of the grid. The Amending Regulation also includes provisions relating to the generation facilities to be established by universities and research centers for scientific and educational purposes. These provisions of the Amending Regulation should be read in conjunction with the general Energy Sector Research and Development Support Regulation, which was issued on 8 June 2011.⁵ ⊕

⁵ Published in the Official Gazette No. 27605 dated 8 June 2010.