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THE DRAFT ELECTRICITY MARKET LAW

This Article provides information regarding the draft Electricity Market Law (the “Draft Law”), which is intended to replace the current Electricity Market Law No. 4628¹ (the “Current Electricity Market Law”). The Draft Law has been published on the official website of the Ministry of Energy and Natural Resources, open to public comment until 23 February 2012.

The Draft Law envisages certain substantial changes in the current electricity market system, such as types of licenses, introduction of a pre-licensing process, modifications to the authorities of the Energy Market Regulatory Authority (“EMRA”), enhanced supervision over distribution companies, and extended deadlines for some incentives. Set forth below is a summary of the main features of the Draft Law:

1. Changes in the Types of Licenses and Market Activities

The Draft Law defines each electricity market activity separately and frames the remaining provisions based on such categorization rather than license types as is the case under the Current Electricity Market Law. The electricity market activities listed under Article 4 of the Draft Law are (i) generation activities, (ii) transmission activities, (iii) distribution activities, (iv) wholesale activities, (v) retail sale² activities, (vi) market operation activities, (vii) export activities, and (viii) import activities.

There are two major amendments to the types of licenses:

- (i) Auto-production, as a license type, will be abolished as of the effective date of the Draft Law. Pursuant to Temporary Article 7 of the Draft Law, auto-production license holders will be required to apply for issuance of a generation license by 31 December 2012 without being subject to any license issuance fees.
- (ii) Wholesale and retail sale activities are to be joined under one license type, namely a supply license (*tedarik lisansı*). Holders of a supply license will be entitled to perform wholesale and/or retail sale activities without being subject to any regional restrictions. Pursuant to Temporary Article 12 of the Draft Law, wholesale and retail sale license holder companies will be issued supply licenses after the effective date of the Draft Law. Additionally, the total amount of electricity supplied by a group of companies shall not exceed 20% of the total electricity supplied in Turkey.

¹ Published in Official Gazette No. 24335 (reiterated) dated 3 March 2001.

² Wholesale and retail sale licenses are collectively referred to as a supply license.

2. Electricity Market Operation Activities

Under the Draft Law, any markets which are established or may be established in the future are collectively referred to as “organized wholesale markets”. These include markets in which both the wholesale and retail sale of power, capacity or their by-products, are conducted; e.g., the day-ahead market, real time market³ (*günlü piyasa*), balancing power market, ancillary services market, over-the-counter market and by-products market.

The Draft Law introduces a new electricity market activity named “market operation”, defined in Article 11 as “*operation of organized wholesale markets and financial settlement of activities taking place in such markets*”. This activity, which is currently conducted by Electricity Market Financial Settlement Center (*PMUM*), will be conducted by Enerji Piyasaları İşletme Anonim Şirketi (“*EPIAŞ*”), to be established as a public law entity operating under a market operation license to be issued by EMRA. EPIAŞ is envisaged to operate the day-ahead market, daily market, balancing power market, ancillary services market, over-the-counter market and by-products market. The National Load Dispatch Center (*MYTM*), on the other hand, will continue its position and operations as the system operator.

3. Preliminary License

The Draft Law introduces a “preliminary license” (*ön lisans*) mechanism. Pursuant to Article 6 of the Draft Law, a preliminary license shall be granted to generation license applicants. The term of the preliminary license shall not exceed 24 months, during which applicants must obtain the relevant permits, approvals, licenses and other similar documents as well as the ownership or usufruct right of the facility area. In the event a preliminary license holder cannot fulfill the requirements within the preliminary license period, such legal entity will not be granted a generation license. The preliminary license period can be extended once, for half the preliminary license period, by EMRA.

During the preliminary license period, any direct or indirect changes in the shareholding structure, any share transfers or any transactions resulting in a share transfer (except inheritance or bankruptcy cases) or non-compliance with any requirements stipulated by EMRA shall invalidate the relevant preliminary license.

Temporary Article 11 of the Draft Law provides that generation license holders which are (i) still in their pre-construction period, or (ii) have not been able to complete the requirements of pre-construction although their pre-construction period has elapsed may apply to EMRA within one month as of the effective date of the Draft Law for issuance of a preliminary license. If a license holder described in (i) above does not apply for a preliminary license and cannot fulfill the requirements of pre-construction within one month after the effective date of the Draft Law, its generation license shall be cancelled and its performance bond forfeited. If a license holder described in (ii) above does not apply for a preliminary license within one month after the effective date of the Draft Law, its generation license shall be cancelled and its performance bond forfeited.

³ Such daily market is not defined in the Draft Law, and is currently not regulated under other relevant legislation other than the balancing power market which constitutes an example of real time balancing activities.

Pursuant to Temporary Article 14, generation license applications pending before EMRA at the effective date of the Draft Law are to be evaluated and finalized as applications for preliminary licenses.

4. Notification to EMRA for Share Transfers

Under the Current Electricity Market Law and the Electricity Market Licensing Regulation⁴, prior approval of EMRA is required for (i) transfer of 10% (5% for publicly held companies) or more of the shares of a license holder, (ii) transfer of generation facilities, and (iii) any amendment to the articles of association of all license holders.. However, Article 5(3) of the Draft Law envisages to remove such approval requirement and to provide a notification requirement for the following cases:

- Transfer of 10% (5% for publicly held companies) or more of the shares of the generation license holders,
- Changes in control of the generation license holder, and
- Any transactions resulting in a change in ownership of the generation facilities.

Additionally, the Draft Law envisages removing the requirement for EMRA approval for amendments to the articles of association of license holders.

However, legal entities whose tariffs are subject to EMRA regulation (e.g., distribution companies) are subject to approval from EMRA for transfer of 10% (5% for publicly held companies) or more of their shares, or change of their control.

5. Repayment of Investment Costs for Connection to the Grid

Pursuant to the Current Electricity Market Law, the necessary investments for transmission facilities and new transmission lines for the connection of generation facilities to the system can be made or financed jointly by the relevant legal entity(ies) requesting connection, if Türkiye Elektrik İletim Anonim Şirketi (“TEİAŞ”) or the relevant distribution company does not have the financial capability for such investments. In the Current Electricity Market Law, repayment of the total investment cost by TEİAŞ to the project company can be made either by:

- (i) cash payment in installments for a maximum period of 10 years (for facilities commissioned by 31 December 2015), or
- (ii) redemption from the transmission tariff (for facilities commissioned after 31 December 2015).

Article 8(7) of the Draft Law provides that the repayment of all such investment costs shall be made by cash installments, during a maximum period of 10 years commencing from the temporary acceptance of transmission facilities by TEİAŞ.

⁴ Published in Official Gazette No. 24836 dated 4 August 2002.

6. Provisions Specific to Distribution Companies

The Draft Law introduces a number of new provisions relating to distribution companies:

Involvement in Other Market Activities (Article 9(1)): Under the Current Electricity Market Law, generation companies cannot become shareholders in a distribution company such that they have control over the distribution company. Article 9(1) of the Draft Law envisages removing such limitation and allowing generation companies to become controlling shareholders in distribution companies. However, the same article provides that distribution companies will not be permitted to become, directly or indirectly, shareholders in any other legal entities operating in the electricity market.

Independent Board Member (Article 5(13)): According to the Draft Law, EMRA will appoint an independent member to the board of directors of distribution companies. Any lawsuit initiated against such appointed board member will be deemed to be initiated against EMRA. Accordingly EMRA, vested with a right to recourse, shall be liable for such compensation claims.

Cancellation of License (Article 29(4)): According to the Draft Law, EMRA will not be entitled to cancel distribution licenses.⁵ Instead of cancellation, in the event a distribution license holder fails to perform its material duties in accordance with the principles and procedures under the relevant legislation or impairs the quality of distribution to an intolerable level or becomes incapable of performance, the following measures, individually or collectively, may be imposed by EMRA:

- i. Appointment of a new board member replacing the current member;
- ii. If the distribution license holder fails to fulfill its obligatory services required to be performed within the scope of their tariffs, the financial burden arising out of such non-compliance shall be reimbursed from the income of the relevant company through its other operations, dividends of current shareholders and personal assets of the registered shareholders; and/or
- iii. Confiscation and transfer of shares of the license holder to the Undersecretariat of Treasury and, consecutively, transfer of the relevant distribution license to a third party meeting the requirements as stipulated by the Draft Law.

Market Share (Article 31): The total volume of power distributed by the distribution license holders within the same group of companies shall not exceed 30% of the total power distributed in all regions in the previous year.

Unbundling Requirement (Article 10(5)): The period set forth for the unbundling requirement of distribution companies, determined as 1 January 2013 and which was expected to be extended, remains as is under the Draft Law. Retail sale activities currently conducted by distribution companies shall be performed by a separate supply company to be established

⁵ Under the Current Electricity Market Law, distribution licenses can be cancelled by EMRA by taking precautionary measures and announcing a tender within 120 days for the sale of the relevant distribution facility.

with the same shareholding structure as the relevant distribution company as from 1 January 2013.

Payment of Infrastructure Construction Fees (Article 30(9)): Infrastructure works performed by transmission and distribution license holder legal entities shall be exempt from infrastructure construction fees.

7. Extended Deadlines

The deadlines for the applicability of certain incentives and other mechanisms are envisaged to be extended by the Draft Law as follows:

Incentive/Mechanism	Current Electricity Market Law	Draft Law
Price equalization mechanism	Applicable until 31 December 2012	Extended to 31 December 2015
Corporate and value added tax exemptions in transfer, merger or demergers of license holders as part of privatization processes	Applicable until 31 December 2010	Extended to 31 December 2017
50% discount on transmission system utilization fee for the first five years of operation	Applicable for power plants commissioned by 31 December 2012	Applicable for power plants commissioned by 31 December 2015
Exemption from stamp taxes and duties during the investment period	Applicable for power plants commissioned by 31 December 2012	Applicable for power plants commissioned by 31 December 2015

Incentives regarding relocation of railways, stamp tax exemption of documents prepared in relation to water utilization right agreements, interest exemption of repayments of loans arranged with the former Electricity Energy Fund remain as is under the Draft Law.

8. Grace Period for Compliance with Environmental Requirements

A grace period until 31 December 2018 will be granted to Elektrik Üretim Anonim Şirketi (“EÜAŞ”), its affiliates, subsidiaries, operation units and public generation facilities established within the scope of Privatization Implementations Law No. 4046⁶, as well as in the event of their privatization, to complete all required environmental permits under the applicable environmental legislation. This grace period is envisaged to introduce a temporary exemption until the end of 2018 for private investors which will take transfer of EÜAŞ power plants as a result of privatizations.

9. Wind and Solar Energy Applications

The current structure for wind applications (which include the TEİAŞ opinion for connection to transformers and competition among multiple applications) provided by the Current Electricity Market Law and the Regulation Regarding the Selection Process for Multiple

⁶ Published in Official Gazette No. 22124 dated 27 November 1994.

Wind Project Applications⁷ has been reflected in the Draft Law, both for wind and solar energy generation applications. Pursuant to Articles 7(5) and 7(6) of the Draft Law, standardized measuring reports prepared for a period of at least one year within the previous three years shall be submitted during the generation license application process based on wind or solar energy.

⁷ Published in Official Gazette No. 27707 dated 22 September 2010.