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Global Legal Group

The International Comparative Legal Guide to: Gas Regulation 2011

A practical cross-border insight
into Gas Regulation work

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1 Overview of Natural Gas Sector

1.1 A brief outline of Spain's natural gas sector, including a general description of: natural gas reserves; natural gas production including the extent to which production is associated or non-associated natural gas; import and export of natural gas, including liquefied natural gas (LNG) liquefaction and export facilities, and/or receiving and regasification facilities ("LNG facilities"); natural gas pipeline transportation and distribution/transmission network; natural gas storage; and commodity sales and trading.

A Legal overview

The natural gas sector in Spain has substantially changed in the last decade due to the implementation of the European directives in relation to the creation of a sole internal gas market.

The regulation of the natural gas sector in Spain is essentially contained in Law 34/1998, on hydrocarbons, dated October 7th, 1998 (the "**1998 Hydrocarbons Law**"), which implemented Directive 98/30/EC of the European Parliament and the Council. Directive 2003/55 dated June 26th, 2003 was implemented through Law 12/2007, which incorporated several changes to the 1998 Hydrocarbons Law. It should be noted that although Directive 2009/73/EC, of July 13th, concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, has not been implemented yet, the 1998 Hydrocarbons Law already applies most of its basic principles (e.g. unbundling, freedom of the consumers to choose their gas suppliers, etc.).

The Spanish regulations distinguish between regulated activities (natural gas transportation, which includes transportation, regasification and storage and distribution activities) and non-regulated activities (wholesale activities "*comercialización*"). Companies undertaking regulated activities must abide by specific regulatory requirements as further explained in sections 3 and 4 below.

The main competent bodies in Spain with regards to the natural gas sector are the Ministry of Industry, Tourism and Commerce (the "**Ministry of Industry**"), the relevant Autonomous Regions, the National Energy Commission ("**CNE**"), which is the Spanish regulator for the gas market and for the energy sector generally, and the "*Corporación de Reservas Estratégicas de Productos Petrolíferos*" or "**CORES**", which is the Spanish organisation responsible for the supervision of the accomplishment of minimum stocks duties and for managing the strategic reserves of natural gas. In addition, Enagás, S.A. ("**Enagás**"), which is the incumbent transportation company, is responsible for the management of the Spanish gas system or the System Technical Manager ("*Gestor*

Técnico del Sistema" or "**GTS**").

B Spanish Gas sector overview

Gas exploration and production activities are almost irrelevant in Spain (in 2008 less than 0.0003 % of the total gas consumption) and, therefore, the Spanish gas system relies almost entirely on imported natural gas.

The vast majority of the gas (73% of the total consumption in 2008) is introduced in Spain in the form of liquefied LNG through LNG carriers to one of the six LNG terminals currently operating (Huelva, Barcelona, Cartagena, Bilbao, Sagunto and Galicia).

In addition, there are five international pipeline connections: two connections with Portugal (through Tuy and Badajoz), one with Morocco (through Tarifa), and two with France (through Navarra and Guipúzcoa). New pipelines are expected to become fully operational shortly (Almería - Medgaz).

In 2008, the national transportation pipeline network amounted to 10,189 km, out of which Enagás owns 82%. As for the distribution network, the Gas Natural Group is the leading company owning more than 83% of the total distribution network, which amounted in 2008 to 57,935 Km.

As regards gas storage, there are only two (basic) underground gas storage ("**UGS**") facilities currently operating in Spain: (i) a depleted offshore field called Gaviota (off the Basque Coast) with a capacity of 779 Mm³(n); and (ii) a depleted field known as "*Serrablo*" located in the municipality of Huesca, with operating capacity of 890 Mm³(n). Such UGS facilities are operated by Enagás. In addition, LNG terminals also allow storage capacity (a map of the Spanish Transportation System, including, storage and regasification facilities, as of the third quarter of 2009, is available in the Spanish CNE's website: http://www.cne.es-cne-doc-consumidores-red_gas_V2_2009).

In 2008, the Spanish Government issued the 2008-2016 Energy Infrastructures Plan (this Plan has been recently modified by the Ministerial Order ITC/2906/2010, by which the Annual Programme and certain extraordinary actions to be carried out in the electricity and natural gas transportation system is approved), a mandatory plan containing the main gas transportation (and power) infrastructures to be developed in Spain. Among such projects, we would highlight the following:

- **LNG facilities:** Construction of three new LNG terminals, (Gran Canaria and Tenerife (Canary Islands) and Musel (Asturias)), which have an aggregated regasification and storage capacity of 445,000 m³.
- **Transportation pipelines:** With the aim of decreasing Spain's dependence on LNG, the 2008-2016 plan foresees several projects with respect to the pipeline network, including: (i) the duplication of the "*Euskadur*" pipeline connecting the

Spanish gas network through France to 2.5 bcm per year; (ii) the construction of a new 25 Km pipeline connecting Cataluña with France; and (iii) the construction of a pipeline connecting Spain with the Algerian fields (the Medgaz pipeline). As for the national transportation network, there is a whole plan for the development of an appropriate gas transportation network in the Canary Islands.

- **Storage facilities:** As a governmental priority, the plan contains six UGS projects, of an aggregate capacity of 3.4 bcm: (i) an aquifer under development in Yecla (Guadalajara) with an operating capacity planned to be in excess of 1 bcm (around 1,050 Mm3(n)); (ii) a project to convert a depleted offshore oil field called “Castor”, off the Castellón coast, with an operating capacity of 1,100 Mm3(n); (iii) two other projects intended to use depleted gas fields in the Southwest (known as “Marismas” and “Poseidón”), with an estimated operating capacity of 300 Mm3(n) and 250 Mm3(n), respectively; and (iv) two additional projects known as “Las Barreras” and “El Ruedo”, both former reservoirs, with an estimated operating capacity of 162 Mm3(n). However, according to the information provided in the website of the CNE, such projects have incurred significant delays in 2008.

(Figures taken from the CNE website: http://www.cne.es/cne/doc/publicaciones/PA002_09.pdf.)

1.2 To what extent are Spain’s energy requirements met using natural gas (including LNG)?

According to the information issued by the Ministry of Industry, out of the total Spanish energy requirements in 2008, 24.5% were met directly by natural gas (including LNG).

1.3 To what extent are Spain’s natural gas requirements met through domestic natural gas production?

As stated in question 1.1 above, Spain imports almost its entire national gas requirements from foreign gas producing countries. In particular, during 2008, the five principal foreign suppliers of gas were: (i) Algeria: 35% (12.3 % LNG); (ii) Nigeria: 19%; (iii) Persian Gulf: 13%; (iv) Egypt: 12.42%; and (v) Trinidad and Tobago: 11.1%. [Source: CNE].

1.4 To what extent is Spain’s natural gas production exported (pipeline or LNG)?

Spain is not a producer country. However, Spain is a transit country for gas pipelines connecting Portugal to Algeria.

2 Development of Natural Gas

2.1 Outline broadly the legal/statutory and organisational framework for the exploration and prodxuction (“development”) of natural gas reserves including: principal legislation; in whom the State’s mineral rights to natural gas are vested; Government authority or authorities responsible for the regulation of natural gas development; and current major initiatives or policies of the Government (if any) in relation to natural gas development.

As gas exploration and production activities are almost irrelevant in Spain, the main policies of the Government with respect to natural gas reserves relate to the enhancement of the security of supply and the diversification of the energy resources; one of the priorities is

the creation of UGS facilities (please refer to question 1.1 above).

In this regard, it is worth noting that the storage of gas is required in Spain not only to modulate seasonal fluctuations to the demand of gas, but also to fulfil the obligations imposed by the 1998 Hydrocarbons Law on wholesale suppliers and direct consumers in the market to maintain certain security and operating stocks (“*reservas estratégicas*” and “*reservas operativas*”) equivalent to 20 days’ worth of their firm (non-interruptible) sales or supplies, of which almost all shall be kept, by law mandate, in UGS facilities.

Although according to the Spanish law, UGS facilities are deemed to be transportation facilities and, as such, are subject to their legal regime (as explained in section 3 below), we refer in this section to some particularities regarding their legal ownership and operation regime which have certain similarities with the statutory and organisational framework foreseen in the 1998 Hydrocarbons Law for the exploration and production of gas. On the contrary, due to its limited interest for the reasons explained, we are not explaining hereunder to the exploration and production of gas.

2.2 How are the State’s mineral rights to develop natural gas reserves transferred to investors or companies (“participants”) (e.g. licence, concession, service contract, contractual rights under Production Sharing Agreement?) and what is the legal status of those rights or interests under domestic law?

Title to both offshore and onshore UGS facilities is awarded in the form of an administrative concessions (“*concesiones*”) granted by the central Government. Such administrative concessions are classified as concessions for the use of public domain assets owned by the central State (“*dominio público estatal*”).

In addition, in the case of offshore UGS projects it needs to be borne in mind that a separate concession will be required to use the coast and the beach line even if only to cross it with pipelines connecting the storage facilities to the entry and exit point.

2.3 If different authorisations are issued in respect of different stages of development (e.g., exploration appraisal or production arrangements), please specify those authorisations and briefly summarise the most important (standard) terms (such as term/duration, scope of rights, expenditure obligations).

UGS concessions are supposed to culminate a permitting process that starts with an exploration or investigation permit (“*autorización administrativa de exploración o de investigación*”). Such permits are issued by the regional governments, unless more than one region is affected or it is an offshore project, in which case the central Government is competent. The initial duration of such permits is 6 years, but a 3-year extension (with a reduction in the area covered by the permit) may be obtained.

According to the 1998 Hydrocarbons Law, UGS concessions have a maximum initial duration of thirty (30) years, but may be renewed in two periods of 10 years each. Even at the end of a concession, if a new concession is to be awarded by tender in respect of the same facilities, the former concessionaire has a preference recognised by law.

2.4 To what extent, if any, does the State have an ownership interest, or seek to participate, in the development of natural gas reserves (whether as a matter of law or policy)?

As stated, title to UGS facilities is granted by the central

Government by way of a concession for the use of public domain assets.

2.5 How does the State derive value from natural gas development (e.g. royalty, share of production, taxes)?

All hydrocarbons exploitation concessions (and consequently, the UGS concession) need to pay a certain amount (known as “*canon de superficie*” or “surface fees”) per each hectare and year comprised by the concession. The amount of the fees payable increases during the first 20 years (every 5 years) and then starts to decrease every five years. Such fees payable are set out in the 1998 Hydrocarbons Law (First Additional Provision).

2.6 Are there any restrictions on the export of production?

As a general rule, exports are free subject to the EU regulations, however, as already stated, Spain is not a gas producer country.

2.7 Are there any currency exchange restrictions, or restrictions on the transfer of funds derived from production out of the jurisdiction?

No such restrictions apply.

2.8 What restrictions (if any) apply to the transfer or disposal of natural gas development rights or interests?

A UGS concession may be assigned to a third party, but a prior authorisation from the Ministry of Industry is required.

2.9 Are participants obliged to provide any security or guarantees in relation to natural gas development?

As part of the application process of a UGS concession the applicant needs to post a guarantee to secure its compliance with its obligations and duties under the concession. Such guarantee is also expected to secure its decommissioning obligations.

2.10 Can rights to develop natural gas reserves granted to a participant be pledged for security, or booked for accounting purposes under domestic law?

Pursuant to the Spanish regulations, the works or facilities constructed over public domain plots, by virtue of a concession, may only be mortgaged as a security for the loans granted to finance such works or facilities. In all cases, a previous administrative authorisation is required. In addition, the mortgage would be cancelled upon the end of the relevant concession.

2.11 In addition to those rights/authorisations required to explore for and produce natural gas, what other principal Government authorisations are required to develop natural gas reserves (e.g. environmental, occupational health and safety) and from whom are these authorisations to be obtained?

Please refer to section 3 below in respect of the authorisation regime applicable to all transportation facilities.

2.12 Is there any legislation or framework relating to the abandonment or decommissioning of physical structures used in natural gas development? If so, what are the principal features/requirements of the legislation?

The 1998 Hydrocarbons Law provides that the application for a UGS concession already needs to incorporate a decommissioning plan and an indication of the restoration works to be undertaken. The concessionaire must fund a decommissioning provision in its accounts in an amount to be determined in the respective concession.

If a UGS concession is cancelled or annulled and the facilities need to be decommissioned (upon a prior authorisation), the prudent costs incurred in such decommissioning are treated as part of the concessionaire’s remuneration (except where the concessionaire is at fault) and the concessionaire may request an additional remuneration for the decommissioning costs (subject to audit).

Special rules on the determination of the decommissioning provision for the *Gaviota and Serrablo* UGS facilities have been issued in the Ministerial Order ITC/3802/2008.

2.13 Is there any legislation or framework relating to gas storage? If so, what are the principle features/requirements of the legislation?

As explained in question 2.1 above, UGS facilities are deemed to be transportation facilities and are subject essentially to the same legal regime explained in section 3 below although certain particularities related to TPA access apply (please refer to question 4.4 in this regard).

3 Import / Export of Natural Gas (including LNG)

3.1 Outline any regulatory requirements, or specific terms, limitations or rules applying in respect of cross-border sales or deliveries of natural gas (including LNG).

Pursuant to the 1998 Hydrocarbons Law, EU imports, exports and exchanges are free subject to EU regulations. It should be noted, however, that in Spain only wholesale suppliers and direct consumers may freely import natural gas from any country (in the case of the direct consumers, only for their own consumption). Transportation companies may only import natural gas for the purpose of filling their tanks with the minimum operating levels and the GTS may also import to comply with its duties. As distribution companies can no longer supply gas, such companies cannot buy or import gas either.

The only restriction applicable to imports of gas is the need to maintain a certain diversity of supply sources, such that the aggregate of certain imports of natural gas by wholesale suppliers from any country may not exceed 50% of the aggregate of the total imports. Furthermore, any group made up of gas suppliers and direct consumers importing over 7% of the gas quantities in Spain needs to diversify its supplies such that not more than 50% of their supplies may come from the principal supplier country to Spain (currently, Algeria). Moreover, no company or group of companies is allowed to import and sell more than 70% of the total national gas consumption.

In principle, any company introducing gas in the Spanish System for the supply of third parties would need to qualify as a wholesale supplier and, therefore, would have to comply with the technical requirements and the regulatory obligations set out in the applicable regulations (see section 6 below). On the contrary, if the gas is sold

or purchased outside the Spanish territory, to or from a Spanish-based counterparty, such gas supplier would be free to engage in the transactions without being affected by any of such obligations. This would be the case, for instance, for transactions in which the delivery of gas would take place offshore or transactions related to LNG in which a sale takes place and the title passes on or before the discharge flange connecting a vessel to the LNG facilities.

4 Transportation

4.1 Outline broadly the ownership, organisational and regulatory framework in relation to transportation pipelines and associated infrastructure (such as natural gas processing and storage facilities).

The 1998 Hydrocarbons Law defines transportation companies as the companies authorised to construct, operate and maintain LNG terminals, transportation pipelines and basic storage facilities. Further, the transportation network is deemed to comprise: (a) the primary network (“*red básica*”), which consists mainly of high-pressure pipelines (with a pressure above 60 bars), LNG terminals, basic storage facilities, compression stations, international connections to the Spanish gas system and national connections to the basic network; and (b) the secondary network (“*red secundaria*”), consisting of lower pressure pipelines (i.e.: those pipelines which have a pressure between 16 and 60 bars).

As stated in section 1, Enagás is the incumbent transportation company and, as such, the GTS. Apart from Enagás, the other main transportation companies are Gas Natural Transporte, S.A. and Naturgas Energía Transporte, S.A.

Due to the natural monopolistic characteristics of the gas networks infrastructure, gas transportation (including LNG and basic gas storage) are considered regulated activities and thus transportation companies need to comply with specific regulatory requirements (as are the distribution companies).

Among such regulatory requirements, we would highlight the obligation of having an exclusive corporate purpose and abiding by the legal and functional unbundling obligations set out by the 1998 Hydrocarbons Law. In particular, gas transportation companies may not undertake the production or supply of natural gas (classified as non-regulated activities), although the same group of companies may comprise all such activities through different subsidiaries. However, even under such circumstances (the same group of companies undertaking regulated and non-regulated activities), the 1998 Hydrocarbons Law contain additional provisions aimed at ensuring a functional separation of the different activities.

4.2 What Governmental authorisations (including any applicable environmental authorisations) are required to construct and operate natural gas transportation pipelines and associated infrastructure?

Without prejudice of the concession regime applicable to UGS (see section 2 above), the applicable regulations set forth that the construction, transfer, modification, and closing of a gas transportation facility is subject to a previous administrative authorisation (“*autorización administrativa previa*”).

To that end, a company needs to prove that it holds the required:

- “legal capacity” (formerly this was proven by becoming Spanish or EU companies, with an exclusive transportation purpose);
- “technical expertise”, which may be proven through the

submission of reports and other documentary evidence, but is also legally presumed if the company itself, directly or through an affiliate, or at least one of its shareholders with a minimum stake of 25%, has already operated transportation assets at least during the preceding three years; and

- “economic capacity” to support the financial viability of the relevant transportation project, which leaving aside other means of evidence, is deemed to be fulfilled if the company has equity resources amounting at least to Euro 5 million or 25% of the relevant transportation project budget.

In addition to the previous authorisation, the following permits must be obtained a transportation facility can enter into service: (i) the approval of the engineering construction project (“*proyecto de ejecución*”) necessary for the commencement of the works; and (ii) the final commissioning certificate (“*acta de puesta en servicio*”), without which the relevant facility cannot start its commercial operation and perceive the applicable regulated remuneration.

Such authorisations will be granted either by the Ministry of Industry, in the event that the facilities belong to the primary network or affect more than one region, or by the regional authority where the facility is to be located.

From an environmental perspective, transportation facilities may be subject to a strict environmental control by being required, in most of the cases, to obtain an integrated environmental authorisation (“*declaración de impacto ambiental*”) from the relevant authorities, before the construction work starts and to fulfil several environmental requirements.

Finally, there is a series of environmental and planning requirements and licences related to the municipal activity and operation that may be required at a municipal level.

4.3 In general, how does an entity obtain the necessary land (or other) rights to construct natural gas transportation pipelines or associated infrastructure? Do Government authorities have any powers of compulsory acquisition to facilitate land access?

The 1998 Hydrocarbon Law provides for a general recognition of gas transportation as an activity of public interest (“*actividad de interés público*”). As such, the granting of the preliminary administrative licence referred to above (or, in the case of a UGS, of an UGS concession) confers the transportation company the right to request: (i) either the expropriation of the particular land on which the transportation facility is to be constructed; or (ii) the rights of way (“*servidumbres de paso*”) and other property encumbrances imposed on the land owner in favour of the transportation company for the purposes of allowing the construction and operation of the relevant facility. In practice, in respect of underground infrastructure, the granting of rights of way is the most common mechanism to obtain access to the plots.

4.4 How is access to natural gas transportation pipelines and associated infrastructure organised?

Gas natural transportation and distribution companies must allow third party access (“*TPA*”) to the users of the gas network (i.e.: wholesale suppliers and direct consumers). TPA to gas facilities is regulated (not negotiated TPA) and is basically governed by the provisions of Royal Decree 949/2001, subsequently amended by RD 1434/2002. In particular, the TPA system is organised and supervised by the competent energy authorities (mainly the CNE and the GTS), based on mandatory tolls, charges and tariffs and standard form contracts drafted on a non-discriminatory and transparent basis.

A copy of such standard form is available at the following website: http://www.cne.es/cne/contenido.jsp?id_nodo=52&&keyword=&auditoria=F.

Certain general remarks need to be made in respect of the organisation of the TPA system and the allocation of capacity to the transportation users:

- As a general rule, capacity is allocated to the gas system's users on a "first come, first served basis" through the procedure referred to in question 4.6 below. In principle, all natural gas facilities subject to TPA need to provide for a minimum 25% of their capacity to be available for contracts with a duration not exceeding 2 years (short-term contracts). Furthermore, no single party may contract for more than 50% of such short-term capacity.
- However, in the case of (basic) UGS facilities different rules have applied since 2007. As contracting for UGS capacity is directly linked to the obligation to maintain certain minimum strategic and operating reserves (see question 2.1 above), the Spain UGS capacity is no longer booked on a first come, first served basis, but rather on an annual basis as a function of the capacity booked on the previous year. In particular, the GTS reserves certain capacity: (i) for wholesale suppliers and direct consumers (10 days' worth of sales or consumption allocated in the previous year that were destined for strategic security stocks and an additional capacity of 10 days' worth of their sales); and (ii) a capacity equivalent to 30 days' worth of consumption for consumers connected to pipelines at 4 bars or lower.
- Only to the extent that there is any UGS capacity left after the mandatory amounts have been booked, the remainder capacity will be allocated through specific auctions organised by an independent entity chosen by the GTS and supervised by the CNE (currently OMEL, the electricity market operator).
- The system is supplemented by a secondary market capacity where the entities with capacity assigned may transfer their capacity, total or partially, through a bilateral contract (except for such capacity allocated to the strategic security reserves). Even the injection and extraction rights linked to such capacity may be traded in such market.

4.5 To what degree are natural gas transportation pipelines integrated or interconnected, and how is co-operation between different transportation systems established and regulated?

As a consequence of the regulated TPA system, different regulations apply in order to ensure access to the gas transportation and distribution system and a coordinated allocation of gas storage capacity.

In addition, Spain has implemented the concept of the "Technical Manager of the System" ("GTS") (Enagás), or TSO, as defined in the Directive EC/2003/73, modelled on the lines of the "System Operator" for the electricity market. The GTS was first introduced by virtue of Royal Decree-Law 6/2000, dated 23 June, with the purpose of having an entity whose main purpose and obligations are precisely guaranteeing the continuous and secure supply of gas and ensuring a proper co-ordination among access points, storage facilities, transportation and distribution. In this regard, it should be noted that all gas agents must abide by the GTS's instructions with respect to the gas sector.

Finally, it is worth noting that the Spanish Government issued by virtue of Order ITC/3126/2005 a whole set of rules for the technical management of the system, aiming at ensuring the correct functioning of the gas system, the quality, continuity and security of

the gas supply and the co-operation between the different transportation agents ("NGTS").

4.6 Outline any third-party access regime/rights in respect of natural gas transportation and associated infrastructure. For example, can the regulator or a new customer wishing to transport natural gas compel or require the operator/owner of a natural gas transportation pipeline or associated infrastructure to grant capacity or expand its facilities in order to accommodate the new customer? If so, how are the costs (including costs of interconnection, capacity reservation or facility expansions) allocated?

Under the current regulatory framework, wholesale suppliers and direct consumers in the market are entitled to TPA to transportation and distribution facilities.

TPA rights are first exercised by filing an application for capacity with the owner of the relevant facilities through standard application forms.

A TPA application may only be refused on the basis of the following grounds:

- if there is not enough capacity available;
- if serious economic and financial difficulties would arise for the owner of the facilities under existing take-or-pay contracts (or similar contracts). If such were to be the case, the owner of the facilities will be required to file an application with the Ministry of Industry so as to evaluate the actual extent of the economic difficulties invoked; or
- if access is requested by a supplier who is resident in a country which would not provide reciprocal access to a Spanish operator.

Once a TPA request has been accepted, the parties must conclude a TPA contract within the following 24 business days. If such term has elapsed without an agreement, the applicant may have recourse to the CNE, which will provide a solution to the conflict.

As a separate issue, it should be noted that the expansion of the transportation networks is subject to the mandatory 2008-2016 Energy Infrastructure Plan referred to in section 1 above and, therefore, in Spain, as a general rule, it is not permitted to develop any transportation facilities that are not included in the plan, even if such expansion is required to attend new TPA requests. However, regular updates of the plan are contemplated such that sponsors may apply the Government for new projects to be incorporated in the plan.

4.7 Are parties free to agree the terms upon which natural gas is to be transported or are the terms (including costs/tariffs which may be charged) regulated?

As stated, TPA to gas facilities is regulated and therefore gas agents wishing to have access to a transportation facility must execute standard-form TPA agreements. Parties may be free to agree on those terms and conditions which are not regulated, provided that all users are treated on an objective, transparent and non-discriminatory basis.

In addition, it should be noted that the 1998 Hydrocarbons Law allows for new projects or capacity increases to apply to be exempt from TPA rules (in line with the rules of Article 27 of Directive 2003/55/EC and substantially in line with the rules of Article 36 of the new Directive 2009/73/EC), but to date there is no precedent yet of any such exemption having been granted in Spain.

Finally, non-basic storage is expressed to be subject to negotiated TPA. However in Spain negotiated TPA has only been provided for

access to the oil transportation and LPG facilities, but not in the natural gas industry where regulated TPA has been the standard since 1998.

5 Transmission / Distribution

5.1 Outline broadly the ownership, organisational and regulatory framework in relation to the natural gas transmission/distribution network.

The activity of gas distribution is carried out by entities transporting gas through medium and low pressure pipelines (below 16 bars) and those that distribute gas directly to a single customer from the primary and secondary transportation networks irrespective of the pressure. In addition, the Spanish system also regards as gas distribution the satellite LNG plants that supply the distribution network.

Gas Natural Group is the leading distribution company in Spain, with a market share of approximately 81.4 % in 2008. Other relevant players are Naturgas and certain Infrastructure Funds managed by Goldman Sachs (as a result of the purchase of the natural gas distribution business owned by Endesa).

Like gas transportation, the distribution of gas is considered a regulated activity and, therefore, the general requirements and obligations referred in section 4 above also apply to such companies.

In this regard, it should be noted that, since the liberalisation of the market carried out through the Law 12/2007, distribution companies can no longer supply natural. Before 30 June 2008, the Spanish natural gas retail supply market was divided between (a) a tariff-based market, and (b) the liberalised market, being both gas distribution and supply companies entitled to carry out any of such activities. However, as of 1 July 2008, the tariff-based market has been eliminated and there is only a liberalised market where gas is supplied exclusively by wholesale suppliers at free prices or by suppliers of last resort (“*comercializadores de último recurso*”), who are also wholesale suppliers, at regulated prices (please refer to section 6 below).

5.2 What Governmental authorisations (including any applicable environmental authorisations) are required to operate a distribution network?

Please refer to question 4.2.

5.3 How is access to the natural gas distribution network organised?

The TPA regime applicable to distribution facilities is essentially the same as those described in questions 4.4 to 4.7 above.

As a particularity (also applicable to the transportation pipeline network), it must be noted that the relevant user needs to execute a TPA contract with the owner of the entry point to the gas distribution and transportation system (or an intermediate delivery point). That contract needs to be supplemented through the execution of an annex for each of the delivery or exit points connecting the end consumer.

Consequently, in addition to the common requirements applicable to any formal TPA application (as described in question 4.6 above), an application for access to the network needs to contain an indication of the exit points that will initially be contracted for; and

once access is granted to the relevant distribution network, an user may change exit points provided that such user is a wholesaler and that there is enough capacity available. In such cases, the relevant TPA contract need not be modified, but only completed by means of an addendum.

5.4 Can the regulator require a distributor to grant capacity or expand its system in order to accommodate new customers?

Unlike the gas transportation network, distribution companies are obliged to expand their distribution network in the areas for which they have been issued with authorisations, when such an expansion is necessary to attend the requests from new customers to be connected, and provided that there is sufficient capacity available (for supplies below 4 bars it is by law presumed that such capacity exists if the new consumption planned does not exceed 100,000 kWh/year).

Connecting a new customer for supplies below 4 bars in a new development will be carried out at regulated prices. On the contrary, for new supplies above 4 bars, such obligation will be conditional upon reaching an agreement on the costs to be borne by the applicant for the connection.

5.5 What fees are charged for accessing the distribution network, and are these fees regulated?

In consideration for the TPA to a distribution facility, the relevant user shall pay the mandatory tariffs set out in the applicable regulations (mainly contained in Royal Decree 949/2001, of 3 August and related regulations).

Such tariffs consist mainly of: (i) a fixed charge or reservation fee (“*término de reserva de capacidad*”) paid to the owners of the entry point; and (ii) the so-called “transmission charge” (“*término de conducción*”) paid to the owners of exit points. The transmission charge varies according to the consumption of the final consumer and the design pressure of the facilities to which the final consumer is connected. In addition, the applicable tariffs are due to be revised yearly.

5.6 Are there any restrictions or limitations in relation to acquiring an interest in a gas utility, or the transfer of assets forming part of the distribution network (whether directly or indirectly)?

a) Acquisition of a stake in or by regulated companies

Pursuant to the 14th Function attributed to the CNE by the 1998 Hydrocarbons Law: (i) any company carrying out regulated activities; or (ii) any company intending to acquire a stake over 10% or any other conferring a significant influence over a company performing “regulated activities” or holding “strategic energy assets”, must hold a prior authorisation by the CNE in order to make the acquisition.

However, the prohibition referred in (ii) above was declared contrary to Article 56 of the European Treaty by the Court of Justice of the European Communities on 17 July 2008 and, therefore, although it has not been formally abrogated in Spain, it may be assumed that such provision will be no longer applicable to European companies, as the CNE has already stated in its Resolution dated 18 September 2008 issued by the CNE with regard to the acquisition of Unión Fenosa, S.A., by Gas Natural SDG, S.A.

b) Acquisition of a stake over 3% in more than one principal

operator in the gas natural sector: authorisation to exercise voting rights beyond such percentage

Article 34 of Royal Decree-Law 6/2000 provides that individuals or entities that participate, direct or indirectly, in more than 3% of more than one principal operator (“*operador principal*”) in the energy markets (including the gas market), may not exercise their voting rights exceeding the 3% threshold referred to above or to appoint directors, unless the prior authorisation of the CNE has been obtained. Such restriction would apply also to a principal operator wishing to carry out any of the aforementioned actions in respect of any other principal operator in the same market.

The principal operators are designated by the CNE, taking into account certain rules. In this regard, pursuant to two CNE’s resolutions dated 17 March 2009 and 3 July 2009, the principal operators in the natural gas market are Gas Natural Group, Iberdrola Group, Unión Fenosa Group, Endesa Group and Hidrocarbónico/EDP. However, it should be noted that Gas Natural and Unión Fenosa merged during 2009 and, therefore, belong to the same group.

c) Transfer of assets

Royal Decree 1434/2002 provides that any transfer of transportation or distribution assets (including UGS or LNG facilities) shall be previously approved by the relevant competent authority (e.g.: the Ministry of Industry or the Regional Authority, as the case may be).

6 Natural Gas Trading

6.1 Outline broadly the ownership, organisational and regulatory framework in relation to natural gas trading. Please include details of current major initiatives or policies of the Government or regulator (if any) relating to natural gas trading.

As opposed to gas transportation and distribution, natural gas trading is now a liberalised activity that may only be carried out by wholesale suppliers (“*comercializadores*”) at free prices to certain type of consumers (those acceding directly to third party gas networks or direct consumers in the market) and by suppliers of last resort (“*comercializadores de último recurso*”) at regulated prices. From 1 July 2009, such regulated prices are only available to consumers connected to pipelines at 4 bars or below and with annual consumption of less than 50,000 kWh. In 2008, the gas quantities supplied to non-regulated customers amounted to 96% of the total consumption.

As for the licensing requirements, before 28 December 2009, any company carrying out gas trading activities in Spain was required to be licensed as a wholesale supplier and have been granted with an authorisation as such. The requirements to be granted such a licence are substantially similar to those referred in question 4.2 above.

This situation has changed upon the recent enactment of Law 25/2009, dated 22 December, for free access to services activities, which implements Directive 2006/123/EC (“**Law 25/2009**”), amending the 1998 Hydrocarbons Law. In particular, pursuant to such Law, the wholesale supply licence referred to above is no any longer required and is substituted by the compliance with certain requirements, evidencing a company’s technical capacity and by imposing on such company certain reporting obligations to the Ministry of Industry. However, in the case of companies located in third countries not pertaining to the European Union in which analogous rights have not been recognised, such companies must still obtain an administrative authorisation prior to the start of their

services as supply companies in Spain.

To become a wholesale supplier, an applicant needs to submit a statement confirming it complies with the technical requirements set out and notifying the Ministry of Industry Tourism and Trade of the start of operations as a supplier. In addition, if so required by the Ministry of Industry, Tourism and Trade or the CNE, any applicant must evidence compliance with the technical requirements set out in Royal Decree 197/2010 and in further developing regulations.

To prove the satisfaction of the technical capacity requirement, applicants must have available the human and technical resources necessary to operate in the Spanish gas system in accordance with the *Normas de Gestión Técnica del Sistema and its Procolos de Detalle*.

Wholesale suppliers must post a guarantee equivalent to the payment obligations within an invoicing period to be determined. Please note that the rules to calculate the amount of such guarantee have to be developed by the Ministry of Industry, Tourism and Trade. If a wholesale supplier does not intend to supply end consumers, such guarantee will however not be necessary and the wholesale supplier will only need to post the guarantees needed for the activity (e.g. guarantee for the access to the transportation facilities).

In addition, a wholesale supplier needs to prove that it has the natural gas supply agreements necessary to meet the natural gas needs of its customers.

Statement forms to be used in the hydrocarbons sector have been published by the Resolution of the General Directorate of Energy, Policy and Mines of 3 May 2010.

Finally, any company wishing to become a last resort supplier has to be appointed as such by the Government by means of a Royal Decree.

6.2 What range of natural gas commodities can be traded? For example, can only “bundled” products (i.e., the natural gas commodity and the distribution thereof) be traded?

Natural gas products may be traded along with other products (such as electricity) by duly licensed suppliers. The following services may be traded separately: (a) supply of natural gas or LNG; (b) regasification; (c) pipeline transportation; (d) LNG or UGS storage; or (e) distribution. Even the injection and extraction rights associated to specific UGS capacity may be traded within the secondary market referred in question 4.4 above. Bundling the commodity and the use of the infrastructure (on a regulated TPA basis) would be feasible.

7 Liquefied Natural Gas

7.1 Outline broadly the ownership, organisational and regulatory framework in relation to LNG facilities.

Because of its complete dependence on gas natural imports, Spain has developed a sophisticated transportation and distribution network, which includes six LNG terminals (please refer to section 1 above for a description of such facilities). In this regard, it is especially significant that, as stated in section 1 above, out of the total national gas requirements in 2008, 73% were introduced in Spain in the form of liquefied LNG.

Enagás is the owner of the three LNG facilities located at Barcelona, Cartagena and Huelva. The other three located at Sagunto, Mugardos and Bilbao are owned by various energy

companies (e.g. Endesa).

LNG facilities are deemed to be part of the transportation system and, therefore, the legal framework explained in section 5 below is also applicable to these facilities.

7.2 What Governmental authorisations are required to construct and operate LNG facilities?

The authorisations and permits required for the construction of an LNG facility are substantially the same as those referred in question 4.2 above.

7.3 Is there any regulation of the price or terms of service in the LNG sector?

LNG facilities are considered part of the transportation network and, as such, TPA to such facilities is regulated. The price for the use of LNG facilities is also regulated through mandatory tolls and charges for regasification and LNG in-plant storage set out in the applicable regulations.

As a particular characteristic of the tolls applicable to LNG facilities, such tolls include the use of the facilities necessary for vessel discharge and for LNG transport to storage tanks, as well as a 5-day in-plant operative LNG storage (although from April 2009 users have to pay for the 5-day operational storage). In-plant stocks exceeding this operative storage are charged a specific LNG storage toll.

In addition, a common feature for regasification and transportation tolls is the fact that they allow for certain flexibility as to the actual use of capacity. As long as the maximum daily amount nominated in a relevant month does not fail to reach 85% of the total daily amount contracted for or exceed 105%, users are not penalised in terms of the applicable tolls and are charged the maximum daily amount nominated during that month. Account must be taken, at all events, of the “use it or lose it” principle.

7.4 Outline any third-party access regime/rights in respect of LNG Facilities.

The TPA regime applicable to LNG facilities is the same as that explained in questions 4.4 to 4.7 above.

8 Competition

8.1 Which Governmental authority or authorities are responsible for the regulation of competition aspects, or anti-competitive practices, in the natural gas sector?

As of 1 September 2007, all competition aspects in Spain are governed by Law 15/2007, of 3 July, on the Defence of Competition (“LDC”). The LDC foresees that antitrust rules in Spain are enforced by the National Competition Commission (“CNC”) (and, in some cases, by regional competition authorities established by the regional governments).

The CNC is an autonomous body composed of two sections: (i) the Investigation Directorate (in charge of conducting investigations on anticompetitive conducts); and (ii) the Council (that is in charge of deciding on the cases submitted by the Investigation Directorate).

Apart from the CNC, the CNE also has some competences in controlling the compliance of the Spanish competition rules within the energy sector. These competences are limited to the application

of the sectorial legislation, not the LDC.

8.2 To what criteria does the regulator have regard in determining whether conduct is anticompetitive?

The LCD reproduces almost entirely the definition of anticompetitive conducts set forth in Articles 101 and 102 of the Treaty on the Functioning of the European Union (“TFEU”) regarding restrictive practices and abuse of dominant position and, therefore, the criteria to determine whether they are in line with the EU legislation. The only exception to this rule is the fact that the LDC forbids conscious parallelism, a conduct not included within the scope of Article 101 of the TFEU.

8.3 What power or authority does the regulator have to preclude or take action in relation to anti-competitive practices?

As stated, the CNC is the main body in charge of controlling and enforcing the Spanish antitrust rules, for which purposes it is vested with broad powers, including inspection and sanctioning powers. In the exercise of these powers, the CNC may launch on-the-spot inspections or an address information request to any economic operator and to public entities. All entities are obliged to collaborate with a CNC investigation.

In addition, the CNE may initiate investigations or proceedings in order to prosecute breaches of the antitrust rules in the energy sector, including the gas sector, but it does not have the investigative and sanctioned powers vested in the CNC by the LDC.

8.4 Does the regulator (or any other Government authority) have the power to approve/disapprove mergers or other changes in control over businesses in the natural gas sector, or proposed acquisitions of development assets, transportation or associated infrastructure or distribution assets? If so, what criteria and procedures are applied? How long does it typically take to obtain a decision approving or disapproving the transaction?

Merger control in Spain is an exclusive competence of the CNC, which is responsible for deciding whether or not to clear concentrations or to subject clearance to certain conditions or commitments.

a) Spanish thresholds for mandatory filing

The LDC sets forth that concentrations that are not subject to mandatory filing pursuant to the European Merger Control Regulation should be notified to the CNC if, as a consequence of the transaction, the following thresholds are exceeded:

- a share of 30% of the national market, or of a defined geographical market within it, for a given product or service, is acquired or increased as a result of the transaction; or
- the aggregate turnover in Spain of the companies involved in the transaction exceeds EUR 240 million during the last financial year and the turnover in Spain of at least two of the parties exceeds EUR 60 million.

b) Procedural issues

In general, notifications in Spain are time-consuming, as the documentation to be submitted before the CNC is very complete and follows substantially the forms provided in the EU. However, in some cases (e.g.: none of the parties are active in the same geographic and relevant product market), the LDC allows the parties to file a simplified form.

Pursuant to the LDC, the proceeding may be resolved in one or

two phases, based on the complexity of the competition issues therein raised. In particular:

- **Phase 1:** If the operation does not raise competition concerns, the Council may authorise it within one month from filing. Failure to notify the parties of a decision within this deadline will amount to a tacit approval of the transaction.
- **Phase 2:** If the Council considers that the transaction may affect effective competition in the market, it will open the second phase of the proceedings. This second phase is longer, and includes the issuance of a statement of objections by the Investigation Directorate and even an oral hearing. The Council must take a decision on the case within two months from the opening of the second phase or the transaction will be deemed tacitly approved.

The potential antitrust concerns raised by the Investigation Directorate may be eliminated at both Phase 1 and Phase 2 if the parties propose commitments that remove these potential concerns. The Council may also impose the conditions that it considers necessary to re-establish competition in the market.

The Council of Ministers may exceptionally intervene in a merger control process in order to clear transactions that have been blocked or modify the conditions / commitments approved by the Council. The Council of Ministers can only base its intervention in grounds different from competition (generally, public interest reasons). In this case, the Council of Ministers will have one additional month to issue its final decision, after which, if no resolution has been granted, the CNC's decision will be effective.

9 Foreign Investment and International Obligations

9.1 Are there any special requirements or limitations on acquisitions of interests in the natural gas sector (whether development, transportation or associated infrastructure, distribution or other) by foreign companies?

Please refer to question 5.6 above.

9.2 To what extent is regulatory policy in respect of the natural gas sector influenced or affected by international treaties or other multinational arrangements?

Please note that international treaties, together with the EU regulations, are directly applicable in Spain.

10 Dispute Resolution

10.1 Provide a brief overview of compulsory dispute resolution procedures (statutory or otherwise) applying to the natural gas sector (if any), including procedures applying in the context of disputes between the applicable Government authority/regulator and: participants in relation to natural gas development; transportation pipeline and associated infrastructure owners or users in relation to the transportation, processing or storage of natural gas; and distribution network owners or users in relation to the distribution/transmission of natural gas.

Pursuant to the 1998 Hydrocarbons Law, the CNE has been entrusted with the role of resolving disputes in relation to the

technical management of the gas system and the exercise of TPA rights. The time conferred to the CNE to issue a resolution in relation to these matters is three months. CNE resolutions may be appealed before the Ministry of Industry and subsequently before the National High Court ("*Audiencia Nacional*").

10.2 Is Spain a signatory to, and has it duly ratified into domestic legislation: the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards; and/or the Convention on the Settlement of Investment Disputes between States and Nationals of Other States ("ICSID")?

Yes, both of them.

10.3 Is there any special difficulty (whether as a matter of law or practice) in litigating, or seeking to enforce judgments or awards, against Government authorities or State organs (including any immunity)?

In relation to this matter it should be noted that in Spain public entities would not be granted immunity for suits and, therefore, public administrations are subject to the rulings of the Courts or to arbitration awards.

This being said, it should be borne in mind that, in the principles of the Spanish 1978 Constitution (Article 132.1), there is the inability to seize assets attached to the public domain ("*inembargabilidad de los bienes de dominio público*"). Both Article 132.2 of the Spanish Constitution and Article 339 of the Spanish Civil Code provide for a broad definition of the assets which are to be considered of public domain (those expressly contemplated by law and, in any case, the maritime-terrestrial zone, beaches, territorial sea and natural resources of the economic zone and the continental platform) and therefore, it would be necessary to analyse on a case-by-case basis, depending on the public entity concerned, which of its assets would be attached to the public domain.

10.4 Have there been instances in the natural gas sector when foreign corporations have successfully obtained judgments or awards against Government authorities or State organs pursuant to litigation before domestic courts?

For the time-being, we are not aware of any particular cases, but nothing should prevent a foreign corporation from successfully obtaining a judgment against the Spanish government authorities or State organs.

11 Updates

11.1 Please provide, in no more than 300 words, a summary of any new cases, trends and developments in Gas Regulation Law in Spain.

Law 25/2009 and Royal Decree 197/2010 have facilitated the licensing of new gas suppliers with a view to increase the depth of the gas trading markets.



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