Subject: Legal questions regarding the Nord Stream II project (your note of 19.11.2015)

The Nord Stream II project foresees the construction of two additional pipelines from the Russian coast via the Baltic Sea to north-eastern Germany, parallel to the current Nord Stream I. In view of upcoming meetings and discussions regarding this project, and following our meeting on 28 October, you have requested a written opinion of the Legal Service concerning the legal framework applicable to the off-shore part of Nord Stream II.

I – Application of EU Energy law

The most important issue when examining the legal framework applicable to Nord Stream II appears to be the applicability of EU energy law, and more precisely of Directive 2009/73/EC concerning common rules for the internal market in natural gas (hereinafter the "Gas Directive") to a pipeline such as Nord Stream II, with a single entry point in a third country and a single exit point on EU territory.

In order to examine the legal situation of Nord Stream II under the Gas Directive, it is necessary to first clarify the qualification of such a pipeline.

The Legal Service shares your analysis when you conclude that Nord Stream II should be qualified as a transmission line. Indeed, it does not appear to fulfill the requirements to be qualified as an upstream pipeline as it does not link a gas production source to the transmission grid.[1] Moreover, Nord-Stream is a single line connecting two transmission

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[1] Article 2, point 2, of the Gas Directive defines an "*upstream pipeline network*" as "*any pipeline or network of pipelines operated and/or constructed as part of a (...) gas production project, or used to convey natural gas from one or more such projects to a processing plant or terminal or final coastal landing terminal*".

systems (the German and the Russian one) and does not constitute a transmission system in itself.[2]

As a transmission line which crosses a border for the sole purpose of connecting the national transmission systems of Russia and Germany, Nord Stream II possesses in principle the material characteristics of an "interconnector" as defined by Article 2, point 17, of the Gas Directive. However, by defining an interconnector as "*a transmission line which crosses or spans a border between Member States for the sole purpose of connecting the national transmission systems of those Member States*", that provision excludes a transmission line which crosses a border between a Member States and a third country.

Your note suggests that the rules of the Gas Directive applicable to the transmission of natural gas should apply to Nord Stream II, but that it should not be possible to have recourse to Article 36, which foresees the possibility to exempt major new gas infrastructures from those rules under certain conditions only in the case of interconnectors (as well as LNG and storage facilities).

The Legal Service does not share this interpretation. The Gas Directive sets up a coherent regime, where third-party access, unbundling and tariff regulation should contribute to the opening of the gas market and its liberalization while providing for the possibility to grant exemptions so as not to discourage major new investments. Applying certain rules to Nord Stream II without giving it the possibility to be exempted would depart from this coherent regime foreseen by the legislator and give that pipeline a different and less favourable treatment in comparison to a similar pipeline crossing an internal border. It would seem hard to argue that such a difference in treatment would be objectively justified. There is no indication that such a differential treatment would be the result of the deliberate will of the EU legislator. On the contrary, the fact that no possibility of exemption is foreseen for transmission lines between a Member State and a third country under Article 36 tends to confirm the interpretation that the legislator has not foreseen the application of the Directive to a pipeline crossing an external border.

It must also be noted that compliance with the Gas Directive requires action on the part of the Member States and their regulatory authorities (see, for example, Article 9 on ownership unbundling, Article 32 on third-party access, Article 33 on access to storage, and, more generally, Article 41 on the duties and powers of the regulatory authorities). In imposing duties on the relevant Member States and authorities, the Gas Directive acknowledges that the jurisdiction of the national regulatory authorities is limited and that, on cross-border issues, they need to cooperate with the authorities of other Member States (e. g. Article 34(2) on cross-border disputes concerning upstream pipeline networks and Article 42 on the regulatory regime for cross-border issues). Furthermore, cross-border coordination is an essential aim of Regulation (EC) No 715/2009 on conditions for access to the natural gas transmission networks (the "Gas Regulation").

By contrast, no provision of the Gas Directive or the Gas Regulation expressly imposes any particular obligations on Member States concerning a transmission line stretching

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[2] In accordance with Article 2, point 13, of the Gas Directive, "system" "*means any transmission networks*", and, pursuant to Article 2, point 4, of the Gas Directive, it is the task of the transmission system operator to operate, ensure the maintenance of, and if necessary, develop the transmission system in a given area, and where applicable, its interconnections with other systems. An interconnection is therefore a point where two systems meet, rather than part of an overall system.

into a third country. The silence of the Directive on that point is all the more relevant as the Directive expressly acknowledges the need to take the situation in a third country into account when it comes to ownership unbundling. A specific regime is foreseen in Article 11 on the certification of transmission system operators or transmission system owners that are controlled by persons from third countries. A look at the system set up by the Directive therefore gives the impression that it only covers the situation in a third country where it expressly so provides.

Apart from the fact that the German authorities have no jurisdiction on Russian territory, where the single entry point of Nord Stream II is located, it thus does not appear that the Gas Directive has imposed any particular obligations on those authorities in the case of a pipeline built for the exclusive purpose of transporting gas from Russia to Germany.[3]

In the absence of a clear provision in the Gas Directive requiring, for instance, a regime of third-party access, tariff regulation or ownership unbundling to be put in place for pipelines connecting Member States with third countries, one must conclude that EU law as it stands has not foreseen any mechanism that could achieve the goals of the Gas Directive with regard to such pipelines.

One may add that, even if it were possible not to apply the same legal framework to the pipeline as a whole and therefore to apply EU law until the border of EU jurisdiction and different rules on the other part of the pipeline, such partial application would, in practice, not meet the purpose of the Gas Directive (ensuring non-discriminatory access of producers to the transport network). Indeed, if Russian law is applicable at the single entry point, then an exclusive access could be given to one single producer in compliance with Russian law and, as a consequence, rules on tariffs and ownership unbundling applicable further down the pipeline where there is no access would not reach the purpose to ensure non-discriminatory access.

We are therefore in a situation of "conflict of laws", which would better be solved through international negotiations.

II - General application of EU law

Your note also raises general questions regarding the applicability of EU law to a pipeline according to its geographical situation (exclusive economic zone of a Member State, territorial waters of a Member States, and between the landing point in a Member State and the first connection to the onshore network).

From a general and abstract perspective, one can derive from the principles of EU and international law that EU law applies to the exclusive economic zone of a Member State, its territorial waters, and between the landing point in a Member State and the first connection to the onshore network.

However, the applicability of EU law depends not so much on general principles governing its territorial jurisdiction, but on the applicability of the specific provisions of secondary EU law relevant for the legal issues at stake. The limits of the applicability of

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[3] The possibility for the German regulatory authority to make available capacity for virtual reverse flow on the pipeline does not need to be taken into consideration here because the EJC has held, in Case C-198/12, *Commission v Bulgaria*, that there is no obligation under EU law to provide a virtual reverse flow transmission capacity.

the Gas Directive have been described above. The applicability of EU rules on public procurement and environment for the part of the pipeline falling under EU jurisdiction should be assessed in regard to their specific provisions, taking especially into account whether they exclude or not the possibility to be applied to projects involving a third country and whether their provisions could be, in practice, applied only to part of a pipeline without affecting the legal regime applicable to the other part.

Lastly, consideration might be given to Article 18 TFUE, which enshrines the principle of non-discrimination on grounds of nationality with the scope of application of the Treaties. However, given that EU secondary legislation on energy does not regulate the transport of gas from a third country to a Member State, the situation at hand does not fall within the scope of application of the Treaties within the meaning of Article 18 TFEU.[4]

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[4] In so far, the present situation needs to be distinguished from that underlying Case C-628/11, *Jet Management*, where the Court took the view that air transport services provided between a third country and a Member State by an air carrier holding an operating licence issued by another Member State were regulated by secondary legislation and that the fact that the air transport services concerned were provided from a third country was not such as to prevent that situation from falling within the scope of application of the Treaties within the meaning of Article 18 TFEU.