



Energetic Times in the Turkish Energy Market

The Turkish Government recognized over a decade ago that the State could not (and perhaps should not) develop sufficient energy generation capacities for Turkey's growing industries. It was clear that more private investor involvement was imperative for developing Turkey's energy market, which has been dependent on imported energy since the Republic's establishment in 1923. The liberalization process that began in 2001 was arguably successful, at least to a certain extent, and as we wrote in our article of July 2011, "Shifting Up a Gear",¹ further steps were needed for achieving the targeted liberalization. Some of these long-awaited steps have been partly taken, while some are expected in this year.

Electricity Market

Privatization and Role of the Private Sector

Since the enactment of the former Electricity Market Law in 2001, Turkey has partly achieved its aim to form a liberal, competitive and transparent electricity market. Private entities now have a substantial stake in all electricity market activities, apart from transmission. Although it took the Government eight years to successfully initiate the privatization process, since 2009, 12 out of the 20 distribution companies owned by the state distribution company, TEDAŞ, have been privatized. The privatization processes in the remaining eight distribution companies are continuing. The privatizations of four distribution companies (namely Akdeniz Elektrik Dağıtım, Gediz Elektrik Dağıtım, Aras Elektrik Dağıtım and Boğaziçi Elektrik Dağıtım) were approved by the Privatization High Council on 7 March 2013.

Akdeniz Elektrik Dağıtım² was sold to the Limak-Cengiz-Kolin Joint Venture with a bid of USD 546 million; Gediz Elektrik Dağıtım³ was sold to the Elsan-Tümaş-Karaçay Joint Venture with a bid of USD 1.23 billion; Aras Elektrik Dağıtım A.Ş.⁴ was sold to Kiler Alışveriş Hizmetleri Gıda Sanayi ve Ticaret A.Ş. with a bid of 128.5 million and, finally, Boğaziçi Elektrik Dağıtım⁵ was sold to the Limak-Cengiz-Kolin Joint Venture with a bid of USD 1.96 billion.

Of the four remaining distribution companies, Enerjisa won the tender for İstanbul Anadolu Yakası Elektrik Dağıtım,⁶ with a bid of USD 1.23 billion; Enerjisa also won the tender for Toroslar Elektrik Dağıtım,⁷ with a bid of USD 1,73 billion; the İşkaya-Doğu Joint Venture won the tender for Dicle Elektrik Dağıtım,⁸ with a bid of USD 387 million; and Türkerler

¹ <http://www.kolcuoglu.av.tr/Uploads/EBulletin/turkeyenergy.pdf>

² distributing electricity in Antalya and Isparta.

³ distributing electricity in İzmir and Manisa.

⁴ distributing electricity in Erzurum, Ağrı, Ardahan, Bayburt, Erzincan, Iğdır and Kars.

⁵ distributing electricity in the European Region of İstanbul.

⁶ distributing electricity in Anatolian Region of İstanbul.

⁷ distributing electricity in Adana, Antep, Hatay and Mersin.

⁸ distributing electricity in Diyarbakır, Urfa, Mardin and Şırnak.

İnşaat won the tender for Vangölü Elektrik Dağıtım,⁹ with a bid of USD 118 million. Following the conclusion of these eight distribution companies' privatizations, all electricity distribution companies owned by TEDAŞ will be privatized.

Subsequent to the privatization of the distribution companies, eyes have now turned to generation companies. The last days of 2012 witnessed one major electricity power plant privatization. The Seyitömer Thermal Power Plant was sold to Çelikler İnşaat for approximately USD 2.25 billion. Originally, the first state-owned generation company to be privatized was Hamitabat Elektrik. Although the Privatization Administration announced the tender of this company in 2011, the tender process was cancelled because there was only one bidder. This tender was re-announced in August 2012. While four bidders applied for preliminary qualification, after the final negotiations on 6 March 2013, Hamitabat Elektrik was sold to Limak with a bid of USD 105 million. The Turkish Competition Authority also approved the privatization of Hamitabat Elektrik.

In addition to Hamitabat Elektrik, the Kangal Thermal Power Plant was also privatized. In February 2013, the Kangal Thermal Power Plant was sold to the Konya Şeker-Siyah Kalem Joint Venture with a bid of USD 985 million.

According to the Electricity Market Sector Report pertaining to 2011, in the year 2011, 60% of the total electricity generated in Turkey by power plants were operated by private companies. Following the envisaged privatizations, the private sector's role will increase substantially. Nonetheless, the extent to which the State's role will diminish is questionable. In addition to the nuclear power plants discussed below, the Turkish Government is evidently planning to have a stake in large coal-based power plants. On 3 January 2013, Turkey and the United Arab Emirates signed an agreement for the development of coal fields in southern Turkey to generate electricity. This USD 12 billion project will be the largest Arab investment in the Turkish energy sector. According to the agreement, the coal reserves at Afşin-Elbistan, in southern Turkey, will be put to use for electricity generation.

Legislation

The New Electricity Market Law (the "**New EML**") was enacted by the Parliament and published in the Official Gazette dated 30 March 2013. The New EML envisages substantial changes in the electricity market, particularly regarding license types and licensing procedures. The New EML abolishes auto-production licenses. Accordingly, the Energy Market Regulatory Authority ("**EMRA**") will grant generation licenses to current auto-production license holders without any license fee. The New EML introduces "supply licenses", combining what used to be called a wholesale license and a retail sale license.

The New EML also introduces a "preliminary license" mechanism for generation license applicants. During the term of a preliminary license, not to exceed 24 months, generation license applicants will be required to obtain the other required permits and approvals (e.g. permits and approvals regarding the generation facility's construction) as well as ownership or usufruct rights over the relevant facility's land. This will create a more convenient licensing procedure for generation license applicants, who used to face the risk of not being granted a license but had to incur substantive costs for securing land rights and other facility permits.

⁹ distributing electricity in Bitlis, Hakkari, Muş and Van.

Another novelty of the New EML is that the state generation company, EÜAŞ, will be able to renovate or enhance the current facilities and the ones that will be acquired. Furthermore, EÜAŞ will be able to increase the capacity of the facilities and form partnerships with private-law companies for new facilities.

Recently, one of the most widely discussed topics is the formation of an Energy Exchange. Energy Minister Taner Yıldız stated in November 2012 that most of the work on the long-awaited Energy Exchange, similar to the European Energy Exchange in Germany, has been completed. The electricity market will lead the envisaged energy exchange works, which aims to combine electricity, natural gas and petroleum exchanges. The New EML introduces a new market activity, namely the "market operation activity". Accordingly, market operation activity is the (i) operation of an organized electricity wholesale market; (ii) financial settlement operations of market activities; and (iii) other financial transactions related to market activities. The market operation activity is going to be conducted by a newly established company. The company will be called Enerji Piyasaları İşletme A.Ş. (**EPIAŞ**) and will be established within six months following the enactment of the New EML. Under the New EML, EPIAŞ will be an independent company and the Istanbul Stock Exchange will be one of its shareholders.

Renewable Energy

Although Turkey has a rich renewable energy potential, most of this potential has not been utilized so far. According to EMRA's Investors Guide, the share of renewables in the power generation sector was 25.2% in 2011. However, in 2012, 78% of all new energy investments were in renewable energy facilities.

Although the long-awaited Law Amending the Law on the Utilisation of Renewable Energy Sources for the Purpose of Generating Electrical Energy (the "**Amended RES Law**") was enacted at the end of 2010, because of incentives and bureaucratic processes that are not at desired levels, private investors are not too happy with the Government's perspective of this sector.

Solar Power

2012 witnessed major legislative adoptions on solar power. On 22 February 2012, EMRA issued the Communiqué on Standards for Measurement for Wind and Solar Power License Applications. Subsequently, the Regulation on Contests for License Applications Regarding the Establishment of Solar Energy Based Generation Facilities was published in the Official Gazette on 29 May 2012.

Subsequent to the completion of these long-awaited solar power regulations, in May 2012, EMRA decided that generation license applications will be accepted between 10 and 14 June 2013. Although investors requested the postponement of the license application deadline, as of the date of this E-Bulletin there has been no news of postponement. Considering the early deadline set for the applications and the limitations imposed by the Government, there may be fewer applications than expected.

The limitations that are seen to impair the development of this sector are, generally, as follows:

- The total capacity of generation facilities based on solar power to be connected to the transmission system until 31 December 2013 cannot exceed 600 MW.

- Each license granted for a generation facility based on solar power is restricted to a maximum capacity of 50 MW.
- The total surface area that can be used for establishing a solar power plant cannot exceed 20,000 m².

Wind Power

While the developments in the solar energy sector are below expectations, there have been remarkable developments in the wind sector. According to the statistics published on the website of the Ministry of Energy, although Turkey has 48,000 MW of wind energy potential, only 1,792 MW was utilized as installed power as of the end of 2011. In 2012, the installed power has increased to approximately 2.272 MG.

Energy generation based on wind power consisted of 3% of the total electricity generation in 2012. 13% of the power plants that were put into operation in 2012 are wind-powered. In early 2012, the president of the Turkish Wind Energy Association described Turkey as potentially the largest wind market of Europe.

In the near future, while some energy companies such as RES Anatolia and Borusan EnBW are expected to build their own wind-powered plants, some other companies, like Boydak Enerji, are expected to increase their investments by acquiring existing wind-powered facilities.

Generating Electricity without License

Energy Minister Taner Yıldız has stated that as of the adoption of the Regulation on Electricity Generation without License in July 2011, more than 500 individuals and legal entities that intend to generate electricity through renewable resources without any license requirement applied to distribution companies, in accordance with the said regulation.

The New EML increases the limit of installed generation capacity for not being subject to any licensing procedure, from 500 kWh to 1 MW.

Nuclear Energy

Following the signing of an intergovernmental agreement with Russia in 2010 for the construction and operation of the Akkuyu Nuclear Power Plant, Turkey has now started to plan two more nuclear power plants. Construction of the Akkuyu Nuclear Power Plant in Mersin is expected to commence in 2014 and to be fully completed in 2023 as construction will be spread over time and completed in phases. When its construction is fully completed, the Akkuyu Nuclear Power Plant will annually generate approximately 35 GW of electricity.

On the other hand, negotiations continue for the second nuclear power plant, contemplated to be in Sinop. The Government is likely to choose between South Korea, Japan and China as its partner in connection with this project. As for the third nuclear power plant, studies have commenced. İğneada, a district of the city of Kırklareli, is likely to be the location.

Natural Gas Market

The role of natural gas in Turkey's growing energy consumption is becoming increasingly important. Natural gas is highly preferred in industrial and household consumption as well as in electricity generation. However, as a positive development, Energy Minister Taner

Yıldız stated that the share of natural gas used in electricity generation decreased to 40%, from 44% in the previous year. Since Turkey is dependent on imported natural gas, the decrease of this share and the increase of generation through renewable energy resources are positive developments.

Privatization and Role of the Private Sector

Since the liberalization process in the natural gas market has not progressed as successfully as it did in the electricity market, the legal framework continues to improve, to support this purpose. While BOTAŞ solely owns and operates the transmission system, the Ministry of Energy is working to transfer existing import contracts in accordance with Article 2 of the Natural Gas Market Law. In September 2011, the tender for the transfer of Mavi Akım gas purchase contracts, executed between Gazprom and Turkey, was cancelled on the ground that Gazprom rejected to sign the seller's consent protocol. Following the cancellation of Mavi Akım gas purchase contracts' transfer, the private sector's import from Russia, Western Natural Gas Line, where BOTAŞ's gas purchase contract expired on 31 December 2011, were brought to Ministry of Energy's agenda. EMRA granted import licenses to four companies, namely Akfel, Bosphorus Gaz, Kibar Enerji and Batı Hattı Doğalgaz, to import natural gas from the Western Natural Gas Line. On the other hand, the Russian gas company, Gazprom, acquired 60% of Avrasya Gaz A.Ş.'s shares in 2012 and strengthened its position in the Turkish gas import and wholesale markets.

As for the privatization of natural gas distribution companies, one of the largest distribution companies, Başkent Doğal Gaz Dağıtım (distributing natural gas in Ankara) was sold to Torunlar, with a bid of USD 1.162 billion and the tender process was approved by the Privatization High Council on 14 March 2013. Istanbul's distribution company, İGDAŞ, has not yet been privatized although its privatization has been on the agenda for quite some time.

The proposed amendments to the Natural Gas Market Law were made publicly available for comments until 10 October 2012. The draft amendment law sets forth new provisions for liberalizing the natural gas market. One of the key factors of liberalization of the natural gas market is the increase of number of eligible consumers, eligible to purchase natural gas from local production companies, import companies, distribution companies and wholesale companies. On 13 December 2012, EMRA adopted a decree, whereby the threshold for consumers to qualify as eligible consumers became zero. The exception to this is domestic consumers. Domestic consumers that consume at least 300,000 m³ per year will be qualified as eligible consumers. EMRA's President Hasan Köktaş stated that the long-awaited decree's purpose is to create competition in the market. As a result of this competition, eligible consumers may purchase natural gas at less than the regulated tariff prices.

BOTAŞ's Legal Structure

The proposed amendments to the Natural Gas Market Law include provisions concerning the restructuring of BOTAŞ. Accordingly, BOTAŞ will be separated into three legal entities, one for conducting transmission activities; one for operation of LNG facilities and storage activities; and the third to perform the other natural gas market activities.

LNG

Other than spot LNG imports, BOTAŞ currently imports liquefied natural gas from two countries, namely Algeria and Nigeria with long-term LNG import agreements. Turkey imports 4.4 million m³ of LNG from Algeria. According to Energy Minister Taner Yıldız,

Turkey and Algeria have agreed on the extension of the LNG import agreement for 4.4 million m³ for ten years. Before the extension, the term of the above-mentioned LNG import agreement was set to expire in 2014.

In addition, the Ministry of Energy is negotiating with Qatar regarding the importation of 6 million m³ of LNG, to diversify Turkey's natural gas sources. On the other hand, Qatar is likely to establish a new LNG facility in Turkey. The Qatar Minister of Energy and Industry has confirmed the negotiations with a Turkish company on the establishment of a LNG facility.

Petroleum Market

Privatization

The largest petroleum related deal in 2012 was the acquisition of 10.32% shares of state-owned Petkim Petrokimya Holding A.Ş. ("**Petkim**"), Turkey's only petrochemicals company. Petkim was acquired in a deal valued at USD 168 million by the State Oil Company of Azerbaijan Republic (SOCAR) which had previously acquired 51% of Petkim's shares.

Legislation

On 21 December 2012, the Prime Ministry submitted to the Turkish Parliament the bill of the new Turkish Petroleum Law (the "**Draft Petroleum Law**"). It is now being reviewed by the Parliament and is slated to be enacted in the near future. The Draft Petroleum Law will abolish the existing Petroleum Law, which was enacted in 1954.

The Draft Petroleum Law divides Turkey into two petroleum districts, namely land and maritime districts. The Draft Petroleum Law includes a provision allowing petroleum right holding companies to market and export natural gas that they have produced, to wholesale companies, export companies, distribution companies or to eligible consumers, without applying the storage related condition.

Accordingly, if an entity (regardless of being incorporated in Turkey or abroad) has a petroleum right (i.e. holds an exploration license or production lease) and produces natural gas in Turkey and wants to sell this gas to the entities mentioned above, it can be granted a wholesale license and will not be subject to any conditions regarding storage capacity.

Furthermore, under the Draft Petroleum Law, operation license holders may be granted permission for pipeline construction in order to transfer the petroleum that they have produced.

Transit Projects

Due to Turkey's geopolitical location, Turkey plays a key role in transit projects. Because of this geopolitical advantage, the number of transit petroleum and natural gas pipeline projects has increased in the past few years; and as a result so has the experience of the Ministry of Energy. After the success of the Baku-Tbilisi-Ceyhan Crude Oil Petroleum Pipeline ("**BTC**"), several natural gas transportation projects, with a purpose of bringing gas from the East (particularly Azerbaijan) to Europe, such as Nabucco, Interconnector Turkey-Greece-Italy (ITGI), the Trans-Adriatic Pipeline (TAP) and the Trans Anatolian Pipeline Project (TANAP) became widely discussed topics in Turkish as well as international media. On 26 June 2012, the governments of Turkey and Azerbaijan signed the Intergovernmental Agreement (IGA) for the construction and operation of TANAP. Attached to the IGA is a

Host Government Agreement, signed between the Government of Turkey and the TANAP Project Company. The IGA and HGA were together ratified in March 2013, thereby becoming Turkish law and thus forming a special legal regime for the TANAP Project. The TANAP Project's HGA is the first HGA in the country's history, which has been ratified as signed and subsequently published in the Official Gazette. It is clear that the Turkish Government is paying special importance to this project, which will be the longest energy pipeline in the region, being 2,000 km. TANAP is expected to significantly contribute to the energy supply security of the European Union.

All in all, 2013 will be a landmark year for Turkey's energy market, as well as its role in the international energy arena. The commencement of solar projects and the expected new wind facilities will add to Turkey's generation capacity. 2013 and 2014 will also be crucial in Turkey's development of nuclear energy. With more private sector involvement in the petroleum, electricity and gas markets, not only in upstream but also downstream, Turkey will hopefully develop into a very strong player in the world energy market. All this seems quite successful for a country that did not have an energy policy in place, just a decade ago.

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