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**Subject: State aid N 594/2009
Aid to Gaz-System S.A. for gas transmission networks in Poland**

Excellency,

The Commission wishes to inform Poland that, having examined the information supplied by your authorities on the matter referred to above, it has decided to raise no objections to the aid measure.

I. PROCEDURE

1. By electronic notification of 29 October 2009, the Republic of Poland notified the above-mentioned measure. The Commission asked additional information by a letter of 15 December 2009. The Polish authorities submitted the requested information by letter registered on 13 January 2010.

II. DESCRIPTION OF THE MEASURE

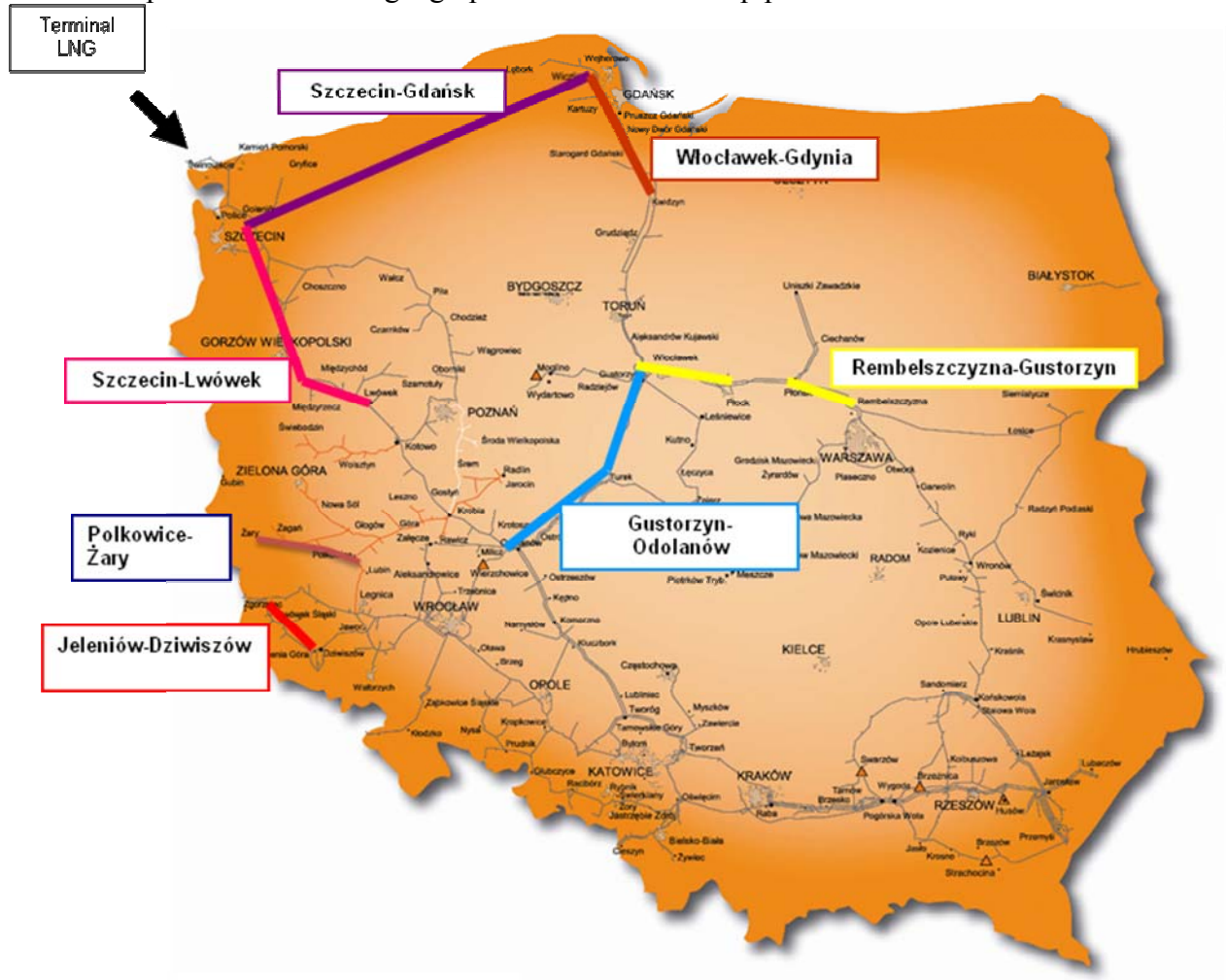
2. The aid will be granted for construction of approximately 953 km of gas pipelines to Operator Gazociągów Przesyłowych Gaz-System S.A. (Gas Transmission System Operator Gaz-System S.A., hereinafter Gaz-System) for implementation of 7 investment projects involving pipelines with equipment for the transmission of natural gas:
 - Szczecin – Gdańsk gas pipeline
 - Gustorzyn – Odolanów gas pipeline

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- Szczecin – Lwówek gas pipeline
- Rembelszczyzna – Gustorzyn gas pipeline
- Włocławek – Gdynia gas pipeline
- Jeleniów – Dziwiszów gas pipeline
- Polkowice – Żary gas pipeline.

3. The map below shows the geographical location of the pipelines.



4. Implementation of the project will contribute to the development of the Polish natural gas transmission system, to optimising its performance, and to increasing its throughput. It will also make it possible to receive gas from new sources and to transmit gas in new directions.

5. The main aims of the project are:

- improvement of energy security in Poland and in the European Union as a whole by diversifying the sources of supply for Poland and tightening the market closer with the EU market. Implementation of the aforementioned investment measures will make it possible to reverse the flow of gas, by introducing gas from the north into the gas transmission system via planned terminal for Liquid Natural Gas (LNG) and from the west via future interconnectors with other EU states.

- reduction of gas transmission losses. New pipelines will emit approximately 76% less gas as the old, existing pipelines. This will lead to a reduction of 13% of gas emissions of the total Polish gas network.
 - development of a competitive market in gas by enabling Gaz-System, at the earliest possible opportunity, to introduce the possibility of the services of a networked gas transport system that would be fully based on the provisions of access by third parties (TPA). In this way, all interested entities would have equal access to the transmission system. The TPA principle is currently only applied to a limited extent, due to the inadequate throughput of the transmission system in relation to the demand. Development of the system will increase its throughput capacity. It will also eliminate the so-called bottlenecks (locations restricting the throughput of the system). This will enable new entities dealing in gas to join the market, and thus allow competition on the network to come about.
6. A further distributional and social effect of the provision of public co-financing for the development of the transmission system is the fact that the cost of the investments will not be transferred to the consumers. According to the available calculations the gas transmission tariff would need to increase up to 43% over the next five years in the absence of aid.
 7. The beneficiary of the aid (Gaz-System) is a gas Transmission System Operator (TSO) appointed by the President of the Energy Regulatory Office (ERO) on the 18 December 2006, until 1 July 2014, i.e. for the period in which the concession will be valid. About 99.5% of its revenues are revenues from the transmission of gas.
 8. The company has been fully unbundled (legal, functional and accounting unbundling) from the mother-company PGNiG SA as a result of implementing the Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas (Gas Directive)¹.
 9. The beneficiary belongs in 100% to the Polish state. Gaz-System owns 51% of all gas transmission networks in Poland (these do not include the Jamal pipeline which is a transit pipeline). It also operates the remaining transmission networks on the basis of an operational leasing agreement of 6 July 2005 valid for 17 years with the owner of this remaining network - the PGNiG. Therefore a full ownership unbundling of the TSO will be reached when the entire gas transmission network in Poland will be owned by Gaz-System after the leasing contract is expired.
 10. Gas transmission in Poland is regulated by concessions given by the ERO. The concession fee is 0.0004% of the revenues of the preceding year of operator. The concessions can be annulled basically in cases when the operator is breaking the conditions of the concession or in cases of bankruptcy, division or mergers of the company. The concessions cannot be transferred to third parties by the network operator. Operators are subject to fines if they do not maintain the networks in required technical shape. Operators are required to estimate the fulfilment of these obligations and to report on current demand and forecast future demand for gas in annual reports. These reports are verified each year by the ERO.

¹ OJL 176, 15.07.2003

11. The concession obliges companies to transmit gas in line with the rules specified in the Energy Law of 10.04.1997². Gaz-System is required to grant access to the network on the basis of an agreement with gas supplier designed in-line with this Law. As regards the TPA rules the Energy Law implements the rules specified in the Gas Directive by requiring to ensure:
- non-discriminatory TPA to gas transmission networks for all companies allowed supplying gas in Poland,
 - providing each operator with sufficient information to allow appropriate supervision of gas transport (i.e. storage system, transmission system),
 - providing users of the system with the essential information required to ensure effective access to the system.
12. Gaz-System can deny the access to the transmission network in case of limited technical capacities of transmission. Access cannot be denied if technical possibilities of transmission exist, the supplier is legally entitled to use the transmission network, there is measurement equipment in place which measures the quantity and quality of the gas supplied and the transmission of gas will not result in an increase in tariffs of transmitted gas for other suppliers. In all cases of denying the access gas suppliers can appeal the decision to the ERO and to the administrative courts.
13. The capacity within the transmission system and on exit points is governed by the rule first-come-first-served.
14. Separate set of rules governs the access to entry points of gas to the transmission system i.e. interconnectors with Denmark, Czech Republic and Lithuania and the interconnector with the planned LNG terminal. However these rules have also an impact on the effective access to gas transmission system in Poland. The access to entry points is organised in Poland on the basis of the Open Season procedure established in line with the European Regulators' Group for Electricity and Gas (ERGEG) Guidelines of 21 May 2007³. In line with this procedure, companies receiving access to the entry points receive as first access to the transmission system in order to ensure uninterrupted flow of gas in the whole system. In case if the demand for transmission on the interconnectors is higher than the existing capacity, the capacity will be reduced "pro rata" (but not more than 10%) and with priority for agreements of higher economical value ensuring quickest returns on investments to the interconnectors. Part of the capacity i.e. 10% is also reserved for the short term agreements.
15. The prices for transmission of gas are tariffs designed in line with the rules established by the ERO and need its approval every year. The tariffs cover two types of costs:
- all substantiated costs of companies transmitting gas including costs of depreciation (40 years in case of gas transmissions networks), maintenance and development of the networks, taxes, wages etc.
 - the return on capital.

² Journal of Laws 2006 No 89

³ C06-GWG-29-05c, <http://www.ceer-eu.org>

16. The tariffs are based on the principle of covering all substantiated costs, protection of consumers against unsubstantiated increase of tariffs and avoidance of cross-subsidisation by introducing separate accounting for gas transmission transactions.
17. Tariffs cover a justified return on engaged capital of the operators. The ERO applies in respect to the TSO a calculation method where the Weighted Average Cost of Capital (WACC)⁴ is multiplied by the sum of net engaged capital and of the liquidity. The return on capital applicable to Gaz-System as of 1 June 2009 amounts to 10.8%, however the ERO limited the return to 9% in exercising its powers to limit the tariffs due to social concerns.
18. According to a special regulation applying for State –owned companies, Gaz-System is as well obliged to pay to the State 15% of its gross income.
19. The notification covers a individual projects inline with the provisions of Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999⁵, planned for implementation in the framework of the 2007-2013 Environment and Infrastructure Operational Programme (EIOP). Individual projects are investment undertakings with strategic importance for the implementation of the operational programme.
20. The co-financing agreement is signed with the beneficiary following a positive conclusion of evaluation of the application for co-financing and its annexes in line with the method for selection of individual projects was laid down in Article 21(1) of the Act of 6 December 2006 on the development policy⁶. The agreement contains a clause whereby payment of the funds is conditional upon the nature of the State aid decision of the European Commission. Any provisions related to the decision must be incorporated into the agreement and when the funding is paid to the beneficiary.
21. The maximum share of co-financing of a project under the EIOP measure in terms of eligible expenditure was established in the detailed description of EIOP priorities and may not exceed 57% of the so called "financial gap" applicable to all projects financed from Structural Funds as laid down in the Structural Funds Regulation⁷. This method limits the aid to 57% of investment costs minus all foreseeable revenues resulting from operating the infrastructure after investment. The Regulation requires that the eligible expenditure on revenue-generating projects shall not exceed the current value of the investment cost, less the current value of the net revenue from the investment over a specific reference period for investments in infrastructure or other projects where it is possible to objectively estimate the revenues in advance. In other words the aid shall be limited to these costs of the project which are not possible to be financed from the revenues resulting from implementing of the project.

⁴ The interest rates use for calculation reflect the market typical interest rates

⁵ OJ L 210, 31.7.2006

⁶ Journal of Laws No 227, entry 1658, as subsequently amended

⁷ Council Regulation (EC) 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999 (OJ L 210 of 31 July 2006, page 25)

22. According to the information provided by Polish authorities (calculations version of 15 September 2009), the cost of the individual tasks and the co-financing sought by the beneficiary are as follows⁸:

No	Project – task name	Estimated total cost (mln PLN)	Estimated value of eligible expenditure (mln PLN)	Estimated amount of co-financing (mln PLN)
1	Szczecin - Gdańsk pipeline	1 133.62	929.20	302.11
2	Gustorzyn - Odolanów pipeline	778.36	638.00	304.06
3	Szczecin - Lwówek pipeline	865.74	709.62	279.04
4	Rembelszczyzna - Gustorzyn pipeline	581.94	477.00	190.80
5	Włocławek - Gdynia pipeline	143.96	103.70	30.96
6	Jeleniów - Dziwiszów pipeline	151.53	150.00	65,10
7	Polkowice - Żary pipeline	98.82	81.00	35.64
	TOTAL	3 753.97	3 088.52	1 207.71

23. On the basis of the principles of “financial gap”, Poland approved very detailed Guidelines for beneficiaries on how the funding gap needs to be calculated in respect to the aid under the scheme. In the notified scheme, the Polish authorities explained that the aid will not be regarded as engaged capital. Therefore the aid will not generate additional revenues for beneficiary in terms of return of engaged capital. The aid is expected just to have an impact on the costs of operating the infrastructure i.e. the costs related to operation of the networks will increase as more gas will be transmitted due to the new pipelines, the costs to maintain the network, depreciation and property tax will also increase. Poland expects that due to the investments the tariff will increase because of the increase in operating costs, but it still will remain lower as in the case the aid would not be granted. Therefore, and because the aid is not regarded as engaged capital Poland argues that the aid grants no advantage to the beneficiary.

24. As all revenues of the TSO are regulated, and must receive prior approval by the ERO. The level of this revenue is determined on an annual basis, based on plans for the tariff year and results for previous years. Due to the above, results determined in the ex-ante regulated revenue are regulated in subsequent tariff years. When the project implemented by the beneficiary generates the revenue not taken into account when signing the co-financing contract, the principles of reducing co-financing or potential recovering of the funds apply. These principles are determined in Article 55.4 of Regulation No. 1083/2006 and “Guidelines on the method of making payments and settlements” issued by the Minister of Regional Development. If circumstances that might result in reducing the level of maximum co-financing for the revenue-generating project occur, the beneficiary, not later than when filing the application for the final payment and then, three years after

⁸ The differences between the estimated values given on the list and the values currently transmitted by the beneficiary are due to the updating of the financial data. The list is of an indicative nature, which means that the data it contains is estimated, and may be given more precisely at the stage of submitting applications for co-financing or when signing the agreement on co-financing. Changes may result inter alia from a final decision by the beneficiary as to the scope of the eligible expenditure to be included in the application for co financing. Another contributory factor is the updating of the cost of individual works planned to be undertaken in the framework of the project.

closing the operational programme, is obliged to notify the responsible authority of these circumstances, when necessary updating the information in this respect in accordance with the "Guidelines of the Minister of Regional Development regarding selected issue related to preparation of investment projects, including revenue-generating projects". In accordance with the Act of 30 June 2005 on public finance and the co-financing contract, the competent authority controls fulfilment of the beneficiary's duties regarding the principles of calculation, surplus control and compensation recovery. In accordance with Article 211 of the Act on public finance, when co-financing received by the beneficiary was used contrary to its purpose or with a breach of procedures applying in respect of the project implementation, or its receipt was unjustified, or the amount excessive, it should be recovered in accordance with the procedure and principles defined in the aforementioned Act. At the same time, all documents and accounting entries related to the implementation of the project are verified by competent national institutions, European Commission and European Court of Auditors. The beneficiary is obliged to ensure access to the documentation and submit to checks.

25. The overall maximum budget for this measure amounts to 1207.71 million Polish Zloty (about 300 million Euro). The aid is financed from Structural Funds of the EU within the EIOP. Poland notified the aid scheme until 31 December 2013.
26. The Polish authorities consider that this support measure does not involve State aid because it does not mainly affect competition between Member States and due to the tariff setting mechanism it does not grant an advantage to the beneficiary.

III. ASSESSMENT

Existence of State aid and legality

27. Article 107(1) of the Treaty provides that "*any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, shall, in so far as it affects trade between Member States, be incompatible with the common market*".
28. The aid is granted from State resources within the meaning of Article 107(1) of the TFEU because the transfer of Structural Funds resources is subject to the discretion of Poland
29. As regards the presence of an economic advantage to beneficiaries of the scheme the Commission considered the following elements:

Advantage to the operator

30. The supply of gas is regulated in Poland via concession contracts with the Gaz-System TSO owning or leasing the network. The profits for the TSO taking into account investment needs and the tariffs for gas transmission are under the control of the public authorities i.e. independent ERO. Therefore the authorities are able to control the benefits which the beneficiary is receiving when operating the transmission network.
31. The networks are natural monopolies: it is economically and technically inefficient to construct separate networks. As it is normally economically inefficient to have two networks serving the same geographical area, regulation is the only way to prevent

excessive monopolies rents for the services provided. Furthermore, pursuant to energy internal market legislation⁹, network operator do not have control over their customers portfolio (as the networks are subject to stringent third party access rules) and prices charged to network users are subject to strict regulatory monitoring: regulatory authorities must define tariff-setting methodologies or set tariffs themselves in a way which allows necessary investments to be carried out to ensure the viability of the network. Due to the natural monopoly character of gas transmission networks, it is likely that the regulatory authorities will in the future continue to be able to control the benefits which the network operator receives.

32. The amount of subsidy is calculated on the basis of the method of "funding gap" which ensures that only those investments costs will be financed by aid which will not be covered by any benefits generated by the operation of the improved network. Such approach aims to keep the tariffs for transmission and the operator's profits on the same level as if the part of the investment financed by the aid would not be realised. Therefore the measure will enable operator to continue to provide transmission services of gas for affordable prices to residential users and businesses, despite the investments in extension of networks.
33. Furthermore the method to calculate the tariff ensures that the investment subsidy will not increase the engaged capital on basis of which the remuneration of the operator is calculated.
34. However, the method of calculating the tariff lead to an increase of revenues of the Gaz-System operator as its operating costs will increase. Among those operating costs, depreciation will increase to the extent to cover also the new infrastructure generating additional revenues to Gaz-System.
35. The investments will take place without an engagement of capital of Gaz-System which normally would need to take place when the investments would need to be financed without aid. Therefore Gaz-System can benefit to an extent of opportunity costs of the capital that it would otherwise need to finance the investments without the aid. In addition, as the gas transmission systems belong to Gaz-System, Gaz-System will obtain additional assets in its position. Although the assets financed by the aid will not be treated as engaged capital and therefore will not be a basis of an increase in tariffs, Gaz-System will become owner of assets which it would be able to use e.g. as a collateral to obtain credits from the banks.
36. In the view of the direct benefits to Gaz-System in form of additional revenues covering full depreciation and in form of avoided costs of capital that would need to be used if the investments would not be financed without the aid he aid will give a direct advantage within the meaning of Article 107(1) of the TFEU, to the beneficiary of the aid. As the financing by the State of a particular investment is considered conferring an advantage and this advantage is only granted to Gaz-System, that advantage is selective.

⁹ Directive 2003/54/EC of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC (OJ L 176 of 15.07.2003, page 37) and Directive 2003/55/EC of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC (OJ L 176 of 26 June 2003, p. 57).

Distortion of competition – affectation of intra Community trade

37. The market for transmission of gas is by definition bound to the location of the network and therefore local by nature. In the same vein, it should be noted that networks designed for the transmission of energy to the population in a given area, just as electricity and natural gas transmission networks, exhibit the properties of local "natural monopolies". It means that in cases when a network exists, it would be very unlikely that it would be economical to duplicate the network by creating a new one, even if of a much better quality than the existing one. In the case at hand a new transmission systems will be created in areas where no such networks exists. As soon as the envisaged investments will be finalised the properties of the "natural monopolies" will prevent other companies to invest in pipelines in the same regions. Therefore the contemplated subsidies may deter other companies to invest themselves in the envisaged new gas transmission networks currently because the aid is granted, and in the future when the pipelines will exercise the properties of a "natural monopoly". .
38. As the Polish gas market is currently suffering of lack of competition what is partially due to the lack of gas transmission networks allowing flow of gas from west to east and from the new LNG terminal, it is likely that the new investments will attract new suppliers of gas from other EU and non-EU States to use these networks to enter the gas market and operate in Poland. Therefore constructing of the new networks will give some suppliers of gas indirect benefits of increased sales to the new customers. Therefore the aid is likely to affect competition on the downstream markets of gas in Poland to the benefit of the new entries to the market. This is also the declared aim of the measure as explained by Poland.
39. As gas is traded between Member States in the EU and the new pipelines are likely to attract gas flows from the west to the east and from the new LNG terminal, it is likely that the trade between Member States will be affected.
40. Gaz-System is receiving 99.5% of its revenues from transmission of gas in Poland. Due to legal provisions aiming to prevent cross-subsidisation and separate accounts introducing transparency, it is unlikely that the aid will distort competition on other markets then gas-transmission on which Gaz-System is active and receives 0.5% of its revenues.

Conclusion on existence of the aid

41. Taking the above into consideration the Commission concludes that the measure involves State aid within the meaning of Article 107 (1) of the TFEU.
42. By notifying the aid measure, the Polish authorities have complied with Article 108(3) of the TFEU.

Compatibility under Article 107(3)(c) of the TFEU

43. As regards support for gas infrastructure, aid for such projects does not fall within the scope of the 2008 Environmental Aid Guidelines¹⁰.

¹⁰ OJ C 82 of 01.04.2008

44. The Commission notes that the measure aims to modernise gas transmission networks in Poland with no prospect for modernising the networks on regular commercial conditions i.e. financed from the tariffs, in the near and medium term. The Commission also notes that the measure does not fall under one of the existing frameworks and guidelines. The areas covered by the measure are all located within areas eligible under the European Regional Development Fund, as well as Article 107 (3) (a) assisted areas within the meaning of the Guidelines on national regional aid for 2007-2013 (hereafter Regional Aid Guidelines (RAG))¹¹.
45. However, the regional aid is designed to contribute to regional development by supporting investment and job creation. It promotes the expansion and diversification of the economic activities of enterprises located in the less-favoured regions, in particular by encouraging firms to set up new establishments there. In the case at hand neither job creation nor setting up new establishment are the main objective of the aid. As stated by Polish authorities and assessed below, the main objective of the aid is the development of the Polish system for the transmission of natural gas and in this way contributing to the creation of the basic infrastructure for the operation of the internal market in natural gas and increased energy security in the European Union. . The Commission therefore considers that the assessment of the compatibility of the measure with the common market requires an assessment of the contribution of the measure to the development of the European Union market for gas and the contribution to the security of supply of the European Union and needs a wider basis for assessment as the RAG and therefore needs to be based directly on Article 107(3)(c) which states that: “*aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest*” may be considered to be compatible with the common market.
46. In order to be compatible under Article 107(3)(c), an aid must pursue an objective of common interest in a necessary and proportionate way. In this regard, the Commission considers it appropriate to assess the following questions:
- (1) Is the aid measure aimed at a well-defined objective of common interest (i.e. does the proposed aid address a market failure or another objective of common interest)?
 - (2) Is the aid well designed to deliver the objective of common interest? In particular:
 - (a) Is the aid measure an appropriate instrument, i.e. are there other, better-placed instruments?
 - (b) Is there an incentive effect, i.e. does the aid change the behavior of firms?
 - (c) Is the aid measure proportional, i.e. could the same change in behavior be obtained with less aid?

¹¹ OJ C 54, 4.3.2006, p. 13

- (3) Are the distortions of competition and the effect on trade limited, so that the overall balance is positive?

Objective of Common Interest

47. As further documented below, the aid measure has to aim at a well-defined objective of common interest. An objective of common interest is an objective which has been recognised by the EU as being in the common interest of the EU Member States.
48. Gas pipelines created in the framework of the Environment and Infrastructure Operational Programme – the 10.1 measure contribute to the development of the Polish system for the transmission of natural gas. They increase the system's efficiency by increasing its capabilities, thus ensuring greater security of supply. These pipelines also make a key contribution to the promotion of the interest of the European Union, which may be defined as the creation of the basic infrastructure for the operation of the internal market in natural gas and increased energy security. This becomes evident in the context of development plans for inter-system connections between different Member States. Implementation of the investment covered by the present notification is essential for the:
- Inter system connection between Poland and the Czech Republic,
 - Baltic inter system link/Baltic Interconnection, Skanled Baltic Pipe,
 - Development of the transmission system in the Lasow region (Poland-Germany connection).
49. The connection between Poland and Czech Republic is part of the development of the preferred trans-European link on the North South axis. Furthermore, it will open up the possibility of a link between the Polish transmission network and the Baumgarten hub. Ultimately, it could be possible to connect to the Nabucco gas pipeline, which is significant in terms of the functioning of the internal market in gas in both countries. The Danish and Polish transmission systems must be redeveloped in order to allow the flow of gas from Denmark to Poland, and reverse flow from Poland to Denmark. Bearing in mind recent gas crises (winters of 2006 and 2009), the integration the Polish and German transmission networks, will make a significant contribution to improving security, diversification and ensuring stable supplies of gas to end users in Poland.
50. The development of transmission pipelines has latterly been defined as an EU interest in high number of documents and legal provisions issued by the European Union institutions. In the "Communication from the Commission to the European Council and the European Parliament – an energy policy for Europe"¹² the Commission references to the construction of new gas pipelines, notably to set up new hubs in the Baltic countries in order to increase security of supply by diversifying the connections with other EU Member States.
51. The Gaz-System projects have strategic value not only for Poland, but also as alternative elements of the system linking the markets of European Member States in the Baltic region and for eliminating bottlenecks. The rationale for implementation of these projects is therefore in line with the provisions of the "Communication from the Commission – Green Paper – towards a secure, sustainable and competitive European energy network"¹³,

¹² COM(2007) 1

¹³ COM(2008)782 of 13 November 2008

52. The construction of strategic gas pipelines is further justified in the context of the provisions of the Decision No 1364/2006/EC of the European Parliament and of the Council of 6 September 2006, laying down guidelines for trans European energy networks and repealing Decision 96/391/EC and Decision No 1229/2003/EC establishes the priorities for trans European energy networks.
53. The proposed gas pipelines constructed by Gaz System S.A. come under the priorities laid down in the framework of European Commission Communication of July 2008 concerning Second Strategic Energy Review (SER2). Most importantly, strengthening the transmission system in North West Poland will prepare the way for potential connections on the East West axis with the Baltic States. In addition, this work will allow the transfer of significant quantities of gas from a new source of supply, namely the LNG terminal at Świnoujście. Therefore the investment in the infrastructure used for the transport of fuel regasified at the LNG terminal in Świnoujście is consistent with the second of the aforementioned priorities.
54. Furthermore, the development of the North South transport axis in Poland will ensure the fulfilment of the SER2 priority concerning the integration of the markets of Northern Europe and Scandinavia with Central and Southern Europe. This will open up new possibilities for the development of the market and will increase security of supply at regional and Community level.
55. Furthermore the measure at hand aims at increasing primary energy savings by reducing transmission losses of gas of the overall gas transmission network in Poland. The new pipelines supported with aid have by 76% less gas losses as those normally existing in Poland. Therefore if part of the gas normally transmitted in Poland will be using the new pipelines the overall gas losses of the total transmission system will fall by 13%.
56. Pursuant to the Gas Directive, TSOs are required to develop the transmission system notably as regards throughput of their reciprocal interconnectors. In addition, the Member States must ensure access to the transmission system for third parties. In the context of such requirements, implementation of the aforementioned Gaz-System's investments may be perceived as compliance with the duties imposed on Poland under these provisions. Indeed the full implementation of the provisions of the Gas-Directive, notably the third party access to the gas transmission infrastructure strengthens the EU dimension of the envisaged investments.
57. In this respect the Commission notes that the benefiting company has been fully unbundled (legal, functional and accounting unbundling) from the mother-company PGNiG SA in order to implement the provision of Gas Directive in respect to transmission of gas. Furthermore Poland implemented the provisions of the Gas Directive regarding the third party access rules to transmission pipelines. Access cannot be denied if technical possibilities of transmission exist, the supplier is legally entitled to use the transmission network, there is measurement equipment in place which measures the quantity and quality of the gas supplied and the transmission of gas will not result in an increase in tariffs of transmitted gas for other suppliers. In all cases of denying the access gas suppliers can appeal the decision to the ERO and to the administrative courts. These provisions seem to ensure that the rights of gas companies to access the gas transmission network in Poland are satisfied.

58. The capacity within the transmission system and on exit points is governed by transparent rule of first-come-first-served. Separate set of rules governs the access to entry points of gas to the transmission system. However these rules are organised in Poland on the basis of the Open Season procedure established in line with the European Regulators' Group for Electricity and Gas (ERGEG) Guidelines of 21 May 2007¹⁴.
59. It can thus be concluded that the Polish scheme aims at a well-defined objective of common interest.
60. The project was included in the list pursuant to the procedures in force in the framework of the 2007-2013 Environment and Infrastructure Operational Programme, and comply with the conditions for assistance laid down in the Detailed Description of Priorities for the aforementioned programme.

Appropriate Instrument

61. With regard to the present scheme Polish authorities pointed out that the Gaz-System is obliged by Law to develop the network. However as the TSO is constrained in its investment decisions by the capital which it has at its disposal, in order to fulfil its obligations in transmitting gas it can postpone the investments necessary from the national and EU policy interests, to the future. Imposing any legal obligation to realise the investments at hand could only be financed via an increase in tariffs for gas transmission as any investments in infrastructure realised by a network operator can only be financed from tariffs. This would in turn increase prices for gas for consumers, which has been considered to be socially unacceptable.
62. Financing of construct 953 km of new pipelines would require increase in tariffs for transmission of gas by up to 43% over the five years period if the investments would be financed by the TSO. Polish authorities argue that, at present, such increase in tariffs is uneasy from the social point of view in particular as, according to Poland, the transmission tariffs in Poland are among the highest within the EU. Indeed the whole territory of Poland, entirely qualifies as an assisted region under the derogation laid down in Article 107(3)(a) of the TFEU, in conformity with the regional aid map for Poland¹⁵ with an Gross Domestic Product per capita in Purchasing Power terms is below 75% of EU average and the average costs of gas in the households budgets amounts to ca 11%. Therefore the investments being in line with the EU energy policy would not be realised by the TSO in the foreseeable future and currently can only be achieved with the assistance of aid.
63. Consequently, the Commission considers that State aid is an appropriate instrument to achieve investments in transmission system network in Poland in the case at hand.

Incentive Effect

64. As further shown below, the aid granted for the envisaged measures provides the necessary incentive effect. State aid provides an incentive effect if the aid changes the recipients' behaviour towards reaching the objective of common interest. According to the

¹⁴ C06-GWG-29-05c, <http://www.ceer-eu.org>

¹⁵ State Aid N 531/2006 – Poland – Regional aid map for 2007-2013.

Polish authorities the system of calculating the tariffs for transmission of gas does not provide enough incentives for the Gaz-System to invest in extension of the gas transmission network in the next future. This is because the investments to construct 953 km of new pipelines are major investments changing the whole networks system. To finance such investments the TSO would need to increase significantly the engaged capital, far above the "business as usual" maintenance costs. According to the tariff setting mechanism in order to receive remuneration on such increase engaged capital the tariff would need to increase to a level which is unacceptable for the regulator from social point of view. Therefore, as the regulator would prevent increase in tariffs to match the costs of investments, companies would not be able to cover these costs of the investments, at least not in the next future. It follows that in order to achieve the security of supply and energy saving effects the foreseen investments can only be financed by a support from the State.

65. Therefore it can be concluded that the scheme will provide for the necessary incentive effect.

Proportionality

66. A State aid measure is proportional if the measure is designed in a way that the aid as such is kept to the minimum and if the beneficiaries are selected in a non-discriminatory, transparent and open process. As regards proportionality of the aid, the amount of the aid will be calculated on the basis of the "funding gap" i.e. all the benefits which can be predicted for the lifetime of the project will be deducted from the aid and will be financed by the operator. Such contribution of the beneficiary goes beyond the timeframe of the non applicable Environmental Aid Guidelines which require deducting benefits calculated in the first 5 years only. Moreover as there is only one TSO in Poland the choosing Gaz-System as beneficiary cannot discriminate against other potential beneficiaries. Furthermore comprehensive mechanism is put in place to ensure that the benefits are properly calculated any surpluses are controlled and recovered if they arise unduly.
67. Poland presented as well the preliminary calculations of the aid intensities of the concrete investment projects. According to the calculations of 15 September 2009, the intensity of co-financing to be applied for by the beneficiary varies from project to project from 29.85% to 47.66% (average 39.1%) of the "funding gap". Therefore the maximum aid intensity of the projects of 57% of the "funding gap" foreseen when preparing the measure is not reached.
68. These aid intensities appear to be lower as the aid intensities applicable under the Regional Aid Guidelines for Poland. The RAG allows aid from 30% to 50% for total investment costs for large investment projects depending on concrete regions at NUTS II level¹⁶. In the regions affected by the investments at hand the maximum aid intensity will be 40% and 50% of total investment costs. The aid intensities of the notified projects are in absolute terms lower as the 50% threshold. In addition these aid intensities will apply to the eligible costs calculated on the basis of funding gap and not on the basis of total costs.
69. In view of the above it can thus be concluded that the State aid granted for the envisaged measures is proportional, and is limited to a minimum.

Distortion of Competition and Balancing Test

70. The market of gas transmission is a "natural monopoly" market where the TSO is being assigned by the State. It could be argued that in theory other company than Gaz-System could apply for a TSO concession and invest in the envisaged pipelines on its own, at least in the medium term. Therefore the contemplated subsidy, in so far as they contribute to development of existing network, have the effect of deterring operator to invest themselves in new gas transmission networks. After the investment is in place, due to its "natural monopoly" character no future investments in the same pipelines are expected..
71. However, the impacts on competition on the market for transmission of gas are mitigated on the downstream markets, as the beneficiary of the aid is obliged to ensure the third party access to its network for all suppliers of gas.
72. As explained above suppliers of gas may derive benefits from the aid in getting the possibility to enter the gas market in Poland due to the construction of the new pipelines. Therefore it cannot be excluded that the aid may distort competition on markets where companies distributing and producing or trading gas are active. However, the aid scheme ensures that the aid is proportionate and the aid amount is limited to the minimum necessary.
73. On the other hand appropriate TPA provisions ensure that access to the networks is granted in a non-discriminatory manner, the scheme ensures the positive effects in terms of energy saving and interpenetration of gas systems, within the internal market. Hence relatively low negative effects are outweighed by the identifiable positive effects of the aid.
74. Therefore it can be concluded that the possible distortions of competition and trade resulting from the State aid for the envisaged measures are limited, and that the overall balance with regard to the objective of common interest is positive.

Conclusion

75. The Commission thus concludes that the aid scheme is compatible with 107 (3) (c) of the TFEU.

IV. CONCLUSION

76. The Commission has accordingly decided not to raise objections to the notified measure, because the aid can be found compatible with the common market in accordance with Article 107 (3) (c) of the TFEU no longer applies and Article 61 (3) (c) of the EEA Agreement, since it pursues an objective of common interest in a necessary and proportionate way.
77. The Commission reminds the Polish Authorities that, in accordance with article 108 (3) of the TFEU, plans to refinance, alter or change this aid have to be notified to the Commission pursuant to provisions of the Commission Regulation (EC) No 794/2004 implementing Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 of the EC Treaty now 108 of the TFEU (OJ L 140, 30.4.2004, p.1).
78. If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/community_law/state_aids/state_aids_texts_pl.htm

Your request should be sent by registered letter or fax to:

European Commission
Directorate-General of Competition
State Aid Registry
B-1049 BRUSSELS
Telefax n°: + 32-2-296.12.42

Please, mention the name and number of the case in all the correspondence.

Yours faithfully,

For the Commission

Joaquin ALMUNIA
Vice-President of the Commission