

Deconsolidation under option 3 of the Directive

The overriding objective of the Directive 2009/73/EC (the 3rd Gas Directive, or the “Directive”) is to create independent network operators free from the influence or control of energy producers and suppliers, particularly belonging to the same group. The Directive offers two main routes to this objective: ownership unbundling and ring-fencing. If, however, the EU Commission, having verified its status, is satisfied that a TSO already has independent status at the time the Directive became law, this is an acceptable alternative to ring-fencing, provided that its status gives a “guarantee of more effective independence” (Art 9.9, third line) than the ring-fencing requirements of Chapter IV of the Directive.

Where this alternative is available (and properly certified and verified in accordance with the Directive) it follows that the TSO is already independent and accordingly its results should no longer be being consolidated with other group companies for the reasons set out in our previous note. The alternative in Article 9.9 is not therefore a defense against deconsolidation and certainly not a justification for continued consolidation: in fact it means that deconsolidation should already have occurred. It is a contradiction to claim that Article 9.9 conditions are met while continuing to consolidate SRG’s results. Indeed continued consolidation is in itself evidence that the requirements of Art 9.9 have not been satisfied.

Moreover, in reality, option 3 is not a substantively different option from ring-fencing under Chapter IV of the Directive: it is simply one of timing. Put simply, if an independent TSO already existed at the time the Directive became law - and the Republic of Italy can only certify this if the EU Commission has verified SRG’s independence - there is no need to fulfill the ring-fencing requirements of the Directive because the objective mandated by it has already been achieved. It is therefore appropriate to test whether SRG is independent for the purpose of the Directive by considering the extent to which it satisfies the ring fencing requirements set out in Option 2.

The SRG 2009 Report on Corporate Governance (the “SRG Report”) suggests that SRG is unlikely to be considered to be sufficiently independent under Option 2 and therefore would fail to meet the standards required under Option 3. For example:

- (a) Article 19 of the Directive requires that all board members, including the CEO, be appointed by a supervisory body and be independent but SRG’s CEO has been proposed by Eni and appointed by SRG shareholders’ meeting; furthermore, only its non-executive directors are independent. Article 19 also requires the local regulatory authority evaluate the independence of the board members - but the Italian regulatory authority does not have such power;
- (b) Article 20 requires the constitution of a supervisory body and, hence, the introduction of a dual governance system but SRG has a traditional organisational structure with no supervisory body; and
- (c) Article 21 requires the appointment of an independent competition and non-discrimination compliance officer but the equivalent position within SRG, created in compliance with the Directive 2003/55/EC (the 2nd Gas Directive), is held by the CEO, who is not independent from Eni.

Furthermore, it is unlikely that SRG could meet the Directive independence requirements in other ways not specified by Chapter IV of the Directive. The Directive introduced more stringent ring-fencing requirements because the functional unbundling mandated by the 2nd Gas Directive has not led to the effective unbundling of the TSOs (Recital 7 of the Directive). The SRG Report is evidence of a corporate governance and control structure which complies with, and in some cases goes beyond, the requirements of the 2nd Gas Directive and the Italian

implementing regulations; however, it does not appear that SRG can demonstrate that it has implemented other measures which, at least from a corporate governance and control perspective, achieve an equivalent level of independence as would be achieved by the implementation of the Directive's ring-fencing requirements.

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