



MINISTER OF JUSTICE
HUNGARY

XX-EUJMFO/352/5/2015.

Budapest, "21" January 2016

Ms Elżbieta Bieńkowska
Member of the European Commission
European Commission

Bruxelles

Response of the Hungarian Government to the European Commission's Letter of Formal Notice of 19 November 2015 in the infringement case 2015/4231 concerning procurement issues in relation to the nuclear power plant construction in Paks, Hungary (SG-Greffe(2015)D/13441)

Dear Commissioner,

The Government of Hungary has the honour to respond to the European Commission's ("Commission") letter of formal notice dated 19 November 2015 ("LFN") opening infringement proceedings against Hungary for an alleged breach of Hungary's EU public procurement obligations in relation to the project for the construction and operational support for a nuclear power plant ("NPP") in Paks, Hungary ("Project" or "NPP Paks II"). In the course of the on-going dialogue conducted between the Commission and the Government of Hungary in relation to the Project and taking into account the shared information and documentation in this regard, the Government of Hungary exceptionally and on a case-by-case basis shares its position related to the issues put forward by the Commission in the English language.

A. Preamble

In the LFN, the Commission contends that Hungary has failed to fulfil its EU law obligations, by awarding the Project directly to the State Atomic Energy Corporation, Rosatom. The Commission concludes that the exemption from the procurement rules for contracts awarded

pursuant to international agreements does not apply. It argues that the IGA does not include "different procedural rules" within the meaning of this exemption and that the IGA is not concluded in conformity with the basic principles of the TFEU, in particular on the basis that Hungary had no competence to enter into the IGA given its scope falls within the exclusive competence of the Commission under the Common Commercial Policy ("CCP"). The Commission further considers that there is no justification for the direct award through a reference to the Euratom Treaty. On this basis, the Commission submits that there has been a potential infringement of EU law.

The Government of Hungary considers that it has not breached any of its EU law obligations in relation to NPP Paks II and that it was fully entitled to enter into the Intergovernmental Agreement with Russia on Cooperation in the Peaceful Use of Nuclear Energy ("IGA"). The Project has been specifically designed to comply with EU law and the Government of Hungary has engaged with the Commission, including Directorate General for Internal Market, Industry, Entrepreneurship and SMEs ("DG GROW") at every key stage, including prior to signature of the IGA when on 26 November 2013 Hungary informed the Commission (see the presentation of Hungary attached hereto as Annex A) and on 10 December 2013 notified the draft of the IGA to the Commission, to comply with its obligations with EU law. This response should be read in conjunction with all of Hungary's previous submissions to the Commission, including notably those of 4 September 2014 and 2 September 2015.

The Government of Hungary emphasises at the outset the right of Member States to determine autonomously their energy mix, including the role and share of nuclear energy. As the Commission is well aware from previous submissions, NPP Paks II is Hungary's only viable option to implement its national energy policy and maintain long term security of electricity supplies in Hungary.

Given in particular the vital national importance of the Project for Hungary, and the open and transparent approach that Hungary has adopted towards the Commission throughout the procedure, beginning with the detailed workshop of 26 November 2013 with the participation of DG GROW (then called DG MARKT) prior to the signature of the IGA, the Government of Hungary is extremely disappointed by the lack of engagement on the Commission's side, and apparent lack of appreciation of the facts of the case, over a period of more than two years, including most recently at the meeting between the Minister of State heading the Prime Minister's Office, and Commissioner Bienkowska on 12 January 2016. The Government of Hungary respectfully considers that the Commission has not in this case observed its duties of loyal co-operation and good administration as far as Hungary is concerned and the way its procedure has been conducted has, in effect, discriminated against Hungary.

Moreover, as far as Hungary is aware, the Commission has not investigated other EU nuclear projects which have not followed public tendering procedures under the EU procurement directives and we see no justification for the apparent difference in treatment accorded to Hungary and the Project.

Factual background

Hungary has been considering how to address its electricity supply needs for a number of years. In 2009 the democratically elected Hungarian Parliament – with the support of the major parliamentary groups – adopted the Decree No 25/2009. (IV. 2.) pursuant to which the Hungarian Parliament gave its preliminary conceptual consent to the commencement of the preparatory works for the implementation of the new NPP units on the Paks site. After assessing the relevant options, in 2011 the National Energy Strategy for the period up to 2030 was implemented, including a commitment to long-term nuclear energy. This culminated in the decision to build a new nuclear power plant adjacent to the existing Paks I nuclear plant, which would in due course replace Paks I's ageing reactors. This decision reflects Hungary's freedom under the Treaty on the Functioning of the European Union ("TFEU") (Article 194) to choose its own energy mix.

NPP Paks II is an essential project for Hungary's security of supply and is crucial not only to Hungarian citizens, but also for reducing reliance on gas supplies from third countries within Hungary and across the EU in line with EU objectives. It is key that the Project is delivered on time in the most efficient manner taking into account the existing infrastructure in Paks I.

One of the known key challenges for new nuclear projects is the requirement for large capital investment in the construction period. At the relevant time, Hungary had limited access to the financial markets. Having considered all relevant options, it became clear that the Project, including the financial terms offered by Russia, was the only viable option to ensure the financing and maintenance of the capacity. It is to be emphasised that the IGA and its associated Agreements constitute "a package deal", covering NPP Paks II, the financing of NPP Paks II, the supply of nuclear fuel, and in due course the option on temporary storage of nuclear waste. The existing Paks I reactors are also based on the Russian VVER technology and the technical continuity which the Project represents is also an essential element. Hungary has a long experience with VVER reactor technology, with its technical, nuclear safety, operation and maintenance features. The new VVER-1200 units have been developed on the basis of this technology. Using the existing experience represents definite advantages not only in the future safe and economic operation of the NPP, but also in the required licensing of the units.

In these circumstances, the Government of Hungary is satisfied that there was no viable alternative to the Project, or that any other supplier, necessarily supplying a different nuclear technology, could have offered a similar package. It is notable that, as far as is known, no other supplier of nuclear technology has made any complaint about this aspect of the package. Hungary has been advised that the [REDACTED] nuclear technology supplier [REDACTED] was not offering, or able to offer, the fixed price turnkey solution required by the EPC specifications, nor the financing or the nuclear waste temporary storage option aspects of the package deal. The same is true of [REDACTED] providers who were not offering in the market fixed price turnkey solutions for a generation III+ technology with as much as 80% financing without security

obligations or ownership rights over the asset. Hence, factually there were no operators from the EU or elsewhere that were foreclosed from access to the Hungarian market or the Project.

In these circumstances, and without prejudice to the question of whether in the light of the EURATOM Treaty, the Treaty on European Union ("TEU") and the TFEU have any application at all, the Project has been carefully and specifically structured to fall within the exemption for international agreements provided by Article 22 lit.a of the Directive 2004/17/EC ("Utilities Directive"). As set out in more detail below, the IGA appoints the Russian State Atomic Energy Corporation Rosatom (which is a government agency) (see paras. 25) (Clause 2.1 of IGA) as responsible for designating, in accordance with Russian procurement legislation, another state owned entity to be the counter-party in the Implementation Agreements. Pursuant to these rules, Rosatom has designated Joint-Stock Company Nizhny Novgorod Engineering Company Atomenergoproekt ("NIAEP"), and the IGA envisages that sub-contracts will be open to EU and non-EU economic operators and will be awarded following public tendering processes (see Clause 3.6 of IGA). This means that a major part of the Project – effectively only with the exception of the VVER technology based nuclear steam supply system – will be open to EU sub-contractors, thus extending the benefits of the Project well beyond Rosatom and NIAEP to potential EU sub-contractors.

10

Hungary's position

Hungary strongly believes that it has fully complied with its obligations under the TEU, the TFEU and the EURATOM Treaty, and that there is no legal basis for the Commission to open an infringement procedure.

11

Firstly, the IGA and the Implementation Agreements fall within the scope of the EURATOM Treaty and the public procurement rules (or indeed other TFEU rules) do not apply to them:

12

- The nuclear reactors here in question fall within the scope of the EURATOM Treaty: Article 41 and Annex II.
- EURATOM is a sectorial treaty that contains special rules dealing with the sensitive nature of the nuclear industry. It therefore takes precedence over the application of the TFEU as confirmed by European case law and recognised by the Commission, and such precedence is reflected in Article 106a of EURATOM (which was amended following the Treaty of Lisbon). Article 106a expressly provides which Articles of the TEU and TFEU apply to the EURATOM Treaty. None of the "four freedoms" under the TFEU are there mentioned.
- The EURATOM Treaty establishes a nuclear common market (e.g. Articles 92 et seq.), thus precluding the application of the TFEU common market rules and indeed envisages the possibility of international cooperation for nuclear projects including investment: Articles 102 to 104.

- The EURATOM Treaty expressly contains a mechanism for the Commission to review such international cooperation agreements, and the Commission's powers are limited to operating within that framework: Article 103. After the detailed workshop in November 2013 and the notification of the draft IGA in December 2013, the Commission raised no objections to the IGA within the EURATOM framework in January 2014, as shown by the letter from Director-General Mr. Dominique Ristori.
- In addition, in April 2015 the Euratom Supply Agency ("ESA") concluded, and thereby approved, the Nuclear Fuel Supply Contract ("NFSC") which, as one of the Implementation Agreements envisaged by the IGA, is an integral part of the Project.
- Furthermore, the NFSC co-signed by the ESA endorses and takes into account the chosen technology for the planned nuclear power plant since nuclear power plants having a technology other than VVER cannot use the fuel rods to be supplied under the NFSC. Accordingly, the supplier of the VVER technology is named and determined in the NFSC and the Commission did not object to that choice when reviewing the NFSC.
- In these circumstances, where Hungary had acted with full transparency, while the Commission had not even replied on the merits of the case, further review by the Commission over two years after the first workshop in November 2013 and the notification of the draft IGA to the Commission, and after President Barroso's letter of February 2014, is *ultra vires*.

In any event, even assuming that the TFEU applies, under the EU public procurement framework there is a specific exemption for this type of international agreement. Such exemption provides that a contract may be awarded pursuant to the rules in an international agreement that has been completed in compliance with the Treaty where it relates to the joint implementation or exploitation of a project by two States. Hungary carefully considered the structure of the Project and the content of the IGA to ensure that (regardless of EURATOM) the conditions in such exemption would in any case be met.

13

- Firstly, Article 22 of the Utilities Directive (and the equivalent article in Directive 2004/18/EC ("Procurement Directive"); Utilities Directive and Procurement Directive together "Procurement Directives")¹ requires that an international agreement is entered into *in accordance with the Treaty*. This necessarily means that the Member State had the competence to enter into such an agreement. Hungary has a sovereign right under Article 194 TFEU to choose its energy mix and therefore was entitled to conclude an agreement with a non-EU country regarding the development of a nuclear plant.

¹ Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors; and Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

- Secondly, Hungary rejects the Commission's interpretation that the scope of the IGA contravenes the EU's exclusive competence to enter international agreements affecting the Common Commercial Policy. The IGA relates to one single project and does not regulate access to the Hungarian or EU procurement markets by Russian entities at large. Moreover, the Commission's interpretation would render the Article 22 exemption meaningless since Member States could never enter into agreements regarding the award of contracts relating to a particular project with non-EU countries. Similarly, Articles 102 to 104 of the EURATOM Treaty would have little meaning.
- Thirdly, contrary to the Commission's contention, the IGA sets out clear procedures for the award of the Implementation Agreements. It designates competent authorities within each state (public bodies) but does not bind them to enter into the Implementation Agreements. It then sets out specific requirements both for (i) the appointment and negotiation of the companies that will enter into the Implementation Agreements and (ii) the award of sub-contracts under such Agreements.
- Fourthly, the IGA and the EPC contract provide for the application of the TFEU principles of non-discrimination, transparency and equal treatment to the award of sub-contracts. Accordingly, it provides for a significant part of the Project to be subject to public tendering procedures which will comply with those principles.

Furthermore, the case law of the CJEU also envisages derogations of the principle of non-discrimination and the free movement rules in the TFEU in certain circumstances that, in our view, are met by the Project. These derogations or restrictions must pursue a common objective compliant with the TFEU, must be in the general interest and must not go beyond what is necessary to achieve that objective.

14

- Security of supply is a legitimate general interest and development of the nuclear industry is clearly a common objective of the EU in light of the existence of the EURATOM framework.
- The IGA and the Implementation Agreements are appropriate and proportionate, and the fact that the majority of the Project will be sub-contracted in accordance with the principles of non-discrimination, transparency and equal treatment, and via EU-wide notices, means that any restrictions to fundamental freedoms would be limited to the minimum necessary.²

Moreover, there are potentially other considerations supporting the legality of the IGA within the EU procurement framework, for example, the technical reasons exemption provided under

15

² Similarly, Article 106(2) TFEU provides a limited derogation from the Treaty rules for (*inter alia*) certain undertakings responsible for carrying out a service of general economic interest, where the application of the Treaty rules would "obstruct the performance, in law or in fact, of the particular tasks assigned to them".

Article 40(3) lit. c of the Utilities Directive. In the interests of time we have not explored these considerations in detail in this response.

The chronology and steps for the implementation of the IGA is contained in Annex B attached hereto.

Final considerations

It can be seen from the foregoing that Hungary is not in breach of any aspect of EU law given, notably, the scope of the EURATOM Treaty, the exemption for international agreements under Article 22 of the Utilities Directive, and the overriding considerations of general interest referred to above. In addition, with the exception of the VVER technology based on nuclear steam supply system itself, as to which the practical possibility of an alternative supplier can be ruled out, a major proportion of the works in question will be open to EU tendering procedures in any event. 16

Moreover, the dilatory and, in Hungary's view, discriminatory way in which the Commission has conducted this case over more than two years, well knowing that the vital interests of a Member State are at stake, given the importance of the Project for security of supply in Hungary, is, in the view of the Government of Hungary, highly regrettable. 17

In all such circumstances, the Commission's request that the Government of Hungary suspend all further award procedures related to the Project and refrain from concluding contracts pursuant to the procedural rules under the IGA (LFN, p. 7) has no legal basis, and is in any event inappropriate and out of time. The Government of Hungary respectfully reminds the Commission that the duty of sincere cooperation under Article 4(3) TEU applies also to the Commission. Further, the Government of Hungary wishes to remind the Commission that the Implementation Agreements have been concluded and Sub-Agreements will be concluded by NLAEP, not by Hungarian authorities. 18

Notwithstanding the foregoing, Hungary will continue to be available for further discussions with the Commission in good loyal partnership, and will continue cooperating with DG GROW. Hungary has always been open to face to face meetings in order to explain and avoid further factual mistakes by DG GROW. As Hungary has always proceeded in a timely manner, we urge DG GROW to engage fully with us and re-consider its position promptly so that we can conclude this matter and avoid further delays to the Project, which is essential for the future of Hungary and its citizens. Given that Hungary is a Member State, the Project is also strongly for the benefit of the European Union as a whole since, *inter alia* it reduces reliance on gas imports from third countries and it promotes economic growth. 19

B. Background/Facts

The factual statements of the Commission are in main aspects incorrect. These factual inaccuracies have an impact on the Commission's legal reasoning. The Government of Hungary wishes to clarify in particular the following aspects:

Structure of the Project

The Project is structured in three levels: the intergovernmental agreements, the Implementation Agreements and the Sub-Agreements. Irrespective of the structure overview, explanations and clarifications in various submissions and meetings, the Commission continues to misinterpret certain aspects. At the level of the IGA no contracts have been awarded (see below paras. 24 et seqq.). 21

In any event a major part of the project volume has to be tendered prior to entering into the Sub-Agreements. This scheme has been developed in close consultation with the Commission and in particular has been specifically addressed and discussed already in the meeting with the Commission, including DG GROW, on 26 November 2013. 22

1. Intergovernmental Agreements

The IGA establishes cooperation of Hungary and the Russian Federation for the joint implementation of the Project. The IGA contains the main obligations of the Russian Federation (Articles 4 and 5 IGA) and Hungary (Articles 4 and 6 IGA). The IGA is an agreement between States under public international law. The IGA together with the Intergovernmental Agreement on the Extension of a State Credit to the Government of Hungary for the Financing of the Construction of a Nuclear Power Plant in Hungary of 28 March 2014 ("Financing IGA") forms the international law framework for the implementation of the Project. 23

a) The Competent Authorities

Hungary and the Russian Federation each designated a government agency as its competent authority (Article 2 (1) IGA) ("Competent Authorities"). The Russian Federation has designated State Atomic Energy Corporation Rosatom ("Rosatom") as its Competent Authority, which according to Russian laws has a status comparable to a government authority,³ and Hungary has designated the Ministry of National Development. 24

25

³ Russian legal acts relevant for the status of Rosatom applicable on the date of conclusion of the IGA: Federal Act 44-FZ of 5 April 2013; Government Resolution 840 of 16 August 2012; Government Resolution 888 of 26 November 2008 (operational rules of Rosatom); Federal Act 317-FZ of 1 December 2007 on the establishment and operation of Rosatom; ; Government Resolution 514 of 2 October 2004; Government Decree 264 of 2 June 2004; Government Resolution 260 of 1 June 2004; Federal Act 183-FZ of 18 July 1999; Federal Act 7 of 12 January 1996; Federal Act 170-FT of 21 November 1995.

Rosatom is a legal entity with special legal status which carries out statutory tasks, represents and acts on behalf of the Russian Federation and enjoys autonomy against the state on a certain level.

- Rosatom was established by the Russian Federation by the Federal Act 317-FZ of 1 December 2007 ("Federal Act"). This Federal Act regulates the objectives, rights and operation of Rosatom which are underlying the fact that Rosatom has a status comparable to a government authority.
- Article 4 of the Federal Act defines an exhaustive list of objectives of Rosatom on the field of nuclear energy. The most important are the following: (i) implementation of state policy, (ii) enforcement of laws, (iii) control over state property, (iv) provision of state services, (v) international co-operation, (vi) ensuring nuclear safety and (vii) supervision of nuclear materials.
- The Federal Act states that Rosatom exercises control over the use of nuclear energy on behalf of the Russian Federation and is empowered to adopt laws and submit draft bills and other legislation to the President and the Government of the Russian Federation (Art. 2 and 8 of Federal Act). Further, in accordance with the Federal Act, Rosatom ensures the fulfillment of the obligations and is entitled to enforce the rights of the Russian Federation stemming from such international agreements which fall within the scope of Rosatom (Art. 14 of Federal Act). Besides the IGA, Rosatom has been appointed as competent authority in further international agreements on peaceful use of nuclear energy (e.g. in the intergovernmental agreements with Turkey, Niger and Finland).

The Competent Authorities coordinate the cooperation under the IGA and control the implementation of the measures aimed at ensuring the effective fulfillment of the agreement (Article 2 (3) and (4) IGA), but they neither award any implementation or sub-agreements nor act as contractors under any implementation or sub-agreements. 26

b) No Award through the IGA and the Financing IGA

The IGA and the Financing IGA are neither public procurement contracts nor contain an award of a public contract. In particular the IGA does not contain an award of the Implementation Agreements. It sets out procedural rules for their conclusion and contains a procurement scheme for the subsequent award of the Sub-Agreements (cf. Articles 3 (5) and (6), 8, 11 IGA). The Financing IGA contains only a financial framework for the Project, but does not bind the parties to the implementation of the Project. Neither the IGA nor the Financing IGA predetermines any terms and conditions of the Implementation Agreements which have been subsequently negotiated and concluded. The parties to the 27

Implementation Agreements are neither parties to the IGA nor to the Financing IGA. They are not entitled to any claims under the IGA or the Financing IGA.

Thus, the Project is not implemented through "a direct award in an international agreement" (contrary to LFN, p. 5) or "a procurement through an IGA" (contrary to LFN, p. 5).⁴ The Commission's assessment is based on a misunderstanding of the structure of the Project.

2. Implementation Agreements

The Implementation Agreements have been concluded between the Hungarian Authorized Organization – MVM Paks II Nuclear Power Plant Development Private Company Limited by Shares ("Paks II") – and the Russian Authorized Organization NIAEP, together with Paks II "Authorized Organizations") as designated Authorized Organizations of Hungary and the Russian Federation respectively, pursuant to the IGA (cf. Article 3 (1), (2) and (5), Article 8 IGA).

Paks II has been designated as the Hungarian Authorized Organization by the Ministry of National Development pursuant to Government Decree 1429/2009. (VII.31.). Paks II was established by the MVM Magyar Villamos Művek Company Limited by Shares ("MVM") on 10 August 2012. MVM is a single-shareholder company which is fully owned by the Hungarian National Asset Management Inc. and therefore *de facto* by the Hungarian State. Paks II remained a 100% subsidiary of MVM until 11 November 2014 when the Hungarian State directly acquired 100% of the shares in Paks II. Pursuant to the Decree of the Minister of National Development No 45/2014 (XI. 14.) the Prime Minister's Office is entitled to exercise the ownership rights on behalf of the Hungarian State.⁵

Hungary is not a contracting entity with regard to the Implementation Agreements (contrary to LFN, p. 4). Hungary is a party to the IGA which sets out the further structure of the implementation of the Project and has designated Paks II (which is 100% owned and controlled by the Hungarian State, cf. para. 30)) in accordance with the procedural rules of the IGA. Paks II is the contracting entity of the Implementation Agreements.

Further, Rosatom is not a party to the Implementation Agreements (contrary to LFN, p. 1, 5). The Government of the Russian Federation has designated NIAEP in accordance with the procedural rules of the IGA as contractor for the Implementation Agreements (see paras. 85 et seqq.). NIAEP has been designated as Russian Authorized Organization by the Russian Competent Authority by letter of 14 October 2014.

⁴ Cf. also LFN, p. 2: "the direct award through the IGA"; p. 6: "awards through international agreements"; p. 7: "by directly awarding the contract [...] in the international agreement".

⁵ The ownership structure of Paks II was also explained in the Hungarian authorities' replies to the requests for information by the Commission dated 1 December 2014 and 27 January 2015 and the official English version of the company register extract of Paks II was handed over to the Commission at a meeting in October 2015.

The Authorized Organizations Paks II and NIAEP concluded the EPC Contract after the Government of Hungary had informed the Commission about its intention to sign it in the meeting on 27 November 2014 in the context of the Article 41 EURATOM procedure. In this meeting DG GROW was also present, but did not make any comment or raise any concern on public procurement matters raised in the LFN.

33

The final version of the NFSC was concluded on 2 April 2015. The European Commission wrongly states that the NFSC was concluded in December 2014 (LFN, p. 1). The NFSC was co-signed by the Euratom Supply Agency in consultation with the Commission on 20 April 2015.

34

3. Sub-Agreements

The parties to the Implementation Agreements must engage further organizations in the implementation of the Project. A substantial part of the volume of the Project will be procured from other companies. NIAEP is obliged under the IGA, which has been transposed into national law, to *"carry out procurement procedures in accordance with the principles and general requirements of transparency (including prior publication of contract notices EU-wide in the English language), equal treatment and non-discrimination as well as independent review regime"* (Article 3 (6) IGA).

35

C. Engagement with the Commission

Hungary has comprehensively, in detail and in due time communicated to and consulted with the Commission and its services all aspects of the Project, including procurement related matters, in numerous submissions and meetings.

36

In order to ensure transparency and full compliance with EU law, the Government of Hungary has been in close consultation and open discussions with the Commission for more than two years and well before the signing of any agreement. Since then, the Government of Hungary has met with all involved Directorate Generals ("DG") and units of the Commission many times and cooperated to the fullest extent possible. DG GROW (formerly DG MARKT) – in its own proceedings and, as observant, in the proceedings of other involved DGs – has been constantly involved in this dialogue.

In order to engage with the Commission proactively at every stage of the Project, several meetings have been organized with the Commission involving DG GROW:

37

- Prior to the notification of the draft IGA to the Commission on 10 December 2013 a half-day workshop was organized on 26 November 2013 in order to discuss all relevant aspects of the IGA – including procurement issues – with all responsible DGs including representatives of DG GROW. The discussions prior to and in this

initial workshop of November 2013 led to modification of the draft IGA, in particular on the procurement scheme for the Sub-Agreements.

- Prior to the notification of the draft Implementation Agreements on 8 July 2014 another meeting dedicated to the procurement issues was held with the Commission. As a follow-up of this meeting, the Government of Hungary provided a prompt and comprehensive answer to the Commission's request for information concerning the Project on 4 September 2014.
- ~~Prior to the signing of the Implementation Agreements on 27 November 2014~~ another meeting relating to the procedures under Article 41 EURATOM Treaty took place with all relevant DGs participating, including DG GROW.
- Numerous other meetings with the Commission and its services have been held.⁶

Further the Government of Hungary has, besides other communications⁷ with the Commission more generally, frequently exchanged communications with

38

- DG Growth (DG GROW),⁸
- DG Competition (DG COMP)⁹ and

⁶ E.g. meetings with different services on 3 June 2014 (workshop), 23 July 2014, 8 September 2014, 12 November 2014, 21 January 2015, 3 March 2015, 19 May 2015, 6 July 2015, 15 July 2015, 16 July 2015, 22 September 2015, 29 September 2015, 9 October 2015.

⁷ Cf. also the further correspondence such as Submission of the draft IGA to the Commission under the Article 103 EURATOM Treaty procedure, 10 December 2013; Letter from Prime Minister Viktor Orbán to the Commission's President José Manuel Barroso of 23 January 2014; Letter of Commission President José Manuel Barroso to Prime Minister Viktor Orbán of 7 February 2014, Barroso(2014)153242 and 294667; Notification of the Financing IGA to DG MARKT and DG ENER, 26 March 2014; Notification of the draft Implementation Agreements to the Commission under Article 103 EURATOM Treaty procedure, 18 September 2014; Submission of the signed EPC Contract to the Commission (DG ENER) on 5 May 2015.

⁸ E.g. Letter of Hungary to DG Grow of 26 March 2014; Request for Information by DG Grow of 13 August 2014; Submission of Hungary to DG Grow of 4 September 2014; Letter of Hungary to DG Grow of 29 April 2015; Letter of DG Grow to Hungary of 19 May 2015; EU Pilot Request of DG Grow to Hungary of 25 June 2015; Answer of Hungary to EU Pilot Request of DG Grow of 2 September 2015; Letter of Hungary to DG Grow of 1 October 2015; Letter of DG Grow to Hungary of 13 October 2015; Letter of Hungary to DG Grow of 15 October 2015; Letter of Hungary to DG Grow of 17 November 2015.

⁹ E.g. Letter of DG Comp to Hungary of 13 March 2014, SA.38454 (2014/CP); Letter of Hungary to DG Comp of 10 April 2014; Submission of Hungary of the Briefing Paper for the Meeting of 23 July 2014 and 5 August 2014; Submission of Hungary of Independent Market Price Report on 15 September 2014; Submission of Hungary of Risk Allocation Summary on 23 September 2014; Letter of DG Comp to Hungary of 1 December 2014, SA.38454 (2014/CP); Letter of DG Comp to Hungary of 27 January 2015, SA.38454 (2014/CP); Submission of Hungary of updated Risk Allocation Summary of 30 January 2015; Communication of Hungary to the European Commission in Reply to Information Requests of 18 February 2015; Letter of Hungary to DG Comp of 2 March 2015; Submission of Hungary of Project Financial Model of 13 and 16 March 2015; Letter of DG Comp to Hungary of 18 March 2015, SA.38454 (2014/CP); Letter of Hungary to DG Comp of 16 April 2015; Letter of Hungary to DG Comp of 23 April 2015; Letter of

• DG Energy (DG ENER)¹⁰.

In these meetings and submissions the Government of Hungary has replied to all requests for information by the Commission and constantly emphasized its commitment to fully comply with EU and EURATOM laws, as also expressed in the IGA.¹¹

As the TFEU explicitly acknowledges (Article 194 (2) subpara. 2 TFEU; for more detail see paras. 55 et seq., 72) and as the exhaustive nature of the EURATOM Treaty confirms (see paras. 46 et seq.), Hungary can autonomously decide on its energy mix and has the right to opt for nuclear energy as a key element of its sovereign energy policy. Hungary did so. In 2009 the democratically elected Hungarian Parliament – with the support of the major parliamentary groups – decided on its energy mix, opted for nuclear energy and gave its consent to the preparatory works for the new NPP units at Paks.¹²

The Project enables Hungary to implement this choice. Notwithstanding this prerogative of the Member States, the Government of Hungary has had extensive communications with the Commission on its energy policy approach, including the Project, and has taken account of the Commission's reasonable positions. With regard to public procurement

Hungary to DG Comp of 29 April 2015; Letter of Hungary to DG Comp of 4 May 2015; Letter of Hungary to DG Comp of 13 May 2015; Notification as Non-Aid-Measure by Hungary of 22 May 2015; Letter of DG Comp to Hungary of 5 June 2015, SA.38454 (2015/N); Letter of Hungary to DG Comp of 9 June 2015; Letter of Hungary to DG Comp of 12 June 2015; Letter of Hungary to DG Comp of 14 July 2015; Letter of DG Comp to Hungary of 17 July 2015, SA.38454 (2015/N); Letter of Hungary to DG Comp of 6 August 2015; Letter of DG Comp to Hungary of 12 August 2015, SA.38454 (2015/N); Letter of Hungary to DG Comp of 19 August 2015; Letter of DG Comp to Hungary of 21 August 2015, SA.38454 (2015/N); Letter of Hungary to DG Comp of 4 September 2015; Letter of DG Comp to Hungary of 30 September 2015, SA.38454 (2015/N); Letter of Hungary to DG Comp of 29 October 2015.

¹⁰ E.g. Communication to the European Commission of the Investment Project relating to the "Paks II Project" under Article 41 EURATOM Treaty of 15 August 2014; Letter of Hungary to DG Ener of 31 October 2014; Letter of DG Ener to Hungary of 31 October 2014; Letter of Hungary to DG Ener of 25 November 2014; Letters of DG Ener to Hungary of 22 December 2014; Letter of Hungary to DG Ener of 3 February 2015; Letter of Hungary to DG Ener of 20 February 2015; Letter of DG Ener to Hungary of 09 March 2015; Letter of Hungary to DG Ener of 6 March 2015; Letter of DG Ener to Hungary of 30 March 2015; Letter of Hungary to DG Ener of 13 April 2015; Letter of DG Ener to Hungary of 22 April 2015; Letter of Hungary to DG Ener of 30 April 2015; Letter of DG Ener to Hungary of 1 June 2015; Letter of Hungary to DG Ener of 4 June 2015; Letter of Hungary to DG Ener of 23 July 2015; Commission's view in accordance with Article 43 of the EURATOM Treaty of 8 September 2015; Letter of Hungary to DG Ener of 8 September 2015; Letter of Hungary to DG Ener of 9 September 2015; Letter of DG Ener to Hungary of 24 September 2015; Letter of Hungary to DG Ener of 1 October 2015; Letter of Hungary to DG Ener of 15 October 2015.

¹¹ Cf. Article 11 (3) IGA where the parties "acknowledge that the Hungarian Party, Hungarian Competent Authority and Hungarian Authorized Organization have obligations relating to the European Union and the European Atomic Energy Community.", see also Preamble of the IGA where the parties confirm to take account of "the obligations of Hungary under the relevant laws of the European Union and of the European Atomic Energy Community"; see also Letter from Prime Minister Viktor Orbán to Commission President José Manuel Barroso, 23 January 2014, p. 2.

¹² 25/2009. (IV. 2.) OGY határozat az atomenergiáról szóló 1996. évi CXVI. törvény 7. §-ának (2) bekezdése alapján, a paksi atomerőmű telephelyén új atomerőművi blokk(ok) létesítésének előkészítését szolgáló tevékenység megkezdéséhez szükséges előzetes, elvi hozzájárulás megadásáról

matters related to the Project, it has, in light of these discussions with the Commission, modified the procurement framework of the IGA and the EPC Contract (see above para. 37), in particular through introducing an open procurement framework for the subsequent award of the Sub-Agreements as set out above. In particular:

- At the workshop on 26 November 2013 the Government of Hungary informed the Commission, including DG GROW of the core points of the Project, especially of the planned IGA. After that the Government of Hungary provided a draft of the IGA to the Commission on 10 December 2013 in which the remarks of the Commission had been already taken into account. The European Commission confirmed by letter of 14 January 2014 that its services *"did not find any element that would as of itself impede the application of the EURATOM Treaty in the meaning of its Article 103"*. The IGA was only signed after this approval and the Hungarian National Assembly subsequently adopted Act II of 2014 by which the IGA was incorporated into national legislation. Act II of 2014 came into effect on 12 February 2014.
- The Government of Hungary also notified a draft of the Financing IGA prior to its conclusion to the Commission on 26 March 2014. The Hungarian Parliament adopted the Act related to the state credit on 23 June 2014.
- The Government of Hungary consulted with the Commission on all aspects, including procurement related matters in June and July 2014. At these meetings the Commission was informed that the negotiations on the Implementation Agreements already started and that the drafts would be notified to the Commission. The Government of Hungary provided drafts of the Implementation Agreements to the Commission on 18 September 2014, prior to Paks II's conclusion of the Implementation Agreements. The signed EPC Contract was submitted to the Commission (DG ENER) on 5 May 2015.
- Upon request of the Commission,¹³ the Government of Hungary further provided the Commission access to the signed EPC Contract including its Procurement Policy appendix (Appendix 1.15 to the EPC Contract).¹⁴ The Government of Hungary – in order to facilitate the assessment of the Project by DG GROW – has offered access to the Procurement Policy at the facilities of DG ENER and at the Permanent Representation of Hungary to the European Union in Brussels.¹⁵ DG GROW has

¹³ Letter of DG Comp to Hungary of 27 January 2015, SA.38454 (2014/CP).

¹⁴ Cf. also Letters of Hungary to DG Comp of 23 April 2015, 29 April 2015, 4 May 2015, 13 May 2015, 22 May 2015, 9 June 2015, 12 June 2015, 14 July 2015, 6 August 2015, 19 August 2015, 4 September 2015

¹⁵ Letters of Hungary to DG GROW of 1 October 2015, 15 October 2015 and 17 November 2015.

never followed up on this offer – despite its announcement to do so¹⁶ – and did not assess the EPC Procurement Policy during the EU Pilot procedure or prior to the LFN of this infringement procedure. The omission to properly assess the procurement scheme and Procurement Policy may have contributed to the factual misconceptions of the Commission.

The Government of Hungary received remarkably little engagement from the Commission, prior to initiating EU Pilot proceedings regarding the Project on 24 June 2015. Since the EU Pilot proceedings were launched, the Commission has neither provided constructive feedback on the arguments of the Government of Hungary nor put forward any specific proposals how to solve the issue. Notwithstanding the Government of Hungary's best efforts to try to resolve the issue, the Commission surprisingly initiated an infringement procedure on 19 November 2015.¹⁷ 42

Hungary considers that the inaccurate factual basis of the LFN indicate that the Commission has not taken due account of the information provided by the Government of Hungary throughout this process. Further, DG GROW did not make any attempt to review the Procurement Policy for Sub-Agreements prior to the opening of this infringement procedure.¹⁸ The approach of the Commission compromised the purpose of the EU pilot procedure and is further indication of the Commission's discriminatory approach vis-à-vis the Hungarian NPP Project. 43

Separately, as far as Hungary is aware, the Commission has not investigated other EU nuclear projects which have not followed public tendering procedures under the EU procurement directives and which, at first sight, seem comparable to the situation in Hungary. We see no justification for the apparent difference in treatment accorded to Hungary and the Project. 44

Finally, as set out above, we wish to reiterate that we have, at all stages, engaged in an open manner with all relevant DGs, with a view to securing compliance with Hungary's EU law obligations; the Commission was given ample opportunity to provide comments on the Project in its early stages. However, rather than signalling concerns around compliance with the procurement rules, 45

¹⁶ Letter of DG Grow to Hungary of 13 October 2015.

¹⁷ Cf. Letter of Hungary to DG GROW of 17 November 2015.

¹⁸ DG GROW had been provided access to the Procurement Policy at the facilities of DG ENER and the Permanent Representation of Hungary to the European Union in Brussels. See eg. Letter of DG GROW to Hungary of 13 October 2015.

- the Commission raised no objections to the IGA within the EURATOM framework in January 2014, followed by President Barroso's direct assurances set out in the letter of February 2014.
- Similarly, DG GROW was present in the 27 November 2014 meeting in which the Government informed the Commission of its intention to sign the Implementation Agreements and no objections were raised during the meeting or thereafter, prior to signing such agreements.

~~The NFSC, one of the Implementation Agreements, names and determines the supplier of the VVER technology and the Commission did not object to that choice before the ESA co-signed the NFSC in April 2015. In these circumstances, we consider that the Commission's actions and assurances gave rise to a legitimate expectation for Hungary that the Project, and the Implementation Agreements envisaged therein, are compliant with EU law. This is all the more true in respect of aspects of the Project as fundamental as the choice of VVER supplier.~~

Hungary respectfully submits that there are doubts as to whether the Commission acted in an open and transparent manner pursuant to the duty of sincere cooperation in Article 4(3) TEU on matters of public procurement.

D. EURATOM Treaty Precludes Application of TFEU: the Project is Outside the Scope of Utilities Directive and General Principles in the Treaty

1. EURATOM Treaty as *Lex Specialis*

The EURATOM Treaty contains a self-contained and autonomous set of rules on the implementation of infrastructure projects in the field of nuclear energy. Therefore, neither the Utilities Directive or the Procurement Directive nor the basic procurement principles inferred from the TFEU are applicable to the Project and its implementation. 46

As a sectoral instrument within a "*highly specialized field*"¹⁹, the EURATOM Treaty is *lex specialis* to the TFEU (cf. Article 106a (3) EURATOM Treaty). In the scope of the exhaustive provisions of the EURATOM Treaty, the TFEU – and EU secondary law based on the TFEU – does not apply. Where the exercise of powers under the EURATOM Treaty would be impeded by the exercise of powers deriving from the TFEU within the sphere of the EURATOM Treaty, the EURATOM Treaty prevails. 47

In the present case there is no doubt that the core elements of the agreements in question – the supply of nuclear reactors, nuclear technology and nuclear fuel – fall within the scope 48

¹⁹ ECJ, Ruling 1/78 on Draft Convention of the International Atomic Energy Agency on the Physical Protection of Nuclear Materials, Facilities and Transports [1978] ECR 2151, paras. 14, 15.

of EURATOM Treaty: see e.g. Articles 41 and Annex II, Articles 52 to 66 and Article 103. Article 106a (1) of the EURATOM Treaty as currently in force specifically provides which articles of the TEU and the TFEU are to apply to the EURATOM Treaty. The articles of the TEU and the TFEU there set out do not include any of the Treaty articles on the "four freedoms" and thus do not include the rules on free movement of goods or services, or the right of establishment from which the public procurement rules derive. There is thus no basis for the application of those rules in the present case.

To the extent that it might be suggested that certain other aspects of the Project, for example some of the construction works, might not, strictly speaking, be within the scope of EURATOM, in the first place those other aspects are ancillary to the main purpose of the project, which is the construction and operation of a nuclear facility, including the supply of nuclear fuel, which is plainly within the EURATOM Treaty. The existence of ancillary works does not displace the application of the EURATOM Treaty, notably as regards the nuclear island and its associated technology. In any event, and of central importance to the legal analysis in this case, all works outside the supply of core nuclear reactors, technology and fuel will in any event be subject to tendering procedures in accordance with TFEU principles so there will be no even theoretical breach of public procurement rules in that regard.

The Commission itself has emphasized the independence and primacy of the EURATOM Treaty as *lex specialis* regarding economic activities related to nuclear projects and has rejected any attempt to construe the EURATOM Treaty in a way as to allow the unjustified recourse to the TFEU.²⁰ The Commission acknowledged in its decision *Kernkraftwerke Lippe-Ems GmbH* that the EURATOM Treaty

*"[a]s a sectoral Treaty containing special rules for a common policy [...] takes precedence over the general provisions of the EC Treaty".*²¹

Any subsidiary application of the TFEU – and EU secondary law based on the TFEU – on matters falling into the scope of the EURATOM Treaty thus depends on the (non-) exhaustive nature of the respective EURATOM Treaty's provisions.²²

The EURATOM Treaty has established a self-contained system of competition rules which precludes recourse to the general (procurement) provisions laid down in the TFEU or the Procurement Directives.

²⁰ European Commission, decision of 21 February 1994, 94/285/Euratom – Procedure in application of the second paragraph of Article 53 of the Euratom Treaty, [1994] O.J. EC of 17 May 1994, L 122, p. 30, para. 22.

²¹ European Commission, decision of 21 February 1994, 94/285/Euratom – Procedure in application of the second paragraph of Article 53 of the Euratom Treaty, [1994] O.J. EC of 17 May 1994, L 122, p. 30, para. 22.

²² ECJ, Opinion 1/94 *GATS and TRIPS* [1994] ECR I-5267, para. 24; cf. for the Treaty on the European Coal and Steel Community ECJ, Case 239/84 *Gerlach / Minister van Economische Zaken* [1985] ECR 3514, para. 10 et seq.; Case 328/85 *Deutsche Babcock / Hauptzollamt Lübeck-Ost* [1987] ECR 5136, para. 12.

The EURATOM Treaty follows a different approach than the TFEU and the Procurement Directives with regard to market regulation. The EURATOM Treaty has a clear *"promotional character"*²³ stemming from its objective to encourage investments in a (initially nascent) highly capital-intensive and complex market (see further on characteristics of the NPP market paras. 77 et seq., 120 et seq.). The EURATOM Treaty focusses on enabling individual international cooperation in order to promote growth in this area.

53

The EURATOM Treaty's rationale is to encourage nuclear investment projects which is further reflected in the following provisions.

54

- The EURATOM Treaty enables investments in NPP projects.
 - The EURATOM Treaty aims at *"creating the conditions necessary for the speedy establishment and growth of nuclear industries"* (Article 1 subparagraph 2 EURATOM Treaty).
 - The Commission shall *"facilitate investment and ensure, particularly by encouraging ventures on the part of undertakings, the establishment of the basic installations necessary for the development of nuclear energy in the Community"* (Article 2 lit. c EURATOM Treaty) and *"ensure wide commercial outlets and access to the best technical facilities by the creation of a common market in specialised materials and equipment"* (Article 2 lit. g EURATOM Treaty).
 - Title II lists the provisions for *"the encouragement of progress in the field of nuclear energy"* (Articles 4 et seqq. EURATOM Treaty).
 - The EURATOM Treaty obliges the Commission *"to stimulate action by persons and undertakings and to facilitate coordinated development of their investment in the nuclear field"* (Article 40 EURATOM Treaty).
- The EURATOM Treaty contains procedural rules for new investment projects. Their exhaustive character excludes the application of compulsory tender procedures under the general public procurement rules.
 - Undertakings *"shall communicate to the Commission investment projects"* (Article 41 EURATOM Treaty) and the Commission *"shall discuss with the persons or undertakings all aspects of investment projects which relate to the*

²³ Cusack, CMLR 40 (2003), p. 117 (126); Pechstein, EuZW 2001, p. 307 (310).

objectives of this Treaty." (Article 43 EURATOM Treaty, emphasis added). Thus, every investment-related facet of a nuclear project – including aspects of public procurement – has to be assessed by the Commission solely in the framework of the EURATOM Treaty. The Member State may rely on the final nature of this assessment within the procedure under Article 41 EURATOM Treaty.

- The EURATOM Treaty contains specific rules for joint undertakings within the meaning of Articles 45 et seqq. EURATOM Treaty. Applying the general public procurement laws parallel to these detailed provisions (requiring *inter alia* the approval of the Council, see Article 49 EURATOM Treaty) does not comply with the objective of facilitating and enabling NPP projects.
- Articles 92 et seqq. EURATOM Treaty further contain rules on the nuclear common market which argues against the applicability of the basic procurement principles inferred from the fundamental freedoms laid down in the TFEU.²⁴ In particular, Article 97 EURATOM Treaty contains a provision specifically dealing with the opportunity for natural or legal persons *"to participate in the construction of nuclear installations of a scientific or industrial nature in the Community"*.
- The EURATOM Treaty acknowledges the importance of international cooperation within NPP projects. It aims at encouraging and enabling common transboundary projects, but does not intend to impede them by allowing the general procurement provisions to prevent individual and tailored solutions on the international level (see for details on this objective paras. 109 et seqq.).
 - The EURATOM Treaty intends to establish such relations that *"foster progress in the peaceful use of nuclear energy"* (Article 2 lit. h EURATOM Treaty).
 - Articles 103 et seqq. EURATOM Treaty imply that international cooperation for nuclear energy infrastructure projects must be possible.
 - Further provisions of the EURATOM Treaty also emphasize the significance of international cooperation in the field of nuclear energy (e.g. the

²⁴ Article 106a (1) EURATOM Treaty on the application of certain provisions of the TFEU and the TEU also does not refer to the fundamental freedoms in the TFEU. Article 203 EURATOM Treaty includes an amendment clause which would be deprived of its meaning if, despite the exhaustive character of the EURATOM Treaty, the general public procurement provisions applied.

commitment in its Preamble²³ and Articles 1 subparagraph 2, 10, 16 (5), 64, 73, 101 et seq., 206 EURATOM Treaty).

The TFEU acknowledges the delimitation of competences in the energy sector between Member States and the EU and thereby confirms the exhaustive nature of the EURATOM Treaty with regard to investments in nuclear energy projects: Article 194 (2) subpara. 2 TFEU emphasizes the *"Member State's right to determine the conditions for exploiting its energy resources, its choice between different energy sources and the general structure of its energy supply"*. The provision is an expression for sovereignty rights reserved by Member States in the energy sector. The measures addressed in Article 194 (2) subpara. 2 TFEU are legislative measures adopted by Council and Parliament. However, *a fortiori* this must be true for acts of the Commission as well, as the Commission may not circumvent the provision's rationale by applying the general EU procurement laws to circumvent a Member State's decision on its energy mix. This overarching nature of Article 194 TFEU has recently also been reconfirmed by Advocate General Mengozzi who qualified the article as being

55

*"a general provision which relates solely to the energy sector and, consequently, delineates a competence which may be defined as sectoral because it relates to a single and comprehensive subject-area [...]"*²⁶

The Project is based on an autonomous decision of Hungary in the energy sector concerning and shaping its general structure of energy supply. As a specialization of the general principle of subsidiarity (cf. Article 5 (3) TEU), Article 194 (2) subpara. 2 TFEU preserves the Member States' right to act independently also in the area of nuclear energy policy – unless the EURATOM Treaty as *lex specialis* includes particular boundaries of their competences. But – as set out above – the EURATOM Treaty protects the Member States' power to translate its autonomous determination of its energy mix into action without the constraints of the general public procurement provisions.

56

2. Non-Applicability of General Procurement Provisions to other NPP Projects

The Commission practice for decades acknowledged the self-contained character of the EURATOM Treaty with regard to the application of public procurement laws to NPP projects: to our knowledge, the Commission has until this procedure against Hungary not

57

²³ In the preamble to the EURATOM Treaty, the Member States emphasize to conclude the Treaty with the desire *"to associate other countries with their work and to cooperate with international organisations concerned with the peaceful development of atomic energy"*.

²⁴ Opinion of Advocate General Mengozzi delivered on 18 April 2012 in case C-490/10, *Parliament v Council*, para. 33, emphasis added.

initiated any infringement procedures or EU Pilot processes against any EU Member State on an NPP project although a number of Generation III+ NPP projects have been implemented without any tender procedures for the nuclear reactor choice, irrespective of the involvement of contracting authorities or public undertakings as contracting entities which have directly awarded service, supply or works contracts to contractors.

This highlights the Commission's unequal and discriminatory treatment of NPP Projects in different EU Member States.

We are aware of a number of EU nuclear projects which have been launched in recent years, for which it seems that no tendering process for selection of nuclear reactor technology was conducted and which, at first sight, seem comparable to the situation in Hungary. For instance:²⁷

- Kozloduy (Bulgaria 2014)²⁸
- Flamanville 3 (France 2007)²⁹

The Government of Hungary is also aware that in one case where a Member State tendered for a Concession Agreement relating to the co-investment in an NPP and technology provision (Lithuania), the public procurement process failed and led to direct negotiations with a new party with a much more limited bargaining position for Lithuania due to the public failure of the tender. Furthermore the level of equity interest reserved for the State owned utility of the Member State in question and that of other Member States' State owned utilities was determined by Lithuania without a tender for such interests.

E. Alternative Consideration: Directive 2004/17/EC

In any event, the Project and its implementation also comply with the general public procurement requirements under the European Treaties and the Procurement Directives (see I and II) that would only apply, if – contrary to the Government of Hungary's position – the EURATOM Treaty were not *lex specialis* on the NPP contracts.

²⁷ The following list is based on publicly available information. The Government of Hungary has verified the information to the extent possible.

²⁸ Westinghouse Electric Company LLC (US-Japanese company) ("Westinghouse") and Kozloduy NPP plc (a subsidiary of the state-owned energy holding company Bulgarian Energy Holding EAD) signed an agreement in August 2014 for the expansion of the Kozloduy NPP by the construction of a seventh reactor ("Agreement"). The Agreement was approved by the Bulgarian Government. The Agreement provided, amongst other things, that Westinghouse's pressurized water reactor AP 1000 would be used as the reactor for the expansion of the Kozloduy project and that Westinghouse would be responsible for design, engineering and fuel for the new unit.

²⁹ The Flamanville NPP is owned and operated by Électricité de France (EDF). EDF awarded the contract for the supply of the nuclear reactor (European Pressurized Water Reactor) directly to Areva without a formal tender procedure (contract signed in April 2007). The contract included engineering and the construction of the reactor components.

For this hypothetical alternative scenario it could be assumed – hypothetically – that the Utilities Directive would be applicable to the EPC Contract, while the NFSC would in any case be exempt (see 2.).

61

1. Exemption for international agreements under the Utilities Directive

However, even on this assumption, the further Implementation Agreements, in particular the EPC Contract, have been concluded in accordance with the exemption under Article 22 lit. a Utilities Directive ("International Agreement Exemption"). If – contrary to the Government of Hungary's position – the EURATOM Treaty were not *lex specialis* on the NPP contracts, the International Agreement Exemption would apply; and moreover the procurement requirements of the TFEU and the Utilities Directive would still have to be interpreted in the light of the objectives of the EURATOM Treaty.

62

Such International Agreement Exemption provides that a contract may be awarded pursuant to the rules in an international agreement that has been completed in accordance with the Treaty where it relates to the joint implementation or exploitation of a project by two States.

63

I. IGA concluded "*in accordance with the Treaty*"

The IGA has been concluded "*in accordance with the Treaty*" within the meaning of Article 22 lit. a Utilities Directive. Hungary has the competence to enter into the IGA (contrary to LFN, p. 6; see paras. 65 et seqq.) and the IGA complies with EU primary law in substance, in particular with procurement obligations of Hungary (contrary to LFN, p. 5 et seq.; see paras. 100 et seqq.).

64

a) Contract Conclusion Power of Hungary

The conclusion of the IGA, including to determine its own energy mix in accordance with Article 194 of TFEU lies within the competence of Hungary and does not infringe the exclusive competence of the EU under Articles 2 (1), 3 (1) lit. e, 207 and 216 TFEU. The competence for the conclusion of an international agreement on the joint implementation of the sustainment of capacity of a specific NPP between a Member State and a non-EU Member State has not been conferred to the European Union, and thus remains in the competence of the Member State (Article 4 (1), Article 5 (1) TEU).

65

(i) Division of Foreign Relation Powers between the EU and the Member States – Legal Standard for the Determination of an EU Competence

The TFEU and the TEU acknowledge the division of competences between the EU and the Member States. The TFEU confers exclusive and shared competences on the EU (cf. Article 2 (1) and (2) TFEU). Competences not conferred upon the EU in EU primary law (as exclusive or shared competences) remain with the Member States (Article 4 (1) TEU).

66

The limits of EU competences are governed by the principle of conferral (Article 5 (1) sentence 1 TEU) and the use of EU competences is governed by the principles of subsidiarity and proportionality (Article 5 (1) sentence 2 TEU).

The conclusion of international trade agreements with third countries falls into the scope of the CCP for which the exclusive competence has been conferred to the EU (Articles 2 (1), 3 (1) lit. e, 207 TFEU). This competence covers the power to adopt legislation on the conditions for access of companies from third countries to the EU's procurement market and to conclude international agreements on such access.³⁰

The competence for a measure has to be based on objective factors, which are amenable to judicial review, including the objective and the content of the measure.³¹ The key aspect in delineating possible competences for a measure is whether the act in question relates principally to a particular field of action, having only incidental effects on other policies, or whether both aspects are equally essential.³² A measure – as the Commission acknowledges (LFN, p. 6) – falls under the CCP *"only if it relates specifically to international trade in that it is essentially intended to promote, facilitate or govern trade and has direct and immediate effects on trade in the products concerned."*

Article 207 (1) TFEU aims at securing common *"principles"* and preventing Member States from undermining the unity and consistency of the CCP. It can be inferred from this *rationale* that the competence of Article 207 TFEU covers only contracts of a general nature and in practice the contracts concluded by the EU under the CCP are actually of such general nature. The EU is party to numerous multilateral and bilateral agreements on international trade such as the Agreement Establishing the World Trade Organization ("WTO") and subsequent agreements such as the Agreement on Government Procurement ("GPA") and the revised WTO Agreement on Government Procurement ("GPA 2014")³³. They relate to the EU as a whole and have either a regional or a sectorial approach.

(ii) Scope and Effects of the Project is Within the Competence of Hungary

The Commission's position on the scope of the CCP is contrary to the case-law of the ECJ which requires an act to relate *"specifically"* to international trade in order to fall within the scope of the CCP.³⁴ Each international agreement between Member States and third states on the joint exploitation or implementation of a project setting out a specific procurement regime – such as the NPP Paks II Project – has only certain *vague, indirect and incidental* effects on international trade. If these effects were sufficient to bring such projects into the scope of the CCP, the International Agreement Exemption – explicitly

³⁰ ECJ, Case C-360/93 *Parliament v Council* [1996] ECR I-5267, paras. 27 et seqq.

³¹ ECJ, Case C-347/03 *Regione autonoma Friuli Venezia and Ersa* [2005] ECR I-03785, para. 72; Opinion 1/78 *International Agreement on Natural Rubber* [1979] ECR 2894, paras. 36, 52.

³² ECJ, Joined Cases C-164/97 and C-165/97 *Parliament v Council* [1999] ECR I-1153, para. 14.

³³ The GPA 2014 (OJ L 68, 7.3.2014, page 2) entered into force on 6 April 2014.

³⁴ ECJ, Opinion 1/94 *GATS and TRIPS* [1994] ECR I-5267, para. 57.

referring to the conclusion of agreements by *Member States*, but not the EU – would be rendered meaningless, contrary to settled case-law of the ECJ³⁵ which requires every provision to be construed as having a meaningful scope of application. The same would be true as regards Articles 102 to 104 of the EURATOM Treaty.

EU primary law, in particular the EURATOM Treaty (for more details on its interpretative guidance see paras. 110 et seqq.), requires a more balanced and considerate interpretation of the scope of the CCP: In case of infrastructure energy projects, provisions in EU primary law relevant for the assessment of the division of competences between the EU and the Member States in this sector must be taken into due account.³⁶ The exercise of the competences conferred in the field of the CCP shall not affect the delimitation of competences between the EU and the Member States (Article 207 (6) TFEU).

71

EU primary law emphasizes the competences of Member States in the field of (nuclear) energy matters:

72

- Hungary has the competence to *"determine the conditions for exploiting its energy resources, its choice between different energy sources and the general structure of its energy supply"* (Article 194 (2) subpara. 2 TFEU). *"Decisions on energy mix are a prerogative"*³⁷ and *"[i]t is for each Member State to decide whether or not to rely on nuclear electricity."*³⁸ The provision is an expression for sovereignty rights reserved by Member States in the energy sector (see para. 55).³⁹ Also with regard to the NPP Paks II Project, the Commission previously assured the Government of Hungary that *"the Commission respects Member States' basic choices concerning their energy mix"*.⁴⁰ This acknowledgement of the national competence takes due account of the fact that NPP projects need a solid legal basis in the respective Member State's national laws.
- The EURATOM Treaty acknowledges that Member States cooperate with third states for the financing of nuclear projects (Article 46 (2) lit. e EURATOM Treaty).

³⁵ ECJ, Case C-2/08 *Abraham et al.* [2008] ECR I-1223, paras. 29 et seqq.; Case 90/83 *Paterson v Fedel* [1984] ECR, paras. 26 et seq.

³⁶ On the requirement of balancing the objectives included and expressed in EU primary law (based on the example of environmental protection) cf. ECJ, Case C-379/98 *Preussenelektra* [2001] ECR I-2159, paras. 70 et seqq.

³⁷ European Commission, Communication from the European Commission to the European Parliament and the Council of 28 May 2014 – European Energy Security Strategy, COM (2014) 330 final, p. 17.

³⁸ European Commission, Communication from the Commission to the European Council and the European Parliament of 10 January 2007 – An Energy Policy for Europe, COM (2007) 1 final, p. 18.

³⁹ Opinion of Advocate General Mengozzi delivered on 18 April 2012 in case C-490/10, *Parliament v Council*, para. 33.

⁴⁰ Letter of Commission President José Manuel Barroso to Prime Minister Viktor Orbán, 7 February 2014, Barroso (2014) 153242 and 294667.

- Further, Articles 103 et seqq. EURATOM Treaty acknowledge the Member States' competence to enter into international agreements for the construction of an NPP in its territory.⁴¹

(iii) Not Within EU Competence for Common Commercial Policy

The IGA is not an international trade agreement within the meaning of the CCP. It neither establishes a general legal regime for (nuclear) energy cooperation nor regulates the access by Russian or (non-)EU Member State companies to the Hungarian procurement market.

73

(1) Individual Project, not General Common Market

The IGA does not qualify as a general act. It does not establish – in contrast to the cases decided by the ECJ⁴² – a bilateral system of general rules on the access to markets including the general procurement market. The IGA forms the legal basis for the capacity sustainment by one single NPP project and relates to financial and technical cooperation on a state-to-state level for this specific and clearly defined energy infrastructure project. Also taking into consideration its economic effects it is apparent that the impact of the IGA on the European internal market and thus on the CCP is clearly confined and limited in volume. The IGA has no direct effects on the CCP (on the economic effects see also paras. 75 et seqq.).

74

(2) General Access of Russian Companies to EU Market

Based on a misconception of the scope of the IGA the Commission holds that Hungary committed itself to *"open a substantial section of its public procurement market to one third country and, by necessary implication, close the same section of the public procurement market to operators from all other third countries and the EU"* (LFN, p. 6).

75

However, the EU procurement market is already open for access by Russian companies. The EU has not taken restrictive measures for Russian companies on tenders comprising products originating in third countries and relations with those countries (Article 58 et seq. Utilities Directive).

76

⁴¹ As confirmed by the European Commission in its letter of 14 January 2014, the IGA does not impede the competences of EURATOM.

⁴² ECJ, Case C-360/93 *Parliament v Council* [1996] ECR I-5267, para. 30. In this case the Community had concluded a Memorandum of Understanding ("MoU") with the United States on government procurement and relevant implementation measures by the Community. The MoU included a *"duty to extend the benefits of Directive 90/531 to US products, suppliers and contractors"*. The IGA does not include a general duty to extend the benefits of the European procurement regime to companies from Russia. It only relates to an individual project. Russian companies do not enjoy the benefits of the European procurement regime under the IGA and will still have to be treated as third country companies.

(3) No Market Foreclosure

The IGA did not foreclose a substantial section of Hungary's public procurement market. To the contrary: After several years of market evaluation and discussion with the few suppliers of the Generation III pressurized water reactors (PWR) in the world, the Russian party was the only one able to offer the required reactors together with the financing necessary for this highly capital-intensive and complex NPP project (cf. also paras. 96 et seqq.). In particular Hungary was advised that neither the [redacted] nuclear technology provider [redacted] nor [redacted] providers were able to offer a similar package for the EPC Contract for generation III+ technology, including the fixed-price turnkey contract nature and the related financing and temporary nuclear waste storage option. Hence, factually there were no operators from the EU or elsewhere that were foreclosed from access to the Hungarian market or the Project.

77

Contrary to the Commission's assumption (LFN, p. 6), the IGA did not foreclose this project from others, but – to the contrary – obliged the contractor to the Procurement Policy included in the IGA and set forth in the ECP and thereby ensures access of others to significant parts of the Project on the level of the Sub-Agreements (see paras. 35, 91).

78

Further, the IGA only refers to one specific, clearly defined project, but does not generally limit the access to a whole market section (see also para. 74).

79

(4) International Law

The Government of Hungary has discretion to choose its partners for cooperation on a state-to-state level. This is also acknowledged in the GPA/GPA 2014 which does not apply to contracts for projects on the basis of an international agreement. The GPA 2014 provides for its inapplicability to procurement conducted "*under the particular procedure or condition of an international agreement [...] relating to the joint implementation by the signatory countries of a project*" (Article II 3 (e) ii. GPA 2014). The EU made a similar reservation to the GPA in its General Note which applied prior to the GPA 2014.⁴³ The rationale of the exemption is to promote – in the light of the goals of the WTO – international cooperation and economic integration even if such cooperation does not extend the GPA procurement rules to third states.⁴⁴

80

⁴³ According to the General Note of the EU ("General Notes and Derogations from the Provisions of Article III", Annex I to the Plurilateral Agreement on Government Procurement (GPA)), the GPA did not apply to contracts awarded under "*an international agreement and intended for the joint implementation or exploitation of a project by the signatory States*" (cf. General Note of the European Community No. 4 of 14 January 2003; WT/Let/438).

⁴⁴ The United Nations Conference on International Trade Law (UNCITRAL) also advises in its Model Law on Public Procurement (United Nations Document A/66/17, Annex I) that in case of obligations from treaties or other forms of agreements with one or more other states the requirements of the treaty or agreement prevail over the procurement law (Article 3 lit. a).

(iv) **Authorization of the Member States to Agree on Procedural Rules on Procurement in International Agreements**

Even if the EU – contrary to the Government of Hungary's opinion – in general was competent, Article 22 lit. a Utilities Directive in connection with Article 2 (1) TFEU authorized the Member State to agree on procedural rules for the organization and award of project contracts in an international agreement, as Hungary did in the IGA. 81

Member States may legislate and adopt binding acts in the areas of exclusive competence of the EU if they are "*empowered by the Union or for the implementation of Union acts*" (Article 2 (1) TFEU). The EU may empower the Member States also in a directive or in a regulation.⁴³ 82

Article 22 lit. a Utilities Directive authorizes the Member State to agree on "*procedural rules*" for the organization and award of project contracts in an international agreement. The IGA contains such procedural rules for contracts (and does not go beyond that scope, in particular does not contain general rules on market access, see paras. 74 et seqq.). 83

II. Different Procedural Rules

The IGA sets forth "*different procedural rules*" within the meaning of Article 22 lit. a Utilities Directive (contrary to LFN, p. 5). The cooperation under the IGA is structured by specific procedural requirements on the conclusion of the Implementation Agreements and Sub-Agreements. 84

a) Conclusion of Implementation Agreements

The IGA sets forth the procedural rules for the conclusion of the Implementation Agreements. The IGA requires that each party to the IGA identifies public entities in their respective countries for the conclusion of the Implementation Agreements: The respective Competent Authorities have to designate a state-owned and state-controlled Authorized Organization and to notify its choice to the other party (Article 3 (1), (2) IGA) (see para. 29). Pursuant to the IGA the notion of "state-owned and state-controlled" requires a direct or indirect state ownership (or equivalent) of not less than 95% of the participation and voting rights (or equivalent) (Article 3 (3) IGA). The Russian Competent Authority, Rosatom, has to designate the Authorized Organization from its group of companies (Article 3 (1) IGA). The IGA also sets out specific requirements the Authorized Organizations have to fulfil, in particular with regard to their financial and technical capability to implement the Project (Article 3 (1), (2) IGA). Any replacement of the Authorized Organization requires the prior written consent of the other party's Competent Authority (Article 3 (4) IGA). 85

⁴³ ECJ, Case C-174/84 *Bulk Oil* [1986] ECR 576, paras. 31 et seqq.

Further, the cooperation under the IGA – and therefore also the designation of the Authorized Organisations – has to comply with the applicable laws of Hungary and the Russian Federation (Article 11 (1) IGA). This includes the national procurement laws of both parties.⁴⁶ Thus, in addition to the procedural rules set out in the IGA itself, this reference introduces additional procedural requirements for the conclusion of the Implementation Agreements. 86

The Authorized Organizations, i.e. NIAEP and Paks II, have to conclude – and after consultation with the European Commission meanwhile have concluded – three Implementation Agreements (Articles 3 (5), 8 IGA), in particular the EPC Contract and the NFSC.⁴⁷ 87

Neither the EPC Contract nor any other contract was awarded by or within the IGA (contrary to LFN, p. 2, 5 et seqq.). The IGA does not award anything. It is an international agreement between states subject to public international law. The EPC Contract could in accordance with the IGA only be concluded by Paks II and NIAEP pursuant to the procedural rules of the IGA. 88

b) Conclusion of Sub-Agreements

NIAEP awards works and services as general contractor under the EPC Contract to sub-contractors by entering into Sub-Agreements (Article 3 (6) IGA). 89

These Sub-Agreements are envisaged to cover a substantial part of the Project volume. NIAEP is obliged – as further set forth in the IGA and the EPC Contract – *"to carry out procurement procedures in accordance with the principles and general requirements of transparency (including prior publication of contract notices EU-wide in the English language), equal treatment and non-discrimination as well as independent review regime"* (Article 3 (6) IGA). This clause establishes that NIAEP is obliged to tender the Sub-Agreements in the European Union. 90

If the EPC Contract were awarded to NIAEP in an EU-wide tender without the IGA, such an obligation would not exist for NIAEP. Thus, for all practical purposes the IGA ensures more competition and more public procurement for the Project than any other solution. The Sub-Agreements will cover significant elements of the Project for which companies in the EU are capable of tendering and offering, unlike the comprehensive fixed-price turnkey EPC Contract for which no EU company has the scope or resources to offer 91

[REDACTED] a fixed price solution including financing for up

⁴⁶ At the time of signing the IGA, the Russian procurement regime was in particular included in Federal Act 44-FZ of 5 April 2013 on public procurement.

⁴⁷ For details on the Implementation Agreements see paras. 29 et seqq.