

DECISION No. 316

Of 29.11.2004

concerning the measure of financial support granted

by the Ministry of Economy and Trade to

S.N.P Petrom S.A.

THE COMPETITION COUNCIL,

Having regard to the provisions of Decree No. 57/2004 for the appointment of the members of the Competition Council,

Having regard to the provisions of the Competition Law no.21/1996, published in the Official Gazette, Part I, no. 88 of April 30, 1996, amended and completed by GEO no. 121/2003 approved by Law no. 184/2004,

Having regard to the provisions of the Law on State Aid no. 143/1999, published in the Official Gazette, Part I, no. 370 of 03.08.1999, amended and completed by Law no. 603/2003,

Having regard to the provisions of the Europe Agreement establishing an association between Romania, on one hand, and the European Communities and their Member States, on the other hand, ratified by Law no. 20/1993, published in the in Official Gazette, Part I, no. 73 of 12.04.1993,

Having regard to the provisions of the Regulation regarding state aid for the protection of the environment, published in the Official Gazette, Part I, no. 470 of 2 July 2002,

Having regard to the provisions of the Regulation for the amendment and completion of the Regulation regarding state aid for the protection of the environment, published in the Official Gazette, Part I, no. 521 of 9 June 2004,

Based on the following:

I. PROCEDURE OF NOTIFICATION

Under Note no. 102186/DIP/14.09.2004, registered at the Competition Council under no. RG 6480/14.09.2004, the Ministry of Economy and Commerce (MEC) notified, on the basis of Article 6 of the Law no. 143/1999 on State aid with subsequent amendments and completions, the measures of financial support to be granted to S.N.P Petrom SA.

II. DESCRIPTION OF THE MEASURE

II.1. SNP Petrom SA. The description of the company's activity and financial situation. Information about the relevant market.

(1) The National Oil Company "Petrom" SA was established by Emergency Government Ordinance No. 49/1997. SNP Petrom carries out the following activities:

- exploration and production: the former state autonomous regie "PETROM" RA
- refining: the petrochemical plants Petrobrazi and Arpechim, the chemical fertilizer plant Doljchim, INCERP
- transport: the infrastructure of the road transport of oil products (Transpeco Bucharest branch)
- distribution: 41 PECO branches, in each county and in Bucharest City.

(2) The social capital of SNP Petrom SA on June 30, 2004 is of ROL 38,210,381,859 thousands, being held by the Romanian state, through the Ministry of Industry and Commerce in proportion of approximately 93.05% and by private investors approximately 6.95%.

(3) SNP Petrom SA has as activity object, mainly, the exploring and exploiting of oil and natural gas deposits on-shore and from the continental shelf of the Black Sea,

refining and processing crude oil, transport and marketing of gas, crude oil import and export, oil products, machinery, equipments and specific technologies.

(4) The company produces crude oil, natural gas, diesel oil, petrol, fuel oil, CLU, LPG, gasoline, ethane and other refined products. SNP "Petrom" SA carries out oil operations in 225 exploitation - development and exploration blocks. The 2002 production was 5810 thousands tons of crude and condensed oil, 6062 million standard cubic meters of natural gas, 179 thousands tons of gasoline and 76 thousands tones of ethane, mostly from old and mature fields as new technologies meant to improve the condition of wells and fields were intensively used..

(5) The relevant markets on which the company is acting are: the market of exploring and exploiting oil and natural gas ores, on-shore and on the continental shelf of the Black Sea, the crude oil refining and processing market and that of the oil products' distribution and commercialization.

(6) S.N.P. "Petrom" S.A. markets its products on the domestic market as well as by export. The main customers are: S.C. Distrigaz Sud S.A., S.C. Distrigaz Nord S.A., S.C. Termoelectrica S.A., S.C. Electrocentrale S.A., S.C. Rafinaria Astra S.A., S.C. Rafinaria Steaua S.A., S.C. Petrolsub S.A., S.C. Rompetrol Rafinare S.A. Petromidia, S.C. Rafo S.A., S.C. Interagro S.A., S.C. Siderurgica S.A., S.C. Republica S.A., S.C. Oltchim S.A., towards which the company delivers crude oil and natural gas. The company also exports oil products through its own refineries Arpechim Pitesti and Petrobrazi Ploiesti towards different customers, through sale at the Commodities Exchange.

(7) The market position of SNP Petrom :

a) The sector of crude oil and natural gas exploration and production

Although many foreign companies are involved in exploration activities (such as Ramco, Tullow), SNP PETROM carries out most of the successful exploration operations.

A.1. Crude oil - SNP Petrom SA is the only crude oil producer in Romania, without any other competitor in this activity field.

A.2. Natural Gas - SNP Petrom SA realizes approx. 35% of the domestic production of natural gas. The other operator on the market is Romgaz, which covers 43% of the domestic consumption of natural gas of Romania.

b) Refining sector - SNP Petrom SA owns two of the most important refineries in Romania (Petrobrazi Ploiesti and Arpechim Pitesti) with a total operating capacity of 8 mill. T/year. Both refineries have a high Nelson complexity index, comparable with the refineries from West Europe, as well as important stockpiling capacities. In 2002,

the two refineries represented together 35.7% of the operational refining capacity in the sector and 55% of the total processed crude oil.

c) Distribution and Marketing – The distribution and commercializing activity for the refined products is totally liberalised and open to competition, starting with 1994. SNP Petrom is the leader in retail sales, with 42% of the gasoline sales and operates almost 29% from the total filling stations. Among the company's important competitors we find: Rompetrol, Shell, MOL, OMV, Lukoil and Agip. From the total filling stations approx. 57% are private stations which do not operate under one brand name, representing 20 – 25% of the total sales of fuels in the distribution network.

(8) The economical - financial situation of S.N.P. PETROM S.A. is presented in the following tables:

Table No. 1 **mil.**
ROL

No.	Indicator	Financial year		
		2001	2002	2003
	TURNOVER of which:	55,905,016	72,721,218	71,345,927
	- on the Romanian market	45,905,208	51,861,146	50,575,247
	- exported	9,861,510	20,540,181	19,833,688

Source: Petrom balance sheets

Table No. 2 **mil.**
ROL

No.	Indicator	Financial year		
		2001	2002	2003
	GROSS PROFIT	4,318,825	3,346,831	3,198,260
	NET PROFIT	2,717,479 (97,467 mil €)	2,282,082 (65,379 mil €)	1,440,494 (35,034 mil €)

Source: Petrom balance sheets

III. THE DESCRIPTION OF THE PRIVATISATION PROCESS

(9) In December 2002, following an open tender procedure, MEC, through OPSPI, appointed as financial advisers a consortium comprising Credit Suisse First Boston (Europe) Limited and ING Bank NV, London Branch (the “Advisers”).

(10) Following due diligence on Petrom (from January 2003 to May 2003) the Advisers along with their consortium members (which included specialist legal, environmental, accounting and oil & gas reserve audit experts), submitted their privatisation strategy to the MEC in May 2003.

(11) Following the Advisers' reports and recommendations, and in order to obtain an optimal combination of contribution to the State budget and much needed investments into Petrom, in August 2003 the Government adopted the privatisation strategy for Petrom that provided, *inter alia*:

- that the long term future of Petrom should be ensured through maximising the level of investment into it and the transfer of know-how to improve Petrom's operating efficiency;
- that the privatisation would aim to attract strategic investors active in the oil industry that can identify the opportunities to make efficient use of the company and create added value;
- that a 51% stake in Petrom will be made available to such strategic investors, through a combination of a direct sale by the MEC of 33.34% of the existing shares of Petrom and a simultaneous share capital increase and issuance of new shares in favour of the strategic investors.

(12) A privatisation announcement was published in the Romanian and international business press (including the *Financial Times*, international edition, on 26 August 2003). The announcement called for expressions of interest from strategic investors that fulfilled the following criteria: (a) had annual revenues from oil and gas activities in excess of U.S.\$ 1,000 million for the last three years; (b) possessed technical and managerial expertise of a minimum of three years in the oil and gas sector, appropriate to the size of the proposed privatisation; and (c) were able to provide a bank reference letter issued by a reputable bank. Consortia were also allowed, on the condition that at least one of the members of the relevant consortium qualify as a strategic investor and the combined turnover of the consortium from oil and gas activities for the last three years be in excess of U.S.\$1,300 million.

(13) The purpose of the prequalification process was to maintain the highest standards of quality of bidders and to filter out short term financial investors whose primary objectives may not have been in line with the Government's strategy for Petrom.

(14) Following the publication of the privatisation announcement, 15 expressions of interest were received from investors from Europe (within and outside the EU), the Middle East and the United States of America:

- (i) Alon Inc., USA ("**Alon**")

- (ii) Conoco Phillips, UK
- (iii) Eni Spa, Italy (“**Eni**”)
- (iv) Gazprom, Russian Federation (“**Gazprom**”)
- (v) Glencore International A.G., Switzerland (“**Glencore**”)
- (vi) Grup Sicomiga Single Man Ong Profit, Romania
- (vii) Halliburton, USA and Regal Petroleum Plc., Great Britain and S.C. Tender S.A., Romania
- (viii) Hellenic Petroleum S.A., Greece (“**Hellenic Petroleum**”)
- (ix) Kanooz Al Watan Oil and Energy Division, Saudi Arabia and Maple Resources Corporation USA
- (x) MOL plc, Hungary (“**MOL**”)
- (xi) Occidental Oil and Gas Holding Corporation, USA (“**Occidental**”)
- (xii) OMV AG, Austria (“**OMV**”)
- (xiii) Phoenix Oil LTD, Cyprus
- (xiv) PKN Orlen S.A., Poland (“**PKN**”)
- (xv) TNK – BP, Great Britain and the Russian Federation

(15) On 3 October 2003, following the review of the relevant documentation filed together with the expressions of interest and based on the recommendations of the Advisers, MEC, through OPSPI, short-listed the following 11 investors to participate in the privatisation process: Alon, Conoco Phillips, Eni, Gazprom, Glencore, Hellenic Petroleum, MOL, Occidental, OMV, PKN Orlen and TNK – BP.

(16) Eight of the eleven short-listed investors then signed a confidentiality agreement and purchased the presentation file. Starting from 13 October 2003, they were allowed to access a physical and a web-based electronic data room maintained by Petrom. They were also given ample opportunity to meet with the management of the company and perform site visits. The due diligence process continued until the beginning of April 2004.

(17) An initial draft of the privatisation agreement was distributed to all eight potential investors, who were asked to comment as part of their preliminary non-binding offers. Each bidder received the same revised draft (all bidders were treated equally).

(18) Investors were required to submit their preliminary non-binding offers by 24 November 2003, requiring them to highlight major issues identified during the initial due diligence process and submit a mark up of the preliminary draft

privatisation agreement circulated by MEC/OPSPI. Six pre-qualified investors submitted preliminary, non-binding offers. These included: Gazprom, Hellenic Petroleum, Occidental, OMV, MOL and PKN Orlen.

(19) All bidders who submitted the preliminary non binding offers were invited for discussions on the draft privatisation agreement at the headquarters of OPSPI in Bucharest with a view to providing the bidders with an opportunity to comment and express their opinions on the draft agreement. These negotiations were held in a non-discriminatory and transparent manner, with all potential bidders being given an opportunity to express their comments on the proposed contractual framework both in writing and in interactive sessions held at OPSPI's headquarters in Bucharest. Following each round of discussions, MEC/OPSPI provided revised drafts of the privatisation agreement and other associated contractual documents.

(20) A final draft of the privatisation agreement was distributed to all potential bidders (i.e. Gazprom, Hellenic Petroleum, Occidental, OMV, MOL and PKN Orlen) on 12 March 2004 for the purposes of formulating their final binding bids.

(21) The draft of the privatisation agreement, which was available to all the bidders without discrimination, contained as following:

- provisions related to the granting of an indemnities for historical pollution and certain abandonment costs;
- The cancellation of overdue historical tax obligations and penalties.

(22) On April the 8th, 2004, the Advisers sent to all bidders confirming letters referring to the obligations owed to the state budget by S.N.P. PETROM S.A.. These letters requested that the final offer be made by taking into consideration that by the coming into force of GO no. 15/2004 regarding the regulation of certain financial measures, the company does not owe any taxes or duties towards the general consolidated state budget.

(23) The date on which the final binding bids were due was set for 15 April 2004. On the announced deadline for the submission of final offers, three investors submitted their proposals for the privatisation of Petrom: OMV, MOL and Occidental.

(24) Based on the review of the offers submitted by these three candidates, MEC, through OPSPI, decided to start direct discussions with OMV, who had offered the highest price, with a view to reaching a final agreement on the contractual framework applicable to this transaction. The privatisation agreement between MEC/OPSPI and OMV (the "Privatisation Agreement") was signed on 23 July 2004.

(25) On the basis of the above, the Competition Council concludes that the privatisation of Petrom has been effected by means of a fully transparent, non-discriminatory and open bidding procedure:

- a competitive tender has been held, open to all oil industry players, transparent and unconditional and allowed a broad range of oil and gas companies to participate;
- the terms for bidding and the tender rules were the same for all the six bidders which clearly and unequivocally expressed their intention to purchase a majority stake in SNP Petrom S.A.;
- the Privatisation Agreement has been concluded with OMV, who was the highest bidder; and
- all bidders were given sufficient time (between October 2003 and April 2004) and information (access to a physical and web-based electronic data room, opportunity to meet with the management and to perform site visits, access to the draft of the Privatisation Agreement) to carry out a proper evaluation of Petrom as the basis for their final bid.

(26) This procedure ensured that a competitive price reflecting the fair market value of Petrom was reached, in accordance with market economy principles, as all factors influencing the value of Petrom were discussed during the negotiations and reflected in the price eventually offered by the bidders.

IV. Presentation of the financial incentives provided in the Privatization Agreement an The Draft Law on privatization of SNP Petrom SA.

- A. Environmental Indemnity
- B. Overdue historical tax obligations
- C. Royalties
- D. E&P Taxation Stability
- E. Geological quota

IV.1 Environmental Indemnity

(27) The Environmental Indemnity is a contractual arrangement whereby the State agrees to take responsibility for any unknown, un-quantified liabilities that may arise in the future for Petrom from the effects of pollution caused prior to privatisation. The purchaser is responsible for ensuring future compliance with environmental laws and shall be responsible for any pollution caused after closing, as well as for past pollution that was known and quantified at the time of signing the Privatisation Agreement.

(28) [...]¹

(29) The Privatisation Agreement includes a list of all existing compliance schedules and the amounts associated with the quantifiable obligations, amounting in the aggregate to Euro 178,5 million. This amount was accepted by OMV as an existing obligation of Petrom and was factored into OMV's valuation of Petrom.

(30) [...]¹

IV.2 Overdue historical tax obligations

(31) In accordance with the Privatisation Agreement, all taxes, levies, duties, imposts, charges and withholdings in the nature of taxation due by Petrom in respect of any financial year up to and including 31 December 2003 and all penalties of any kind relating thereto which were incurred up to 8 April 2004 have been paid or cancelled and Petrom shall no longer have any liability in respect thereto. This has been enacted by Emergency Government Ordinance No. 15/2004 and is also provided in Art. 11 of the Draft Law for privatisation.

IV.3 Royalties

(32) The Privatisation Agreement provides that the current percentage level, basis and manner of calculation of royalties payable by Petrom in accordance with the concession agreements concluded by Petrom with the competent authority (the "Individual Concession Agreements") shall be maintained for a period of ten years as of the Closing Date. This provision is to be found as well in Art. 15 of the Draft Law as such as stability in the field of royalties is to be applied at the request of all owners of individual agreements of concession in the field of exploration and exploitation of oil and natural gas ores.

IV.4 E&P Taxation Stability

(33) The Privatisation Agreement contains a stand-still provision for E&P Taxation (Exploration and Production Taxation). This provision is of general validity, in the sense that it is to be applied during the entire period in which are applicable to Petrom and other companies which undertake exploration and exploitation of oil and natural gas in Romania. Thus, except as it may be otherwise required under EU-wide laws or regulations that become applicable to Romania, certain provisions of the Fiscal Code of Romania relating to provisioning, depreciation, deductible expenses and taxation regime applicable to the activities of exploration and production shall remain in force until 31 December 2014 and shall not be amended to the detriment of Petrom.

(34) The provisions of the Fiscal Code to which the Privatization Agreement refers contain certain specific rules related to companies in E&P sector. It should be noted

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that this refers to specific E&P taxation (“the taxation regime applicable to the exploration and production activities of the Company”), so it does not encompass generally applicable taxes such as profit tax, VAT etc.

IV.5 Geological quota

(35) [...] ²

(36) The expense quota for the development and modernisation of crude oil and natural gas production, refining, transportation and distribution of oil products, as provided in the Government Decision No. 168/1998, and such quota was applied by Petrom until privatisation. The Privatisation Agreement provides that this tax incentive shall be maintained for a limited period of time, namely until 31st of December 2006.

(37) [...] ²

(38) [...] ²

V. The assessment of the financial measures provided in the Privatization Agreement and the Draft Law for privatization of SNP Petrom SA

V.1 The character of State aid

A. The Environmental Indemnity

(39) The financial measures from state resources granted to certain undertakings to facilitate the repair of damages to environment for rehabilitation of industrial sites may be assessed according to the Regulation on State aid to environment protection. Normally, no aid for environment protection is allowed if the polluter may be clearly identified. The polluter has to finance the rehabilitation of environment damages according to the “polluter pays” principle.

(40) According to the Regulation on State aid for environment protection, actions focused on the protection of the environment may yield benefits in the form of an increase in sustainable development, higher employment rates and competitiveness, and the effective application of the “polluter pays” principle as well as the total internalisation of environmental costs, by imputing such costs to the polluters, represent the main instruments for achieving these objectives.

(41) [...] ²

(42) Petrom’s environmental position was assessed by three internationally reputed environmental consultants, as follows: Dames & Moore in 1999, Nexant in 2001 and URS Corporation in 2003 (the latter being part of the consortium advising MEC on the privatisation). In their reports, all three consultants made it clear that the liabilities associated with historical contamination are extremely difficult to assess. The 2003 URS report reads that *“even for refinery sites that have had a series of assessments*

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undertaken, there are still no reliable assessments of the magnitude of contamination, the potential need for regulatory –driven remediation and associated clean-up costs”. Similarly, the report states “Soil & groundwater issues are typical of oil production, refining and transportation & distribution companies and primarily relate to the leakage and/or spillage of crude oil and petroleum products. Spills and leaks may arise from old or poorly maintained pipes, storage tanks or processing plant and may lead to the soil and groundwater below facilities becoming contaminated with hydrocarbons and other substances. This contamination may migrate from the site within sub-surface groundwater flows leading to impacts outside of site boundaries”.

(43) One of the main reasons why the historical liabilities are difficult to assess is their very nature of being contingent, rather than actual liabilities. In this respect, the 2003 URS report states that: “[...], soil and groundwater contamination is common at oil industry sites worldwide. It is important to recognize that contamination itself does not necessarily directly lead to an environmental liability.

(44) As a state-owned company, Petrom has inherited most of its asset base from the state-owned oil industry operating in Romania for more than 50 years in a legal framework which, at least during the communist era, was little concerned with environmental issues. In certain areas (such as the Ploiesti area) the causes of pollution and the attribution of liability is further complicated by the fact that multiple refineries operate within the same general area and the area was subject to extensive bombing by allied forces during the second world war.

(45) While Petrom has of late directed significant investments in improving its operations, historical pollution remains difficult to assess and to remedy, primarily due to the fact that Petrom’s operations are spread at thousands of locations all over Romania. Petrom owns and/or operates a large number of sites (approximately 2,000) spread all over Romania, including oil fields, storage facilities, refineries, a fertilisers plant, and retail filling stations. These sites are, from an environmental standpoint, subject to the jurisdiction of the local environmental authorities and the environmental consultants have noted significant variability of the environmental operating permits and the compliance schedules throughout the country, which make it impossible to determine whether the costs for contamination issues set out in the compliance schedules cover all known issues adequately. As for the unknown issues, an attempt to identify them would involve a portfolio-wide comprehensive (Phase 2) study, involving intrusive investigation on the contaminated sites, which was estimated to take 2 years to complete without giving certainty in relation to the extent of the potential liabilities.

(46) The Competition Council takes into account that the pollution caused by the company in the years when it was passed from the State owned economy to the market economy, cannot be blamed to the undertaking as the actual responsibility for pollution is of the state. Under those circumstances, the company cannot be forced to pay the

historical environmental damages, according to the principle “the polluter pays”. Though the company made significant investments (during 2000-2003 over USD 250 mil.) for adapting to the international environmental standards, and closed an important proportion of the polluting installations, the total removal of the causes pollution generating was not possible. In the same time, the impossibility to eliminate the polluting sources lead to the increase of the environmental damages produced by the company.

(47) The Competition Council finds that SNP Petrom’s privatization process was transparent, open and unconditioned, without giving any advantage to the investor OMV. Specifically in relation to the historical pollution issues, the final draft of the Privatisation Agreement circulated to all bidders on 12 March 2004 included specific and detailed provisions relating to the availability of an environmental indemnity from the state in connection with liabilities arising from such pollution.

(48) For SNP Petrom SA, total quantification of the historical environmental damages was impossible, as evidenced by the conclusions of the experts hired for this purpose.

(49) The state’s responsibility was limited as follows:

- the exclusion of the amounts covered by the provisions already created by Petrom in respect of abandonment, amounting to approximately Euro 22.3 million;
- the exclusion of known, quantified remedial action amounting to approximately Euro 178.5 million; and
- the undertaking in relation to abandonment liabilities will be valid for 30 years after the Closing Date, whereas that in relation to environmental losses will expire 15 years after the Closing Date.

B. Overdue historical tax obligations

(50) Any waiver of State debts, which confers an advantage to an undertaking has to be assessed in accordance with the State aid Law no 143/1999, with subsequent amendments and completions.

(51) [...] ³

(52) After the adoption of G.O nr. 15/2004, in implementing the write-off of Petrom’s tax obligations, MEC has notified the facilities to Competition Council for authorization.

(53) The Competition Council issued the Decision no. 155/17.05.2004 on the authorization of individual aid granted to SNP Petrom SA. The State waived the debts of the Company and these incomes had to be used by SNP Petrom SA as financial

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source for an investment plan during the period 2004-2007. The State aid was authorized having as its objective the regional development according to the Regulation on regional aid and Multisectoral Regulation on regional aid for large investment projects.

(54) By the Note no. 102.186/DIP/14.09.2004, MEC re-notified the fiscal facility granted by G.O no. 15/2004, under these reasons:

- the price offered by OMV reflects the cancellation of fiscal obligations and the State acted as a private investor in the market economy. As a consequence the facility concerned is not State aid;

- when it notified to the Competition Council the individual State aid granted to SNP Petrom SA on the basis of G.O. no.15/2004, MEC failed to take into account the fact that the measures are part of the necessary and complex conditions for privatization and as a consequence the measures cannot be assessed in isolation.

(55) The Competition Council found that the bidding procedure was open, transparent and unconditional. No advantage was conferred to the investor (OMV) which has offered the market price and, as a consequence no State aid was provided to OMV.

(56) In relation to the advantage offered to SNP Petrom SA, the Competition Council assessed to what extent the State has acted as a private investor. Any existing tax obligations would in any event have resulted in a corresponding deduction from the enterprise value of Petrom and, consequently, a reduction in the price offered by the bidders. Moreover, Petrom's outstanding tax obligations were difficult to assess because certain of these obligations were disputed by the company. As the tax liabilities could not be quantified, but all bidders were assured that Petrom would be free of such old liabilities, it was the most appropriate solution to cancel these obligations as any other solution, e.g. decreasing the price to be paid, could have wrongly estimated the amount concerned. This might have created an disadvantage either for OMV or the State.

(57) If these obligations had not been cancelled, the price offered by the bidders would have been discounted so that the burden of having to pay such obligations was taken into account (the final equity valuation of a company is always arrived at by subtracting the amount of debt from the enterprise value). It can therefore be said that the overdue historical budgetary obligations were paid by OMV as part of the price paid in the privatisation process and that the State's "loss" as a result of such obligations not being paid by the company was recovered through the corresponding increase in upfront revenues - the price paid by the investor.

(58) Furthermore, the cancellation also does not constitute an advantage to Petrom, as the tax liabilities were disputed and it is highly unlikely that the Romanian State could have recovered these amounts. Historically, many of these obligations proved impossible to collect. The solution of cancelling all outstanding tax obligations was

perceived to be the most likely option to maximise the net proceeds from the privatisation payable to the State. The State has thus acted as a private investor would have done in similar circumstances.

(59) In conclusion, the Competition Council considers that the annulment of the overdue fiscal obligations does not constitute State aid. This facility was part of the package submitted to any possible investors in the course of a transparent and open tender procedure as a result of which a fair market value was arrived at. By acting in this manner, the State has complied with the private investor principle.

C. The Royalties paid in accordance with the Individual Concession Agreements

(60) It is the policy of the Romanian state, endorsed by the Government and the National Agency for Mineral Resources, to make the best use of the existing reserves still available in Romania. As many of the existing oil and gas fields are in an advanced stage of depletion, a higher royalty would increase the already high costs of extracting oil from those fields and make their exploitation unsustainable from the economic standpoint. As Romania's reserves will continue to decline over the coming years, an increase in royalties is not envisaged because it is economically unjustified.

(61) Both the Petroleum Law No. 134/1995, which was in force until recently, and the new Petroleum Law currently in force, Law No. 238/2004, include provisions to the effect that the petroleum agreement remains in force for its entire duration, save for the adoption of legal provisions more favourable to the holder of the petroleum agreement. Since the provisions of petroleum agreements include rules regarding the level and payment of royalties, it may be inferred that the above-mentioned legal provisions refer to royalties as well. In addition, according to Article 30 of Petroleum Law no. 238/2004, the concession is concluded by agreement between the National Authority for Mineral Resources and Romanian or foreign legal entities selected by a public request for offers.

(62) The stand-still in respect of the percentage level and calculation of the royalties paid by Petrom pursuant to the Individual Concession Agreements was provided by OMV in its final offer and, this provision is reflected in the price paid. If this provision had not been included in the Privatisation Agreement, OMV, as any other of the bidders, would have had to take account of a possible increase in the concession duties (which form part of its production costs) and would thus have offered a lower price. In these circumstances the state chose to offer the limited stand-still in respect of the percentage level and calculation of the royalties in exchange for a higher price. These provisions are to be applied at request to all owners of individual concession agreements in the field of exploration and exploitation of oil and natural gas ores.

(63) The Competition Council considers that the state acted as a private investor would have acted in similar circumstances in order to create the conditions for obtaining the best possible price. In addition, the way of royalties are established does not involve State aid taking into account the fact that the percentage level is set out by law in a transparent and non-discriminatory manner.

D. E&P Taxation Stability

(64) As regards this stand-still provision of the privatization Agreement, it should be noted that this refers to specific E&P taxation (“the taxation regime applicable to the exploration and production activities of the Company”), so it does not encompass generally applicable taxes such as profit tax, VAT etc.

(65) The reasons invoked by MEC support the idea that this measure does not involve state aid as the state do not intend to modify the Taxation E&P or the introduction of new taxes and moreover the State acted as a private investor in similar circumstances. The State agreed with the measure in the Privatization Agreement for keeping the purchase price for Petrom at a higher level than it would have been able to obtain without providing such comfort. Apart from OMV also other bidders have expressed their interest in maintaining the E&P taxation at the current level, as this is an important part of the production costs, with a direct influence on the value of the company.

(66) The State does not have in its view to grow the taxation in E&P sector as many of the existing oil and gas fields are in an advanced stage of depletion, a higher taxation would increase the already high costs of extracting oil from those fields and make their exploitation unsustainable from the economic standpoint. As Romania's reserves will continue to decline over the coming years, an increase in taxes is not envisaged because it is economically unjustified. OMV insisted that it receive legal certainty from the seller/MEC as regards stability of E&P Taxation. As this E&P tax represents a substantial part of Petrom's tax burden, an increase of this tax in the short term would have the effect of indirectly increasing the purchase price negotiated between the parties and reflecting the market price. This E&P provision is to be applied during the entire period to all companies active in the exploration and exploitation of oil and natural gas sector in Romania.

(67) This benefit would merely reflect the value of the transaction. It could therefore not be said that this benefit would be one of the kind which OMV would not be able to obtain in normal circumstances. In these conditions, the State agreed the best offer which includes the taxation stability. We may conclude that the State acted like a private investor.

(68) Regarding the criterion of affectation of trade on the communitarian market, the Privatization Agreement provides that Taxation Stability E&P will be of application **“except as it may be otherwise required under EU-wide laws or regulations that**

become applicable to Romania". Thus, SNP Petrom SA will not benefit of preferential fiscal treatment in comparison with the others undertakings which are active on the European Union market. In addition, the measure will incentives the extraction of energy resources (oil and natural gas), in connection to which consumption on the European market greatly exceeds the intra-community production. Europe is a net importer of energy resources from extra-community countries which have obvious natural advantages in the production of these resources.

E. Geological Quota

(69) The Geological Quota was already in existence at the time of OMV's bid, having been established through Government Decision No. 168/1998. The 35% deductible quota may be used under Government Decision No. 168/1998 to cover investment needs in the oil refining, transport and distribution sectors, for the geological research works aimed at the discovery of new reserves, for the development of production, for the upgrade and modernisation of equipment. Government Decision No. 168/1998 establishes a state aid scheme, which is an existing scheme within the meaning of Article 3 of Law No. 143/1999 regarding state aid, and the expense quota regulated by this decision continues to apply to the other companies activating in the oil and gas sector.

(70) The notification sent to the Competition Council by MEC submits that the provisions referring to the Geological Quota do not imply the granting of state aid in favour of Petrom/OMV. These provisions were included in the Privatisation Agreement following intense negotiations between OMV and MEC and the fiscal benefit thus obtained was reflected in the price agreed by the parties. In fact, taking into account the fact that this incentive has existed since the year 1998, OMV's request to maintain the Geological Quota is motivated by the need to ensure a stable taxation environment applicable to exploration and exploitation activities. Other bidders have also indicated that they expect that regime applicable to the exploration, exploitation and production of crude oil to remain unchanged. Given the overwhelming importance of the exploration and production activities in Petrom's business, any change in the regime applicable to such activities (including the elimination of an existing incentive) would have a significant impact on the valuation of Petrom.

(71) The financial statements of Petrom, including the application of the Geological Quota, were made available to bidders in the data room, and bidders had the opportunity to discuss this issue with the company's relevant department in meetings organised as part of the due diligence process. In addition, the Geological Quota was briefly analysed in an advisor report also made available in the data room. It can therefore be held that all bidders were aware of the existence of the Geological Quota and, even though only OMV requested an express standstill in relation to this tax

incentive, one can fairly assume that, given its impact on the company's financial statements, all bidders factored the Geological Quota into their valuation of Petrom.

(72) In their final bid, OMV made an express assumption to their valuation that the Geological Quota (as regulated by Government Decision No. 168/1998 and as applied by Petrom until the date of final bids) would be maintained for ten years after the Closing Date. In subsequent meetings with MEC, OMV have made it very clear that they could not maintain the offered price if this assurance could not be given. After negotiations, OMV finally accepted a scaled down version of the Geological Quota in terms of time (to two years: 2005-2006) and scope of application (only to exploration and extraction of crude oil and natural gas). It was obvious from the terms of OMV's bid, as well as from subsequent negotiations in which OMV repeatedly emphasised the importance of the Geological Quota to their valuation of Petrom, that the price offered by OMV would have been significantly lower if the Geological Quota arrangements had not been implemented and it can therefore be held that OMV has paid for the Geological Quota as part of the price offered in the tender.

(73) MEC submits that, in the event the Competition Council considers that the tax measure consisting of the profit tax exemption for a separate reserve financed through the deduction of a 35% quota from the income derived from oil and gas represents state aid because it provides tax benefits regarding the Geological Quota, such aid is fully compatible with the specific regulations regarding state aid.

(74) The Competition Council considers that the tax measure represents state aid granted on the basis of an existing state aid scheme, for which no notification obligation exists pursuant to Article 3 corroborated with Article 6 paragraph. (1) Of Law No. 143/1999 regarding state aid, as subsequently amended.

(75) According to Article 13 of Law No. 143/1999, the Competition Council may request the grantor to take measures to eliminate the incompatibility of existing state aid when it is acknowledged that the granting of state aid distorts or threatens to distort competition or unjustifiably affects trade with Member States of the European Union.

(76) [...] ⁴

(77) [...] ⁴

(78) [...] ⁴

(79) [...] ⁴

(80) [...] ⁴

⁴ Confidential data

(81) The difference between the maximum amount resulted from applying the geological quota and the amounts included in the investments plan to be realized will be financed from Petrom's own resources or loans.

(82) Although the Geological Quota was assessed from the perspective of an existing aid scheme (due to the fact that it has been in existence since 1998), the proposed investments offer sufficient basis for the Geological Quota to be considered compatible aid, even if analyzed under regional aid guidelines, the relevant intensities being observed (circa 19%).

(83) The Competition Council concludes that the existing state aid does not unduly affect competition and trade between Romania and the Member States of the European Union. The Competition Council issues the present decision provided that no other investments aid will be granted in relation to the above mentioned investment program.

VI. CONCLUSIONS

(84) The facilities granted to SNP Petrom under the form of covering of the historical environmental damages are not a State aid.

(85) The incentives granted to SNP Petrom in the form of cancellation of tax liabilities to the consolidated general budget of the State, as well as the stability with regard to the percentage level and manner of calculation of the royalties paid by Petrom pursuant to the Individual Concession Agreements, for a period of ten years, are not a State aid, as the State acted as a prudent private investor whose aim was to obtain the best price in exchange for the majority block of shares.

(86) The fiscal stability referred to in the Privatisation Agreement and the Draft Law on the privatisation of SNP Petrom is not a measure involving a State aid, as the State acted as a prudent private investor in similar situations. Even if this were to confer a possible advantage to SNP Petrom, this does not affect the trade of Romania with the Member States of the European Union.

(87) The Geological Quota set out by Government Decision No. 168/1998 and limited until 31 December 2006 is an existing State aid for investments which does not unreasonably affect the competition and trade of Romania with the Member States of the European Union.

DECIDES

Art. 1. By virtue of letter a) of paragraph (2) of Article 12 of Law No. 143/1999 on the State Aid, as amended, the Competition Council ascertains that the indemnity for historical environmental damages, the cancellation of the tax liabilities to the consolidated general budget of the State, the stability with regard to the percentage level and upon the calculation of the royalties paid by SNP Petrom, as well as the tax stability for a period of ten years in the Exploration & Production sector are not State aid.

Art. 2 The Geological Quota set out by Government Decision No. 168/1998 is an existing aid for investments which does not unreasonably affect the competition and trade of Romania with the Member States of the European Union. No further investments aid will be granted for the investment program in relation to which the Geological Quota applies, as set out above.

Art. 3. By virtue of Article 10 of Law No. 143/1999 on the State Aid, as amended, the Decision of the Competition Council No. 155/17.05.2004 on the individual State aid granted to SNP Petrom is revoked.

Art. 4. This Decision shall be applicable as of the date it is communicated.

Art. 5. According to the provisions of Article 29 of Law No. 143/1999 on the State aid, as amended, this Decision may be challenged by the interested parties at the Court of Appeal Bucharest, Administrative Litigation Section, within thirty days of the date of its communication.

Art. 6. This Decision shall be notified by the Secretariat General of the Competition Council to:

- Ministry of Economy and Commerce, Calea Victoriei nr. 152, sector 1, Bucuresti, code 70034;
- SNP Petrom SA, Calea Victoriei, nr. 109, sector 1, Bucuresti