

Decision of the Competition Council

DECISION no. 13/ 01.02.2005

concerning the notification of the Ministry of Public Finance regarding the financial support for S.C. ELECTROCENTRALE GALATI S.A.

THE COMPETITION COUNCIL,

Based on the provisions of the Decree no. 57/2004 for the appointment of the Competition Council members,

Based on the provisions of Competition Law no. 21/1996, published in Official Journal of Romania, Part I, no. 88 on 30 April 1996, with amendments and completions;

Based on the provisions of Law no. 143/1999 on state aid published in the Official Journal of Romania, Part I, no. 370 on 3rd August 1999, with amendments and completions,

Taking into account the provisions of European Agreement establishing an association between Romania, and European Communities on one side and the Member States of those, on the other side, approved by Law no. 20/1993, published in Official Journal of Romania, Part I, no. 73 on 12 April 1993;

Taking into account the provisions of the Regulation on state aid in the form of compensations granted to certain undertakings entrusted with services of general economic interest.

On the following grounds,

I.PROCEDURE

(1) By the note no. 109601/23.12.2004, registered at the Competition Council with the no. RS-AS 106/23.12.2004, the Ministry of Public Finance notified to the Competition Council under Art. 6 of *Law 143/1999 on state aid, with subsequent amendments and completions*, the financial support for S.C. ELECTROCENTRALE GALATI S.A. The state aid is granted on the basis of G.D. no. 1734/2004 regarding the guarantee by the Ministry of Public Finances of an external credit in limit of the amount of USD 22 million contracted by S.C. Electrocentrale Galati S.A. in order to complete the financing of acquisition of energy resources on the domestic and foreign market for the winter 2004-2005 – black oil and natural gas.

(2) Since the data presented in the notification submitted was not complete, supplementary information was requested by the note addressed under no. DAAS 26/10.01.2005, at which it was responded by the note no. 130/11.01.2005.

(3) The notification became effective on the date the information were complete, namely on 11.01.2005.

II. DESCRIPTION OF THE FINANCIAL SUPPORT

2.1. The beneficiary of the state support measure

(4) The beneficiary of the notified state measure of support is S.C. ELECTROCENTRALE GALATI S.A.

(5) S.C. ELECTROCENTRALE GALATI S.A. was established in accordance with the Romanian law, as a local interest commercial company, based on the GD no. 1580/2003, as a result of restructuring S.C. TERMOELECTRICA S.A. Under art. 2 of G.D. no. 1580/2003, S.C. ELECTROCENTRALE GALATI S.A. – a Romanian legal person – *“organised as a joint stock commercial company and functioning according to the law and its own statutes”*

(6) The shareholders' equity of S.C. ELECTROCENTRALE GALATI S.A. is in total amount of ROL 1,226,326,928 thousand, being divided in a number of 12,263,269 shares, with a par value of ROL 100,000/share, constituted by partially taking over the assets of S.C. Termoelectrica S.A.

(7) The company is headquartered in Galati, 3 Smardan Street and registered with the Trade Registry under no J17/27/2004, with the unique registering number R16044852.

(8) According to legal provisions, S.C. ELECTROCENTRALE GALATI S.A. was granted by ANRE the license no. 590/09.03.2004 for the production of caloric energy and for supplying caloric energy to the final consumers directly connected to production or transport installations.

(9) The company's financial and economic results, based on the balance sheet data are presented in Table no. 1.

Table no. 1 – *Financial and economic situation of the company in the first semester of 2004*

- ROL thousand -

Indexes	2004
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	as of June 30th
Total turnover	1,434,315,073
Gross profit on Romanian market	350,203,244

Source: Notification form and supplementary information

From data presented in Table no. 1 the company makes a profit on the whole activity, mainly from the production of electric energy.

(10) According to Art.5 of the company's articles of association, S.C. ELECTROCENTRALE GALATI S.A.'s objective is the production and supply of electric energy, production, dispatch, transport, distribution and supply of thermal power, by performing trade acts, under the laws in force, according to their line of business as approved, through the company's articles of association. S.C. ELECTROCENTRALE GALATI S.A.'s main line of business is the production of electric and thermal power. The company is active in the Galati city area and ensures the electric and thermal energy for the city's household and industrial consumers. In accordance with Art. 16 par.1 of the Law on electrical energy 318/2003, *"the activities and services for which licenses are being granted are of public interest, except for those dedicated especially for the satisfaction of the license or authorization holder's own consumption."* These services may not be offered by the undertakings under normal market conditions since the service suppliers are imposed certain mandatory conditions related to their supply. At the local level, the thermal energy production for the final consumers' central heating in the city of Galati is made by S.C. ELECTROCENTRALE GALATI S.A., and the distribution and supply of thermal power for the household consumers is made by S.C. APATERM GALATI S.A.

(11) S.C. ELECTROCENTRALE GALATI S.A.'s obligations as an electrical and thermal power producer, under art. 30 of the Law on electrical power are:

- to insure supply of electricity and heating power produced in cogeneration and system technological services, and to observe the licensing criteria, the contract clauses and the regulations in force;
- to maintain a reserve of fuel in sufficient amount or, as the case may be, a sufficient water reserve to meet the continuous production and supply of electricity and heating power as provided in the regulations in force;
- to observe the operational requests of the transport and system operator;
- to insure heating supplies, at a uniform quality and quantity level, under the contract terms.

(12) Given the above, the services of general interest entrusted to the company are:

- heating power production;
- electric power production.

(13) The heating power production service represents 37% from the total activity of S.C. Electrocentrale Galati S.A.

(14) Electricity and heating power are produced in cogeneration and are supplied within the National Electricity Grid, and is meant for a market regulated by the National Authority for Energy (ANRE). The source for the production of the heating and electric energy and the transport networks for the thermal agent belong to S.C. Electrocentrale Galati S.A. and the thermal points and the distribution networks belong to S.C. Apaterm S.A. Galati.

(15) The company's secondary activities are production and sale of the de-hardened treated water and of treated de-mineralized water.

(16) The manufactured products/ services provided are:

1. thermal energy
2. electrical energy
3. hot water for the population
4. hot water for the undertakings
5. additional water for heating
6. demineralized water
7. unreturned condensed
8. de-hardened water.

(17) The supply of urban caloric energy for the heating and preparation of consumption hot water is realized through the thermo system of the city of Galati, system entrusted to the company on the basis of GD no. 1580/2003.

(18) S.C. ELECTROCENTRALE GALATI S.A. has an installed power of 535 MW and a operating power of 375 MW, and it is dedicated to the supply of heating power of urban and industrial consumers from the city of Galati, and to the supply an electricity to the National Electricity Grid.

2.2. The market affected by the financial support granted to the company

(19) The company is active on the market for the production and supply of electrical power, the production, dispatch, transport, distribution and supply of heating power observing the legislation in force.

(20) The market affected by the financial support analyzed in this decision is the market for the services of production, distribution, transport and supply of heating power. These services stand for 37% of the total business of S.C. ELECTROCENTRALE GALATI S.A., and the measures of financial support granted by the state and notified by the Ministry of Public Finances aim at ensuring the necessary fuel for the production and supply of heating power dedicated to the heating and ensuring the hot water for the population and undertakings. The geographical market is represented by the city of Galati, with a number of 87,900 dwellings in which live about 185,000 people, institution-type consumers (social-cultural entities), industrial-type consumers.

(21) The market for heating power is a regulated market, the prices for this energy are set by ANRE, both for household consumers and the industrial ones, by government decrees; the company is bound to ensure the supply of thermal power to all those who are linked to the network, without any discrimination. Also, all the network consumers are captive consumers, since they cannot chose their supplier of heating power.

(22) S.C. Electrocentrale GALATI S.A. is the only producer of thermal energy locally. The evolution of the themal and electric energy sales, in structure, is presented in Tabel no. 2.

Tabel no. 2: *Structure of electric and thermal energy sales realized in 2004 (10 months)*

Services	2004 (10 months)
Electric energy	57 %
Thermal energy	37%
Demineralized water	6%
De-hardened water	0%
Total	100%

Source: Supplemental information

Tabel no. 2 shows that electric and thermal energy contribute over 90% from the total sales of the company.

2.3. Modalities of granting the financial support

(23) According to the winter schedule in the energy field for Oct. 2004-March 2005, included in G.O. 1240/2004 of 05.08.2004, published in the Official Gazette, Part I, 765/20.08.2004 on the approval of the winter schedule in the energy field for October 2004-March 2005, the heating power consumption was considered based mainly on the forecast of the undertakings under the public local administration which ensure over 70% of the necessary for the population.

(24) The financial measure of support notified by the Ministry of Public Finance consists in the state guarantee for an external credit in order to complete the financing of the acquisitions of energy resources from the country and from importing for the 2004-2005 winter (crude oil and natural gas) necessary to perform the activity of general economic interest and public interest set through the regulations in force, in accordance with G.O. 1240/2004 on the approval of the winter schedule in the energy field for October 2004-March 2005. G.O. 1734/2004 approves an external loan limited to USD 22 million by S.C. ELECTROCENTRALE GALATI S.A.. G.O. 1734/2004 allows the Ministry of Public Finances to guarantee in 100% a credit from the Austria Creditanstalt Bank amounting at USD 22.000.000, the equivalent of ROL 635,184,000 thousand.¹[...] ²

¹ The credit was contracted in USD, and the equivalent in Lei was calculated at the ROL/USD exchange rate on Dec.15, 2004, mainly 28,872 ROL/USD.

(25) According to the data in the notification, S.C. ELECTROCENTRALE GALATI S.A. did not previously benefit from state aids, and it was setup on 01.01.2004 through G.O. 1580/2003.

2.4. Assessment of the financial measure of support

(26) *The Guidelines on state aid in the form of guarantees* set the criteria to assess aids granted in the form of guarantee.

(27) According to par. 4.2. of the *Guidelines on state aid in the form of guarantees*, an individual state guarantee does not constitute state aid if the following conditions are met cumulatively:

- (a) the borrower is not in financial difficulty;
- (b) the borrower would in principle be able to obtain a loan on market conditions from the financial markets without any intervention by the State;
- (c) the guarantee is linked to a specific financial transaction, is for a fixed maximum amount, does not cover more than 80% of the outstanding loan or other financial obligation, except for bonds and similar instruments, and is not open-ended;
- (d) the market price for the guarantee is paid.

(28) The analysis of the global economic and financial situation of S.C. ELECTROCENTRALE GALATI S.A. shows in conclusion that the company is not in difficulty. From the information supplied by the beneficiary, we saw that the company is able to contract credits from a commercial bank, under market conditions, without state intervention. Thus, the Competition Council deems that the conditions under par. 4.2., sections (a) and (b) from the *Guidelines on state aid in the form of guarantees* are met.

(29) However, since the guarantee covers more than 80% of the loan, we underline the fact the condition under par. 4.2. section (c) from the *Guidelines on state aid in the form of guarantees* is not met, and thus, there is undoubtedly a state aid in the case of the guarantee S.C. ELECTROCENTRALE GALATI S.A. benefits from.

(30) In accordance with par. 3.2. of the *Guidelines on state aid in the form of guarantees*, the state aid in the form of guarantee may be calculated “in the same way as the grant equivalent of a soft loan, the interest subsidy representing the difference between the market rate and the rate obtained thanks to the State guarantee after any premiums paid have been deducted ».

(31) Since a commercial bank would have granted S.C. ELECTROCENTRALE GALATI S.A. a similar credit, without the state guarantee, with an annual interest rate of 3-month Libor plus a margin of 3.25%, the Competition Council deems that this can be judged as a preferential rate for the calculation of the financial support in the form of guarantee.

² confidential dates

(32) Under the circumstances, the financial support granted in the form of guarantee in order to obtain a USD 22 mill. credit is equal to the net grant equivalent³ related to this loan, as below:

- The discounted difference between the market interest rate and the interest rate obtained thanks to the state guarantee, from which the guarantee premium paid by the company to the Ministry is deducted, is of : USD 1,293,738 – USD 55,000 = USD 1,238,738 respectively ROL 35,764,843 thousand.⁴

(33) Par. 2.1.1. of the *Guidelines on state aid in the form of guarantees* stipulates that , usually, the beneficiary of such a support of 100% is the borrower, since it gets the possibility - as shown above – to obtain better financial terms than the normal market ones.

(34) Under par. 2.2. of the *Guidelines on state aid in the form of guarantees*, under specific circumstances, the lender may also become beneficiary of the state guarantee, mainly if a guarantee is granted ex-post for a loan – in this case the guarantee may be aid for the lender.

(35) The guarantees granted by the Ministry of Public Finances for the credits are an ex-ante condition for these credits to enter into force. The guarantees were issued before any withdrawal/usage of any amount of money from the loan. The guarantees were not issued as an existing loan before their granting by the state.

(36) In the government decision to approve the state guarantees of the external credits to be contracted by the company, the maximum values of the credits to be guaranteed are set (and the interest rates and the related commissions), the aim of the credit and the guarantor (the Ministry of Public Finances). Based on these government decisions, the company sets the credit parameters by mutual agreement with the Ministry of Public Finances (granting period/maturity, grace period, reimbursement method). Eventually, the standard bid solicitation are drafted for the external banks of first rank.

(37) The bid solicitation consists in information needed by the interested banks so that they may structure a competitive price bid: the type of loan, the borrower, the 100% state guarantee (by indicating the government decision), the value of the loan, the credit maturity, grace period, the reimbursement method, the way of reply, the deadline for submittal of bids and any other data that may be necessary to draft a proper bid. Since there is a standard bid solicitation, all banks receive the same information and benefit from equal treatment, under transparent and free access terms for bid submittal.

³ The grant equivalent was computed in accordance to Annex 2, par. 3 of the Regulation on the regional aid, taking into consideration the terms of the loan, the reimbursement graphics, and a rate of adjustment for inflation of the USD of 3% during 2004-2010.

⁴ The rate of exchange taken into account was the National Bank of Romania rate on 15.12.2004 is of 28,872 ROL/USD.

(38) After the analysis of the bid received upon the date mentioned in the bid solicitation, the bank with the most advantageous terms is chosen. Since all the banks are of first rank, the main parameters of the credit are the same, and the main criteria to adjudicate among them is the cost of the credit (related interest rate and commissions).

(39) Given the above factors, no financing bank can be judged at the detriment of another bidding bank. Consequently, the Competition Council ascertains that the state guarantee does not grant any advantage to the lender, but only to the borrower, namely S.C. Electrocentrale Galati S.A.

2.5. Costs resulting from providing of the public service of general economic interest

(40) The public service to produce, transport, distribute and supply thermal energy to captive consumers, entrusted to the company, is regulated by ANRE. In order to perform the public service, the company incurs costs for raw material (fuel), materials, staff expenses, environment protection expenses, repairs and investment costs, metering costs and others.

(41) S.C. Electrocentrale Galati S.A. holds a management bookkeeping (as a basis for the management decisions) where the company activities of being separately treated. Production, transport, distribution and supply of thermal energy to captive consumers, which is the public service obligation, is thus presented separately from the other activities of the company. The separate financial and accounting recording for the activities that stand for the public service of general economic interest is a mandatory condition imposed to the undertaking through the licence entrusting him with the performance of the particular public service.

(42) At the end of each year, the company is bound to submit to ANRE, justifying documents to show the effective costs related to the public services provided that year and the volume of thermal energy produced and sold each month. To the input data, the standard methodology is applied in order to determine the costs to produce, transport, distribute and supply the thermal energy. Thus, at the beginning of each fiscal year, S.C. Electrocentrale Galati S.A. calculates a budget of incomes and expenses. Also, a calculation of prices to be charged is sent for approval to ANRE, who set the national base price and the local delivery price.

2.6. The difference between the national reference price and the local delivery price of thermal energy

2.6.1 The national reference price

(43) The national reference price was established by the GEO no.162/1999 for thermal energy supplied to the population in centralized systems, for home heating and hot water preparation.

(44) By establishing a national reference price the aim is to obtain a balance between the affordability degree of the population and the state budget subsidization. As for the social dimension, the weight of this price in the budget of an average income family and the cost of thermal energy are considered when justifying this price.

(45) The level of the national reference price for thermal energy is established in advance by Government decision at the proposal of ANRE as an average of the local prices of the producers using the same fuel type, to which the related distribution tariffs are added. Also, the national reference takes into consideration the subsidization possibilities from the state budget. The standard methodology of this price is established by order of ANRE. Factors influencing the modification of the national reference price are: the price of the fuel, price of electric energy, the consumer price index, exchange rate (ROL/USD or ROL/EURO). The national reference price in 2003-2004 was regulated by the following administrative acts, as resulting from Tabel no. 3 below:

Tabel no. 3 Administrative acts establishing the level of the national reference price of thermal energy

	2003	2004
Administrative act setting the national reference price	HG nr.686/ 03.07.2002	HG nr.1155/ 23.07.2004
National reference price level (ROL/GCAL)	800,000	896,000

Source: National legislation in force

2.6.2 The local delivery price of thermal energy

(46) The local delivery price for the heating energy is established by A.N.R.E., both for the population as well as for the undertakings. The methodology of establishing the local delivery price is being applied by A.N.R.E. to all thermal energy co-generation producers. Thus, the undertaking has the obligation to submit to A.N.R.E., at the end of each fiscal year, justifying documentation outlining the costs related to the discharged public service in the respective year and the quantities of thermal energy which were produced and sold in each month of the year.

(47) Prices are set separately for each activity/service, the local delivery price resulting from adding the production price, the transport service tariff and the tariff for the distribution and supply service.

(48) Local delivery prices are set at the beginning of each year and adjusted at the beginning of each second half of the year. The following stages are pursued:

- identification of regulated activities and services;
- identification of production sources for caloric energy (separate sources and/or cogeneration);
- estimation of quantities delivered to final consumers based on the undertaking's previous year figures, taking into account the losses in the transport networks and of produced quantities, taking into account the own consumptions of the power plant;
- assignment of technological fuel expenses;
- allocation of direct expenses, excluding fuel expenses, broken down by activities/services and producing sources;
- allocation of indirect, general and administration expenses by services, on a pro rata basis with the value of direct expenses, excluding fuel;
- determining total expenses with the production of thermal energy;
- determining unit costs;
- redistributing by activities of expenses related to own consumptions;
- allocation of financial expenses by regulated services;
- determining total expenses for the regulated services.

2.6.3 Conclusions

(49) The national reference price is regulated on grounds related of social protection. Thus, if the local price for producing and supplying the heating energy is higher than the national reference price, the population will only pay the latter.

(50) If the local price of the gig calorie (GCAL) is higher than the national reference price, the difference incurred by the supplier is subsidized as follows, according to the GEO no. 162/1999:

- a) by the state budget, up to the ceilings approved through the budget law, allocated for this purpose;
- b) by the local budgets, for the part left uncovered through the state budget.

2.7. Costs in excess of the local delivery

(51) When analyzing the measures of support for S.C. ELECTROCENTRALE GALATI S.A. one must consider that, for the services of production, transport, delivery and supply of heating energy, the company registers costs higher than the local price for supplying heating energy established by A.N.R.E., this situation resulting from the management accounting of the undertaking, in which expenses are separately recorded.

(52) The unit operating cost of the service was calculated based on effective expenses recorded by the company in each year of the analyzed period, respectively expenses for raw materials, materials, personnel, environment, repairs, investments, metering of the real production of thermal energy delivered in the respective year.

(53) In reality the local delivery price established by A.N.R.E. does not cover all costs due to the fact that fuel price increase estimates are not considered. Subsequent to the fuel

price increase during the year A.N.R.E. is adjusting the energy price only when the increase is more than 5% and the adjustment refers only to the fuel; however, it is common knowledge that as a chain effect, the raw materials and materials prices increase also. This increase is taken into account is not considered when adjusting but only when prices are reviewed, once a year. Thus, there is a gap (lag) during the year between the costs of the energy operator and the local delivery price.

(54) The high operating costs of S.C. ELECTROCENTRALE GALATI S.A. are due mainly to the following causes:

- the natural gas, raw materials and materials are bought at prices comparable with the international ones. Contrary, heating energy is sold on local market at a price established by ANRE lower than the medium international price ;
- proposals of price increasing are submitted to local authorities and to A.N.R.E. after the sub suppliers already increased their product prices and considering that until the company gets the A.N.R.E. certifying documents and decision uncovered costs shall be record;
- A.N.R.E. agreed technological loss are lower as the real loss which are higher because of old transport and distribution pipe line networks which require high maintenance costs. Those costs are not considered when the reference price is estimated by A.N.R.E;
- the population pays a national reference price for the caloric energy, approved by Government Decision and established mainly according to the purchasing power of the population, the difference between this and the production and distribution costs of thermal energy being subsidized. This subsidy hardly reaches the producer, because the Local Council budget which ensures a significant percentage of it (55%) does not have the liquidities required to pay in due time. As a result of the delays in providing the subsidies, the financial costs of the company increase because the real value of the subsidies is significantly diminished by the inflation rate; thus, a part of the real costs remains not covered.

(55) In Table no. 5 presented in the Annex[...] ⁵, the evolution of the local delivery price for caloric energy as hot water and the real costs of production, transport, distribution and supply of it for 2004 are shown, as well as the forecast for the period 2004-2005. As it may be noticed, during analyzed period, most of the times, the operating cost for producing, transporting, delivering and supplying heating energy - hot water - is higher than the local delivery price, both for the population and for the undertakings.

(56) The differences between the local delivery price and the real cost of production, transport, distribution, delivery and supply of caloric energy lead to company losses from operating the service, losses which are shown in Table no. 4 .

Tabel no.4 - Losses generated by the discharge of the service of general economic interest[...] ⁶

⁵ Confidential dates

⁶ Confidential dates

III. ANALYSIS OF THE STATE MEASURE OF SUPPORT

3.1. Object of the decision

(57) On the basis of the notification to the Competition Council by the Ministry of Public Finances, the object of the present decision consists of the financial support measure in form of state guarantee in total amount of ROL 22 bilion. These measures of the financial support are analyzed by S.C. ELECTROCENTRALE GALATI S.A. in the context of meeting the public service requests during 2004-2005.

3.2. Obligation of service of general economic interest

(58) The financial support granted to a company entrusted with a service of general economic interest is not considered state aid for the purposes of Art, 2 of *Law 143/1999 on state aid with subsequent amendments and completions*, if the following conditions are cumulatively met:

- a) the obligation to discharge a service of general economic interest is entrusted through a normative/administrative act and is clearly defined;
- b) the parameters based on which the compensation is calculated must be established in advance, in an objective and transparent way, in order to avoid granting an economic advantage to the beneficiary;
- c) the compensation must not exceed the amount necessary to totally or partially cover the costs incurred through the service of general economic interest, taking in consideration the relevant incomes and a reasonable profit in performing these obligations;

if the undertaking entrusted with the service of general economic interest was not selected through open public tender which would have allowed the selection of an bidder able to discharge this public service at the lowest costs, then the level of compensation must be set based on a comparative analysis of the company's costs and the costs of well-managed and profitable enterprise which meets all the conditions set for the performance of the particular public service, given the relevant incomes and a reasonable profit from the meeting of the service of general economic interest obligations.

3.3. The condition from par. 3.2. a):

(59) S.C. ELECTROCENTRALE GALATI S.A. is entrusted with the production, transport, distribution and supply of heating energy for the population, institutions and undertakings, under the ANRE licenses no.511/2002, 512/2002, 576/2003. In the licenses are mentioned, among other things, the obligations specific for the undertakings performing a service of general economic interest, namely: continuity in supplying heating energy, ensuring access to heating networks for new customers, achieving performance standards. Also, by EGO no.162/1999, producers and suppliers of thermal energy are under the obligation to sell thermal energy to the population at a fixed price

which regularly is lower than the costs incurred by the discharge of the service (national reference price).

(60) According to the *Law on town management no. 326/2001*, the supply of heating which is centralized produced is a public use service.

(61) According to Law no, 326/2001, public services must fulfill the following conditions:

a) continuity both in quality and quantity, according to the conditions stipulated in the contract;

b) adaptability to consumers' requests;

c) equal access to the public service, in the conditions stipulated in the contract;

d) ensuring the public health and life quality.

(62) Organization, operation and functioning of public services must ensure:

a) meeting the quantity and quality demands of users, according to the contract provisions;

b) the optimal operation in safety, profitability and economic efficiency conditions of buildings, equipments, installations and all assets, according to the projected technological parameters and in compliance with the requested conditions, operation guidelines and organization and functioning regulations;

c) protecting the public estate and environment by observing the legal provisions;

d) informing and consultation the citizens with the purpose of protecting the health of the population benefiting from these services.

(63) The obligations of the operators which are suppliers/providers of public services towards the consumer are mainly the following:

a) to serve all users in the area for which they were authorized/certified;

b) to comply with all the performance parameters settled by the local public authorities and the national regulating authority, respectively ANRE;

c) to supply the information requested by the local public administration and the national regulating authority and to enable the access to the documentation of the respective utilities, according to the conditions of the operating contract.

(64) The supply of thermal energy for heating and the preparation of consumption hot water is realized through the thermal system of the city of Galati.

(65) Given the above, we note that S.C. Electrocentrale Galati S.A. has the obligation to ensure the effective functioning of the production, transport, distribution and supply of thermal energy, essential for the population, institutions and undertaking in the city of Galati. More than that, the company is obliged to supply these services at a regulated price, taking into account the affordability degree of the consumer. Consequently, one can conclude that S.C. ELECTROCENTRALE GALATI S.A. by licenses, is entrusted with the discharging of a service of general economic interest.

3.4. The condition from par. 3.2. b):

(66) According to this criterion the compensation of the public service obligation must be calculated on pre-established objectives and based on transparent parameters and may not grant an economic advantage to the beneficiary.

(67) The two parameters based on which the level of the compensation is calculated are the national reference price, established by ANRE, and the local delivery price established by ANRE. These parameters are set in advance by Government decision, at the proposal of ANRE.

The methodology used to establish the national reference price is based on the following:

- price of fuel used for the production of caloric energy;
- the electric energy price;
- the consumer price index;
- the USD/ROL exchange rate.

The local delivery price is set based on the methodology of establishing regulated prices for purchase/sale, transport and distribution tariffs for caloric energy issued by ANRE. The producers of caloric energy submit to the regulatory authority the own price calculation; this contains the costs incurred in the previous 12 months, fixed and variable, as well as estimated costs for the following 12 months of operation. The regulatory authority analyses the variable costs (price of fuel, specific consumptions related to the production of caloric energy, losses of caloric energy in the transport and distribution networks), as well as fixed costs and approves the local delivery price of the caloric energy, resulting different local delivery prices specific to each company.

(68) The information submitted to the Competition Council prove the fact that the procedure mentioned at paragraph 67 is carried out based on the criteria of *ex-ante* calculation, the parameters based on which the compensation for the service of general economic interest is established are usually set up in advance.

3.5. The condition from par. 3.2. c):

(69) Condition 3.2.c) requires that the compensation must not exceed the costs incurred through the service of general economic interest.

(70) From Table no. 5[...] ⁷ it can be seen that during the analyzed period S.C. ELECTROCENTRALE GALATI S.A. has recorded losses of ROL 38,282,659 thousand caused by the negative difference between the national reference price and the local delivery price for the heating energy.

(71) The financial support measures from which the company benefits in the period 2004-2005 is in amount of ROL 35,764,843.536 thousand granted under the form of state guarantee.

(72) Taking into account the losses of ROL 38,282,659 thousand that the company incurred due to the performing of the service of general economic interest of production and transport of caloric energy, it can be seen that the facilities granted to the company under the form of guarantees amounting to ROL 35,764,843.536 thousand do not fully cover the company losses. Thus, the financial support granted to the company does not exceed the total costs incurred from the performing of the public service.

(73) Under these circumstances it is considered that the state aid granted to S.C. ELECTROCENTRALE GALATI S.A. during 2004-2005 represents only a compensation for the costs related to the performing of the public service of general economic interest for the production, transport, delivery and supply of heating energy in the city of Galati.

3.6. The condition from par. 3.2. d):

(74) S.C. ELECTROCENTRALE GALATI S.A. was not entrusted with the service of general economic interest of production and transport of caloric energy following a public tender procedure.

(75) The public service of production and transport of caloric energy was entrusted to S.C. ELECTROCENTRALE GALATI S.A. by a license from ANRE no.1619/09.03.2004. Thus, in order to establish the compensation level, it is necessary to analyze the costs that another well-run undertaking would have had, in providing the same service.

On the Romanian heating energy market there are acting other producers and suppliers as well (e.g, Termoelectrica, CET Govora, CET Bacau, Electrocentrale Oradea, etc.). Still, a comparison with these companies would not be relevant, as they are also public undertakings receiving aid from the state for discharging the public service obligation. However, making a comparative analysis with other undertakings producing and supplying heating energy, it can be noticed that their situation is similar to the situation of to the analyzed undertaking, respectively the real costs of the service exceed local delivery prices set by ANRE and the causes leading to this situation are in fact similar.

(76) Considering the above, one can conclude that the four conditions under point 3.2 are not met cumulatively, mainly the condition under par. 3.2. (d) was not proved. Therefore, the state support measures for S.C. ELECTROCENTRALE GALATI S.A., notified by

⁷ confidential dates

the Ministry of Public Finance, constitute state aid for the purposes of *art. 2 of Law 143/1999 on State aid, with subsequent modifications and completions* and of the *Regulation on state aid in the form of compensations granted to certain undertakings entrusted with services of general economic interest*.

(77) The total value of the state aid granted to S.C. ELECTROCENTRALE GALATI S.A., between 2004 – 2005 is of ROL 35,764,843.536 thousand.

IV. Compatibility of the Aid

(78) According to the *Regulation on state aid in the form of compensations granted to certain undertakings entrusted with services of general economic interest* compensations granted in view of discharging the service of general economic interest may constitute state aid compatible with a normal competition environment if the following conditions are met:

- a) the state aid is necessary for discharging a service of general economic interest;
- b) the state aid does not unduly affect the trade between Romania and the EU Member States.

4.1. State aid necessary for discharging a service of general economic interest

(79) In order to be able to assess the necessity of the aid with respect to the discharging of the service the following conditions should be observed:

- the beneficiary needs to be officially entrusted with discharging a clearly defined service of general economic interest; and
- the compensation level should not exceed what is necessary to discharge the service of general economic interest, taking into account the revenues arising from its performance.

(80) As discussed under point (59) above S.C. ELECTROCENTRALE GALATI S.A. is delivering a service of general economic essential for the population, institutions and undertakings and that it is clearly defined by license.

(81) S.C. ELECTROCENTRALE GALATI S.A. operates its service is under the public ANRE licenses no. 1654/2004, no.1619/2004, no.1618/2004. The licenses in conjunction with the relevant law clearly define the obligations of the service that the company is supposed to discharge. Therefore, it can be concluded, that S.C. ELECTROCENTRALE GALATI S.A. has been officially entrusted with the public service that it discharges.

(82) It follows, that under the conditions of a regulated market for discharging this service the company can not impose on its consumers a price that is sufficient to cover its operating costs. This is the main cause for which the company has annual losses.

Furthermore, the compensation granted to the company does not fully cover all the costs that are currently being incurred by the provision of the public service.

(83) Therefore, one can conclude that the state aid granted to S.C. ELECTROCENTRALE GALATI S.A does not exceed what is necessary to discharge under normal conditions of continuity, safety and comfort the public service of production and transport of caloric energy within the city of Galati.

(84) Without granting this compensation its activity would be blocked, therefore it could not deliver the service anymore This could have serious consequences on population and undertakings of the city of Galati, who would be lacking caloric energy, especially in the cold season.

4.2. No unduly affect the trade between Romania and the EU Member States

(85) It needs to be noted that the activity of the company is restricted to a limited geographical area, represented only by the city of Galati S.C. ELECTROCENTRALE GALATI S.A. is the only operator. The company is not involved in export activities. Under these circumstances it is considered that the commerce with the Member States in not unduly affected.

4.3. There is no over-compensation

(86) The state aid granted to S.C. ELECTROCENTRALE GALATI S.A. under the form of a guarantee granted by the state for an external loan does not represent an over-compensation because it does not exceed the costs which are absolutely necessary in order to perform the service of general economic interest. Taking into consideration that the company keeps separate accounting records for the activity representing the service of general economic interest, respectively the production, distribution and supply of heating energy as hot water, the cross subsidization possibility is being ruled out.

(87) Thus, the two conditions provided at point (78), conditions provided in the *Regulation on state aid in the form of compensations granted to certain undertakings entrusted with services of general economic interest* are cumulatively met, for appreciating that the support measures for S.C. ELECTROCENTRALE GALATI S.A., representing compensations for performing the service of general economic interest, is state aid compatible with the normal competitive environment.

(88) The state aid granted to S.C. ELECTROCENTRALE GALATI S.A. in total amount of ROL 35,764,843.536 thousand is compatible with a normal competition environment.

DECIDES

Art. 1. The measures of financial support granted during 2004-2005 to S.C. ELECTROCENTRALE GALATI S.A. constitute state aid for the purposes of Art, 2 of *Law 143/1999 on State aid, published in the Official Monitor, Part I, no, 370 on August the 3rd 1999, modified and completed by Law 603/2003 and GO 94/2004 on regulation of financial measures, approved with modifications and completions by the Law no.507/2004.*

Art. 2. The notified state aid represents a necessary compensation to achieve, under normal conditions of safety and continuity the service of general economic interest to produce, transport, distribute and supply heating energy, and this compensation does not affect the trade between Romania and the EU Member States in an unjustified way.

Art. 3. Pursuant to Art. 12 art. 2 (b) corroborated with Art. 14 par. 1 (j) of *Law 143/1999 regarding state aid with subsequent modifications and completions*, we authorize the state aid for to S.C. ELECTROCENTRALE GALATI S.A. as aid to achieve under conditions of safety and continuity the service of general economic interest.

Art. 4. Pursuant to Art. 24 of *Law 143/1999 with subsequent modifications and completions*, suppliers shall annually convey to the Competition Council information regarding the state aid granted to S.C. ELECTROCENTRALE GALATI S.A. in view of monitoring the aid.

Art. 5. This decision is applicable as of its date of communication.

Art.6. Pursuant to Art, 29 of *Law 143/1999 regarding state aid with subsequent modifications and completions*, this decision may be appealed by he interested persons before the Bucharest Court of Appeal, the administrative section, within 30 days from its communication.

Art.7. This Decision shall be communicated by the General Secretariat of the Competition Council to:

- The Ministry of Public Finance, Apolodor Street, no. 17, sect, 5, Bucuresti;
- S.C. ELECTROCENTRALE GALATI S.A., street Soseaua Smardan, no.3, Galati, judetul Galati.

Art. 8. The Secretariat-General and the Directorate for State Aid Authorization of the Competition Council shall pursue the fulfillment of the present Decision.

PRESIDENT
MIHAI BERINDE

From table no. 5 it can be seen that the company registers losses during the period 2004-2005 of ROL **33,826,261** thousand related to the performing of the service of production, transport, distribution and supply of the caloric energy. We mention that the calculation of these losses is presented in Table no. 5 from the Annex presenting in detail in each month the evolution of the difference between the local delivery price and the real cost of production and supply of caloric energy, separately for population and undertakings.