

DECISION of the Competition Council

no. 45 on 15.03.2005

on the State aid to be granted to S.C. FOSERCO S.A. TG. OCNA

The Competition Council

Based on:

Taking into consideration the Decree no. 57/2004 regarding the appointment of the Competition Council;

Taking into consideration the provisions of the Competition Law no. 21/1996, published in the Official Gazette no 88, I Part on 30.04.1996, with the subsequent modifications and completions;

Taking into consideration the provision of the Law no 143/1999 on State aid, published in the Official Gazette no 370/03.08.1999, Part I, with the subsequent modifications and completions;

Taking into consideration the dispositions of the European Agreement establishing an association between Romania, on one hand, and the European Communities and their Member States on the other hand, ratified by the Law no.20/1993, published in the Official Gazette, Part I , no. 73 on April the 12th, 1993;

Taking into consideration the dispositions of the Regulation regarding the state aid for the rescue and restructuring of the firms in difficulty, published in the Official Gazette Part I, no. 470 of July 02, 2002;

Based on the following,

1. PROCEDURE

- (1) By the address no. 108359/17.06.2004, registered at the Competition Council with the no. RS-AS 69/22.06.2004, the Ministry of Public Finance notified, in the basis of art. 6 of *the Law no. 143/1999 on the state aid with the subsequent modifications and completions*, the intention to grant the restructuring state aid for S.C. FOSERCO S.A. Tg. Ocna, as specific state aid allocation within a state aid scheme represented by the *EGO no. 40/2002 for*

recuperating the budgetary arrears, approved with modifications and completions by the Law no. 491/2002 with the subsequent modifications and completions.

- (2) The Competition Council sets out that, previously, the Ministry of Public Finance notified the intent to grant a state aid for the same undertaking, its granting being forbidden by the Decision no 151/14.05.2004, as it didn't met the provisions of the Regulation on the state aid for rescuing and restructuring firms in difficulty, referring to the beneficiary's contribution and to the return to viability after the implementation of the restructuring plan.
- (3) Afterwards, the state aid's beneficiary brought arguments to show that the information from the notification form submitted by the Ministry of Public Finance, referring to the beneficiary's contribution to the restructuring plan, the market share and the affiliation to a group were incorrect. According to art. 10 in the Law no. 143/1999 on the state aid, with the subsequent modifications and completions, a previously adopted decision can be revoked after the grantor and the initiator of the state aid bring their arguments, if the decision is based on incorrect information received during the procedure and were decisive in its taking. Therefore, the Ministry of Public Finance, as state aid grantor together with the beneficiary and with the Company for research, geological engineering and design for the extractive industry of gas and oil PETROSTAR S.A. – Ploiesti, elaborated a new restructuring plan, as a result of the re-assessment of the economical- financial situation of S.C. FOSERCO S.A.. This way, the Ministry of Public Finance started a new notification procedure as it was set out in Para. (1).
- (4) By the address no. DAAS/528/12.07.2004, supplementary information was requested, based on art. 6 align. (4) in the Law no. 143/1999 on state aid, with the subsequent modifications and completions. The answer was received by the address no. 3587/23.09.2004, registered at the Competition Council with the no. DAAS/715/27.09.2004. As the received answer didn't clarify all aspects, a comeback request of supplementary information was issued with the address no. DAAS/804/19.10.2004. Also, during the analysis procedure of the case in subject.
- (5) The requested information were submitted in the address no. 4548/ 23.11.2004, registered at the Competition Council with the no. DAAS/976/25.11.2004.

2. DESCRIPTION OF THE STATE AID MEASURE

2.1. The legal base for granting the state aid

- EGO no 40/2002 for the recovery of budgetary arrears, approved with modifications and completions by the Law no. 491/2002 with the subsequent modifications and completions;
- The methodology regarding the granting procedure and the components for the facilities for the payment of the obligations unpaid to the state budget, administrated by the Ministry of Public Finance, approved by the Order of the minister of finances no. 580/2002, with the subsequent modifications and completions;

2.2. The concrete modality for granting the state aid

- (6) The state aid in amount of ROL 265,000,453,133 consists in:
- The exemption from the payment of delay interests and penalties related to the budgetary obligations, in amount of ROL 48,831,386,750 according to the Convention no. 364/19.12.2003;
 - The exemption from the payment of the delay interests and penalties related to the social security budget until 08.04.2002 for unpaid debts on 31.12.2001, in amount of ROL 67,940,489,224 within the conditions provisioned in the Convention no. 416/26.03.2004;
 - The exemption from the payment of the delay interests and penalties related to the obligations to the unemployment security budget, in amount of ROL 6,117,365,774 within the conditions provisioned in the Convention no. 417/26.03.2004;
 - The rescheduling of the payment for a 60 month period, of the obligations unpaid to the consolidated state budget in amount of ROL 142,111,211,385 within the conditions provisioned in the Conventions no. 364/19.12.2003, 416/26.03.2004 and 417/26.03.2004.

3. THE STATE AID MEASURES BENEFICIARY

- (7) The beneficiary of the financial measures granted by the state is S.C. FOSERCO S.A. Tg. Ocna.
- (8) The company was established in 1952, under the name of Schela de Foraj – Tg. Ocna. In 1991, by the re-organization of the activity of the Autonomous Regie Petrom-RA, Schela de Foraj – Tg. Ocna became a joint stock company with its equity wholly owned by the State, with the name of S.C. FOSERCO S.A., being registered to the Commerce Register Bacău, with no. J04/563/1991. Subsequently, as a result of the enforcement of the Law 55/1995, the shareholders structure modifies, the state owning through the State Ownership Fund – 85.46%, the rest of 14.54% being held by other shareholders, natural persons.
- (9) Starting with February 1999, S.C. FOSERCO S.A. became a totally private company, when S.C. R.P.T. OIL S.R.L. acquired the share package owned by the State, representing 85.46% from the social capital, by (contract of privatisation no. 752/09.11.1998).
- (10) As a result of the transfer of the shares' ownership right, on 12.09.1999, the shareholders' structure was the following:

Table no. 1- *The shareholders' structure on 12.09.1999*

SHAREHOLDERS	Shareholders' equity ownership	
	Number of shares	Percentage in shareholders' equity (%)
S.C. RTP OIL S.R.L.	421,096	85.46

Other shareholders natural persons	71,648	14.54
Total	492,744	100.00

Source : Notification from the Ministry of Public Finance

- (11) At the end of 1999, the major shareholder made a capital increase, so that its share package was of 93.317%. Afterwards, on 15.06.2000, the shares resulted from the capital increase, free of any charges, were sold through a Sale-Purchase contract to the company Brington Capital S.A.
- (12) On December the 31st, 2003, the company shareholders' structure is the following:

Table no. 2- *The shareholders' structure on 31.12.2003*

SHAREHOLDERS	Shareholders' equity ownership	
	Number of shares	Percentage in shareholders' equity (%)
BRINGTON CAPITAL S.A.	472,200	44.042
S.C. RTP OIL S.R.L.	421,096	39.275
F.S.L.I PETROM	107,217	10.000
Other shareholders physical persons	71,648	6.683
Total	492,744	100.00

Source : Notification from the Ministry of Public Finance

- (13) The company acts in the extractive industry field. Its main activity object is:
- The drill of probes for geological research, exploiting and injections for oil and gas, thermal waters and other useful substances;
 - Major repairing for probes, manufacturing production probes and de-casing-of probes;
 - surface construction- assembly workings and assembly drilling installations;
 - repairing, recovery and reconditioning of the drilling fluid.
- (14) The performed services are:
- assembly /wrecking drilling equipment;
 - assembly /wrecking air lines;
 - water, gas and fuel supply;
 - instalment access roads;
 - instalment dill mess;
 - maintenance and repairing drilling equipments and tools, electrical and Diesel engines.
- (15) From the point of view of the production flow, the company is structured in 7 workshops (The drilling workshop, the Mechanical workshop, the C.M., workshop, the Fluid station, Tool platform, Auto Column), located at the premises of the company; part from the activity is carried out at locations of the drills requested by customers.

- (16) S.C. FOSERCO S.A. Tg. Ocna is a member of the International Association of the Drilling Contractors (IADC), having a prolific experience in the gas and oil drilling probes, controlled drilling and workover, using modern drilling installations and advanced drilling fluids. During its activity, the company successfully made drilling workings for small, medium and big depth drilling, based on contract brought to the end at a high technical level, in accordance with the international standards and the labour protection regulations.
- (17) S.C. FOSERCO S.A. has highly qualified personnel, trained in specialized institutions, capable to make all types of drilling activities. The evolution of the employees number and the labour productivity during 1999-2003 is the following:

Table no. 3- *The evolution of the personnel number and of the labour productivity*

INDEXES	1999	2000	2001	2002	2003
Average no. of personnel	454	376	400	417	384
Labour productivity	81,933	153,489	189,192	339,365	323,293

Source : *The restructuring program of the company*

- (18) The economic-financial results based on the data from the balance sheets on the last 5 years are the following:

Table no. 4- *The turnover evolution during 1999-2003*

	ROL MIL.				
	1999	2000	2001	2002	2003
TOTAL TURNOVER	37,225	57,712	75,677	141,515	124,145
TURNOVER on the domestic market	37,225	57,712	72,420	115,867	88,321
TURNOVER on the export market	-	-	3,257	25,648	35,824

Source : *Notification from the Ministry of Public Finance*

- (19) It can be seen that that the total turnover made by the company registers an increasing trend until 2002; in 2003, the turnover decreases with 12.2% compared to 2002. The company performs drilling services mainly for the domestic market.

Table no. 5- *The evolution of the company's losses for the last 5 years*

PROFIT/LOSS		ROL MIL.		
1999	2000	2001	2002	2003
-30,638	-58,161	-24,736	-29,647	-72,661

Source :Notification from the Ministry of Public Finance

- (20) It can be seen that in each year of the analyzed period, the company registers a negative result of the financial exercise, mainly due to the unpaid tax debts accumulated before privatization, debts which caused significant delays and penalties.

4. DESCRIPTION OF THE MARKET WHERE S.C. FOSERCO S.A. TG. OCNA ACTS

- (21) The relevant market for S.C. FOSERCO S.A. Tg. Ocna is the market of the drilling services and ancillary activities. The geographical market for the services performed by the company is the whole Romanian territory. Starting with 2001, the company carried out services even outside Romanian borders, namely in Kazakhstan.

4.1. Domestic market

- (22) The domestic market of drilling services and ancillary activities is characterized by a low number of beneficiaries and many bidders.

a) DEMAND

- (23) The demand on the Romanian drilling market is represented by the two big companies acting in the field of extractive and hydrocarbons' industry: S.N.P. PETROM S.A. Bucuresti, in the field of oil and gas extraction and SNGN S.A. Medias, in the field of natural gas extraction.
- (24) S.N.P. PETROM S.A. carried out in the last 5 years (1999-2003) a drilling activity representing 80-90% from the total volume (drilled meters) at national level. In the drilling activity for PETROM, the high proportion is held by the exploiting probes (approx. 89%), while the drilling for research activity represents approx. 11%.
- (25) SNGN ROMGAZ carried out in the last 5 years a drilling activity representing approx. 10-20% from the total national volume. From the evaluative point of view, it can be seen an increase of the market share of ROMGAZ in the last 3 years (from 5.4% in 2001 to 20.9% in 2003) and, implicitly, a decrease of the market share for PETROM..
- (26) The two companies represent approx. 52% from the total turnover made by S.C. Foserco S.A.

Table no. 6- The main customers and their proportion in the company's turnover

No. Curt.	Customer name	% - turnover
1	S.N.G.N. Romgaz – Medias	27.88
2	S.N.P. Petrom – București	23.68
3	AMRONCO	3.02
4	Foreign customers	28.86
5	Others	16.56

Source : The restructuring program of the company

- (27) In the near future (3-5 years) it cannot be forecast any major changes regarding the customer structure for the probe drilling activity and, implicitly, the structure of the demand on the drilling market, even in the context of the two major companies being submitted to the privatization process .

b) OFFER

- (28) Previous to the year 1990, the drilling operators were organized and acting on geographical criteria, being within the structure of the oil trusts. After 1990, the scaffolds drilling activity was externalized from the oil and gas field, the drilling scaffolds being organized as independent undertakings. They activated during 1990-2003 on a contradictory market, the tendency correlated with the decrease of the gas and oil production. From these reasons it intervened the “natural selection”, generated by the law of offer and demand, which lead to the decrease of the competitors on the drilling market.

(29) ¹[...]

(30) ²[...]

(31) ³[...]

(32) ⁴[...]

- (33) The annual average level of the physical accomplishments of S.C. FOSERCO S.A. is of 10-11 thousand meters drilled every year. The company had during 1999-2003 the following physical accomplishments in the oil and gas probe drilling:

Table no. 7- The evolution of the accomplishments of S.C. FOSERCO S.A

Year	Accomplishments (drilled meters)
1999	8,792
2000	12,912
2001	14,536
2002	9,430
2003	8,440

Source: The restructuring program

- (34) As far as the technical endowment of the companies acting on the market of the drilling services in Romania is concerned, according to the data supplied by the Drilling Contractors Association in Romania, it is found a reduction of the installations in the net worth of the

¹ confidential data

² confidential data

³ confidential data

⁴ confidential data

undertakings, reduction generated by: the end of the economical lifetime of the installations, the drilling companies' reduced financial possibilities for re-technology programs, very high acquisition costs for performing drilling installations, very high costs with the maintaining of the drilling installations. During 1999-2003 there is a general increasing trend for the degree of utilization of the production capacities, from approx. 27% in 1999 to approx. 38% in 2003.

- (35) Analyzing in comparison the demand and offer on the Romanian drilling market during 1999-2003 it can be seen that in the whole analyzed period, the demand was under the level of the offer, the proportion demand-offer showing an average level of 44% (the minimum level of the proportion was registered in 2003 and the maximum one in 2001).
- (36) The assessment of the evolution of the drilling services market in Romania during 2004-2008 was made in three scenarios:
- pessimistic: the drilling activity would go, in 2008 to the average level registered during 1999-2003;
 - average: the drilling activity of SNP PETROM S.A. would reach in 2008 the maximum level registered during 1999-2003, and SNGN ROMGAZ S.A.'s activity would register an average annual increase of 5%;
 - optimistic: the drilling activity of SNP PETROM S.A. would reach in 2005 the maximum level registered during 1999-2003 and would remain constant during 2006-2008 and for SNG ROMGAZ S.A. would be foreseeable an annual average increase of approx. 10%.
- (37) The forecast scenarios underline the fact that the level of demand will continue to be below the level of the offer on the gas and oil drilling probes' market in Romania. Therefore:
- in the pessimistic scenario, the average proportion demand- offer will be of approx. 45%, due to an annual decrease with approx. 3% of the offer from the drilling companies;
 - in the average scenario, the average proportion demand-offer will be of approx. 55%. The average scenario can be characterized as representing a medium trend of the evolution on the future drilling market, with an increase of the drilling activity of 13%;
 - in scenariul optimist, the forecast average proportion demand-offer is of 64%. This scenario can be characterized as showing a more accentuated increase of the drilling activity in Romania compared to the previous period (with 32%), which could be generated by possible short-term capital infusions, as a result of the privatization of the main customers.
- (38) Under the conditions of the three forecast scenarios, it is estimated that the market share of S.C. Foserco S.A. in the drilling activity shall have the same trend as in the previous period, namely to remain between 3.5% and 4%.

4.2 External market

- (39) Since 2001, S.C. Foserco S.A. Tg. Ocna capitalized its services outside Romania, respectively in Kazakhstan. The main customers on the external market are Upetrom –Kazakhstan and Tasbulat Oil Kazakhstan.

- (40) The proportion of the turnover at export in the total turnover is presented in the following table:

Table nr. 8- *Proportion of the turnover at export in the total turnover*

Year	1999	2000	2001	2002	2003
Proportion of exports in accomplished turnover (%)	-	-	4,3%	18,1%	28,9%

Source : MFP Notification

5. THE RESTRUCTURING PROGRAM

- (41) The state aid in amount of ROL 265,000,453,133 is granted for restructuring S.C. FOSERCO S.A Tg. Ocna and of its return to viability.
- (42) With this purpose, the company elaborated a restructuring program comprising organisational, management, financial, technical and technological measures.
- (43) The restructuring program was made based on the market study elaborated by the Company for research, technological engineering and design for the oil and gas extractive industry PETROSTAR S.A. Ploiesti, taking into account the three scenarios for the market evolution: pessimistic, intermediary and optimistic.
- (44) The accomplishment of the restructuring program needs a financial effort of ROL 674,705,453,133.
- (45) To summarize, the restructuring program provisions the following:

Measures regarding the organisational and managerial restructuring of the Company

- *Lease of assets domestically and abroad:*

The measure consists in leasing to domestic and foreign customers of some drilling equipment, tools, accesories, fixings and drilling spare parts.

The cost of implementing the measure is of ROL 10,600 mln. and is to be borne from the Company's own resources.

The estimated economic effect consists in collecting revenues amounting ROL 238,500 mln. coupled with the reduction of maintenance costs of these assets with ROL 15,300 mln.

In 2004, the company concluded a lease agreement with Tasbulat Oil, from Kazakhstan, for an F-200 drilling installation.

- *Extension of rendered services on the external market*

The measure consists in rendering assistance and consulting services to foreign clients, technical assistance based on an agreement concluded with UFK-Kazakhstan, required for drilling programs in the perimeters concessioned by Petrom-OMV.

The cost of implementing the measure is of ROL 18,900 mln. and is borne from the company's own resources.

The economic effect estimated consists in increasing revenues obtained by approximately ROL 22,700 mln.

In 2004 a technical assistance agreement was concluded with UFK-Kazakhstan, upon which S.C. Foserco S.A. Tg. Ocna specialists provide technical assistance in drilling matters, identifying and applying solutions adequate to the specific conditions of the area.

- *Implementing a quality management system according to ISO 9001:2000*, with consequences in the quality of rendered services and promoting the company image on the market.

Implementation cost: ROL 110 mln., borne from company own sources.

Deadline: 2004.

- *Organisation of business on profit centers*

The measure consists in organising the company's activity on profit centers aiming to identify and eliminate non-profitable activities.

The implementation cost of the measure is of ROL 100 mln. and is borne from company's own sources.

The effects estimated to be obtained: revenue increase amounting to ROL 2,000 mln. and cost reductions amounting ROL 1,000 mln.

Deadline: 2004-2005.

- Modernisation of IT equipment and implementation of an IT system for financial accounting in order to improve management accounting
- The implementation cost of the measure is of ROL 110 mln. and is borne from the company's own sources
- Implementation deadline: 2005.

B. Measures regarding the technical and technological restructuring of the Company

⁵[...]

C. Measures regarding the financial restructuring of the company

- *Sale of assets*

The measure consists in dismantling and sale of two drilling installations type T- 50, F-100, respectively.

The cost of implementing the measure is of ROL 12,000 mln. and will be borne by the company's own sources.

⁵ confidential data

The economic effects: cash contribution of ROL 12,000 mln. and reduction of expenses for maintenance and equipment repairs of ROL 1,500 mln.

Implementation deadline: 2005 for the T50 type, and 2007, respectively for the F-100 type.

- ***Exemption from payment of charges and penalties for delayed payment of company debt to the state consolidated budget as well as rescheduling over a 60 months period of budgetary debt.*** The total value of the facilities representing state aid is of ROL 265,000,453,133.

(46) To summarise, the measures contained in the restructuring plan are outlined in Table no. 9.

Table no. 9 - *Summary of the company restructuring measures*

MEASURE	DEAD LINE	COSTS (ROL mill.)	FINANCING		STATE AID (ROL mill.)	EFFECTS	
			OWN FUNDS (ROL mill.)	INVESTOR' S FUNDS (ROL mill)		Costs reduction (ROL mill.)	Receipts increase (ROL mill)
I. Organisational measures	2004-2008	29,610	29,610	-	-	263,200	16,300
II. Technical and technological measures	2004-2008	368,095	160,715	207,380	-	375,200	75,000
III. Financial measures	2004-2008	277,000	12,000	-	265,000	12,000	1,500
Total I+II+III	2004-2008	674,705	202,325	207,380	265,000	650,400	92,800

Source: *Restructuring programme*

- (47) The restructuring programme, through the financial restructuring component, allows for the possibility of increasing cash flow, providing a stable cash flow, which will ease the financial activity of the company. This way the company will be able to meet its current debt to the State, and to allocate required liquidity in order to execute planned investments required to develop and support the production programme in the long run.

6. STATE AID CHARACTER OF THE FINANCIAL SUPPORT GRANTED TO THE COMPANY BY THE STATE

- (48) Art. 2 from Law no. 143/1999 regarding the State aid, with subsequent changes and completions, defines state aid as any support measure granted by the State or by administrative and territorial authorities from state resources, irrespective of the form, which distort or threaten to distort competition, by favouring of certain enterprises, of production of certain goods, rendering certain services, or affecting trade between Romania and member states of the European Union, being considered compatible with a normal competition environment.
- (49) Thus, in order to decide on the state aid character of the financial support granted to S.C. FOSERCO S.A. Tg. Ocna, we have to analyse how the state defining criteria mentioned above are met.
- (50) The facilities from which S.C. FOSERCO S.A. Tg. Ocna is benefiting are represented by rescheduling and exemption from payment of due budgetary liabilities representing tax, fees, contributions and other budgetary revenues, as well as interest and penalties for delayed payment which are due and not paid to the consolidated state budget.
- (51) Analysing this financial support measures, the Competition Council has found that there is no doubt that these measures are financed from state resources and allow for an advantage of a certain undertaking, namely S.C. FOSERCO S.A. Also, there is no doubt that the financial measures could distort competition and affect trade between Romania and member states of the European Union, because the company renders drilling services abroad.
- (52) To conclude, the financial support measures granted are not considered state aid and fall under Law no. 143/1999 regarding state aid, with the subsequent modifications and completions.

7. EVALUATION OF THE STATE AID MEASURES INTENDED TO BE GRANTED TO S.C. FOSERCO S.A. Tg. Ocna

- (53) The objective of the state aid is the restructuring of S.C. FOSERCO S.A. in order to restore the viability of the company by the end of the restructuring period. The state aid must be analysed according to the criteria provided in the Regulation on State aid for rescue and restructuring firms in difficulty (hereinafter the Regulation).
- (54) S.C. FOSERCO S.A. Tg. Ocna did not benefit from State aid for rescue and/or restructuring before.
- (55) Among the causes leading to the deterioration of the financial results of the company we mention the following:
- the financial blockage, leading to a late collection of the receivables;
 - the decrease, in the analysed period, of the demand for the core services of the company;

- the imposition by some beneficiaries of some material consumptions and execution tariffs, without taking into consideration the inflation rate and the depreciation of the national currency;
- the practical impossibility to update the remainder to be executed in the following periods, whilst the acquisition prices for raw materials, fuel, transport and other services bought by the company, present monthly increases.

(56) The set objectives during the restructuring programme are:

- Increasing the turnover;
- Increasing productivity;
- Recovery of losses;
- Increasing cash flow;
- Diminishing debt;
- Increase of net worth;
- Reduction of inventory;
- Increasing the load factor of the installations;
- Reducing costs and full financing of costs from collected revenues;
- Increase of net profit net;
- Increase of self financing capacity;
- Improving performance indicators.

(57) The final purpose of the set objectives, after implementing the restructuring programme, is to restore the viability of the company in such a way that the company fully covers its costs and can compete on the market on its own.

(58) Continuing to operate without implementing a restructuring programme would lead to:

- Losing the acquired market segment due to lack of financial means required to restart the productive cycle and lack of an adequate marketing strategy;
- Degradation of existing tangible assets by the continued diminishing of the capacity utilisation;
- The employees' dissatisfaction with negative consequences over the quality of products and of the social climate.

(59) The non granting of the state aid could lead eventually to the liquidation of the company, with consequences like:

- Collective layoffs, leading to immediate and long term increase in unemployment in the area whereas the unemployment rate is higher compared to the Bacau county average;
- Negative economic and social consequences for those subject to layoffs, whereas many of the employees of SC FOSERCO SA are the only family providers, for an average of three family;
- Increase of budgetary expenses regarding allowances for unemployed, support allowances and other forms of social protection granted to people subject to layoffs which from contributors to the budget become consumers of financial resources;
- Reduction of company contributions related to employees;
- Partial recovery of debt to budgetary creditors and third parties;

- Reduction of business volume for suppliers and services performers in the area collaborating with SC FOSERCO SA.

- (60) The Competition Council notices that the undertaking that benefited from the State aid is situated in the city Tg. Ocna, having the highest unemployment rate from the County Bacau, respectively 6.2% (from the first half of the year 2004).
- (61) The analysis of the notified measure was carried out according to criteria the criteria for granting the State aids contained by the Regulation on state aid for rescue and restructuring firms in difficulty.

7.1. ELIGIBILITY OF S.C. FOSERCO S.A. Tg. Ocna – COMPANY IN DIFFICULTY

- (62) S.C. FOSERCO S.A. is a company in difficulty since it was confronted with several problems that negatively influenced its production, economical and financial activity.
- (63) The main economic and financial indicators of the company in the analysed period are presented in Table no. 10.

Table no. 10- *Evolution of economic and financial indicators in 1999-2003*

ROL thousand					
FINANCIAL INDICATORS	1999	2000	2001	2002	2003
1. Revenues, of which:	37,318,084	58,553,771	94,062,745	185,970,756	139,217,369
- operating	37,280,128	56,814,737	72,389,505	141,515,144	136,686,610
- financial	22,082	23,629	13,482,187	179,597	2,530,759
- exceptional	15,874	1,715,405	8,191,053	44,276,015	-
2. Turnover	37,224,964	57,711,711	75,676,990	141,515,144	124,144,883
3. Total expenses, of which:	67,955,917	116,714,379	118,798,355	215,618,080	211,878,549
- operating	52,219,079	64,217,019	90,610,389	180,622,470	209,888,302
- financial	308,068	9,596	1,474,135	1,079,216	1,990,247
- exceptional	15,428,218	52,487,764	26,713,831	33,916,394	-
4. Gross Profit profit (+)/ loss (-)	-30,637,281	-58,160,608	-24,735,610	-29,647,324	-72,661,180
5. Net result profit (+)/ loss (-)	-30,637,281	-58,160,608	-24,735,610	-29,647,324	-72,661,180
6. Total debt, of which:	85,312,389	157,291,270	209,467,763	243,925,127	258,344,945
- budget	67,448,408	136,174,386	177,862,806	201,708,651	236,512,410

7. Past due debt, of which:	79,027,616	99,017,595	168,311,224	213,544,812	67,785,467
• budget	57,071,448	58,249,429	147,958,609	175,181,559	55,807,712
• suppliers	18,913,098	17,965,463	13,683,603	38,363,253	11,977,755
• other debt	3,043,070	22,802,703	6,669,012	-	-

Source: Restructuring programme

(64) The financial analysis outlines the decreasing trend of the exercise result as well as of the company's debt. The important volume of the debt, interest and related penalties, accrued to the budget as well as to other creditors, exposed the company to the risk of foreclosure of its patrimony. As of 31.12.2003 current liabilities surpassed current assets by 1.85 times and total liabilities surpassed total assets by 1.16 times. The highest percentage in total liabilities is represented by debt to the state budget. The main debt of the company derived from before 1999. As of 30.11.1998, the company has recorded in its books debt to the budget amounting ROL 17.660.070.000. Lack of liquidity determined the company to adjourn the payment of this debt to the budget, which generated increases and penalties for delayed payment to a large amount; this led to an increase of exceptional expenses; this not only nullified the operating result but even surpassed them which in turn generated company losses from one year to another.

(65) The main arguments used to establish that S.C. Foserco S.A. is a company in difficulty are the following:

a) *Evolution of the turnover* is presented in Table no. 11.

Table no. 11 – *Evolution of turnover for 1999-2003*

Indicators	1999	2000	2001	2002	ROL mill. 2003
Turnover	37,225	57,712	75,677	141,515	124,145

Source: Restructuring programme

Important to notice that, in current prices, the turnover of the company is fluctuating, with a decrease of it in 2003 over 2002.

b) *Evolution of the net result of the exercise* is presented in Table no. 12

Table no. 12 – *Evolution of the net result of the exercise in 1999-2003*

Indicators	1999	2000	2001	2002	ROL mill. 2003

Net result	-30,638	-58,161	-24,736	-29,647	-72,661
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Source: Restructuring programme

It is to be observed that the net result of the exercise shows a constant negative evolution, having a peak in 2003, when the loss surpassed shareholders' equity by 2.71 times.

c) *Evolution of shareholders' equity* is presented in Table no. 13

Table no. 13 – *Evolution of shareholders' equity in 1999-2003*

Indicators	1999	2000	2001	2002	ROL mill. 2003
Shareholders' equity	-40,680	-69,423	+31,652	-155	-47,176
Net result	-30,638	-58,161	-24,736	-29,647	-72,661
Net result/ Shareholders' equity	-75.3%	-83.8%	-78.1%	-191.3%	-154%

Source: Restructuring programme

Correlating with the exercise result, shareholders' equity show, except for 2001, negative values, demonstrating that the company is in a difficult situation due to losses reported from previous years.

d) *Evolution of general liquidity indicator* is presented in Table no. 14

Table no. 14 – *Evolution of general liquidity in 1999-2003*

Indicators	1999	2000	2001	2002	2003
Current assets (ROL mill.)	21,461	33,881	67,682	78,987	139,572
Current Liabilities	85,312	157,291	209,468	243,925	258,345
General liquidity (Current assets/ Current liabilities)	0.25	0.22	0.32	0.32	0.54

Source: Restructuring programme

The evolution of the indicator reveals the fact that the company is not able to pay its current debt by converting its current assets in liquidities. The level of general liquidity, in absolute terms, is way below the average margin accepted by financial analysts in specialty literature (1.2-1.5).

e) *Evolution of patrimonial solvability* is presented in Table no. 15

Table no. 15- *Evolution patrimonial solvability in 1999-2003*

Indicators	1999	2000	2001	2002	2003
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Shareholders' equity (ROL mill.)	-40,680	-69,423	+31,652	-155	-47,176
Total liabilities (ROL mill.)	44,634	87,869	241,120	251,770	292,497
Patrimonial solvability (Shareholders' equity/total liabilities)	-0.91	-0.79	0.13	0.00	-0.16

Source: Restructuring programme

Due to the steep decrease in shareholders' equity, coupled with an increase in liabilities, because of an increase of debt, it can be noticed a diminishing of the solvability, with even negative values, generated by losses carried forward from one year to another and led to decapitalization of the company.

f) *Evolution of the indebtness ratio* is presented in Table no 16.

Table no.16 *Evolution of the indebtness ratio 1999-2003*

Indicators	1999	2000	2001	2002	2003
Total liabilities (ROL mill.)	85,312	157,291	209,468	243,925	258,3445
Total assets (ROL mill.)	44,634	87,869	241,120	251,770	292,497
Indebtness ratio (Total liabilities /Total assets)	1.91	1.79	0.87	0.99	0.88

Source: Restructuring programme

The evolution of the indicator reflects an increase, year over year, of the companies liabilities, which coupled with the result of the exercise indicates the inability of shareholders' equity to generate profit to cover the debt accrued by the company.

g) *Evolution of net worth* is presented in Table no. 17.

Table no. 17- *Evolution of net worth in 1999-2003*

ROL mill.					
Indicators	1999	2000	2001	2002	2003
Net worth	-40,678	-69,422	31,652	7,845	-46,354

Source: Restructuring programme

The analysed period reveals the disappearance of the almost entire net worth.

h) *Receivable collection timing* is presented in Table no. 18

Table no. 18 - *Receivable collection timing in 1999-2003*

Indicators	1999	2000	2001	2002	2003
Receivables (ROL mill..)	3,783	16,785	49,109	61,483	29,321
Turnover (ROL mill.)	37,225	57,712	75,677	141,515	124,145
Receivables/ turnover*365	37.1	106.2	236.9	158.6	86.1

Source: Restructuring programme

The evolution of this indicator shows a relatively growing trend which signals an imminent crisis of liquidity for the company.

i) Net profit ratio

This ratio has constant negative values, due to the fact that the company has losses every year; this ratio reflects the influence of accrued debt impacting exercises in the analysed period.

j) Return on equity ratio

Represents the ability of the company to generate profit from investing shareholders' equity. Whilst the gross profit is negative and the capital employed is diminished by the reported results, this ratio, also, has negative values throughout the period.

- (66) With regard to the above it is appreciated that S.C. Foserco S.A. Tg. Ocna is a company in difficulty according to art. 2 from the *Regulation*.

7.2. BELONGING TO A BUSINESS GROUP

- (67) According to the provisions of Art. 2 paragraph (5) of the Regulation on state aid for rescue and restructuring firms in difficulty, a company belonging to a larger business group is normally not eligible for rescue and restructuring aid, except for the case when it can be proved that the difficulties of the company are its own and do not result from an arbitrary allocation of costs inside the group and that the difficulties are too serious to be dealt within the group.
- (68) The shares of S.C. FOSERCO S.A. Tg. Ocna are owned as follows:
- **BRINGTON CAPITAL S.A**- owns 44.042% of the company's shares. It is a foreign legal person, incorporated in the British Virgin Islands, and became shareholder of S.C. Foserco S.A. by buying the shares from S.C. RPT OIL S.R.L;

- *S.C. RPT OIL S.R.L. Constanta* holds 39.27% of the shares. It is a Romanian legal person incorporated with the Registry of Commerce at no. J134530/1994, held by 5 associates, natural persons, none of them with a majority position;
- *The Federation of the Free and Independent Unions in the Oil Industry (FSLI)* owns 10% of the shares, being a union federation which does not own the resources required to restore the viability of the company without resort to state aid. The financial resources of FSLI are made, mainly, from union dues, and their size is limited to the financing of their own activity;
- *Other shareholders* – 6.68% of the shares – natural persons who became shareholders subsequent to the Mass privatisation program, mainly employees of the company and their family members, (some got retired in the meantime), who do not possess financial resources.

(69) Analysing the data in the Brington Capital S.A.'s financial statements of 2001, 2002, 2003 it is noticed that the company's financial resources are limited, being earmarked for working capital. In 2001-2003 the company posted a total cumulated profit of USD 7,150, not sufficient to finance costs required for the restructuring of SC Foserco S.A. Thus, in 2003, the company has total assets of USD 111,470 of which USD 49,160 represent cash and cash equivalents as well as receivables of USD 62,310. In terms of liabilities, the company registered unpaid payment obligations (suppliers, payroll, fees and other creditors) amounting USD 58,650. Equity was in amount of USD 52,280, of which USD 50,000 represents the shareholders' equity, the difference of USD 2,820 representing retained earnings.

(70) The evolution of the net result of S.C. RPT OIL S.R.L. shows the fact that, in 1999-2003, this company did not have the financial power to sort out the difficulties confronting S.C. FOSERCO S.A.

Table no. 20: *Evolution of financial results of S.C. RPT OIL S.R.L. in 1999-2003*

ROL thou.					
Indicators	1999	2000	2001	2002	2003
Net profit/ Net loss	-4,054,409	1,465,247	1,871,882	4,842,761	-9,011,691,000

Source: *S.C. RPT OIL S.R.L. balance sheets*

As it can be noticed, the company has a profit only in 2000, 2001 and 2002, but it is too small to cover S.C. Foserco S.A.'s debt and help it rebalance.

(71) ⁶ [...]

⁶ confidential data

- (72) According to the above mentioned, the shareholders of S.C. Foserco S.A. Tg. Ocna do not have the financial means to help the company turnaround more than it has already been done. The significant shareholders of SC Foserco SA have used all legal means afforded by their financial resources in order to support the economic turnaround and restructuring.

7.3. THE RESTORATION OF THE COMPANY VIABILITY

- (73) According to Article 12 of the Regulation state aid for rescue and restructuring firms in difficulty the restructuring plan has to include the elimination of unprofitable activities and to offer to the company the long term viability, allowing to it to function with own resources.
- (74) The restructuring plan of S.C. FOSERCO S.A. Tg. Ocna was worked out after a SWOT analysis that includes strong and weak points from juridical, commercial, production, financial and human resources view points, and describes the circumstances that lead to the appearance of difficulties the company face with.
- (75) The strategy of S.C. FOSERCO S.A. Tg. Ocna aims to preserve the strong points of the company and to eliminate the weak ones. The focus is on increasing the labour productivity by revamping equipment and transportation means, reducing operating expenses, especially those for disassembling, transportation-assembling installations, reducing the non-productive time of the installations, extending services offered on external markets by having competitive prices, realising profit centres, preserving/dismantling and sale of worn out installations, reducing receivables collection timing.
- (76) After implementing the restructuring programme, in all three scenarios of market evolution, the company becomes viable and will have a positive evolution of shareholders' equity as well as of return on equity, return on assets, being thus able to carry out business by its own resources.
- (77) The fact that the implementation of the measures contained in the restructuring plan assures the viability of the company is demonstrated as well by the profit and loss account estimates in the intermediary hypothesis, for the next 5 years, which is shown in Table no. 19.

Table nr. 19 *Evolution of leading economic and financial indicators forecast for 2004-2008*

ROL mill.					
INDICATOR	2004	2005	2006	2007	2008
1. Total revenues, of which:	284,350	296,860	309,920	323,556	337,792
- operating	260,920	272,400	284,386	296,900	308,775
- financial	16,630	17,560	18,534	19,556	21,817
- exceptional	6,800	6,900	7,000	7,100	7,200
2. Turnover	280,000	290,000	300,000	315,000	325,000
3. Total expenses, of which:	212,362	221,494	230,796	240,259	249,869
- operating	196,726	205,185	213,803	222,569	231,472

- financial	15,636	16,309	16,993	17,690	18,397
- exceptional	-	-	-	-	-
4. Gross result profit (+) / loss (-)	71,988	75,366	79,124	83,297	87,923
5. Profit tax	-	-	2,659	20,824	21,981
6. Net result profit (+) / loss (-)	71,988	75,366	76,465	62,473	65,942
7. Covered loss	71,988	75,366	68,489	-	-
8. Profit after loss deduction	-	-	7,976	62,473	65,942
9. Personnel	380	383	386	390	394
10. Labour productivity - ROL mill./employee	736.8	757.2	777.2	807.7	824.9

Source : Restructuring programme

- (78) It is to be noticed that starting with 2006 the company covers entirely its losses and makes a profit with an ascending evolution by 2008.
- (79) The implementation of the restructuring programme has as objective the radical change of the economic and financial position of the company in such way that by the end of the restructuring period, the company to be able to cover entirely its costs and to be able to compete by its own forces on the market, illustrated by the cash flow estimate in the intermediary version:

Table no. 20- *Evolution of company's cash flow estimate in 2004-2008*

					ROL mill.
INDICATOR	2004	2005	2006	2007	2008
1. Operating revenues	260,920	272,400	284,386	296,900	308,775
2. Operating expenses, of which depreciation	196,726 30,570	205,185 31,010	213,803 31,370	222,569 31,950	231,472 32,425
3. Operating result	64,194	67,215	70,583	74,331	77,303
4. Financial revenues	16,630	17,560	18,534	19,556	21,817
5. Financial expenses	15,636	16,309	16,993	17,690	18,392
6. Financing result	994	1,251	1,541	1,866	3,420
7. Exceptional revenues	6,800	6,900	7,000	7,100	7,200
8. Exceptional expenses	-	-	-	-	-
9. Exceptional result	6,800	6,900	7,000	7,100	7,200
Gross profit	71,988	75,366	79,124	83,297	87,923

Profit tax	-	-	2,569	20,824	21,981
Depreciation	30,570	31,010	31,370	31,950	32,425
CASH FLOW	102,558	106,376	107,925	94,423	98,367
Rescheduled debt	36,235	44,835	35,686	12,138	10,688
Free cash flow	66,323	61,541	72,239	82,285	87,679

Source : Restructuring programme

- (80) Upon implementation of the measures, at the end of the restructuring plan – year 2008 – the following indicators are to be met:

Table no. 21- *Target company indicators for the year of 2008*

No.	INDICATOR	
1.	Net profit	ROL 65,942 mln.
2.	Turnover	ROL 325,000 mln.
3.	No. of employees	384
4.	Shareholders' equity	ROL 160,200 mln.
5.	Receivables collection timing	25 days
6.	Indebtness ratio	0.08
7.	Liabilities payment timing	30 days
8.	Return on assets	55%
9.	Return on equity	41%

Source: Restructuring program

7.4. AVOIDANCE OF SIGNIFICANT DISTORTION OF THE NORMAL COMPETITIVE ENVIRONMENT

- (81) Through the grant of the aid and application of the restructuring program of S.C. FOSERCO S.A. the structure of the relevant market is not modified by anti-competitive effects; this operation has the purpose of raising economic efficiency of the company by reducing the production costs and does not lead to a liquidity surplus which might be used in aggressive activities that distort competition on the market without any connection with the restructuring process.
- (82) The market share of S.C. FOSERCO S.A. Tg. Ocna on the drilling and related services market in Romania, in 1999-2003, varies between 3.1 and 4%. (according to the market study). During the restructuring period, respectively 2004-2008, the company estimates that it will maintain its market share within the same limits: 3,1%-4%. Since the market share on relevant market of the company is very small at the country level, it is considered that, according to Article 13 of the Regulation on state aid for rescuing and restructuring firms in difficulty, there is no significant distortion of the competition.
- (83) the restructuring program the S.C. FOSERCO S.A. Tg. Ocna does not increase its market share on internal market and will improve the utilization level of production capacity.

- (84) The evolution of the utilization level of production capacities during the period 1999-2003 is presented in Table no. 22.

Table no. 22- *Utilisation level of production capacity by S.C. Foserco S.A.*

Year	Annual capacity (drilling, m)	Load factor (%)
1999	22,460	39
2000	21,817	59
2001	30,175	48
2002	18,430	51
2003	17,906	47

Source: Restructuring programme

- (85) State aid will be used only for restoring the viability of the company, not allowing the beneficiary, during the application of the restructuring plan, to extend its production capacities.
- (86) In order to minimise as much as possible the negative effects of granting this state aid on trade conditions, in such a way that the positive effects in view to mitigate the negative effects, by the end of the restructuring period the company will reduce its production capacities with 10% as compared with the 2003 level. Establishing such a compensatory measure the Competition Council took into consideration the fact that, according to the market study, the company does not own a significant position on the relevant market (having a market share of 3.1%-4%, which it intends to maintain at the same levels during the restructuring period).

7.5. AID LIMITED TO THE MINIMUM

- (87) According to the provisions of Article 14 of the Regulation on state aid for rescuing and restructuring firms in difficulty, the amount and intensity of the state aid must be limited to the minimum necessary in order to allow the restructuring to be made depending on the existing financial resources of the company and shareholders.
- (88) Before granting the State aid, the beneficiary analyzed all financing possibilities of restructuring plan. Thus, in order to contribute to the restructuring program, the beneficiary will appeal to sales and assets leasing, that are not related to main object of activity; these measures are parts of the restructuring plan.
- (89) The restructuring program is financed by own resources of the company, investor contribution and state aid, which proves that the value of the state aid is reduced to the minimum necessary for the program to be finalized in the operating conditions proposed by the company as state aid beneficiary.
- (90) S.C. FOSERCO S.A.Tg. Ocna has a substantial contribution to the implementation of the measures from the restructuring program, 60.7% respectively of the total financial effort. The

required State aid amounting ROL 265,000.4 mill. relieves the company from payment of debt and allows it to become eligible to obtain loans, limiting in this way the State aid to the minimum strict necessary.

7.6. STATE AID INTENSITY AND RESTRUCTURING COST

(91) The amount and the intensity of state aid must be strictly limited until the objectives of the restructuring programme are met.

(92) The cost of restructuring S.C. FOSERCO S.A Tg. Ocna amounts ROL 674,705,453,133 being born as follows:

- own resources of the company ROL 202,325 mill. of which:

- depreciation: ROL 157,325 mill. ;
- sale of assets: ROL 12,000 mill ;
- penalties paid by investor for failing to meet
- in due course the investments assumed by
- the privatization contract: ROL 33,000 mill.

- *investor's contribution*

ROL 207,380 mill.

- *state aid*

ROL 265,000 mln.

(93) The state aid intensity, calculated as ratio between the state aid value and the restructuring cost, is of 39.3 %.

7.7. OBSERVANCE OF THE PRINCIPLE „ONE TIME, LAST TIME”

(94) S.C. Foserco S.A Tg. Ocna has never received restructuring aid, so that Art. 18 of the Regulation on state aid for rescue and restructuring firms in difficulty, which stipulates the fact that restructuring aid must only be granted once, is observed.

7.8. MONITORING AND ANNUAL REPORTING

(95) In accordance with the provisions of Art. 17 of the Regulation on state aid for rescue and restructuring firms in difficulty, the Competition Council is permanently monitoring the way of implementation of the restructuring plan, so that this does not fail to accomplish the objectives of the restructuring plan.

(96) The Competition Council will continue to monitor the implementation of the restructuring plan until the end of the period, so that it will ensure that there will be no increases in production capacities, major deviations from the achievement of the restructuring measures and that the aid will not lead to supplementary liquidities to be used for other activities than the ones comprised in the restructuring programs.

8. CONCLUSIONS

- (97) Following the analysis based on the notification form, market study, information received from the supplier and beneficiary, as well as the report of the Bacau Competition Inspectorate, following on - site verifications, the Competition Council concludes that the aid intended to be granted to S.C. FOSERCO S.A Tg. Ocna is not in a position to significantly distort the normal competitive environment and does not infringe the proper application of the international treaties to which Romania is a party.
- (98) Following the analysis made, it was found out that the state aid in total amount of ROL 265,000.4 million consisting of payment facilities granted on the basis of the G.E.O no. 40/2002 for recovering the budgetary arrears, approved with modifications and completions by the Law no. 491/2002 with subsequent modifications and completions, fulfils the granting criteria in accordance with the *Regulation on state aid for rescue and restructuring firms in difficulty*.

DECIDES

Art. 1. The measure notified by the Ministry of Public Finance, whose beneficiary is S.C. FOSERCO S.A Tg. Ocna represents State aid in the meaning of Art. 2(1) of the Law no. 143/1999, with the subsequent modifications and completions.

Art. 2. On the basis of Art. 10 of the Law no. 143/1999 on state aid, with subsequent modifications and completions, the Competition Council Decision no. 151/14.05.2004 is revoked.

Art. 3. On the basis of Art.12 paragraph(2) c) corroborated with Art.14 paragraph(1) e) of the Law no. 143/1999, with subsequent modifications and completions, the State aid in the view of restructuring that is intended to be granted to S.C.FOSERCO S.A. Tg. Ocna, is authorized, conditional on the observance of Art. 4 and Art. 5 of the present Decision.

Art. 4. The company is compelled to implement entirely the assumed restructuring plan.

Art. 5. The company will reduce production capacity with 10% compared to the level of the year 2003.

Art. 6. In case of non compliance with the present decision, provisions of art. 13 from Law no.143/1999, with the subsequent modifications and completions will be applied.

Art. 7. The value of the state aid that will be granted is ROL 265,000,453,133.

Art. 8. Decision becomes applicable on the communication date.

Art. 9. According to the Art. 24 of the Law no. 143/1999, with the subsequent modifications and completions, the granting authorities will transmit to the Competition Council information on the state aids granted, with the view to their inventorying and monitoring. The Ministry of Finance will transmit to the Competition Council annual reports on the implementation of the restructuring plan. The first report will be transmitted to the Competition Council in 6 months since the decision is issued.

Art. 10. According to the provisions of Art. 29 of the Law no. 143/1999 on State aid, with subsequent modifications and completions, the present decision may be challenged by the interested persons by administrative proceedings before the Bucharest Court of Appeals, within 30 days following the communication date.

Art. 11. This Decision will be communicated by the General Secretariat of the Competition Council to:

- the Ministry of Public Finance, Apolodor Street, no. 17, sector 1, Bucharest;
- S.C. FOSERCO S.A, Str. Avram Iancu, nr. 2, loc. Tg. Ocna, jud. Bacau.

PRESIDENT

MIHAI BERINDE