

DECISION OF THE COMPETITION COUNCIL

No 73 on 19.04.2005

**regarding the financial support measures granted by the Ministry of Economy and Trade to the Subsidiary Company for Electricity Distribution and Supply
ELECTRICA DOBROGEA SA**

THE COMPETITION COUNCIL,

Taking into account the provisions of the Decree no.57/2004 for the appointment of the Competition Council's members,

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

Taking into account the provisions of the Law no. 143/1999 regarding the State Aid, published in the Official Monitor of Romania, Ist Part, no. 370 on 3.08.1999, with the subsequent modifications and completions,

Taking into account the provisions of the European Agreement regarding 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 Monitor of Romania no.73, Part I, on 12.04.1993,

Based on the following reasons,

I. THE PROCEDURE

(1) By the address no. 100881/ICS/14.02.2005, registered at the Competition Council with no. RS-AS 2/16.02.2005, the Ministry of Economy and Trade notified to the Competition Council, based on art. 6 in the Law no. 143/1999 regarding the state aid, with the subsequent modifications and completions, the notification of the financial support measures granted to the Subsidiary Company

for Electricity Distribution and Supply ELECTRICA DOBROGEA SA (hereby named SC FDFEE Electrica Dobrogea SA).

(2) By the addresses of the State Aid Authorization Department no. DAAS/220/03.03.2005 supplementary data were requested based on art. 6 align. (4) in the Law no. 143/1999 regarding the state aid, with the subsequent modifications and completions. The Ministry of Economy and Trade answered by the addresses no. 1583/10.03.2005. The notification became effective when the data were complete and exact, namely on 10.03.2005.

2. DESCRIPTION OF THE MEASURE

2.1. LEGAL BASIS FOR GRANTING THE STATE AID

(3) The legal basis for granting the state aid is:

- EGO no. 37/2004 on measures to reduce arrears in the economy;
- GD no. 1000/2004 on certain measures to develop and finalize the privatization and the modification and completion of the Privatization Strategy for the undertakings that are electricity distribution and supply subsidiaries „Electrica Dobrogea” SA and „Electrica Banat” SA;
- Law no. 570/2004 on certain measures for privatizing the undertakings that are electricity distribution and supply subsidiaries „Electrica Dobrogea” SA and „Electrica Banat” SA, as well as some measures for regulating the activities of the commercial companies acting in the electricity field.

2.2. Beneficiary of the state measures of support

2.2.1. Preamble

(4) SC Electricity Distribution and Supply Subsidiary “Electrica Dobrogea” SA is one of the 8 subsidiaries of the commercial company of Electricity Distribution and Supply “ELECTRICA” SA Bucuresti. The subsidiary Electrica Dobrogea was established on 01.03.2002 due to the legal and institutional harmonization of the Government policy with the provisions and demands of the European legislation.

(5) FDFEE Electrica Dobrogea SA’s main activity object is the distribution and trade of electricity in south-east region of Romania, namely in Dobrogea (2 counties: Constanta and Tulcea) and in Baragan (2 counties: Calarasi si Ialomita). In the same time, the undertaking also makes the following:

- dispatching distribution installations;

- elaborating prescriptions and normatives specific to the activity of electricity distribution, according to the regulations prior issued by the National Authority of Regulation in the Energy Field (ANRE);
- projecting and implementing the communication and informatics systems, following to insure their inter-connecting and function.

(6) The distribution activity consists in the exploiting, maintaining and developing the distribution network in order to transmit the electricity from the transport producers/ operators /other distributors to the final consumers, according to the signed contracts, under proper safety and quality conditions.

(7) SC FDFEE Electrica Dobrogea SA carries out its distribution activity based on the license issued by ANRE, on approx. 25.000 square km from the country's area through its 4 subsidiaries (Constanta, Calarasi, Tulcea si Slobozia), being in the service of approx. 593,000 consumers reported at a population in the area of approx. 1.7 millions inhabitants, from this point of view being the smallest subsidy from the eight subsidies in the territory belonging to Electrica. SC FDFEE Electrica Dobrogea SA's subsidiaries aren't legal persons by their own.

(8) Electricity supply activity represents, according to the *Law of Electricity* no. 318/2003, the commercial activity of electricity sale-purchase, carried out by a legal person, based on the license issued by ANRE. The distribution activity represents the transmission of electricity through the specific infrastructure, consisting in networks of 110 kv or below this voltage level. According to the art. 16(1) in the *Law of Electricity* „the activities and services licenses are granted for, are of public interest, excepting from those exclusively designated for the owner of license or authorization's own consumption”.

(9) Among the obligations of SC FDFEE Electrica Dobrogea SA, according to the *Law of Electricity* no. 318/2003, are also the following:

- ensuring the continuity and safety in the supply of electricity upon contracts;
- carrying out the activity of commercializing the electricity based on commercial contracts/ frame contracts – for the regulated market;
- ensuring the users' access under technical connection conditions and access to supply information regarding the electrical distribution network;
- exploiting, renewing the technology, re-habilitating and developing the electrical distribution networks, meeting the technical regulations in force;
- fulfilling the performance standards for the supply service;

- ensuring, based on the frame-contracts, the supply of electricity for the captive consumers located in the areas for which SC FDFEE Electrica Dobrogea SA owns supply license;

- monitoring the safety in functioning of the electrical distribution networks, as well as the performance indexes for the distribution service.

(10) SC FDFEE Electrica Dobrogea SA makes almost all its incomes from the distribution and electricity trading activity. According to the received supplementary information, it is mentioned that SC FDFEE Electrica Dobrogea SA's activity related to the year 2004 was ended with a gross result of ROL 632,708,806 thousands, related to a turnover of ROL 6,616,382,000 thousands¹.

2.2.2. The market on which SC FDFEE Electrica Dobrogea SA acts

(11) The service's relevant market is represented by the electricity distribution and supply market, formed by two segments:

- the regulated segment;
- the competitive segment.

(12) On the regulated segment, SC FDFEE Electrica Dobrogea SA supplies and delivers electricity to the captive consumers. It is considered as captive consumer the person who, from technical, economic or regulative reasons cannot choose its supplier.

(13) The competitive segment encloses trading of electricity between the suppliers and the eligible consumers, based on:

- a) bilateral negotiated contracts closed between the electricity producers and the suppliers;
- b) bilateral negotiated contracts closed between the electricity suppliers and the eligible consumers;
- c) import and export electricity contracts;
- d) transactions through bidding on the spot market;
- e) specific services transactions.

According to the *Law no. 318/2003* the eligible electricity consumer is the one able to choose its supplier and to directly close a contract with it for the necessary energy, having access to the transport and/or distribution networks. The eligible consumers are those recognized by A.N.R.E. after fulfilling the legal conditions,

¹ The results are estimated as the auditor didn't finalized the financial statements yet.

important being the quantity of electricity used during a one year period which, at the level of 2004, must be higher than 1GW/h.

(14) The market regulator is ANRE which issues licenses, authorizations, decisions of prices and tariffs. During the development of the domestic market and/or of the integration in the international markets, ANRE has the obligation to decide the step-by-step opening, in whole or in part, of the regulated activities towards competition. Opening the electricity market is made by progressively increasing the proportion of the competitive market, according to the provisions of the energetic strategy and policy.

(15) Being in line with the EU's objectives on totally opening the market until 2007, ANRE established for each year, starting with the year 2000, a certain market opening degree, by increasing the number of eligible consumers. The market had the following evolution:

- 2000 – 15% market openness;
- 2001 – 25% market openness;
- 2002 – 33% market openness;
- 2003 – 40% market openness;
- 2004 – 50% market openness.

It is aimed that until 2007, the electricity market to be liberalized 100%, as follows:

- 2005 – 55% market openness;
- 2006 – 80% market openness;
- 2007 – 1 January – 100% - for the undertakings;
- 1 July – 100% - for population.

2.2.2.1. The regulated segment

(16) The regulated segment of the market encloses the natural monopoly activities and the distribution at regulated price, based on frame contracts. The price and tariffs systems are established by ANRE based on its own methodology elaborated for this purpose. In the same time, ANRE establishes the contracted quantities during the en-gross transactions between the producers and the suppliers.

(17) SC FDFEE Electrica Dobrogea SA, based on the obligation of public service, has to supply electricity to the captive consumers at a regulated price and based on the frame contracts.

(18) The undertaking has a number of 596,784 captive clients, structured as follows:

- houses – 551,793;
- undertakings – 44,991.

2.2.2.2. Competitive segment

(19) On the competitive market the supply prices are freely negotiable between suppliers and eligible consumers whereas the tariffs (of distribution, transport, storage), that are also part of the final price, are fixed by ANRE.

(20) Within SC FDFEE Electrica Dobrogea SA's activity area, 189 clients are licensed as eligible consumers.

2.2.2.3. *The geographical market*

(21) SC FDFEE Electrica Dobrogea SA's electricity distribution and supply activity is limited to the South-East area of Romania, area for which the company owns distribution and supply licenses issued by ANRE, namely for the counties: Constanta, Calarasi, Ialomita and Tulcea.

(22) The market share owned by SC FDFEE Electrica Dobrogea SA on the electricity distribution and supply market from Romania is of 8.81%.

(23) The main competitors of the company are the producers of electricity and the licensed electricity suppliers.

3. Description of the privatization process

(24) In view of privatizing the main state companies from the electricity distribution and supply field, in 2000, the Ministry of Economy and Trade (MEC) and the Ministry of Public Finances, upon an open auction, appointed as financial consultant a consortium led by BNP Paribas Corporate Finance.

(25) Upon the reports and recommendations of the Consultants, on 6 december 2002, the Romanian Government adopted *G.D. no. 1377/2003 approving the Strategy for privatization of the undertakings, electricity distribution and supply subsidiaries*, „Electrica Dobrogea” SA and „Electrica Banat” SA, which provided, among others:

- privatizing the ELECTRICA SA's subsidiaries with strategic investors which can prove that they have enough technical and management capabilities, namely which have the financial capacity to sustain the development of the undertaken company;
- reaching a competitive level of technical and economic performances by the undertakings, under the conditions of this sector's liberalization, on the domestic as well as on the regional market;
- offering to strategic investors 51% participation to FDFEE Electrica Dobrogea's registered capital, through a combination between MEC's direct sale of 24.6% of existing shares, the increase of registered capital, and issuance of new shares in favor of the strategic investors.

(26) Strategic investors could submit letters to express their interest either for Electrica Dobrogea SA, for Electrica Dobrogea SA, or for both of them. The selection process enclosed two stages:

1. a pre-qualifying stage, based on the letters of interest;
2. a competitive selection stage of offers consisting in:
 - submitting the preliminary or unengaged offers, followed by negotiations,
 - submitting and selecting the final offers and engagements, followed by the negotiation with the selected bidder.

(27) The privatization advertising was published in the Romanian and international printed-media (including in *Financial Times*, the international edition, on 8 January 2003). The advertising requested letters of interest from strategically investors fulfilling the following criteria:

- proper technical and operational experience (number of clients and the sold quantity of energy to be at least equal to those of Electrica Dobrogea);
- adequate power and financial resources (total value of the assets and own capitals to exceed three times those of Electrica Dobrogea, to own a long term debt rating of at least „BBB-” according to Standard&Poor's or Fitch or „Baa3” according to Moody's);
- satisfactory experience and involvement in similar transactions.

(28) After the publication of the advertising, were received three letters of interest, on the limit date of February the 28th, 2003, from the following companies: Public Power Corporation (PPC Greece), EVN AG (Austria), BKW-FMB Energie AG (Switzerland), Enel SpA (Italy), the consortium formed from GRIVCO Energy (Romania) and ABB (Sweden).

(29) After the assessment of the relevant documents submitted together with the letters of interest and Consultants' advice, all the potential investors were declared pre-qualified to continue the privatization process, excepting the consortium formed from GRIVCO Energy (Romania) and ABB (Sweden).

(30) From the pre-qualified investors only two acquired the company's presentation dossier and starting with May the 19th, 2003 had access the data chamber. ENEL SpA submitted the unengaged offer to acquire the undertaking on July the 10th, this being the only investor interested to purchase the company. [...]².

(31) In the fall of 2003 ENEL SpA continued the due dilligence process as well as the discussions on working groups. These discussions continued at the beginning of 2004.

(32) As a result of these clarifications sessions, the negotiation Commission, assisted by consultants, presented to the Italian investor in the last decade of February 2004, a package of documents generally named the Improved Contract Frame. According to the privatization strategy approved by the Romanian Government by *GD no. 1377/2002*, it would have been made available to all bidders which continued to participate at the privatization process. Based on these documents ENEL prepared the offer engaged for FDFEE Electrica Dobrogea's privatization, submitted on March the 4th, 2004. [...]³.

(33) Subsequent to this moment, the parties started the final clarification stage for the contract proposals (the share sale-purchase contract, concession, services) included in the Offer in order to end the transaction.

(34) On June the 15th, 2004 was signed a Protocol finalizing the negotiations on the transaction documents. The privatization contract of SC FDFEE Electrica Dobrogea SA closed between SC ELECTRICA SA (as Seller) and ENEL SpA (as Buyer) was signed on July the 19th, 2004 and was approved by GD no. 1000/2004.

(35) Under the condition of fulfilling all the criteria for pre-finalizing and finalizing, ENEL SpA shall receive, from the date of the finalization, a number of shares representing 51% form FDFEE Electrica Dobrogea's registered capital. This will be accomplished by buying a number of shares representing approx. 24.6% from the registered capital of FDFEE Electrica Dobrogea from SC ELECTRICA

² Confidential data.

³ Confidential data.

SA and by subscription of a supplementary number of shares within a majority of the social capital of FDFEE Electrica Dobrogea.

(36) The bidding process was a competitive one, opened to all participants in the electricity distribution and supply field, transparent and unconditional. All the potential investors were declared pre-qualified, excepting the consortium established from GRIVCO Energy (Romania) and ABB (Suedia). Between them, two acquired the company's presentation dossier, ENEL SpA being the only investor submitting the unengaged offer for acquiring the company. The investor benefited by enough time (between March and July 2004) and information (access in the data chamber physically organized, the possibility to meet the company's management and to make visits at the company's headquarters), to make a proper assessment of Electrica Dobrogea as base of the offer.

(37) Based on the above, the Competition Council concludes that the privatization of SC FDFEE Electrica Dobrogea SA was made under an open bidding procedure, non-discriminatory, transparent and unconditional. This procedure ensured, pursuant to the principles of the market economy, a competitive price which reflect the correct market value of FDFEE Electrica Dobrogea, since all the factors which may have influence over the value of the company were discussed during negotiations and were finally reflected in the price offered by ENEL SpA.

4. Financial facilities provided for in the Privatization Contract

1. Measures of financial support provided by GEO no. 37/2004;
2. Measures of financial support provided by the Law no. 570/2004;
3. Not covering by the company of losses incurred after the conversion of debts into shares

4.1. Measures of financial support provided by GEO no. 37/2004

(38) Through GEO no. 37/2004, the Romanian Government wanted to create a mechanism through which arrears in the economy may be reduced and the degree of attractiveness of companies at issue may be increase for the strategic investors. The relevant provisions in GEO no. 37/2004 are Art. 1, Art. 5 and Art. 6.

a) *Provisions of Art. 6 of GEO no. 37/2004*

(39) According to *art. 6(2)* of the Ordinance, the unpaid claims of SC FDFEE Electrica Banat SA and of SC FDFEE Electrica Dobrogea SA, within the limit of ROL 1,977 bill., are taken over by the Protocol in order to be recovered by the Authority for State's Assets Capitalization (AVAS), in 30 days from the coming into force of the emergency ordinance.

(40) [...] ⁴.

(41) [...] ⁵.

(42) SC Electrica SA cannot use those sums but for reducing its own debts unpaid to the electricity producers Termoelectrica SA and SN Nuclearelectrica SA.

(43) [...] ⁶.

(44) According to *art. 6(5)*, the interests, delay majorities and penalties of any kind, owed by the electricity consumers to SC FDFEE Electrica Banat SA and SC FDFEE Electrica Dobrogea SA, whose claims were taken over by AVAS, are being annulled.

(45) [...] ⁷.

b) Provisions of article 1 of the GEO no. 37/2004

(46) According to *art. 1(4)*, the legal entities - electricity consumers who pay the whole value of the bills standing for current and arrear obligations for electricity consumption by June the 30th, 2004, shall benefit from write-off of majorities and penalties for late payments.

(47) [...] ⁸.

c) Provisions of article 5 of the GEO no. 37/2004

(48) According to *art. 5(1)*, the undertakings in the mining field benefit from deferral, for a future exemption from the payment, of the commercial debts towards SC ELECTRICA SA, as well as towards its subsidiaries, representing the

⁴ Confidential data.

⁵ Confidential data.

⁶ Confidential data.

⁷ Confidential data.

⁸ Confidential data.

value of the bills, including tariff majorities, related to the closed mines and pits, owed until December the 31st, 2003.

(49) [...]⁹.

(50) Art. 5(5) provisions that in the limit of the exempted sums mentioned at point (50) the obligations of SC ELECTRICA SA and its subsidiaries towards SC Termoelectrica SA, including the delay majorities and penalties, to be paid until December the 31st, 2003 are exempted from the payment.

(51) [...]¹⁰.

4.2. Financial support measures provisioned by the Law no. 570/2004

(52) *The Law no. 570/2004 on certain measures for privatizing the undertakings, electricity distribution and supply subsidiaries, "Electrica Dobrogea" - S.A and "Electrica Banat" - S.A., as well as certain measures for regulating the activities of the undertakings acting in the electricity distribution field* establishes the legal framework for the end of privatization and for the accomplishment of certain conditions for transferring the ownership right on the shares representing 51% from the equity of each undertaking which is electricity distribution and supply subsidiary. The relevant provisions in the Law no. 570/2004 are those of art. 6, art.10, art.11, art.12.

a) Provisions of art. 6 in the Law no. 570/2004

(53) According to this article, the Ministry of Economy and Trade guarantees the fulfillment, by SC ELECTRICA SA (the Seller), of the obligations to indemnify the possible prejudices bared by ENEL SpA (the Buyer), and owed due to the breach of the seller's declarations and guarantees, included in the privatization contract, within the limit of 50% from the price paid by ENEL SpA for the shares object of the sale.

(54) ENEL may submit its indemnity claim to SC ELECTRICA SA and MEC within a 36 months period from the date when the transfer of the ownership right on the shares took place. If ENEL SpA doesn't recover the prejudice from SC ELECTRICA SA, it shall report to ELECTRICA as well as to MEC the amount of the uncovered prejudice.

⁹ Confidential data.

¹⁰ Confidential data.

(55) In 30 days from the date when the notification is received, MEC shall make all the efforts necessary to see that the obligation is fulfilled by ELECTRICA. If SC ELECTRICA SA doesn't pay the whole sum, MEC shall pay for the company this obligation towards ENEL, in a special account opened for this purpose by SC Electrica SA.

(56) If SC ELECTRICA SA cannot pay due to the reorganizing liquidation, bankruptcy or blockage of its accounts, MEC shall fulfill the guarantee obligation by paying it directly into the account of ENEL SpA.

(57) For diminishing ELECTRICA's unpaid risk the Romanian State, through MEC, imposes to it, according to art. 8 in *the Law no. 570/2004*, to establish a deposit with an amount equal to the guarantee ceiling, in order to cover the sources necessary to fulfill the obligations to pay the indemnity for the prejudices incurred to ENEL SpA.

b) Provisions of art. 10 in the Law no. 570/2004

(58) According to art. 10, due to the annulment of the payment obligations of SC ELECTRICA SA towards the Risk Fund for internal and external loans guaranteed by the State, SC ELECTRICA SA annuls the payment obligations of SC FDFEE Electrica Banat SA and of SC FDFEE Electrica Dobrogea.

(59) [...] ¹¹.

c) Provisions of art. 11 in the Law no. 570/2004

(60) According to this article the interests, delay majorities and penalties owed for the delay of the payment towards the electricity and transport services' suppliers are exempted, having the value of the electricity acquired by SC ELECTRICA SA in the name of SC FDFEE Electrica Banat and SC FDFEE Electrica Dobrogea, as well as by them in their own name until the date when the shares ownership right was transferred to ENEL SpA. In the same way, are annulled the interests, delay majorities and penalties owed due to the delay in the payment of the quantities of electricity supplied by SC ELECTRICA SA to the undertakings which are electricity distribution and supply subsidiaries Electrica Banat SA and Electrica Dobrogea SA.

¹¹ Confidential data.

(61) [...] ¹².

d) Provisions of art. 12 in the Law no. 570/2004

(62) According to this article, the Ministry of Public Finances and the Ministry of Economy and Trade are entrusted to negotiate with the International Bank for Reconstruction and Development the granting of a partly risk guarantee (PRG) to guarantee, in name and in the Romanian State's account, for a 5 year period from the date when the ownership right was transferred, until the limit of [...] ¹³, as well as the interests and other related costs. The ceiling of [...] ¹⁴ is not individualized for each of the two subsidiaries, respectively SC FDFEE Electrica Banat SA and SC FDFEE Electrica Dobrogea SA.

(63) The partial risk guarantee covers the regulating risk specific to the companies involved in the electric energy distribution sector (the risks incurred by the modification, abolition of the regulating frame, the lack of application or incorrect application of the regulations regarding the electricity delivery adopted by ANRE). and had as purpose the reduction of the non-implementing risk regarding the regulations setting the distribution tariff.

4.3 Not covering by the company of losses incurred after the conversion of debts into shares

(64) [...] ¹⁵.

(65) The Privatisation contract provides that any loss bared by the company due to the conversion of the debts into shares already sold or due to the conversion, in process, of the debts into shares will not be borne by itself in the end.

(66) The difference between the nominal value of the shares after the conversion and the value resulted from their selling shall be covered by the Ministry of Public Finance and paid to the company.

5. Analysis of the financial measures provided by the Privatization Contract of SC FDFEE Electrica Dobrogea SA and their state aid character

¹² Confidential data.

¹³ Confidential data.

¹⁴ Confidential data.

¹⁵ Confidential data.

5.1 The analysis of the financial support measures from which SC FDFEE Electrica Dobrogea SA benefits

(67) These facilities have been granted to FDFEE Electrica Dobrogea and may fall within the scope of Law no.143/1999 on the State aid, as these constitute selective State financial support measure which may have the potential to distort the normal competitive environment by giving an economic advantage to the company thereby affecting trade between Romania and the Member States of the EU.

(68) However, in this context one needs to note that these facilities are being provided to FDFEE Electrica Dobrogea within the context of its privatization, after which the Romanian State will continue to maintain a significant share in the company. Therefore, in as far as the behavior of the State within the privatization can be compared to that of any other market operator of a comparable dimension, the facilities may be free of aid.

(69) In order to establish whether the grant of the facilities within the privatization involves elements of State aid it needs to be assessed whether a private investor/vendor in similar circumstances would have done the same. Therefore, it needs to be examined, considering all options at the disposal of the State, whether the granting of the facilities represented the economically most advantageous option for the State.

5.1.1. Financial support measures granted based on EGO no. 37/2004

(70) The measures provided by GEO no. 37/2004 aim to reduce the budgetary arrears in the economy and to increase the attractiveness at privatization of the companies in the field of utilities. In the case of FDFEE Electrica Dobrogea, these measures aim the maximization of the price that would be received by the Romanian State after the sale of the controlling interest, thus the state acts such as a private investor in a market economy.

a) Art. 6(2) in EGO no.37/2004

(71) The taking over by AVAS of SC FDFEE Electrica Dobrogea SA's commercial outstanding claims for recovering them may fall under the incidence of the Law no. 143/1999 on the State aid, as it is a selective support measure, giving

an advantage to SC FDFEE Electrica Dobrogea SA, and therefore being possible to distort the competition and the trade with the Member States.

(72) The non-payment in due time of debts by Electrica Dobrogea's clients resulted in majorities and penalties related to the debts to its own suppliers of electricity. [...] ¹⁶.

(73) When the bidding offers for the acquisition of the company were made, there was a certain uncertainty regarding the degree of FDFEE Electrica Dobrogea chances to recover the debts, existing the risk that this uncertainty degree to be highly over-assessed by the investors, which from prudence reasons could be tempted to take exaggerated protection measures when elaborating the price offers, this way disadvantaging the Romanian State.

(74) If the State would have not ordered the taking over of FDFEE Electrica Dobrogea's claims by AVAS, it is possible that ENEL SpA might deduce these sums from the offered price supposing that it does not recover them.

(75) Regarding the above mentioned facts, the Competition Council considers that the Romanian State acted like a prudent private investor, interested in maximizing the benefits obtained from the company's sale.

b) Art. 5(5) in EGO no. 37/2004

(76) [...] ¹⁷.

(77) Any existing obligations would have had as result the proper deduction of this sum when the company was assessed and therefore, the decrease of the price offered by the bidders. So it can be said that the majorities and penalties owed by FDFEE Electrica Dobrogea to its suppliers were paid by ENEL SpA as a part of the price paid during the privatization process and that the loss of SC ELECTRICA SA as Seller due to the non-payment by the company of these obligations was recovered through the increase related to the immediate proceeds - the price paid by the investor- and also by the investment foreseen to be carried forward in the company with the perspective of a sustainable public services operator.

(78) ENEL SpA, knowing the level of the exemption, took the facility into account, the buying offer reflecting the advantage offered to SC FDFEE Electrica Dobrogea

¹⁶ Confidential data.

¹⁷ Confidential data.

SA. The Competition Council considers that the State acted according to the prudent private investor's principle, trying to privatize an undertaking free of any unpaid obligations in order to maximize the price it could have received from the transaction.

5.1.2. Financial support measures granted based on the Law no. 570/2004

a) Art. 6 in the Law no. 570/2004

(79) The Ministry of Economy and Trade guarantees the fulfillment by SC ELECTRICA SA of the obligations to indemnify the possible prejudices based by ENEL SpA, in the limit of 50% from the price paid by ENEL SpA for the shares subject of the sale.

(80) This is not about a guarantee in the classical sense of the term. It is about a mechanism by which the Buyer is protecting itself from eventual prejudices suffered following the breach of the Seller's statements and warranties, often met in commercial transactions. In the case of the privatization agreement of SC Electrica Dobrogea SA, the Seller declares and warrants for the Buyer: the legal status of the company, the debts taken over by the company when it was established, financial statements, certificates certifying ownership over land, goods held by the company as well as other aspects.

(81) This guarantee is limited to an amount of 50% from the price of the shares subject to the sale. Also it is limited in time, respectively 3 years from concluding the privatization agreement and it is linked to past events (statements and warranties made by Electrica).

(82) The mechanism of the guarantee is actually protecting the Romanian State from incurring any loss, as Electrica is obliged by the Law 570/2004 to block the corresponding total amount under this guarantee in a bank account at the disposal of MEC. This amount can immediately be triggered in case of any claim from the buyer. In these conditions, the Competition Council considers the risk of default for the guarantee to be very low. [...] ¹⁸.

(83) In addition, although the guarantee only appeared in a later phase of the procedure when only ENEL was still interested in buying the company, the same would have been granted to any other bidder which would have stayed in the

¹⁸ Confidential data.

process (in accordance with the privatization strategy approved by the Romanian Government by GD no. 1377/2002). In that sense, one could argue that it is a general measure, available to all bidders.

(84) If there was no guarantee mechanism, the buyer would have introduced supplementary risk elements which would have led to a significant reduction of the price. Therefore, the Romanian State acted as a private prudent investor, using the the guarantee mechanism in order to obtain a price as high as possible when selling the company. Moreover, the mechanism of this guarantee is designed in such a way that the Romanian State exposure under the guarantee is considerably low, as the amounts are deposited at its disposal and the actual non-payment risk from Electrica SA is reduced as there are no precedents of such non-payment.

b) Art. 10 of the Law no. 570/2004

(85) [...] ¹⁹.

(86) The amount of these facilities was known by the investor since the beginning, so one could say that those exemption from the payment of the obligations to SC Electrica SA were paid by ENEL SpA as part of the price offered during the privatization process and that the „loss” of the seller due to the non-payment of these obligations by the company was recovered through the increase of the immediate incomes – the price paid by the investor. Therefore, the State acted according to the private prudent investor principle.

c) Art. 11 of the Law no. 570/2004

(87) [...] ²⁰.

(88) These amounts appeared because of the fact that in time, Electrica has been used as one of the channels for unblocking the financial block-out in the Romanian economy. In this sense, in the history of the Electrica companies, there have been issued by the Romanian State different normative acts, forcing Electrica to cancel penalties to customers. In addition, through legislation also, Electrica Dobrogea was bound to convert into shares its receivables towards a part of its clients (state owned companies), at face value, the majorities and penalties related to these receivables being exempted.

¹⁹ Confidential data.

²⁰ Confidential data.

(89) On the other hand, though, due to the fact that Electrica was not exempted at its turn from payment of majorities and delay penalties owed to the electricity producers, these accessories have kept growing. In this way, a certain imbalance was created between the upstream penalties and downstream penalties.

(90) [...] ²¹.

(91) [...] ²².

(92) Mention should be made that the company was established in 2002, being spun off from SC Electrica SA and in this way the liabilities have been inherited pro-rata from SC Electrica SA, which at its turn inherited these liabilities when CONEL (former national electricity company) has been restructured. By including all these penalty obligations in the electricity tariff, it would lead to an explosion of the tariff.

(93) [...] ²³.

c) Art. 12 in the Law no. 570/2004

(94) The Romanian State granted a partly risk guarantee (PRG) for a 5 year period starting with the date when the ownership right was transferred, till the ceiling of [...] ²⁴, as well as the interests and other costs related to the risks incurred by the modification, abolishing of the regulation frame, the lack of application, or incorrect application of the regulations adopted by ANRE referring to electricity distribution. This way, the Ministry of Public Finance shall retain in a distinct account, for a period of 5 years, the equivalent of the sum of [...] ²⁵ for both electricity distribution subsidiaries (SC Electrica Banat SA and SC Electrica Dobrogea SA).

(95) The PRG mechanism is covering the regulatory risk created by ANRE not respecting the existing issued regulations, changing such regulations or through its abusive application of such regulations, referring to the distribution tariffs methodology and to the principle of pass-through from the supply methodology.

²¹ Confidential data.

²² Confidential data.

²³ Confidential data.

²⁴ Confidential data.

²⁵ Confidential data.

(96) The PRG mechanism must be analyzed taking into account that SC Electrica Dobrogea SA is active in sector regulated by ANRE. The market regulator (ANRE) has the mission to create and apply the regulatory system, required for the operation of the sector and electric and heating market in terms of efficiency, competition, transparency and consumer protection. In these circumstances, the company's activity is under permanent control and scrutiny from ANRE.

(97) Using this type of bank guarantee promoted by the World Bank, related to the regulation specific risk for the energy distribution companies is a guarantee mechanism aiming to reduce the risk of non-implementing the regulations establishing the distribution tariff. The lack of such guarantee is seen by the investor as a supplementary risk, therefore requesting a higher weighted average cost of capital (WACC), having as result an increase in the distribution tariffs for consumers.

(98) The mechanism consisting in the issue of a guarantee by a commercial bank, with the Romanian Government and the World Bank's counter guarantee, was proposed to the investor ENEL as it have taken into account in its offer a relatively high regulation risk, leading to the increase of the index named the Weighted Average Cost of Capital (WACC) real, pretax, to a level over 14% (for the first three years regulating period), respectively 12% (for the following 5 years regulating period). This was a consequence of the fact that besides the price paid for acquiring the shares, ENEL SpA has set as its target in the Business Plan attached to the Privatization Agreement of SC Electrica Dobrogea SA, to make an investment program amounting approximately [...] ²⁶ during 2005-2009. Following this important financial effort ENEL SpA wishes, as any other private investor, a higher weighted average cost of capital (WACC) as possible. But, the acceptance by the state of a higher WACC means its recovery through tariff, by its increase, with a significant social impact and to the detriment of the general economic development.

(99) In order to keep the company value offered by ENEL, but to decrease the lever of WACC to reasonable values (12%, respectively 10%) it was necessary to partly eliminate the regulation risk assumed by ENEL, by offering a Partially Risk Guarantee (PRG). By introducing this mechanism, the initial sum representing the increase of tariffs for the next 8 years, was reduced by approx. 10 times, the sum being estimated at approx. Eur 50 million for FDFEE Electrica Banat and FDFEE Electrica Dobrogea. This without taking into account the effect on national level

²⁶ Confidential data.

too, as the above mentioned recovery index is a sector index, applicable for all the electricity distribution and supply companies.

(100) The Ministry of Economy and Commerce emphasize that the PRG mechanism is a solution more advantageous than reflecting the WACC 2% increase in the tariffs for the consumers. The differential amount would have been cashed by the investor as sure sums to cover the risk of certain subsequent potential modifications referring to the regulated tariffs. So, it was chosen to maintain lower regulated tariffs for the consumers in exchange of a partial risk guarantee, the Romanian State being able to avoid the granting of the compensation by a coherent behaviour of ANRE, and in this way the risk of default it is assumed as very low.

(101) More than that, by issuing such guarantee, the Romanian State shows its commitment and credibility in respecting a certain path towards a modern regulatory system, similar with those existing in the EU member states. Considering the low risk of default and also by simulating through the financial model the decrease in value – assuming the same level of investment in the next 5 years – it can be seen that the approx. EUR 50 million gained in the enterprise value at this moment is comparable with the net present value coming from the EUR 60 million covered by the PRG but distributed over the 5 years. Even so, the low risk of default is giving a high discount to the PRG amount. [...] ²⁷.

(102) Such guarantee is actually securing a certain revenue stream for the operator and in such way the future investments committed by Enel in its business plan, attached to the Privatization Agreement, are secured as well. Also, a guarantee of this type can be offered in a commercial transaction, but for Electrica as seller of FDFEE Electrica Dobrogea, the legal restrictions stop it to engage itself in guarantees higher than 50% from the price paid by the investor for the sold existing shares. Therefore, it cannot be claimed that this would be an advantage that ENEL couldn't obtain under normal circumstances.

(103) As there are contemplated regulations issued by a Romanian authority, and also the State has issued such PRG mechanism, the Competition Council considers the risk of default for the guarantee to be very low. [...] ²⁸.

(104) Once granted the partly risk guarantee, it implicitly represents a guarantee for the investors subsequently participating to the privatization process of the

²⁷ Confidential data.

²⁸ Confidential data.

undertakings in the electricity distribution and supply field. In such a way the positive effect for the Romanian State is multiplied in the further privatization transactions.

5.1.3. Not covering by the company of losses incurred after the conversion of debts into shares

(105) As mentioned at point (64) FDFEE Electrica Dobrogea was forced on legal way to convert its claims, owed by several debtors - State owned companies- to nominal value. These shares were transferred towards AVAS, which has to repay to FDFEE Electrica Dobrogea the price received from the sale of these shares, the difference to the nominal value following to be given to the company by MPF.

(106) [...] ²⁹.

(107) [...] ³⁰.

5.2. The analysis of the financial support measures granted by SC FDFEE ELECTRICA DOBROGEA SA to its clients

(108) The facilities granted by FDFEE Electrica Dobrogea in the basis of art. 1(4), art. 5(1) and art. 6(5) in the EGO no. 37/2004 mentioned at points (47), (49) and (45) of the present decision, can fall under the incidence of the Law no. 143/1999 on the State aid, as they have selective character, giving an advantage to SC FDFEE Electrica Dobrogea SA's clients an being possible to distort the competition and the Trade with the Member States.

(109) These facilities' state aid character and their compatibility with the normal competitive environment shall be object of a subsequent analysis of the Competition Council.

6. Conclusions

(110) The Competition Council notes that the privatization procedure insured, according to the market economy principles, the obtaining of competitive price reflecting the correct market value of FDFEE Electrica Dobrogea, as all the factors influencing its value were discussed during the privatization process and reflected

²⁹ Confidential data.

³⁰ Confidential data.

in ENEL's final offer. The buyer benefited of enough time and complete information to make a proper assessment as base for its offer.

(111) Synthetically, it can be considered that the measures provisioned in the privatization contract are of two types:

- (i) measures for the annulment of certain obligations of the undertakings, precisely quantified (i.e. amount of debts and penalties annulled),
- (ii) measures by which the State meant to clarify the situation that risk to be overrated by the investors in an unfavorable manner for the state, that would lead to a considerable decrease of the price offered, such as: buyer's actions that could bring damages to the seller; risks incurred by the modification, abolishment of the regulating framework; not applying or incorrectly applying the ANRE regulations; taking over of claims by AVAS; not covering by the company of losses incurred after the conversion of debts into shares).

(112) [...] ³¹

(113) [...] ³².

(114) In the supplementary information received from the Ministry of Economy and Commerce it is specified that in the Privatization Contract is enclosed a clause according to which the acquisition price shall be adjusted according to the modifications incurred in the net financial position of SC Electrica Dobrogea SA, in comparison to the reference value from the date when the privatization contract was signed. This value adjusting the price represents 51% from the difference between the net financial positions at the date when the transaction was finalised and respectively on 31.12.2004. [...] ³³.

(115) [...] ³⁴.

(116) [...] ³⁵.

(117) The solutions presented were considered to be the best ones in order to maximize the net incomes from the privatization paid to the state. During the

³¹ Confidential data.

³² Confidential data.

³³ Confidential data.

³⁴ Confidential data.

³⁵ Confidential data.

privatization the State, through Electrica S.A. aimed not only to maximize the selling price but also to attract a well known investor as well as to protect the population from significant increases in the future of electricity tariffs. Therefore, the State behaved as a private investor would behave in similar conditions.

(118) In conclusion, the Competition Council considers that the facilities granted to SC FDFEE Electrica Dobrogea are not state aid as they are part of the package offered to any potential investor within a transparent and open bidding procedure after which the real market value was established. Therefore, acting this way, the State fulfilled the private investor's principle, obtaining a price higher than it was expected from a company's privatization, with real development perspectives in future, in which the State will still own 49% of the registered capital.

DECIDES

Art. 1. Based on art. 12(2) letter a) in the Law no. 143/1999 on State aid, with the subsequent modifications and completions, it is found that the support measures notified by the Ministry of Economy and Trade enclosed by the privatization contract of SC FDFEE ELECTRICA DOBROGEA SA, consisting in annulment of interests, delay majorities and penalties deed to its suppliers and to SC Electrica SA, exemption of the obligation owed to Electrica, taking over the outstanding claims by AVAS, not covering by the company of losses incurred after the conversion of debts into shares, the PRG mechanism, the guarantee within the limit of 50% from the price paid for the shares object of the sale, do not constitute state aid in the sense of art. 2 of Law 143/1999 on State aid, with the subsequent amendments and completions.

Art. 2. The present Decision is applicable upon its communication.

Art. 3. According to provisions of art. 29 of Law 143/1999 on state aid, with subsequent modifications and completions, the present decision may be appealed by the interested persons before the Bucharest Court of Appeal, administrative section, within 30 days from its communication.

Art. 4. The present decision will be communicated by the General Secretariat within the Competition Council to:

- The Ministry of Economy and Trade, Calea Victoriei nr.152, sector 1, Bucharest;

- S.C. FDFEE ELECTRICA DOBROGEA S.A., Str. N. Iorga nr. 89, Constanta, Constanta County.

Art. 5. The General Secretariat and the Directorate for Authorization of State Aid within the Competition Council shall pursue the fulfillment of the present decision.

PRESIDENT

MIHAI BERINDE