



Energy

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Romania

Laurentiu Pachiu, Delia Vasiliu & Radu Dudău
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Overview of the current energy mix, and the place in the market of different energy sources

Romania is the largest oil and gas producer in Central and Eastern Europe, but a net importer on both counts. According to BP's Statistical Review of World Energy (2016), Romania's proved reserves at the end of 2015 were 100 million tons of oil (with a reserve to production ratio of 19.5) and 100 billion cubic metres (bcm) of gas (with a reserve to production ratio of 10.4).

While domestic gas production covered in excess of 95% (97.61%¹) of total consumption in 2015, domestic oil production only covered around 40% of the consumption demand in 2015. Therefore, although the country has the EU's third-lowest dependence on energy imports (without new oil and gas sources), this dependence is expected to exceed 50% in 10 years' time. However, these prospects could be significantly improved by the newly discovered Black Sea gas deposits. The largest gas deposit discovered in the Black Sea is the Domino-1 field which could hold up to 84 billion cubic metres of natural gas. Therefore, Romania's natural gas reserves could see a twofold or threefold increase as a result of the development of Black Sea gas fields. As a result, the natural gas transmission system operator is developing a pipeline which will feed the natural gas extracted from the Black Sea in the BRUA (Bulgaria Romania Hungary Austria) interconnector.

Oil production amounted to four million tons in 2015 and total consumption was 9.1 million tons.²

Romania produces 84,000 barrels of oil per day, while the average consumption of oil is 191,000 barrels per day.³ While Romania is an experienced oil producer, production per well is among Europe's lowest, because Romanian oil and gas fields are highly mature and fragmented after more than a century of exploitation.

The refining stock is old and in need of investment, five refineries being decommissioned in the last four years, with refining capacity decreasing from 500,000 barrels per day to 246,000 barrels per day.

Romania produced 10.3 bcm of natural gas in 2015 and consumed 10.3bcm. Domestic gas demand has been declining for most of the last 20 years, with a noticeable increase in 2011 and 2012, due to governmental support for domestic fertiliser producers. The declining gas consumption can be attributed to the decommissioning of numerous industrial facilities. Households are the primary natural gas consumers and account for around 25% of the total consumption of natural gas in Romania.⁴ The two dominant gas producers are state-owned Romgaz (48.51%) and OMV Petrom (47.3%). There are also independent producers, such as Amromco Energy (3.3%) and Stratum Energy (1.86%).

The main sources of electricity generation in Romania (approximate percentages valid for 2015⁵) are as follows: Coal 27.63%; Hydro 27.15%; Nuclear 18.27%; Gas 14.34%; and Renewable sources (other than Hydro) 12.51%.

Although numerous E-RES facilities have been commissioned in the last five to seven years, only 12.51% of the total electricity generated and dispatched into the grid in 2015 was produced by E-RES facilities other than hydropower. CEZ owns the biggest wind farm in Romania, the Fântânele-Cogealac wind park, with a capacity of 600 MW.

The main electricity generation companies are state-owned, represented by Nuclearelectrica, the operator of the only nuclear power plant in Romania, having a capacity of 1,400 MW, Hydroelectrica's system of hydropower plants, and around 20 thermal coal-fuelled power plants, all these together generating around 70% of the country's total electricity production.

Changes in the energy situation in the last 12 months which are likely to have an impact on future direction or policy

In the nuclear sector, the government has advanced in negotiations with a Chinese investor for the development of a further two nuclear reactors (reactors 3 and 4) at Romania's only nuclear power plant in Cernavoda, based on a support scheme that is quite similar to the one at Britain's Hinkley Point. The finalisation of such kind of investment may essentially change the entire energy environment in Romania.

Chinese investors have also been selected by the government for the development of a 600 MW coal-fired power plant using supercritical technology at Rovinari, in one of the two major coal basins in Romania. Such a project has the potential to bring a breath of fresh air to a dying state-supported coal industry.

The recent investigation launched by the European Commission (EC) into the Romanian gas market may also be considered an important event. According to the statement of the EC of 7 June 2016, the investigation started against the state-owned natural gas producer Romgaz; the Romanian gas TSO, Transgaz; and Romania's largest oil & gas company, OMV Petrom, into alleged anti-competitive conduct and abuse of dominant position, particularly with regard to practices designed to stall the export of Romanian natural gas to the EU market.

The gas network operators of Bulgaria and Romania signed a contract on 6 April 2016 with Austrian construction firm Habau PPS Pipeline Systems to complete the Romanian-Bulgarian (Giurgiu-Ruse) gas interconnector linking the two countries. The two countries planned to have the 25-km pipeline operational in 2013, but it has been delayed due to technical problems experienced in laying pipes under the Danube River. The pipeline should be operational by the end of 2016 at the latest and will have a maximum capacity of 1.5 bcm of gas/year from Bulgaria to Romania. The capacity from Romania to Bulgaria will be of 500 mcm/year. Bulgaria has also launched the construction of a gas pipeline to Greece, which will carry Azeri gas to Romania and Hungary.

The National Uranium Company (CNU), in charge of Romania's uranium mining activity, decided to temporarily close down the last remaining functional uranium mine in Romania (i.e. the Crucea-Botușana mine, located in the north-east region, Suceava County). Until 2011, between 55% and 75% of CNU's uranium mining and processing activity was subsidised by the state. Though subsidies stopped after 2011, CNU then tried to recover some of the losses from its sole customer, Nuclearelectrica, by increasing the price for processed uranium (UO₂) by around 75%. In effect, Nuclearelectrica contracted a foreign supplier for the fuel, which left CNU in a critical situation. Under new management appointed in 2016, CNU is currently trying to identify solutions to this situation.

Developments in government policy/strategy/approach

The government, through the Minister of Energy, has engaged in the drafting of a long-term National Energy Strategy which is supposed to be released in September 2016.

The government has also repeatedly expressed its desire to re-visit the taxation of upstream operations. Although this debate has lasted almost three years, no draft law has yet been officially disclosed. According to industry sources, the government's intention is to keep royalties at existing levels, but to add a supplementary profit tax of 35%, on top of the regular corporate profit tax of 16%. Operators would thus be levied 51% in taxes plus royalties in a range of 3–13.5%. Industry associations are strongly against such tax policy which they argue is against stabilisation and predictability pledges of the government.

In the electricity sector, the Ministry of Energy has launched public consultations on amendment proposals to several laws and regulations in the energy sector (e.g. Government Decision (GD) 1215/2009 relating to the bonus scheme for high-efficiency cogeneration, the electricity and natural gas Law 123/2012, or to the renewable energy support scheme provided under Law 220/2008) aimed at encouraging new investments and solving important issues of the industry.

Romania further needs to present its national framework plan on implementing the Alternative Fuels Directive 2014/94/UE, aimed at developing the market for alternative fuels by mid-November 2016. The transposition of the said directive is expected to contribute to emissions-reduction from transportation, with a significant impact on major sectors of the Romanian economy, including the energy sector.

Developments in legislation or regulation

In mid-2016, Romania implemented the EU Public Contracts Directives, including Directive 2014/25/EU, as well as EU Directive 2013/30/EU on the safety of offshore oil and gas operations, both with particular relevance for the energy industry.

In the oil and gas sector, it is worth mentioning that the natural gas liberalisation schedule has been suspended. The Romanian Government has decided to freeze the regulated price of natural gas starting 1 July 2016 until 31 March 2017. The regulated prices, to be paid by households, district heating plants (CETs), and gas-fuelled cogeneration units for domestically produced natural gas, will stay at Lei 60/MWh for this period. This comes in a context where, in 2012, following negotiations with the IMF and the EC, the Romanian Government approved a price deregulation calendar for domestically produced gas consumed by household customers, which was supposed to reach market level as of 1 October 2018. The calendar was thereafter extended until mid-2021 by Government Decision (GD) 488/2015. However, keeping up with that calendar would have meant increasing gas prices by 10% as of 1 July 2016, to Lei 66/MWh. Hence, the regulated gas price would have already become higher than the day-ahead market price, currently at Lei 63/MWh. The final price to be paid by consumers, however, will still be influenced by several other factors, such as the amount and price of imported gas, transmission tariffs, etc. Furthermore, as of 9 February 2016, the National Agency for Mineral Resources (ANRM) increased the domestic oil transport service tariff charged by state-owned oil transport system operator Conpet, by 1.4% to Lei 79.75/ton (before VAT). The decision was contested by the Romanian Association of Petroleum Exploration and Production Companies (ROPEPCA), which claimed that the tariff increase would negatively impact the petroleum industry and the country's overall economy.

The Romanian Energy Regulatory Authority (ANRE) has set new energy tariffs starting 1 July 2016, with a drop in transmission and system service fees, as well as a cogeneration tax reduction. Transmission fees charged by TSO Transelectrica went down by 10.8% to Lei 18.7/MWh, while the system service fee dropped by 6.3% to Lei 12.88/MWh. The decrease of transmission fees has a very low impact on electricity bills, since it represents merely a small fraction of electricity's final price. However, considering all the fee reductions, households' energy prices are expected to drop by 2%.

Judicial decisions, court judgments, results of public inquiries

Romania's largest O&G company, OMV Petrom, lost the case against Romania's Competition Council in which it challenged the highest fine ever issued by the said authority in Romania. However, the court reduced the fine against OMV Petrom from €82m to €66.5m, which means that the state will have to pay back some €15.5m to the company because the fine was enforced immediately after it was issued, at the end of 2011. Although the court reduced the amount, this remains the biggest sanction ever ruled by the Competition Council.

Lukoil Romania, part of Russian group Lukoil, also lost the case against the Competition Council on 22 April 2016. Lukoil's fine was reduced too, from almost €31m to €25m. In 2011, the competition authority sanctioned six oil companies with fines totalling €196m for making a deal to simultaneously withdraw a gasoline type from the market. The other four sanctioned companies were OMV Petrom Marketing, Mol Romania, Rompetrol Downstream and Eni Romania. All the companies challenged the sanctions, but lost. However, they had their fines reduced by a total of €37m, to €159m.

Romania's largest (and state-owned) electricity producer Hidroelectrica has won two separate court cases against energy traders Energy Holding and EFT AG, which were asking the company for a total of Lei 102m (around €22m) in damages. Their plight was a drop in supplied electricity in late 2011 and early 2012, over which Hidroelectrica invoked *force majeure*. The producer still has four similar cases pending. When entering insolvency in 2012, Hidroelectrica terminated several preferential contracts with energy traders who had managed to conclude long-term bilateral contracts with the state-owned power producer at very low prices. The traders would later resell the electricity at much higher prices.

As part of Hidroelectrica's plan to redeem its finances and get listed on the stock market once it comes out of insolvency, the company's judicial administrator announced that it will sue the Romanian state at the European Court of Justice for the annulment of a water tax that is costing the hydro-power producer €80–100m per year.

The Romanian state lost an ICC Paris arbitration case against the Italian energy group Enel, in which it claimed compensation of approx. €1bn for failing to comply with the privatisation contract of Electrica Muntenia Sud.

Major events or developments

As an important development, it is worth noting that 2015 was Romania's greenest year to date. According to data published by TSO Transelectrica, Romania produced 8.1 TWh of electricity from renewable energy sources (RES) in 2015, 3% above the previous year. RES thus accounted for 16% of the 51.74 TWh used in 2015. According to the Energy Ministry, Romania has met its objective as to share of total renewable energy – of 24% for 2018 – as today, Romania has already reached 27%. On 10 March 2016, wind-produced electricity amounted to its highest level in Romanian history, reaching 2,700 MWh. Wind

gained the highest share of the electricity mix that day, at 33%, followed by hydro-power, nuclear and coal. Although the country is getting a growing amount of electricity from renewable sources, the producers are currently dealing with a series of financial issues. Initially, the country had put in place a support scheme which generated almost €8bn worth of investments in the renewable sector. In the meantime, the incentives were curtailed, so investors are struggling to generate revenues. Projects are allotted a number of green certificates depending on the technology. Associations in the industry say that some projects risk going into insolvency or bankruptcy.

On 21 June 2016, the Bucharest Tribunal decided that the state-owned power producer Hidroelectrica can exit insolvency (after four years of insolvency). The decision is not final, but it is enforceable. Since 2012, Hidroelectrica faced two insolvency procedures. It first became insolvent in 2012, after losing \$1.4 bn over six years from unfavourable contracts under which it sold its electricity output below market prices. It thereafter underwent restructuring, cancelled the contracts and posted record high profits. In 2014, a court ruling over litigation with some of its former clients pushed the company back into insolvency. In mid-June, Hidroelectrica won a contract worth €12.7m to provide electricity until 2017 to the Bucharest subway operator Metrorex, and a contract worth €8.62m with the Bucharest Autonomous Authority of Transport (RATB). Once the company's management is handed over to its two shareholders, the Energy Ministry and Fondul Proprietatea, the next steps will be the appointment of a new supervisory board, and the company's public listing expected to take place in November 2016, when Hidroelectrica could list a 15% stake, on the Bucharest and London Stock Exchanges.

The Romanian National Company for Nuclear Activities (RAAN) went officially bankrupt after the competent court rejected, on 4 June 2016, RAAN's appeal against a lower court decision which decided on 28 January 2014 to begin bankruptcy procedures for RAAN. Later on, in June 2015, the National Administration of States Reserves and Special Problems (ANRSPS) stopped buying heavy water from RAAN, as their inventories were already sufficient to supply the nuclear reactors of Cernavodă power plant for 50 years. ANRSPS's decision entailed that heavy water production stopped, leaving the company with no production activity that could have helped save it from bankruptcy.

One of the main state-owned electricity and heat producer, Hunedoara Energy Complex (CEH), has re-entered insolvency and similarly, the Romanian thermal power plant CET Govora entered insolvency after a court decision of 9 May 2016. The power producer CET Govora lost €30.5m after state-owned chemical producer Oltchim entered insolvency in January 2013. The amount represents Oltchim's debt to CET Govora. The thermal power plant has been confronted with a lack of coal stocks, the blocking of coal transports, and a stop in the delivery of spare parts, materials and services from over 200 suppliers.

Proposals for changes in laws or regulations

Of particular relevance for the energy sector is a draft law facilitating the development of the BRUA by Romania's national TSO, Transgaz. The draft law aims to facilitate the construction and operation of a 500+300km natural gas pipeline ensuring interconnections with Hungary, Bulgaria and the Romanian Black Sea offshore discoveries.

Moreover, the Romanian upstream industry associations are also lobbying for new legislation which aims at improving some shortcomings of the Petroleum law, particularly, on issues such as access of operators to blocks, development of upstream infrastructure and management of classified information.

Important changes in legislation are further expected in the renewable energy sector in relation to the promotion of energy from biogas, biomass and geo-thermal sources. The promotion system of such renewable energy resources by means of a bonus granted to producers (with installed capacity of 6 MW) and investors in power stations (of up to 1 MW), shall consist in the difference between the fixed tariff/MW established by the regulator for supplied energy and the average monthly sale price on the Day Ahead Market. However, details on the implementation of such bonus scheme are still expected to be issued by the regulator.

* * *

Endnotes

1. ANRE Gas Market Report for 2015.
2. BP's Statistical Review of World Energy 2016.
3. BP's Statistical Review of World Energy 2016.
4. ANRE Gas Market Report for 2015.
5. ANRE Monthly Report of the Electricity Market December 2015.



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Laurentiu Pachiu, the managing partner and founder of Pachiu & Associates, has longstanding experience in various corporate matters, being a lawyer who has been witness to and participated in the shaping of the corporate and M&A market in Romania. The energy practice initiated by Mr. Laurentiu Pachiu has been among the first legal practices of such a kind established in the country, the firm founded by Laurentiu growing at the same fast pace at which the Romanian energy market evolved. The firm is now assisting some of the largest energy projects in the country, in both the oil and gas sectors, energy infrastructure, as well as the renewables sector. He is a graduate of Bucharest University School of Law and a graduate of the Diplomatic Academy of the German Federal Ministry of Foreign Affairs. Laurentiu is also a member of the Association of International Petroleum Negotiators.



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