

PN-ACG-121

**REPUBLIC OF MOLDOVA**  
**CORPORATIZATION OF THE GAS AND**  
**ELECTRIC COMPANIES**

**NIS INSTITUTIONAL BASED SERVICES**  
**ENERGY EFFICENCY AND MARKET**  
**REFORM PROJECT**  
**CONTRACT NO CCN-00-93-00152-00**

**MOLDOVA ENERGY SECTOR REFORM**  
**DELIVERY ORDER NO 19**

*Final Report*

*Prepared for*

U S Agency for International Development  
Bureau for Europe and NIS  
Office of Environment, Energy, and Urban Development  
Energy and Infrastructure Division

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September 1998

Republic of Moldova

**CORPORATIZATION  
OF THE  
GAS AND ELECTRIC COMPANIES**

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Republic of Moldova

**CORPORATIZATION  
OF THE  
GAS AND ELECTRIC COMPANIES**

## Overview

The plan for restructuring of the energy sector was formulated well before Hagler Bailly commenced its technical assistance pursuant to Delivery Order No 19 on September 1, 1997. The Moldovan consulting firm ARIA (Agency for Enterprise Restructuring and Assistance) was engaged through the World Bank beginning in October, 1996, to study restructuring programs in other countries and formulate a plan for Moldova in compliance with SAL II loan conditionalities. As evidenced by the passage of GoM 628 during July, 1997, a plan endorsed by the World Bank had received approval of the Government before Hagler Bailly began its work. The dynamic unfolding of these events influenced the extent and nature of the technical assistance requested by our counterparts with respect to "corporatization" in both the electric and gas sectors, as described in further detail below.

## Electricity Sector

GoM 628 "Concerning The Approval Of Electricity Sector Restructuring Plan", July 8, 1997, established the basic restructuring scheme for the electricity sector as

- Three separate combined heat and power joint stock companies (JSCs) corresponding to the three Moldovan plants on the Right Bank: CHP 1 and CHP 2 located in Chisinau and CHP North located in Balti,
- Five distribution companies JSCs serving exclusive geographic areas with monopoly utility services: North Electric Distribution Company (EDC), Northwest EDC, Central EDC, Chisinau EDC and South EDC,
- One state company, Moldtranselectro, providing high voltage transmission and central dispatch services (also retaining ownership of Costesti HES, a small 16 Mw hydroelectric plant on the River Prut (bordering Romania) used for load-following and system regulation purposes,
- The separation from Moldenergo (which was the case *de facto* in any event due to the separate political status of the Transnistria region) of MoldovaGRES (a large thermal plant with operating capacity of about 650 Mw) and Dubasari HES, a small 48 Mw hydroelectric plant on the Nistru (or Dniester) River (bordering Ukraine), and
- Ancillary enterprises (construction, machine shops, schools, etc.)

This decree also established the basic framework for creating an energy sector regulator and a process for privatizing the newly established companies. This decree signified the Government's commitment to significant reform in the electricity sector and set the stage for subsequent decrees which implemented this overall plan.

As illustrated by the two memorandum attached, Hagler Bailly worked with ARIA to provide policy guidance and counsel during the preparation of the documents necessary for filing with the Minister of Justice under Moldovan law to create the JSCs called for in GoM 628. Actual preparation of the documents was carried out by the Moldovan's themselves who were best equipped, as mutually agreed, to complete this work.

GoM 1059 "Reorganization Of Moldenergo State Company", November 13, 1997, is the decree through which the Government authorized and ordered the legal establishment of the separate corporations described above. In fact, the CHPs and EDCs became JSC's upon registration with the Ministry of Justice during October and November, 1997, just prior to the Government's official endorsement of this restructuring. Moldtranselectro's registration was delayed until August 3, 1998, but upon its registration and licensing by ANRE shortly thereafter, all of the significant entities involved in electricity sector reform had become both corporatized and licensed.

### Gas Sector

Moldovagaz created 36 local gas distribution companies (GDCs) during 1996, pursuant to Parliamentary Resolution no 611\_XIII, dated October 27, 1995. Additionally, "Gazsnabtranzit" private joint stock company, created in accordance with the Parliamentary Resolution no 305-XIII, dated December 6, 1996, had the effect of transferring 50% ownership of the high pressure transit pipeline system operated by Moldovagaz to their sole gas supplier, Russia's Gazprom. This deal with Gazprom was a debt/equity swap to satisfy \$140 m in accumulated payment arrears.

Shortly after Hagler Bailly began its work in Moldova, another plan was announced which would re-aggregate all gas operations once again into a single entity (a JSC) with ownership divided as follows:

- Republic of Moldova                      50%  
   Consisting of
  - State shares retained                      35%
  - Transnistria                                  14%
  - Managers/employees                      1%
- Russia's Gazprom                          50%

This reorganization plan was driven by Moldova's failure to pay Gazprom for the gas delivered over many years in an effort to satisfy these accumulated arrears and prevent Gazprom from denying gas supplies in the future. This "privatization plan" was approved by the Government and presented to the Parliament in late 1997. Parliament approved the plan in GoM 212 "On The Reorganization And Privatization Of Gas Sector Of The Republic Of Moldova", February 26, 1998, copy attached. However, nothing was implemented before the Parliamentary elections held in April, 1998, and the new Government has not acted quickly to implement this arrangement.

We understand that the new Government is reconsidering the matter and may not want to consummate this agreement

These actions by the Moldovan Government and Moldovagaz have precluded any alternative corporatization activities, such as the World Bank and USAID may have contemplated initially as more compatible with a functionally disaggregated gas sector. From the regulatory viewpoint Hagler Bailly is proceeding to work with ANRE in establishing a license and tariff regime that does reflect a functional breakdown of the different transit, transmission, distribution and supply activities of the sector. These important elements of economic reform will proceed regardless of the corporate structures ultimately adopted by the gas industry in Moldova.

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**GOVERNMENT OF THE REPUBLIC OF MOLDOVA**

**RESOLUTION n 628**  
of July 8, 1997

Concerning the approval of Electricity Sector Restructuring Plan

In order to implement the measures contained in the Program of activity of the Government of the Republic of Moldova for the years 1997-1998 and in the Resolutions of the Government of the Republic of Moldova n 478 "Concerning the additional measures to improve the financial situation of the energy enterprises in the Republic of Moldova" of September 2, 1996 and n 169 "Concerning the urgent measures for straightening the financial situation of the energy enterprises" of February 25, 1997 the Government of the Republic of Moldova DECIDES

- 1 To approve the Electricity Sector Restructuring Plan
- 2 The Energy and Fuel Department, Ministry of Privatization and State Company "Moldenergo" will assure the integral execution and in established terms the measures indicated in the Electricity Sector Restructuring Plan
- 3 Mr Ion Gutu, Deputy Prime minister, Minister of Economy and Reforms, is charged to perform the control on the execution of this resolution

PRIME MINISTER OF  
THE REPUBLIC OF MOLDOVA

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# Plan for Electric Power Sector Restructuring

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## A Demonopolization of the Electric Power Sector

Currently the supply with electric power in the Republic of Moldova is performed by only one public enterprise, the "Moldenergo" State Company. Also it is practically the only one, which generates the thermal power for Chisinau and Balti municipalities.

Currently the situation of "Moldenergo" State Company is in a deep financial crisis and there exists the danger of its being unable to fully supply all the consumers with power as needed.

### 1 The major problems of Moldenergo

The major problems of "Moldenergo" are as follows:

- 1 Chronic arrears of electric power consumers to "Moldenergo" State Company and arrears of "Moldenergo" to its suppliers (the arrears accounted to 450 million lei, accounts payable to 1233 million lei as of April 1, 1997)
- 2 Inadequate prices policy and the system of crossed subsidies not allowing for covering the production costs and for creation of sufficient funds for repair, renovation and development (loss due to the above reasons is estimated at 368 million lei in 1995 and 216 million lei in 1996)
- 3 The technical losses and enormous amount of theft from the network (22 percent from deliveries) which are conditioned by physical and moral depreciation of equipment (60 percent of the equipment were used for over 21 years and 40 percent for over 26 years), as well as lack of an adequate system for measure and control
- 4 The lack of any element of competition in the electric power market resulted in the lack of financial transparency in the activity of energetic units and their low efficiency. The current structure of the company is very complex and inadequate for market relations, with an enormous number of personnel (1 employee is responsible for 80 clients as opposed to 145 clients in OECD countries). The structure of the company is given in the Annex No 1.
- 5 The processes of electric power production, transportation and distribution are inefficient and of low quality (frequent drops of voltage, unstable frequency, which may drop down to 49.3 Hz, fan like disconnection, the available generation capacity amounts to only 45 percent of the installed one). The installed and available capacities for electric power generation in electric power stations are given in the Annex No 2.
- 6 Unjustified involvement of political influence in the economic activity of "Moldenergo" (while adopting the tariffs the emphasis is laid on the social aspect of the problem and the free electric power supply is imposed on the company).

The cumulated negative effect of the financial and technical problems, currently persisting in the electric power system, affects the state's energy security, conducts to the instability in the electric power industry.

The Debt Management Plan for the Energy Sector of the Republic of Moldova referred to the necessary actions for improving the financial condition of the electric power enterprises. To provide for the continuity effect in promoting the economic reforms and for market economy principles implementation, it is necessary to undertake an organizational restructuring of electric power sector. The new structure of the sector will provide for the creation of prerequisites for its further sustainable development and viably meet the optimal needs of national economy and population in electric power.

## **Objectives**

The Plan comprises short-, medium- and long term actions for the achievement of the following strategic objectives:

- 1 Viable supply of power to consumers in sufficient amounts, with adequate quality and at the minimum prices
- 2 Implementation of competition elements, where possible, or of regulation based on efficient enterprises, in the area of consumption - through protection and other actions aiming at the reduction of production costs
- 3 Diversification of fuel supply sources to guarantee an optimal supply of different types of fuel
- 4 Attraction of local and foreign capital through establishment of clear and stable rules, in order to release the state of the necessity to fund the sector in one of the following ways: invoicing services, exploitation and maintenance, management, etc., credits, preferably without state guarantee, bonds, preferably convertible in stock
- 5 Reduction of state influence on the processes of electric power production and supply
- 6 Creation of the legal and normative framework, which will establish the rights and obligations of all participants in the electric power market

Practical accomplishment of the above-mentioned objectives will be performed through

- De-centralization and corporatization of the electric power sector
- Separation of the auxiliary activities and the social and cultural facilities from the main activity
- Implementation of a system for regulating of activity in the electric power market and consumers protection

The scheme of interconnections between the agents on electricity market, the electricity and financial flows are presented in Annex 3 and 4

In order to regulate the activity of the companies on energy market an independent body will be created – National Energy Regulatory Agency (ANRE)  
Economic Agents who will exercise above-mentioned functions will perform their activity on a licensed and contractual basis

## **General Principles**

The Electric Power Sector has 6 basic functions

- a) generation of electric power,
- b) power transportation (voltage networks),
- c) dispatch system,
- d) purchase/sale of power,
- e) distribution of electric power (low voltage networks),
- f) retail sale of electric power

The Restructuring of the Electric Power Sector of the Republic of Moldova will be achieved through its gradual division according to the functional principle

- organization of generators as independent entities in form of joint stock companies, and their privatization,
- organization of high voltage transmission lines (35 kV and higher), as well as the Dispatching Center as independent state enterprises,
- organization of regional distribution lines (0.4 to 10 kV) into independent entities as joint stock companies and their privatization (the 6 through 10 kV transformation stations included),
- organization of retail distributors (private enterprises) which have no low voltage transmission lines and which have no territorial sale limitations,
- organization of wholesale electric power sales through private enterprises,
- separation and corporatization of auxiliary activities,
- transfer of social activities to administrative public institutions or their separation and privatization

The scheme of the relationships among agents in the electric power market and the scheme of power flows and cash flows are shown in Annexes 3 and 4, respectively

In order to achieve a normal functioning in the area, an independent regulatory entity will be created the National Energy Regulatory Agency (ANRE)

Economic agents performing the above-listed functions will work based on licenses provided by ANRE and other concerned institutions and based on bilateral contracts

## Power Generation

### General Description

Electric power supply is performed by 6 power plants

- CTE-1, Chisinau,
  - CTE-2, Chisinau,
  - CHE Balti
- } within "Moldenergo"
- CHE Dubasari, within the Eastern Network (with a separate legal statute)
  - CERS Costesti, within the Northern Network, pertaining to "Moldenergo"
  - Moldova CERS, an enterprise with separate legal statute

It should be mentioned that the situation is different for different enterprises

- 1 *Depreciation* Over the last years no significant investments have been made, the depreciation level is reflected practically by the time the boilers, turbines (generators) putting into function

No	Power station	Time between putting into function of boilers	Time between putting into function of turbines
1	CET-1	1950-1968	1957-1962, 1994
2	CET-2	1975-1991	1976-1980
3	CET Balti	1955-1988	1970, 1995
4	CERS Moldova	1963-1980	1963-1982
5	CHE Costesti	x	1975-1978
6	CHE Dubasari	x	1954-1955

### 2 *Market share and the installed capacity*

In the table below is shown the difference between the market shares of different electric power stations (1995)

	<i>CERS Moldova</i>	<i>CTE-1</i>	<i>CTE-2</i>	<i>CTE Balti</i>	<i>CHE Costesti</i>	<i>CHE Dubasari</i>	<i>Sugar factories</i>	<i>Import, Ukraine</i>	<i>Total</i>
Supply	2,327 3	106 4	794 4	80 9	84 5	239 7	15 6	1,996 7	5,645 5
In %	41 2	1 9	14 7	1 4	1 5	4 2	0 3	35 4	100 0

The available capacities are given in Annex 2

### 3 Generation principles

CTE-1, CTE-2 and CTE Balti are co-generating electric and thermal power, their costs being lower than at CERS Moldova, where the condensation principle is being used. CHE Costesti and CHE Dubasari have very low generation costs.

### 4 Scope of utilization

CHE Costesti and CHE Dubasari are used generally only for the regulation of the load curve.

*These substantial differences among the electric power generators account for their **different positions** in the electric power market in case of its de-monopolization. Therefore, the regulation of the market will be of utmost importance, if one of the objectives is to maintain the existence of the less efficient producers.*

### 5 De-monopolization principles

The function of electric power generation will be separated from the "Moldenergo" state company, while the generation units CTE-1, CTE-2, CTE-Balti will be organized as joint stock companies and independent legal entities. CERS-Moldova has already an independent enterprise status.

The Hydroelectric stations from Costesti and Dubasari will be incorporated in the transportation system, since their generation capacity is relatively low, while the operation starting costs are insignificant, thus they may be used as load curve regulating levers.

In addition to local generator systems, the electric power supply will also include imported power. The electric power import will be done based on a separate license issued by ANRE. In order to protect the interests of local generator companies, licenses will be issued for certain amounts of power.

The generator company will have the right to perform direct sales at agreed prices to consumers or distributors, based on contracts, providing for supply of an amount regulated by ANRE.

Also, in case the generator company has available capacity, it may render generation services, i.e. services of electric power generation, on behalf of or to third parties. This opportunity will be available only in 2 to 3 years, when the ANRE develops the respective regulations for operations and the electric power market will achieve the respective level of development.

In order to provide for long-term security of supply with electric power in the country, the existent generation capacities should be renovated and investments should be made in building new capacities. The current owner of the generators as well as the generator companies, which are being formed, do not have the necessary funds. The international experience shows that the best solution to the issue would be the attraction of private investments. Upon de-monopolization of the sector, private investors will prefer to invest in generator companies in order to have a secure market and profit margin.

The adopted legal framework ("Law on Electric Power Generation, Transportation and Distribution", Operation Regulations, Licenses for Operations) will provide for the necessary conditions for promoting investments in new local generation capacities. This can be achieved by rendering sale privileges to local generator companies or by introducing import licenses for certain amounts of power. Thus, this strategy creates the conditions for the emergence of competition and for the increase of the share of local generation in the total amount of electric power supply.

The power generation function will be realized through provision of licenses.

The Implementation Schedule

Action	Date	Responsible
Creation of Joint Stock Companies on the basis of electric power stations and their statutes adoption	July 1, 1997 – September 1, 1997	Ministry of Privatization, Energy Department
<ul style="list-style-type: none"> <li>• Calculation of accounts receivable and payable which are to be transferred to each electric power station (proportionally to turnover) and the equity capital as a difference between assets and debts</li> </ul>	July 1, 1997 – July 15, 1997	
<ul style="list-style-type: none"> <li>• Inventory of the fixed assets and verification of balance accuracy</li> </ul>	July 16, 1997 – August 1, 1997	
<ul style="list-style-type: none"> <li>• Development of statutes (charts) for the organized Joint Stock Companies</li> </ul>	July 16, 1997 - August 15, 1997	
<ul style="list-style-type: none"> <li>• Approval of the decision on the creation of Joint Stock Companies on the basis of electric power stations</li> </ul>	August 15, 1997 – September 1, 1997	

*Responsibilities of the Power Generator*

- publication of available capacities
- verification of quality standards for services and the publication of the verification outcome
- the electric power production and supply will be performed only based on licenses and contracts

*Rights of the Power Generator*

- power supply to foreign consumers if the local customers have no demand for full capacity,
- the cessation of power supply if the client has not complied with his contract responsibilities,
- reject power supply applications to customers who have not paid for the power supplies by another generator as of the date of application

# Transportation and Dispatching

## General Description

The transportation is performed through 7 transportation and distribution entities

- Northern Networks
  - Northern-Western Networks
  - Central Networks
  - Chisinau Networks
  - South Networks
- } within "Moldenergo" enterprise
- 
- Eastern Networks
  - Southern-Eastern Networks
- } as separate entities in the State Company "Moldenergo"

Each of the above entities are further divided into district electric power networks

These entities perform two functions

Transportation function the voltage networks and transformation stations for 35 kV and more, and

Distribution function 0.4 - 10 kV

The voltage networks and transformation stations managed by the above-mentioned networks are as follows (as of January 1, 1996)

Voltage, kV	0.4	6-10	35	110	330	400
Voltage networks, km	39,168	28,916	2,397	4,104	530	214
Number of stations, units	17,575	2,941	181	209		6

Thus, as the above Table shows, the Transporter will acquire 7,245 kilometers of high voltage networks and 396 electric power transformation stations

### *Principles for Restructuring*

The high voltage network, the Dispatching Center and the Costesti and Dubasari Hydroelectric Stations will be organized in a separate entity – the Transportation and Dispatching Enterprise. This enterprise will be organized as a state owned industrial unit or as a Joint Stock Company in which the state will belong no less than 51% of shares

The base functions of this enterprise will be the formation and regulation of system energy and power load balance, the transportation of electricity by intermediate of high voltage network to the distributors and consumers

During the transition period, till the stabilization of electricity market and in order to ensure the electric security, the Transportation and Dispatching Enterprise on the basis of the license issued by the ANRE will have the right to conclude electricity buying/selling contracts. This fact will be possible only with the permission of ANRE (with the particular examination of each case) and under the conditions provided by ANRE. This necessity will disappear and will be definitely prohibited after a period not more than 2-3 years, except the sale of electricity from the Hydroelectric Stations

In this period of time in the area of commercial activity the priority will be given to the distributors and commercial agents – wholesalers and retailers. Therefore the Transportation and Dispatching Enterprise will be obliged to register and execute the contracts of these agents. As an objective cause of refusing to register these contracts can be only the excessive system load and only with the approval of ANRE

The payment for electricity and transportation services will be performed in accordance with the conditions of signed bilateral contracts and the tariffs regulated by ANRE

#### The Implementation Schedule

<b>Action</b>	<b>Date</b>	<b>Responsible</b>
Creation of Transport and Dispatching Enterprise	June 1, 1997 – September 1, 1997	Ministry of Privatization, Energy Department, "Moldenergo"
<ul style="list-style-type: none"> <li>• Inventorying of fixed assets and working capital, determination and distribution of assets and liabilities between the new created energy entities</li> </ul>	June 1, 1997 – August 1, 1997	
<ul style="list-style-type: none"> <li>• Adoption of Resolution concerning the creation of Enterprise</li> </ul>	August 1, 1997 – September 1, 1997	
<ul style="list-style-type: none"> <li>• Registration of Enterprise and Organization of its activity</li> </ul>	Beginning with September 1, 1997	

## **Distribution**

### General Description

As mentioned earlier, distribution, similar to transportation, will be performed through 7 entities (Electric power networks) organizationally divided into several other entities, District Electric Power Networks

No	Name	Number of district networks
1	Central Electric Networks	11
2	Southern Electric Networks	9
3	Eastern Electric Networks	4
4	North-Western Electric Networks	6
5	South-Eastern Electric Networks	3
6	Northern Electric Networks	9
7	Chisinau Electric Networks	4

These networks have 75,329 kilometers of electric power networks, 68,084 of them being 0 4-10 kV networks

#### De-monopolization principles

The current distribution system will be divided into 7 regional distribution companies. This number was reached by calculating the technical and economic efficiency. The distributors will have regional distribution networks (0 4 to 10 kV).

The distributors will distribute and sell electric power on the basis of separate licenses (one for distribution and one for sale). They will purchase electricity from the generator or from the wholesale supplier at tariffs calculated according to methodologies controlled by ANRE.

Initially licenses for retail sale will be provided only to distributors having electric power networks. Within two to three years the possibility will be reached to provide licenses to agents not having electric power networks. In order to achieve this it is necessary to oblige the regional distributors to transport (according to technical possibilities, which should be regulated) electric power for any other retailer, who does not have transportation networks.

The distributors will conclude contracts for electric power supply for one year with each of the consumers, the contracts being registered at the distribution agency, ANRE and Transporter. This will contribute to a more exact and efficient planning of generation and distribution.

~~The tariffs for power purchase from the generator for large consumers will not be regulated by ANRE.~~

Retailers will have the possibility to purchase services for generation, transportation and distribution of power. By introducing competition at the stage of distribution, some compensation is done for the limitation of competition at the power generation stage.

## Implementation Schedule

	<b>Action</b>	<b>Date</b>	<b>Responsible</b>
1	Creation of the distributors regional Joint Stock Companies with statute of separate legal entity on the basis of low voltage regional distribution networks	July 1, 1997 – September 1, 1997	Ministry of Privatization, Department for Electric Power "Moldenergo"
	▪ Calculation of accounts receivable and acc payable which are to be transferred to each distribution company (proportionally to business data and the equity capital as a difference between assets and credit debts)	July 1, 1997 – July 15, 1997	
	▪ Inventory of fixed assets verification of balance accuracy	July 16, 1997 – August 15, 1997	
	▪ Development of statute for the Joint Stock Companies to be organized	July 16, 1997 – August 15, 1997	
	▪ Approval of decision on creation of Joint Stock Companies on the basis of high voltage network	August 15, 1997 – September 1, 1997	
2	Concluding of bilateral contracts with electric power generating enterprises and/or with foreign wholesale suppliers and salesmen and contracts registration in the Dispatching Center	September 1, 1997 – December 31, 1997	Distribution companies

## National Energy Regulatory Agency

The de-monopolization of the electric power sector will be possible only upon the creation of an independent institution, which will regulate the relationships between agents in the electric power market, the National Energy Regulatory Agency

The responsibilities dealing with licensing of production, dispatching, distribution, transportation and supply of electric power, the control of the compliance with the consumers' requirements and the responsibility following from the special legal regulations regarding the production, dispatching, transportation and distribution of electric power, control of tariffs, promotion of competition will be performed by ANRE, created by governmental decision

The Agency will have the following responsibilities

- Issuance of licenses for production, transportation, distribution, supply and other activities in the electric power sector,
- Monitoring the observance by the licensees of the rules and conditions contained in the licenses issued by the Agency,
- Elaboration of tariffs calculation methodology for electricity,
- Approval of regulations of commercial activity and verification of the tariffs calculation,
- Identifying of the information which will be published by Licensees,
- Licensing of the specialists performing their activity in the Energy Sector,
- Promotion of the competition

### Schedule of Actions for ANRE Creation

Action	Terms	Responsible parties
Approval of the Decision for the creation of the National Energy Regulatory Agency	Till July 1, 1997	Government
Development of the models of licenses	July 15- November 30, 1997	ANRE members
Issuance of licenses	Starting with December 1, 1997	

## 8. Establishment of Tariffs

*ANRE will not set the level of the tariff, but elaborate the methodology according to which the agents in the electric power market will calculate costs and tariffs*

The tariff for electric power production, transportation and dispatching, distribution and supply will have to include the costs for the efficient work of the electric power units, as well as the necessary profit for the continuation of the activity by license holders

The tariffs for electric power production, transportation and dispatching, distribution and supply will, as well as other payments and fees will be correlated with the following requirements and basic principles

- a) When establishing the tariffs the costs for the following will be taken into account
  - maintenance of reserve installed power,
  - compliance with the environmental protection
- b) the rules of tariffs calculation will be established in a way that will promote reliable power supply at minimal prices , as well as the efficient utilization of production capacities

The detailed methodology for tariffs calculation and application will be developed by ANRE and approved by the Government for a period of 5 years

The license holders will submit to ANRE all the data needed by ANRE for the tariffs supervision. The license holders will set an accounting system providing for the transparency of incomes and expenses

The separation of activities in the Electric Power Sector will not lead to the increase of tariffs, because every economic agent will have different profit margin rates such that the sum of all companies profit does not exceed the level of profit projected for the case when a single company existed

## 9 Responsibilities of the State in New Conditions

The fact should be mentioned that in the new conditions, when the electric power sector will be privatized to a great extent, the state will be of no less importance than today

First of all the state will create the **legal framework** which will control the activity of the actors in the electric power market, the Act on Electricity, the Regulation on ANRE, etc

Secondly, the state will be the **main arbitrator** having the responsibility to detect possible violations of rules in the market

Thirdly, the state will hold the **control package in the transportation and dispatching**, which have a very important role

Another type of state's activity, which is no less important, consists in the *promotion of the energy policy* of the country

- Establishment of the strategy for electric power sources development and their interconnection with other states,
- Approval of the electric power stations building with the capacity of over 20 MW,
- Approval of the type of fuels to be utilized by the electric power stations with the capacity greater than 20 MW,
- Establishment of conditions for the import and export of electricity,
- Promotion of producers interests in international relations in issues of strategic import of fuel,
- Determination of the minimal amount of state fuel reserves

The range of the activities is much wider and requires a *higher responsibility* and, respectively, *competence* on the part of the state. The lack of competence of the state and errors made by the state in the current conditions may have a great impact on the Energy Sector

## 10 Insurance of Electric Power Security in New Conditions

At the actual transition stage of the Republic to the market economy a key element of state policy is represented by the energy security which affects directly the economic security of the country. The term of energy security refers to the state's capability to ensure a reliable and sufficient energy supply in order to cover the needs of the national economy and households for a short and long period of time. This fact should not concern the environment aspect and the life level of population. In fact the nucleus of indigenous energy sector is the electricity industry, that's why the most important aspect of energy security is represented by the electric security of the state. Among the essential factors that influence and determine the electric security of the Republic of Moldova we can nominate the following

- **Access to regional and world electric resources** it is very important that the state has access to energy resources anytime when it needs. Actually it exists 14 High Voltage Lines (HVL) of electricity import/export with Ukraine (the capacity being of 1 million kW) and only 3 connection HVL with Romania (150 Th kW),
- **Diversity of import sources** this fact ensures an optimal choice, which is characterized by minimal costs and the reduction of possible risks due to conjuncture fluctuations. It should be noted that at present the main part of installed (84%) and available (665) electric capacity on the territory of Moldova is concentrated at the CERS Moldova and the bought electricity from this station for the right river needs constitutes 47% (as of 1996) of the delivery in the network (from Ukraine – 31%),
- **Integration of electric systems** it means economic and technical efficiency, reliability and viability. Nowadays in Europe it exists the tendency of integration of electric systems in the framework of UCPT system, to which adhered such countries as Czech Republic, Slovakia, Poland, Hungary and till the year of 2000 possibly Romania, Bulgaria and Albania will connect too. The UCPT system is not

compatible with CIS's system and on a long time basis this causes for Moldova the danger to be isolated and support an economic and political risk,

- **Organization form and management of electricity sector** it is an urgent need to introduce the elements of competitiveness and efficiency in this industry

Taking into account the above-mentioned reasons it is evident the fact of proceeding to a radical and without delay restructuring of electricity sector Only by a real accomplishment of the de-monopolization and privatization process

- the electricity market will be liberalized, accompanied with the establishment of transparent commercial relations,
- the political barriers will be eliminated,
- the competitive elements will be introduced in the appropriate market areas (in the field of generation and distribution) and, where competition is not possible, creating monopoly entities that will be reduced to a few well-defined functions, easy to manage and regulate As a result of electricity sector de-monopolization and privatization the private interest will represent the most important driving force and incentive in the development of industry and the achievement of maximal economic and technical efficiency by minimizing the costs and thefts (for each operational function separately) In such a way all the consumers will benefit of reasonable tariffs and reliable and qualitative services

In case the activities in the electric power market acquire a commercial nature, the *penalties for of the suppliers* will become possible That is, the consumer will be able to forward complaints for compensating for the damages conditioned by non-compliance with the terms of the contract by the supplier, in case the supplier does not respond or rejects the complaint, the consumer will be able to apply to the economic court with the issue of compensation for the damage

The above provide for a *much more* secure electric power supply, than currently, when the consumer does not benefit from guarantees of the necessary quality and volume

In order to provide for a better security in the electric power supply, the Transporter will be able to conclude contracts for purchase/sale of electric power, recommended to be done with advance payment But this will be done only with the consent of ANRE (for each contract) and only in cases set by ANRE (when the distributor refuses to conclude the contract for different non-commercial reasons, etc ) The need for this will vanish within 2 to 3 years and will be *forbidden*

Over the first three years, if the distributor is unable to honor the responsibilities in supplying electric power to the solvent consumers for different reasons (revocation of license by ANRE, lack of funds, lack of ability to find suppliers, etc ), ANRE will have the right to provide to other distributors the right to supply electric power to the solvent consumers of the former distributor (in case of significant consumers, the right may be provided to wholesale agents)

Over the following years, this right will be provided also to the retail agents

## B General Principles of Privatization

### 1 Introduction

The previously developed restructuring actions of the electricity sector will be efficient and effective only in the context of its privatization, especially of generation and distribution. Two very strong rationales show the necessity of electric power sector privatization in the Republic of Moldova:

- 1 Efficiency of planning and operational activity. There is a growing perception that the big and integrated state monopolies are not the most efficient units in the electric power production or in the effort of consumers protection from the monopolists potential abuses. In the Republic of Moldova the electric power monopoly employs excessive labor and performs highly inefficient operations. The excessive staff and low efficiency of such arrangements is obvious even in industrialized countries.
- 2 The debt of the country. This rationale is even more acute than the previous one. The Government cannot and will not be able to fund the maintenance and the extension of the generating capacity in order to meet future demand. This problem is even more important if we take into consideration the fact that the availability of power resources is the factor /the primary prerequisite/ for economic growth. If the Government continues the credits' policy the current burden will become even worse.

On the other hand, the time is very near ahead, when the Government of the Republic of Moldova will no longer have the easy access to credit resources or to the acceptable credit resources.

Thus, the privatization is no longer a social option but an economic imperative.

Other reasons leading to the idea of electricity sector privatization are:

- possibility of collection of the necessary financial sources into the budget,
- elimination of cross subsidies,
- creation of prerequisites for private sector development in electric power generation (investment in existing sector or in additional generating capacities). This will allow for a long-term electric power supply security.
- Development of competition among agents in the electric power market (salesmen, generators), which will result in efficiency growth of power resources utilization at all levels (primary power consumption, electric power production and consumption). Finally, this will facilitate the decrease of commercially viable prices as occurred in the countries which have already begun the power sector restructuring and privatization,
- Promotion of the market economy principles through private property.

## **2. Action Plan to Proceed**

1 According to the Restructuring and Demonopolization Plan by 1<sup>st</sup> of December 1997, the following preconditions for the privatization of the Electricity Industry must be fully in place

- there are four independent generation companies corporatized,
- there are seven independent distribution companies corporatized,
- the corporatization must be performed in the way that at least 50 percent plus one voting share in each of the companies specified under point 3 will be available for sale to strategic investors,
- there is the National Energy Regulatory Agency operating,
- all the elements of the regulation are in operation and the purchase and sale contracts are executed,
- the new regulatory regime ensures that the revenue position of the companies is adequate, the economic prices are introduced,

2 The adequacy of the general legal framework to attract sufficient investor interest is to be ensured

Some of the specific issues that should be addressed foundation and operation of companies, foreign investment, banking, foreign exchange, financial market, accountancy, taxation, land, environment, privatization, investment protection, local governments

***Deadline:***

1<sup>st</sup> of December 1997

***Responsible:***

Ministry of Justice, Ministry of Economy, Ministry of Privatization and Ministry of Finances

3 The following companies must be privatized

- four generation companies, namely Moldova Power Plant, CHP-1 Chisinau, CHP-2 Chisinau and CHP Balti
- seven distribution and supply companies which hold and operate low-voltage networks

At least 50 percent plus 1 voting share (the simple majority) in each from the above companies will be offered to strategic investors through open international tendering. It will be one round tender with firm bids. The tenders must be issued by 1<sup>st</sup> of June 1998. The Government retains the right to approve the main principles of the tender rules. The time table for implementing the privatization is attached

***Deadline:***

1<sup>st</sup> of June 1998

***Responsible:***

Ministry of Privatization

4 The Government shall ask the Parliament to specify the volume of the shares in the companies under point 3 that can be privatized and shall ask the permission of the Parliament for the implementation of the privatization specified under point 3

***Deadline:***

1<sup>st</sup> of October 1997 for getting the permission

***Responsible:***

Government

- 5 The Ministry of Privatization must elaborate the plan for the allocation of shares of the companies that will be available above the 50 percent plus one voting share. The Government retains the right to approve the Plan.

***Deadline:***

1<sup>st</sup> of May 1998

***Responsible:***

Ministry of Privatization

The reasoning for the allocation of the above mentioned shares could be

- higher privatization revenues could be obtained if bigger package of shares is offered to the strategic investors,
- the Government might have control objectives. These objectives can be met either by retaining a significant minority package of shares or by introducing "special" or "golden" shares,
- the Government might consider to sell shares to the employees of the companies on preferential rates or transfer shares to the municipalities, social fund or other state institutions,
- the Government might consider to allocate shares for public offering through stock exchange or other ways

### **3 Method, organization and timing of the envisaged privatization**

#### *3.1 The method*

The method of privatization is *competitive trade sale with single round of firm bids*. This method satisfies most of the privatization objectives and corresponds to the short time requirements.

To complete the competitive trade sale, the Lead Financial Advisor, in cooperation with the concerned institutions and companies, will prepare extensive and detailed tender documents which set out information on the industry structure, the regulatory regime, the present financial and technical conditions of and prospects for the companies, the rules of the tender process, and contains the draft share purchase and sale agreements as well as drafts of other contracts that might be necessary to complete the deals. The preparation of tender documents is in the responsibility of the Lead Financial Advisor and is to be done by the 1<sup>st</sup> of June 1998.

All the eleven companies will be tendered simultaneously. However, the Ministry of Privatization, with the help of the Lead Financial Advisor, during the elaboration of the detailed privatization action plan, shall consider the grouping (generation companies, distribution companies).

#### *3.2 Strategic issues*

The following strategic issues will need to be looked at and decided during the elaboration of the tender and the share purchase and sale agreement terms.

##### 3.2.1 Size of the strategic stake to be offered

During the preparation of the tender documents, the Ministry of Privatization, with the assistance of the Lead Financial Advisor, shall optimize the size of the stakes to be offered with regard to the following considerations: in order to secure serious bids, the strategic stakes sold will need to be of such a size that the trade investors are able to be sure of obtaining a certain degree of management control. The strategic investors would also want assurance that on long run they are the largest single shareholder.

The decision on offering at least 50% + 1 voting share to the trade investors satisfies both their requirements and is in line with the intention to involve advanced management know-how as quickly as possible.

The maximization of privatization proceeds would require to elaborate and approve the plan for the allocation of the remaining shares latest before the issue of the tenders, taking into account issues highlighted under point 5 of the *Action Plan to Proceed*.

##### 3.2.2 Government control

The Government might have control objectives in the generation and/or the distribution supply companies. This might be exercised:

- through holding the blocking minority of the shares, or
- holding a single "special share". The "special share" will provide no right to dividends but will permit to veto various decisions which the company can only take in its general meeting.

The decision on this will be made by the Government following the marketing study results of the Lead Financial Advisor and the plan on the allocation of the shares above 50 percent plus one voting share to be offered to the strategic investor

### 3 2 3 New investments

The Financial Advisor, with the help of the Technical Advisor and the Accounting Advisor, will provide proposals on whether there are requirements for new and urgent investment in the companies that should be compulsory funded by the new investors or not

### *3 3 The timing of the privatization*

The timing and the activities involved are shown on the attached timetable as Annex 5

### *3 4 The activities to be performed before starting the creation of tender documents*

#### 3 4 1 Selection and contracting of Lead Financial Advisor

The Ministry of Privatization will appoint the Lead Financial Advisor, which should be an investment bank with good reputation with sufficient experience in organizing trade sales. It will be selected through limited international tendering. The firms, which are invited, will preferably be chosen from those having Moldavian experience. The main tasks of the Lead Financial Advisor are

- to familiarize itself with the industry and the general investment environment,
- to prepare and manage the implementation of the overall privatization process on behalf of the Vendor (Ministry of Privatization),
- to market the sale,
- to refine the privatization strategy (including consulting the Vendor on the strategic stake, the further shares allocation, investment requirements, sequencing of sales) and to prepare the detailed action plan for the Privatization Project,
- to define the right project structure and processes and specify the resources necessary to prepare and execute the privatization,
- to monitor the process and signal if the set deadlines are threatened and suggest to the Vendor corrective measures,
- to prepare the tender documents, getting substantial inputs from the Legal, Accounting and Technical Advisors, as well as from the National Energy Regulatory Agency, the Energy and Fuel Department, all the companies of electricity sector,
- to assist the Vendor in selection and management of the Accountant and the Technical Advisor (including the preparation of terms of reference),
- to assist the Vendor together with the Legal Advisor throughout the whole tendering process, including the negotiations required, contracting and financial closing

The Lead Financial Advisor will be assigned by the 1<sup>st</sup> of Octoberber 1997. Responsible – Ministry of Privatization

### 3 4 2 Selection and contracting of Legal Advisor

The Ministry of Privatization will appoint the Legal Advisor which should be a firm with good reputation and preferably with sufficient experience in Moldova. It will be selected through limited international tendering. The Legal Advisor will be appointed before selecting the Lead Financial Advisor in order to have the legal support in contracting the Lead Financial Advisor. The basic tasks of the Legal Advisor are

- to familiarize itself with the industry and the general investment environment and in cooperation with the Lead Financial Advisor to evaluate the legal environment from the point of view of the investors and to signal if measures are to be taken,
- to organize and perform legal due diligence,
- to draft all the legal documents related to the transactions,
- to provide legal assistance throughout the whole preparation and tendering process, including negotiations, contracting and financial closing

The Legal Advisor will be assigned by the 1<sup>st</sup> of August 1997. Responsible – Ministry of Privatization

### 3 4 3 Selection and contracting of Accountant Advisor

The Ministry of Privatization will select and appoint the Accountant Advisor. It should preferably be an international accounting firm. It will be selected through limited international tendering with assistance of the Lead Financial Advisor. The firms which are invited should preferably be chosen from those having Moldovan experience. The main tasks of the Accountant Advisor are

- to prepare Accountant's Reports of the enterprises in privatization (the Terms of Reference will be defined by the Lead Financial Advisor),
- to provide input for the Lead Financial Advisor and the Legal Advisor to formulate the appropriate tender and contractual terms,
- to provide input for the Lead Financial Advisor for performing valuation,
- to assist the Vendor (Ministry of Privatization) throughout the project

The Accountant Advisor will be managed by the Lead Financial Advisor on behalf of the Vendor

The Accountant Advisor will be assigned by the 1<sup>st</sup> of December 1997. Responsible – Ministry of Privatization

### 3 4 4 Selection and contracting of Technical Advisor

The Ministry of Privatization will select and appoint the Technical Advisor. It should preferably be an international engineering firm. It should be selected through limited international tendering with assistance of the Lead Financial Advisor. The firms which are invited should preferably be chosen from those having Moldovan experience. The basic tasks of the Technical Advisor are

- to prepare Technical Advisor's reports on the industry and the companies (the Terms of Reference will be defined by the Lead Financial Advisor),
- to provide input to the Lead Financial Advisor for the valuation and defining investment requirements,
- to assist the Vendor (the Ministry of Privatization) throughout the project

The Accountant Advisor will be managed by the Lead Financial Advisor on behalf of the Vendor

The Technical Advisor will be assigned by the 1<sup>st</sup> of December 1997 Responsible – Ministry of Privatization

### 3.4.5 Refinement of the privatization strategy and elaboration of detailed action plan

After the Lead Financial Advisor familiarized itself with the features of the reorganized and de-monopolized electricity industry, with the general legal framework and the investment environment, as well as collected sufficient information on the potential investor's interest, it will have to refine the privatization strategy and to elaborate the detailed action plan in order to define the necessary resources and their allocation for the implementation of the privatization process. This is to be done by the 1<sup>st</sup> of January 1998 Responsible – Lead Financial Advisor

### *3.5 Creation of the tender documents*

Since all of the details of the new organizational, regulatory and operational structures (corporatization, legislation, licenses, industry codes, dispatch rules, contracts, etc.) will be prepared by 1<sup>st</sup> of October, 1997, the privatization project will mainly comprise the activities related to the preparation and implementation of the share purchase and sale transactions

The outcome of the preparation will be the Information Memorandum for the trade sales of the companies. The Information Memorandum will contain all the documentation related to the tender. It will be prepared in the way that gives a fair and fairly complete information to the potential investors enabling them to assess the present conditions and the future prospects of the companies. The draft share purchase and sale agreements will be prepared. The Vendor's due diligence (legal, accounting, technical) will be a substantial part supporting this activity. The financial valuation of the companies is also to be performed in order to assess the value of the companies and to enable the Vendor to set appropriate contractual terms

The tender documents will be issued by the 1<sup>st</sup> of June 1998 Responsible – Ministry of Privatization

### **3.6. Marketing**

Before and in parallel to the preparation of the Information Memorandum the Lead Financial Advisor will undertake a marketing drive to identify and meet with likely investors. In advance of the issue of tender documentation the Lead Financial Advisor will ensure that potential investors have a good understanding of the privatization process, the organizational, operational structures and regulatory regime of the industry as well as on the companies that are for sale. The feedback from the potential investors will be used in structuring the tender process, formulating the tender rules and designing contract terms. The marketing drive is very important. Therefore the Lead Financial Advisor has to be assigned by the 1<sup>st</sup> of October 1997

### **3.7 Clarification**

Although the Information Memorandum will contain both the detailed tender rules and substantial amount of information on the industry and the individual companies, potential investors will inevitably seek for clarification of various issues prior to submission of bids. Clarification will entail the potential investors examining the companies and associated data in further detail. The Ministry of Privatization will make possible for the potential investors to visit the companies as well as to

examine a range of data and information, which could be made available. Information rules will be set up which contain substantial amount of written information specified by the advisers. The Ministry of Privatization, the National Energy Regulatory Agency, the companies to be privatized, the Energy and Fuel Department, and the Advisors will be available to answer the questions.

The Clarification phase will last until mid-August 1998.

### **3 8 Bid evaluations and negotiations**

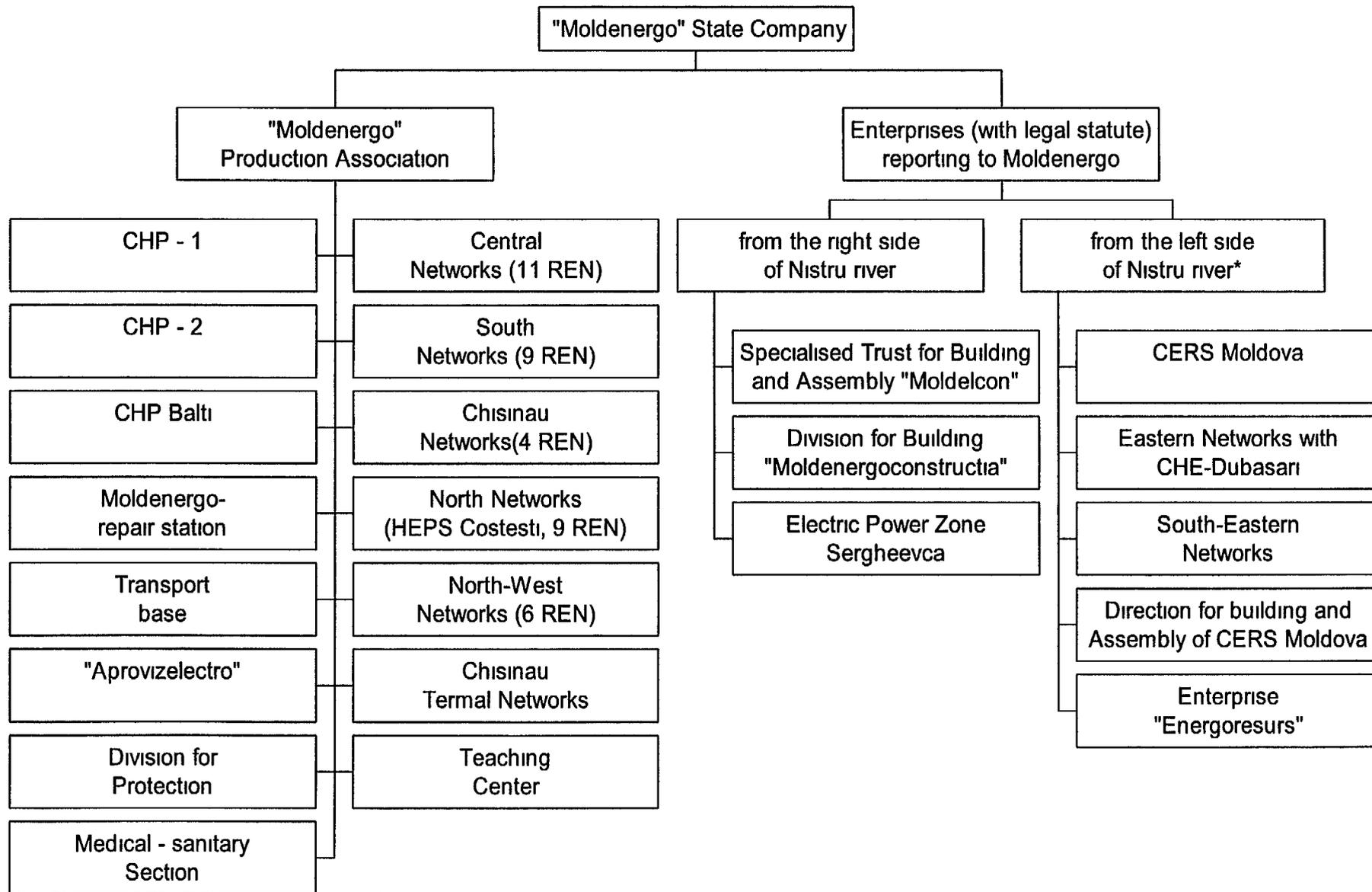
On receipt of the bids they will be screened for compliance with the terms and conditions of the tender. Bids will then pass a "technical" quality threshold. Thereafter any conditions will be evaluated or removed through negotiations in order to ensure that bids comply with the required terms and conditions. The bids of acceptable quality will be compared and the Vendor (Ministry of Privatization) will select the highest immediately or will negotiate further in the event higher prices still can be obtained.

### **3 9. Selection of the winners**

The winning bidders will be required to sign the sale and purchase agreement. In order to expedite the closure of the trade sale of each company it will be necessary to

- arrange for signing of the agreements,
- meet all conditions precedent of the sale and purchase agreements,
- arrange for payments for shares, the transfer of funds and the delivery of shares certificates

**Current Structure of "Moldenergo" state Company (since March 20, 1995)**

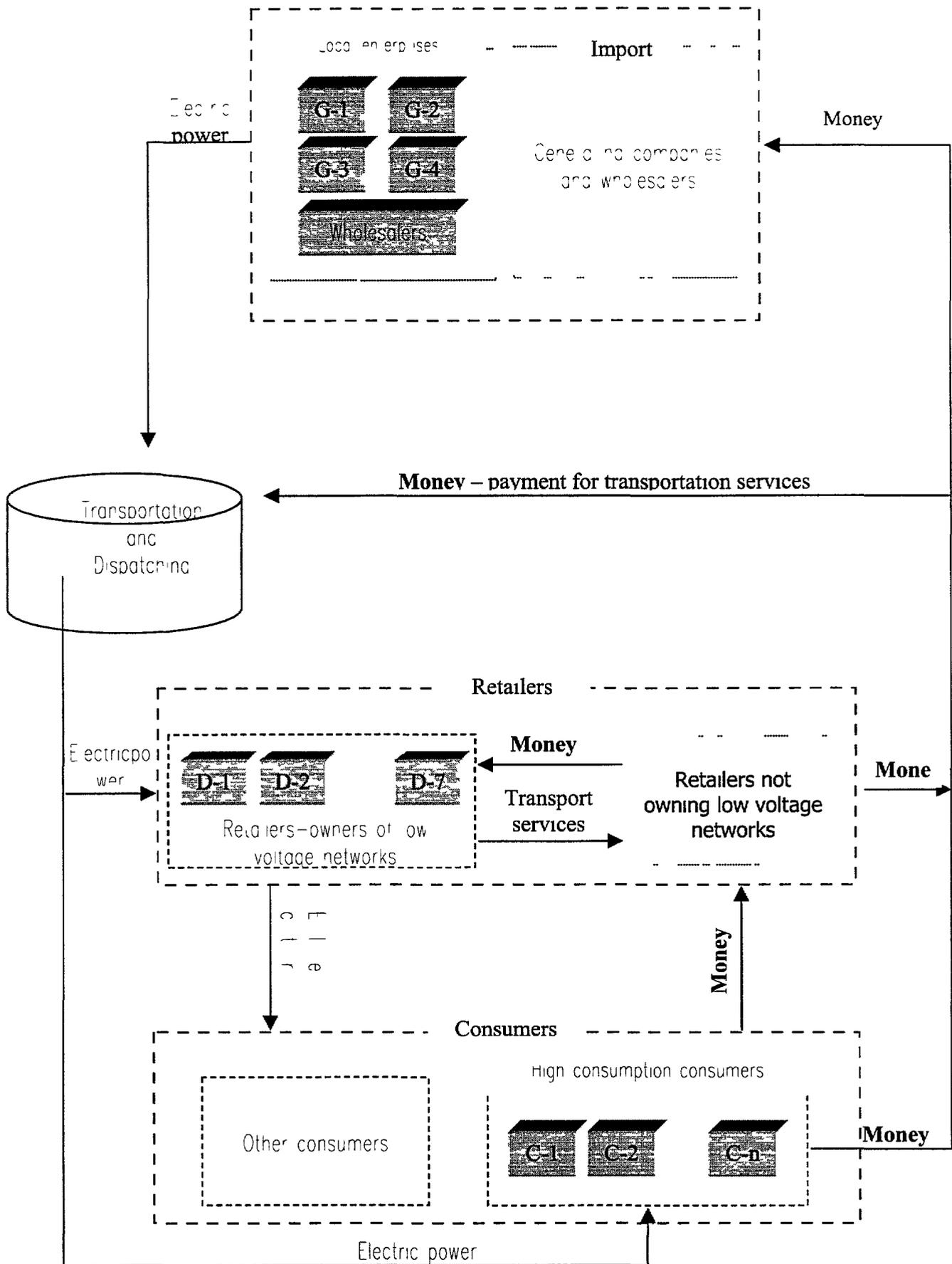


\* "de facto" are not subordinated to Moldenergo

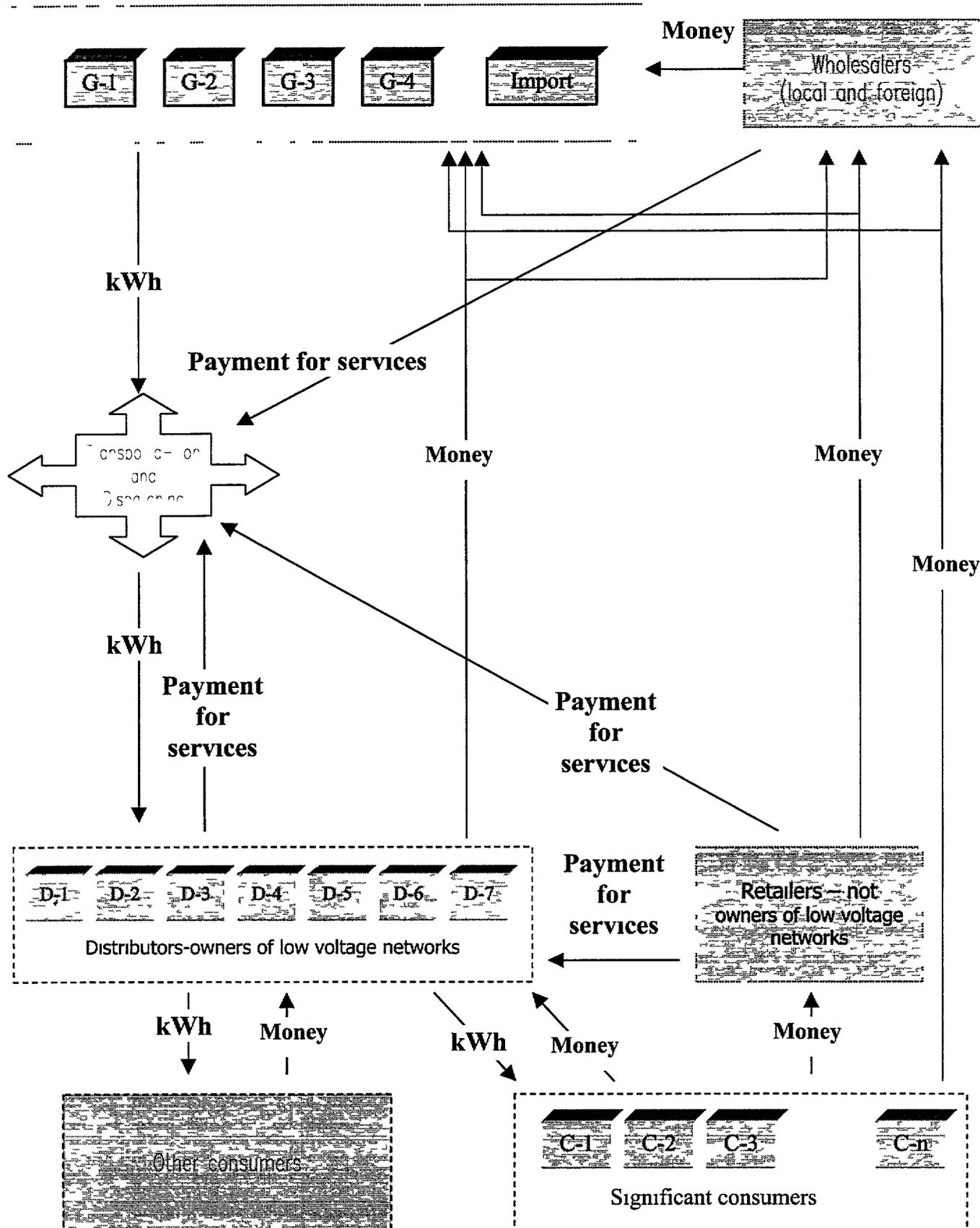
**Installed and available electric power generating capacities in the Republic of Moldova**

Electric power station	Installed capacity		Available capacity		
	MW	%	MW	% from total	% from installed capacities
<b>Power stations from the right side of Nistru river</b>	440	14.6%	408	30.1%	92.7%
<b>including</b>					
CHP-1 Chisinau	58	1.9%	47	3.5%	81.0%
CHP-2 Chisinau	240	8.0%	240	17.7%	100.0%
CHP Balti	28	0.9%	15	1.1%	53.6%
HES Costesti	16	0.5%	16	1.2%	100.0%
<b>Sugar beet factories power stations</b>	98	3.3%	90	6.6%	91.8%
<b>Power stations from the left side of Nistru river</b>	2568	85.4%	948	69.9%	36.9%
<b>including</b>					
CHP Moldova (Cuciurgan)	2520	83.8%	900	66.4%	35.7%
HES Dubasari	48	1.6%	48	3.5%	100.0%
<b>Total</b>	3008	100.0%	1356	100.0%	45.1%

Relationship between agents on the electric power market



Electric power and cash flows



## TIMETABLE FOR THE IMPLEMENTATION OF THE PRIVATIZATION

	Responsible	Cooperators	1997						1998									
			Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
Restructuring finished																		
New regulatory regime fully in place																		
Selection and contracting of the LFA	V	LA																
Selection and contracting of the LA	V																	
Review of the general legal environment and the development of the restructuring process, industry related legislation, regulation, initiating correcting actions if necessary and possible	LA LFA	V	.....	.....	.....	.....	.....	.....	.....	.....								
Refinement of the privatization strategy and elaboration of the Detailed Action Plan	LFA	V			.....	.....	.....	.....	.....	.....								
Marketing drive	LFA	V								→								
Selection and contracting of the AA and TA	V	LFA																
Preparation of the tender documentation	LFA	LA,TA,AA,C																
prepare tender rules	LFA																	
asses investment requirements	LFA																	
prepare financial models, valuation	LFA																	
set up information rooms (industry, company)	LFA	LA																
conduct technical audit	TA	C																
conduct accountant's audit	AA	C																
conduct Vendor's legal due diligence	LA	C																
prepare draft share purchase and sale and other transaction agreements	LA	LFA,V,C																
set evaluation criteria	V, LFA																	
editing, design, printing	LFA																	
Issue of tenders	V, LFA																	
Clarification		LFA,V,C																
bidders due diligence																		
answering bidders questions	V,LFA,LA,C																	
finalizing draft contract terms	V, LFA, LA																	
Submission of bids																		
Evaluation of bids	V LFA LA																	
Selection and negotiations with preferred parties	V, LFA, LA																	
Completion of the agreements, financial closing	V, LFA, LA																	

V - Vendor (Ministry of Privatization) LFA - Lead Financial Advisor, LA - Legal Advisor, AA - Accounting Advisor C - Companies (incl Moldenergo) TA - Technical Advisor

## MEMORANDUM

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**TO** Mr Ceslav Ciobanu, ARIA  
**CC**  
**FROM** James Tasillo  
**DATE** 09/17/97  
**SUBJECT** Asset Valuation for Moldenergo

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In our mutual work together to achieve the successful restructuring and privatization of Moldenergo, it is of vital importance to consider carefully the issue of asset valuation and avoid any actions which may make it more difficult or impossible to attract private investment to the electricity sector

In a market economy, the value of assets can only be determined by market forces. This means that when a "willing buyer" and a "willing seller" freely agree on a price which each considers to be fair (i.e., there is no external coercion applied in the transaction process), the value of the item traded is the price mutually agreed upon by the parties.

An example of such a transaction that is familiar to ordinary people would be to consider the "asset value" of your personal automobile. You know what you paid for it and, considering how long you have owned and used the car, its current condition and your estimate of its remaining life, you probably have an opinion about its value. If you asked your friends and neighbors to give you their estimates of its value, you would probably find each one has a different idea about your car's "asset value." However, none of these calculations or opinions will matter if you decide to sell your car to someone else. Then, if you find a buyer and reach agreement on price, the actual selling price is the only true measure of what your car is worth (and you have the cash in your hand to prove it).

The power industry is far more complex than this simple example, but the principles are exactly the same. At the time that the entities within the power sector enter into a privatization process that brings private investors to Moldova to compete for the right to purchase and own Moldenergo's assets, the price agreed between the Government and investors will determine the true market value of these assets.

Because this is the way that a private market economy functions to determine value, there is a danger that assigning value to assets using administrative methods (by accounting rules, indexing, etc.), which by their nature cannot accurately anticipate the results of the future privatization process, will lead to an unrealistic and misleadingly high level of valuation for Moldenergo assets. Just like the example of the car, an owner often thinks the value of his property is much higher than the reality of what he can get when he actually negotiates a price in the market place.

In the case of Moldenergo, we should not engage in a valuation process – prior to the

privatization process – that has the potential to produce unrealistic expectations among government officials and the populace. An equally important reason to avoid asset valuation now is that potential private investors may decide not to participate in any sale of Moldenergo assets if it appears that the price has already been established by the Government and therefore the possibility for successful negotiations is compromised from the beginning.

I strongly recommend that we allow the privatization process to determine the value of Moldenergo's property (the only way which produces a truly useful result) and avoid any administrative adjustment of historic book values at this time. Instead, we should complete the critical first step of creating separate corporate entities as soon as possible in preparation for the privatization process which is soon to follow.

## MEMORANDUM

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**TO** Anatol Saracuta, Director General, ANRE  
Valeriu Stavinski, Deputy Director General, ANRE

**CC** J Tasillo

**FROM** H Bhatia

**DATE** 09/30/97

**SUBJECT** Arguments in Support of Debt Allocation Plan

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The current accounts payables on the books of Moldenergo have accumulated over a number of years. As of September 97, the net payables in excess of receivables amount to 860 million lei.

In order to effectuate a reorganization of Moldenergo into distribution, transmission and generation entities, with the ultimate goal of privatizing the distribution and generation entities in the near future, it is essential to decide on allocation of these obligations in such manner so as to maximize the opportunity for privatization and make it attractive for a strategic investor to make reasonable offer and assume ownership and operation of the entities with minimum encumbrances.

The bare fact remains that these obligations were incurred during the regime when Moldenergo, as an enterprise was government owned and all its obligations were inherently assumed by the government. It would be naive to assume that a private investor would assume the enterprises' prior debts without an appropriate adjustment in the offering price. Typically, the investor would insist that all prior obligations be discharged or assumed by the Seller. Therefore, the discussion whether the payables be under distribution or generation or transmission entities is rather academic. As they say "you can run but you cannot hide" It might therefore be prudent to face this issue in an objective manner. Since the GOM is the sole owner of Moldenergo, the debt obligation ultimately must be assumed by the GOM.

From the point of view of mechanism, however, and to meet any governmental accounting procedures, it makes sense that the entity which is most likely to remain government-owned in the future and least likely to be privatized, assume the prior debts.

This would suggest therefore that the new transmission entity "Moldtranselectro" ought to assume the net payable debts of current Moldenergo.

This provides several options to the government to deal with the debts. Basically it can either pay off these debts through the tax structure, i.e. from national budget, or it can assess additional surcharge on the consumers of electricity. Since the surcharge shall be uniformly applied to all electricity consumers as bani/kWh, it would appear fair and non-by-passable charge to all users.

of electricity Such a charge can be assessed by the transmission company to all distribution entities who shall have the regulatory authority to pass it on to the ultimate consumers

Such an allocation of prior obligation shall enhance the privatization process and bring about the full benefits of privatization which ought to be the primary goal of this restructuring

If you wish to discuss this further, please let me know

**Governmental Resolution Nr 1059**  
**November 13, 1997**  
On the  
**REORGANIZATION OF "MOLDENERGO" STATE COMPANY**

In order to fulfill the Law "On Privatization Program during 1997-1998", the Governmental Resolution nr 628, of July 8, 1997 "Concerning the approval of Electricity Sector Restructuring Plan", as well as to assure the energy security of the country, the Government of the Republic of Moldova DECIDES

1 To reorganize "Moldenergo" SC through creation of new legal independent entities as follows

State Company "Transelectro", Chisinau,

Joint Stock Company "Centrala electrica cu termoficare nr 1" (CHP-1) Chisinau,

Joint Stock Company "Centrala electrica cu termoficare nr 2" (CHP-2) Chisinau,

Joint Stock Company "Centrala electrica cu termoficare Nord" (CHP North) Balti,

Joint Stock Company "North Distribution Networks" Balti,

Joint Stock Company "North-West Distribution Networks" Donduseni,

Joint Stock Company "Central Distribution Networks" Vatra, Chisinau,

Joint Stock Company South Distribution Networks" Comrat,

Joint Stock Company "Electric Networks", Chisinau,

Autonomous Joint Stock Company for heat production and distribution "RAPDET", Chisinau,

Joint Stock Company "Aprovizelectro", Chisinau,

Joint Stock Company, Construction and Assembling Enterprise "Electron", Chisinau,

Joint Stock Company "Energoconstructie", Chisinau,

Joint Stock Company "Armo-Beton", Bac101,

Joint Stock Company "Transenergoreparatie", Chisinau,

Paramilitary State Enterprise "Scutul Energetic", Chisinau,

2 To set up the main functions of "Moldtranselectro" SC establish the balance and power capacity, centralized administration and dispatch of energy system, provide continuous transmission of electric energy through high voltage networks, maintenance of the technological regime of activity of the integrated energy system, provide necessary condition for functioning in parallel with energy systems of neighboring countries

The Activity of "Moldtranselectro" SC will be managed by the General Director, appointed through governmental decision

After the reorganization of "Moldenergo" SC, its successors will be charged with carrying out loan agreements and contracts for the purchase of fuel, equipment, materials and spare parts

During the transition period only "Moldtranselectro" SC will have the right to buy energy from local power plants During this period the distribution networks will buy energy from "Moldtranselectro" SC, as well as foreign and local wholesale independent suppliers

3 After reorganization of "Moldenergo" SC, the Department of Energetic will be fully authorized to administrate, until the privatization, the operational activity of newly economic entities

4 The Department of Energy together with the Ministry of Privatization and State Property Administration will transfer the social assets of "Moldenergo" SC to local public administration within 2 months, as specified in the attachment nr 1

5 In accordance with the effective legislation, the newly created entities will own the lands property previously used by them

6 Within a month, the Ministry of Economy and Reforms, the Department of Energy together with the energy sector's enterprises shall set up tariffs for energy production, transmission and distribution in accordance with the base tariff, established through the Governmental Decision Nr 512, of June 5, 1997 "Concerning the prices and tariffs for natural gas, electric and heat energy and measures of social protection of vulnerable population"

7 To abrogate the Governmental Decision Nr 193, of March 20, 1997 "Concerning the approval on "Moldenergo" SC Statute"

8 The control over the decision's fulfillment will be under the responsibility of Mr Ion Gutu, Deputy Prime Minister, Minister of economy and reforms

Prime Minister  
of the Republic of Moldova

ION CIUBUC

**Annex 1**  
to the Governmental Decision Nr 1059  
of November 13, 1997

List of social assets to be transfer  
to the balance of local public authorities  
[See Romanian list]

## MEMORANDUM

To J Tasillo

From I Comendant

Date March 24, 1998

Subject The status of items # 4 and # 5 of GOM 1059 issued on November 13, 1997

According with your request from MEMO of March 15, 1998 I am presenting you the report on the actual state of carrying out of GOM decision 1059, item #4 and #5, as following

**1 The social assets specified in the attachment no 1 of GOM 1059 and its status on March 23, 1998**

No	Name of social asset	Owner on 11/13/97	To Be Transferred To	Actual status
1	Kindergarten no 165	RAPDET	Mayorality of mun Chisinau	It is not transferred officially, but all the expenditures are borne by Mayorality
2	Kindergarten no 136	RAPDET	Mayorality of mun Chisinau	It is not in the balance of RAPDET From the beginning, it was in the balance of Mayorality
3	Kindergarten no 65	RAPDET	Mayorality of mun Chisinau	<b>It is considered transferred</b> , but the appropriate documents are not signed yet Mayorality made the Kindergarten into a school
4	Cultural club "Energeticianul"	South Distribution Networks, Comrat	Mayorality of mun Comrat	All the documents are prepared but not signed since it is not decided yet who the Mayor will be DisCo does not bear any expenditures
5	CHP North club	CHP North	Mayorality of mun Balti	It was not transferred They sent an appropriate letter to the Mayorality, which expressed the desire to take the club assets into their balance The matter is in process
6	The mansion, Nucarilor str , 11	RAPDET	Mayorality of mun Chisinau	<b>It was transferred</b>
7	Holiday camp "Energeticianul", Vadul-lui-Voda	CHP-2	Mayorality of mun Chisinau	It is not transferred The documents are not prepared Nobody wants to take it on his balance because it is too far from the cities and it is not attractive
8	Kindergarten no 149	CHP-2	Mayorality of mun Chisinau	<b>It was transferred</b>

Items # 4 and # 5 of GOM 1059

No	Name of social asset	Owner on 11/13/97	To Be Transferred To	Actual status
9	The mansion, Mircea cel Batrin, 42/1	CHP-2	Mayoralty of mun Chisinau	<b>It will be transferred</b> by March 28, 1998
10	The 1030 m portion of Transnistria str	CHP-2	Mayoralty of mun Chisinau	<b>It was transferred</b>
11	The foundation of mansion No 10 and 11 from Mircea cel Batrin str	CHP-2	Mayoralty of mun Chisinau	It is not transferred Nobody wants to take it on his balance because it is not attractive

Due to the fact that the terms of GOM 1059 were not respected, the Department of Energy presented a request to GOM that a new deadline for transferring Social Assets be established until the beginning of the privatization process

**2 Explanation of item # 5**

Item # 5 of GOM 1059 is not written clearly in Romanian That's why the English version creates misunderstandings about the meaning A literal translation is the following

**In accordance with the effective legislation, the lands (property) previously used by newly created entities are delivered to them for their use**

RESOLUTION 212  
February 26, 1998

On the reorganization and privatization of gas sector  
of the Republic of Moldova

In accordance with the Individual Plan for Reorganization and privatization of gas sector of the Republic of Moldova presented to the Government of Moldova to fulfill the Law regarding the Privatization program for 1997-1998, no 1217-XII dated June 25, 1997, and with the view to consolidate production and economic relations between gas enterprises to improve payments and reduce debts to Russian "Gazprom" Joint Stock Company for the gas supplied, the Parliament RESOLVES

Art 1 To authorize the Government to reorganize "Moldovagaz" concern by its merging with "Gazsnabtranzit" private JSC according to existing legislation and to create Moldovan-Russian Joint Venture (hereinafter Joint Venture)

Art 2 To determine, that during amalgamation of business, mentioned in Art 1, the contribution of the Republic of Moldova to the statutory fund of the Joint Venture will be as follows

- a) state share to the property of "Gazsnabtranzit" private joint stock company, created in accordance with the Parliamentary Resolution no 305-XIII, dated December 6, 1996,
- b) state share to the property of "Moldovagaz" Joint Stock Companies, created according to the Parliamentary Resolution no 611\_XIII, dated October 27, 1995, excepting "Inkorgaz" and "Gazproekt" Joint Stock Companies

Art 3 - In order to reduce Moldova's debts for the gas supplied, to authorize the Government to transfer to Russian "Gazprom" part of funds mentioned in p b), Art 2 as contribution to the Joint Venture's statutory fund, the "Gazprom" share being 50%

Art 4 - In case of issuance of any additional shares states ownership stake should not be less than 35% Reduction of this stake could be performed only with the acceptance of the Parliament

Art 5 - To entitle the joint stock companies, created during the privatization of gas sector (except "Inkorgaz" and Gazproekt" JSCs), to swap their shares to the Joint Venture's shares according to the current legislation

Art 6 - To charge the Government with designating persons entitled to represent the state during the creation of the Joint Venture and to observe the interests of the Republic of Moldova in the activity of Joint Venture's Board of Directors

Art 7 – In connection with the creation of Joint Venture as a result of merging “Moldovagaz” and “Gazsnabtranzit” to exempt from stamp-duty

Art 8 – To declare points 3,4 and 5 of the Annex to the Parliamentary Resolution on Individual project for reorganization and privatization of “Moldovagaz” enterprises”, no 611-XIII, dated October 27, 1995 null and void

Art 9 – Within 3 months the Government should present to the Parliament proposals on amending the effective legislation according to the present resolution

Art 10 – The control over the fulfillment of the present resolution will be performed by the Committee for economy, industry and privatization

Art 11 – The present resolution becomes effective upon its publication

Dumitru Motpan  
Chairman of Parliament

February 26, 1998  
#1556-XIII

**REPUBLICA MOLDOVA**

**CORPORATIZAREA  
ÎNTRINDERILOR  
SECTOARELOR ENERGETIC  
SI GAZE NATURALE**

**NIS Institutional Based Services  
Proiect Eficienta Energie si Reformarea Pietei  
Contract No CCN-Q-00-93-00152-00**

**Privind reformarea sectorului energetic  
al Republicii Moldova  
Delivery Order No 19**

*Raport final*

*Elaborat pentru*

Agentia SUA pentru Dezvoltare Internationala  
Departamentul pentru Europa si CSI  
Biroul Mediu Ambient, Energetica si Dezvoltare Urbana  
Directia Energetica si Infrastructura

*Elaborat de către*

Hagler Bailly  
1530 Wilson Boulevard  
Suite 400  
Arlington, VA 22209-2406  
(703) 351-0300

Septembrie 1998

Republica Moldova

**CORPORATIZAREA  
ÎNTRINDERILOR SECTOARELOR  
ENERGETIC SI GAZE NATURALE**

**Cuprins**

**Descriere Generala**

**Sectorul Energetic**

- GoM 628 “Cu privire la aprobarea Planului de Restructurare a Sectorului Energetic”, 8 iulie, 1997
- HBLX Memo “Evaluarea mijloacelor fixe ale Moldenergo”, 17 septembrie, 1997
- HBLX Memo “Argumente vizând susținerea planului de alocare a datorilor
- GoM 1059 “Reorganizarea Companiei de Stat Moldenergo”, 13 noiembrie, 1997

**Sectorul Gaze Naturale**

- GoM 212 “Cu privire la Reorganizarea și Privatizarea Sectorului Gaze a Republicii Moldova”, 26 februarie, 1998

Republica Moldova

## CORPORATIZAREA ÎNTRINDERILOR SECTOARELOR ENERGETIC SI DE GAZE

### Descriere Generala

Planul de restructurare a sectorului energetic a fost elaborat pana Hagler Bailly a început sa acorde asistenta tehnica in conformitate cu Delivery Order No 19 din 1 septembrie 1997. Compania de consultanta din Moldova – ARIA (Agentia pentru Restructurarea Întreprinderilor si Asistenta), fiind angajata de către Banca Mondiala in Octombrie 1996 a început sa studieze diverse programe de restructurare ale altor tari si sa formuleze un plan asemănător pentru Moldova in conformitate cu conditiile împrumutului pentru ajustări structurale SAL-II. După cum este mentionat in Hotărârea Guvernului 628, aprobata in iulie 1997, Guvernul a aprobat un plan sustinut de către Banca Mondiala pana la începerea activității Hagler Bailly in Moldova. Evoluarea dinamica a evenimentelor a influentat extinderea si natura asistentei tehnice ceruta de către omologii nostri in domeniul “corporatizării” sectoarelor gaze si energetice, după cum este descris in continuare.

### Sectorul Energetic

GoM 628 “Cu privire la aprobarea Planului de Restructurare a Sectorului Energetic” 8 iulie 1997 a stabilit schema de baza a restructurării sectorului energetic după cum urmează

- Trei societăți pe actiuni producătoare de energie electrica si termica situate in Moldova pe partea dreapta a râului Nistru: CET 1 si CET 2, localizate in Chisinau si CET-Nord – Bălți,
- Cinci companii de distributie deservind teritorii geografice bine determinate fiind monopoliste in prestarea serviciilor energetice: Compania de Distributie Nord (CDN), Compania de Distributie Nord-Est, Compania de Distributie Centru (CDC), Retelele Electrice Chisinau si Compania de Distributie Sud,
- O companie de stat, Moldtranselectro, ce prestează servicii de transport si de dispecerat central (având in proprietatea sa si CHE Costesti, centrala hidroelectrică cu o capacitate de 16 MW situata pe râul Prut (la frontiera cu România) si utilizata pentru a regla curba de sarcina),
- Separarea Moldenergo (caz datorat *de facto* statutului politic separat al regiunii Transnistria) de Moldova: GRES (centrala termoelectrică cu o capacitate de circa 650 MW) si de CHE Dubasari, centrala hidroelectrică cu o capacitate de 48 Mw situata pe râul Nistru (la frontiera cu Ucraina), si
- Întreprinderi auxiliare (constructie, centre de reparatii, scoli, etc )

Aceasta hotărâre stabilește, de asemenea, atât cadrul necesar pentru crearea organului regulatoriu din sector cât și procesul pentru privatizarea întreprinderilor nou create. Aceasta hotărâre a marcat angajarea Guvernului în procesul de reformare a sectorului energetic și a stabilit etapele de elaborare a hotărârilor ulterioare care au contribuit la implementarea acestui plan în general.

După cum este arătat în memorandumurile anexate, Hagler Bailly a colaborat cu ARIA pentru a acorda asistență și servicii de consultanță în evaluarea politicii pe parcursul pregătirii materialelor necesare a fi coordonate cu Ministerul Justiției în conformitate cu legislația Moldovei pentru a crea Societățile pe Acțiuni menționate în GoM 628. Elaborarea curentă a documentelor a fost efectuată de către partea moldovă dat fiind faptul că dispuneau de mai multă informație și a fost convenit de a realiza astfel această activitate.

GoM 1059 "Cu privire la reorganizarea Companiei de Stat Moldenergo", 13 noiembrie, 1997 este hotărârea prin care Guvernul autorizează și ordona stabilirea juridică a entităților separate menționate mai sus. De fapt CET-urile și DISCO au devenit Societăți pe Acțiuni odată cu înregistrarea acestora la Ministerul Justiției pe parcursul lunilor Octombrie și Noiembrie ale anului 1997, apriori aprobării oficiale a Guvernului a acestei restructurări. Înregistrarea Moldtranselectro a fost reținută până la 3 August 1998, dar până la înregistrarea acesteia și după eliberarea licențelor de către ANRE toate întreprinderile semnificative ale sectorului energetic au fost corporatizate și autorizate prin licența să presteze serviciile indicate.

### Sectorul Gazelor Naturale

În conformitate cu Hotărârea Parlamentului nr 611 din 27 octombrie 1995, pe parcursul anului 1996 Moldovagaz a creat 36 companii locale de distribuție a gazului. Suplimentar, Compania pe Acțiuni privată "Gazsnabtranzit" a fost afectată în urma transferării a 50% din sistemul gazoductelor magistrale private exploatate de către Moldovagaz unicului lor furnizor RAO Gazprom. Aceasta afacere cu Gazprom a fost o tranzacție realizată pentru a rambursa cele 140 milioane dolari datorii acumulate.

Nu mult după demararea lucrului Hagler Bailly în Moldova a fost promovat un alt plan vizând reintegrarea tuturor întreprinderilor gaze într-o singură Societate pe Acțiuni, a cărei proprietate va fi împărțită după cum urmează:

- |                               |     |
|-------------------------------|-----|
| • Republica Moldova           | 50% |
| Din care                      |     |
| • Acțiuni aparținând statului | 35% |
| • Transnistria                | 14% |
| • Manageri / angajați         | 1%  |
| • Gazprom Rusia               | 50% |

Acest plan de reorganizare a fost elaborat din cauza imposibilității Moldovei de a plăti Gazprom pentru gazul livrat pe parcursul a mai multor ani în scopul acoperirii datoriilor acumulate și pentru a evita întreruperea furnizării de gaze pe viitor de către Gazprom. Acest "plan de

privatizare” a fost aprobat de către Guvern și prezentat Parlamentului la sfârșitul anului 1997. La 26 februarie 1998 Parlamentul a aprobat hotărârea 212 “Cu privire la reorganizarea și privatizarea sectorului gaze a Republicii Moldova”. O copie a documentului vizat este anexată. Totuși, până la alegerile parlamentare din aprilie 1998 nimic nu a fost implementat, iar noul Guvern nu a activat atât de repede întru îndeplinirea acestei hotărâri. Ne dăm bine seama că Guvernul reexaminează această problemă și s-ar putea să nu dorească să implementeze acest acord.

Aceste măsuri întreprinse de guvernul Republicii Moldova și Moldovagaz au împiedicat oricare activități alternative de corporatizare, cum ar fi dezintegrarea sectorului gaze și care au fost preconizate de către Banca Mondială și USAID inițial. Din punctul de vedere al reglementării Hagler Bailly continua să coopereze cu ANRE pentru a stabili licențele și regimul de tarife ce ar reflecta o analiză funcțională a diferitelor activități din sector așa ca tranzitarea, transportul, distribuția și furnizarea gazelor. Aceste elemente importante ale reformei economice vor continua necătând la structurile corporative adoptate de către industria gaze a Moldovei.