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Energy sector privatizations in Romania

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The privatization of state-owned utilities – traditionally the ultimate bastions of state ownership in Romania – has begun. The privatization of the most important energy companies – the national oil company Petrom and the two natural gas distributors, Distrigaz Nord and Distrigaz Sud – as well as two of the eight electricity distribution and supply companies, is now under way.

So far, the privatization process has been sustained by the need to restructure the existing entities, as well by the continuous quest for the best legislative solutions. Thus, after the general privatization framework (Government Emergency Ordinance No 88/1997 on the privatization of companies) had been adopted, Law No 137/2002 was approved. This piece of legislation contains certain measures for speeding up the privatization process by the introduction of new methods of privatization, such as mixed-capital companies and the public-private partnership approach in the utilities sector.

Moreover, in relation to the electricity sector, an important step was taken in 2003 when Law no 318/2003 (the Electricity Law) was adopted. The Electricity Law implemented EU Directive 2003/54/EC dated June 26 2003 concerning common rules governing the domestic electricity market. The Electricity Law repealed Government Emergency Ordinance No 63/1998 on electric and thermal energy, and made a distinction between the regulation of activity in the field of electricity and combined heat and power and the regulation of the centralized production of thermal energy. The privatization of companies operating in the electric power sector has only been effected with respect to the electricity distribution and supply companies – that is, the subsidiaries of Electrica.

In spite of these developments, there are still some sensitive legal issues to be resolved. These issues reflect the particularities of the electricity sector privatization process, which all investors must take into account.

Legal status of the land used in the electricity sector

Certain aspects of the legal regime governing the land owned by the companies to be privatized must be clarified. The uncertainty concerns whether it is the state or the company that owns the land. Where the owner is the state, the law sets out a special procedure for the attestation of the right of ownership.

In respect of land for which certificates attesting ownership rights have not been obtained, or where such certificate is issued after privatization, the value of the land has to be included in the share capital of the respective company, and this share capital

increase shall be deemed to be a contribution in kind. The investor therefore runs thus the risk of its participation being diluted. However, if the share capital increase happens after the privatization of the company, the buyer or its successor has the right to purchase a number of supplementary shares to maintain its investments in the share capital at the same level as before the increase. The supplementary shares must be sold at face value.

Unlike ordinary privatizations, in case of Electrica's subsidiaries, the risk of facing share capital increases after privatization with the supplementary shares is likely to occur, due to the technical difficulties in obtaining the certificates attesting the right of ownership.

Existence and reduction of arrears

One of the major problems of the Romanian economy is the large amount of arrears. The state has always been in the delicate position of favouring either debtors (many of them undergoing special management programmes to become more attractive to potential investors) or creditors (which are beginning to be privatized, as it is the case with the electricity suppliers).

This situation has had a great impact on the financial status of electricity distribution and supply companies. For instance, they have had to agree, and stick to, rescheduling plans with their creditors in respect to their debts. Another solution aimed at balancing the interests of debtors and creditors was to swap the debts into shares, to be acquired by the utilities' suppliers.

Recent measures taken to reduce economic arrears were implemented by Urgent Government Ordinance No 37/2004. Of particular note is the cancellation of the penalties owed by consumers of electricity, heat, water and natural gas who have delayed paying their current and outstanding obligations. However, it also states that consumers of electricity, heat, water and natural gas that fail to pay their current obligations, and any obligations resulting from payment rescheduling plans, will be disconnected and remain so until the payment of such obligations.

As regards the two electricity companies under privatization, the above ordinance envisages a mechanism for the reduction of their non-paid receivables, whereby their outstanding commercial receivables will be transferred, up to a certain amount, to the Authority for the Recovery of State Assets. In exchange, the Ministry of Public Finance will issue, within 45 days from the date of the transfer protocol, state bonds on the domestic market of a total value equivalent to the transferred receivables. The amounts collected from the issuance of such state bonds shall be transferred by the Ministry of Public Finance to Electrica in satisfaction of the debts owed by Electrica Banat and Electrica Dobrogea to Electrica. Electrica shall use the amounts received to pay the outstanding debts it owes to the energy producers Termoelectrica and Nuclearelectrica. Subject to the success of this system, it is highly possible that it will be applied also to the other six electricity distribution and supply companies undergoing privatization.

Maintenance and service companies

Another aspect of the privatization process is the existence of the eight maintenance and service companies, which are branches of Electrica. Such branches have the exclusive right to provide maintenance and services to Electrica for a period of five years from their establishment – in other words, until 2007. This aspect is noteworthy because one of the core elements of the privatization negotiations may be the elements comprised in these service agreements entered into between the subsidiaries and their shareholder, Electrica.

Legislative instability

The privatization of the Romanian energy sector has just begun. The success of the process depends on the sound acknowledgement of all the legal issues involved. So far it appears that the authorities managed to address some of the problems after the process was started to satisfy investments, but the general impression is that legislative instability has once again been favoured, to the detriment of investors.

Banking

Recommended firms

Linklaters Miculiti & Asociatii

Nestor Nestor Diculescu Kingston Petersen

Musat & Asociatii

Stoica & Asociatii

Zamfirescu & Partners

CMS Cameron McKenna Cristina Brinzan Law Office

Gide Loyrette Nouel

Haarmann Hemmelrath

Mihaela Grama-Popovici Law Office

Rubin Meyer Doru & Trandafir/Herzfeld & Rubin

Schönherr Rechtsanwälte

Studio Legale Tonucci

Capital markets

Recommended firms

Linklaters Miculiti & Asociatii

Musat & Asociatii

Nestor Nestor Diclescu Kingston Petersen

Mihaela Grama-Popovici Law Office

Schönherr Rechtsanwälte

Stoica & Asociatii

Zamfirescu & Partners

CMS Cameron McKenna Cristina Brinzan Law Office

Haarmann Hemmelrath

Rubin Meyer Doru & Trandafir/Herzfeld & Rubin

Mergers and acquisitions

Recommended firms

Linklaters Miculiti & Asociatii

Nestor Nestor Diclescu Kingston Petersen

Babiuc Sulica & Associates

CMS Cameron McKenna Cristina Brinzan Law Office

Musat & Asociatii

Rubin Meyer Doru & Trandafir/Herzfeld & Rubin

Despina Fruth Oprisan Law Offices

Haarmann Hemmelrath

Mihaela Grama-Popovici Law Office

Schönherr Rechtsanwälte

Project finance

Recommended firms

CMS Cameron McKenna Cristina Brinzan Law Office

Linklaters Miculiti & Asociatii

Musat & Asociatii

Nestor Nestor Diclescu Kingston Petersen

Schönherr Rechtsanwälte

CMS Cameron McKenna Cristina Brinzan Law Office

Cristina Brinzan's team of three partners and 14 associates in Romania is a highlight of CMS's central and eastern European network. The office is recommended in all practice areas but is particularly noted for its corporate work, especially for private equity houses and venture capital funds.

This capability has been further enhanced in the last year by the arrival of formerly London-based corporate partner Stephen Forster in the Bucharest office. Forster has a wide experience of corporate finance that encompasses a speciality for project finance work. He advised the winning bidder for the London Underground public-private partnership, one of the most complex UK deals of the last few years.

The firm worked on the first public-to-private leveraged buyout in Romania – Advent International's takeover of Romanian pharmaceuticals company Terapia. It also advised the Constanta County Council on the privatization of its water and sewerage services, the largest such deal outside of Bucharest. In banking, CMS advised Crédit Lyonnais and TriGránit on two facilities totalling €98 million (\$118 million).

Key contact partner

Cristina Brinzan

Gide Loyrette Nouel

Bruno Leroy is French firm Gide's resident partner in Romania, and has been the head of the office since it opened in 1998. He has worked on many of the country's privatizations, including acting for Renault on the purchase of Dacia, the country's leading car distributor and retailer.

The firm is strong on banking advice. It worked on the first syndicated credit facility governed by Romanian law to do without a state guarantee – the €50 million (\$60.5 million) loan to hypermarket operator Hiproma from a syndicate led by ING. In mergers and acquisitions, Gide's stand-out deal was Renault's takeover of Dacia, which was one of the first mandatory takeover public offers to be successfully completed on the Bucharest Stock Exchange. The firm was also involved with the modification of the Romanian Securities Act that made takeovers of this type possible in Romania.

Key contact partner

Bruno Leroy

Linklaters Miculiti & Asociatii

The Bucharest branch of Linklaters, managed by partner Michael Tétreault Schilling, is a market leader for capital markets work, a fact illustrated by the firm's work on all of the Romanian government's eurobond issues so far. It also acted on Termoelectricas' €150 million (\$181 million)

eurobond issue, the first ever non-state entity to enjoy the state's guarantee. Schilling himself is highly recommended for this work, as is head of banking and finance Adrian Catalin Buboaca. Another well-regarded personality in the office is Delia Simona Pachin, the head of the energy and natural resources department.

Most of Schilling's time is taken up with corporate and privatization work. He has represented the Romanian government on several privatizations, including its largest one to date – the \$500 million privatization of Sidex, Romania's largest steel company.

More recently, the firm has advised the Ministry of Industry and Resources on the privatization of Romania's national oil and gas company, SNP Petrom, and Romania's two national gas distributing companies, Distrigaz North and Distrigaz South – two of the largest privatizations in central and eastern Europe last year. Linklaters also advised OTE International Investments on its acquisition of the Romanian national telecommunications company, Romtelecom, and GeCAD Software on the disposal of its antivirus arm to Microsoft. Lastly, the firm recently advised Deutsche Bank and ABN AMRO on financing an acquisition agreement between the UK Ministry of Defence and the Romanian Ministry of Defence over the transfer, regeneration and modernization of the former Royal Navy Frigates Coventry and London.

Key contact partner

Michael Tétreault Schilling

Leading lawyer

Michael Tétreault Schilling

Musat & Asociatii

One of the largest, oldest and best-established law firms in Romania, Musat is the benchmark by which all other firms measure their share of the market. The firm has 11 partners and 65 associates in Bucharest and hired six new associates in the banking department alone last year.

Cornel Popa, who joined the firm from competitors Babiuc Sulica a couple of years ago, is highly recommended by his peers and the firm has just made him up to partner by the firm.

Musat is one of the country's leaders for capital markets work in terms of the quality of its advice. Last year it advised Banca Transilvania on a share capital increase with the help of the European Bank for Reconstruction and Development. It also advised LNM Holding on a voluntary delisting, helped the Bucharest Stock Exchange with several regulatory issues and advised the National Securities and Exchange Commission on its compliance with national legislation.

Musat is also strong in mergers and acquisitions, and was involved with General Electric's joint venture with Turbomecanica in the jet propulsion industry. Partner Gheorghe Musat heads the M&A practice.

Key contact partners

Stefan Damian
Gheorghe Musat
Florentin Tuca

Leading lawyer

Cornel Popa

Nestor Nestor Diculescu Kingston Petersen

Linklaters Miculiti & Asociatii and Nestor Nestor Diculescu Kingston Petersen are the two strongest players in Romania. And although Nestor does not have the advantage of an international link or the experience of foreign-qualified lawyers in its ranks, it more than holds its own.

The firm was involved with the privatization of Fibrex, the national manufacturer of synthetic fibres, acting for RadicNylon, the buyer and a member of the Radici Group in Italy. In project finance it has been involved in several of the country's largest projects, including steel producer Sidex's revolving credit facility. The firm acted as local counsel to CSFB and Banque Paribas. Nestor has represented several other international banks, including Merrill Lynch, which it advised on the structuring of a debt and equity offering in Romania.

Key contact partner

Ion Nestor

Leading lawyer

Ion Nestor

Rubin Meyer Doru & Trandafir

in association with Herzfeld & Ruben

Wall Street firm Herzfeld & Ruben has offices in New York, Los Angeles, Miami, Wolfsburg (Germany) and Romania's capital Bucharest, where it operates under the name of Rubin Meyer Doru & Trandafir. The Romanian office has four partners and 10 associates, and two of the partners are US-qualified.

Internationally Herzfeld & Ruben specializes in corporate work, and Bucharest is no different. The office has been involved in four of the seven largest privatizations in Romania since 1989. The biggest was the acquisition of telecommunications operator RomTelecom, at the time the largest ever foreign investment in the country. It also worked on the acquisitions of Romania's largest refinery, the largest metals plant and one the biggest cement manufacturers.

Key contact partner

Sergiu Doru

Schönherr Rechtsanwälte

The Bucharest office of Austrian firm Schönherr is strong for banking, capital markets and project finance, in fact all

finance work. It advised Raiffeisen Bank and Bear Stearns on the lending facilities required for building the M6 motorway, acted for the Romanian Commercial Bank on several cross-border transactions and advised Deutsche Bank on a number of investments in Romania over the last year.

In project finance it can count Italian tyre-maker Pirelli, Austrian public utility EVN and DaimlerChrysler among its clients, and has been involved with many of Romania's largest motorway and utilities projects.

Key contact partner

Christof Lindinger

Zamfirescu & Partners

Name partner of this well-respected local firm, Calin Zamfirescu, is highly regarded in the Romanian legal market as an able and experienced corporate finance lawyer. The firm often advises HVB Bank Romania on financing deals and last year worked on three such transactions, including the financing of the Autonomous Regies of Romania, which are managed by local councils. It has also worked on several capital markets transactions for HVB, and last year advised Banca Romana Pentru Dezvoltare, part of the Société Générale group, on a bond issue.

In insolvency and restructuring Zamfirescu's most notable recent work was done acting for the liquidator on the insolvency and liquidation of Bankoop.

Key contact partner

Calin Zamfirescu

Leading lawyer

Calin Zamfirescu