

## **Report of the Group of Observers**

### **Procurement of electricity in Moldova (2017)**

#### **I. Background**

Given the limited size of the market and the strong political involvement, annual electricity procurement by suppliers, transmission and distribution companies in Moldova has been suffering from a lack of transparency and allegation of collusion between traders and generators. As a transitional measure on the long way to establishing an open and organized wholesale market, the Energy Community Secretariat (“the Secretariat”) drafted Guidelines for the Annual Procurement of Electricity to be used in the 2017 procurement (“the 2017 Guidelines”).

The 2017 Guidelines were meant to steer the process of identification of the most economical source of electricity to cover both the demand of the regulated suppliers and the losses of the transmission and distribution companies. The 2017 Guidelines are based on the principles of transparency, non-discrimination and wide publicity, which should be the pillars of any competitive bidding process. They are also based on the existing legal framework in Moldova and on the Energy Community *acquis*.

Interested parties (state authorities, electricity operators) were consulted during the drafting process.

The final draft of the Guidelines was sent to the Ministry of Economy of Moldova on 21 December 2016.

On 5 January 2017, the Ministry of Economy issued an order, which approved the 2017 Guidelines (“the Ministry’s Order”). The Ministry’s Order recommended that the transmission system operator, the distribution system operator and the regulated suppliers comply with the 2017 Guidelines during the process of procurement of electricity for 1 April 2017 – 31 March 2018.

#### **II. The Role of the Group of Observers**

The 2017 Guidelines provided for the creation of a Group of Observers whose task was the monitoring of the procurement procedure. The members of the Group of Observers were the representatives of Moldovan energy regulator ANRE, the Ministry of Economy in Moldova, the Secretariat, the EU Delegation to Moldova and the EU High Level-Advisor for Energy Policy.

The task of the Group of Observers was to make its best efforts to ensure that the principles of equity, transparency and non-discrimination were respected throughout the procurement process, rather than to guarantee the legality of the procurement procedure.

The observations of the Group of Observers (both from the present report or from various communications during the procurement procedure) are solely based of the information made available to members of the Group of Observers either by the Ministry of Economy or by the companies involved in the procurement procedure. The Group of Observers did not have the means to check the accuracy of the information received.

#### **III. The 2017 electricity procurement procedure**

The 2017 Guidelines provided for a tender procedure to be followed by all the companies which needed to procure electricity. The procurement procedure needed to be concluded by 31 March 2017. As presented below, the initially envisaged calendar was not respected in the end, due to numerous extensions of deadlines.

### **1. *The invitation to express interest in tender***

All companies have published on their website or sent to a number of suppliers an invitation to express interest in tender. The invitation contained a template for a letter of intention to be submitted by interested parties, as well criteria to be fulfilled and documents to be supplied by them. This was the only stage of the procurement procedure in which no delays occurred.

### **2. *The identification of potential suppliers and the qualification process***

As a next step, and based on the responses received to the invitation launched in accordance with point 1 above, the companies were tasked with the preparation of a list of qualified suppliers, i.e. suppliers which complied with the criteria mentioned in the invitation to express interest.

*Gas Natural Fenosa* informed the Group of Observers on 27 January that they received letters of interest, accompanied by supporting documentation, from *Energocom*, *MGRES* and *DTEK Pavlogradugoli*. Upon review of those documents, the Secretariat, the EU Delegation and the EU High Level-Advisor for Energy Policy submitted questions and requests for additional documents. Not all the queries were answered by the companies. For example, *MGRES* provided only a license valid for 6 months (instead of minimum one year as required by the 2017 Guidelines). This seems to be related to a provision of Moldavian Law which does not allow companies from Transnistria to be licensed for more than 6 months. *Energocom* failed to specify the source of electricity or evidence about access to electricity or power to execute the transaction, arguing they are still negotiating with several providers. On 3 February, *Gas Natural Fenosa* communicated that its final list of potential suppliers was formed by *Energocom*, *MGRES* and *DTEK Pavlogradugoli*.

*Moldelectrica* informed the Group of Observers on 6 February that it had received less than three letters of intention within the initially-established deadline (3 February), so it decided to extend the deadline with one week.

*FEE-Nord* informed the Group of Observers on 7 February that it received three letters of intention by 6 February, namely from *Energocom*, *MGRES* and *Energokapital*. The supporting documentation submitted by *Energocom* and *MGRES* was, however, incomplete; among others, the Group of Observers was not provided with proof that *Energocom* had no debts to the state budget and that *MGRES* had a license for production of electricity valid for at least one year. On 16 February the Secretariat submitted a list with missing documents, but it was not provided with any of them.

*RED Nord-Vest* received letters of intention from *Energocom*, *MGRES* and *DTEK Pavlogradugoli*. Upon review of the documentation, the Secretariat submitted a list of queries on 22 February. Among other problematic issues, at that point in time neither *MGRES* nor *DTEK Pavlogradugoli* submitted declarations that they comply with the Moldovan Electricity Market Rules, and *Energocom* did not submit information regarding the source of electricity. No answer was provided to the Secretariat's questions.

*RED Nord* also received letters of intention from *Energocom*, *MGRES* and *DTEK Pavlogradugoli*. *Red Nord* failed to properly inform the Group of Observers about its list of potential suppliers. The GO received some information from them for the first time in the meeting of 24 February.

### **3. Launching the request for bids and reception of offers**

In this step of the procedure, the Ministry of Economy started to involve itself repeatedly.

During a meeting that took place on 24 February, the Minister of Economy requested the companies to postpone the deadline for reception of offers with two weeks, until 16 March. The reason given by the Minister of Economy was that more clarity was needed with regard to the conflict in Ukraine and whether or not Ukraine could be considered a secure source of electricity. All the companies involved agreed on the extension.

Already early in March it became obvious that the procurement procedure was being delayed, and that some of the companies considered skipping some stages of the procedure altogether (e.g. the price negotiations envisaged after the bid opening).

On 13 March the Secretariat issued a letter to the Minister of Economy, urging the Moldovan authorities to respect their commitments and to conduct the procurement procedure in accordance with the principles of transparency and non-discrimination. The letter was co-signed by the EU Delegation representative and the EU High Level-Advisor for Energy Policy.

On 14 March another meeting took place at the Ministry of Economy in Moldova. As the meeting was announced only a few hours in advance, representatives of the Secretariat could not attend. The meeting was attended, however, by representatives of the EU Delegation and the EU High Level-Advisor for Energy Policy. During the meeting, the Minister of Economy requested yet another extension of the deadline for submission of offers, this time until 27 March. Among the arguments mentioned by the Minister in support of his request was the energy crisis in Ukraine originating from Donbass region, and that allegedly no offers will be received by any of the companies (even though, at that point, the deadline had not expired) and that during the following week a delegation from the Moldovan Government would make a visit to Ukraine to further discuss security of supply issues.

As the previous contract for procurement of electricity expired on 31 March 2017, the extension of the deadline until 27 March left little time for a proper evaluation of the offers and a separate phase of negotiations. Furthermore, it was proposed during the 14 March meeting that bidders could submit their offers by email and fax as opposed to sealed envelope. The Secretariat, in an email dated 15 March, generally agreed that extension of the deadline is possible under the 2017 Guidelines. However, the Secretariat opposed giving the bidders the option to submit their offers by email or fax, or by any other means than sealed envelope.

All companies with the exception of *Gas Natural Fenosa* agreed to postpone the deadline for the receipt of the offers until 27 March. *Gas Natural Fenosa* held a meeting of the committee for reception and opening of the offers on 16 March, as initially scheduled. However, only *DTEK Pavlogradugoli* was present with an offer in the *Gas Natural Fenosa* offices in Barcelona, as initially envisaged. Both *Energocom* and *MGRES* had informed the company already on 15 March (one day after the meeting organised by the Ministry of Economy) that they are not in a position to submit their respective offers until 27 March. As a result, *Gas Natural Fenosa* also decided to

postpone the deadline until 27 March, arguing that it was trying to obtain competition and that therefore hoping to receive more than one offer.

On 24 March, the Group of Observers was informed of another extension of the deadline for reception of offers, this time until 30 March. The extension came as a result of letters by *DTEK Pavlogradugoli* and *Energocom* that they will not be ready to submit an offer by 27 March, and by another recommendation by the Ministry of Economy that the date for reception of offers be extended until 30 March. The representative of the EU Delegation to Moldova raised concerns regarding the transparency and reliability of the procurement procedure. The Secretariat stated that, in its view as well, transparency and reliability of the procedure were jeopardised by the continuous postponement of deadlines. It further asked the Ministry of Economy for a detailed assessment of any alleged security of supply risk and a report on the negotiations between Moldova and Ukraine. No response came from the Ministry, which deemed the request inappropriate.

Because of this latest postponement, *Gas Natural Fenosa* had to move the place of receipt of offers from Barcelona to Chisinau, allegedly because the contracts with the winner/s should have been finalised until 31 March at midnight, and for practical reasons everything should have been done in one place.

On 30 March in the morning, the Ministry of Economy sent a letter to all companies organizing auctions requesting to postpone the deadline again until 31 March. The reason for the Ministry's request were letters from *DTEK* and *Energocom* who was still determining which would be the most advantageous source of electricity and therefore could have not submitted their offers on time. *MGRES* was the only company which submitted an offer to *Gas Natural Fenosa* on 30 of March. During the meeting, it was decided by the representatives of *Gas Natural Fenosa* that the deadline would be postponed one last time, until 31 March. Both the Secretariat and the EU Delegation reacted to this postponement and expressed their hope that the procedure would not be rushed because of the short time available, and that transparency and non-discrimination should prevail.

No offers were received by the other companies organizing auctions.

#### **4. Evaluation of offers**

Representatives of the EU Delegation, the EU High Level-Advisor for Energy Policy and the Secretariat (via video-conference) monitored the opening and evaluation of the offers on 31 March in *Gas Natural Fenosa's* headquarters in Chisinau.

On 31 March *Gas Natural Fenosa* received valid offers from *MGRES* and *Energocom* (offering electricity purchased from *DTEK Pavlogradugoli*). *MGRES* initially offered a price of \$ 58.5 per megawatt hour, which was lowered to \$ 54.4 per megawatt hour during the second round of the auction.

The winner was *Energocom*, which agreed to a price of \$ 50.2 per megawatt hour after having offered \$ 54.5 per megawatt hour in the first round of the auction. *Energocom's* offer had a clause of quarterly indexation of the price with the electricity wholesale market price in Ukraine. In addition, tougher conditions for advance payments were included in *Energocom's* offer. To make the two offers comparable (*DTEK Pavlogradugoli* and *Energocom*), *Gas Natural Fenosa* considered an extra \$ 0.4 – 0.7 per megawatt to be added at *Energocom's* offered price, only for comparison. Still *Energocom* remained the cheaper source for electricity.

On 31 March, the other companies received an initial offer from *Energocom* with the price of \$ 54.5 per megawatt hour and after *Gas Natural Fenosa's* auctions were concluded at \$ 50.2 per megawatt hour an improved offer of the same lower price was sent to them by *Energocom*. Finally, *Energocom* was declared the winner in all auctions.

#### **IV. Progress compared to previous electricity procurement procedures**

Compared to the procedure from the past years (or rather the lack thereof), the Group of Observers took note of a number of positive developments:

1. The 2017 Guidelines significantly improved the procurement procedure in a situation where only two external sources of supply exist, the Ukrainian Power Market and *MGRES*;
2. The Ministry of Economy was open to the idea of having an open, competitive procedure and adopted the 2017 Guidelines through an order;
3. The Ministry of Economy proved rather active and responsive during the procurement procedure;
4. According to the information provided, no more offshore companies acting as intermediaries were involved in the 2017 tender;
5. In the second round of price negotiations, there was real competition between *Energocom* and *MGRES*;
6. The state-owned companies, perhaps not so well trained in competitive market practices, had to make an effort to comply (at least partially) with the 2017 Guidelines;
7. The media reported on the 2017 Guidelines and the citizens were informed that the procedure was being monitored by a group formed by, *inter alia*, international organisations.

#### **V. Challenges**

However, there is serious room for improvement for the next annual procurement procedure.

The 2017 electricity procurement procedure had a number of important flaws, among which:

1. Press reports suggest that information was leaked (for example, media reported already in January 2017 that Moldova is interested in buying electricity from Ukraine; also, on 28 March they were announcing that *DTEK* would supply electricity to Moldova as of 1 April). Such reports create a suspicion that high-level negotiations and dealings were taking place in parallel to the procurement procedure;
2. There is a general lack of clarity on the reasons why *DTEK* was planning to bid in its name (and did so on 16 March for *Gas Natural Fenosa*) but finally decided not to submit directly an offer on 30 March;
3. Many of the questions and requests for information of the Group of Observers from the initial phases of the procedure remained unanswered;
4. The regulatory authority ANRE showed no interest or activities within the Group of Observers, despite it was meant to play a central role in monitoring the process;
5. The deadline for receiving the offers was postponed several times, up until the previous contract almost expired. This put a great pressure on the ones conducting the procedure and assessing the offers, since everything had to be done within hours;

6. The Ministry of Economy had a multiple role in the procedure: sending recommendations to postpone the deadlines, negotiating with the Ukrainian counterparts, sending letters not always clearly separable from the interests of *Energocom*, and acting as a member of the Group of Observers;
7. The companies were somehow weak in front of the Ministry of Economy and of the bidders, accepting to postpone deadlines continuously as requested.

## **VI. Recommendations**

Compared to the previous years, the 2017 electricity procurement process has shown significant steps forward made by both the state authorities and the companies.

At the same time, there is significant room for improvement. Looking forward to the 2018 electricity procurement procedure, a few recommendations can be formulated already at this stage:<sup>1</sup>

1. *Energocom* is a state-owned trader, which puts it at a significant advantage in relation to other competitors in a tender procedure largely organised, influenced and monitored by the state. Such situations should be avoided in the future, at least by adding enhanced transparency rules, incorporating Chinese walls in their governance and/or clear exclusion criteria in the tender documentation. Intermediaries such as *Energocom* and their electricity acquisition and contracts should be subject of the Group of Observers monitoring.
2. Postponements of deadlines should be initiated by the contract-awarding companies and not by the Ministry. Any postponement may not happen arbitrarily and with the effect of confusing participants or putting them under time pressure. Any changes in the time-table should be well-justified, limited to circumstances not foreseeable at the time of setting the deadlines, transparent and non-discriminatory;
3. All the questions from the Group of Observers should be answered within the respective deadlines;
4. Given its active role and interests in the procurement procedure, the Government should not be part of the Group of Observers;
5. The creation of a coupled electricity market between Ukraine and Moldova in accordance with the Energy Community rules and best practices should take center stage in the discussions during 2017.

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<sup>1</sup> Based on the 2017 experience, the Secretariat, in cooperation with the EU Delegation and the EU High Level-Advisor for Energy Policy, will prepare a list of amendments to the 2017 Guidelines, which will be proposed for adoption to the Moldovan authorities.