EUROPEAN COMMISSION

Brussels, 27.04.2010
C(2010)2532 final

Subject: **State aid N 691/2009**

               Hungarian stranded costs compensation scheme

Sir,

1. PROCEDURE

(1)   Following pre-notification contacts, the Hungarian authorities notified the above-mentioned aid measure pursuant to Article 108 (3) of the Treaty on the Functioning of the European Union (hereinafter referred to as the TFEU) by electronic notification dated 15 December 2009, registered with the Commission on the same day.

(2)   The Hungarian authorities submitted additional information on 28 January, 5 March and 10 March 2010, by letters registered on the same days.

2. DESCRIPTION OF THE MEASURE

2.1. Background

(3)   Since the mid-nineties, a large part of the electricity produced in Hungary was purchased by the publicly owned electricity wholesaler Magyar Villamos Művek Zrt. (hereafter referred to as "MVM") from several power generators via long-term Power Purchase Agreements (hereafter referred to as the "PPAs"). These agreements were signed between 1995 and 2001 for durations ranging from 15 to 27 years.

(4)   The PPAs reserved all or most of the generation capacities of the power plants that they covered for MVM, on which the PPAs imposed the obligation to buy minimum quantities

Őexcellenciája Dr BALÁZS Péter
Külügyminiszter
Bem rakpart 47
H - 1027 BUDAPEST

of electricity from each of these plants, at a price covering all justified variable and fixed costs, including a return on capital.

(5) On 4 June 2008, in case C-41/2005 *State aid awarded by Hungary through Power Purchase Agreements*[1], the Commission found that these PPAs involved State aid incompatible with the internal market as of 1 May 2004[2] (hereinafter referred to as the "PPA Decision"). The Commission required Hungary to refrain from granting that State aid and to recover the illegal and incompatible State aid already received by the beneficiaries since 1 May 2004. For the purposes of calculating the amounts to be recovered from the beneficiaries, Hungary was required to resort to a simulation model of the Hungarian wholesale electricity market.

(6) On 10 November 2008, the Hungarian Parliament endorsed a law[3] mandating the early termination of the PPAs by 31 December 2008. The law also provides for the establishment of a stranded costs compensation scheme for the power generators affected by the termination of the PPAs. The notified scheme is aimed at implementing this latter provision.

2.2. The notified stranded costs compensation scheme

2.2.1 General principles of the notified scheme

(7) The notification contains a draft Decree which is intended to be adopted once the notified scheme has been approved by the Commission. Its main elements are described below.

(8) The notified scheme aims at compensating three power generating companies for stranded costs arising from investments in power plants built before the liberalisation of the electricity market that were covered by a guarantee of operation and remuneration offered by the PPAs. As a consequence of the new liberalised electricity market in which the power generating companies operate as well as of the early termination of their PPAs and the obligation to reimburse the aid illegally received through these PPAs since 1 May 2004[4], the past investment decisions of these undertakings have become uneconomical: their investments are expected not to be recouped through the revenues generated by the operation of the power plants. The stranded costs correspond to the difference between the investments costs concerned and the operating profits generated by the power plants in the past and expected to be generated in the future until the expiry dates of the PPAs as initially foreseen in those PPA agreements[5].

(9) The beneficiaries of the notified scheme are:

- Budapesti Erőmű ZRt, a subsidiary of Electricité de France,

- Dunamenti Erőmű ZRt, a subsidiary of Gaz de France Suez,

- Pannon Hőerőmű ZRt, a subsidiary of Dalkia, whose shareholders are Veolia Environnement, which holds a 66% stake, and Electricité de France, which holds a 34% stake.

---

[1] OJ L 225, 27.8.2009, p. 53.
[2] The date when Hungary joined the EU.
[3] Act LXX of 2008
[4] This obligation seeks to put the power generators concerned in an economic situation equivalent to that in which they would have found themselves in the absence of the aid embedded in the PPAs as of 1 May 2004.
[5] The dates at which the PPAs would have expired in the absence of the Commission decision and national legislation mentioned in section 2.1.

(10) The implementation of the notified scheme will be a two-stage process to assure that the compensation does not go beyond the real eligible stranded costs. At the first stage, once the notified scheme has been approved by the Commission, the beneficiaries will receive an amount of aid as described in section 2.2.2 below, which is a compensation for their eligible stranded costs. Subsequently, for each beneficiary, the Hungarian authorities will monitor the operating costs and revenues related to the power plants concerned until the originally foreseen expiry date of the PPAs previously covering those plants[6]. At the second stage, which will take place for each beneficiary once the originally foreseen expiry date of its PPAs has been reached, the Hungarian authorities will recalculate the stranded costs of the undertaking on the basis of the real cost and revenue data collected in the course of the monitoring process and as the case may be, they will require this undertaking to repay part of the aid received at the first stage of the process. More detailed information is provided on this "claw-back mechanism" in section 2.2.3 below.

(11) It follows that the overall aid amount received by one beneficiary on the basis of the notified scheme will be the difference between the aid amount received at the first stage of the process and the amount reimbursed in the context of the claw-back mechanism which will take place at the second stage of the process.

(12) Furthermore, the Hungarian authorities intend to synchronise the first stage of the implementation of the notified scheme, as described above, and the recovery of illegal and incompatible State aid pursuant to the PPA Decision. In practice, if the difference between the amounts to be recovered pursuant to the PPA Decision and the amount of aid granted in application of the first stage of the notified scheme is positive, the undertakings concerned have to pay the difference to the State.

(13) If this difference is negative the Hungarian authorities have decided that the State will not make any payment to the company. In that case, the company will not have to make any payment to the State budget because the amount of aid that it could receive in application of the first stage of the notified scheme will exceed the amount to be recovered pursuant to the PPA Decision.

(14) Therefore, the granting of aid at the first stage of the notified scheme will take the form of a reduction in the amounts recovered from the beneficiaries in application of the PPA Decision, but will never give rise to cash payments from the State budget. The granting of stranded cost aid will be conditional on the effective recovery of illegal State aid pursuant to the PPA Decision since the beneficiaries will receive no aid under the notified scheme without simultaneous execution of Commission's recovery decision.

2.2.2 *Calculation of the stranded costs and the aid amount granted at the first stage of the process*

(15) The calculation methodology of the stranded costs and the aid amounts has been developed by London Economics, a consultancy hired by the Hungarian authorities, and adjusted by the Hungarian Energy Office[7]. London Economics has also developed the market simulation used to calculate the amounts to be recovered pursuant to the PPA Decision.

---

[6] When a company was covered by several PPAs with different termination dates, the most remote amongst these dates will be taken into account.
[7] The Hungarian Energy Office is Hungary's independent regulatory authority for the electricity market. The designation of such bodies is imposed on Member States by Article 23 (1) of Directive 2003/54/EC of the European

(16) The stranded costs of each of the beneficiaries have been computed as the difference between the two following terms cumulated over time:

  – the first term is the current value on 31 December 2009 of the "justified investment costs" incurred by the beneficiary in relation to the power plants previously covered by PPAs.

  – the second term, is the sum of the present value on 31 December 2009 of 1) the cash flows generated by the operation of these power plants in the past; 2) the cash flows expected to be generated in the future until the originally foreseen expiry date of the PPAs; and 3) the net present value on 31 December 2009 of the future book value of these power plants at the originally foreseen expiry date of the PPAs.

(17) As for the first indent above, the "justified investment costs" are the initial investment costs incurred before Hungary's accession to the EU on 1 May 2004, as well as subsequent investments that were undertaken before but not completed on 1 May 2004 and could not be profitably called off, and investments that were undertaken after 1 May 2004 because they were absolutely necessary for the continued operation of the plants, notably for safety reasons or to ensure compliance with environmental regulations. These investment costs are then updated to their current value on 31 December 2009 by multiplying them by the rate of return of the company (company's weighted average cost of capital) and the inflation factor.

(18) As for the second indent above, the cash flows related to the company's core business (electricity and heat sales and energy ancillary services) are calculated as the sum of three elements:

  – The current value on 31 December 2009 of the past cash flows (up to 2008), which are computed as the difference between the revenues from the sales of electricity, thermal energy, and system services and the costs of operation, while also taking into account the tax effect. The current value is then obtained by multiplying the past cash flows by the company's rate of return and the inflation factor.

  – The discounted value on 31 December 2009 of the expected future cash flows, discounted by the company's rate of return and inflation factor and calculated as follows:

    ▪ First, the cash flows related to electricity sales for the period 2009-2011 are calculated on the basis of the simulation model used by the Hungarian authorities in the context of the implementation of the PPA Decicion[8], while also taking into account the tax effect of depreciation. The cash flows arising from the sales of thermal energy and system services are calculated on the basis of historical ratios between the sales of thermal energy (respectively, system services) and the sales of electricity. In the case of system services, historical capacity fees resulting from the tenders organised by the Transmission System Operator for ancillary services are

---

Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC (OJ L 176, 15.07.2003, p. 37).

[8] See point 5 above

also taken into consideration to forecast future revenues from system services.

- ▪ Second, for the years following 2011, the simulation model was not used because of too many uncertainties surrounding market conditions in that remote period, which would have rendered the results of the simulation unreliable. Therefore the Hungarian authorities have used the simulated cash flow for year 2011 and replicated it until the originally foreseen expiry date of the PPAs.

- − The company's book value at the originally foreseen expiry date of the the PPAs following normal depreciation rules, discounted on 31 December 2009.

(19) The maximum amount of stranded costs for each beneficiary is defined as the algebraic sum of the maximum amounts of stranded costs of all assets covered by the PPAs. The stranded costs resulting from those calculations are set out in Annex 4 of the Draft Decree for each beneficiary (see column B of table 1 below). These "stranded costs" have been calculated without account being taken of the fact that part of the past revenues obtained by the beneficiaries constitute illegal State aid that will be reimbursed pursuant to the PPA Decision. Therefore, the eligible stranded costs for which each beneficiary could be compensated, taking into consideration the forthcoming reimbursement of illegal State aid, is the sum of the (positive or negative) stranded costs amounts set out in Annex 4 and the amounts to be recovered pursuant to the PPA Decision (see columns C and D of table 1 below).

(20) However, as indicated at point 13 above, the Hungarian authorities have decided not to fully compensate these eligible stranded costs in all cases: in cases where they exceed the amounts to be recovered pursuant to the PPA Decision, the State will not pay to the company the difference between these two amounts.

(21) The aid amount granted to each beneficiary at the first stage of the implementation of the notified scheme will thus be equal to or lower than the eligible stranded costs. These aid amounts are provided in column E of the following table.

Table 1: Aid amounts granted at the first stage of the implementation of the notified scheme

Company (amounts in thousand HUF)	Maximum amounts of stranded costs as set out in Annex 4 of the draft Decree	Recoverable amounts of aid pursuant to the PPA Decision	Eligible stranded costs	Aid amounts granted at the first stage of the implementation of the notified scheme
A	B	C	D = B +C	E
Budapesti Erőmű ZRt	89 209 966	44 203 608	133 413 574	44 203 608
Dunamenti Erőmű ZRt	22 171 991	125 352 538	147 524 529	125 352 538
Pannon Hőerőmű ZRt	3 936 511	9 398 827	13 335 338	9 398 827
Total	**115 318 468**	**178 954 973**	**294 273 441**	**178 954 973**

(22) It should be noted that all three companies fall within the situation described at point 13 above: the aid amounts that they will receive at the first stage of the scheme are lower than the eligible stranded costs resulting from the calculation methodology developed by Hungary.

2.2.3 *Monitoring and claw-back mechanism*

(23) According to Article 14 of the draft Decree, the Hungarian Energy Office will monitor the real cash flows generated by the operation of the assets originally covered by the PPA between the entry into application of the notified scheme and the originally foreseen expiry dates of the PPA. It will apply the calculation methodology described in section 2.2.2 above and use in the calculation the real values of the parameters that relate to the period subsequent to 31 December 2009, which had to be estimated in order to calculate the stranded costs *ex ante*. All the cost and revenue data used in the calculation will be discounted on 31 December 2009.

(24) If at the end of the originally foreseen span of the PPAs, the actual value of the stranded costs calculated as indicated above (hereafter referred to as "SC_{actual}") is negative (that is to say, if the actual value of the eligible stranded costs, taking into account the reimbursement of illegal aid pursuant to the PPA Decision, is lower than the aid amount received at the initial stage of the notified scheme), the Hungarian Energy Office will automatically require the undertaking to pay to the State budget the discounted value at the date when that payment will be made of the lower of the following two amounts: - SC_{actual} or the full aid amount received at the first stage of the implementation of the scheme, as specified in table 1 above. This mechanism is intended to ensure that the total aid amount received under the notified scheme (in 2009 value) will not exceed the eligible stranded costs calculated taking into account the actual performance of the company and the reimbursement of the illegal aid pursuant to the PPA Decision.

(25) Also this mechanism cannot lead to payment from the State to the beneficiaries. It can only take the form of payments from the beneficiaries to the State.

3. ASSESSMENT OF THE MEASURE

3.1. Existence of State aid

(26) The Commission has first analysed to which extent the notified measure includes State aid within the meaning of article 107 (1) TFEU. For a measure to be State aid within this meaning, it has to be imputable to the State and be financed through State resources, provide a selective advantage to undertakings, distort – or threaten to distort – competition and affect trade between Member States.

(27) Firstly, under the notified scheme, three companies will receive from the State a compensation linked to the difference between on the one hand, certain investments costs, and on the other hand, the past and foreseeable revenues generated by the operation of the corresponding assets. The implementation of this scheme will thus amount to reducing the costs of these companies in order to help them recoup their investments. It therefore provides them with an economic advantage, which is selective because it benefits only three undertakings in one specific sector (electricity generation). As for the financing of the measure, the Commission notes that the expenses of the stranded costs compensation scheme are borne by the Hungarian State, which will recover less repayable State aid than it would otherwise do and, thus, will forego revenues. Therefore, the notified scheme will be

financed through State resources. Furthermore, the decision to grant stranded costs compensation is clearly imputable to the State, since it is provided by law.

(28) There is no doubt either that the measure threatens to distort competition and will affect trade between Member States. Indeed, electricity markets have been opened to competition and electricity has been traded between Member States since the entry into force of Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity[9]. Intra EU flows are all the more important in this case as Hungary is centrally located in Europe, surrounded by seven countries, with which it has six interconnectors. Through three out of those six interconnectors, the Hungarian transmission system is linked to three EU Member States (Austria, Romania and Slovakia). In 2007, Hungary imported 14 680.2 GWh and exported 10 693.6 GWh. Furthermore, the three beneficiaries of the scheme are subsidiaries of large international energy groups which have operations in several Member States. Therefore, the notified scheme threatens to distort competition and will affect trade between Member States.

(29) In view of the above, the Commission concludes that the measure constitutes State aid within the meaning of Article 107 (1) TFEU.

3.2 Lawfulness of the aid and "standstill obligation"

(30) By notifying the scheme before its implementation, the Hungarian authorities have fulfilled their obligation pursuant to Article 108 (3) TFEU.

(31) In particular, the Hungarian authorities undertook not to put the notified aid measure into effect until the Commission has reached a decision.

3.3. Compatibility of the aid

(32) Article 107 (1) TFEU provides for the general prohibition of State aid within the EU.

(33) Article 107 (3) (c) provides for the authorisation of State aid to facilitate the development of certain economic sectors, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. The Commission has developed several guidelines and communications that explain how it will apply the derogation contained in this Article.

(34) The Commission communication relating to the Methodology for analysing State aid linked to stranded costs[10] (hereafter referred to as the "Methodology") is designed to analyse aid granted to incumbents in the electricity sector in a context where certain decisions taken by these incumbents prior to liberalisation no longer make business sense after liberalisation.

(35) The first point of section 3 of the Methodology explains that stranded costs "may, in practice, take a variety of forms: long-term purchase contracts, investments undertaken with an implicit or explicit guarantee of sale, investments undertaken outside the scope of normal activity, etc." In this particular case, the aid concerns investments in power plants built before the liberalisation of the electricity market in Hungary, and these investments were carried out with the PPAs as an explicit guarantee of sale. Such investments do constitute a

---

[9] OJ L 27, 30.1.1997, p. 20.
[10] Adopted by the Commission on 26.07.2001; see the text of the Methodology on the Commission's website: http://ec.europa.eu/competition/state_aid/legislation/stranded_costs_en.pdf

category of stranded costs covered by the Methodology as has been acknowledged by the Commission in several previous decisions[11].

(36) The Commission therefore takes the view that the notified measure falls within the scope of the Methodology. It should therefore be first analysed whether the aid tallied with the conditions laid down in points 3.1 to 3.12 of the Methodology which set out rules for the identification and quantification of stranded costs.

(37) In line with point 3.1 of the Methodology, the power plants that give rise to stranded costs were built before the entry into force of Directive 96/92/EC in Hungary (i.e. 1 May 2004, which is the date on which Hungary joined the EU). In exceptional cases, investment made after that date in relation to these existing power plants are taken into account in the calculation of the stranded costs. This concerns investments that were undertaken before but not completed on 1 May 2004, provided that they could not be profitably called off at that date, i.e. that completing them and generating revenue by operating them led to lower stranded costs than those that would have existed if these investment projects had been halted. This also concerns investments undertaken after 1 May 2004, provided that they were absolutely necessary for the continuation of the operation of the power plants concerned, for example for safety reasons or for ensuring compliance with environmental regulations, and that not making those investments and stopping production would have led to higher stranded costs due to the induced loss of revenues.

(38) The list of the individual investments taken into account in the calculation of the stranded costs that were not completed on 1 May 2004 has been provided to the Commission together with a specific justification prepared by the Hungarian Energy Office as to why they fulfil the conditions mentioned at point 37 above. The Commission notes in particular that the Hungarian Energy Office excluded from the list of investments taken into account in the calculation of stranded costs all investments relating to new power generating blocks. The Commission is satisfied with the justifications provided.

(39) In accordance with point 3.2 of the Methodology, there is no doubt as regards the existence and validity of the sale guarantees under which the investments were carried out, since these guarantees are explicitly mentioned in the PPAs.

(40) In accordance with point 3.3 of the Methodology, the investments involved are very significant and may generate very large losses, as demonstrated by the calculation of the stranded costs. The Commission takes the view that as can be derived from table 1 the losses resulting from the investments are indeed significant and were these losses not to be compensated in any way, they significantly affect the competitiveness of the undertakings concerned and might even affect their viability.

(41) The Commission also notes that the impact of stranded costs is computed at the consolidated level: in particular, any negative stranded cost generated by any asset of one company, is counted in the computation of total stranded costs. The Commission also notes that the three beneficiaries belong to three different groups, Electricité de France, Gaz de France Suez and Dalkia, so that the impact of their respective stranded costs have to be

---

[11] See in particular cases NN 49/99 – *Spain – Competition transition costs scheme* – OJ C 268, 22.9.2001, p. 7; N 133/2001 – *Greece – stranded costs,* OJ C 9, 15.1.2003, p. 6; N 161/2004 – *Portugal – Portuguese stranded costs*, OJ C 250, 8.10.2005, p. 9; C 43/2005, *State aid awarded by Poland as part of Power Purchase Agreements and the State aid which Poland is planning to award concerning compensation for the voluntary termination of Power Purchase Agreement,* OJ L 83, 28.3.2009, p. 1.

computed separately. The Commission notes in this respect that the 34% stake held by Electricité de France in Dalkia, which is the majority shareholder of Pannon Hőerőmű ZRt, cannot lead to the conclusion that Pannon Hőerőmű ZRt and Budapesti Erőmű ZRt, whose majority shareholder is Electricité de France, are part of the same group. Indeed, Pannon Hőerőmű ZRt can be considered belonging to the Veolia Environnement group, since Veolia Environnement is the majority shareholder of Dalkia. Veolia Environnement is a privately owned company whereas the French State is the majority shareholder of Electricité de France, hence they belong to two different groups. Moreover, since the amounts of stranded costs calculated separately for Pannon Hőerőmű ZRt and Budapesti Erőmű ZRt are both positive, considering these two companies as part of one single entity would not affect the total amount of aid that they could receive. Indeed, the aim of the calculation of stranded costs at consolidated level is to avoid a situation where a company receives stranded costs compensation for its unprofitable assets without account being taken of its other assets, which may be very profitable.

(42) In accordance with point 3.4 of the Methodology, the investments undertaken by the beneficiaries are irrevocable. Indeed, there is no other way to recoup an investment in a power plant than to operate it or sell it at a price that cannot exceed the revenue that the power plant is expected to generate by selling its electricity on the market.

(43) Point 3.5 of the Methodology provides that commitments or guarantees linking enterprises belonging to the same group cannot qualify as stranded costs. In this specific case, stranded costs are linked to investments in power plants and not to bilateral agreements between parties. There is therefore no need to check whether these stranded costs arise from commitments or guarantees binding companies within the same group.

(44) In accordance with paragraph 3.6 of the Methodology, the Hungarian authorities provided the Commission with a list of investment costs included in the calculation of the stranded costs. Having analysed these categories of costs, the Commission reaches the conclusion that the aid would not exceed what is necessary to repay the shortfall in investment return over the lifetime of the assets, including where necessary a reasonable profit margin. The computation of the maximum value of stranded costs is based on a number of economic assumptions, including in particular a market simulation of wholesale electricity prices performed in order to determine the future cash flows of each power plant. These future cash flows, as well as the past cash flows generated by the power plants concerned, are deducted from the investments costs found to give rise to stranded costs.

(45) The market simulation predicts the efficient commitment and dispatch that would occur under a scenario characterised by perfect competition and simulates, on an hourly basis, a competitive electricity price. The simulated competitive price is derived from the marginal average cost of delivering electricity under the simulated scenario. The Commission is satisfied that the methodology followed by the Hungarian authorities constitutes an appropriate way of estimating future cash flows.

(46) In line with point 3.7 of the Methodology, the computation of the stranded costs takes account of the profits generated by the assets involved: the past and future expected cash flows generated by the assets are deducted from the investments costs giving rise to stranded costs. The real value of the stranded costs, calculated at the originally foreseen termination date of the PPAs is the difference between these investment costs and the real cash flows generated by the power plants up to the originally foreseen expiry date of the PPAs. However, it results from the rules laid down in the draft Decree that the "eligible

stranded costs" for which aid can be granted are in fact the sum of the stranded costs calculated by Hungary for the company concerned and the illegal aid to be reimbursed pursuant to the PPA Decision. The Commission considers that this approach is appropriate. Indeed, the illegal aid amounts to be recovered pursuant to the PPA Decision were part of the revenues received by the beneficiaries from MVM (the electricity wholesaler) in the past. Since that part of the past revenues will be reimbursed to Hungary, it should be deducted from the stranded costs calculated by Hungary in order to establish the amount of aid that each beneficiary can receive in application of the notified scheme. The calculation of the aid amount as set out in the draft Decree is consistent with this logic.

(47) In accordance with point 3.8 of the Methodology, the value of the investments that qualify as stranded costs has been reduced by the value of other aids awarded in the past for the assets concerned. The Commission notes that this point does not apply to the incompatible aid received on the basis of the PPAs, since this aid will be reimbursed by the beneficiaries.

(48) In accordance with point 3.9 of the Methodology, account of possible variation of stranded costs due to variation of economic data has to be taken. As explained in section 2.2.3 above, the actual aid granted will be reviewed at the end of the original term of the PPAs of each beneficiary. On the basis of the real values of the parameters used for the *ex ante* computation of the stranded costs (forecasted electricity price, forecasted sales quantities, forecasted revenues from system reserves, forecasted revenues from heat sales, fuel costs, costs of CO_2 emission, personnel costs etc.), downwards adjustments to the aid amount might be made. However, no upwards adjustment may be made, as this calculation can only result in the beneficiaries having to make a payment to the State.

(49) In accordance with point 3.10 of the Methodology, costs depreciated before the transposition of Directive 96/92/EC into national law, which for Hungary coincides with its accession to the EU, cannot give rise to stranded costs. Since the PPAs were designed in such a way as to provide for the payment of fixed categories of costs aimed in particular at allowing the depreciation of the assets (the electricity prices set in the PPAs covered fixed, variable and capital costs), and since the methodology takes into account the cash flows obtained by the beneficiaries before Hungary's accession to the EU, the value of the assets that was depreciated prior to liberalisation is automatically deducted from the amounts of stranded costs in the compensation method.

(50) In line with paragraph 3.11 of the Methodology, the stranded costs eligible for the aid are calculated on the basis of the most economic solution from the point of view of the beneficiaries, so that these stranded costs are minimised. First of all, the Commission notes that when the owner of a power plant has made investments in a power plant, and is faced with the risk that these investments are not recouped by cash flows, it is essentially faced with two possibilities. The first possibility consists in closing down or selling the plant and therefore foregoing future profits that could be generated by the operation of the plant. The second possibility consists in keeping on operating the plant in order to generate cash flows, and as the case may be, make the investments that are absolutely necessary for the continuation of operation. Choosing the more economic strategies amongst those two minimises stranded costs. The Commission considers as it has done in various occasions[12] that it is unlikely that the sale of any of the power generating units concerned could have decreased the stranded costs of the beneficiaries since a reasonable buyer would not

---

[12] See for example case N 161/2004 – *Portugal – Portuguese stranded costs*, OJ C 250, 8.10.2005, p. 9

purchase an asset for more than the cash flows it can expect to obtain by operating it in the liberalised market. As regards the investments undertaken before but not completed at 1 May 2004, it is justified to take them into account in the calculation of the stranded costs to the extent they could not be profitably called off on 1 May 2004, i.e. that the profits generated after 1 May 2004 thanks to the completion of these investments (compared to a counter-factual situation where those investments would not have been made) were expected to compensate the investments costs to be incurred after 1 May 2004 to complete these investments. Similarly, investments undertaken after 2004 that were absolutely necessary for the continuation of the operation of the plants were taken into account in the calculation of the stranded costs insofar as completing them was expected to be more economic for the company than not completing them and halt the operation of the plant. In light of these considerations, the Commission takes the view that the eligible stranded costs as calculated by Hungary do not exceed the minimum levels necessary to allow the assets concerned to continue to be run in conditions that allow them to be economically viable.

(51) The payment period for compensation extends until the initially foreseen termination date of the PPAs, namely as far as 2024. Paragraph 3.12 of the Methodology states that "costs which some undertakings may have to bear after the time horizon indicated in Article 26 of the Directive (18 February 2006) cannot, as a rule, constitute eligible stranded costs within the meaning of this methodology". However, footnote 5 of the Methodology also states that "investments which cannot be recouped or are not economically viable as a result of the liberalisation of the internal market in electricity may constitute stranded costs within the meaning of this methodology, including in cases where they are, in principle, to extend beyond 2006."

(52) The Commission notes that the investments in question are investments in power plants. These are particularly long-term investments, which are very sensitive to electricity price trends that are difficult to predict, in particular during the transition to a fully liberalised market. The costs of these investments cannot be recouped in cases where electricity prices are lower than the prices provided for when the power plants were built.

(53) Under these circumstances, the Commission takes the view, as it did in previous cases concerning Greece[13], Portugal[14] and Poland[15], that footnote 5 of the Methodology applies to these specific stranded costs and justifies the award of compensation after 2006 and until the initially foreseen termination date of the PPAs.

(54) In light of the above, the Commission concludes that the notified measure satisfies points 3.1 to 3.12 of the Methodology and that the stranded costs concerned are therefore eligible within its meaning.

(55) The Commission also needs to analyse whether the measure fulfils the conditions laid down in points 4.1 to 4.6 of the Methodology.

(56) In line with point 4.1 of the Methodology, the aid granted on the basis of the notified scheme will not exceed the eligible stranded costs, which, as demonstrated by the analysis

---

[13] N 133/2001 – *Greece – stranded costs* (OJ C 9, 15.1.2003, p. 6).

[14] Case N 161/2004 – *Portugal – Portuguese stranded costs* (OJ C 250, 8.10.2005, p. 9).

[15] C 43/2005, *State aid awarded by Poland as part of Power Purchase Agreements and the State aid which Poland is planning to award concerning compensation for the voluntary termination of Power Purchase Agreement* (OJ L 83, 28.3.2009, p. 1).

above, have been clearly determined and isolated on the basis of justified investment costs and cash flows.

(57) In accordance with point 4.2 of the Methodology, the aid effectively granted will take account of actual trends in underlying economic data since the total aid amount will be revised at the end of the originally foreseen termination date of the PPAs on the basis of the real values of the stranded costs. In particular, account will be taken of actual electricity prices and quantities sold. If the aid amount granted at the first stage of the implementation of the notified scheme turns out higher than the real eligible stranded costs, the beneficiaries will have to reimburse to the State the difference between the aid initially granted and the real eligible stranded costs, if this difference does not exceed the aid amount received at the first stage of the implementation of the notified scheme. Otherwise, the beneficiary will reimburse the full amount of aid received at the initial stage of the implementation of the notified scheme, discounted to the date when that payment will be made.

(58) In line with point 4.3 of the Methodology, the Hungarian authorities have undertaken to provide the Commission with an annual report on the implementation of the measure, satisfying the requirements laid down in that part of the Methodology.

(59) Point 4.4 of the Methodology states that degressive aid would be viewed favourably by the Commission, as it will help the company to speed up its preparations for a liberalised market. In this case, the aid will be granted at one time, and a claw-back mechanism will be applied subsequently. In view of the factual circumstances of the case the Commission considers this method to be satisfactory and notes that it also has the effect of enabling the company to operate in a liberalised market, whilst at the same time limiting the distortion of competition.

(60) In accordance with paragraph 4.5 of the Methodology, the maximum amount of aids is fixed in advance for each beneficiary: those amounts are specified in table 1 above. These amounts take account of future productivity gains that may be achieved by the beneficiaries. Furthermore, the notification of the aid specified in particular how account will be taken of changes in various economic data (e.g. electricity prices, sold quantities, fuel costs, CO_2 emission costs, personnel costs etc.) in the calculation of the real stranded costs, on the basis of which the claw-back mechanism will be applied.

(61) Finally, in accordance with paragraph 4.6 of the Methodology, the Hungarian authorities specified that the beneficiaries of the measure should not receive any rescue and restructuring aid until ten years have elapsed since the expiry dates of the PPAs as initially foreseen in those agreements. This period, which extends until 30 July 2034 for Budapesti Erőmű Zrt., 31 December 2025 for Dunamenti Erőmű Zrt. and 31 December 2020 for Pannon Hőerőmű Zrt., is compatible with the "one time last time" principle as interpreted by the Commission in point 73 of the Community guidelines on State aid for rescuing and restructuring firms in difficulty[16]. This rule is laid down at Article 5 (2) of the draft Decree.

(62) Hence, the measure is compatible with points 4.1 to 4.6 of the Methodology. Therefore, the measure complies with the methodology for analysing State aid linked to stranded costs.

---

[16] OJ C 244, 1.10.2004, p. 2.

Assessment of a potential cumulative effect with incompatible aid – Application of the Deggendorf[17] case law

(63) Part of the aid found incompatible with the internal market in the PPA Decision has benefitted the future recipients of the notified aid and not yet been recovered from them by Hungary.

(64) In its *Deggendorf* Judgement, the Court of Justice found that when the Commission examined the compatibility of State aid with the internal market, it had to take all the relevant factors into account, including, when appropriate, the circumstances already considered in a prior decision and the obligations which that decision may have imposed on a Member State. Moreover, the Court of Justice stated that the Court of First Instance had not erred in law by finding that the Commission had acted within its powers in a case where it took into account the following elements in its assessment of the compatibility of an aid measure:

- the cumulative effect of that aid and of another aid previously found incompatible with the internal market,

- the fact that this incompatible aid had not yet been recovered by the Member State.

(65) In the present case, the PPAs can no longer give rise to State aid since they have been already terminated. Furthermore, Hungary committed to synchronising the recovery of the incompatible aid received by the beneficiaries through their PPAs between 2004 and 2008, and the granting of aid under the notified scheme. Therefore, the granting of aid under the notified scheme will not predate the recovery of the incompatible aid received by the beneficiaries, but both operations will be carried out simultaneously. It follows that the notified aid will have no cumulative effect with that of the incompatible aid received by the beneficiaries on the basis of their PPAs.

(66) Therefore, there is no cumulative effect such as the one at issue in the *Deggendorf* case which could lead to the conclusion that the notified aid is incompatible with the internal market even though it complies with the criteria laid down in the Methodology.

3.4. Conclusion

(67) The Commission concludes that the measure notified by the Hungarian authorities to compensate for the stranded costs incurred by the beneficiaries of the PPAs entered into in the mid-nineties constitutes State aid within the meaning of Article 107 (1) TFEU and that this State aid is compatible with the internal market in application of Article 107 (3) (c) TFEU.

(68) The Commission emphasizes that this conclusion is based on the commitment of the Hungarian authorities as foreseen by the draft Decree attached to the notification, that the first stage of the notified scheme and the execution of the recovery requirement contained in the PPA decision will be carried out simultaneously, so that in practice, the Hungarian State will not make any payment to the beneficiaries but instead, will forego the amounts to be

---

[17] C-355/95 *TWD v. Commission* [1997] Rec. I-2549, par. 25-27.

repaid to it in application of the PPA decision. As it appears from the elements described above, both the calculation of the eligible stranded costs and the compatibility of the notified scheme with the internal market depend on the fact that the granting of aid in application of the first stage of the notified scheme and the recovery of illegal aid in application of the PPA Decision will actually be performed simultaneously.

(69) Therefore, the Commission calls Hungary's attention to the fact that the authorisation provided by the present decision applies to the notified scheme only insofar as it is implemented in conjunction with the recovery requirement of the PPA decision as foreseen by the draft Decree attached to the notification.

(70) If the PPA Decision were to be annulled by the European Courts and if the Hungarian authorities reimbursed to the undertakings concerned the amounts recovered in application of the PPA Decision, they would have to deduct the amounts of aid granted in application of the notified scheme. Should Hungary then decide to grant compensation for any stranded costs that the companies concerned may still have at that point, such a compensation would have to be notified to and approved by the Commission in accordance with the procedure laid down at Article 108 (3) TFEU prior to implementation.

4. DECISION

(71) The Commission has accordingly decided not to raise any objections to the measure.

(72) If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/community_law/state_aids/state_aids_texts_hu.htm

(73) Your request should be sent by registered letter or fax to:

> European Commission
> Directorate-General for Competition
> State Aid Greffe
> **B-1049 Brussels**

> Fax No: +32 2 29 61242

<div align="center">
Yours faithfully,

For the Commission

Joaquín ALMUNIA
Vice-President of the Commission
</div>