Commission Decision

of 11 June 2003

declaring a concentration to be compatible with the common market and the EEA Agreement

(Case COMP/M.2947 - Verbund/EnergieAllianz)

(Only the German version is authentic)

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings,[1] as last amended by Regulation (EEC) No 1310/97,[2] and in particular Article 8(2) thereof,

Having regard to the Commission decision of 4 February 2003 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations,[3]

Having regard to the final report of the Hearing Officer in this case,[4]

Whereas:

(1) On 20 December 2002 the Commission received notification of a proposed concentration under Article 4 of Council Regulation (EEC) No 4064/89 ("the Merger Regulation"). The Austrian undertakings Österreichische Elektrizitätswirtschafts-Aktiengesellschaft ("Verbund"), EVN AG ("EVN"), Wien

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1 OJ L 395, 30.12.1989, p. 1; corrigendum OJ L 257, 21.9.1990, p. 13.

2 OJ L 180, 9.7.1997, p. 1.

3 OJ C …

4 OJ C …

Energie GmbH ("Wien Energie"), Energie AG Oberösterreich ("Energie OÖ"), Burgenländische Elektrizitätswirtschafts-Aktiengesellschaft ("Bewag") and Linz AG für Energie, Telekommunikation, Verkehr und Kommunale Dienste ("Linz AG") planned to acquire within the meaning of Article 3(1)(b) of the Merger Regulation joint control of E&S GmbH ("E&S") and Verbund Austrian Power Trading AG ("APT"). EVN, Wien Energie, Energie OÖ, BEWAG and Linz AG were to manage their interests jointly under the name EnergieAllianz Austria ("EnergieAllianz").

(2) The Commission examined the notification, and found that the notified concentration fell within the scope of the Merger Regulation and raised serious doubts as to its compatibility with the common market and with the functioning of the Agreement on the European Economic Area ("the EEA Agreement").

(3) On 4 February 2003, therefore, the Commission decided to initiate proceedings in the case under Article 6(1)(c) of the Merger Regulation and Article 57 of the EEA Agreement.

(4) After a thorough investigation of the case the Commission has come to the conclusion that in itself the notified concentration would indeed strengthen a dominant position as a result of which effective competition would be significantly impeded in a substantial part of the common market. But the competition concerns to which the transaction gave rise have been overcome by the commitments entered into by the notifying parties.

I. THE BUSINESS OF THE PARTIES

(5) Verbund generates and transmits electricity and supplies it to industrial customers and to electricity distributors; it also trades in electricity. Verbund is the biggest electricity generator in Austria, and operates the high-voltage grid throughout the country with the exception of Vorarlberg and the Tyrol. Verbund deals with large customers through a 55% subsidiary, Verbund - Austrian Power Vertriebs GmbH ("APC"); the bulk of the other shares in APC, which do not carry controlling rights, are held by Energie Steiermark Holding AG ("Estag"), a company which is itself controlled jointly by the *Land* of Styria and the French electricity supplier Électricité de France ("EdF"). Verbund and Estag also jointly own Steweag-Steg GmbH ("Steweag-Steg"), which is a regional distributor in Styria, Verbund holding 34% of the capital and Estag 66%; Steweag-Steg differs from APC in that here Verbund and Estag exercise joint control.[5] Verbund has a minority 35.12% holding in Kelag - Kärntner Elektrizitäts-Aktiengesellschaft ("Kelag"), which is controlled by an intermediate holding company owned jointly by the *Land* of Carinthia and the German company RWE AG ("RWE"). Verbund also has interests in companies that supply electricity to households on the liberalised Austrian electricity market; these interests currently include 20% stakes in Unsere Wasserkraft GmbH & Co. KG ("Unsere Wasserkraft"), which is a joint venture with Estag,[6] and MyElectric Stromvertriebs GmbH

5 Commission Decision of 14 December 2001 in Case COMP/M.2485 – Verbund/Estag, paragraph 7.

6 This company previously traded under the name RWA Wasserkraft, and was subsequently renamed Unsere Wasserkraft; it was originally owned 50-50 by Verbund and Raiffeisen Ware Austria AG ("RWA"): Commission Decision of 17 September 2001 in Case COMP/M.2541 – RWA/Verbund/JV. At the end of 2002 all of RWA's shares and part of Verbund's shares were sold to Estag.

("MyElectric"), which is controlled by Salzburg AG für Energie, Verkehr und Telekommunikation ("Salzburg AG"). Verbund itself is controlled by the Republic of Austria, which holds 51% of the shares.

(6) The members of EnergieAllianz distribute electricity regionally, in Lower Austria (EVN), the Vienna area (Wien Energie), Upper Austria (Energie OÖ), the Linz area (Linz AG) and Burgenland (Bewag); this includes supplying to final consumers. Energie OÖ also has a 26.13% stake in Salzburg AG, the regional supplier in the *Land* of Salzburg. With the exception of Bewag, the members of EnergieAllianz all generate electricity. The members also distribute gas and heat regionally, and provide services relating to transport, the environment, waste management, waste disposal, telecommunications and cable television. Majority holdings in all the members of EnergieAllianz are held by regional authorities.

II. THE TRANSACTION

(7) The planned transaction would consolidate the electricity business of Verbund and EnergieAllianz in two joint ventures, E&S and APT. The electricity generation capacity of Verbund and the *Land* corporations that are members of EnergieAllianz would continue to be in separate ownership. But generation would be directed by the trading company APT, which would be owned 67% by Verbund and 33% by EnergieAllianz. The electricity generated in Verbund's and EnergieAllianz's power stations would be supplied exclusively to APT. APT would handle electricity trading. APT would also supply electricity to E&S, which would be owned 67% by EnergieAllianz and 33% by Verbund. E&S would deal with all the large customers formerly with EnergieAllianz or Verbund which have an annual consumption of more than 4 GWh, and would supply them with electricity. APT would supply electricity to the *Land* corporations which are members of EnergieAllianz, and those corporations would supply commercial customers with a consumption of 0.1-4.0 GWh and household customers up to 0.1 GWh. APT would also supply electricity to the remaining *Land* corporations that are not party to the transaction and the city corporations outside the areas supplied by EnergieAllianz.

III. A "CONCENTRATION"

(8) APT and E&S are to be subject to the joint control of Verbund and EnergieAllianz. The agreement of both sides on the supervisory board, or in the case of E&S on the shareholders' committee, would be needed for investments of over €[…]* million, the determination of general principles of business policy (including the principles of pricing and product policy), and the conclusion of purchase and supply contracts for an amount of more than […]* TWh a year and a duration of more than […]* years. On the management board the agreement of both sides would be needed for important items such as production and sales planning on a multiannual, annual, monthly, weekly and daily basis, and for "day ahead" operations. Strategic decisions would require the agreement of both sides at a consortium meeting (*Syndikatsversammlung*).

* Parts of this text have been edited to ensure that confidential information is not disclosed: those parts are enclosed in square brackets and marked with an asterisk.

(9) APT and E&S are to be linked together by this consortium meeting, which would be common to the two of them and on which they would be equally represented. APT would handle procurement for E&S.

(10) APT and E&S would be performing on a lasting basis all the functions of autonomous economic entities. They would have their own management and sufficient financial, personal, tangible and intangible resources, and on the markets on which they operate they would play an active role.

(11) The transaction therefore constitutes a "concentration" within the meaning of Article 3(1)(b) of the Merger Regulation.

IV. PROCEDURE

(12) The Commission examined the notification and found that the notified concentration fell within the scope of the Merger Regulation and raised serious doubts as to its compatibility with the common market and with the functioning of the EEA Agreement. On 4 February 2003, therefore, the Commission decided to initiate proceedings in the case under Article 6(1)(c) of the Merger Regulation and Article 57 of the EEA Agreement.

(13) On 10 April 2003 the Commission, in accordance with Article 18 of the Merger Regulation, sent the notifying parties a statement of objections, to which they replied by letter of 25 April 2003. At the notifying parties' request a hearing was held on 29 April 2003, which was attended by the notifying parties and a number of third parties. After proceedings were initiated and after the hearing took place there were discussions between the Commission and the notifying parties in which the notifying parties were kept abreast of the progress of the case.

(14) On 12 May 2003 the notifying parties submitted commitments which they proposed to enter into. The Commission carried out a market test, in the course of which it consulted third parties; it concluded that the commitments proposed were not sufficient to resolve the competition concerns raised by the transaction, and informed the parties accordingly. The parties then modified the commitments in such a way that the Commission can now clearly determine, on the basis of its assessment of information already received in the course of the investigation, including the results of prior market testing, and without the need for any other market test, that the competition problems that had been identified have been resolved. The proposed changes to the commitments were submitted in sufficient time to allow proper consultation of Member States, as required by the Commission notice on remedies acceptable under Council Regulation (EEC) No 4064/89 and under Commission Regulation (EC) No 447/98 ("the Remedies Notice").[7, 8]

V. A "COMMUNITY DIMENSION"

(15) The combined aggregate worldwide turnover of all the undertakings concerned is more than €5 000 million (in 2001: Verbund €1 784 million, EVN €1 015 million, Wien

7 OJ C 68, 2.3.2001, p. 3, paragraph 43.

8 The full text of these modified commitments is attached in the Annex to this Decision ("Annex").

Energie €1 822 million, Energie OÖ €2 042 million, Bewag €165 million, and Linz AG €427 million).[9] More than two of the undertakings have an aggregate Community-wide turnover of more than €250 million (in 2001: Verbund €[…]* million, EVN €[…]* million, Wien Energie €[…]* million, Energie OÖ €[…]* million, and Linz AG €[…]* million). The undertakings in EnergieAllianz achieve more than two thirds of their aggregate Community-wide turnover in Austria, but Verbund achieves less than two thirds of its aggregate Community-wide turnover in Austria. The notified concentration therefore has a Community dimension within the meaning of Article 1(2) of the Merger Regulation. It is not a case for cooperation with the EEA Surveillance Authority under the EEA Agreement.

VI. APPRAISAL UNDER ARTICLE 2 OF THE MERGER REGULATION

A. THE STRUCTURE OF THE AUSTRIAN ELECTRICITY INDUSTRY

1. The legal framework

(16) Until 1999 the electricity industry in Austria was governed by the second Nationalisation Act of 1947, which provided for a strict division of tasks and far-reaching territorial protection for the undertakings operating in the industry. Verbund was essentially responsible for generating energy in large power stations, building and operating transmission grids, and trading in electricity with foreign countries. The nine *Land* corporations, Bewag (Burgenland,), Kelag (Carinthia), EVN (Lower Austria), Energie OÖ (Upper Austria), Salzburg AG (Salzburg), Steweag (Styria), Tiwag (Tyrol), VKW (Vorarlberg) and Wienstrom (Vienna) and the five city corporations in the *Land* capitals Graz, Innsbruck, Klagenfurt, Linz and Salzburg distributed electricity to all categories of customer in their own areas. What the *Land* corporations did not generate themselves they generally obtained from Verbund.

(17) The Electricity Market Directive was initially transposed into Austrian law by the Electricity Industry and Organisation Act (*Elektrizitätswirtschafts- und Organisationsgesetz*). From 19 February 1999 all final consumers with an annual electricity consumption of at least 40 GWh, or from 1 February 2000 20 GWh, became entitled to access to the grid, and could freely choose their electricity supplier. From 19 February 1999 operators of distribution networks who had a transmission network at their disposal, essentially the *Land* and city corporations, were also entitled to grid access.

(18) In 2000 the Energy Liberalisation Act carried the liberalisation of the Austrian electricity market further. Since 1 October 2001 all customers are entitled to grid access, irrespective of their consumption or sales volume, and are free to choose their supplier. The coordination contracts between Verbund and the *Land* corporations came to an end the same day.

(19) The legal responsibility for market supervision and the protection of competition, in particular industry-specific regulation and supervision of unbundling, rests on Energie-Control GmbH ("E-Control"), which is a company formed under private law

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9 Turnover calculated in accordance with Article 5(1) of the Merger Regulation and with the Commission notice on calculation of turnover, OJ C 66, 2.3.1998, p. 25.

and wholly owned by the Republic of Austria. Above E-Control there is an independent state supervisory authority, the Energy Control Commission, which is responsible for deciding on appeals against decisions taken by E-Control, approving grid access charges, and settling disputes over the granting of grid access.

2. Present situation of electricity generation and supply

(20) In 2001 a total of 62 250 GWh of electricity was generated in Austria. Hydroelectric production consisted of 29 494 GWh from run-of-river power stations and 12 340 GWh from reservoir power stations. In 2001, therefore, 67.2% of total generation was in hydroelectric power stations. Thermal stations generated 20 416 GWh, 32.8% of the total. The following table shows the breakdown of electricity generation between the main undertakings operating in this sector:

Table 1
Electricity generation in Austria in 2001

Producer	**Output** (GWh)	**Share of total output**
Verbund	[20 000–25 000]*	[30–40%]*
Steweag-Steg°	[1 000–6 000]*	[0–10%]*
Energie OÖ°°	[1 000–6 000]*	[0–10%]*
Wienstrom°°°	[1 000–6 000]*	[0–10%]*
EVN°°°	[1 000–6 000]*	[0–10%]*
Linz AG°°	[0–4 000]*	[0–10%]*
Bewag	0	0.0%
Kelag	[1 000–6 000]*	[0-10%]*
Salzburg AG	[0–4 000]*	[0–10%]*
Tiwag°	[1 000–6 000]*	[0–10%]*
VKW incl. VIW°	[1 000-6 000]*	[0–10%]*
Other electricity suppliers and industry	[10 000–15 000]*	[15–25%]*
Total output°	62 250	100.0%

° estimated

°° financial year 2000/2001

°°° calendar year 2001

Source: The parties, citing company reports and E-Control statistics

(21) Austria is divided into three control areas. Each of the two western *Länder*, Vorarlberg and the Tyrol, is a control area by itself, and forms part of the German control block. All the other *Länder* together, accounting for by far the larger part of the country, make up the eastern control area, or “Austrian Power Grid” (APG) area, which is a separate control block. Here Verbund operates the high-voltage grid, and as the control area manager it is responsible under the rules of the UCTE for maintaining a balance between generation and consumption by providing or withdrawing balancing energy.

(22) The *Land* corporations - the members of EnergieAllianz plus Steweag-Steg in Styria, Salzburg AG in the *Land* of Salzburg, Kelag in Carinthia, Tiwag in the Tyrol, and VKW in Vorarlberg - operate the distribution grid in their traditional supply areas. They obtain electricity both from Verbund and from their own power stations and to some extent also from foreign suppliers and energy traders.

(23) Both Verbund and the *Land* corporations supply electricity to final consumers. There are also a large number of smaller local and private electricity supply undertakings operating as distributors and supplying to final consumers, some of whom currently have their own generation capacities.

B. RELEVANT PRODUCT MARKETS

1. Introduction

(24) A relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices and their intended use. The main tests indicated in the Commission notice on the definition of relevant market for the purposes of Community competition law ("the Relevant Market Definition Notice") are demand substitution, supply substitution and potential competition.[10]

(a) The parties' activities overlap

(25) The proposed concentration would group together the existing electricity sales activities of Verbund and EnergieAllianz.

(26) The parties' activities overlap essentially in supply to industrial and large commercial consumers ("large customers") and distributors, and in electricity trading, and to a lesser extent in supply to households and small businesses ("small customers", in Austria also commonly known as "tariff customers"). There is also some overlapping in the supply of the balancing energy needed to maintain a balance between generation and consumption.

(27) In the generation and transmission of electricity there is no overlapping between the parties' activities on the market, because each party's power generation branch supplies the power it generates only inside the organisation, so that power is available to the market not at the generation stage but only at the downstream commercial stage, while grid operation is in each case a natural monopoly. But the position of the parties in the generation of power must be taken into account when assessing the effects of the concentration on the relevant markets.

(b) Distinguishing the relevant product markets

(28) The parties initially suggested that there were separate relevant product markets in supply to small customers, supply to large customers, electricity trading including supply to distributors, and the provision of balancing energy.

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[10] OJ C 372, 9.12.1997, p. 5, paragraphs 7 and 13 ff.

(29) In their reply to the statement of objections, and at the hearing, the parties changed their standpoint on the precise classification of supply to large and small customers. They now take the view that in this area a distinction has to be drawn between price-oriented and service-oriented customers. For price-oriented customers, price is the only decisive criterion in the choice of a supplier of electricity, while service-oriented customers need additional services such as full supply, energy management or balancing energy, and will consequently look at the quality of those services too when choosing an electricity supplier.

(30) According to the parties view as they explained it at the hearing, the price-oriented customers market includes some distributors, namely the large regional suppliers ("large distributors", also known as "*Land* suppliers" or "*Land* corporations"), and the municipal utilities in *Land* capitals; but it includes only very few large customers.[11] All those taking part in electricity trading belong to the price-oriented customers market. All other distributors ("small distributors") and large customers belong to the service-oriented customer market. The provision of balancing energy continues to be regarded as a separate market.

(31) The Commission has already had occasion to consider market conditions in Austria, in the *Verbund/Estag* case.[12] But that decision left it open whether the market in the supply of electricity in Austria should be segmented by customer group.

(32) In the present case the Commission has come to the conclusion that, as suggested by the notifying parties, there are separate relevant markets in supply to small customers, supply to large customers and small distributors (described by the parties as "service-oriented"), and supply to large distributors and electricity traders (described by the parties as "price-oriented").

(33) In the present Decision it will not be necessary to determine

(a) whether a distinction should be made between relevant product markets in supply to large customers and supply to small distributors;

(b) whether a distinction should be made between relevant product markets in supply to large distributors and supply to electricity traders;

(c) whether for competition purposes the provision of balancing energy constitutes a separate relevant product market.

1. Supply to final consumers: Distinction between large and small customers

(34) Although the Austrian market is fully liberalised in regulatory terms, the parties take the view that the supply of electricity to final consumers should be divided into separate relevant product markets, in supply to small customers (private households, small businesses and farms) and large customers (industry and large commercial consumers); the parties now bracket large customers in the category of "service-oriented customers."

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11 One such being ÖBB, the federal railways.

12 Commission Decision of 14 December 2001 in Case COMP/M.2485 – Verbund/Estag.

As a dividing line between large and small customers, the parties propose the consumption and load values below which under the general legal provisions in force in Austria standardised load profiles are applied. Under the law as it stands, customers with an annual consumption of less than 100 000 kWh a year, or in other words less than 0.1 GWh a year, or a connected load of less than 50 kW, are offered standardised load profiles.

(35) According to the information assembled by the Commission in this proceeding, the supply of electricity should indeed be segmented, as the parties propose, into a market in supply to small customers and a market in supply to large customers (industrial and large commercial consumers); the Commission's enquiries have not identified any grounds for further differentiation.[13]

(36) As the parties submit, and as the Commission's enquiries confirm, there are substantial differences between the demand behaviour of large customers and mass customers. Large customers are usually more price-sensitive, and correspondingly more ready to change suppliers than small customers are. Negotiating power and conduct of negotiations are also different. This is reflected in different sales strategies adopted by the energy suppliers and a different level of prices. For large customers value for money and flexibility of supply are the major considerations, while for mass customers there is a further marketing differentiation (for example between "clean energy", especially from domestic hydroelectric sources, and electricity from fossil fuels or nuclear energy), and a qualitative approach to customers.

(37) Large customers and mass customers usually take power at different voltage levels, and this too helps to differentiate them. It is true that the voltage at which electricity is supplied is not in itself a barrier to entry, in view of the "postage stamp tariff" payable for through-transmission. But the lower the voltage at which current is delivered, the higher the share of the entire bill accounted for by the grid itself. The relative advantage to the customer of a change of suppliers is therefore lower at lower grid voltages with higher grid prices.

2. Supplying distributors: distinction between regional distributors ("*Land* corporations") and smaller distributors

(38) The parties initially argued that all supply to distributors should be considered part of the electricity trading market, because the business of a distributor largely matches the accepted definition of electricity trading, namely the purchase and sale of electricity with a view to gain. This classification also matches the practice of Austrian electricity suppliers in their company reports, where they classify supply to wholesalers and distributors together in the single category of "trading". In their reply to the Commission's statement of objections, and at the hearing, the parties changed their position to argue that a specific group of distributors, namely the small distributors, should be included among the "service-oriented" customers, along with industrial and large commercial consumers. They

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[13] Consideration might possibly be given to the question whether a limited number of very large consumers, such as ÖBB for example, ought to be separated from the other large customers, and excluded from the large customers market (or the large customers and small distributors market). But this would not ultimately affect the structure of the large customers market and consequently its assessment for competition purposes, and if this segment is indeed assessed separately no competition concerns in fact arise.

pointed to similar prices, similar purchasing behaviour, and a need for additional services alongside the necessary power itself.

(39) According to the information assembled by the Commission, supply to the large regional distributors or *Land* suppliers and supply to all other distributors must indeed be assigned to separate relevant product markets.

(a) It need not be decided whether supply to small distributors, once distinguished from supply to large distributors, should be included in the market for supply to large final consumers, or whether it constitutes a separate market

(40) The Commission's enquiries have established that demand for electricity from smaller distributors, including all the municipal and local utilities and private utilities,[14] is clearly distinct from demand from large distributors or indeed from the trading market. Small distributors, whose annual turnover is in most cases well below 500 GWh, are usually supplied under annual or multiannual supply contracts, often coupled with a full supplier contract that makes it unnecessary to buy any additional energy and includes delivery of whatever balancing energy is required. Because of their small size these distributors have not got the financial and administrative capacities they would need in order to engage in active purchasing management on trading markets. They therefore depend on long-term, stable supply contracts, usually with just one seller, typically an upstream regional supplier. For the same reasons, separate purchase of balancing energy by these distributors is at present the exception rather than the rule. As the parties indicated at the hearing, full supply with electric power is a core element, linking supply to small distributors to the market for large customers.

(41) However, there is also evidence to suggest that the terms of supply to small distributors are different from those of supply to industrial and large commercial consumers. The small distributors supply mainly to households and small firms, and given this customer structure their purchasing behaviour differs from that of large customers, as their power requirements are not the same.[15] And unlike large customers, smaller distributors compete within their own supply areas with other, bigger distributors, including especially the members of EnergieAllianz, to supply to certain categories of final consumer (usually small customers with an annual consumption of less than 0.1 GWh and commercial customers with an annual consumption of 0.1-4.0 GWh).

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14 That is to say all Austrian distributors with the exception of the *Land* suppliers (the EnergieAllianz companies plus Steweag-Steg, Salzburg AG, Kelag, Tiwag and VKW) and the companies associated with them, and also excluding Verbund and EnBW Austria. In their reply to the Commission's statement of objections the parties to the transaction argued that the classification of some municipal utilities in *Land* capitals was not straightforward, because their purchasing behaviour was closer to that of the *Land* supplier than to that of the other small distributors. But this question is of no importance here, because the precise classification of these municipal utilities does not affect either the assessment for competition purposes of the market in supply to small distributors (or large customers and small distributors) or of the market in supply to large distributors (or the market in electricity trading including supply to large distributors).

15 This may be the reason why, as many small distributors have told the Commission, the terms that their suppliers give to small distributors are less favourable than those offered to industrial and large commercial consumers. This is contested by the notifying parties.

(42) For purposes of this Decision, however, it is not necessary to reach a final judgment on the question whether supply to small distributors constitutes a relevant product market of its own, separate from the large customers market. It is clear that supply to small distributors, who depend on full supply contracts, is in any even not to be assigned to the same market as supply to regional distributors or energy traders. Whether we suppose that there is one market in supply to large customers and small distributors, or two separate markets, the transaction at issue would in any event create or strengthen a dominant position on both of these conceivable markets.

(b) There is no need to decide whether supply to regional suppliers constitutes a separate relevant product market, or whether it should be included in the electricity trading market

(43) Supply to the big Austrian distributors ("*Land* suppliers", "*Land* corporations"), that is to say the members of EnergieAllianz and Steweag-Steg, Salzburg AG, Kelag, Tiwag and VKW, is clearly distinguished by a number of features from supply to smaller distributors.

(44) Until the Austrian electricity market was liberalised, the *Land* suppliers drew their entire requirements of electricity, apart from what they produced themselves, from Verbund, to which they were bound by coordination contracts. When the market was fully liberalised on 1 October 2001, and the coordination contracts came to an end, the *Land* suppliers became free to choose their sources of supply. Given the volumes of electricity they need and their greater financial and administrative capacities, they are in a stronger position than the small distributors to take practical advantage of the scope legally open to them. The regional suppliers take their electricity requirements, apart from what they generate themselves, partly from Verbund and partly from other *Land* suppliers, foreign electricity suppliers and the trading market. They do not usually conclude full supplier contracts, but conduct their own energy management and make their own arrangements to procure additional volumes and balancing energy.

(45) The parties contend that supply to the Austrian regional suppliers forms part of the broader market in energy trading. But the Commission's enquiries provide clear evidence that the market in supply to the regional suppliers has to be distinguished from the electricity trading market proper.

(46) Electricity trading is to be understood as the buying and selling of electricity at one's own risk and for one's own account. In earlier decisions the Commission has found energy trading to be a market in the process of formation, which was made possible only by customers being given a free choice in the wake of liberalisation.[16] In addition to independent traders with no generating capacity or grid of their own, electricity traders include, on the supply side and to some extent on the demand side as well, electricity generators, distributors and importers.

(47) Electricity trading can be divided essentially into the following categories:

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[16] Decision of 28 September 1999 in Case IV/M.1557 – EdF/Louis Dreyfus, paragraphs 16-18; Decision of 13 June 2000 in Case COMP/M.1673 – VEBA/VIAG, OJ L 188, 10.7.2000, p. 1, paragraph 18.

(a) over-the-counter ("OTC") trading, where individual bilateral contracts are negotiated and concluded outside any central exchange or marketplace;

(b) trade in physical electricity products on exchanges; on the recently founded Energy Exchange Alpen-Adria (EXAA) in Graz, spot deliveries are traded in the form of single-hour contracts, and beginning in 2003 dealing in electricity futures will also be possible;

(c) trade in non-physical financial derivatives, known as energy derivatives, which is only at its initial stages, and in Austria still plays only a minor role.

(48) The *Land* corporations essentially supply final consumers (large customers and tariff customers) and smaller distributors. As already explained, the *Land* suppliers' customers usually take all of their electricity requirements (beyond what they generate themselves) from one and the same supplier. To guarantee their customers full supply of this kind, the regional suppliers depend on long-term fixed contracts for the greater part of their electricity requirements at least.

(49) For this reason most of the electricity required by the *Land* suppliers cannot be met through short-term exchange dealings. Whether more long-term supplies purchased OTC on the open market would be sufficient is not clear from the Commission's enquiries; at least one regional supplier stated that the electricity trading markets had not got the necessary liquidity for this either.

(50) Although all this suggests that there is a separate relevant product market in supply to the large regional suppliers, the question can remain unanswered here, because the transaction would not create or strengthen a dominant position on such a market.

3. Balancing energy

(51) The supply of electricity differs from most other product markets in that electricity cannot easily be stored and the amount of energy to be supplied is not known with any precision in advance. Consumption forecasts are incorporated into schedules and load profiles. But the forecasts do not as a rule coincide with actual consumer behaviour. Specially generated balancing energy is therefore needed to ensure that the difference between electricity output and load is always met.

(52) The balancing energy needed to maintain a balance between production and consumption in a control area is provided

(a) by adjusting the volume of electricity generated inside the control area (this is known as secondary regulation); or

(b) by drawing on what is called the minute reserve, which is an additional regulatory instrument that can be called upon in the short term; or

(c) if complete adjustment cannot be achieved either by secondary regulation or out of the minute reserve, by "involuntary exchange" between a control area and the surrounding UCTE control areas.

(53) The parties take the view that the competitive conditions for the provision of balancing energy are so different from those of the other electricity supply markets that there is a separate relevant product market.

(54) The position of the parties in the provision of balancing energy, especially in the form of the minute reserve, is a factor that helps to create or strengthen dominant positions on several electricity supply markets. This is so whether or not the provision of balancing energy, and especially of the minute reserve, is itself a separate relevant product market. For purposes of this Decision, therefore, the precise treatment of the provision of balancing energy in the definition of product markets can remain open.

C. RELEVANT GEOGRAPHIC MARKET

(55) The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogenous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different within those areas. The main tests are demand substitution, supply substitution and potential competition.[17]

(56) The notifying parties consider that in the case of supply to large customers, distributors and energy traders, the relevant geographic market reaches beyond Austria, while in the case of small customers it is confined to Austria. They take the view that the relevant geographic market in supply to large customers includes Austria and Germany, essentially because of the capacity of the interconnectors through which electricity can be imported especially from Germany. They also argue that the liberalisation of the electricity market under the Electricity Market Directive, which has been fully implemented in Austria, has opened the Austrian market to foreign suppliers, and that this liberalisation must be reflected in the definition of the relevant geographic market for purposes of merger control.

(57) The Commission's enquiries have established that in accordance with the criteria for the definition of the geographic market the geographic markets in the supply of electricity to large customers, small distributors and small customers do not extend beyond Austria. A possible market in supply to large regional distributors may be wider.

1. The market or markets in supply to large customers and small distributors and the market in supply to small customers are purely domestic

(a) The structure and the legal framework of the electricity markets in Austria are fundamentally different from those of the neighbouring countries

(58) The breakdown of market shares between the parties and their competitors on the electricity supply markets in Austria is fundamentally different from that in the neighbouring countries or in the EEA as a whole, and this in itself indicates that in geographic terms the relevant markets are confined to Austria.[18] It will be enough here to

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17 Relevant Market Definition Notice (see footnote 10), paragraphs 8 and 13 ff.

18 Relevant Market Definition Notice (see footnote 10), paragraph 28.

point out that none of the main electricity suppliers at EEA level, such as EdF, E.On, RWE or Enel, has a market share of 5% or more of the market in supply to small customers, large customers or small distributors in Austria. The same applies to the main competitors on the German electricity markets, E.On, RWE, EnBW and Vattenfall. And no Austrian electricity supplier has a share of 5% or more of any electricity supply market in a neighbouring Member State or at EEA level.

(59) The legal framework in Austria is quite different from that in neighbouring Switzerland or Germany. In Switzerland the Electricity Market Directive does not apply. In Austria and Germany the Directive has been implemented in very different ways: in Germany, there is negotiated network access under what is known as an associations agreement, and competition supervision by the Bundeskartellamt; in Austria, network access is given against a "postage stamp tariff", and an independent regulator has been set up.

(b) Electricity imports are minor in the case of supply to large customers and smaller distributors

(60) Imported electricity plays only a relatively small part in supply to Austrian electricity customers. At the level of energy trading there are substantial dealings in electricity, especially between Germany and Austria,[19] but at the level of structured supply to final consumers and small distributors there are only limited exports of electricity from Germany to Austria.

(61) In 2002 total sales to large customers in Austria amounted to 25.6 TWh. The Commission's enquiries have established that deliveries to large customers by German suppliers (EnBW and E.On)[20] amounted to less than 1 TWh. This is less than 3% of total sales to large customers in Austria. The Swiss supplier Atel did not supply any large customers. The Commission's market investigation did not give any indication that this situation might change decisively in the near future.

(62) The same applies to small distributors. In the course of its investigations the Commission asked Austrian distributors to state their electricity suppliers. Out of 75 private, municipal or local electricity utilities only one customer, a purchasing association of smaller distributors, said it had been supplied by a foreign supplier. The total electricity supplied to the 75 distributors in 2002 was about 3 500 GWh. The amount supplied by the foreign supplier to the purchasing association of smaller distributors in that year was less than 200 GWh. This is less than 3% of total sales to small distributors in Austria. Since then the foreign supplier has lost this customer, to Steweag-Steg, in which Verbund has a holding.

(c) Foreign suppliers have so far responded to Austrian invitations to tender only to a limited extent, and have practically never secured contracts

(63) Since the liberalisation of supply to large customers, those customers have changed their supplier in an appreciable number of cases. But as a rule the new supplier was

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19 Austria traditionally exports peak load power to Germany and imports base load power from Germany.

20 In Austria RWE supplies final consumers only through its Austrian subsidiary Kelag. Vattenfall has no dealings with final consumers in Austria.

Austrian. The same applies to small distributors, who have been less inclined to change than large customers. When tenders were called for, foreign suppliers put in bids only in a very few cases. The foreign suppliers involved were mainly EnBW in the case of large customers and Atel in the case of smaller distributors. In invitations to tender for supply contracts since the liberalisation, the 123 customers questioned in the course of the enquiries (48 industrial and large commercial consumers, including big chain customers,[21] and 75 smaller distributors) had asked foreign suppliers to submit a bid only in what was very much a minority of cases, and in almost all such cases the foreign supplier was EnBW. Only very rarely did foreign suppliers secure the contract. Once again the sole exception was EnBW: 4 of the 123 customers surveyed awarded the electricity supplier's contract to EnBW in the year 2000, 8 in 2001, and 12 in 2002. The first and second alternative suppliers were as a rule Austrian suppliers too, with the exception of EnBW in a few cases. EnBW's share of the market in supply to large customers was similarly small, at well below 3%. Atel's share of the market in supply to small distributors was always well below 5%. Other foreign suppliers did not operate in Austria, with the exception of a marginal presence of E.On on the large customer market.[22]

(64) Thus foreign suppliers export mainly on a wholesale basis, but do not deliver to final consumers and supply smaller distributors only to a limited extent.

(d) Although there are no technical barriers to access that might prevent foreign suppliers from expanding their business in Austria, market access is rendered difficult by established customer relationships and preferences, distribution costs, and a price level lower than that in Germany

(65) The small part played on the market by foreign suppliers cannot be attributed to technical barriers to access. The parties rightly point out that there are no bottlenecks in the interconnectors between Germany and Austria or between Switzerland and Austria. The interconnectors have a capacity equal to some 25% of Austrian electricity consumption.[23] In purely technical terms, therefore, substantial imports would be possible.

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21 "Chain" customers are customers that draw power from a large number of supply points. An example would be big retail chains.

22 At a late stage in the proceedings the parties submitted figures for conduct in respect of bids made to large customers of EnergieAllianz, which suggest that conduct in respect of bids to these customers was somewhat different. But the sample submitted by the parties is considerably smaller than the sample used in the Commission's investigation. In addition, the sample, with very few exceptions, includes no small Austrian distributors. In addition, it is not clear how many bids attributed to foreign suppliers genuinely originated with those suppliers, or how many bids were competitive offers that would have been seen by customers as possible alternative sources of supply. The bulk of foreign bids came from EnBW. For the other German suppliers the parties' figures confirm the statements made here.

23 Source: UCTE, Statistical Yearbook 2001. The notifying parties quote a figure over 25%, because they refer exclusively to the thermal transfer capacity of the interconnectors. But according to E-Control, only the net transfer capacity is relevant in practice, because that calculation takes account of the whole grid and makes projections on the basis of the weak points: it asks what capacities are in practice available on the interconnectors in order to ensure steady network operation in the event of the failure of a circuit or transformer.

(66) Inside the eastern control area, however, there is a bottleneck between north and south. The two 380 kV grids are linked by lines with the lower 220 kV voltage level. Bottlenecks of this kind are ultimately barriers to imports. Large deliveries for consumption in areas beyond the bottlenecks can quickly overload the grid. The grid operator then has to intervene and manage electricity flows in order to restore the security of the grid.

(67) The transfer charge payable for through-transmission of electricity to another control area (the cross-border tariff, or "CBT") acts as a barrier to entry only to a limited extent. As has already been said, Austria is divided into three control areas. In the eastern control area, comprising the entire country with the exception of Vorarlberg and the Tyrol, and in the east of the Tyrol too, Verbund operates the high-voltage grid and is responsible for maintaining the balance between production and consumption. The Vorarlberg and Tyrol control areas belong to the German control block. It is true that on electricity transmitted direct from Germany to the eastern control area there is a transfer charge of € 0.5/MWh.[24] But if the same electricity is routed through Vorarlberg and the Tyrol there is in fact no transfer charge to be paid. On legal grounds no transfer charges are payable on through-transmission between control areas inside Austria, and because the Vorarlberg and Tyrol control areas belong to the German control block there is no transfer charge for through-transmission from Germany to those areas either.

(68) Competitors have submitted, however, that there are a number of barriers to access that make it very difficult for them to enter the market; these include:

– distribution and customer acquisition costs;

– the required minimum size of the balance group;

– the fragmentation of network operators; and

– the need for a large proportion of hydroelectric power in the electricity mix, especially in the case of small customers.

(69) The effect of these barriers to access is that the Austrian markets in supply to large customers, small distributors and small customers are still not integrated with the German markets, even though there are no major technical barriers. This is so despite the measures already taken or still to be taken in respect of the electricity market as part of the single market programme, and especially the new Electricity Market Directive shortly to be enacted.[25] These measures are intended to open up domestic markets that were previously isolated from one another, but the Commission's enquiries show that the sought-after results are not certain and immediate enough to justify the conclusion that the relevant geographic market is in fact larger. The same applies with respect to the forthcoming enlargement of the European Union, because for the integration of the electricity markets in Austria and those of neighbouring candidate countries, the Czech

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24 The European Association of Transmission System Operators, ETSO, is currently in the closing stages of discussion of a complete abolition of transfer charges with effect from 2004, and their replacement by other methods of setting prices for cross-border transfers of electricity.

25 Relevant Market Definition Notice (see footnote 10), paragraph 32. On the proposed amendment of the Electricity Market Directive, see paragraph 103.

Republic, Slovakia, Hungary and Slovenia, the technical and economic requisites are satisfied to a far smaller extent than they are in the case of integration with the markets of Germany.

(70) Because of the distribution costs that have to be incurred, entry to the Austrian market with a view to long-term supply to distributors and large customers is worthwhile only if a certain minimum number of customers can be secured. As well as bearing the costs of establishing distribution arrangements, which are needed for any market entry, a new supplier entering the market has to set up a balance group which is big enough to keep the risk of having to pay for balancing energy within reasonable limits. The offset between unexpected consumption surpluses and deficits is easier within a big balance group than it is within the balance group of a new entrant, which is necessarily small: such competitors inevitably have a higher percentage requirement of balancing energy, involving a higher risk of increased costs, to make up what they cannot meet themselves for lack of generating capacity of their own in the control area.

(71) That the costs of balancing energy, and especially the cost risk they involve, form a very appreciable barrier to entry was stated by the overwhelming majority of market participants in the Commission's market investigation.

(72) A further cost factor in Austria is the fragmentation of network operators. At local level Austria is covered by more than 100 network operators, each with its own through-transmission costs. This makes market entry difficult for suppliers who do not possess a detailed knowledge of the market. Even though larger industrial firms often take electricity at higher network levels, and are consequently less affected by the number of operators at the lower network level, this fragmentation in the lower segments of the large customer market does have the effect of a barrier to market entry.

(73) In addition, for marketing reasons, a new entrant has to have a sizeable hydroelectric component in the electricity mix in order to supply small customers. In Austrian electricity generation hydroelectric power plays a paramount role, accounting for more than 67% of total generation. Especially in the case of supply to small customers, this has the effect of a further barrier to entry. A substantial proportion of small Austrian customers attach great importance to "clean" electricity, that is to say electricity generated using domestic water power rather than fossil or nuclear fuels. On the small customers market, therefore, Austrian energy suppliers, whose capacity is mainly hydroelectric, have an additional advantage over foreign suppliers, who have to ensure that they have sufficient availability of hydroelectric power and build up an appropriate brand image for their small customer business.

(74) A study commissioned by the parties from the firm Frontier Economics argues that a relatively small increase in electricity prices for large Austrian customers, of around [0-5%]*, would be enough to make the investment in distribution costs and customer acquisition costs on entering the market profitable in the short to medium term. Applying the so-called SSNIP test, the conclusion is that the relevant market extends beyond Austria. The following points need to be made here.

(75) The Frontier Economics study does not — as the SSNIP test would suggest — explain satisfactorily how an increase in the prices of the incumbent (regarded as a hypothetical monopolistic undertaking) and the subsequent movement of customers to one or more new market entrants would affect its profitability. Even if a new market entry coincides

with a small but permanent price increase (in the range of 5-10%) by the monopolistic undertaking and the undertaking loses market share as a result, this still does not prove that it would not profit from the price increase nevertheless, on account of a marked increase in the profit margin.[26]

(76) Another crucial weakness in the Frontier Economics model is that it fails to take sufficient account of real competitive prices, basing itself on notional prices instead.[27] These notional prices are higher than the real prices for two reasons. First, the study erroneously equates "opportunity costs" (which serve as a basis for the hypothetical calculation of the competitive price in the market for large customers) with (wholesale) trading prices, and in so doing fails to take account of the fact that the vendor on the (wholesale) trading market incurs (opportunity) costs over and above its production costs (i.e. the cost price) and the achievable profit margins.[28] If these are taken into account, it is clear that the sale of electricity on the (wholesale) trading market becomes less attractive for Austrian producers than direct sales to final consumers, and hence that the competitive price for large customers in Austria is overestimated.[29] Second, the Commission's market investigation revealed that retail prices in the Austrian market for large consumers are often lower than the (wholesale) trading prices. The study therefore overestimates the actual competitive prices in Austria and hence the scope for profit for a new entrant following a further price increase.

(77) The statements made by market participants suggest that the parties' assumption regarding the acquisition discount to be granted by new entrants is also somewhat unreliable. On this evidence, it seems highly probable that the discount is in fact higher than assumed by the parties and that even according to the parties' model — which is based on hypothetical assumptions — entry would become profitable in the short term only after a price increase of well over 5%.[30]

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26 Relevant Market Definition Notice (see footnote 10), paragraph 17.

27 "Since the market for service-oriented customers is in a transitional phase, and the historical prices for last year (2002) give little indication of the prices to be expected in this and subsequent years, we use a hypothetical approach as a basis for calculating the competitive price" (Frontier Economics, *Gutachten zur Frage der Marktabgrenzung*, p. 61).

28 For more details see paragraph 89.

29 Conversely, these costs, which — except for the CBT — also fall on the buyer, push up the possible arbitrage costs of a new entrant wishing to sell traded electricity to final consumers in Austria.

30 For example, the Frontier Economics study bases its estimate of the short-term profitability of a new entrant — who retains customers for one year — on the assumption of a [<1%]* acquisition discount for customers with an annual consumption of over 100 GWh and a discount of [<5%]* for customers with an annual consumption of 4-20 GWh and 20-100 GWh. In their reply to the Commission's request for information of 2 May 2003, the parties extended this assumption of a [<5%]* discount to large customers with an annual consumption of 0.1-4 GWh.

By contrast, the Commission's market investigation of undertakings whose competitive situation in the eastern control area is comparable to that of a new entrant came up with average values which, at the upper end of the scale, were 300%, 63%, 100% and 183% (for customers consuming >100 GWh, 20-100 GWh, 4-20 GWh and 0.1-4 GWh) higher than the assumptions made in the Frontier Economics study. Even at the lower end of the scale only one value, that of the 20-100 GWh customer group, fell within the range of the

(78) To sum up, there are serious doubts as to the practical relevance and hence the validity of the scenario presented by the parties in the Frontier Economics study. Indeed, when other real factors are taken into account, the most likely conclusion appears to be that in some cases price increases of far more than 5% would certainly be profitable for a hypothetical monopolistic undertaking in the market to supply large customers and small distributors in Austria.

(e) The retail price level is lower in Austria than in the neighbouring Member States

(79) In addition to all these barriers to entry, there is the decisive point that the level of the prices charged to large customers in Austria is well below the German level. According to information supplied by the parties, the gap in prices to industrial customers was about 20% in 2001, and in the case of households it was twice as big.[31]

(80) In their reply to the Statement of Objections and at the hearing the parties claimed that there was already substantial convergence of retail prices in Germany and Austria. However, the parties failed to produce any concrete evidence to support this claim, which runs counter to statements by other market participants. The Commission has assessed the statements by large customers and small distributors regarding the net

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study's assumptions, whereas the other three values were in some cases much higher, by 50% for the over 100 GWh group, by 25% for the 4-20 GWh group, and by 133% for the 0.1-4 GWh group. It is therefore impossible to argue that the study's assumptions correspond to the real market conditions on this crucial point.

In reply to the Commission's request for information of 2 May 2003, the parties presented a sensitivity analysis of the study's results in relation to higher acquisition costs. However, this analysis went no further than acquisition costs that were 50% higher than the original estimates. As explained above, in some cases this lies well below the results of the market investigation. However, even on these assumptions a price increase of over 5% was required to make a profit on customers with annual consumption of 4-20 GWh and 20-100 GWh. For large customers consuming 0.1-4 GWh the profit threshold of new entrants was a price increase of over 5% even without any increase in the assumed acquisition costs in the context of a sensitivity analysis (no such analysis was undertaken by the parties). (For this group of customers the market investigation showed that acquisition costs were 133%-188% above the value stated by the parties. This suggests that an increase in prices of well over 10% would be needed before profitability could be reached in this customer group.)

So a critical view of the assumptions made in the Frontier Economics study leads to the conclusion that price increases of well over 5% would be required to make market entry profitable in the short term under the Frontier Economics model.

Note on the market investigation: the Commission asked for the views of seven undertakings which are sufficiently familiar with the market in Austria and whose market position in the eastern control area is comparable to that of a market entrant, namely the German undertakings E.On and EnBW, the Swiss firm Atel, the western Austrian suppliers Tiwag and VKW and two undertakings that are operate only in the lowest segment of the large customer market — MyElectric and Ökostrom. The Commission received replies from six of the seven undertakings, which in some cases quoted an upper and a lower limit on discounts for the one-year customer acquisition of market entrants. The question they were asked was, "In your experience what is the first-year acquisition discount which your firm may obtain from a supplier at present *for the same electricity product* in order to induce a customer in the APG area to switch supplier? Please give this discount *as a % of the net electricity price* (excluding through-transmission costs and extra charges)."

31 Presentation, "Österreichische Stromlösung", January 2002, p. 9. Prices for consumption of 24 GWh per year. Source: Eurostat, international regulators.

energy prices they have paid from 2000 to 2003. This statistical analysis shows that, overall, the prices paid in Austria by the market participants consulted appear to have remained at the same level since the end of 2001. On average prices fell substantially in 2001 — by around 15% for large customers and by around 20% for small distributors. After another slight drop in 2002 (around 0-5% for large customers and around 5-10% for small distributors), prices rose again slightly in 2003 by an average of around 2-5% for large customers and small distributors. Combined with the above-mentioned statements by the parties on price levels in Austria in 2001, this means that prices in Austria must still be well below those in Germany, especially as the parties do not assume a drop in prices in Germany.

(81) A major factor in this difference in prices is the low average production costs of Austrian hydroelectric generators. Against this the parties argue that hydroelectric schemes do not necessarily enjoy a production cost advantage, because their capital costs are higher than those of other power stations. But this argument is not convincing, for the following reasons.

(82) A large proportion of Austrian electricity production is hydroelectric based. This applies especially to Verbund: hydroelectric power accounts for [about 90%]* of its total electricity output. [More than two thirds]* of Verbund's hydroelectric power is generated in run-of-river power stations, and [less than one third]* in reservoir power stations. From information on the cost structure of hydroelectric stations supplied by the parties it appears that run-of-river power stations are written off over a period of […]* years. Of the electricity generated by Verbund in run-of-river power stations, [well over half] is generated in stations more than […]* years old; the bulk of Verbund's hydroelectric production is therefore extremely cheap. By [the year …]* another […%]* of Verbund's run-of-river capacity will have been fully written off. From information supplied by Verbund it also appears that the period of depreciation of reservoir power stations is […]* years. Of Verbund's reservoir station output, […]* is generated in stations more than […]* years old. By [the year …]* another […]* of Verbund's reservoir station capacity will have reached the limit for full depreciation. Less than [10-30%]* of Verbund's reservoir station output comes from power stations built in the last […]* years.

(83) In the case of more recent run-of-river stations (and one thermal station) another cost factor of potential benefit to Verbund is the possibility of claiming compensation for "stranded costs".[32]

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32 In order to compensate for the higher costs of unprofitable power stations that were built in the expectation of continued monopoly rights and on the basis of obligations imposed and guarantees of operation given by the authorities ("stranded costs"), the Electricity Market Directive provides that aid may be granted for a limited time. By decision of 25 July 2001 the Commission authorised aid of €560 million for a number of run-of-river hydroelectric stations and one thermal station belonging to Verbund (state aid measure No N 34/99, Austria, compensation of stranded costs).

The parties point out that this decision is unlikely to be put into effect in Austria. Nevertheless, a partial limit on production cost risks is a beneficial cost factor.

(84) For these reasons it can be accepted that the largest Austrian electricity producer, Verbund, has a favourable production cost base. This finding can be extrapolated to Austrian electricity production as a whole.

(85) However, the notifying parties submit that since liberalisation wholesale prices in Austria have tended to draw towards the German level. According to the wholesale prices recorded by Platts, the price differences shrank further in 2002 and came close to German prices. The parties conclude that the price level in Austria is not a barrier to entry.

(86) When seeking to define the geographic market, however, one must not look at the cost price, that is to say the wholesale price. Although many electricity customers have a price adjustment clause in their contracts with their suppliers which refers to the level of wholesale prices, the final price is not identical to the wholesale price.

(87) Since liberalisation, prices to final consumers in Austria have been well below prices in the neighbouring Member States, as shown above. In the case of prices to small customers, the parties do not dispute this fact. But retail prices to large customers in particular fell appreciably when liberalisation began. Although wholesale prices have risen in Austria in recent years, retail prices have not moved to the same extent. They continue to be below the level of prices in the neighbouring Member States.

(88) The parties to the merger argue that this situation is explained by predatory pricing policies pursued immediately after liberalisation, and can only be a transitory phenomenon, as otherwise Austrian electricity producers would find it more economic — even in the short term — to sell electricity on the international markets instead of supplying it to final consumers in Austria at possibly lower prices (arbitrage).

(89) First of all it must be pointed out that if markets had already been integrated the parties' explanation should also apply to Germany, and the price level on retail markets in Germany should therefore also have fallen temporarily below the market price. However, this is not the case, nor is any such claim made by the parties. With regard to likely developments in the near future, the parties' argument is not convincing, for the following reasons.

(90) First, the sale of energy on the trading markets entails significant costs and risks. When exporting energy for trading purposes, Austrian electricity suppliers must factor in the transport costs, which consist of through-transmission charges, network costs and the CBT payable on electricity leaving Austria — currently EUR 0.5 per MWh. Selling electricity on the trading markets in, for example, Germany also involves administrative and other transaction costs (e.g. charges for trading on the stock exchange). Moreover, demand and prices are much more volatile on the trading markets than in the retail business, while the risk of default on the trading market is much higher, as the Enron case has shown. The notifying parties have clearly taken these points on board. At the hearing they cited as one of EnergieAllianz's main reasons for the proposed merger its efforts to reduce its dependence on the "volatile international trading markets".

(91) Second, according to the information available to the Commission, Austrian undertakings have a strong tendency to hold on to customers in their home supply area. This is explained by the fact that the Austrian *Land* suppliers are under the majority control of regional authorities. There is also an economic justification for this strategy in that the density of customers in a given area is a pertinent factor in calculating distribution costs.

This basic corporate strategy of Austrian electricity suppliers, which is also pursued to a limited extent by Verbund vis-à-vis "its" Austrian customers, will continue to exist after the merger and provide an incentive to keep Austrian customers even at very favourable prices. The Commission has even been told that this fact alone — and the close customer relations it generates — raises additional barriers to market entry.

(92) Finally, mention must also be made of the significant volume of low-cost in-house production in Austria, which rules out any clear correlation between the cost prices of Austrian electricity suppliers and prices on the trading markets.

(93) For the above-mentioned reasons it cannot be assumed that developments in retail prices and in the prices for supplying small distributors in Austria and Germany will be driven by sufficiently homogeneous factors in the foreseeable future, even if the cost factor of trading prices were to behave in similar fashion. This is not belied by the fact that, because of commercial considerations, Austrian electricity suppliers, including the parties to the merger, are striving to increase profit margins by tying retail prices as closely as possible to developments in trading prices, which have risen sharply over the last two years.

(94) For the reasons set out, therefore, the lower price level in Austria acts as a barrier to entry. A significant number of the parties' current and potential competitors have confirmed as much in the market investigation.

(f) Special factors in defining the geographic market for small customers

(95) With regard to the relevant geographic market in supply to small customers, the notifying parties argue that in Austria this market still has strong local and regional characteristics. It is true that it was not liberalised until October 2001, and the switching rates of small customers are still low, so that the overwhelming majority of small Austrian customers still obtain electricity from their original local and regional distributors. The parties therefore deduce that at present the traditional supply area of each Austrian distributor constitutes a separate relevant geographic market in supply to small customers.

(96) However, statements by the parties reveal that customers do switch to other Austrian regional suppliers, in particular new suppliers such as Switch (a subsidiary of EnergieAllianz), MyElectric and Unsere Wasserkraft, or other firms supplying environment-friendly electricity, whether nationwide or in the eastern control area. Small customers also come together to form supra-regional purchasing pools and organise their supplies of electricity at a level reaching beyond their region, though still within Austria.[33] This is evidence of a definite trend towards the integration of small customer markets within Austria, without however extending the market beyond Austria's borders.

(g) Conclusion

(97) For these reasons, it must be supposed that the geographic markets in supply to large customers, small distributors and regional suppliers do not extend beyond Austria.

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[33] It is of less importance here whether these pools of small electricity consumers should already be classified in the lower segment of the large customer market or still in the small customer market. Internal documents of the parties suggest that the parties are trying to keep these customers associated with the market for small customers.

2. The market in supply to Austrian regional distributors could extend beyond Austria

(98) The parties express the view that the geographic market in supply to the large regional distributors does not extend beyond Austria. However, for the purposes of this Decision this question need not be answered.

(99) The fact that the Austrian *Land* suppliers traditionally draw most of their electricity requirements from Verbund, apart from what they produce themselves, does suggest a geographic market confined to Austria, as does the fact that significant volumes are also supplied between *Land* corporations. Only since liberalisation have foreign suppliers and electricity traders come into the picture as sources of electricity. Individual *Land* suppliers have argued that, because of the volumes of electricity required, the low prices in Austria and the need for a high proportion of hydroelectric power, they are very much dependent on supplies from Verbund in order to continue delivering power to small customers.

(100) On the other hand, there are signs of a geographic market extending beyond Austria. The parties have submitted that in 2002 the regional suppliers that were members of EnergieAllianz received [>60%]* of their supplies from non-Austrian sources. Only around [<30%]* of EnergieAllianz's requirements for bought-in electricity came from Verbund, while [<15%]* came from other Austrian suppliers. Given that EnergieAllianz makes only relatively small purchases on the trading market, it can be assumed that a major share of the electricity it delivers to customers but does not produce itself comes from foreign suppliers. The Austrian regional distributors also draw a significant proportion of their electricity supplies from non-Austrian suppliers. This is particularly true of Tiwag and VKW, whose supply areas technically belong to the German control block and which traditionally obtain considerable amounts of electricity from Germany.

(101) Nevertheless, the question of the geographic market in the supply to regional distributors can be left open, as even if this market were confined to Austria, the proposed merger would not create or strengthen a dominant position on that market.

3. A conceivable geographic market in the provision of balancing energy would be confined to the eastern control area

(102) If the provision of balancing energy is taken to be a relevant product market, that market is geographically confined to the particular control area. Under the rules that govern European transmission grids, balancing energy can be provided in Austria only inside a control area. The minute reserve component in balancing energy, which is decisive for purposes of cost, cannot be transmitted over control area borders. Even taking into account the ongoing negotiations on opening up the eastern control area to Germany, this situation is unlikely to change in the short term. In the present case the relevant geographic market would therefore be the eastern control area, for which Verbund is the responsible control area manager.

4. Effects of liberalisation measures

(103) In all probability a new Electricity Market Directive and a Regulation on cross-border energy exchanges will enter into force in the near future.[34] Some major components in this legislative package are to take effect on 1 July 2004, and other aspects are to take effect by 1 July 2007. The package comprises a series of provisions that can be expected to make market entry by foreign providers considerably easier in the medium term. The main such provisions concern with network access, tougher unbundling measures, and harmonised rules on cross-border transfers of electricity. This aspect is considered in section VIII, as part of the assessment of commitments.

D. EFFECT OF THE MERGER

1. The merger would create a dominant position on the market in supply to large customers and small distributors

(104) The proposed merger would place the firms concerned in a dominant position on the market or markets in the supply of electricity to large customers and small distributors in Austria.

(105) The Court of Justice of the European Communities has defined a dominant position as a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of consumers. Such a position does not preclude some competition, but enables the undertaking which profits by it, if not to determine, at least to have an appreciable influence on the conditions under which that competition will develop, and in any case to act largely in disregard of it so long as such conduct does not operate to its detriment.

(106) The existence of a dominant position may derive from several factors which, taken separately, are not necessarily determinative but among these factors a highly important one is the existence of very large market shares. In addition, the relationship between the market shares of the undertakings involved in the concentration and their competitors,

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[34] Common Position (EC) No 5/2003 of 3 February 2003 adopted by the Council, acting in accordance with the procedure referred to in Article 251 of the Treaty establishing the European Community, with a view to adopting a Directive of the European Parliament and of the Council concerning common rules for the internal market in electricity and repealing Directive 96/92/EC: OJ C 50 E, 4.3.2003, p. 15; and, most recently, European Parliament legislative resolution on the Council common position for adopting a European Parliament and Council directive on common rules for the internal market in electricity and repealing Directive 96/92/EC (15528/2/2002 – C5-0034/2003 – 2001/0077(COD)), 4.6.2003: P5_TA-PROV(2003)0242.

Common Position (EC) No 4/2003 of 3 February 2003 adopted by the Council, acting in accordance with the procedure referred to in Article 251 of the Treaty establishing the European Community, with a view to adopting a regulation of the European Parliament and of the Council on conditions for access to the network for cross-border exchanges in electricity: OJ C 50 E, 4.3.2003, p. 1; and, most recently, European Parliament legislative resolution on the Council common position for adopting a European Parliament and Council regulation on conditions for access to the network for cross-border exchanges in electricity (15527/2/2002 – C5-0036/2003 – 2001/0078(COD)), 4.6.2003: P5_TA-PROV(2003)0244.

especially those of the next largest, is relevant evidence of the existence of a dominant position.[35]

(a) The merger would give Verbund/EnergieAllianz a very high combined market share

(107) The merger would result in very high combined market share for the firms involved, which, according to the case-law of the Court of Justice, is itself an indication of a dominant position.[36]

(108) The structure of the market in supply to large customers is shown in the following table:

Table 2
Electricity sales to special customers 2001

Supplier	Supply (GWh)	Market share
Verbund	**[1 500–3 500]***	**[5–15%]***
Bewag	[0–2 000]*	[0–10%]*
Energie AG OÖ	[1 500–3 500]*	[5–15%]*
EVN	[1 500–3 500]*	[5–15%]*
Linz Strom AG	[0–2 000]*	[0–10%]*
Wienstrom	[3 500–7 000]*	[15-25%]*
total EnergieAllianz	**[10 500–13 000]***	**[45–55%]***
Steweag-Steg	**[1 500–3 500]***	**[5–15%]***
Kelag	[0–2 000]*	[0–10%]*
Salzburg AG	[0–2 000]*	[0–10%]*
Tiwag	[0–2 000]*	[0–10%]*
VIW/VKW	[0–2 000]*	[0–10%]*
Other	[0–2 000]*	[0–10%]*
Total	**24 900**	**100.0%**

Source: Information from Verbund in response to request for information of 28 February 2003

(109) Verbund's share of the market in supply to large customers in 2001 was [5–15%]*. The market share of the companies belonging to EnergieAllianz was [45-55%]*. The direct combined market share of the parties to the merger was therefore [55–65%]*. In addition, Steweag-Steg, which is jointly controlled by Verbund and Estag, achieved a market share of [5–15%]*. All remaining competitors have market shares of less than 10%.[37]

(110) The Commission's investigations have established that the structure of the market in supply to small distributors is as follows:

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35 Court of Justice in Case 85/76 *Hoffmann-La Roche* v *Commission* [1979] ECR 461, paragraph 39; see also Court of First Instance in Case T-102/96 *Gencor* v *Commission* [1999] ECR II-753, paragraphs 201 and 202.

36 *Hoffmann-La Roche* (see footnote 35), paragraph 39.

37 On market shares in 2002, see paragraph 122.

Table 3
Electricity sales to small distributors

	2000	2001	2002
Verbund	**0-5%**	**0-5%**	**5-10%**
EnergieAllianz	**40-50%**	**30-40%**	**30-40%**
Parties combined	40-55%	30-45%	35-50%
Steweag-Steg	30-40%	30-40%	20-30%
Salzburg AG	0-5%	0-5%	0-5%
Kelag	0-5%	0-5%	0-5%
Atel	0%	0-5%	0-5%
Tiwag	10-15%	15-20%	15-20%
	100%	**100%**	**100%**

Source: Commission's market investigation (data from the parties and competitors). In order to avoid revealing any business secrets, only ranges are given.

(111) In 2002, Verbund and EnergieAllianz had market shares of between 35% and 50%. Steweag-Steg's share was 20-30%. The merged entity, including Steweag-Steg (jointly controlled by Verbund), would therefore have a market share of 70-80%. Its remaining competitors, with one exception, have market shares of less than 5%.[38]

(112) Besides the parties, the remaining competitors in both of the markets affected are basically the *Land* corporations Salzburg AG, Kelag, Tiwag and VKW. The gap between their market shares and those of Verbund/EnergieAllianz will not be significantly narrowed in the foreseeable future. Moreover, the parties to the merger have holdings in two of their remaining competitors. As already mentioned, Verbund has a minority shareholding in Kelag, which is jointly controlled by the *Land* of Carinthia and RWE. Besides the *Land* and the City of Salzburg, Energie OÖ has a 26.13% share in Salzburg AG. Energie OÖ's shareholding carries participation rights conferred by the articles of association, relating in particular to the appointment of the managing board and major energy transactions, which go beyond the statutory rights of a minority shareholder.[39]

(113) Since the parties, with Steweag-Steg, have similar shares of the markets for both small distributors and large customers (in both cases over 70%), and since the structure of the competition is similarly fragmented on both markets, the same applies if we assume only one market for the supply of large customers and small distributors.

(b) The parties' pre-eminent position would be secured by their leading position in electricity generation

(114) The parties' pre-eminent market position is primarily based on their position on the upstream electricity-generation market. Their position on this market has the direct result of increasing barriers to entry on the markets in supply to large customers and small distributors, and increases the risk that existing competitors will be marginalised still

38 Tiwag's market share falls to below 15% if supply to the Innsbruck municipal plants, which are affiliated with Tiwag, is left out. At the same time, the combined market share of the parties would increase by a number of percentage points.

39 Reply from Salzburg AG dated 27 February 2003 to a request for information from the Commission.

further. It is therefore unlikely that the parties' position on the relevant market will be disputed in the foreseeable future.

(115) Verbund's share in gross electricity generation in Austria in 2001 was around [35–45%]*. Its already pre-eminent position on this market prior to the merger would be considerably strengthened by the addition of EnergieAllianz's capability (some [10–20%]* of generation in Austria), bringing the post-merger combined share of the parties to some [55–65%]* of total electricity generation in Austria.

(116) Verbund/EnergieAllianz's position would also ensure that they could improve the cost base of generation by closing down unprofitable thermal stations and could cover the generation costs of a considerable block of hydroelectric resources by claiming, depending on the market situation, compensation for stranded costs.[40]

(117) Of particular significance in this connection is the parties' position on the market for hydroelectric power generation. In Austria, tariff customers in particular set great store by being supplied with "clean" electricity, i.e. electricity which has not been generated by nuclear power and which to a large extent comes from local hydroelectric sources. In addition, electricity from hydroelectric sources is cheap to generate, especially where the power stations concerned have been written off.[41]

(118) This dependence of their competitors on the parties to the merger applies particularly to small local distributors, which often — despite the possibility of through-transmission — in practice cannot, for lack of their own resources, take part in the wholesale market and thus depend on Verbund/EnergieAllianz for their electricity supply. Numerous small private and municipal power utilities stated, in the course of the Commission's investigation, that their suppliers, with which they competed for delivery to large customers, supplied industrial and commercial customers at cheaper prices and on better terms than themselves.

(c) The costs of balancing energy place the remaining competitors at a disadvantage vis-à-vis Verbund/EnergieAllianz and at the same time constitute a barrier to entry for new competitors

(119) The Commission's investigations have shown that the risk of facing unplanned costs for balancing energy is greater for smaller market players than for large ones. This was the line taken by a majority of the competitors which provided the Commission with comments on the subject. Many of them consider balancing energy to be a significant factor in the minimum size required for a new competitor to enter the market. The merger will make it even easier for the parties to achieve cost benefits through the coordination of their balancing energy costs and the fact that these costs will be easier to plan. The impossibility for remaining and new competitors to derive similar benefits from their size will help to marginalise remaining competitors even further and make market entry more difficult.[42] The merger will therefore raise the threshold for entering

[40] See footnote 32.

[41] See paragraph 82.

[42] This follows from the statistical fact that within the large-customer market the balancing energy risk — and with it the balancing energy cost risk — falls as the size of the balance group increases. Likewise, the

the markets in supply to large customers and small distributors, which is already high for small companies and new entrants given the difficulty of planning balancing energy costs.

(120) This effect would be heightened by the parties' pre-eminent position in the provision of balancing energy. Verbund and EnergieAllianz are the largest suppliers in this area, with a combined market share, depending on the supply period, of between 60% and 90%.

(d) The merger would eliminate Verbund as a current and potential competitor and would thus remove a major competitive force in Austria

(121) Following the merger, Verbund would cease to compete to attract customers, and will disappear as a current and potential competitive force. Following the liberalisation of the Austrian electricity market, Verbund, as the largest electricity generator, was the most important and active new entrant on the markets in supply to large customers and distributors.

(122) Thus, it was able (without Steweag-Steg) to increase its share of the large-customer market from [5–15%]* to [10–20%]* between 2000 and 2002. On this market, it is by far the biggest competitor with EnergieAllianz, which increased its market share in the same period [by 0–5%]*. One other company, EnBW, was able to increase its market share, but still by significantly less than the parties.

(123) The same is true of the market in supply to small distributors. Enquiries made by the Commission of small private and municipal power utilities in the course of its investigation revealed that, when power procurement contracts were put out to tender after liberalisation, in many cases competition for the contract was between EnergieAllianz and Verbund. The previous supplier (regional supplier) was often in a privileged position in these negotiations owing to the regional customer loyalty of the municipal utilities, and it frequently obtained the contract. This underlines the strong position of the regional suppliers in this respect.

(124) As a result of the merger, therefore, Verbund would disappear as a competitive force from the market for large customers and the market in supply to small distributors. On both markets, Verbund was the biggest challenger to the already very strong position of EnergieAllianz. Given the combined pre-eminent position of Verbund/EnergieAllianz, therefore, the ensuing market structure is likely to be consolidated. The impact of the legislation discussed in paragraph 103 cannot be expected with sufficient certainty to counter such consolidation within a sufficiently short time.

(e) Conclusion

(125) The merger would combine the existing generation and sales activities of Verbund and EnergieAllianz into a single economic entity, which would hold a pre-eminent market

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parties' argument that very small balance groups had lower balancing energy costs, since they did not reach the threshold of energy deviation that triggered the minute reserve, is not convincing, at least as far as the large-customer market is concerned. This is because in the large-customer sector even a few customers can purchase significant amounts of energy.

position compared with its remaining competitors. Verbund would be eliminated as a current and potential competitor, although prior to the merger it was a major competitive force in the only very recently liberalised Austrian electricity market. This would considerably worsen the structure of competition, and decidedly reduce alternatives for large customers and small distributors. The merger would thus create a dominant position on the Austrian markets in supply to large customers and smaller distributors.

2. The merger would strengthen a dominant position on the market in supply to small customers

(126) The merger is likely to strengthen EnergieAllianz's dominant position on the market in the supply of electricity to small customers (households and small businesses) in Austria.

(a) Even before the merger, EnergieAllianz already has a dominant position on the market in the supply of electricity to small customers

(127) The market in supply to small customers is structured as follows:

Table 4
Electricity supply to Austrian tariff customers in 2001

Supplier	Supply (GWh)	Market share
Verbund	**[0]***	**[0%]**
Bewag	[0-2 000]*	[0-10%]*
Energie AG OÖ	[1 000-3 000]*	[5-15%]*
EVN	[2 000-4 000]*	[10-20%]*
Linz Strom AG	[0-2 000]*	[0-10%]*
Wienstrom	[3 000-5 500]*	[15-25%]*
total EnergieAllianz	**[10 000-12 500]***	**[45-55%]***
Steweag-Steg	**[0-2 000]***	**[0-10%]***
Kelag	[0-2 000]*	[0-10%]*
Salzburg AG	[0-2 000]*	[0-10%]*
Tiwag	[0-2 000]*	[0-10%]*
VIW/VKW	[0-2 000]*	[0-10%]*
Others	[3 000-5 500]*	[15-25%]*
Total direct supply	**22 992**	**100%**

Source: Information provided by Verbund in response to request for information of 28 February 2003

(128) So, EnergieAllianz alone already has a market share of [45-55%]*, which is sufficient reason to suspect the existence of a dominant position. That share is approximately eight times the market share of EnergieAllianz's nearest competitors Steweag-Steg and Kelag. A large proportion of the market ([15-25%]*) is divided between numerous small and very small private or municipal distributors. The traditional supply area of the firms in EnergieAllianz, on the other hand, covers most of Austria.

(129) Given the reluctance of Austrian final consumers to switch supplier, it is unlikely that this market situation will change much in the short to medium term. Only 1.9% of small

customers in Austria changed their electricity supplier in the first twelve months after liberalisation.[43] Switching rates collected by EnergieAllianz over a period of 14 months give a very similar figure.[44] What is noticeable is that a significant proportion (between 20% and 30%) of these customers switched between suppliers within EnergieAllianz, and that consequently EnergieAllianz as a whole showed a switching rate that was below average. EnergieAllianz pursues a dual-brand strategy, whereby supply from the respective regional supplier belonging to EnergieAllianz is supplemented by a cheaper supplier from EnergieAllianz, Switch, in order to retain price-sensitive customers likely to be lost to new suppliers. Internal documents from EnergieAllianz show that only Switch positioned itself in price terms in relation to the new suppliers. It was therefore possible for EnergieAllianz to behave to an appreciable extent independently of its competitors and customers.

(130) An overall assessment of these factors shows that, prior to the merger, EnergieAllianz already has a dominant position on the small customers market.

(b) The merger would increase EnergieAllianz's already very high market share

(131) Although Verbund's current share of the small-customer market is small, Steweag-Steg, which is jointly controlled by Verbund, has a [0-10%]* market share. With Steweag-Steg, Verbund/EnergieAllianz's market share would come to [50-60%]* and thus to approximately ten times the market share of the nearest remaining competitor. Given the existing market structure, this addition of market share is strong evidence that the merger would strengthen a dominant position.

(c) The merger would eliminate Verbund as a current and potential competitor and thus a significant force for competition on the household customers market in Austria

(132) A majority of household customers who have switched supplier since the start of liberalisation switched to a company in which Verbund had an interest, namely MyElectric or Unsere Wasserkraft (formerly RWA Wasserkraft). More than [35-45%]* of all customers who switched from the largest EnergieAllianz suppliers, EVN and Wienstrom, switched to one of these two companies. According to figures from EnergieAllianz, as much as [75-85%]* of small customers formerly supplied by EnergieAllianz switched between July 2002 and March 2003 to MyElectric or Unsere Wasserkraft. While Verbund has reduced its share in Unsere Wasserkraft and while, as is clear from internal documents,[45] this was done in connection with the merger, this does not change the fact that, through its holdings, Verbund is still a challenger to EnergieAllianz on a market in which switching rates are still low. Further evidence of

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[43] Figure based on amounts purchased; 0.8% of households and 3% of other tariff customers E-Control, Annual Report 2002, p. 70.

[44] Annex 10 to EnergieAllianz's reply to the Commission's request for information of 28 February 2003. The data for WienEnergie have not been included, because the reply was incomplete in this respect.

[45] Verbund-Austrian Power Vertriebs GmbH (HGB) shareholders' committee, 7th meeting, 28 November 2002, agenda, item 3.

this is the fact that a significant proportion (more than [20-25%]*) of those switching from EnergieAllianz switched directly to Verbund.[46]

(d) Existing links between Verbund/EnergieAllianz and their competitors, their position on neighbouring markets and specific barriers to entering the small customers market also contribute to strengthening their dominant position

(133) In addition to the links between Verbund/EnergieAllianz and their competitors already described in relation to the markets for large customers and small distributors, a further factor in supply to small customers is that such customers are often interested in being supplied with electricity and gas at the same time. For many customers who purchase both sources of energy, the annual costs of gas exceed those of electrical energy. Numerous suppliers of small customers, especially municipal utilities, are therefore active in both areas ("multi-utilities").

(134) EnergieAllianz has a very strong position in natural gas in Austria as a supplier of gas to final consumers and as a gas wholesaler, the latter through a joint venture with OMV, Econgas, and a joint venture that its partner EVN has with E.On. This also makes market entry and expansion more difficult for rival suppliers on the market in the supply of electricity to households, either because they themselves do not supply gas or because they depend on Econgas for their gas supply.[47]

(135) The barriers to entering the market in supply to small customers are high. This is because of the reluctance of small customers to switch supplier and the relatively high costs of advertising and other measures to attract and support customers. In this area, it is also necessary to invest considerable sums in building up brands. Suppliers without sufficient access to hydroelectric resources or similar "ecological" energy are at a serious disadvantage in Austria.

(136) Generally, municipal utilities depend on supply in the form of what is known as "full supply". In addition to various technical and administrative services, full supply includes the supply of balancing energy. This increases the municipal utilities' dependence on the parties, who are large providers of such services.

(e) Conclusion

(137) The merger would strengthen and secure EnergieAllianz's existing pre-eminent position on the small customer market (or markets) by removing Verbund as a competitive force. It would thus strengthen a dominant position on the market in the supply of electricity to small customers in Austria.

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46 Annex 10 to EnergieAllianz's reply to the Commission's request for information dated 28 February 2003. The data for WienEnergie have not been included, because the reply was incomplete in this respect. Switching rates submitted by EnergieAllianz at the hearing show that in the nine months between July 2002 and March 2003 it was Verbund which gained most small customers (network level 7) switching from EnergieAllianz, after MyElectric and Unsere Wasserkraft. Its percentage share of customers switching from EnergieAllianz fell in this period to some [<15%]*, which is unsurprising in the light of the planned merger.

47 Planned cooperation between Ruhrgas AG and Salzburg AG with a view to supplying final consumers on a multi-utility basis has not been realised to date. If such cooperation had come about, Ruhrgas AG would ultimately have been competing with of EVN, the EnergieAllianz member linked with E.On.

3. The merger would not create a dominant position on a supposed Austrian market in supply to regional suppliers

(138) For the following reasons, the merger would not create a dominant position for the parties on a supposed Austrian market in supply to Austrian regional suppliers.

(139) Unlike small distributors and large customers, the Austrian regional suppliers can already buy to a significant extent from foreign companies. Unlike the former, they can more easily increase such purchases because they have their own energy purchase management and can thus purchase energy from suppliers which do not have their own sales set-up in Austria. It can therefore be expected that supply is sufficient for Austrian regional suppliers. As regards the *Land* corporations in the Tyrol and Vorarlberg, Tiwag and VKW, their supply areas form part of the German control block and they have therefore developed supply links with Germany over time which differ significantly from import business in a liberalised cross-border electricity market. In the eastern control area, Steweag-Steg has long-term supply contracts with its parent firm, Verbund. This would leave, after the merger, only the regional suppliers of Salzburg and Carinthia, Salzburg AG and Kelag as customers in the market for the supply of Austrian regional suppliers. It is expected that there would be sufficient potential competition for the supply of these two corporations.

(140) Furthermore, all Austrian regional suppliers which are independent of the parties to the merger have a degree of self-generation capability, especially from hydroelectric resources.[48] Since hydroelectric supply is not a relevant purchase criterion for all customers (this applies to most industrial customers) and since hydroelectric power may at least to a limited extent be purchased outside Austria, the Austrian regional suppliers are not dependent on hydroelectric supply from Verbund.[49]

(141) In summary, the results of the Commission's investigations have not produced sufficient evidence to conclude that the merger would create a dominant position on an Austrian market in supply to regional suppliers.

VII. COMMITMENTS ENTERED INTO BY THE NOTIFYING PARTIES

(142) In order to overcome the competition concerns identified by the Commission, the notifying parties have submitted the commitments described below, the full text of which is set out in the Annex to this Decision.

(143) Verbund undertakes:

(a) to sell its 55% holding in APC to an independent third party, to be approved by the Commission, before the notified merger takes place;

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48 See Table 1 in paragraph 20.

49 It can also be presumed that the legislation discussed in paragraph 103 will make it easier to supply Austrian regional suppliers from abroad.

(b) to transfer existing contracts with final consumers, and any such contracts concluded prior to the transfer, held by APC in the name and for the account of Verbund, before the sale of its holding in APC;

(c) to sell its 20% holdings in MyElectric and Unsere Wasserkraft;

(d) to refrain from exercising the voting rights deriving from its holding in Steweag-Steg until […]*, wherever its vote could influence the competitive behaviour of the undertaking, particularly with regard to pricing and products, distribution and procurement, and to withdraw its members indefinitely from the Steering Committee that develops distribution policy for Verbund/APC and Steweag-Steg;

(e) to remedy all the problems regarding the Austrian domestic grid (380-kV Styria line and if necessary the Salzburg line) and to develop the interconnectors to Italy and Slovenia as soon as the authorities have given the necessary authorisation and approval.

(144) Energie OÖ undertakes to transfer to an independent trustee to be approved by the Commission the rights deriving from its holding in Salzburg AG (apart from its right to dividends) and the rights deriving from the shareholder agreement concluded with the *Land* and City of Salzburg, by […]*.

(145) Verbund and EnergieAllianz undertake:

(a) to ensure that APT offers APC an electricity supply contract with a duration of at least four years in the first place, under the terms of which APC will be able to take 3 TWh of electricity per year in the form of more precisely described structured supplies, at the prices at which Verbund supplies the new E&S; the contract may be terminated after four years if requested and if the Commission concludes that at that time there are enough other sources;

(b) to make available through APT 450 GWh of electricity per year, of which at least 50% will derive from hydroelectric plants, satisfying the characteristics of the standard load profile, for auction in lots of 20–40 GWh, to be supplied to Austria's high-voltage grid until 30 June 2008 under more precisely specified conditions for the supply of final consumers;

(c) to implement measures described in greater detail regarding the provision of balancing energy; these primarily concern efforts to open up the eastern control area towards the Tyrol and Germany, an offer to Kelag to dissolve the storage partnership between Kelag and Verbund at no additional cost, and for a transitional period [pricing provisions for]* balancing energy provided by Verbund/EnergieAllianz as the market maker;

(d) to allow customers who now find themselves with the new E&S a unilateral right to terminate their electricity supply contracts early, at a date six months following the conclusion of the merger, as long as they give three months' notice, and to ensure that in the first two years after it has started operating the new E&S offers its customers one-year electricity supply contracts;

(e) to implement as quickly and comprehensively as possible the provisions regarding unbundling that will be enacted within the framework of Austria's implementation of the revised Electricity Market Directive.

VIII. APPRAISAL OF THE NOTIFIED OPERATION UNDER ARTICLE 2 OF THE MERGER REGULATION IN THE LIGHT OF THE COMMITMENTS ENTERED INTO

(146) The commitments set out in paragraphs 143 to 145 will overcome the competition concerns regarding the Austrian markets for the supply of electricity to small distributors and large and small customers.

A. APC

(147) The commitment to divest Verbund's controlling majority share in APC prevents the accumulation of the Verbund and EnergieAllianz shares of the market for supply to large customers that would have resulted from the merger. APC is responsible for all of Verbund's distribution activities in this field. The undertaking has all the necessary human and material resources, including know-how, a target group list, an e-commerce platform, back office and systems management to enable the purchaser to enter the market for large customers immediately. All of APC's existing customer relations will be transferred to the purchaser; this represents a market share of over [5-15%]* in terms of large customers. The purchaser must be an independent third party that can guarantee that APC will grow and continue to compete actively with the parties and other competitors in the large customer and distributor market.

(148) The commitment to conclude a long-term contract with APC providing for the structured supply of 3 TWh/year on specified conditions will place APC in the same position with respect to that amount as the parties' own big-customer company E&S. The amount of power referred to in the commitment covers the bulk of what APC has been taking from Verbund/APT. This removes the electricity supply risk to APC's buyer, and the need for the buyer to structure the electricity supply itself. The commitment is therefore likely in the short term either to facilitate the entry of a buyer into the Austrian market, or to make it possible for a buyer substantially to expand its Austrian business. The buyer would be enabled to offer effective competition to the parties after the concentration, and effectively to restrict their market power. This commitment will last for four years in the first place. It may be extended if there are not enough alternative sources of supply available to buyers at the end of that time.

B. STEWEAG-STEG

(149) Verbund's commitment to refrain from exercising its controlling rights in Steweag-Steg with regard to decisions concerning competition until […]*[50] neutralises existing structural links between Verbund and Steweag-Steg for a transitional period. This will have the effect that at least during this period Steweag-Steg's market share will not further reinforce the market position of the merged Verbund/EnergieAllianz.

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[50] This period is to be seen against the background of the legislation discussed in paragraph 103.

C. UNSERE WASSERKRAFT AND MYELECTRIC

(150) Verbund's commitment to divest its minority holding in Unsere Wasserkraft and MyElectric will mean that these undertakings will be unaffected by any influence and financial interest on behalf of the merged entity and will be able to compete with it on the market to supply power to small customers. Unsere Wasserkraft and MyElectric have majority holdings in Estag and Salzburg AG respectively, which will be two of the most important remaining Austrian competitors for the merged undertaking Verbund/EnergieAllianz. These have been the two companies most successful at attracting small customers since liberalisation and through them Verbund has ventured beyond Steweag-Steg's traditional supply market to operate on the small customer market. The Commission takes note of this commitment, without making it a condition or an obligation. The consortium agreement between Verbund and EnergieAllianz requires Verbund to divest these holdings in their entirety.

D. SALZBURG AG

(151) Obliging Energie OÖ to transfer the rights deriving from its minority holding in Salzburg AG to a trustee by the end of December 2007[51] will ensure that at least for the foreseeable future there will be no danger that Energie OÖ's current rights to exert influence and obtain information might reduce the capacity of Salzburg AG to compete actively with the new merged undertaking. During a transitional period this commitment will help to ensure that the parties do not influence the competitive behaviour of Salzburg AG in its dealings with large customers.

E. LIQUIDITY

(152) The commitment to make available to third parties through auctions an annual supply of 450 GWh, of which at least 50% derives from hydroelectric plants, thereby satisfying the characteristics of the standard load profile, in quantities suitable for the supply of small customers ensures that new competitors entering the market for the supply of small customers now and in the future will have access to additional capacity for power generated in Austria. Moreover, they will be able to supply any customers requesting hydroelectric power. This commitment will increase the liquidity available to facilitate new entries and the expansion of existing market shares by undertakings competing with the parties to the merger. Unsere Wasserkraft and MyElectric, who are already competing with the parties in the small customers market, will likewise be enabled to expand their market shares and to safeguard their supplies of power.[52]

F. BALANCING ENERGY

(153) The commitments to make balancing energy available will ease access to balancing energy for third party suppliers on electricity markets, particularly for new entrants. Kelag's position as an alternative supplier of balancing energy in the eastern control area is strengthened by the possibility of being able to end the current storage cooperation arrangements with Verbund economically. At the same time, the price cap

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[51] This period is to be seen against the background of the legislation discussed in paragraph 103.

[52] This period is to be seen against the background of the legislation discussed in paragraph 103.

imposed on the balancing energy supplied by Verbund/EnergieAllianz during the period of transition until there is full competition on Austrian power-supply markets will limit the cost risk to potential customers for balancing energy. Furthermore, the opening-up of the eastern control area towards the Tyrol and Germany, which the notifying parties have undertaken to help bring about, will ensure more competition regarding the supply of balancing energy in the medium and long term.

(154) The commitments relating to balancing energy were agreed between the notifying parties and the Austrian regulator E-Control. The plan is for E-Control to monitor fulfilment of the commitments as the Commission's trustee. E-Control has told the Commission that these commitments will suffice to solve the competition problems detected relating to balancing energy.

(155) Improved access to balancing energy in the eastern control area, particularly for new entrants onto the market, will overcome or reduce what the Commission investigations revealed to be a key obstacle to entry onto the market. This will enable potential competitors in and outside Austria to enter Austria's electricity markets and compete with Verbund/EnergieAllianz.

G. FURTHER COMMITMENTS

(156) The other commitments entered into by the notifying parties regarding the improvements to the Austrian domestic grid, the interconnectors to Italy and Slovenia, special rights to terminate contracts granted to Verbund's large customers who now find themselves with the new E&S and quicker implementation of the unbundling provisions contained in the amended Electricity Market Directive do not in themselves alter the structure of the competitive conditions brought about by the merger. Moreover, the implementation of some of them does not depend solely on the wishes of the parties, as it may require the involvement of third parties (approval by the authorities, the agreement of foreign transmission system operators and implementation by the appropriate Austria authorities of the Electricity Market Directive) or simply relate to the fulfilment of (future) legal obligations. However, they contribute to the gradual removal of current obstacles preventing entry onto the market and integrating Austrian electricity markets in relevant geographical markets stretching beyond national borders in the medium to long term. In this way, these commitments entered into regarding behaviour may help to ensure that the other obligations set out above, particularly those of a structural nature, succeed in fully restoring effective competition. Although they will not be made conditions attached to the exemption decision, they will help to ensure that the remedy package contributes to the real removal of the competition concerns noted.

H. SUMMARY APPRAISAL OF THE COMMITMENTS

(157) The divestiture of Verbund's holdings in APC goes most of the way towards removing the market-share overlaps between Verbund and EnergieAllianz on the market for the supply of large final consumers. Selling APC to an independent third party creates the opportunity for a newcomer, e.g. a major power-supply company currently operating outside Austria, to enter and compete actively on the Austrian market for large customers. The parties have undertaken not to implement the merger before a Commission-approved disposal of APC has taken place, so that full implementation of this commitment is guaranteed. During the period from the opening up of the market

and until full liberalisation[53] the positions of Steweag-Steg and Salzburg AG as competitors will be strengthened by the temporary freezing of their involvement with Verbund and Energie OÖ respectively. The vertical impact of the combination of Verbund's dominant power generating capacity and EnergieAllianz's position as the leading electricity supplier in Austria will be offset at least in part by the fact that sufficient liquidity will be made available on competitive terms to APC and the suppliers competing on the market for small customers. The measures to improve access to balancing energy and the opening of Austrian markets to outside competition in the medium term will also help to overcome obstacles to access to the markets and to increase competition in the markets concerned. Were any competition concerns to arise relating to a conceivable market to the supply of regional distributors, they would be overcome by the remedies.

(158) The overall package of remedies submitted by the notifying parties and other commitments will therefore ensure that the notified merger does not create a dominant position on the markets for the supply of electricity to small distributors and large final consumers, nor will it strengthen the dominant position of EnergieAllianz on the market for the supply of electricity to small customers in Austria.[54]

IX. CONDITIONS AND OBLIGATIONS

(159) The first sentence of the second paragraph of Article 8(2) of the Merger Regulation states that the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

(160) Measures that effect a structural change to the market are to be imposed in the form of "conditions"; implementing steps necessary to achieve this result are to take the form of "obligations". If a condition is not fulfilled, the Commission decision declaring the concentration compatible with the common market is null and void. Where the undertakings concerned commit a breach of an obligation, Article 8(5)(b) of the Merger Regulation empowers the Commission to revoke a clearance decision; Article 14(2)(a) and Article 15(2)(a) of the Merger Regulation empower it to impose fines or periodic penalties on the parties.[55]

(161) In line with this fundamental distinction, the Commission should make it a condition of its decision that the parties comply in full with the commitments by which they undertake

(a) to sell their shares in APC to a third party approved by the Commission, to ensure that APT offers APC an electricity supply contract entitling APC to take 3 TWh a

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53 See paragraph 103.

54 Remedies Notice, paragraph 30.

55 Remedies Notice, paragraph 12.

year, and to refrain from implementing the notified transaction until the sale of the shares in APC is effective (Annex,[56] point A.1);

(b) to make available through APT 450 GWh of electricity for auction each year until 30 June 2008, to be supplied to the Austrian high-voltage grid (Annex, point C);

(c) not to implement the concentration before the necessary authorisations have been obtained (Annex, end).

(162) These commitments are intended to effect a structural change to the market. Of the other commitments, the details of the continued operation of APC, the terms of APC's electricity supply contract, the non-exercise of voting rights in Steweag-Steg, the transfer to a trustee of the shareholder's rights in Salzburg AG, the terms of the auction of electricity, the measures to ensure competition on the market in balancing energy and the grant of a unilateral right to early termination of the electricity supply contracts of large customers who now find themselves with the new E&S should be made the subject of obligations. Essentially they serve to ensure that the conditions already mentioned have the desired effect on competition, or that they are put into effect as planned.

X. CONCLUSION

(163) For these reasons, provided the commitments entered into by the notifying parties are fully complied with, it can be accepted that the concentration does not create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it. Subject to full compliance with the commitments set out in the Annex, therefore, the concentration should be declared compatible with the common market and the EEA Agreement pursuant to Articles 2(2) and 8(2) of the Merger Regulation and Article 57 of the EEA Agreement,

[56] See footnote 8.

HAS ADOPTED THIS DECISION:

Article 1

The notified concentration by which Österreichische Elektrizitätswirtschafts-Aktiengesellschaft, EVN AG, Wien Energie GmbH, Energie AG Oberösterreich, Burgenländische Elektrizitätswirtschafts-Aktiengesellschaft and Linz AG für Energie, Telekommunikation, Verkehr und Kommunale Dienste acquire joint control, within the meaning of Article 3(1)(b) of the Merger Regulation, of the undertakings E&S GmbH and Verbund Austrian Power Trading AG is hereby declared compatible with the common market and the EEA Agreement.

Article 2

Article 1 shall apply subject to the condition that the commitments entered into by the undertakings referred to in Article 1 and set out in point A1, clauses 1, 4 and 6, point C, clause1, and the last sentence on page 6 of the Annex are complied with in full.

Article 3

This Decision is subject to the obligation that the other commitments entered into by the undertakings referred to in Article 1 and set out in the Annex, with the exception of points A2, A3, B and F, must be complied with in full.

Article 4

This Decision is addressed to:

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A-7000 Eisenstadt

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Böhmerwaldstraße 3
A-4021 Linz

EVN AG
EVN Platz
A-2344 Maria Enzersdorf

Linz AG für Energie, Telekommunikation, Verkehr und Kommunale Dienste
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A-4021 Linz

Österreichische Elektrizitätswirtschafts-AG
Am Hof 6a
A-1010 Vienna

Wien Energie GmbH
Schottenring 30
A-1010 Vienna

Done at Brussels, 11 June 2003

For the Commission

Mario Monti
Member of the Commission