

***Case No COMP/M.4238 -
E.ON / PRAZSKÁ
PLYNÁRENSKÁ***

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**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 11/07/2006

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.07.2006

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PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying party

Dear Sir/Madam,

**Subject: COMP/M.4238 – E.ON / Pražská plynárenská
Notification of 06.06.2006 pursuant to Article 4 of Council Regulation
No 139/2004¹**

1. On 06.06.2006, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 (“the Merger Regulation”) by which the undertaking E.ON Czech Holding AG belonging to the group E.ON AG (“E.ON”, Germany) acquires within the meaning of Article 3(1)(b) of the Merger Regulation joint control of the undertaking Pražská plynárenská a.s. (“Pražská plynárenská”, the Czech Republic) by way of purchase of shares in the holding company Pražská plynárenská Holding a.s. (“PPH”). After the transaction, Pražská plynárenská will be jointly controlled by E.ON and the City of Prague.
2. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of the Merger Regulation and does not raise serious doubts as to its compatibility with the common market and the EEA Agreement.

I. THE PARTIES

3. E.ON is a privately owned energy company based in Germany with a focus on the supply of electricity and gas which is active in various countries in Europe and the United States. In the Czech Republic, E.ON among others jointly controls (together with

¹ OJ L 24, 29.1.2004 p. 1.

Oberösterreichische Ferngasgesellschaft) the gas distribution and supply company Jihočeská plynárenská a.s. (“Jihočeská plynárenská”). It also holds minority interests in several other gas distribution and supply companies in the Czech Republic, which however do not confer on E.ON any control or joint control within the meaning of the Merger Regulation.

4. Pražská plynárenská is active in gas distribution in the region of the City of Prague and gas supply to industrial, commercial and household customers in the Czech Republic. Its wholly owned subsidiary Prometheus, energetické služby, s.r.o. (“Prometheus, energetické služby”), is active in the production and supply of district heat to customers in Prague. PPH is a pure holding company with no other business activities than holding the interest in Pražská plynárenská.
5. The City of Prague is a municipality which controls a number of companies supplying utility services to the citizens of the city. These companies include Pražská teplárenská and Pražská energetika, active in the provision of district heat and in the distribution, supply and production of electricity.

II. THE OPERATION AND THE CONCENTRATION

6. Prior to the transaction, Pražská plynárenská is controlled by a pure holding company Pražská plynárenská Holding a.s. (“PPH”) which holds 50.2% of the shares in Pražská plynárenská. Another 49.3% of the shares of Pražská plynárenská are held by RWE Gas International B.V., a wholly owned subsidiary of RWE Energy AG (“RWE”), however without giving it any possibility to directly (jointly) control the company². Additionally, 0.5% of Pražská plynárenská’s share capital is held by other shareholders, including E.ON (0.05%). PPH is in turn jointly controlled by the City of Prague, holding 51% of its shares, and RWE, holding 25%. The remaining 24% of the shares of PPH were held by E.ON without giving it any jointly controlling power³.
7. E.ON and RWE agreed on the acquisition of shares held (directly or indirectly) by RWE in PPH and Pražská plynárenská by an agreement concluded on 1 February 2006. After the transaction, E.ON will thus hold a jointly controlling 49% shareholding in PPH (as well as the non-controlling shareholding of 49.35% in Pražská plynárenská). The transaction is part of a share swap between RWE and E.ON which involves interests held by these two groups in gas companies in the Czech Republic⁴.

² The Board of Directors of Pražská plynárenská is elected by simple majority by its Supervisory Board which consists of nine members. While three of these members are elected by the employees of Pražská plynárenská, the remaining six members are elected by the Shareholders Assembly by simple majority. PPH is thus able to fill all the remaining six seats in the Supervisory Board and thus have simple majority necessary for election of the Board of Directors. The management of Pražská plynárenská is then fully in the hands of the Board of Directors, which has an obligation to ask the Supervisory Board for comments on various key issues including the long-term strategy and annual financial plan. However, the opinion of the Supervisory Board on these matters is not legally binding for the Board of Directors. Therefore, through its power to determine the management of Pražská plynárenská, PPH has sole control over Pražská plynárenská.

³ E.ON and RWE agreed to exercise their voting rights in common. However, if RWE and E.ON cannot agree on a decision to be taken, E.ON has to align its voting with the decision taken by RWE, unless essential interests of E.ON are opposed to this.

⁴ Within the framework of this share swap, E.ON transfers or acquires an option to transfer to RWE its non-controlling minority interests in four other regional gas distribution and supply companies in the Czech Republic (Středočeská plynárenská, Severomoravská plynárenská, Východočeská plynárenská and

8. According to the Articles of Association of PPH, management of PPH lies with a Board of Directors composed of four members elected unanimously by the shareholders. The shareholders do not have any direct influence over strategic decisions regarding PPH beyond election of the Board of Directors, as all decisions (including for example decisions concerning budget or business plan) are taken by the Board of Directors with simple majority (i.e. at least three members). On the basis of an earlier agreement among E.ON, RWE and the City of Prague and after acquiring the shares of RWE, E.ON will be in a position to submit candidates for two members of the Board of Directors of PPH while candidates for the two other members are submitted by the City of Prague. Decisions of the Board of Directors (including budget and business plan of PPH) can be taken only if at least three members of the Board of Directors give their approval. Against this background, as a result of the transaction, E.ON acquires joint control together with the City of Prague of PPH, and indirectly of Pražská plynárenská.
9. The proposed transaction therefore constitutes a concentration pursuant to Article 3 of the Merger Regulation.

III. COMMUNITY DIMENSION

10. The undertakings concerned have a combined aggregate worldwide turnover⁵ of more than EUR 5 billion⁶. At least E.ON and Pražská plynárenská⁷ have a Community-wide turnover in excess of EUR 250 million⁸, but the undertakings concerned do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension.

IV. COMPETITIVE ASSESSMENT

11. The main overlaps between the parties are limited to the distribution and supply of gas in the Czech Republic, where both E.ON and Pražská plynárenská are active. Apart from that, E.ON and the City of Prague are active in the production and supply of electricity and E.ON, Pražská plynárenská and the City of Prague are active in the supply of district heat. However, overlaps in the electricity and district heat markets are marginal.

a) Relevant markets

Gas markets

Západočeská plynárenská) already now controlled by RWE (acquisition of sole control by RWE in these regional distribution companies was approved conditionally by the Czech NCA in 2002). As part of the share swap, E.ON also acquires the 46.7% shareholding of RWE in Jihočeská plynárenská, however this transaction does not change the situation as this company is already now jointly controlled by E.ON and Oberösterreichische Ferngasgesellschaft on the basis of their vote pooling agreement.

⁵ Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C66, 2.3.1998, p25).

⁶ E.ON [...] EUR; Pražská plynárenská [...]EUR.

⁷ Even though the notifying party was unable to provide an exact turnover of the City of Prague calculated in line with the Commission Notice on the calculation of turnover, the transaction has a Community dimension whatever is the exact turnover of the City of Prague.

⁸ E.ON [...] EUR; Pražská plynárenská [...] EUR.

12. Gas markets in the Czech Republic are being gradually liberalised in line with the national sectoral laws transposing the relevant EC legislation. The gas transmission system operator (RWE Transgas) and the regional distribution system operators are obliged to provide access to third parties on a non-discriminatory basis. As of 1 January 2005, 35 most important final customers representing around 25% of total gas consumption became eligible to freely choose their gas supplier. As of 1 January 2006, all final customers with the exception of households became eligible customers. Households will become eligible customers as of 1 January 2007. As of 1 January 2006, the maximum prices of gas for eligible customers are set by the Czech energy regulator Český energetický úřad (ERÚ). At present, ERÚ is preparing a new decree setting out the rules for the functioning of the gas market which aims at further reducing the existing technical and administrative barriers to entry to the market and thus facilitating the introduction of competition into the newly opened gas markets.
13. The notifying party refers to the decision-making practice of the Commission which has in the past distinguished several separate markets for natural gas: (i) transmission of gas through high pressure network; (ii) storage of gas; (iii), distribution of gas through low- and medium-pressure networks and (iv) supply of gas to customers. In particular, according to previous Commission decisions, gas supply can be further divided into (a) the supply of natural gas to traders; (b) supply of gas to regional suppliers; (c) supply of gas to large power plants with a capacity of more than 50 MW; (d) supply of gas to large industrial customers (with an average consumption of more than 500 m³/per hour); (e) supply of gas to other industrial and commercial customers and (f) supply of gas to household customers⁹. The parties however put forward, that the supply of gas to traders and regional distribution companies could in case of the Czech Republic be considered as a single market because there is no obligation on the part of the regional distribution companies to purchase gas from the wholesale gas supplier¹⁰.
14. The large majority of third party respondents have confirmed that such segmentation of the markets may be appropriate. The parties as well as some respondents also referred to the gas consumers' segmentation applied by ERÚ. It distinguishes large customers (annual consumption more than 4,200 MWh), middle-sized customers (annual consumption between 630 and 4,200 MWh), small customers (annual consumption below 630 MWh, excluding households) and household customers. Some of these categories are then further divided into several subgroups according to the annual consumption. It was suggested in the market investigation that the threshold of 52,500 MWh per year used by ERÚ to further subdivide the category of large customers roughly corresponds to the threshold of 500 m³ per hour¹¹ defined by the Commission and may be appropriate for distinguishing the large industrial customers.
15. As regards the geographic scope of the markets, the Commission has in the past defined the above-mentioned markets as at most national¹². For the Czech Republic, the notifying party claims that the markets for gas storage, transmission and supply to

⁹ E.g. case M.3696 - E.ON/MOL.

¹⁰ This was the case in Hungary and led to definition of separate markets for traders on the one hand and regional distribution companies on the other hand in the case M.3696 - E.ON/MOL.

¹¹ The volume of gas amounting to 52,500 MWh per year corresponds to around 570 m³ per hour.

¹² E.g. case M.3696 - E.ON/MOL.

eligible customers¹³ are at least national whereas the distribution market and the supply to non-eligible customers (households) is regional in scope, coinciding with the area covered by the licence issued by ERÚ. The large majority of third party respondents have confirmed this delineation of the geographic markets.

16. However, for the purpose of this case the exact scope of the relevant product and geographic market can be left open, as the transaction does not lead to competition concerns under any alternative definition of the gas markets.

Electricity markets

17. As regards the general competitive structure in the electricity industry, the Czech Republic is pursuing a policy of liberalisation. Pursuant to the Energy Act, and in accordance with the relevant EC directives in this area, the infrastructure of the transmission and distribution of electricity must be held separate from the electricity supply to customers. The electricity transmission system operator (CEPS a.s.) and the regional distribution system operators are obliged to provide connection to third parties on a non-discriminatory basis. In line with the statutory regime the Czech electricity markets have been gradually opening up since 2002 and since 1 January 2006 all end consumers have become eligible and are free to choose their supplier.
18. According to its past practice¹⁴, the Commission distinguishes in particular the following product markets in the electricity sector (i) generation and wholesale supply, (ii) transmission, (iii) distribution, (iv) ancillary services and (v) retail supply of eligible customers¹⁵. The retail supply of electricity was in the past further subdivided into supply of electricity to large industrial customers connected directly to the high-voltage network and supply of electricity to smaller industrial, commercial and domestic customers connected to the low-voltage network. The parties submit that this market definition is appropriate for the Czech Republic as well, which was generally confirmed by the market investigation, although some respondents have indicated that they were not active in the electricity industry and therefore had no opinion.
19. As regards the geographic scope of the markets, the parties regard all the above electricity markets as at least national, with the exception of distribution of electricity, which is considered regional, coinciding with the area covered by the licence issued by the national energy regulator. The parties argue that the market for generation and wholesale supply of electricity may be even wider than national, referring also to the past practice of the Commission¹⁶. The market investigation confirmed that the market is regional in case of distribution of electricity and at least national in case of other markets.
20. However, for the purpose of this case the exact scope of the relevant product and geographic market can be left open as the transaction does not lead to competition concerns under any alternative definition of the electricity markets.

¹³ The gas market is being gradually opened to competition and as of 1 January 2006 all end customers with the exception of households were made eligible customers free to choose their gas supplier. Households should according to the valid legislation become eligible customers as of 1 January 2007.

¹⁴ E.g. cases M.3696 - E.ON/MOL or M. 4110 – E.ON/ENDESA

¹⁵ As of 1 January 2006, all end users of electricity including households became eligible customers in the Czech Republic.

¹⁶ In its decision in the case M.3665 - ENEL/SLOVENSKE ELEKTARNE the Commission left the question open whether – *inter alia* – the Czech market was part of a larger Central European market.

District heat markets

21. With reference to the past practice of the Commission the parties argue that the provision of district heat can be regarded as a separate product market¹⁷. As regards the geographic scope of the market, the parties argue that district heat is distributed over separate networks owned by the local distributor and that different networks cover different geographic areas and cannot be connected to each other. Therefore, according to the parties, the geographic market is local, and limited to the city or part of the city covered by the relevant district heating network. This delineation of the market was largely confirmed by the market investigation.
22. However, for the purpose of this case the exact product and geographic market definition can be left open as the transaction does not lead to competition concerns in the district heating sector under any alternative market definition.

b) Competitive effects

Gas markets

23. After the transaction, E.ON will jointly control two out of in total eight regional gas distribution companies in the Czech Republic - Jihočeská plynárenská and Pražská plynárenská. Their share in the total supplies of gas in the Czech Republic amounted in 2005 to [0-10]% and [5-15]% respectively. Their combined share in the overall gas supply therefore amounted to [10-20]%.
24. As regards the general competitive structure of the gas industry in the Czech Republic, it should first be noted that the position of the parties will, even after the transaction, still be incomparable to the clearly unique position of their vertically integrated competitor RWE. All the remaining six regional distribution companies (accounting together for more than 80% of the total gas supplies in 2005) are controlled by RWE. RWE also controls the transmission system operator RWE Transgas which is at the same time the only importer of gas into the Czech Republic and the main supplier of gas for regional distribution companies¹⁸. According to internal documents of the parties, RWE also holds a [60-70]% share in the storage of gas in the Czech Republic.
25. The parties to the transaction are not active in the markets for transmission and storage of gas. Further, as regards the distribution of gas, the parties to the transaction are active in two different geographic markets (Pražská plynárenská in the Prague region and E.ON - Jihočeská plynárenská in the Southern Bohemia region) which are not even geographically neighbouring. Therefore, the transaction does not lead to any overlap in the distribution of natural gas. Similarly, the activities of the parties do not overlap in the supply of gas to households, at least before 1 January 2007 when households become eligible customers. Further, Pražská plynárenská is not active in the markets for the supply of gas to traders, regional distribution companies and large power plants and the transaction thus will not lead to any horizontal overlaps in these markets either.
26. The activities of the parties overlap however in the supply of gas to other eligible customers where all regional distribution companies as well as the gas importer and

¹⁷ See e.g. case M.3268 – Sydkraft/Granninge

¹⁸ According to the parties, Pražská plynárenská purchased 100% of gas from RWE Transgas while Jihočeská plynárenská purchased 98.5% of gas from RWE Transgas.

transmission system operator RWE Transgas and some so far rather small new entrants compete. The following table shows the market shares of the parties in 2005 in the individual national markets for supply of gas to these categories of eligible customers as defined by ERÚ (including households on a national level which may be relevant after households become eligible customers as of 1 January 2007).

Market	Pražská plynárenská	E.ON	Combined market share
Supply of large customers (annual consumption more than 4200 MWh)	[0-10]%	[0-5]%	[5-15]%
Supply of middle-sized commercial customers (annual consumption between 630 and 4200 MWh)	[20-30]%	[0-10]%]30-40]%
Supply of households	[5-15]%	[0-10]%	[10-20]%

27. The market investigation has generally confirmed the competitive structure of the gas supply markets as presented by the notifying party. The data provided by ERÚ confirmed that the combined market share of the parties in the gas supply markets does not exceed 40% in any of the categories and subcategories of customers defined by ERÚ, while in most of them it amounts to significantly less than 30%.
28. Further, the market share of RWE as the main competitor of the parties in the Czech Republic amounts according to the estimates of the parties even after the transaction to [80-90]% in the supply to large industrial customers, [60-70]% in the supply of gas to middle-sized commercial customers and to [80-90]% in the supply of gas to household customers. These market shares estimates were also largely confirmed by the market investigation and by the data provided by ERÚ.
29. Therefore the market investigation confirmed that the transaction is unlikely to have negative effects on the competitive situation in the gas supply markets. To the contrary, a number of the replies in the market investigation suggested that the transaction may have a pro-competitive effect by weakening the position of the gas supply leader RWE and strengthening the capacity of E.ON to compete more effectively in the liberalised gas supply markets.
30. Irrespective of market transparency, the market investigation did not give any indications of possible coordinated effects as a result of the transaction. Even though there will be (as it is the case even before the transaction) a virtual duopoly in several gas supply markets, the position of E.ON and RWE is not symmetric both as regards their market shares and level of vertical integration in other gas markets. Further, even though there are some structural links due to minority shareholdings of E.ON in some regional distribution companies controlled by RWE, the transaction in fact reduces significantly the extent of these links by eliminating these cross-shareholdings in at least three regional gas distribution companies.
31. Therefore, the transaction does not raise serious doubts as to its compatibility with the common market in any of the possible gas markets in the Czech Republic.

Electricity markets

32. Both the City of Prague (through Pražská energetika and Pražská teplárenská) and E.ON are active in the generation and wholesale supply of electricity and in the retail supply of electricity in the Czech Republic.
33. As regards *generation and wholesale supply of electricity*, the combined market share of the City of Prague and E.ON in the Czech Republic is marginal - below 3%. To the extent that electricity generation may be vertically related to the market for the supply of gas to power plants or large industrial users, the market position of the parties in all these markets is below 25% and therefore does not give rise to any vertically affected markets. Taking into account the marginal position of the parties in the electricity generation and wholesale market, the transaction does not lead to any competition concerns due to potential coordination of competitive behaviour of the City of Prague and E.ON within the meaning of Article 2(4) of the Merger Regulation either.
34. As regards the *retail supply of electricity to end consumers* (both large industrial customers and smaller industrial, commercial and domestic customers), the position of the City of Prague and E.ON is significantly stronger with a combined market share amounting to [25-35]% (Pražská energetika [5-15]% and E.ON [15-25]%). However, the vertical link to the gas supply markets is only indirect via electricity generation, where the position of the parties is marginal (their combined market share is less than 3%, whereas incumbent CEZ's share in electricity production and wholesale supply is in excess of 70%). It is also doubtful, whether supply of electricity to end users could be regarded as neighbouring market, closely related to the gas markets where the joint venture is active, taking into account the fact that in the Czech Republic only to a very limited extent gas is used for the production of electricity. In any event, it is unlikely that the transaction would lead to coordination of competitive behaviour of the parent companies in the electricity supply markets for the following reasons: (i) their co-operation is limited to the activities of Pražská plynárenská in the gas sector and (ii) even with the more than 30% combined market share in the supply of electricity on a national basis, the parties' position would still not be comparable to the competing vertically integrated electricity company ČEZ with a market share of more than 60%. These conclusions would not change under any alternative product or geographic market definition¹⁹.
35. The market investigation has confirmed that the transaction does not affect to any appreciable extent the competitive situation in the electricity markets in the Czech Republic.

¹⁹ Based on the notifying party's best estimate, in the *national* market for the retail supply of electricity to *medium and large industrial and commercial customers* and the supply to *small commercial and industrial customers*, the market share of the E.ON group in the Czech Republic is between [20-30]%. As regards the supply to *households*, its share is between [20-30]%. In each of these two submarkets the City of Prague represents [5-15]%. Data provided by the notifying party supports that market leader CEZ represents almost twice the parties' combined position. On a possible *regional* geographic market, in each of the specific regions the relevant regional supplier (CEZ, E.ON or Pražská energetika) will have a market share in the range of 90-100%, depending on the aforementioned customer groups. E.ON is active in the two Southern regions of the Czech Republic, whereas Pražská energetika is active in and around Prague. However, regardless of their strong, if not dominant position regionally, the parties' combined position in the upstream market for electricity generation and wholesale supply is minimal compared to CEZ. In this light it is considered unlikely that the proposed transaction would lead to competition concerns, in particular as regards coordination of competitive behaviour of the parent companies in the electricity supply markets.

36. Taking into account the above, the transaction does not raise serious doubts as to its compatibility with the common market in any of the electricity markets in the Czech Republic.

District heat markets

37. The City of Prague (through Pražská teplotárenská) and Pražská plynárenská (through Prometheus, energetické služby) are both active in the *provision of district heat* in Prague. However, already before the notified transaction the City of Prague jointly controlled Pražská plynárenská and therefore the proposed operation does not lead to any change with respect to the provision of district heat in the city of Prague. E.ON, on the other hand, owns a number of production units for electricity and heat in Southern Bohemia and Southern Moravia and supplies district heat to customers in the immediate vicinity of these production units.
38. The district heat markets may be considered as downstream markets to the gas supply markets. However, as set forth in paragraph 25 above, the position of the parties in the upstream gas supply markets is rather limited (incomparable to the position of RWE which would always be able to serve as an alternative supplier of gas to the district heat production units) and the parties are active in different, unconnected geographic markets for the supply of district heat downstream.
39. The market investigation confirmed that the transaction does not affect to any appreciable extent the competitive situation in the district heat markets in the Czech Republic.
40. Therefore, the transaction does not raise serious doubts as to its compatibility with the common market in any of the district heat markets in the Czech Republic, nor does it lead to any competition concerns due to potential coordination between the City of Prague and E.ON in the district heat markets within the meaning of Article 2(4) of the Merger Regulation.

V. CONCLUSION

41. For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of Council Regulation (EC) No 139/2004.

For the Commission
signed
Neelie KROES
Member of the Commission