

Mr Märt Ots
Competition Authority
Auna 6
10317 Tallinn

Your ref: 28.02.2011 No 9.1-2/10-0448-030
and 18.03.2011 No 9.1-2/10-0448-037

Our ref: 29.03.2011 No

Dear Mr. Ots,

In response to the positions sent to ASTV in your 28.02.2011 letter and your additional explanations submitted on 02.03.2011 we would like to draw your attention to the important legal aspects of our tariff application. From the CA 28.02.2011 letter and for the reasons outlined in the conclusions of that letter, it appears reasonable to conclude that the CA is about to issue a decision not approving the price of water services for Tallinn and Saue City for 2011 that ASTV has applied for because the CA does not believe this price to be justified. In addition, your rejection of our request for a postponement of the deadline for replying to the CA position seems to confirm that the CA has decided to reach a decision on the case in the shortest term and, more importantly, without taking into consideration our privatisation contract and the recent EU Commission intervention on the matter.

It is clear from pages 26-27 and section 5.1. on page 9 of your response to our tariff application for 2011 that the CA has decided to ignore ASTV's privatisation and the legally binding Services Agreement, which was part and parcel of that privatisation. Such actions unilaterally break the privatisation agreement and Services Agreement. This is further clarified on page 9, where you state that "***Agreements concluded between the City of Tallinn and ASTV do not possess a stronger legal power than the PWSSA, which the CA follows in its tariff approval process. The CA believes that the water tariff submitted for approval by ASTV is justified only if the basis for its formation complies with the principles prescribed in the PWSSA. Therefore the CA is obligated to follow only the PWSSA when analyzing ASTV's tariff application, therefore only a cost-based water service tariff is justified.***". It seems that you use the amended PWSSA as the ultimate authority in justifying why you have decided to completely and explicitly discard ASTV's privatisation agreement and the Services Agreement.

By following such approach, we believe that the CA is ignoring the value of the equity price paid by the investor at the time of the Company's privatisation, so depriving them of their legitimate return on their investments. This is a unilateral modification of the legal and economic conditions set by the same Estonian authorities in view of ASTV's privatization.

Such approach actually overturns the legal and economic "platform" on the basis of which foreign companies decided to invest in the privatised business. As a result, the current position of the CA is infringing well-established EU principles, according to which when privatising companies, Member States shall abide by "*objective and stable criteria which are known in advance*" and, in order to avoid circumvention of that principle, Member States should also refrain from arbitrarily modifying, *ex post facto*, the legal rules and criteria established for the purpose of a privatisation process.

We would also add that the CA position on ASTV's monopolistic position and the consequent need to avoid excessive profit in prejudice of consumers is particularly unjustified in the case at stake, since the existing contracts set at the time of the privatisation, in line with the national sector regulation, took due account of such public interest needs. Indeed, the set of contracts and criteria defined for ASTV privatisation were **conceived and shaped in view of controlling tariff increase**, ensuring quality enhancements, guaranteeing both stable long-term relationships between the parties and maximum benefits from privatisation, while ensuring an adequate return for the investors. The bidding criteria elaborated at that time (in particular, the main criteria concerning the K coefficient) reflected the public need of protecting consumers from monopolistic attempt of excessive profits by keeping tariffs at the lowest maximum level.

Under such circumstances, the CA position is violating the freedom of movement of capital and freedom of establishment, which are fundamental freedoms, enshrined in art 49 and 63 of the Treaty on the Functioning of the European Union (TFEU).

A final remark is addressed to your letter rejecting ASTV request for postponement. In particular, we have to restate that the pending procedures before the CA is closely linked with the object of the Commission's request for information and that this is why we asked the CA to take time in order not to interfere with, and to pre-empt, the Commission assessment on the State measures tackled by ASTV Complaint. It is evident that should the CA adopt final decisions on ASTV tariffs before the Estonian authorities reply to the EU Commission, this will end up jeopardising the *effet utile* of the Commission initiative, which is in stark contrast to the principle of loyal cooperation between Member States and the Commission.

We would like to remind the CA, once again, that ASTV made its application for a 3.5% tariff increase from 1st January 2011 in accordance with the Services Agreement, which embodies the terms and conditions for the provision of EU-level service as well as returns to be made at the lowest possible tariff increase which were agreed at the time of ASTV's privatisation in 2001.

Our application was made based on the tariff mechanism agreed on privatisation. These contracts are fully in line with the then applicable PWSSA and EU law. In order to demonstrate the correctness of this contract and the decisions made at the time of privatisation, as well as the Company's performance against what had been agreed, a detailed and independently verified analysis accompanied our application. This independently verified analysis was submitted to assist the Competition Authority with its analysis of the tariff application, and to illustrate that the returns made since privatisation (i.e. from the period 2001 to 2010) were fully in accordance with those made by other privatised utilities when using internationally acceptable principles (see World Bank Resetting Price Controls for Privatized Utilities to which you yourself refer to in your 28.02 letter footnote 4). This independently verified analysis clearly demonstrates that the returns made by the company and UUTBV since privatisation have not been excessive.

Furthermore, in view of ensuring that the CA can make a fully informed decision by having access to all the key financial and operational terms and conditions of the privatisation and regarding the Company's performance since privatisation, within the file sent to the CA on 09.11.2010 (electronic copies submitted on a CD on 10.11.2010) ASTV included all parts the Services Agreement **as well as key privatisation documents**.

Notwithstanding our comprehensive submission, we have to remark that you have chosen to completely ignore the opinion of internationally renowned and accepted experts as well as our

building blocks analysis, as you have not referred to either of them in a single instance in your 28.02.2011 letter. Analogously, your analysis contained in your 28.02.2011 letter does not refer to any parts of either the Services Agreement or any key privatisation documents.

ASTV considers that such approach is inadmissible and represents a further confirmation that the CA is acting in contrast with consolidated principles of EU Law.

Whilst I reiterate that ASTV's tariff application was made on the basis of the Services Agreement, then in the interests of transparency and to maintain a professional dialogue please find detailed responses to the points raised in your 28.02.2011 letter included in appendix 1 hereto. We do hope you will find these informative and helpful and we very much look forward to an open discussion on any points that require clarification and further discussion, in particular regarding **the unilateral breaking of the Services Agreement and ASTV's privatisation agreement, which will occur, should the CA continue to pursue this course of action.** Should this happen, the Company is prepared to take any legal action necessary international and local to protect its rights and the rights of its shareholders.

Sincerely,

Ian John Alexander Plenderleith
Chairman of the Management Board