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STATE AUDIT OFFICE

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- Press release-

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Impact of energy crisis on JSC MEPSO operation

Auditors expressed adverse opinion on the reality and objectivity of the financial statements for 2021 and qualified opinion on the compliance with legal regulations

The State Audit Office conducted audit on the financial statements for 2021 together with compliance audit of the *Electricity Transmission System Operator of the Republic of North Macedonia, Joint Stock Company for electricity transmission and power system control, in state ownership*, Skopje (JSC MEPSO).

The auditors expressed **adverse opinion** on the reality and objectivity of financial statements for 2021 and **qualified opinion** on compliance with legal regulations, guidelines and policies in place.

In addition, the auditors ascertained that recommendations given by the authorized state auditor in the final regularity audit report for 2016 concerning the IT Strategy and the IT controls of the systems in place, have not been implemented for the most part, which affects and continuously creates high risks in the IT financial processes of the company's operation.

Although the competent services constantly undertake activities, the land recorded in the trade books has not been fully confirmed, and there are differences between the accounting and the factual state of affairs and the title deeds.

JSC MEPSO Skopje owns the electricity transmission network, which consists of line infrastructure facilities (transmission lines), transformer stations (substations), plants, facilities and assets for transmission of electricity and managing the electricity transmission system that functions on 400kV and 110kV voltage level.

The transmission network managed and maintained by the company integrates 109 transmission lines. Part of these transmission lines (30) are registered in the Real Estate Cadastre Agency and JSC MEPSO Skopje holds the title deed. For 79 transmission lines the company does not hold title deeds and procedures have been initiated to determine their legal status.

According to data from the Department of Substations, according to the voltage level the transmission network integrates 5 substations, of which 4 are owned by JSC MEPSO Skopje, and the other is jointly owned by EVN Macedonia JSC, JSC ESM and large consumers directly connected to the power grid. According to data from the Department of Property and Legal Affairs, 32 substations are registered in the Real Estate Cadastre Agency and title deeds have been issued - 10 substations are owned by JSC MEPSO Skopje and 3 are jointly owned by EVN Macedonia JSC and one large consumer. For the remaining 19 substations, EVN Macedonia JSC holds the ownership rights, and for 17 substations ownership rights have not been registered.

The audit identified discrepancy in the number of transmission lines and substations recorded by the competent departments in JSC MEPSO Skopje and with the data in the accounting records, as follows:

	Department of transmission lines	Department of Substations	Department of Accounting	Department of Property and Legal Relations
No. of transmission lines	109		103	100
No. of substations		60	49	Not possible to determine

The substations which were supposed to be jointly owned by JSC MEPSO Skopje and EVN Macedonia JSC, according to the title deeds are registered as property of EVN Macedonia JSC only. Although JSC MEPSO Skopje is making efforts to register these substations based on the Law on transforming Electricity Industry of Macedonia, the Real Estate Cadastre Agency did not issue title deeds for the substations to JSC MEPSO Skopje until the end of the audit.

In addition, with the inspection of the title deeds, the auditors found that for 2 substations there is a right of pledge (mortgage) registered in the amount of 77 million euros to the EBRD as the right holder (creditor), while EVN JSC Macedonia is registered as the mortgagee, as the right holder (owner). Due to the fact that ownership right of JSC MEPSO Skopje has not been confirmed, the decisions that contain risk of alienation of assets with mortgage are made without its consent.

This situation has an impact on the amount of EE transmission tariff, which is determined with a decision issued by Energy Regulatory Commission based on accounting data and financial records submitted by JSC MEPSO Skopje.

The audit report notes that 30% of assets in preparation i.e. 428.352.000 denars represent invested funds in the period 2005-2019 in equipment, consulting services, paid commissions for loan approval and non-withdrawn funds for project loans. Due to lack of information these are not properly linked to investments in a particular asset. These assets in preparation have not been put into use, which affects the depreciation costs, and thus the achieved financial result.

For financing investment activities, such as construction of substations and transmission lines, and revitalization of the transmission network JSC MEPSO Skopje uses funds from several

credit lines, based on signed loan agreements with international financial institutions. Most of the long-term loans (over 90%) have been realized (withdrawn) with the exception of the EBRD loan from 2015, intended for implementation of the Macedonia-Albania Interconnection project - Phase 1. This 37-million-euro loan has been approved and as of 31 December 2021, 2.9 million euros have been withdrawn, i.e. only 8%. With the performed audit, we found that in 2021, based on interest repayment, expenses in the amount of 32.404.000 denars were recorded for withdrawn long-term loans, and commission in the amount of 12.835.000 denars has been calculated and recorded for non-withdrawn credit funds.

As a result of the enormous increase in the price of electricity on the European stock exchanges in 2021, the insufficient production of electricity by domestic producers and the unauthorized taking of electricity from the electricity transmission system by the Balance-responsible parties contributed to the receivables and revenues of JSC MEPSO Skopje from electricity traders – Balance-responsible parties 2021 to amount to 4.210.704.000 denars or 68.5 million euros based on compensation for deviations / imbalances for the electricity taken from the electricity transmission system in 2021. This represents five times greater achievement compared to 2020, when they amounted to 841.792.000 denars i.e. 13.7 million euros.

Namely, due to the increase in the price of electricity, some electricity traders were continuously reducing the purchase of electricity from the open market and used the balance energy of JSC MEPSO Skopje to supply their consumers. This has caused a drastic increase in the costs of JSC MEPSO Skopje towards the European electricity transmission system. Extremely large deviations/imbalances were made in October 2021, due to which JSC MEPSO Skopje invoiced and collected 77.8 million kWh from the electricity producer JSC ESM Skopje in the amount of 25 million euros VAT exclusive. This resulted from the fact that JSC ESM Skopje failed to realize the plans for electricity production, and therefore electricity was withdrawn from the European grid, which created the obligation toward the European electricity transmission system in the amount of 25 million euros for JSC MEPSO Skopje.

Additional reason behind the above state of affairs is the manner of informing by electricity traders, who illegally took electricity from the electricity transmission system. Data received from MEMO DOOEL through Elektrodistribucija DOOEL arrives with 45 to 60 days delay, which is why JSC MEPSO Skopje is not able to do a quick intervention and take timely measures against the traders.

Considering the overall impact on the economic situation in the country caused by the lack of electricity, in November 2021 the Government passed a Decree releasing electricity traders from the obligation to increase bank guarantees based on signed balance responsibility agreements, and JSC MEPSO Skopje signed agreements for reprogramming due and unpaid debts. In December 2022, claims based on signed reprogramming agreements for withdrawn electricity from the electricity transmission system amount to 883.802.000 denars or over 14 million euros. The audit report points to the risk and uncertainty of collection thereof.

In 2021, value adjustment in the amount of 15 million euros was made for part of the receivables under reprogrammed contracts from electricity traders, and for fines and

damages due to interruption of delivery of the contracted electricity. During 2022, part of the receivables (1.2 million euros) were collected.

JSC ESM Skopje is the largest electricity producer in the country and in line with the Energy Law, it is obliged to offer for sale certain percentage of electricity to the Universal supplier - EVN Home DOO. In the past several years, acting upon Government's Extracts, almost the entire quantity of electricity produced by JSC ESM Skopje was sold to the Universal supplier at a fixed (reduced) price by the Government, which is much lower than the market price and the price on HUPX stock exchange. The balance mechanism in JSC MEPSO Skopje is designed in such way that for electricity taken from the electricity transmission system in larger quantity than planned, electricity traders pay to JSC MEPSO Skopje, and for unplanned excess electricity in the electricity transmission system, JSC MEPSO Skopje is obliged to pay electricity traders in line with settlement prices determined with the Methodology for calculation of the settlement price, prescribed in the Rules for Balancing the Electricity System, which is directly influenced by the price at HUPX stock exchange.

The audit found large settlements of deviations in the planned amounts of electricity in JSC MEPSO Skopje in 2021 and 2022. These deviations should occur only in exceptional situations and their occurrence creates great uncertainty in the planning and realization of revenue and expenditure on this basis, in maintaining necessary liquidity of cash assets, as well as in maintaining the balance mechanism. The expenditure for realized surplus of electricity from the Universal supplier of JSC MEPSO Skopje in 2021 amounts to 158.817.000 denars VAT exclusive, while the revenue from the Universal supplier amounts to 412.404.000 denars VAT exclusive.

In the period from 2019 until 2021, JSC MEPSO Skopje has signed agreement with JSC TEC Negotino for provision of electricity in the event of threats to security of supply, breakdowns or major deviations in the consumption from the foreseen quantities of electricity in the electric power system. It was agreed TEC Negotino to retain available power of the thermal power plant only for the needs of JSC MEPSO Skopje. For that period JSC MEPSO Skopje has paid 531.998.000 denars VAT inclusive, of which 219.778.000 denars have been paid in 2021. Although TEC Negotino was financially supported, it was not activated for production of electricity when the energy crisis occurred in October 2021.

Necessary condition for balancing the electric power system is to have equation of the total input and the total output of electricity in the system. The average annual consumption of electricity in the Republic of North Macedonia in the last five years is around 7.430 GWh, where the largest share in the total consumption with over 65% goes to households and street lighting.

According to JSC MEPSO Skopje forecasts, in the period from 2025 to 2030, the adequacy of the system in terms of energy will be satisfied with a significant import of about 55% of the total needs of electricity because of the expected low level of production of electricity of about 3,600 GWh due to reduced operation of TEC Bitola. By activating power plants from renewable energy sources as well as gas power plants, the import of electricity would decrease. As a result of the increase in electricity consumption in the Republic of North Macedonia, projects for large-scale production of electricity are needed.

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