

SERBIA - COUNTRY REPORT 2006

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SCOPE

The Energy Community Treaty requires the adoption, according to a timetable, of certain legal acts from the *acquis communautaire* in the areas of electricity, gas, competition, environment and renewable energy sources. This report is a first analysis of the status quo of each party in relation to the *acquis communautaire*. At this stage it has not been assessed the actual implementation or the functioning of the energy markets.

The report was prepared based on the responses provided by the Parties to a detailed questionnaire regarding the *acquis communautaire* on electricity, gas, renewable energy, environment and competition; on interviews with representatives of relevant organizations from the Parties and finally on the available national legal acts.

1. INSTITUTIONAL BUILDING

1.1. Ministries

The Ministry of Mining and Energy (<http://www.mem.sr.gov.yu>) is responsible of preparing and implementing the legislation for the electricity and gas sectors. The governments of the autonomous provinces have also considerable competences in the energy sector. The Ministry of Science and Environmental Protection (<http://www.mntr.sr.gov.yu>) is in charge of drafting and implementing the legislation in the area of environment and energy efficiency, the last one, in close coordination with the Ministry of Mining and Energy. An independent agency for the promotion of energy efficiency (<http://www.seea.sr.gov.yu>) was set up in 2002 and its tasks were defined under the 2004 Energy Law. The coordination between Administrations would need to be strengthened to facilitate the implementation of the Energy Community Treaty.

The Serbian Statistical Office develops in coordination with the Ministry of Mining and Energy, the national energy statistics. However, there would be a need to harmonise the methodology currently used with Eurostat requirements.

1.2. Energy Regulators

The Energy Agency of the Republic of Serbia (<http://www.aers.org.yu>) was established by the Energy Law in 2004 and it is operational since mid 2005. Among other responsibilities the Agency is responsible for issuing the tariff methodologies for electricity and natural gas prices, as well as the tariffs structures. The Government of Serbia is in charge of the final approval of the tariff structure and final prices. The Energy Agency also issues the licenses and approves the grid code and the market rules.

1.3. Competition Authority

The Competition Authority was established by the Law on Protection of Competition, however the members of its Management Board were not appointed until late April 2006. Competition Affairs were until the establishment of the Authority responsibility of the Ministry of Trade, Tourism and Services (<http://www.minttu.sr.gov.yu>).

2. ELECTRICITY SECTOR

2.1. Introduction

Serbia is in negotiations with the European Union on a Stabilisation and Association Agreement. In the last years Serbia has devoted efforts to bring the electricity legislation in line with the *acquis communautaire*.

The basic legal framework is provided by the 2004 Energy Law. Relevant secondary legislation is mainly in force, with the exception of the especially important Market Rules and the Transmission Grid Code, currently under development. Both drafts have been drafted by the Transmission System Operator (Elektromreza Srbije-EMS) and the texts will soon be submitted to the Energy Regulatory Agency, for approval. Drafting the distribution grid code is responsibility of the Elektroprivreda Srbije-EPS. The final version needs to be approved by the energy regulatory authority.

In the year 2005, it was also adopted the Energy Sector Development Strategy of the Republic of Serbia by 2015. The purpose of the document was to propose the Government a set of recommendations in the area of energy policy in line with the legal framework set in the 2004 Energy Law.

2.2. Public service obligations and customer protection

- Under the 2004 Energy Law the electricity activities have to fulfil a number of public service obligations. The provisions in the Energy Law are further developed in a specific act adopted in 2005 on public utilities and public service obligations.
- There are no specific provisions regarding the appointment of a supplier of last resort.
- Protection of vulnerable consumers is addressed in the Decree on General Conditions for Power Delivery passed in December 2005.

2.3. Monitoring of Security of Supply

- Security of supply is addressed in the Energy Law and in the Decree on General Conditions for Power Delivery with the Government of Serbia being the ultimate responsible. The Decree assigns responsibilities between the Autonomous Provinces, the Ministry of Energy and the Transmission System Operator. Some of the competences are related to the preparation of the energy balances, the infrastructure development plans and the operation of the system.

2.4. Technical rules

- The Transmission Grid Code is being prepared in accordance with the UCTE Operational Handbook. EMS, the appointed TSO, is drafting the Code. The Transmission Grid Code which has to be approved by the energy regulatory authority is expected to enter into force in the second half of 2006.
- The drafting of the Market Rules, which also requires the approval of the energy regulatory authority, will include among other issues the balancing arrangements.
- The distribution grid code is to be prepared in a later stage and its coordination is responsibility of the Elektroprivreda Srbije-EPS. The final approval, as for the transmission grid code and the market rules, is responsibility of the energy regulatory authority.

2.5. Generation

- The generation activity, as it is the case for the rest of electricity activities, requires a license issued by the Energy Agency according to the Energy Law (2004) and the Energy License Code (2005). In addition an Energy Permit Code intended to grant authorisations for the construction or refurbishing of facilities is enforced and responsibility of the Ministry of Mining and Energy. If needed, and on the grounds of

Security of Supply, the legislation allows to tender new capacity. The tendering criteria are established in the Concession Law.

2.6. Unbundling provisions and access to accounts

Transmission System Operator

- The 2004 Energy Law called for the legal unbundling of the Transmission System Operator (TSO) whose tasks are also defined in the law. In July 2005 the incumbent vertically integrated company was legally unbundled into two enterprises; EPS whose activities are generation, distribution and trading; and EMS, in charge of the transmission network activities and the operation of the system. A governmental Decree passed in 2005 formally appoints EMS as the Serbian TSO.

Distribution System Operator

- The Energy Law defined the tasks of Distribution System Operators. An Act was also adopted to establish five distribution companies under the ownership of the incumbent electricity company, EPS, which also has generation facilities. The Energy Law allows however Distribution System Operators to perform retailing to regulated customers without the need of legal and organisational unbundling.

Access and unbundling of the accounts

- The energy regulatory authority has the right to access the accounts of electricity undertakings. Accounting unbundling between energy activities is required under the Energy Law and companies are responsible of ensuring that the accounts are audited by an independent auditor. The reports must be submitted to the energy regulatory authority and publish them in accordance to the legislation regarding accounting.

2.7. Third Party Access (TPA)

- Non discriminatory, transparent and regulated third party access is envisaged in the Energy Law. The Transmission System Operator and the Distribution System Operators are requested under the Energy Law to justify any TPA refusal based on technical grounds. The tariff methodologies are still being drafted by the energy regulatory authority which is using a cost plus methodology. The framework methodology is expected to be presented by the energy regulator in June 2006...

2.8. Market opening

- The national legislation does not include a detailed eligibility calendar. The 2004 Energy Law has established the eligibility threshold at a consumption of 25 GWh per annum. This consumption level is reached by approximately 30 consumers representing 12% in terms of energy. The energy regulator is empowered to modify the eligibility threshold and to keep a register of the eligible customers. At present no eligible customer is however participating in the market as the regulated retail prices are well below costs.

2.9. Direct lines

- The legislation does not establish differences between direct and ordinary lines.

2.10. Safeguard measures

- In case of sudden crisis the Energy Law and the Decree of General Conditions for Power Delivery give the responsibility to manage the electricity operations to the Government and to the Transmission System Operator.

2.11. Cross border trade mechanism

- The Serbian System Operator is participating in the SETSO ITC Compensation mechanism and in the Dry run project for capacity allocation and congestion management.
- As for the allocation of capacity at the interconnectors, the Serbian TSO applies in the eight borders a monthly pro-rata capacity allocation method. The temporary rules valid for the first half of 2006 have been issued by the TSO and are available on its website. The TSO also publishes on its website the available transmission capacity at the interconnectors one month ahead.

3. GAS SECTOR

3.1. Introduction

The NIS, National oil and Gas Company of Serbia, was restructured and reorganised in October 2005 into three different companies. The first company, under the name of NIS, is responsible for the all oil related issues. In addition, the exploration and production activities of natural gas are also under responsibility of NIS. The second company, public oil transport company, Transnafta, will carry out the oil pipelines transportation activities. Srbijagas, the natural gas company, will be responsible from gas related issues mainly transmission, storage, distribution and trade activities.

The Ministry of Energy and Mining is the responsible body granting authorisation for all natural gas facilities construction and refurbishment. The licences are granted by the Energy Agency for the natural gas activities.

The natural gas usage is relatively low in Serbia. The domestic production is very low. Natural gas is currently used mainly in industry. The share of gas in primary energy is slightly high and it is expected to relatively increase in near future. Despite the transmission lines are not well developed, the distribution lines are slightly developed. The gas consumption is expected to slightly increase for the near future. The share of gas in power is quite low.

Third party access (TPA) is regulated according the Energy Law. However the network code is under preparation. Consumers, whose annual consumption is above the 15 million m³/year have right to choose their own gas suppliers. At present, the gas market opening level is around 60%. Although eligible consumers have right to choose their suppliers, this right currently cannot be exercised because of the de facto monopolistic position of Srbijagas.

The distribution activities are under control of Srbijagas. The right of operations is assigned to municipalities and private companies.

The Energy Law foresees the right to import natural gas. However the supply side competition is created by Law, this right has not been exercised yet by private companies.

Serbia has already started to establish legal and regulatory framework for natural gas market. The Energy Law came into force in August 2004. The secondary legislation is still

under preparation (mostly completed). Nonetheless, the new structure is seen to be mostly compatible with 2003/55/EC Natural Gas Directive.

3.2. Public service obligation and customer protection

- The natural gas activities have the status of activities of general interest. The provisions in the Energy law are relied on a specific law adopted in 2005 on public utilities and public service obligations.
- There are no specific provisions regarding the appointment of a supplier of last resort.
- Some groups of customers are protected by the Energy Law but the definition of customers is not clearly defined. The protection of vulnerable customers is intended to be realised by the authorised tariffs customers which is under preparation at the time being.

3.3. Monitoring security of supply

- Security of supply is addressed in the Energy Law. The Law assigns responsibilities between the Autonomous Provinces and the Ministry of Energy and Mining and the Transmission System Operator.
- The energy development plans including energy sources, sustainability of energy required, level of stocks, reserve capacities, reliability of sources etc. are defined by companies and submitted to Autonomous Provinces and local self-government units. Autonomous Provinces and local self-government units are submitted these reports to Ministry of Energy and Mining. Ministry of Energy and Mining is submitted these reports to Government for approval for the forthcoming year.
- The Government of Republic of Serbia is the responsible authority in order to take necessary measures in case of a sudden crisis in the energy market regarding to safeguard measures.

3.4. Technical rules

- It is required an authorisation from the Ministry of Energy and Mining for natural gas facilities construction and refurbishment. The energy companies related to infrastructures mainly transmission, storage and distribution shall be responsible from all technical rules, operational principles and procedures and preparation of network codes. The Network code and other technical rules are subject to the approval of Energy Agency. The network code and other technical rules are under preparation at the time being by the relevant companies in coordination with Energy Agency.

3.5. Unbundling provisions and access to accounts

- The Energy Regulatory Authority has the right to access the accounts of natural gas undertakings. Accounting unbundling is adopted in the Energy Law and the energy regulator is responsible of its monitoring and has right to access to accounts. The natural gas entities are required to publish their account reports and submit the balance sheets and auditing report to Regulatory Agency.
- The Energy Law does not foresee a time table for the unbundling of Srbijagas. However the organisational unbundling is in place currently. The legal and managerial unbundling is not envisaged within the new legal framework.

3.6. Third party access

- Third party access (TPA) is regulated for transmission, storage and distribution activities. System operators are obliged to give access to third parties to the system based on the principles of transparency and non-discrimination rules. The system operators are obliged to justify to the interested party the refusal of access to the network. In case of rejection of access to system, Agency's decision shall be final and binding.
- The tariff methodologies are still being drafted by the energy regulatory authority which will be based on a cost reflective methodology. The framework methodology is expected to be presented by the energy regulator in the coming months.

3.7. New infrastructure and exemptions

- There is no mechanism defined by Law for granting an exemption for new natural gas infrastructures.

3.8. Market opening

- The national legislation does not foresee a staged eligibility calendar yet. The Regulatory Authority has the discretionary right to set the threshold for eligibility. The eligibility threshold is 15 million m³/year for the year 2006. The market opening level is equivalent to about 60%.

4. COMPETITION

The Law on Protection of Competition was adopted in September 2005. The law aims to transpose articles 81 and 82 of the Treaty establishing the European Community. Hence it includes provisions regarding those practices that violate competition the following; agreements between undertakings preventing, restricting or distorting competition; abuse of dominant position; or concentration leading to prevention, restriction or distortion of competition.

The issue of aid granted by the State to certain undertakings which could distort competition is not however covered in this Law.

With the recent establishment of the Competition Authority it is expected that Secondary legislation will be developed.

5. ENVIRONMENT

The Ministry of Environment and the European Agency for Reconstruction have prepared a Draft National Environmental Strategy which is at present under inter-Ministerial consultation. The document intends to cover all the economic activities and also includes an economical assessment of its implementation estimated in 4b euros during the period 2005-2014. About 30% would account for expenditure in the energy sector.

Some legislation aiming to transpose the *acquis communautaire* has been passed such as the procedures for Environmental Impact Assessment or the Law on Integrated Pollution and Prevention Control. Some legislation is still to be transposed and one of the key challenges will be to ensure the implementation of the legislation given the considerable investments required.

6. ENERGY EFFICIENCY AND RENEWABLE ENERGY SOURCES

The National Energy Strategy by 2015 contains some considerations on energy efficiency. However there is no National Plan yet.

Serbia does not have legislation yet on the promotion of electricity from Renewable Energy Sources or the Directive regarding biofuels for transport. The Ministry of Science and the Environmental Protection has been conducting National Energy Efficiency Program (NEEP) in the area of energy efficiency and Renewables and the results are available on the Ministry web site.

7. ENERGY INFRASTRUCTURE PROJECTS

The projects proposed by Serbia that are important for the regional energy market include:

Electricity Generation:

- TPP lignite fired Units 1 and 2 with a total capacity of 700 MW. The construction of the power plant was halted during the Balkan conflict and about 500M US\$ are necessary for its completion.
- CHP power plant in Novi Sad with a capacity of about 200-500 MW.

Electricity Transmission/ Interconnectors:

- Finalisation of the 400 KV transmission line between: Bosnia and Herzegovina (Ugljevik) and Serbia (Sremska Mitrovica). The line of 75 km between BiH and Serbia is completed, together with the appropriate bay in the sub-station in Sremska Mitrovica (400/220/110 kV). The finalization of bays in TP Ugljevik is ongoing and the line is scheduled to be in service, during the spring of 2006. The total cost of the project is approx. EUR 15 million and it was financed by the power company, EMS.
- Construction of 400 kV transmission line between Serbia (Vrsac) and Romania (Timisoara). A Memorandum of understanding was signed between parties and, currently project is in the feasibility study phase. Estimated start year is 2007 and completion year, 2009. The cost of the project, as well as the financing sources is not available at this stage.

Gas:

- Construction of the underground Gas Storage at Banatski Dvor; the project is designed for a total capacity of max 800 million m³, of which 300 million m³ in stage 1. The project is developed in 2 stages 2006/2006 and 2006/2011; the total estimated cost of project is EUR 128 million: EUR 50 million in stage 1 and EUR 78 million in stage 2.
- Construction of a gas supply pipeline between Serbia (Nis)–Bulgaria (Dupnica), with of length of 106 km and a capacity of 1800x106 m³/y; the project is under preparation and the estimated cost is US\$ 60 million.
- Construction of a gas supply pipeline between Serbia (Mokrin)–Romania (Arad), with of length of pipeline length: 76 km; the Pipeline capacity: 1600x106 m³/y; estimated investment costs US\$ 18.5 million. The project is at the proposal stage.
- Construction of a gas transit route from Serbia to Bosnia and Herzegovina (Batajnica-Bijeljina-Novigrad) - Sava Project; the pipeline length: 98 km (Serbian

side); the pipeline capacity: 1200x106 m³/y; the estimated investment cost: US\$ 50 million; the project is in the proposal phase.

- Connection to the Croatian Gas Pipeline System through the routes: Sombor-Osijek, Bačka Palanka-Ilok, Sremska Mitrovica (Šid)-Vinkovci; the estimated cost is: US\$ 4 – 8.5 mil USD and the project status: foreseeable.

8. CONCLUSIONS

Serbia is in negotiations for establishing a Stabilisation and Association Agreement with the European Union although these have been temporarily put on hold.

Serbia has established the basic **institutional framework** for energy, environment and competition affairs with some of them being operational only for a few months. In addition to the relevant Ministerial Departments, the Energy Regulatory Authority and the Competition Authority have been established. Currently there is no National Plan regarding Energy Efficiency.

In **electricity**, in 2004 Serbia adopted the Energy Law which opened the way for the liberalisation and opening of the electricity sector. The Secondary legislation is under way to adopt the Market Rules, the Transmission Grid Code and the Distribution Grid Code. The energy regulatory authority intends to approve by summer a new tariff methodology. While the Transmission System Operator has been recently unbundled, the Distribution System Operators can still however perform supply activities without further unbundling being envisaged. One of the most outstanding obstacles to the true functioning of the market is the low level of the regulated retail electricity prices, which are well below the costs. This is one of the reasons why no eligible customer is participating in the market. Serbia calls for assistance to analyse the problem and to propose solutions.

In **natural gas**, Serbia has already started to establish legal and regulatory framework for natural gas market. The Energy Law came into force in 2004. The secondary legislation is still under preparation. Nonetheless, the new structure is seen to be mostly compatible with 2003/55/EC Natural Gas Directive. The Energy Law does not foresee a time table for the unbundling of Srbijagas. However the organisational unbundling is in place currently. The legal and managerial unbundling is not envisaged within the new legal framework, but a Working Group to propose further restructuring of Srbijagas has been established.

In **competition**, Serbia has recently passed a Law on Protection of Competition which tackles antitrust practices. However it is still to be addressed State Aid.

Serbia has still no legislation regarding the production of electricity from **Renewable Energy Sources** or the promotion of biofuels for transport.

In Environment, Serbia has adopted some legal acts such as the procedures for Environmental Impact Assessment or air pollution. Serbia is also preparing a National Environmental Strategy which also intends to provide an economical assessment of the implementation of the environmental acquis. The energy sector would account under this plan for approximately one third of the investment needs.