

**TO THE MINISTERIAL COUNCIL OF THE ENERGY COMMUNITY**  
**represented by the Presidency and the Vice-Presidency of the Energy Community**

**REASONED REQUEST**

in Case ECS-8/11

Submitted pursuant to Article 90 of the Treaty establishing the Energy Community and Article 28 of Procedural Act No 2008/1/MC-EnC of the Ministerial Council of the Energy Community of 27 June 2008 on the Rules of Procedure for Dispute Settlement under the Treaty, the

**SECRETARIAT OF THE ENERGY COMMUNITY**

against

**BOSNIA AND HERZEGOVINA**

seeking a Decision from the Ministerial Council that Bosnia and Herzegovina,

1. by failing to designate one or more competent bodies with the function of regulatory authorities to cover the entire gas sector in Bosnia and Herzegovina, fails to comply with Article 25 of Directive 2003/55/EC;
2. by failing to implement the requirement of legal unbundling of transmission system operators from other activities not relating to transmission, fails to comply with Article 9(1) of Directive 2003/55/EC;
3. by failing to ensure the independence of the transmission system operators in terms of its organization and decision-making from other activities not relating to transmission, fails to comply with Article 9(1) and (2) of Directive 2003/55/EC;
4. by failing to obligate the transmission system operator of the Federation of Bosnia and Herzegovina to establish a compliance programme, fails to comply with Article 9(2)d of Directive 2003/55/EC;
5. by failing to implement the obligation to audit and publish the accounts of natural gas undertakings, fails to comply with Article 17(2) of Directive 2003/55/EC;
6. by failing to set and apply separate transmission tariffs in Republika Srpska, fails to comply with Articles 18(1) and 25(2) of Directive 2003/55/EC as well as Article 3 of Regulation 1775/2005;
7. by maintaining a possibility for negotiated access to the transmission system in the Federation of Bosnia and Herzegovina, fails to comply with Article 18(1) of Directive 2003/55/EC;
8. by failing to approve and to publish transmission and distribution tariffs (or a corresponding methodology) in the Federation of Bosnia and Herzegovina, fails to comply with Article 18(1) of Directive 2003/55/EC and Article 3 of Regulation 1775/2005;

9. by failing to require the involvement of a regulatory authority in the procedure for exempting major new gas infrastructures from certain provisions of Directive 2003/55/EC, and by not requiring an exemption decision to be reasoned and published in the Federation of Bosnia and Herzegovina, fails to comply with Article 22 of Directive 2003/55/EC;
10. by failing to grant eligibility to all „non-household“ customers in the Federation of Bosnia and Herzegovina, fails to comply with Article 23(1)(b) of Directive 2003/55/EC;
11. by maintaining a reciprocity requirement limiting eligibility in cases of transactions with a foreign supplier, as well as of inner-Bosnian transactions, in the Federation of Bosnia and Herzegovina, fails to comply with Article 23 of Directive 2003/55/EC;
12. by the transmission system operator in Republika Srpska failing to offer third party access services other than firm services and only for one year ahead, fails to comply with Article 4(1)(b) and (c) of Regulation 1775/2005;
13. by the transmission system operator in Republika Srpska failing to balance the gas system in accordance with balancing rules, and to set cost-reflective imbalance charges and publish them, fails to comply with Article 7(1) and (3) of Regulation 1775/2005;
14. by failing to provide for effective, proportionate and dissuasive penalties for non-compliance with the obligations under the Rulebook on the Operation of Transmission Network in Republika Srpska, fails to comply with Article 13 of Regulation 1775/2005;
15. by failing to adopt appropriate legislation and to apply it by the transmission system operator of the Federation of Bosnia and Herzegovina, fails to comply with Articles 4, 5, 6, 7, 8 and 13 of Regulation 1775/2005.

The Secretariat of the Energy Community has the honour of submitting the following Reasoned Request to the Ministerial Council.

## **I. Relevant Facts**

1. As a Contracting Party to the Treaty establishing the Energy Community (“the Treaty”), Bosnia and Herzegovina is under an obligation to implement the *acquis communautaire* on energy as listed in Article 11 of the Treaty. This includes Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas.<sup>1</sup>
2. Bosnia and Herzegovina has never adopted gas legislation on the State level with the purpose and effect of transposing Directive 2003/55/EC. Legislation governing the gas sector is, however, to be found on the level of the two constitutional entities, Republika Srpska and Federation of Bosnia and Herzegovina.

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<sup>1</sup> With effect of 6 October 2011, Article 11 and Annex I have been amended by Ministerial Council Decision 2011/02/MC-EnC so as to replace the Directives and Regulations constituting the so-called Second Package (including Directive 2003/55/EC) by the Directives and Regulations constituting the so-called Third Package. As the latter are only to be implemented by 1 January 2015 (see Article 3 of Decision 2011/02/MC-EnC), the implementation of the provisions of the Second Package, including Directive 2003/55/EC, is still obligatory for the Contracting Parties.

3. In **Republika Srpska**, a Law on Gas has been in force since September 2007.<sup>2</sup> This Law was amended as a response to the Secretariat's Opening letter in the present case.<sup>3</sup> The amendments took effect on 2 January 2013.
4. As regards the market structure, gas supply in Republika Srpska is carried out by three companies, two of which are licensed for trade<sup>4</sup> and supply as well as supply for tariff customers within Republika Srpska only, namely *Sarajevo-gas a.d. Istocno Sarajevo* and *A.D. Zvornik Stan, Zvornik*. The third supplier of natural gas (also) in Republika Srpska is *BH Gas*, licensed by the Federation of Bosnia and Herzegovina.
5. *Sarajevo-gas a.d. Istocno Sarajevo* has a license as a "transporter" of natural gas, and a fourth company, *Gas Promet, Pale* is designated as that entity's transmission system operator.<sup>5</sup> *Gas Promet* also holds a trade and supply license (without, however, currently supplying gas).
6. In the **Federation of Bosnia and Herzegovina**, a Decree on the Organization and Regulation of the Gas Sector applies since November 2007.<sup>6</sup> That Decree was adopted as a transitional solution until the adoption of a State law applying to the gas sector.<sup>7</sup> Due to conflicting positions of the entities,<sup>8</sup> a State law has never been adopted. As a reaction to the Secretariat's Opening Letter and Reasoned Opinion in the present case, the Ministry of Energy, Mining and Industry of the Federation of Bosnia and Herzegovina developed a "pre-draft" Law on Gas.<sup>9</sup> At the time of the present Reasoned Request, however, it has not yet been adopted.
7. In the Federation of Bosnia and Herzegovina, *BH Gas* exclusively performs both supply and transmission system operation.
8. On the State level in **Bosnia and Herzegovina**, the introduction of legislation has been and is subject to controversy. The Ministry of Foreign Trade and Economic Relations („MOFTER") had established a Working Group already in 2007, involving the ministries and transmission system operators of both entities, as well as the MOFTER itself. The task of the Working Group was to develop and propose to the decision-makers an appropriate legal framework for gas in Bosnia and Herzegovina, which would ensure transposition of the gas-related *acquis communautaire* under the Energy Community Treaty. The Working Group, however, could never reach an agreement on one common proposal supported by both entities' experts. The Working Group ceased to operate without any result in May 2009. In a meeting organized upon invitation by the Director of the Secretariat in Vienna on 17 February 2010, it was agreed among all three Ministers in charge of energy to revive the Working Group and make it conclude its work within 30 days. After four meetings, the Working Group in July 2010 reported to the Secretariat on the outcome of its work. Rather than a joint proposal, for which the Group denied its competence, the report encompasses two different proposals by the two entities.

<sup>2</sup> Official Gazette of Republika Srpska No 86/07, Annex 6.

<sup>3</sup> Official Gazette of Republika Srpska No 121/12, Annex 7, and Republika Srpska's comments on the Reasoned Opinion, Annex 5a, at page 2.

<sup>4</sup> "Trade" is defined in the amended Law (Article 3(i)) as "*purchase for the purposes of resale and sale of natural gas at free market to energy undertakings and eligible customers.*" *E contrario*, this makes "supply" a commercial activity at fully regulated prices, see also Articles 37 and 40 of the amended Law.

<sup>5</sup> *Gas Promet Pale* was designated as transmission system operator of Republika Srpska by Government Decree in 2007 (Official Gazette of Republika Srpska 114/07). It holds a transmission system operation license issued by the regulatory authority under No 01-585-04-2/05/09 of 30 July 2009.

<sup>6</sup> Official Gazette of FBiH No 83/07, Annex 8.

<sup>7</sup> See the reply by the Federation of Bosnia and Herzegovina to the Opening Letter, Annex 2b, at page 3.

<sup>8</sup> See below, at paragraph 8.

<sup>9</sup> Annex 9. Apparently, the Government of the Federation of Bosnia and Herzegovina endorsed the draft at its session of 15 May 2013, and it is pending submission to Parliament.

9. Republika Srpska's position at the time was that there should be no gas legislation at all primary or secondary - on State level. Jurisdiction of the State-level national regulatory authority over the gas sector would be conceivable, but should be limited to international cooperation in cross-border issues, reporting to international organizations, approval of capacity allocation and congestion management methods interconnectors and harmonization of transmission tariff methodologies. To avoid separate State-level gas legislation, the extension of competences of the State regulatory authority on electricity, DERK, to gas should be achieved through amendments to the State electricity legislation of Bosnia and Herzegovina. The Federation of Bosnia and Herzegovina advocated for a Law on Gas at state level, with broader competences than Republika Srpska's proposal, extending DERK's jurisdiction to gas, international cooperation, defining a uniform transmission tariff methodology, license issuing and the approval of inter-entity development plans. Distribution should be regulated on the entity level. Unlike Republika Srpska, the Federation also wishes to establish a single transmission system operator on State level.
10. Given the failure to agree on or even draft an approach to State-level legislation, the Secretariat assessed the entities' legislation for compliance with the *acquis*. In its assessment, they fail to transpose, let alone implement, the *acquis communautaire*, by either leaving significant gaps or breaching individual provisions of Directive 2003/55/EC and Regulation (EC) No. 1775/2005. The relevant provisions of domestic law will be introduced and discussed in connection with the provisions from the *acquis communautaire* under point IV. below.

## II. Relevant Energy Community Law

11. Energy Community Law is defined in Article 1 of the Rules of Procedure for Dispute Settlement under the Treaty ("Dispute Settlement Procedures")<sup>10</sup> as "*a Treaty obligation or [...] a Decision addressed to [a Party]*". A violation of Energy Community Law occurs if "*[a] Party fails to comply with its obligations under the Treaty if any of these measures (actions or omissions) are incompatible with a provision or a principle of Energy Community Law*" (Article 2(1) Dispute Settlement Procedures).
12. In the following, a selection of provisions of Energy Community law relevant for the present case is compiled. This compilation is for convenience only and does not imply that no other provisions may be of relevance for its assessment.
13. Article 6 of the Treaty reads:
- The Parties shall take all appropriate measures, whether general or particular, to ensure fulfilment of the obligations arising out of this Treaty. The Parties shall facilitate the achievement of the Energy Community's tasks. The Parties shall abstain from any measure which could jeopardise the attainment of the objectives of the Treaty.*
14. Annex I to the Treaty, entitled "Timetable for the Implementation of the EC Directives No 2003/54 and 2003/55, and the EC Regulation No 1228/2003 of 26 June 2003", reads:
1. *Subject to paragraph 2 below and Article 24 of this Treaty, each Contracting Party shall implement within twelve months of the entry into force of this Treaty: (i) the European Community Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity; (ii) the European Community Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas; (iii) the European*

<sup>10</sup> Procedural Act No 2008/01/MC-EnC of 27 June 2008.



*Community Regulation 1228/2003/EC of the European Parliament and of the Council of 26 June 2003 on conditions for access to the network for cross-border exchanges in electricity.*

2. *Each Contracting Party must ensure that the eligible customers within the meaning of the European Community Directives 2003/54/EC and 2003/55/EC are: (i) from 1 January 2008, all non-household customers; and (ii) from 1 January 2015, all customers.*

15. Article 9 of Directive 2003/55/EC, entitled "Unbundling of transmission system operators", reads:

1. *Where the transmission system operator is part of a vertically integrated undertaking, it shall be independent at least in terms of its legal form, organisation and decision making from other activities not relating to transmission. These rules shall not create an obligation to separate the ownership of assets of the transmission system from the vertically integrated undertaking.*
2. *In order to ensure the independence of the transmission system operator referred to in paragraph 1, the following minimum criteria shall apply:*
  - a. *those persons responsible for the management of the transmission system operator may not participate in company structures of the integrated natural gas undertaking responsible, directly or indirectly, for the day-to-day operation of the production, distribution and supply of natural gas;*
  - b. *appropriate measures must be taken to ensure that the professional interests of persons responsible for the management of the transmission system operator are taken into account in a manner that ensures that they are capable of acting independently;*
  - c. *the transmission system operator shall have effective decision-making rights, independent from the integrated gas undertaking, with respect to assets necessary to operate, maintain or develop the network. This should not prevent the existence of appropriate coordination mechanisms to ensure that the economic and management supervision rights of the parent company in respect of return on assets regulated indirectly in accordance with Article 25(2) in a subsidiary are protected. In particular, this shall enable the parent company to approve the annual financial plan, or any equivalent instrument, of the transmission system operator and to set global limits on the levels of indebtedness of its subsidiary. It shall not permit the parent company to give instructions regarding day-to-day operations, nor with respect to individual decisions concerning the construction or upgrading of transmission lines, that do not exceed the terms of the approved financial plan, or any equivalent instrument;*
  - d. *the transmission system operator shall establish a compliance programme, which sets out measures taken to ensure that discriminatory conduct is excluded, and ensure that observance of it is adequately monitored. The programme shall set out the specific obligations of employees to meet this objective. An annual report, setting out the measures taken, shall be submitted by the person or body responsible for monitoring the compliance programme to the regulatory authority referred to in Article 25(1) and shall be published.*

16. Article 17 of Directive 2003/55/EC, entitled "Unbundling of accounts" reads:

1. *Member States shall take the necessary steps to ensure that the accounts of natural gas undertakings are kept in accordance with paragraphs 2 to 5. Where undertakings benefit from a derogation from this provision on the basis of Article 28(2) and (4), they shall at least keep their internal accounts in accordance with this Article.*
2. *Natural gas undertakings, whatever their system of ownership or legal form, shall draw up, submit to audit and publish their annual accounts in accordance with the rules of national law concerning the annual accounts of limited liability companies adopted pursuant to the Fourth Council Directive 78/660/EEC of 25 July 1978 based on Article 44(2)(g) of the Treaty on the annual accounts of certain types of companies. Undertakings which are not legally*

*obliged to publish their annual accounts shall keep a copy of these at the disposal of the public at their head office.*

3. *Natural gas undertakings shall, in their internal accounting, keep separate accounts for each of their transmission, distribution, LNG and storage activities as they would be required to do if the activities in question were carried out by separate undertakings, with a view to avoiding discrimination, cross-subsidisation and distortion of competition. They shall also keep accounts, which may be consolidated, for other gas activities not relating to transmission, distribution, LNG and storage. Until 1 July 2007, they shall keep separate accounts for supply activities for eligible customers and supply activities for non-eligible customers. Revenue from ownership of the transmission/distribution network shall be specified in the accounts. Where appropriate, they shall keep consolidated accounts for other, non-gas activities. The internal accounts shall include a balance sheet and a profit and loss account for each activity.*
4. *The audit, referred to in paragraph 2, shall, in particular, verify that the obligation to avoid discrimination and cross-subsidies referred to in paragraph 3, is respected.*
5. *Undertakings shall specify in their internal accounting the rules for the allocation of assets and liabilities, expenditure and income as well as for depreciation, without prejudice to nationally applicable accounting rules, which they follow in drawing up the separate accounts referred to in paragraph 3. These internal rules may be amended only in exceptional cases. Such amendments shall be mentioned and duly substantiated.*
6. *The annual accounts shall indicate in notes any transaction of a certain size conducted with related undertakings.*

17. Article 18(1) of Directive 2003/55/EC, entitled "Third party access", reads:

1. *Member States shall ensure the implementation of a system of third party access to the transmission and distribution system, and LNG facilities based on published tariffs, applicable to all eligible customers, including supply undertakings, and applied objectively and without discrimination between system users. Member States shall ensure that these tariffs, or the methodologies underlying their calculation shall be approved prior to their entry into force by a regulatory authority referred to in Article 25(1) and that these tariffs — and the methodologies, where only methodologies are approved — are published prior to their entry into force.*

18. Article 22 of Directive 2003/55/EC, entitled "New infrastructure" reads:

1. *Major new gas infrastructures, i.e. interconnectors between Member States, LNG and storage facilities, may, upon request, be exempted from the provisions of Articles 18, 19, 20, and 25(2), (3) and (4) under the following conditions:*
  - a. *the investment must enhance competition in gas supply and enhance security of supply;*
  - b. *the level of risk attached to the investment is such that the investment would not take place unless an exemption was granted;*
  - c. *the infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that infrastructure will be built;*
  - d. *charges are levied on users of that infrastructure;*
  - e. *the exemption is not detrimental to competition or the effective functioning of the internal gas market, or the efficient functioning of the regulated system to which the infrastructure is connected.*

2. *Paragraph 1 shall apply also to significant increases of capacity in existing infrastructures and to modifications of such infrastructures which enable the development of new sources of gas supply.*
3. (a) *The regulatory authority referred to in Article 25 may, on a case by case basis, decide on the exemption referred to in paragraphs 1 and 2. However, Member States may provide that the regulatory authorities shall submit, for formal decision, to the relevant body in the Member State its opinion on the request for an exemption. This opinion shall be published together with the decision.*
  - (b) (i) *The exemption may cover all or parts of, respectively, the new infrastructure, the existing infrastructure with significantly increased capacity or the modification of the existing infrastructure.*
    - (ii) *In deciding to grant an exemption consideration shall be given, on a case by case basis, to the need to impose conditions regarding the duration of the exemption and non-discriminatory access to the interconnector.*
    - (iii) *When deciding on the conditions in this subparagraph account shall, in particular, be taken of the duration of contracts, additional capacity to be built or the modification of existing capacity, the time horizon of the project and national circumstances.*
  - (c) *When granting an exemption the relevant authority may decide upon the rules and mechanisms for management and allocation of capacity insofar as this does not prevent the implementation of long term contracts.*
  - (d) *The exemption decision, including any conditions referred to in (b), shall be duly reasoned and published.*
  - (e) *In the case of an interconnector any exemption decision shall be taken after consultation with the other Member States or regulatory authorities concerned.*

19. Article 23 of Directive 2003/55/EC, entitled "Market opening and reciprocity" reads:

1. *Member States shall ensure that the eligible customers are:*

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  - (b) *from 1 July 2004, at the latest, all non-household customers;*
  - (c) *from 1 July 2007, all customers.*
2. *To avoid imbalance in the opening of gas markets:*
  - (a) *contracts for the supply with an eligible customer in the system of another Member State shall not be prohibited if the customer is eligible in both systems involved;*
  - (b) *in cases where transactions as described in point (a) are refused because the customer is eligible in only one of the two systems, the Commission may, taking into account the situation in the market and the common interest, oblige the refusing party to execute the requested supply, at the request of one of the Member States of the two systems.*

20. Article 25 of Directive 2003/55/EC, entitled "Regulatory authorities" reads:

1. *Member States shall designate one or more competent bodies with the function of regulatory authorities. These authorities shall be wholly independent of the interests of the gas industry. They shall, through the application of this Article, at least be responsible for ensuring non-discrimination, effective competition and the efficient functioning of the market, monitoring in particular:*
  - a. *the rules on the management and allocation of interconnection capacity, in conjunction with the regulatory authority or authorities of those Member States with which interconnection exists;*

- b. any mechanisms to deal with congested capacity within the national gas system;*
- c. the time taken by transmission and distribution system operators to make connections and repairs;*
- d. the publication of appropriate information by transmission and distribution system operators concerning interconnectors, grid usage and capacity allocation to interested parties, taking into account the need to treat non-aggregated information as commercially confidential;*
- e. the effective unbundling of accounts as referred to in Article 17, to ensure there are no cross subsidies between transmission, distribution, storage, LNG and supply activities;*
- f. the access conditions to storage, linepack and to other ancillary services as provided for in Article 19;*
- g. the extent to which transmission and distribution system operators fulfil their tasks in accordance with Articles 8 and 12;*
- h. the level of transparency and competition.*

*The authorities established pursuant to this Article shall publish an annual report on the outcome of their monitoring activities referred to in points (a) to (h).*

- 2. The regulatory authorities shall be responsible for fixing or approving prior to their entry into force, at least the methodologies used to calculate or establish the terms and conditions for:*
  - a. connection and access to national networks, including transmission and distribution tariffs. These tariffs, or methodologies, shall allow the necessary investments in the networks to be carried out in a manner allowing these investments to ensure the viability of the networks;*
  - b. the provision of balancing services.*
- 3. Notwithstanding paragraph 2, Member States may provide that the regulatory authorities shall submit, for formal decision, to the relevant body in the Member State the tariffs or at least the methodologies referred to in that paragraph as well as the modifications in paragraph 4. The relevant body shall, in such a case, have the power to either approve or reject a draft decision submitted by the regulatory authority.*

*These tariffs or the methodologies or modifications thereto shall be published together with the decision on formal adoption. Any formal rejection of a draft decision shall also be published, including its justification.*

- 4. Regulatory authorities shall have the authority to require transmission, LNG and distribution system operators, if necessary, to modify the terms and conditions, including tariffs and methodologies referred to in paragraphs 1, 2 and 3, to ensure that they are proportionate and applied in a non-discriminatory manner.*
- 5. Any party having a complaint against a transmission, LNG or distribution system operator with respect to the issues mentioned in paragraphs 1, 2 and 4 and in Article 19 may refer the complaint to the regulatory authority which, acting as dispute settlement authority, shall issue a decision within two months after receipt of the complaint. This period may be extended by two months where additional information is sought by the regulatory authorities. This period may be extended with the agreement of the complainant. Such a decision shall have binding effect unless and until overruled on appeal.*
- 6. Any party who is affected and who has a right to complain concerning a decision on methodologies taken pursuant to paragraphs 2, 3 or 4 or, where the regulatory authority has a duty to consult, concerning the proposed methodologies, may, at the latest within two months, or a shorter time period as provided by Member States, following publication of the*



*decision or proposal for a decision, submit a complaint for review. Such a complaint shall not have suspensive effect.*

- 7. Member States shall take measures to ensure that regulatory authorities are able to carry out their duties referred to in paragraphs 1 to 5 in an efficient and expeditious manner.*
  - 8. Member States shall create appropriate and efficient mechanisms for regulation, control and transparency so as to avoid any abuse of a dominant position, in particular to the detriment of consumers, and any predatory behaviour. These mechanisms shall take account of the provisions of the Treaty, and in particular Article 82 thereof.*
  - 9. Member States shall ensure that the appropriate measures are taken, including administrative action or criminal proceedings in conformity with their national law, against the natural or legal persons responsible where confidentiality rules imposed by this Directive have not been respected.*
  - 10. In the event of cross border disputes, the deciding regulatory authority shall be the regulatory authority which has jurisdiction in respect of the system operator, which refuses use of, or access to, the system.*
  - 11. Complaints referred to in paragraphs 5 and 6 shall be without prejudice to the exercise of rights of appeal under Community and national law.*
  - 12. National regulatory authorities shall contribute to the development of the internal market and of a level playing field by cooperating with each other and with the Commission in a transparent manner.*
21. Decision No 2007/06/MC-EnC of the Ministerial Council of the Energy Community of 18 December 2007 on the Implementation of Directive 2005/89/EC, Directive 2004/67/EC and Regulation (EC) No 1775/2005, in its Article 3, obliges the Contracting Parties to implement Regulation (EC) No 1775/2005 on conditions of access to the natural gas network before 31 December 2008.

22. Article 3 of Regulation (EC) No 1775/2005 entitled "Tariffs for access to networks" reads:

- 1. Tariffs, or the methodologies used to calculate them, applied by transmission system operators and approved by the regulatory authorities pursuant to Article 25(2) of Directive 2003/55/EC, as well as tariffs published pursuant to Article 18(1) of that Directive, shall be transparent, take into account the need for system integrity and its improvement and reflect actual costs incurred, insofar as such costs correspond to those of an efficient and structurally comparable network operator and are transparent, whilst including appropriate return on investments, and where appropriate taking account of the benchmarking of tariffs by the regulatory authorities. Tariffs, or the methodologies used to calculate them, shall be applied in a non-discriminatory manner.*

*Member States may decide that tariffs may also be determined through market-based arrangements, such as auctions, provided that such arrangements and the revenues arising therefrom are approved by the regulatory authority.*

*Tariffs, or the methodologies used to calculate them, shall facilitate efficient gas trade and competition, while at the same time avoiding cross-subsidies between network users and providing incentives for investment and maintaining or creating interoperability for transmission networks.*

- 2. Tariffs for network access shall not restrict market liquidity nor distort trade across borders of different transmission systems. Where differences in tariff structures or balancing mechanisms would hamper trade across transmission systems, and notwithstanding Article 25(2) of Directive 2003/55/EC, transmission system operators shall, in close cooperation*

*with the relevant national authorities, actively pursue convergence of tariff structures and charging principles including in relation to balancing.*

**23. Article 4(1) of Regulation (EC) No 1775/2005 entitled "Third party access services" reads:**

1. *Transmission system operators shall:*
  - a. *ensure that they offer services on a non-discriminatory basis to all network users. In particular, where a transmission system operator offers the same service to different customers, it shall do so under equivalent contractual terms and conditions, either using harmonized transportation contracts or a common network code approved by the competent authority in accordance with the procedure laid down in Article 25 of Directive 2003/55/EC;*
  - b. *provide both firm and interruptible third party access services. The price of interruptible capacity shall reflect the probability of interruption;*
  - c. *offer to network users both long and short-term services.*

**24. Article 5 of Regulation (EC) No 1775/2005 entitled "Principles of capacity allocation mechanisms and congestion management procedures" reads:**

1. *The maximum capacity at all relevant points referred to in Article 6(3) shall be made available to market participants, taking into account system integrity and efficient network operation.*
2. *Transmission system operators shall implement and publish non-discriminatory and transparent capacity allocation mechanisms, which shall:*
  - a. *provide appropriate economic signals for efficient and maximum use of technical capacity and facilitate investment in new infrastructure;*
  - b. *be compatible with the market mechanisms including spot markets and trading hubs, while being flexible and capable of adapting to evolving market circumstances;*
  - c. *be compatible with the network access systems of the Member States.*
3. *When transmission system operators conclude new transportation contracts or renegotiate existing transportation contracts, these contracts shall take into account the following principles:*
  - a. *in the event of contractual congestion, the transmission system operator shall offer unused capacity on the primary market at least on a day-ahead and interruptible basis;*
  - b. *network users who wish to re-sell or sublet their unused contracted capacity on the secondary market shall be entitled to do so. Member States may require notification or information of the transmission system operator by network users.*
4. *When capacity contracted under existing transportation contracts remains unused and contractual congestion occurs, transmission system operators shall apply paragraph 3 unless this would infringe the requirements of the existing transportation contracts. Where this would infringe the existing transportation contracts, transmission system operators shall, following consultation with the competent authorities, submit a request to the network user for the use on the secondary market of unused capacity in accordance with paragraph 3.*
5. *In the event that physical congestion exists, nondiscriminatory, transparent capacity allocation mechanisms shall be applied by the transmission system operator or, as appropriate, the regulatory authorities.*

**25. Article 6 of Regulation (EC) No 1775/2005 entitled "Transparency requirements" reads:**

6. *Transmission system operators shall make public detailed information regarding the services they offer and the relevant conditions applied, together with the technical information necessary for network users to gain effective network access."*
7. *In order to ensure transparent, objective and nondiscriminatory tariffs and facilitate efficient utilisation of the gas network, transmission system operators or relevant national authorities shall publish reasonably and sufficiently detailed information on tariff derivation, methodology and structure.*
8. *For the services provided, each transmission system operator shall make public information on technical, contracted and available capacities on a numerical basis for all relevant points including entry and exit points on a regular and rolling basis and in a user-friendly standardised manner.*
9. *The relevant points of a transmission system on which the information must be made public shall be approved by the competent authorities after consultation with network users.*
10. *Where a transmission system operator considers that it is not entitled for confidentiality reasons to make public all the data required, it shall seek the authorisation of the competent authorities to limit publication with respect to the point or points in question.*
11. *The competent authorities shall grant or refuse the authorization on a case by case basis, taking into account in particular the need to respect legitimate commercial confidentiality and the objective of creating a competitive internal gas market. If the authorisation is granted, available capacity shall be published without indicating the numerical data that would contravene confidentiality.*
12. *No such authorisation as referred to in this paragraph shall be granted where three or more network users have contracted capacity at the same point.*
13. *Transmission system operators shall always disclose the information required by this Regulation in a meaningful, quantifiably clear and easily accessible way and on a nondiscriminatory basis.*

26. Article 7 of Regulation (EC) No 1775/2005 entitled "Balancing rules and imbalance charges" reads:

1. *Balancing rules shall be designed in a fair, nondiscriminatory and transparent manner and shall be based on objective criteria. Balancing rules shall reflect genuine system needs taking into account the resources available to the transmission system operator.*
2. *In the case of non-market based balancing systems, tolerance levels shall be designed in a way that either reflects seasonality or results in a tolerance level higher than that resulting from seasonality, and that reflects the actual technical capabilities of the transmission system. Tolerance levels shall reflect genuine system needs taking into account the resources available to the transmission system operator.*
3. *Imbalance charges shall be cost-reflective to the extent possible, whilst providing appropriate incentives on network users to balance their input and offtake of gas. They shall avoid cross-subsidisation between network users and shall not hamper the entry of new market entrants.*  
*Any calculation methodology for imbalance charges as well as the final tariffs shall be made public by the competent authorities or the transmission system operator as appropriate.*
4. *Transmission system operators may impose penalty charges on network users whose input into and offtake from the transmission system is not in balance according to the balancing rules referred to in paragraph 1.*
5. *Penalty charges which exceed the actual balancing costs incurred, insofar as such costs correspond to those of an efficient and structurally comparable network operator and are*

*transparent, shall be taken into account when calculating tariffs in a way that does not reduce the interest in balancing and shall be approved by the competent authorities.*

6. *In order to enable network users to take timely corrective action, transmission system operators shall provide sufficient, well-timed and reliable on-line based information on the balancing status of network users. The level of information provided shall reflect the level of information available to the transmission system operator. Where they exist, charges for the provision of such information shall be approved by the competent authorities and shall be made public by the transmission system operator.*
7. *Member States shall ensure that transmission system operators endeavour to harmonise balancing regimes and streamline structures and levels of balancing charges in order to facilitate gas trade.*

27. Article 8 of Regulation (EC) No 1775/2005 entitled "Trading of capacity rights" reads:

*Each transmission system operator shall take reasonable steps to allow capacity rights to be freely tradable and to facilitate such trade. Each such operator shall develop harmonized transportation contracts and procedures on the primary market to facilitate secondary trade of capacity and recognize the transfer of primary capacity rights where notified by network users. The harmonised transportation contracts and procedures shall be notified to the regulatory authorities.*

28. Article 10(1) of Regulation (EC) No 1775/2005 entitled "Regulatory authorities" reads:

1. *When carrying out their responsibilities under this Regulation, the regulatory authorities of the Member States established under Article 25 of Directive 2003/55/EC shall ensure compliance with this Regulation and the Guidelines adopted pursuant to Article 9 of this Regulation.*

29. Article 13(1) of Regulation (EC) No 1775/2005 entitled "Penalties" reads:

1. *The Member States shall lay down the rules on penalties applicable to infringements of the provisions of this Regulation and shall take all measures necessary to ensure that they are implemented. The penalties provided for must be effective, proportionate and dissuasive. [...].*

30. Article 2(2) of the Dispute Settlement Procedures reads:

*Failure by a Party to comply with Energy Community law may consist of any measure by the public authorities of the Party (central, regional or local as well as legislative, administrative or judicative), including undertakings within the meaning of Article 19 of the Treaty, to which the measure is attributable.*

### **III. Preliminary Procedure**

31. According to Article 90 of the Treaty, the Secretariat may bring a failure by a Party to comply with Energy Community law to the attention of the Ministerial Council. Pursuant to Article 10 of the Procedural Act No 2008/01/MC-EnC of the Ministerial Council of the Energy Community of 27 June 2008 on the Rules of Procedure for Dispute Settlement under the Treaty ("Dispute Settlement Procedures"), the Secretariat shall carry out a preliminary procedure before submitting a reasoned request to the Ministerial Council.
32. The Secretariat, during missions to Bosnia and Herzegovina and in its reports, has repeatedly pointed to the lack of gas legislation on State level and its negative impacts on compliance with the *acquis communautaire*, the governance of the gas sector in Bosnia and Herzegovina and the wider region, and the necessary investment in gas infrastructure.



33. The Director General of DG TREN at the European Commission already in 2007 expressed his serious concern about the lack of a comprehensive legal and regulatory framework for the gas sector and about the lack of compliance with the Treaty.<sup>11</sup> A meeting on the issue was organized by the European Commission on 30 March 2009 and followed up by a letter of Deputy Director *Barbaso* to the three Ministers in charge of energy, deploring the lack of compliance and inviting the stakeholders to reach a solution.<sup>12</sup>
34. In line with its monitoring role under Article 67 of the Treaty, the Secretariat also assessed compliance of the existing legislation governing the gas sector in Bosnia and Herzegovina, i.e. on entities' level, with the *acquis communautaire* under Title II of the Treaty.
35. Following up on this assessment, and in the absence of any progress made by the Working Group established by MOFTER, the Secretariat sent an Opening Letter under Article 12 of the Dispute Settlement Procedures to Bosnia and Herzegovina on 7 October 2011.<sup>13</sup> In the Opening Letter, the Secretariat preliminarily concluded that by failing to adopt, within the prescribed time limit, the national measures necessary to implement Articles 9(1) and (2), 15, 17, 18(1), 22, 23 read together with item 2(i) of Annex I of the Treaty, 25(1) and 25(2) of Directive 2003/55/EC, as well as Articles 3, 4, to 8, 10 and 13 of Regulation (EC) No. 1775/2005, Bosnia and Herzegovina has failed to fulfil its obligations under those Articles.
36. In a reply to the Opening Letter dated 22 December 2011,<sup>14</sup> MOFTER acknowledged that the development of gas legislation in the country is in a "deadlock". On substance, the reply summarizes the positions of the two entities on the future perspective, but does essentially not contest the depiction of the domestic legal and factual situation, nor the compliance assessment related to the individual instances identified by the Secretariat in the Opening Letter. On the contrary, the reply acknowledges that the current situation is characterized by a "lack of compliance".
37. By a letter dated 28 March 2012, the Secretariat notified the Minister of Foreign Trade and Economic Relations that it considers the reply not sufficient "to dispel the concerns raised by the Opening Letter".<sup>15</sup>
38. In the further discussions between representatives of MOFTER and the Secretariat, the Secretariat offered to assist Bosnia and Herzegovina in drafting a State-level law on gas, which hitherto does not exist but would, in the Secretariat's view expressed in the Opening Letter, be "the most effective way to reach a state of compliance with the *acquis communautaire*". MOFTER, in its reply, conditioned the acceptance of that offer on a "broader compromise at the decision-maker level" to be reached. The Secretariat repeated its offer again in the letter to the Minister of 28 March 2012, in which it also proposed to have a meeting dedicated to the present case and possible ways forward. This proposal was not accepted.
39. Representatives of the Secretariat met with representatives of all institutions and companies in Bosnia and Herzegovina, led by the Prime Minister and the three Ministers in charge of energy

<sup>11</sup> Letter by the Director General to the Minister for Foreign Trade and Economic Relations dated 25 June 2007, Annex 13.

<sup>12</sup> Letter by the Deputy Director General to the three Minister in Bosnia and Herzegovina dated 11 May 2009, Annex 14.

<sup>13</sup> Annex 1.

<sup>14</sup> Annex 2.

<sup>15</sup> Annex 3.

on State and entity level, on 14 June 2012 at Mount Jahorina. The legislative situation in the gas sector and the present case were one of four topics addressed in that meeting. On this topic, the three Ministers in charge of energy requested a few additional months to agree internally on the approach to be taken towards (potential) State legislation. The Secretariat has subsequently not been informed about the outcome of these discussions, nor been invited to participate in the drafting of new legislation.

40. In its Implementation Report of 1 September 2012, the Secretariat reiterated that *"Bosnia and Herzegovina has still failed to implement any of the three gas legislative acts required by the Treaty with a delay of 5, 3.5 and 2.5 years respectively"* and concluded that *"[In implementing the gas acquis], Bosnia and Herzegovina is lagging behind all other Contracting Parties ... Bearing in mind that the deadline for implementation of the Third Package is approaching, this gap will become even wider if nothing changes. There are no signs of any improvement."*
41. Under these circumstances, the Secretariat submitted a Reasoned Opinion to Bosnia and Herzegovina under Article 13 of the Dispute Settlement Procedures on 24 January 2013.<sup>16</sup> Bosnia and Herzegovina was given a time-limit of two months, i.e. by 24 March 2013, to rectify the breaches identified in the Reasoned Opinion, or at least make clear and unequivocal commitments in that respect.
42. In the reply by Bosnia and Herzegovina, sent by MOFTER on 3 April 2013 by a letter dated 29 March 2013,<sup>17</sup> the Ministry again did not dispute the facts established by the Secretariat nor contest the legal conclusions related to compliance, but welcomed the Secretariat's involvement triggering a *"first step to a successful implementation of obligations arising from the Treaty establishing the Energy Community"*.<sup>18</sup> While MOFTER claimed that the amendments to the Law on Gas in Republika Srpska and the draft Law on Gas in the Federation of Bosnia and Herzegovina removed some of the compliance concerns raised in the Reasoned Opinion, it was admitted that *"due to different visions of how the internal gas market in BiH should look like, some issues remain unresolved."*<sup>19</sup>
43. Having examined MOFTER's reply, as well as the submissions by the two entities, the Secretariat considers indeed that several issues of non-compliance identified in the Reasoned Opinion can be dropped from this case. These developments are due to the entry into force of the amendments to the Law on Gas in Republika Srpska. Consequently, the Secretariat decided to discontinue the case insofar as violations by the legislation and practice of this entity against the rules pertaining to combined operators (Article 15 of Directive 2003/55/EC), third party access exemptions for new infrastructure (Article 22 of Directive 2003/55/EC) and market opening and reciprocity (Article 23 of Directive 2003/55/EC) are concerned. Other identified cases of non-compliance by the legislation and practice in Republika Srpska were, however, not sufficiently remedied by the amended Law.
44. For the Federation of Bosnia and Herzegovina, the Ministry of Energy, Mining and Industry concludes in its comments on the Reasoned Opinion that all breaches of Energy Community law in this entity were rectified by the recently developed draft Law on Gas.<sup>20</sup>

<sup>16</sup> Annex 4.

<sup>17</sup> Annex 5.

<sup>18</sup> Reply to Reasoned Opinion, at page 1.

<sup>19</sup> Reply to Reasoned Opinion, at page 4.

<sup>20</sup> At page 29 of its comments on the Reasoned Opinion, Annex 5b.

45. As a matter of principle, this point of view is to be rejected. With all respect for the public authority's efforts to improve compliance of the domestic legislation with the Treaty, obligations following therefrom can only be considered *transposed* once a binding piece of legislation has actually entered into force, and replaced the largely non-compliant Decree. The Secretariat recalls that according to well-established case law of the Court of Justice of the European Union, the provisions of directives must be implemented with unquestionable binding force.<sup>21</sup> The conclusions drawn from the legal assessment of the situation in the Federation of Bosnia and Herzegovina can thus only be reconsidered once a compliant Law has entered into force. Moreover, full implementation of the Law and the relevant elements of Directive 2003/55/EC forming the subject-matter of this case – such as the establishment of an effective and independent regulatory authority, unbundling, tariffication, market opening etc. – can only be considered fully *implemented* once they are applied in reality. At this point in time, the draft Law seems to matter mainly as an element for the negotiations with Republika Srpska on the future governance for the gas sector at State level.
46. The Secretariat is willing to continue its assistance to Bosnia and Herzegovina and its entities in implementing the Treaty's *acquis* on gas. As the history of the present case shows, however, it has proved impossible for the authorities to agree on an approach capable of achieving effective implementation. Uncounted missions and meetings at the highest levels, promises made and years of expert working groups discussing the issues raised by the present case have not resulted in concrete measures rectifying the various breaches of Energy Community law, almost seven years after the entry into force of the Treaty. Investments, the opening of markets and infrastructure developments will suffer from this lack of an appropriate legal framework. Concrete results are urgently needed. For this reason, the Secretariat decided to refer this case to the Ministerial Council for its Decision.

## IV. Legal Assessment

### 1. Introduction

47. The subject-matter of case ECS-8/11 consists in several instances of non-compliance by the existing legislation in Bosnia and Herzegovina with the Energy Community *acquis communautaire* related to natural gas, as identified in the Opening Letter and the Reasoned Opinion.
48. In its legal analysis, the Secretariat is aware of and respects the constitutional structure of Bosnia and Herzegovina and the division into two entities. At the same time the State of Bosnia and Herzegovina as a Contracting Party to the Treaty, not its entities, assumes full responsibility for compliance with the *acquis*. Under Article 2(2) of the Dispute Settlement Procedures, this includes „any measure by the public authorities of the Party (central, regional or local [...]) [...]“. Any failure of the (legislative, administrative, regulatory or judicative) authorities Republika Srpska and/or the Federation of Bosnia and Herzegovina to comply with the *acquis* is thus attributable to the State of Bosnia and Herzegovina as a Party to the Treaty.<sup>22</sup> Under Article 2(2)

<sup>21</sup> Case C-296/01 *Commission v France* [2003] ECR I-13909, paragraph 54.

<sup>22</sup> See also Cases 227-230/85 *Commission v Belgium* [1988] ECR I-1, paragraphs 9 and 10. The Court of Justice held that 'the State is free to delegate powers to its domestic authorities as it considers fit and to implement directives by means of measures adopted by regional or local authorities,' but that 'division of powers does not however release it from the obligation to ensure that the provisions of the directive are properly implemented in national law.' According to established case law, a State

of the Dispute Settlement Procedures, the same holds true for any measure taken or not taken by public undertakings. This includes all gas network operators in Bosnia and Herzegovina.

49. In the absence of State legislation governing the gas sector, the legal framework in the entities will have to make good for the lack of state-level legislation on gas by being fully compliant, harmonized and congruent, both on the levels of legislation and its application in practice. Consequently, the following assessment focuses on compliance of the entities' legislation with the requirements of Directive 2003/55/EC and Regulation 1775/2005. As will be set out in more detail in the following, the legislation existing in the entities falls short of fulfilling these requirements on several points.
50. The Secretariat takes note of the explanation by the Federation of Bosnia and Herzegovina related to the temporary character of its Decree in the expectation of a State-level law. If this is meant to justify its various deficiencies in compliance with the Energy Community *acquis*, however,<sup>23</sup> this argument is to be rejected.

## 2. Assessment of the entities' legislation

### (1) Regulatory Authorities

51. Article 25(1) of Directive 2003/55/EC, as incorporated into the Energy Community Treaty, requires Contracting Parties including Bosnia and Herzegovina to „*designate one or more competent bodies with the function of regulatory authorities*“. As explained by Recital 13 of the Directive, the „*existence of effective regulation, carried out by one or more national regulatory authorities, is an important factor in guaranteeing non-discriminatory access to the network*.“ To carry out their tasks, national regulatory authorities need to be vested with a minimum set of competences as defined in Article 25(1)(a)-(h). This includes the fixing or approval of network tariffs, or the methodology underlying the calculation of the tariffs (Article 25(2) of Directive 2003/55/EC). In terms of organization and structure, Article 25(1) of Directive 2003/55/EC requires the regulatory authorities to be established „*wholly independent of the interests of the gas industry*“. Article 25(7) further stipulates that Contracting Parties „*shall take measures to ensure that regulatory authorities are able to carry out their duties ... in an efficient and expeditious manner*“.
52. It is undisputed that in the absence of State-level gas legislation, and unlike in the electricity sector,<sup>24</sup> Bosnia and Herzegovina has not established or designated a body functioning as national regulatory authority responsible for the gas market and infrastructure on the entire territory of that Party, i.e. at State level.
53. In **Republika Srpska**, Articles 4-7 of the Law on Gas, as well as Articles 15-26 of the Law on Energy of 2009, task the Regulatory Commission for Energy (RERS) with regulating the gas sector in that entity.<sup>25</sup> The 2013 amendments to the Law on Gas further aligned this entity's

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'may not plead provisions, practices or circumstances existing in its internal legal system in order to justify a failure to comply with its obligations under Community law.'

<sup>23</sup> Comments attached to the reply to the Opening Letter, Annex 2b, at page 8.

<sup>24</sup> Where a State Electricity Regulatory Commission (SERC) was established in 2002 by Article 4 of the Law on Transmission of Electric Power, Regulator and System Operator of Bosnia and Herzegovina.

<sup>25</sup> The articles from the "Rules of operation of transport network" (OG 64/10) and from the "Rules of operation of distribution network" (OG 110/09), as quoted in Republika Srpska's contribution to the Ministry's reply (Annex 2a) refer to the tasks of the regulatory authority already specified within the Gas Law and introduce a possibility for appeals against the request for



legislation with Directive 2003/55/EC.<sup>26</sup> Its compliance with Article 25 of that Directive does not form part of the subject-matter of the present case, to the extent not covered by any of the specific instances of non-compliance as presented further below in this Reasoned Request. However, RERS only has jurisdiction for Republika Srpska. In the absence of a regulatory authority at State-level, compliance with Article 25 of Directive 2003/55/EC would require the existence of an effective regulatory authority in the other entity as well.

54. In the **Federation of Bosnia and Herzegovina**, no regulatory authority has been designated. This is not disputed. The Decree on the Organization and Regulation of the Gas Sector foresees an „Agency“ as the „*independent regulator of energy activities*“ (as defined in Article 4). According to Article 57(1) of the Decree, the „*Agency is an independent regulator of energy activities which will be established by appropriate regulations of FBiH/BiH*“. This Agency has never been set up.
55. Instead, Article 57(2) provides: „*Until the Agency is established, the function of the regulator will be performed by the Ministry*“. The Ministry of Energy, Mining and Industry, however, cannot be considered a regulatory authority as required by Article 25(1) of Directive 2003/55/EC. It does not fulfill the requirement of independence, given public ownership in the transmission system operator *BH Gas*, and at least one distribution system operator, *Sarajevogas*. *BH Gas*, for instance, was designated by the Government of the Federation of Bosnia and Herzegovina, and the Ministry of Energy, Mining and Industry appoints the members of the Management Board, which in turn appoints the CEO of the company, with the Government's prior consent.<sup>27</sup> In this situation, the Ministry of Energy, Mining and Industry cannot be considered independent.
56. Directive 2003/55/EC clearly requires the specific tasks listed in Article 25 of Directive 2003/55/EC – of which the responsibility “*for fixing or approving prior to their entry into force, at least the methodologies used to calculate or establish the terms and conditions for*” connection and access to network as well as the provision of balancing services in Article 25(2) are of particular importance<sup>28</sup> – to be carried out by a body fulfilling the criteria of Article 25(1) of Directive 2003/55/EC. By not establishing such a body, the Decree is in violation of the latter provision.
57. Moreover, the specific tasks listed in Article 25 of Directive 2003/55/EC have not even been assigned to the Ministry. Article 55(1) of the Decree only stipulates that „*[s]upervision over implementation of this Decree shall be performed by the Ministry*“, a responsibility which is of a general administrative nature including control of legality of acts issued by legal persons (Article 55(2) of the Decree). Hence, aside the absence of a proper regulatory authority as required by the Directive, the tasks expected to be performed by such a body are currently not carried out in the Federation of Bosnia and Herzegovina to the extent required by the Directive and Regulation 1775/2005.
58. The draft Law on Gas tasks the Regulatory Commission for Electricity (in future: Energy) in the Federation of Bosnia and Herzegovina with carrying out the regulatory functions for the gas

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access/connection to respective grid, Articles 4 d). The items of the transmission/distribution licences also referred to by Republika Srpska reiterate the obligations of the companies to comply with the regulatory authority's acts, specify the reporting requirements etc.

<sup>26</sup> Namely Articles 4 and 5 of the Law on Amendments to the Law on Gas.

<sup>27</sup> According to Articles 5,6,7 and 12 of the Law on Public Enterprises in the Federation of Bosnia and Herzegovina, Official Gazette FBiH 8/05.

<sup>28</sup> Case C-274/08 *Commission v Sweden* [2009] ECR I-10674, paragraph 37; Case C-474/08 *Commission v Belgium* [2009] ECR I-175, paragraphs 27 ff.

sector as well.<sup>29</sup> However, even if the draft were to be adopted, the competences of the future regulatory authority explicitly exclude “*regulation of natural gas transport*”,<sup>30</sup> *international trade*,<sup>31</sup> *management, balancing and ancillary services*”.<sup>32</sup> Article 47(2) of the draft tasks the future entity regulatory authority only with “*regulating the market of distribution and storage of gas and management of LNG systems in the Federation of Bosnia and Herzegovina*”. As follows from the more specific provisions of the draft, this exclusion will extend *inter alia* to third-party access, the setting of transmission tariffs as well as to the establishment of network codes and the issues regulated by them. Furthermore, Article 48(3)(b) of the draft also excludes transmission from the regulatory authority’s competences related to the unbundling of accounts.<sup>33</sup> Transmission system operation is obviously a key focus of the tasks conferred on regulatory authorities by Article 25 of Directive 2003/55/EC. If adopted, the draft Law on Gas would fail to transpose and implement any of its individual paragraphs.

59. In the absence of even the most basic of agreements between the two entities on the possibility for and the scope of a future State-level gas law, it is currently very unclear if and when and with which competences a State level regulatory authority would be expected. Under these circumstances, exempting transmission from the scope of activities of a future regulatory authority will leave a significant lacuna in the tasks expected from a regulatory authority under Article 25 of Directive 2003/55/EC. The draft can thus not be considered sufficient to establish a regulatory authority with the scope of powers required by Article 25 of Directive 2003/55/EC in the Federation of Bosnia and Herzegovina.
60. In conclusion, the Secretariat submits that **Bosnia and Herzegovina**, the Contracting Party to the Energy Community, in its entirety has not established or designated one or more competent bodies with the function of regulatory authorities which would cover – alone or complementary – the entire gas market in Bosnia and Herzegovina.<sup>34</sup>
61. Considering its wording, Article 25(1) of Directive 2003/55/EC is not, in principle, opposed to a plurality of regulatory authorities within one Contracting Party. This is different from Directive 2009/73/EC (to be implemented by Bosnia and Herzegovina by 1 January 2015) which requires that “*each Contracting Party shall designate a single national regulatory authority at national level*”.<sup>35</sup> Under the currently applicable Directive 2003/55/EC, the Secretariat thus would not challenge, the (potential) co-existence of two jurisdictions<sup>36</sup> with two separate regulatory authorities complementing each other and covering the entire territory of the Contracting Party in a manner compliant with the *acquis*. In this respect, Directive 2003/55/EC grants Contracting Parties a certain degree of institutional autonomy within the margins of its Article 25.

<sup>29</sup> Article 47 of the draft Law on Gas.

<sup>30</sup> While transport of gas is not specifically defined in the draft Law on Gas, the definition of “*transmission*” in Article 3(50) (“*the transport of natural gas through a high pressure pipeline with a view to its delivery to customers...*”) shows that the exclusion of transport from the scope of the Law excludes also transmission, and thus a key regulated activity in the concept of European energy law and in Article 25 of Directive 2003/55/EC.

<sup>31</sup> Defined as gas purchases or sales with/from a non-domestic seller/buyer for resale purposes, see Article 3(24) of the Draft Law on Gas.

<sup>32</sup> Article 1(2) of the Draft Law on Gas; see also MOFTER’s reply to the Reasoned Opinion at page 3.

<sup>33</sup> As required by Article 25(1)(e) of Directive 2003/55/EC.

<sup>34</sup> As defined by Article 1 of Directive 2003/55/EC.

<sup>35</sup> Article 39(1) of Directive 2009/73/EC. Article 39(2) allows for the continuance of regulatory authorities on entity level if a State level authority exists.

<sup>36</sup> Jurisdiction over the Brcko District does not form part of the present case.

62. However, it follows from case-law of the Court of Justice of the European Union that Contracting Parties, whilst retaining discretion as to the choice of methods in transposing a Directive,<sup>37</sup> are under an obligation to ensure that the Directive is fully effective in accordance with the objectives it pursues. Furthermore, Article 6 of the Energy Community Treaty requires Bosnia and Herzegovina to adopt all the measures necessary to ensure that the Directive is fully effective in accordance with the objective which it pursues.
63. Hence, the institutional autonomy enjoyed by Contracting Parties with regard to organizing and structuring their regulatory authorities may be exercised only in accordance with the objectives and obligations laid down in that Directive.<sup>38</sup> It is to be recalled that the existence of regulatory authorities fulfilling certain criteria as to their independence and effectively executing the tasks listed in Directive 2003/55/EC is a key precondition for arriving at a fully operational and competitive internal gas market, and thus constitutes a key concern of the Directive.
64. It follows from the above that, whilst it enjoys discretion in how to design and structure its regulatory authorities in accordance with its internal constitution, Bosnia and Herzegovina as a Contracting Party to the Energy Community is under an obligation under Article 25 of Directive 2003/55/EC to ensure that the functions assigned to regulatory authorities with respect to the natural gas sector are effectively and independently carried out on the entire territory of Bosnia and Herzegovina.
65. In the absence of a national regulatory authority with jurisdiction over the entire state of Bosnia and Herzegovina, and of a regulatory authority in the Federation of Bosnia and Herzegovina, effective, efficient and independent regulation is not carried out on the entire territory and for all market operators in Bosnia and Herzegovina. This holds true even if one were to assume that the situation in Republika Srpska fully complies with Article 25 of Directive 2003/55/EC,<sup>39</sup> as long as RERS is the only regulatory authority with competences in the gas sector in Bosnia and Herzegovina, and its jurisdiction is limited to the territory of one entity. Bosnia and Herzegovina, to which actions and non-actions of its entities are imputable, thus fails to adopt the measures necessary to implement Article 25 of Directive 2003/55/EC.

## *(2) Lack of legal unbundling*

66. According to Article 9(1) of Directive 2003/55/EC, the transmission system needs to be independent in terms of its legal form where it is part of a vertically integrated undertaking (legal unbundling).
67. In its Reasoned Opinion, the Secretariat concluded that the Law on Energy of **Republika Srpska** “does not provide for legal unbundling of the transmission system operator established in that entity, Gas Promet. The license ... does not impose legal unbundling”. In the 2013 amendments to the Law on Gas,<sup>40</sup> an obligation to “perform legal ... unbundling of natural gas transmission system operation from supply” was now introduced in Article 24 of the Law on Gas. Despite this

<sup>37</sup> Or more precisely: the Decision of the Ministerial Council incorporating this Directive into the Energy Community *acquis communautaire*.

<sup>38</sup> Case C-82/07 *Comision del Mercado des Telecomunicaciones* [2008] ECR I-1265, paragraphs 24-27; Case C-389/09, *Base* [2010] ECR I-9073, paragraphs 24-26.

<sup>39</sup> As claimed by Republika Srpska in attachment 1 to MOFTER’s reply to the Opening Letter and in its comments on the Reasoned Opinion at page 4.

<sup>40</sup> Article 14 of the Law on Amendments to the Law on Gas.



progress in transposition, however, the Secretariat considers that legal unbundling is still to be fully implemented in practice in Republika Srpska.

68. In reality, *Gas Promet* continues to hold licenses for transmission system operation as well as trade and supply.<sup>41</sup> It does currently not exercise supply activities. However, as long as the supply license is not withdrawn, the company cannot be considered fully legally unbundled. Legal unbundling is defined in Article 9(1) of Directive 2003/55/EC as being “*independent ... in terms of its legal form ... from other activities not relating to transmission*”. If a gas undertaking wishes to engage in other activities than transmission, it needs to establish a separate legal entity for this. A license for supply grants the (transmission) undertaking concerned the right to take up this economic activity at its discretion, without further preconditions to be fulfilled. As license holder, *Gas Promet* remains thus entitled to supply gas at any time without having established a separate legal entity for that activity, as would be required under the concept of legal unbundling. That the company currently does not buy and sell gas does not suffice, in the Secretariat’s view, to establish its legally unbundling. Rather, this would require *Gas Promet* to either return the supply license or to transfer it to an independent legal entity. At the time of submitting this Reasoned Request, this has not happened.
69. Furthermore, it is recalled that *Sarajevo-gas a.d. Istocno Sarajevo* holds a license as a “*transporter of natural gas*”.<sup>42</sup> According to Article 3d) of the Law on Gas, as amended, a “*transporter is a legal or natural person who carries out the function of transmission and is responsible for operating, ensuring the maintenance and, in cooperation with transmission system operator, developing the transmission system in a given area*”. The concept of a “transporter” does not feature among the definitions of Directive 2003/55/EC or Regulation 1775/2005. Its definition under the law of Republika Srpska corresponds almost *verbatim* to the definition of a transmission system operator in Article 2 No 4 of Directive 2003/55/EC. In practical terms it functions as a kind of co-operator of the licensed transmission system operator, *Gas Promet*. From the perspective of Directive 2003/55/EC, *Sarajevo-gas a.d. Istocno Sarajevo* is to be considered a transmission system operator. Republika Srpska’s non-compliance with the requirement of legal unbundling in relation to this company follows from the non-disputed fact that it does not only hold licenses for transportation *and* supply,<sup>43</sup> but also carries out both functions in practice.
70. In any event, it is evident from Republika Srpska’s comments on the Reasoned Opinion<sup>44</sup> that the introduction of legal unbundling in the Law on Gas will have to be “*followed by secondary legislation changes and thereby further action to rectify the identified cases of non-compliance*.” At the point of submitting the present Reasoned Request, such secondary legislation has not been enacted. Republika Srpska thus effectively concedes that the situation in Republika Srpska, and transposition in primary law alone, still fails to fully implement Article 9(1) of Directive 2003/55/EC.

<sup>41</sup> *Gas Promet* Pale was licensed as a trader and a supplier in 2010. The license is valid for five years and has not been revoked since.

<sup>42</sup> See the Annual Report for 2011 of the regulatory authority and the licensee conditions at [http://www.reers.ba/sites/default/files/Uslovi\\_transport\\_Sarajevo\\_gas.pdf](http://www.reers.ba/sites/default/files/Uslovi_transport_Sarajevo_gas.pdf). Evidently, Republika Srpska’s comments on the Reasoned Opinion, at page 15, are inadequately translated.

<sup>43</sup> Altogether, the company holds four licenses, one for trade and supply (on the open market), one for supply to tariff customers (on the captive market), one for transport, and one for distribution and distribution system operation.

<sup>44</sup> At page 10 of its comments on the Reasoned Opinion.



71. In the **Federation of Bosnia and Herzegovina**, Article 41(1) of the Decree on the Organization and Regulation of the Gas Sector provides that „[a] *transport system operator that belongs to a vertically integrated undertaking must be independent from other activities unrelated to transport in the sense of legal status, organization and decision-making*“, thus reproducing Article 9(1) of Directive 2003/55/EC.
72. Contrary to the formal requirement of legal unbundling in Article 41(1) of the Decree, however, the Decree itself stipulates that supply and transport/transmission of natural gas are carried out by one and the same company, *BH Gas d.o.o in Sarajevo*. In Article 10 of the Decree, *BH Gas* is designated as the transport/transmission system operator of the Federation. At the same time, Article 59(1) in conjunction with Article 30 of the Decree designates *BH Gas* as one of two companies performing supply of tariff customers with gas. According to Article 31(2) of the Decree, the same company shall also „*regulate the price for supply of tariff customers [...]*“. It is not disputed that *BH Gas* does indeed operate the transmission system in the Federation of Bosnia and Herzegovina, and, at the same time, acts as wholesale supplier to customers on the entire territory of Bosnia and Herzegovina. This involvement in supply evidently thwarts the independence „*in terms of its legal form*“ of the transmission system operator of other activities performed by vertically integrated undertakings not relating to transmission, as required by Article 9(1) of Directive 2003/55/EC. Article 59(3) of the Decree openly acknowledges this case of non-compliance as an „*exception*“ to Article 41(1). The exception formally expired in November 2012. This period was prolonged in line with a loan agreement by the company with EBRD for the ongoing project “construction of the high pressure gas pipeline Zenica – Travnik”. Legal unbundling is one of the “*regulatory requirements*”. The deadline envisaged by the agreement is 31 December 2014.<sup>45</sup> This is not compliant with the deadlines established by the Treaty, namely 1 July 2006.
73. In any event, all other provisions of the Decree quoted in this paragraph and frustrating legal unbundling remain valid regardless of any contractual agreements. The Federation of Bosnia and Herzegovina has thus not implemented Article 9(1) of Directive 2003/55/EC.
74. The draft Law on Gas would reproduce the requirement for legal unbundling, as already included in Article 41(1) of the Decree on the Organization and Regulation of the Gas Sector, in Article 19(1). However, not only does the draft – in accordance with the general exclusion of gas transport from the competences of the regulatory authority to be established under Article 1(2) of the draft – not provide for any enforcement, it does also not set any penalties for non-compliance with the unbundling provisions. Furthermore, the obligation on *BH Gas* to legally unbundle is to be complied with only by 31 December 2014,<sup>46</sup> hence in line with the agreement made with EBRD, 7½ years since this obligation became binding under Energy Community law, and coinciding with the deadline for implementation of Directive 2009/73/EC in Bosnia and Herzegovina. In that respect, the draft Law even falls behind the existing situation. As the relevant provisions concern an existing company in the Federation, its speculation that an Independent System Operator will be established at the State level<sup>47</sup> is without relevance for the present case.

<sup>45</sup> According to a presentation given by the CEO of *BH Gas* at the meeting with the Secretariat at Mount Jahorina, Annex 10, at page 8.

<sup>46</sup> Article 95(6) of the draft Law on Gas.

<sup>47</sup> See e.g. Articles 37(2)(m) and (p), 39(3) and (5) of the draft Law. Presumably, this model is copied on the solution found in the electricity sector.

75. In any event, at the moment of submission of the present Reasoned Request, *BH Gas* as the entity's transmission system operator is not unbundled. Under these circumstances, Article 9(1) of Directive 2003/55/EC cannot be considered implemented by the Federation of Bosnia and Herzegovina. Other than the development of a "pre-draft", the Federation of Bosnia and Herzegovina in its comments on the Reasoned Opinion did not provide any information on measures taken to legally unbundle *BH Gas*.<sup>48</sup> It is undisputed that *BH Gas* is and remains a legally bundled company.

76. Consequently, the Secretariat submits that by not implementing the requirement of legal unbundling in either entity, **Bosnia and Herzegovina**, to which actions and non-actions of its entities and public companies are imputable, fails to comply with Article 9(1) of Directive 2003/55/EC.

*(3) Lack of functional unbundling*

77. According to Article 9(1) of Directive 2003/55/EC, Contracting Parties also need to ensure that transmission system operators belonging to a vertically integrated undertaking are independent in terms of their organisation and decision-making from the other activities not relating to transmission (functional unbundling). Article 9(2) of Directive 2003/55/EC sets a number of minimum criteria aimed at ensuring the independence of the transmission system operator.

78. The 2013 amendments to the Law on Gas in **Republika Srpska**, by modifying Article 24, now transpose the requirement of functional unbundling, including also the minimum criteria listed in paragraphs (2)(a)–(d) of Article 9 of Directive 2003/55/EC. While Republika Srpska correctly pointed to this improvement,<sup>49</sup> it did not address the Secretariat's statement in the Reasoned Opinion that functional unbundling is not complied with in practice by *Gas Promet*, the transmission system operator under its jurisdiction.

79. Whereas the license requirements also oblige the license holder to functionally unbundle the transmission activity from the other activities it performs, this requirement is not subject to any reporting or monitoring obligations, nor do sanctions apply if this requirement is not complied with, as is indeed the case with both relevant companies in Republika Srpska.

80. Both *Gas Promet* and *Sarajevo-gas a.d. Istocno Sarajevo* are joint stock companies and governed by a Shareholders Assembly as the superior body of governance. The Shareholders Assembly appoints the Management Board. The Management Board, in turn, appoints the Board of Directors.

81. In *Gas Promet*, all activities related to gas transmission system operation and transportation of natural gas, natural gas trade and supply are performed within one unified organizational and management structure. The company conducts its business activities as a fully integrated undertaking. The management structure is centralized, with the responsibility of a CEO to whom all subdivisions are accountable. While the company's transmission activities are separated on the level of functional sectors, no safeguards measures have been implemented to ensure the fulfillment of the requirements in Article 9(2) of Directive 2003/55/EC.

<sup>48</sup> In the Federation of Bosnia and Herzegovina's comments on the Opening Letter at page 9, it was still claimed that activities on legal unbundling had started in *BH Gas*, without, however, specifying which kind of activities this would refer to.

<sup>49</sup> At pages 10/11 of its comments on the Reasoned Opinion.



The organization chart of *Gas Promet Pale*.

82. Similarly, for *Sarajevo-gas a.d. Istочно Sarajevo*, all activities related to natural gas transport, trade, supply and distribution and distribution system operation of natural gas are performed under one operational and management structure. The departments are divided along the categories of transport, distribution, economic and financial activities and activities of legal and administrative affairs.
83. In both companies, the managers of the transmission sectors are at the same time members of the Board of Directors and thus participate in the company structures for the supply activities. No measures have been taken that these persons act independently from each other. Moreover, the transmission system operators or “transporters” have no effective decision making rights independent from the integrated utility with regard to the network assets. Compliance programmes are not in place in either company. The situation in Republika Srpska is thus in violation of Article 9(2) of Directive 2003/55/EC.
84. Articles 41 to 44 of the Decree on the Organization and Regulation of the Gas Sector in the **Federation of Bosnia and Herzegovina** transpose the provisions of Articles 9 and 13 of Directive 2003/55/EC related to functional unbundling of system operators. The Decree however does not require a compliance programme to be established in line with Article 9(2)d of Directive 2003/55/EC. In that respect, it fails to transpose Article 9(2)(d) of that Directive.
85. The draft Law on Gas in its Article 19(2(d)) now includes also the requirement on the transmission system operator to develop a compliance programme, to submit it to the regulatory authority and to publish it on the website. At the same time, the regulatory authority will not regulate transmission as a matter of principle.<sup>50</sup> In this situation, the regulatory authority will either be outright prevented from monitoring any compliance programme, which would contravene the duty of effective implementation in Article 6 of the Treaty, or the Law would create a situation lacking clarity and consequently failing to provide legal certainty, thus failing to properly implement Directive 2003/55/EC under well-established case law.<sup>51</sup> Furthermore, the Secretariat notes that even if the draft Law were to be adopted anytime soon and an effectively monitored compliance programme were to be imposed on *BH Gas*, the company would still have six months

<sup>50</sup> See Articles 1(2) and 47(2) of the draft Law on Gas, and paragraph 58 above. As Article 48(3)(b) of the draft stipulates explicitly, the Regulatory Commission to be established will deal with “unbundling of ... management” only between generation, distribution and supply.

<sup>51</sup> Case C-296/01 *Commission v France* [2003] ECR I-13909, paragraph 54.

as from the entry into force of the Law on Gas to comply with the rules on functional unbundling.<sup>52</sup> As in the case of legal unbundling, there are no penalties foreseen for the non-compliance with these rules.

86. With regard to practical unbundling of *BH Gas*, the requirements in the loan agreement with EBRD mentioned above envisage functional unbundling only by 31 December 2013,<sup>53</sup> thus breaching the deadline set by the Treaty.
87. Currently, all the activities performed by the company, namely natural gas transmission system operation and transportation of natural gas, natural gas trade ("import") and supply are carried out within one unified organizational and management structure. The managing bodies of *BH Gas* are the Managing Board and the Managing Director. The Managing Board consists of five members appointed by the Ministry of Energy, Mining and Industry of the Federation of Bosnia and Herzegovina. The Managing Board appoints – subject to approval by the entity Government – the Managing Director and establishes the organization of the company. The company is structured into four departments according to the following organization chart:



88. The company's transmission activities are only separated on the level of functional sectors, i.e. below the company's CEO. The managers of the transmission and supply sectors are at the same time members of the Board of Directors. As in Republika Srpska, this entity's vertically integrated utility has taken no measures that these persons act independently from each other. Moreover, the transmission system operator has no effective decision making rights independent from the integrated utility with regard to the network assets. A compliance programme is not in place. The situation in the Federation of Bosnia and Herzegovina is thus in violation of Article 9(2) of Directive 2003/55/EC also from the point of view of implementation. In any event, even if *BH Gas* would at some point actually establish and apply a compliance programme, this cannot make good for the lack of proper transposition of Article 9(2) of Directive 2003/55/EC.
89. The Secretariat therefore submits that, by not transposing and/or implementing all requirements of Article 9(2) of Directive 2003/55/EC by the respective transmission system operators, **Bosnia and Herzegovina**, to which actions and non-actions of its entities and public companies are imputable, does not comply with Article 9(1) and (2) of Directive 2003/55/EC.

#### (4) Lack of account unbundling

<sup>52</sup> Article 95(4) of the draft Law on Gas.

<sup>53</sup> Annex 10, at page 8.



90. Article 17 of Directive 2003/55/EC requires Contracting Parties to ensure that natural gas undertakings unbundle their accounts in line with paragraphs 2 to 5 of that provision.
91. In **Republika Srpska**, the 2013 amendments introduced two new articles related to the unbundling of accounts by gas undertaking which adequately transpose Article 17 of Directive 2003/55/EC.<sup>54</sup> This is further supported by secondary legislation on general accounting.<sup>55</sup>
92. However, even though the Law on Gas in Article 36a(1) now calls for the publication of the unbundled and audited accounts, as required by Article 17(2) of Directive 2003/55/EC, the accounts of none of the natural gas undertakings licensed in Republika Srpska are currently audited or published. Hence, the situation in that entity still falls short of fully implementing Article 17(2) of Directive 2003/55/EC.
93. In the **Federation of Bosnia and Herzegovina**, Articles 48 to 50 of the Decree on the Organization and Regulation of the Gas Sector deal with the unbundling of accounts. They fail to transpose Article 17 of Directive 2003/55/EC insofar as they refer only to “*the applicable regulations*” with respect to the content of the accounts, and not the specific requirements set by Directive 78/660/EEC (or any national transposition of those) or those set by Article 17 Directive 2003/55/EC itself (i.e. the inclusion of separate balance sheets and profit & loss accounts).
94. Article 17(2) of the draft Law on Gas in the Federation of Bosnia and Herzegovina will slightly improve the transposition of Article 17 Directive 2003/55/EC once adopted. However, Article 48(3)(b) of the draft stipulates explicitly that the Regulatory Commission to be established will deal with “*unbundling of accounts*” only “*for the purpose of avoiding cross-subsidies between generation, distribution and supply*”, and not transmission. This is in line with the general exclusion of transmission from the scope of activities of the regulatory authority under the draft Law. As in the case of legal and functional unbundling, there are no penalties foreseen for the non-compliance with rules on account unbundling. Even if the draft Law on Gas were to be adopted, the company would still have six months as from the entry into force of the Law on Gas to comply with the rules on account unbundling.<sup>56</sup>
95. In any event, Article 59(3) of the Decree exempted the vertically integrated *BH Gas* from compliance with the obligations on accounting unbundling for a period of up to five years, i.e. until November 2012. Despite the expiry of this period, the accounts of *BH Gas* are not published at this point in time. As was explained in the Reasoned Opinion and not disputed by the Federation of Bosnia and Herzegovina in its comments, *BH Gas* submits its reports regularly, in an unbundled way, to the entity Ministry and to EBRD, thus complying with a requirement in the bilateral loan agreement (see paragraph 72 above). This, however, does not satisfy the requirements to publish the annual accounts as required by Article 17(2) of Directive 2003/55/EC, nor the general objective of transparency.
96. Consequently, it is submitted that Article 17 of Directive 2003/55/EC has not been fully implemented by **Bosnia and Herzegovina**, to which actions and non-actions of its entities and public companies are imputable.

#### (5) Third party access tariffs

<sup>54</sup> Article 19 of the Law on Amendments to the Law on Gas.

<sup>55</sup> See page 12 of Republika Srpska's comments on the Reasoned Opinion.

<sup>56</sup> Article 95(4) of the draft Law on Gas.

97. According to Article 18(1) of Directive 2003/55/EC, Contracting Parties have to ensure the implementation of a system of third party access to the transmission and distribution system based on published tariffs. The tariffs, or the methodologies underlying their calculation, shall be approved and published prior to their entry into force by the regulatory authority in accordance with Article 25(2) of Directive 2003/55/EC. Article 3 of Regulation 1775/2005 sets out the basic requirements for the methodology for calculating tariffs to be applied by transmission system operators.

98. In **Republika Srpska**, the importance of “transparent and published tariffs for access as and use of the transmission network” is acknowledged by the amended Law on Gas.<sup>57</sup> According to the Law, access and use of the transmission system to third parties is granted by the “natural gas transporter”, with the consent of the transmission system operator (i.e. Gas Promet).<sup>58</sup> Article 4(2)(c) of the amended Law on Gas vests the Regulatory Commission with the competence to develop a tariff system for the calculation of the price for access and use of the system for transport, distribution and storage of gas. Based on the methodology adopted by RERS, the tariffs are then to be determined by the transmission, distribution and storage operators respectively (Article 43(3) of the Law on Gas). The tariffs for access and use of the network and storage system are to be published in the Official Gazette upon approval by the Regulatory Commission (Article 43(4) of the Law on Gas).

99. Hence, the effectiveness of the system established by the Law depends on its implementation by both the respective operators and the Regulatory Commission. Article 60(2) requires the methodology and tariff system to be issued by the Regulatory Commission. A Tariff Methodology for Transmission, Distribution, Storage and Supply of Natural Gas was adopted by the Regulatory Commission in 2009.<sup>59</sup> However, so far only separate tariffs for distribution and prices for supply of natural gas have been approved by the Regulatory Commission.<sup>60</sup> While according to this Methodology, the costs of transmission are included in the end-user price of natural gas, separate tariffs for access to and usage of the transmission system in particular have not been formally adopted or published. This was confirmed by Republika Srpska both in the reply to the Opening Letter<sup>61</sup> and to the Reasoned Opinion.<sup>62</sup>

100. Where a genuine and separate transmission tariff is lacking, open and non-discriminatory access to the transmission system is all but impossible. The separation of the network into transmission and distribution, with operators to be designated for each of these segments separately and Articles 18 and 25(2) of Directive clearly separating access to the transmission and distribution systems and the respective access tariffs, is one of the fundamental principles underlying Directive 2003/55/EC. Article 25(2) in particular requires separate tariffs for transmission and distribution. Furthermore, the Court of Justice of the European Union has pointed out in a case concerning the electricity sector that “[t]he objective of the Directive can be achieved only by the establishment of precise tariffs or of elements of a methodology of tariff calculation of a level of precision such as to allow economic operators to estimate their cost of

<sup>57</sup> See e.g. Article 22(2) of the amended Law on Gas.

<sup>58</sup> Article 21(5)(c) of the amended Law on Gas.

<sup>59</sup> Rulebook on Tariff Methodology in the System of Transport, Distribution, Storage and Supply of Natural Gas, Official Gazette of Republika Srpska 9/09, Annex 12.

<sup>60</sup> Namely for the company *Sarajevo-gas a.d. Istocno Sarajevo*, on 30 December 2009, and amended in April and November 2011.

<sup>61</sup> Attachment 1 to the Ministry's reply at page 2.

<sup>62</sup> At page 15 of its comments on the Reasoned Opinion.

access to the transmission and distribution networks.”<sup>63</sup> The lack of separately adopted and published tariffs for the usage of transmission network and transmission services constitutes a breach of Articles 18(1) and 25(2) of Directive 2003/55/EC.

101. Similarly, Article 3(1) of Regulation 1775/2005 explicitly requires transmission tariffs to be adopted, which have to fulfill the specific requirements laid down in this provision. In order to be applied, these basic elements of tariffication need to be based on the specific conditions of the transmission network, which differ from distribution. The situation in Republika Srpska thus also violates Article 3(1) of Regulation 1775/2005.

102. In its comments on the Reasoned Opinion, Republika Srpska concedes that separate tariffs for access to and the use of the transmission system in line with the requirements of Directive 2003/55/EC and Regulation 1775/2005 are currently not applied.<sup>64</sup> That there are “ongoing activities on determination of tariffs for usage of certain parts of the transmission system in [Republika Srpska]”, that in “February 2013, tariff process for the issuance of approval for tariffs for usage of natural gas transmission system has been initiated on a section of transmission pipeline Karakaj-Zvornik”<sup>65</sup> and “that this year it is planned to carry out other activities to determine the price for usage of certain parts of transmission system in [Republika Srpska] and the costs of the transmission system operator is started” show that only in 2013, i.e. almost six years after the corresponding obligation took effect under the Treaty, the application of genuine access tariffs is being considered, and that they are still far from being applied on the networks in this entity of Bosnia and Herzegovina.

103. As a justification for the failure to apply transmission access tariffs, Republika Srpska submits that in order to determine the transmission tariffs, it would need to know the transmission tariffs in the Federation of Bosnia and Herzegovina, i.e. the tariffs applied by that entity’s transmission system operator, *BH Gas*. The overall gas price set by this company, however, includes elements for transit and transmission services as well as the purchase price for natural gas according to a structure/methodology which is not disclosed.<sup>66</sup>

104. It is true that the pipeline system on the territory of Republika Srpska has a specific topography. Passing from Serbia through Republika Srpska, it continues through the Federation of Bosnia and Herzegovina (with exit points in Sarajevo) and then rejoins Republika Srpska to end in Pale. This latter part in Republika Srpska, however, is not part of the transmission system but the distribution network. Whilst tariff setting on the distribution system in Pale indeed requires cooperation with *BH Gas* of the Federation of Bosnia and Herzegovina, the arguments brought forward by Republika Srpska cannot justify the failure of setting transmission tariffs on the transmission network in its own territory (i.e. up to the exit point at the border with the Federation of Bosnia and Herzegovina). Republika Srpska’s justification is thus to be rejected, as the costs of providing transmission services should be recognizable to transmission system companies on their own part(s) of networks and attributable to system users.

105. Even if Republika Srpska indeed were prevented to set independent transmission tariffs only due to non-disclosure by *BH Gas* of its price/tariff structure, this cannot be a valid defense under Energy Community law. In this respect, the Secretariat recalls the well-established case

<sup>63</sup> Case C-274/08 *Commission v Sweden* [2009] ECR I-10674, paragraph 40.

<sup>64</sup> Reply to the Reasoned Opinion at page 3, comments of Republika Srpska on the Reasoned Opinion at page 14.

<sup>65</sup> A spur line of 4.7km length.

<sup>66</sup> Page 15 of Republika Srpska’s comments on the Reasoned Opinion.



law by the Court of Justice of the European Union according to which a Contracting Party may not plead internal circumstances to justify a failure to comply with obligations and time-limits laid down by Energy Community law.<sup>67</sup>

106. In the **Federation of Bosnia and Herzegovina**, Article 22(1) of the Decree on the Organization and Regulation of the Gas Sector provides for third party access to the transmission, distribution and storage system. Article 22(3) tasks the regulatory authority to define access „*all in the sense of regulated or negotiated access*“. As far as access to the transmission and distribution networks is concerned, Directive 2003/55 and Regulation 1775/2005 clearly rule out the option of negotiated access, which existed within the European Community as a possibility only under the so-called First Package Directive 98/30/EC. To give the regulatory authority the possibility to opt for a concept of negotiated access violates Article 18(1) of Directive 2003/55/EC, which strictly requires Contracting Parties to impose regulated third party access.
107. The draft Law on Gas, in its Articles 37 and 40, does not make explicit reference anymore to the concept of negotiated access. Instead, regulated access “*based on the published methodology and tariff system issued by the Regulatory Commission*” is envisaged.<sup>68</sup> However, Article 40(4) of the draft clarifies that “[a]ccess to the transmission system is defined by the State level regulator that issues and publishes the methodology ...”. The same goes for the regime applicable to refusals of third-party access.<sup>69</sup> These aspects are thus exempted from the future scope of application of the draft Law on Gas. Even if adopted, the draft Law would factually exempt the transmission system operator *BH Gas* from tariff regulation. This lacuna is conceded by MOFTER in its reply to the Reasoned Opinion, whereby “*jurisdiction for regulating third party access to the transmission system is not subject to [the draft]*”, as it is left for the jurisdiction of a future state regulatory authority.<sup>70</sup>
108. A State-level regulatory authority does not exist. For the reasons explained at paragraphs 8 and 9 above, this is not likely to happen any time soon. Hence, the key element of regulated access, the setting of access tariffs (or the underlying methodology) by an effective and independent regulatory authority, will not be transposed, let alone implemented, by the adoption of the draft Law.
109. As regards access and transmission tariffs, Article 22(4) of the existing Decree requires that „*[r]egulated access shall be based on a published tariff system, or methodology and tariffs that are applied in an objective manner and are equal for all participants in the gas market.*“ However, in the absence of a regulatory authority, in practice the entity Ministry, upon proposal by the companies, sets “bundled” prices for transmission-supply, for the vertically integrated *BH Gas*, and the cantonal Ministry sets prices for distribution-supply. At this point in time, neither separate network tariffs for gas transmission and distribution, nor the methodology for their calculation, are adopted, published or applied in the Federation of Bosnia and Herzegovina.
110. This situation is in breach of Articles 18(1), read in conjunction with 25(2) of Directive 2003/55/EC, as well as Article 3 of Regulation 1775/2005. In order to offer non-discriminatory access to the networks, one of the key objectives of the Directive, network tariffs cannot be

<sup>67</sup> E.g. Case C-387/97 *Commission v Greece* [2000] ECR I-5047, paragraph 70.

<sup>68</sup> Article 40(3) of the draft Law on Gas.

<sup>69</sup> Article 41(5) of the draft Law on Gas.

<sup>70</sup> Reply to the Reasoned Opinion at page 3.



anything else but separated from supply prices. This is one of the most fundamental preconditions for achieving the objectives of the *acquis* in gas. Bundling prices and tariffs practically prevents anybody else but the incumbent supplier from acceding to the network and thus to provide third party access.

111. It must also be noted that regulating supply prices follows a different logic from regulating access tariffs. Whilst the latter constitutes a requirement under Directive 2003/55/EC, the regulation of supply prices needs to be justified as a public service obligation and must comply with the requirements of Article 3(2) of the Directive.<sup>71</sup> “Bundling” access tariffs and regulated supply prices in the way done by the Federation of Bosnia and Herzegovina leads to a situation where these requirements, especially the requirement of a clear definition and of transparency, cannot be complied with either.
112. A review of the entity Ministry’s tariff decision published on the website reveals that there is no specification of the tariff elements related to transmission and supply respectively. This structure also fails to meet the transparency requirements from Article 3 of Regulation 1775/2005.
113. As was stated at paragraph 58 above, the draft Law on Gas will not affect the situation. In Article 37(2)(q) of the draft, it is envisaged that the “*prices for ... the use of the transmission system ... approved by the state regulator will be published on its website not later than 15 days from the beginning of implementation*”. Consequently, the list of tasks in Article 48(2) of the draft mentions issuing the “*methodology and setting tariffs .. for using of distribution systems, storage systems of natural gas and management of LNG systems*”, but not transmission tariffs. As there is no state regulator to approve transmission tariffs, the provisions related to setting and publication of transmission tariffs in the Federation of Bosnia and Herzegovina will remain moot.
114. The Secretariat thus submits that **Bosnia and Herzegovina**, to which actions and non-actions of its entities, authorities and public companies are imputable, by not applying and publishing tariffs for access to and usage of the transmission system in Republika Srpska, as well as by not applying and publishing transmission and distribution tariffs (or the corresponding methodology) in the Federation of Bosnia and Herzegovina violates Article 18(1) of Directive 2003/55/EC as well as Article 3 of Regulation 1775/2005.

*(7) Third party access exemptions for new infrastructure*

115. Article 22 of Directive 2003/55/EC provides for the possibility to exempt major new gas infrastructure from the Directive’s requirements for third party access, and sets the criteria for such exemption both substantive and procedural. They need to be implemented by each Contracting Party, as the lack of such a provision deprives the investors in gas infrastructure of the right to receive an exemption from their third party access which, in turn, may prevent them from receiving an adequate rate of return on their investment and may prevent needed infrastructure from being built.
116. In the **Federation of Bosnia and Herzegovina**, Article 26 of the Decree on the Organization and Regulation of the Gas Sector stipulates a possibility to exempt major new (gas) infrastructure facilities from the requirement of third-party access. Further to listing the conditions for such an exemption and provisions related to increases of capacity in existing infrastructures

<sup>71</sup> See Case C-265/08 *Federutility* [2010] ECR I-3377.

and cross-border consultation in Articles 26(1),(2) and (4), Article 26(3) provides that exemption decisions under that Article „*shall be issued by the Ministry.*“

117. By contrast, Article 22 of Directive 2003/55/EC stipulates in its paragraph 3(a) that, in principle, the regulatory authority may, on a case by case basis, decide on exemptions from third party access of the type envisaged by Article 26 of the Decree on the Organization and Regulation of the Gas Sector. Alternatively, the second sentence of Article 22(3) of Directive 2003/55/EC states that „[Contracting Parties] *may provide that the regulatory authorities shall submit, for formal decision, to the relevant body in the [Contracting Party] its opinion on the request for an exemption.*“ While it is thus not excluded to task the Ministry with decision-making, the involvement of a regulatory authority is mandatory. This is not envisaged in the legislation of the Federation of Bosnia and Herzegovina.

118. The draft Law on Gas in the Federation, in its Article 44(7) envisages the issuance of an opinion of a regulatory authority, namely by the “*Regulatory Commission/Regulator at the state level.*” As MOFTER explains in its reply to the Reasoned Opinion, jurisdiction for dealing with exemption requests and giving opinions to the competent Ministry in charge is indeed to be assigned to a future state regulatory authority,<sup>72</sup> which corresponds to the general approach of the draft to establish regulatory competence over interconnections on the State level. A State-level regulatory authority, however, does not exist. Under these circumstances, Article 44(7) of the draft Law, even if adopted, would remain impossible to implement and apply. It is thus not capable of rectifying the violation of the existing Decree.

119. Furthermore, Article 22(3)(d) of Directive 2003/55/EC requires an exemption decision to be reasoned and published. This requirement has not been transposed into the law of the Federation of Bosnia and Herzegovina. In a similar case against Belgium, the Court of Justice of the European Union underlined the importance of explicit transposition of the requirement to reason an exemption decision which cannot be replaced by any general principles of administrative law.<sup>73</sup> The same applies to the obligation to reason such a decision.

120. While Article 44(4) of the draft Law on Gas contains an obligation to reason and publish any exemption decision, it will remain not applicable, even if adopted, for the reasons set out at paragraph 118 above.

121. The Secretariat thus concludes that **Bosnia and Herzegovina**, to which actions and non-actions of its entities are imputable, has not properly transposed Article 22 of Directive 2003/55/EC.

#### *(8) Market opening and reciprocity*

122. Article 23(1) of Directive 2003/55/EC, read in conjunction with Annex I to the Treaty, required Bosnia and Herzegovina to grant all non-household customers the right to purchase gas from the supplier of their choice (eligibility) by 1 January 2008. Article 23(2) of Directive 2003/55/EC allows for exceptions from the principle that an eligible customer may also choose to be supplied by a supplier from another Party to the Energy Community.

<sup>72</sup> Reply to the Reasoned Opinion at page 3.

<sup>73</sup> Case C-475/08 *Commission v Belgium* [2009] ECR I-11503, paragraph 42.

123. The gas market in the **Federation of Bosnia and Herzegovina** is currently entirely captive. Neither the Decree on the Organization and Regulation of the Gas Sector nor any other legislation applicable in that entity provides for market opening in line with the requirements of Article 23(1)(b) of Directive 2003/55/EC read together with Item 2(i) of Annex I to the Treaty.
124. Article 5 of the Decree on the Organization and Regulation of the Gas Sector envisages that „[t]he gas market shall be opened gradually as set forth in this Decree“. Article 58 of the Decree, however, subjects the implementation of the Decree's provisions on market opening – which in themselves are not compliant with the *acquis*, as will be argued below – to the condition of a national regulatory authority to be established. Article 58(1) of the Decree reads: „Gas market shall be developed gradually by implementing provisions from Articles 34 and 37 after the establishment of the Agency“. As has been stated above at paragraph 54, that Agency has never been established.
125. Article 58(2) of the Decree on the Organization and Regulation of the Gas Sector, making reference to the „characteristic of the natural gas market in Bosnia and Herzegovina/FBiH in the sense of limited number of end customers, undeveloped gas transport system, import of gas from only one transport direction to Bosnia and Herzegovina“ states a necessity „to start the initiative of application of market opening from Article 23 and application of Article 28 of Directive 2003/55/EC.“ The reference to Article 23 of Directive 2003/55/EC in Article 58(2) of the Decree shows that the legislature in the Federation of Bosnia and Herzegovina was well aware of the derogation of the Directive's provision when drafting the Decree and deferring market opening without setting any deadline.
126. At the same time, Bosnia and Herzegovina as the Contracting Party to the Treaty never granted a derogation under Article 28 of Directive 2003/55/EC, or notified it to the European Commission or the Secretariat as required under that provision. That Bosnia and Herzegovina should qualify for such an exemption was claimed several times by representatives of companies<sup>74</sup> as well as by both entities in the Ministry's reply to the Opening Letter.<sup>75</sup> In that respect, it is submitted that Bosnia and Herzegovina, being connected to the gas system of Serbia as another Contracting Party, does not qualify as an isolated market under Article 28(1) of Directive 2003/55/EC. Bosnia and Herzegovina also does not qualify as an emergent market under Article 28(2) of Directive 2003/55. The first commercial supply of its first long-term natural gas supply contract was made in 1979<sup>76</sup> and thus more than 10 years ago. As a result, the lack of market opening in the Federation of Bosnia and Herzegovina violates Article 23(1) of Directive 2003/55/EC.
127. Furthermore, the Decree's provisions on the status of eligible customers are not compliant with Directive 2003/55/EC. Article 29 of the Decree stipulates that an „[e]ligible customer has the right to freely choose its gas supplier which includes the right to change the gas supplier, in accordance with this provision and secondary legislation acts.“ The secondary legislation referred to in that provision has not been adopted. According to Article 34(1) of the Decree, an eligible

<sup>74</sup> At a workshop organized by the Secretariat in April 2008, the representative of BH Gas inquired about a possibility for derogation under Article 28 of Directive 2003/55/EC. He was invited by the Secretariat and the European Commission to address a notification to the Secretariat which has never been done. In the final report of the trilateral Working Group of 2010, the Federation stated that a derogation from market opening according to Article 28 of Directive 2003/55/EC should be initiated, without actually doing so.

<sup>75</sup> Page 5 of Attachment 1 to the reply, page 9 of Attachment 2 to the reply.

<sup>76</sup> To the Secretariat's knowledge, the contract might be even from 1978, but supply started in 1979 – to the *Birac* factory and Sarajevo (distribution network).

customer is defined as either (i) „a customer that uses gas for generation of electricity, regardless of quantity of yearly consumption and within the limits for gas quantities intended for such use“ or (ii) an „end customer that used more than 150 million m<sup>3</sup> of gas in the past calendar year“.

128. The two alternative conditions to which the eligibility status is subjected by Article 34 of the Decree are not in compliance with the concept of market opening under Article 23(1)(b) of Directive 2003/55/EC. According to that provision, the only legitimate condition to be fulfilled by an eligible customer before the expiry of the deadline set in Item 2(ii) of Annex I to the Treaty is his status as „non-household“ customer. Article 23(1)(b) of Directive 2003/55/EC is clear and unconditional in that respect. Any conditions imposed by national law which are different from or supplementary to that provision, such as the ones in Article 34 of the Decree, are in breach of the *acquis communautaire*.
129. Moreover, Article 34(2) and (3) of the Decree stipulates that gas supply contracts involving foreign customers (paragraph 2) or foreign suppliers (paragraph 3) are only permitted if the customer involved is eligible in both the Federation of Bosnia and Herzegovina and the other country. The latter option – a gas supply contract between a non-domestic supplier and a domestic (eligible) customer – is not mentioned by Article 23(2) of Directive 2003/55/EC which in its *littera a*) only envisages a reciprocity requirement for the constellation covered by Article 34(2) of the Decree. It needs to be borne in mind that the reciprocity option offered by Article 23(2) constitutes an exemption to the principle of market opening and, as all exemptions, needs to be interpreted strictly. Extending the scope of the reciprocity requirement to transactions with a foreign supplier exceeds the scope of Article 23(2) of Directive 2003/55/EC and curtails the full market opening envisaged by Article 23(1) of the Directive for eligible customers.
130. Finally, Article 34(4) of the Decree also extends the reciprocity clauses stipulated in paragraphs 2 and 3 of that Article to contractual relations between the two entities of Bosnia and Herzegovina. The provisions reads: „*Provision from paragraphs 2 and 3 of this Article apply as appropriate to the relations between the two entities*“. Extending the (double) reciprocity requirement between two Parties to the Treaty to internal gas transactions also goes beyond what is envisaged by Article 23(2) of Directive 2003/55/EC, and thus equally restricts the full degree of market opening required by Article 23(1) of the Directive in situations with no cross-border relevance.
131. The Secretariat concludes that the Decree of the Federation of Bosnia and Herzegovina is in non-compliance with Article 23(1)(b) of Directive 2003/55/EC insofar as it, firstly, defers market opening and links it to uncertain events in the future, namely the setting up of a regulatory authority and the adoption of secondary legislation by the latter. Secondly, the conditions set by Article 34 of the Decree are not in compliance with Article 23(1)(b) of Directive 2003/55/EC, insofar as they require the fulfillment of criteria additional to those in the Directive. Thirdly, the extension of the reciprocity requirement for eligibility to transactions with a foreign supplier, as well as to inner-Bosnian situations violates Article 23 of Directive 2003/55/EC.
132. According to the draft Law on Gas, customers will be in principle be eligible, with the exemption for household customers, whose right to choose their gas supplier takes effect on 1 January 2015.<sup>77</sup> Contrary to these (apparently) unconditional rules, however, Article 46(1) and (2) as well as Article 75(1) require act of the Regulatory Commission and the future “regulator at state

<sup>77</sup> Articles 46(4) and (5), 75(3) and (4) of the draft Law on Gas.



level” for “defining the scope, conditions and the timeframe for market opening”. This understanding of the draft is confirmed by MOFTER’s reply to the Reasoned Opinion, whereby only a future State Gas law and the regulatory authority established thereunder is expected to set guidelines for market opening “as a precondition for further transposition of Directive [2003/55/EC] in the Federation of Bosnia and Herzegovina.”<sup>78</sup> This approach will either not achieve any market opening at all in the foreseeable future, or it will create confusion among the customers and suppliers subjected to the new Law. Once again, the Secretariat recalls that according to well-established case law of the Court of Justice of the European Union, the provisions of directives must be implemented with unquestionable binding force, and with the necessary specificity, precision and clarity, in order to satisfy the requirements of legal certainty. A solution which maintains, for the persons concerned, a state of uncertainty as regards the extent of their rights and obligations in a field governed by that law cannot be considered proper implementation of a Directive.<sup>79</sup> Even if it were adopted, the Federation’s Law on Gas will not suffice to rectify the existent breach of the Directive’s provisions on market opening.

133. Moreover, the draft in its Article 75(9) still limits “eligible” customers’ right to buy gas from non-domestic suppliers by requiring a license for international trade, and thus a disproportionate impediment on the right to eligibility in the light of Directive’s objective to open and integrate markets across borders.

134. Consequently, the Secretariat submits that in the instances identified above, **Bosnia and Herzegovina**, to which actions and non-actions of its entities are imputable, contravenes Article 23 of Directive 2003/55/EC read together with Item 2(i) of Annex I to the Treaty.

#### *(9) Requirements following from Regulation (EC) No 1775/2005*

135. Regulation 1775/2005 aims at setting non-discriminatory rules for access conditions to natural gas transmission systems.<sup>80</sup> The Regulation requires Contracting Parties to make obligatory on their transmission system operators a number of technical provisions relating to, inter alia, principles for tariffs or their methodology (Article 3), third party access services (Article 4), principles of capacity allocation mechanisms and congestion management procedures (Article 5), transparency requirements (Article 6), balancing rules and imbalance charges (Article 7) and trading of capacity rights (Article 8). Furthermore, the Regulation tasks the national regulatory authority with ensuring compliance by the transmission system operators (Article 10) and requires penalties to be imposed in cases of violations. Adoption, implementation and enforcement of the provisions of Regulation 1775/2005 are indispensable preconditions for the establishment of competitive gas markets. Their implementation is both a legal obligation in itself and a prerequisite for the full implementation of Directive 2003/55/EC.

136. In **Republika Srpska**, the transmission system operator is tasked to adopt and publish the network rules, to be approved by the regulatory authority RERS.<sup>81</sup> They should include rules on access and use of the transmission network, as required by Regulation 1775/2005. *Gas Promet* adopted a Rulebook on the Operation of Transmission Network, which was approved by RERS and entered into force on 14 July 2010.<sup>82</sup>

<sup>78</sup> MOFTER Reply to the Reasoned Opinion, at page 4.

<sup>79</sup> Case C-296/01 *Commission v France* [2003] ECR I-13909, paragraph 54.

<sup>80</sup> Article 1 of Regulation 1775/2005.

<sup>81</sup> Article 22 of the amended Law on Gas.

<sup>82</sup> Official Gazette of Republika Srpska 64/10, Annex 11.

137. Based on the analysis below, the Secretariat submits that the Rulebook fails to fully transpose the provisions of Regulation 1775/2005.
138. The Rulebook does not envisage any obligation on the transmission system operator to provide both firm and interruptible services and to offer those services both on long and short-term basis. In Article 11, the Rulebook mentions the possibility to offer interruptible capacity in principle. In practice, *Gas Promet* provides only firm services and only for one year ahead. This was not disputed in the reply to the Opening Letter or the Reasoned Opinion. It does not comply with the Guidelines annexed to Regulation 1775/2005, which in Item 1(1) requires transmission system operators to offer “*firm and interruptible services down to a minimum period of one day*”. It also does not comply with Item 1(4) of the Guidelines, which require transmission system operators to implement standardised nomination/re-nomination procedures, develop information systems and electronic communication means to provide adequate data to network users. The situation in Republika Srpska thus fails to comply with Article 4(1) lit. (b) and (c) of Regulation 1775/2005.
139. Furthermore, the Law on Gas tasks the transmission system operator „*to issue the system operational rules*“, including, inter alia, „*the manner of providing ancillary services*“. According to Articles 28 and 62 to 66 of the Rulebook, the transmission system operator shall determine “*the manner of providing ancillary services*” and submit it to the regulatory authority for approval. According to the definitions in Article 3(m) of the amended Law on Gas and Article 5 of the Rulebook „*ancillary services*“ include balancing mechanisms.
140. Firstly, however, *Gas Promet* in practice is not involved in the balancing of the network in the entity of Republika Srpska. Rather, balancing – as a pure technical function and not following the rules set by *Gas Promet*’s Rulebook – is performed by *BH Gas* according to no specific balancing rules and without imposing imbalance charges. This was not disputed in the reply to the Opening Letter or the Reasoned Opinion. The situation is in breach of Article 7(1) and (3) of Regulation 1775/2005.
141. Secondly, and even if the Rulebook were actually applied to balancing, it only very generally describes balancing principles. Accordingly, the transmission system operator should impose penalties. In the cases when daily imbalance adds up to an interval of +/-2%, it is to buy/sell gas from/to the network user at a price which is 120%/80% of the “*balancing gas price*”. It is not clear from the Rulebook of *Gas Promet* how that “*balancing gas price*” is determined. In this situation, the Rulebook contravenes Article 7(3) of Regulation 1775/2005 which requires imbalance charges to be cost-reflective. The practice in Republika Srpska also fails to make “*any calculation methodology for imbalance charges as well as the final tariffs*” public, as also required by this provision. This was not disputed in the reply to the Reasoned Opinion.
142. Finally, neither the Law nor the Rulebook lays down rules on effective, proportionate and dissuasive penalties for non-compliance with the obligations under Regulation 1775/2005, as required by Article 13 of that Regulation. Even though the Law on Gas, in Articles 55 to 57, lists instances subject to penalties to be set by the regulatory authority, these lists do not address the detailed requirements of Regulation 1775/2005. The general authority vested in the authorized inspector under Article 54a under the amended Law to prohibit transportation of natural gas in cases of a violation of the Law or secondary legislation adopted thereunder, following the expiry of a deadline for remedying the violation in question, does not fulfil the requirement of

proportionality, as it treats all violations equal regardless of their dimension. It can also not be considered effective and dissuasive, as system operators have no incentive for avoiding violations in the first place, if they can always be remedied within the time limit set, without any penalty to be expected.

143. Republika Srpska acknowledged throughout the preliminary procedure that *Gas Promet's* network code fails to fully implement Regulation 1775/2005. Non-compliance with Article 4(1) lit. (b) and (c),<sup>83</sup> Article 7<sup>84</sup> as well as Article 13<sup>85</sup> of Regulation 1775/2005 was acknowledged in MOFTER's reply to the Opening Letter. In its comments on the Reasoned Opinion, Republika Srpska again conceded that the rules applicable in this entity related to capacity allocation, congestion management and balancing mechanism are not in line with Regulation 1775/2005. They require amendments to the transmission system operator's network code.<sup>86</sup>

144. None of the provisions of Regulation 177/2005 have been transposed in the **Federation of Bosnia and Herzegovina**, neither in the Decree on the Organization and Regulation of the Gas Sector, nor in secondary legislation, which has been made contingent on the establishment of a regulatory authority (Article 60 of the Decree). The only provision of some relevance, Article 11 of the Decree, requires the transmission system operator to *„give precised [sic] information to market participants directly connected to the transport system, sufficiently in advance, about the quantity and the day of gas transport termination and expected decrease of transport capacities.“* This is too general to be considered as transposition of the specific obligations required by Article 6 of Regulation 1775/2005, let alone the detailed requirements in Item 3. of the Guidelines annexed to Regulation 1775/2005. Moreover, the requirements set out in Regulation 1775/2005 are not applied in practice by the transmission system operator *BH Gas*. As regards balancing in particular, and as has been described above, *BH Gas* performs only technical balancing based on no predetermined rules and not imposing imbalance charges. The failure of the Federation of Bosnia and Herzegovina to transpose Regulation 1775/2005 means that this Regulation is not transposed on the entire territory of Bosnia and Herzegovina as a Contracting Party to the Energy Community Treaty.

145. Article 38 of the draft Law on Gas envisages a network code to be established by the transmission system operator, and makes reference, inter alia, to *“criteria for access to the transmission system”, “[p]rocedure for allocation of measures gas quantities ...”, “rules for congestion management”, “[p]rocedure for balancing and costs”, and “... type of services (short-term, long-term, interruptible).”*<sup>87</sup> At the same time, Article 38(3) of the draft requires approval of the network code by *“the regulator on the state level”*, an authority non-existing and with no concrete perspective to ever be established. Similarly, rules to *“define allocation of cross-border capacities of gas and gas transit”* are supposed to be set by the State regulatory authority as well as the methodologies for transport and balancing services, and for the costs of connection.<sup>88</sup> Furthermore, Article 41(2) of the draft Law on Gas, which is limited to the operators of the distribution, storage and LNG networks, makes it clear that the regulatory authority of the Federation of Bosnia and Herzegovina has no mandate to deal with disputes against refusals of third-party access. Adopting secondary legislation defining and ensuring the implementation of

<sup>83</sup> Page 3 of the Republika Srpska's contribution to the reply – “partially complied – need to be improved”.

<sup>84</sup> Page 3 of the Republika Srpska's contribution to the reply – “partially complied”.

<sup>85</sup> Page 3 of the Republika Srpska's contribution to the reply – “partially complied”.

<sup>86</sup> Reply to the Reasoned Opinion at page 3, Comments by Republika Srpska at pages 19/20.

<sup>87</sup> Article 39(2)(e), (h), (j), (k), (n) of the draft Law on Gas.

<sup>88</sup> Article 40(5)-(7) of the draft Law on Gas.

third-party access to the transmission network does - unlike for distribution, storage and LNG<sup>89</sup> – not feature among the tasks of the (future) entity regulatory authority. Consequently, not only will access to the transmission system remain a non-regulated activity and regulated third party access to the network operated by *BH Gas* does not exist, the draft effectively precludes any further legislation implementing Regulation 1775/2005 on the level of the Federation of Bosnia and Herzegovina.

146. Based on the above, the Secretariat submits that **Bosnia and Herzegovina**, to which actions and non-actions of its entities, authorities and public companies are imputable, fails to implement Articles 4 to 8, 10 and 13 of Regulation 177/2005.

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<sup>89</sup> Article 48(2)(p) of the draft Law on Gas.



## ON THESE GROUNDS

The Secretariat of the Energy Community respectfully proposes that the Ministerial Council of the Energy Community declare in accordance with Article 91(1)(a) of the Treaty establishing the Energy Community that

1. by failing to designate one or more competent bodies with the function of regulatory authorities to cover the entire gas sector in Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 25 of Directive 2003/55/EC;
2. by failing to implement the requirement of legal unbundling of transmission system operators from other activities not relating to transmission, Bosnia and Herzegovina fails to comply with Article 9(1) of Directive 2003/55/EC;
3. by failing to ensure the independence of the transmission system operators in terms of its organization and decision-making from other activities not relating to transmission, Bosnia and Herzegovina fails to comply with Article 9(1) and (2) of Directive 2003/55/EC;
4. by failing to obligate the transmission system operator of the Federation of Bosnia and Herzegovina to establish a compliance programme, Bosnia and Herzegovina fails to comply with Article 9(2)d of Directive 2003/55/EC;
5. by failing to implement the obligation to audit and publish the accounts of natural gas undertakings, Bosnia and Herzegovina fails to comply with Article 17(2) of Directive 2003/55/EC;
6. by failing to set and apply separate transmission tariffs in Republika Srpska, Bosnia and Herzegovina fails to comply with Articles 18(1) and 25(2) of Directive 2003/55/EC as well as Article 3 of Regulation 1775/2005;
7. by maintaining a possibility for negotiated access to the transmission system in the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 18(1) of Directive 2003/55/EC;
8. by failing to approve and to publish transmission and distribution tariffs (or a corresponding methodology) in the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 18(1) of Directive 2003/55/EC and Article 3 of Regulation 1775/2005;
9. by failing to require the involvement of a regulatory authority in the procedure for exempting major new gas infrastructures from certain provisions of Directive 2003/55/EC, and by not requiring an exemption decision to be reasoned and published in the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 22 of Directive 2003/55/EC;
10. by failing to grant eligibility to all „non-household“ customers in the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 23(1)(b) of Directive 2003/55/EC;
11. by maintaining a reciprocity requirement limiting eligibility in cases of transactions with a foreign supplier, as well as of inner-Bosnian transactions, in the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Article 23 of Directive 2003/55/EC;
12. by the transmission system operator in Republika Srpska failing to offer third party access services other than firm services and only for one year ahead, Bosnia and Herzegovina fails to comply with Article 4(1)(b) and (c) of Regulation 1775/2005;


13. by the transmission system operator in Republika Srpska failing to balance the gas system in accordance with balancing rules, and to set cost-reflective imbalance charges and publish them, Bosnia and Herzegovina fails to comply with Article 7(1) and (3) of Regulation 1775/2005;
14. by failing to provide for effective, proportionate and dissuasive penalties for non-compliance with the obligations under the Rulebook on the Operation of Transmission Network in Republika Srpska, Bosnia and Herzegovina fails to comply with Article 13 of Regulation 1775/2005;
15. by failing to adopt appropriate legislation and to apply it by the transmission system operator of the Federation of Bosnia and Herzegovina, Bosnia and Herzegovina fails to comply with Articles 4, 5, 6, 7, 8 and 13 of Regulation 1775/2005.

On behalf of the Secretariat of the Energy Community

Vienna, 21 May 2013

Janez Kopač

Director



Dirk Buschle

Legal Counsel

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