Energy Community

ANNUAL REPORT ON THE IMPLEMENTATION OF THE ACQUIS UNDER THE TREATY ESTABLISHING THE ENERGY COMMUNITY

ENERGY COMMUNITY SECRETARIAT

10 SEPTEMBER 2010

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Energy Community Secretariat
Am Hof 4
1010 Vienna
AUSTRIA

Tel:+ 43 1 535 2222
Fax:+ 43 1 535 2222 11

Internet: www.energy-community.org
E-mail: contact@energy-community.org

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PREFACE

The present Implementation Report covers the period between mid 2009 and mid 2010. Its aim is to take stock of the progress achieved by the Contracting Parties in implementing the *acquis* under the Energy Community Treaty.

The Energy Community Treaty integrates national markets in the energy sectors. The energy sectors constitute the backbone of our economies and societies. Availability and affordability of energy are key issues not only on the European and global political agendas, but they are also crucial for our everyday lives. Energy concerns everybody and is of everybody's concern. In Europe, this is nowhere more true than in the Contracting Parties to the Energy Community.

Being a community under the rule of law, it is through the harmonization of laws that the Energy Community aims to achieve its goals and link the markets of the Contracting Parties with each other and with the internal market of the European Union. The implementation of a common set of legal rules – the *acquis* under the Energy Community Treaty – is expected to create a stable regulatory and market framework for achieving the common goals.

To what extent the Contracting Parties live up to their commitments by implementing the *acquis communautaire* is thus of the greatest importance for the progress of the Energy Community. In this respect, one needs to remember that the Contracting Parties have come a long way from the state of their energy sectors in the 1990's to endorsing the European model based on competition, sustainabilty and security of supply. At the same time, and very generally speaking, the gap between transposition of the Energy Community *acquis* and its true implementation is widening. Wholesale markets remain closed, barriers to cross-border trade continue to exist and energy prices are set at a too low level to stimulate investments, allow for market entry of alternative suppliers and incentivise energy efficiency. The Secretariat is determined to use all of its possibilities in order to assist in, as well as to push for an implementation close to the word and spirit of the *acquis*.

Implementation, however, is not static. The Energy Community exists in an ever-changing global and European environment. During the reporting period, the Ministerial Council extended the Energy Community *acquis* to three directives in the area of energy efficiency. Furthermore, the Lisbon Treaty transformed the Energy Community's largest Party, the European Community, into the European Union. In September 2009, the European Community adopted a "third package" of internal market legislation. The third package will not only change European Energy Law on substance, but also the pan-European energy governance model. The new *acquis* on renewable energy was adopted by the European Community as early as 2009. The Energy Community Ministerial Council is about to incorporate these acts, by way of Recommendations, to the Energy Community. The inclusion of the European Union's directive on emergency oil stocks is under preparation. This unprecedented extension of the *acquis* communautiare offers new opportunities and at the same time poses implementation challenges to the Contracting Parties, in which the Secretariat is ready to assist.

Another event within the reporting period of the current report might transform the Energy Community in an equally profound way. In May 2010, the Energy Community experienced its first enlargement by welcoming the Republic of Moldova as its eighth Contracting Party. Ukraine is on a very promising path to achieve the same result. The Energy Community model and the efforts of the Parties and institutions in implementing and developing it continue to matter for the modernization of the energy sectors to the benefit of its economies, societies and citizens. It is also against this background that the present Implementation Report should be read.

2

INTRODUCTION

THE ENERGY COMMUNITY

THE SECRETARIAT

THE APPROACH

2. INTRODUCTION

2.1 THE ENERGY COMMUNITY

The main idea behind the Energy Community is to extend the EU internal energy market to South-East Europe and beyond. The Energy Community was created by the Treaty establishing the Energy Community, signed in October 2005 in Athens and entered into force on 1 July 2006.

The general objective of the Energy Community is to create a regulatory and market framework which is able to attract investments for a stable and continuous energy supply, to create an integrated energy market allowing for cross-border energy trade and integration with the EU market, to enhance security of supply and competition, and to improve the environmental situation. The Treaty covers network energy, which currently includes electricity, gas and oil.

The Parties to the Treaty are the European Union, and eight Contracting Parties, namely Albania, Bosnia and Herzegovina, Croatia, the Former Yugoslav Republic of Macedonia, Moldova, Montenegro, Serbia and UNMIK.

As of June 2010, 14 European Union Member States have the status of Participants (namely Austria, Bulgaria, Czech Republic, Cyprus, France, Germany, Greece, Hungary, Italy, Romania, Slovakia, Slovenia, and the United Kingdom). Georgia, Norway, Turkey and Ukraine currently take part as Observers.

The Energy Community

Source: Energy Community Secretariat

The means to achieve the objectives underlying the Energy Community Treaty is integration by law being based on EU rules and principles. The Contracting Parties committed themselves to implementing selected parts of the *acquis communautaire* on electricity, gas, renewables, energy efficiency, competition, environment and security of supply. Additionally, a unique institutional setup supports the further implementation and development of the *acquis*. The institutions comprise the Ministerial Council as the supreme decision-making body, the Permanent High Level Group preparing its work, the Regulatory Board, Fora for electricity, gas, oil and social issues, and the Secretariat.

2.2 THE SECRETARIAT

The Secretariat of the Energy Community is the only permanent institution under the Treaty. Its roles comprise providing assistance to the Parties and institutions of the Treaty, enforcing the implementation of the Treaty's *acquis* and monitoring the state of implementation.

In accordance with Article 67(b) of the Treaty establishing the Energy Community, the Secretariat shall review the proper implementation by the Contracting Parties of their obligations under the Treaty and submit annual progress reports to the Ministerial Council of the Energy Community.

2.3 THE APPROACH

The present report aims at presenting a true and fair view of the state of play of the implementation of the *acquis communautaire* by the Contracting Parties to the Treaty as of 30 June 2010.

The report is divided into two parts, one general section outlining the relevant *acquis communautaire* and summarizing the state of implementation, and a section assessing the situation for each of the Energy Community's eight Contracting Parties. Both parts follow the scope of the Treaty and comprise chapters on electricity, gas, oil, competition, environment, renewables, energy efficiency and social issues.

Regarding the state of implementation for each Contracting Party, the report follows a three-tiered structure, outlining first the general situation with regard to the implementation of the respective *acquis*, then focusing on progress made within the reporting period, i.e. between mid 2009 and mid 2010, and finally summarizing the state of compliance.

The report has been prepared involving all services of the Secretariat and coordinated by the Legal Counsel. The information used was either provided by the Contracting Parties through missions or other contacts, or was obtained from third parties or publicly available data. The report also bases its assessment on data and analysis reports prepared by the Energy Community Regulatory Board (ECRB).

More detailed information on the Energy Community, its institutions and Contracting Parties, as well as documents related thereto can be found at www.energy-community.org.

3

THE ENERGY COMMUNITY 2009/2010

ELECTRICITY

GAS

OIL

COMPETITION

ENVIRONMENT

RENEWABLE ENERGY

ENERGY EFFICIENCY

SOCIAL ISSUES

3. THE ENERGY COMMUNITY 2009/2010

Developements on the regional level

The following chapter provides an overview of the main developments in the Energy Community from a regional perspective, with a focus on common progress as well as on shortcomings. These conclusions are based on the detailed assessment provided in Chapter 5 for each Contracting Party and sector separately.

In view of the differing characteristics and requirements of the individual energy carriers falling within the scope of the Treaty – electricity, gas and oil – as well as the horizontal character of competition, environment, energy efficiency and social policies, common conclusions are not easily drawn. Each sector and each Contracting Party deserves to be assessed on its own merits. Nevertheless, some general findings and trends which are valid for most of them can be identified:

- Generally speaking, Contracting Parties in all sectors established legal frameworks based on the elements contained in the *acquis*. This finding is without prejudice to the lack of transposition of certain elements, or the lack of implementation and application of these elements in reality. Some degree of principle convergence of the market designs between Contracting Parties, as well as between Contracting Parties and EU Member States, however, exists and is to be attributed to the reform endeavours within the Contracting Parties following their Energy Community membership.

- In the regulated electricity and gas sectors, the applicable Energy Community *acquis* mainly focuses on structural and behavioural aspects of network operation, regulatory supervision and market opening. Transposition of the *acquis* in this respect is normally done by way of sector-specific (primary and secondary) legislation on which the Secretariat very closely cooperates with the Contracting Parties through the network of the Permanent High Level Group members. Other parts of domestic legislation of relevance for the energy sectors, including on authorization/tender procedures, competition and State aid, customs and taxes, environment, energy efficiency, social issues etc. are not always as easily accessible.

- In a similar vein, the transposition of clearly defined requirements in the sector-specific *acquis* is both easier to achieve and to monitor as compared to the proper implementation/application of general principles (related to non-discrimination, undistorted competition, free movement of energy etc.). However, it is those parts of the *acquis* which largely determine the impact and success of market liberalization of the energy sectors. As a rule, one may conclude from the information available that transposition of specific rules is more advanced in the Contracting Parties than the implementation of the general principles and an enforcement culture in general.

- With regard to market opening in particular, the assessment of the Secretariat shows that most Contracting Parties follow the Treaty in granting eligibility to non-household customers. However, by incentivising eligible customers to remain within the regulated sectors through price regulation below market level (see the table below), the practical effect of market opening is jeopardized. Unlimited regulated energy prices create a barrier to entry for new suppliers and thereby threaten the success of other central goals of the Energy Community besides market opening, such as attraction of investments or effective demand-side measures. The Secretariat will address this from the perspectives of Article 3 of the Internal Market Directives and State aid law. Furthermore, market designs based on public suppliers linked to incumbent domestic generators create inherent obstacles for both market opening and free trade in energy.

- Another general trend relates to the lack of definition of public service obligations. The public service nature of energy may justify various kinds of State intervention, but requires a clear definition of what precisely such public service entails. Most Contracting Party content themselves with generally stipulating the public service nature of energy as a basis for, inter alia, across-the-board price regulation. In the future, this needs to be more closely linked to the notion of vulnerability and seen within the broader picture of the entire social welfare system. Regulated tariffs should be phased out and substituted by other market oriented instruments of consumer protection. As a first step price regulation for industrial and small and medium businesses should at least be abolished. The Secretariat concurs with the recent ECRB paper on vulnerable household customers of November 2009.

- The lack of proper wholesale market opening is certainly one of the key issues when it comes to the shortcomings in the implementation of the Treaty. Another issue that needs to be addressed in the future relates to the creation of a regional market, one of the main objectives of the Treaty. In reality, the Contracting Parties still aim at creating or protecting energy autonomy and often sacrifice key principles of the Energy Community *acquis* for that goal. This does not only concern evident breaches of Article 41 EnC such as customs duties, but also import restrictions inherent in the market model, for instance by giving statutory priority to domestic electricity. Other impediments to the free flow of energy concern traders in particular (such as fees or seat requirements as preconditions for licenses) or may relate to the methods of capacity allocation (such as priority access). The Secretariat cannot wait any longer for the future establishment of a Coordinated Auction Office to bring the discriminatory elements inherent in such schemes to an end. With regard to trade barriers for energy, it sent out a comprehensive questionnaire to traders and suppliers in May 2010

- With regard to the regulatory framework, effective independence of regulatory and competition authorities is key for the practical implementation of market opening put into legislation. Governments should not be afraid of strong authorities but recognise their core function as guides to and protectors of energy policies in market reality. That said, effective independence of regulatory and competition authorities is still lacking. The lack of independence in practice provides another good example of the gap between implementation of the *acquis* by letter and by spirit. While competition and regulatory bodies are established in all Contracting Parties and are declared to be independent by law, the reality is often different. This includes not only direct external influences on regulatory decision-making, but also insufficient human resources and effective budgetary autonomy. The case is most critical in Bosnia and Herzegovina, where the question of the regulator's tasks and responsibilities on State level is still open. But also in more advanced Contracting Parties, the Secretariat notes continuing failure to address regulatory and structural shortcomings by the authorities.

- With respect to competition authority, a certain recent trend towards emancipation may be observed in some Contracting Parties, most notably Albania, Croatia and Serbia. It remains to be seen to what extent the competition authorities in the other Contracting Parties can make significant contributions to market opening in the energy sectors. Common features of the energy markets such as various instances of abuses of dominant positions or contractual destination clauses should be more thoroughly scrutinized. The same applies *mutatis mutandis* to State aid, where a study tendered by the Secretariat will provide more insight into the effectiveness of the enforcement schemes.

IS THERE A REGULATED ENERGY PRICE?

CONTRACTING PARTY	ELECTRICITY YES/NO	IF YES, FOR WHICH GROUP OF CUSTOMERS?	GAS YES/NO	IF YES, FOR WHICH GROUP OF CUSTOMERS?
ALBANIA	YES	ALL CUSTOMERS	NO	THERE IS NO GAS MARKET IN ALBANIA
BOSNIA AND HERZIGOVINA	YES	ALL CUSTOMERS	YES	ALL CUSTOMERS
CROATIA	YES	TEMPORARILY BLOCK TARIFFS DEPENDING ON CONSUMPTION	NO	
FYR OF MACEDONIA	YES	ALL CONNECTED BELOW 110KV	YES	INDUSTRIAL CUSTOMERS (THERE IS NO DISTRIBUTION NETWORK YET)
MONTENEGRO	YES	ALL CUSTOMERS	NO	
SERBIA	YES	ALL CUSTOMERS	YES	ALL CUSTOMERS
UNMIK	YES	ALL CUSTOMERS	N/A	N/A

Source: ECRB, "Vulnerable Household Customers - An ECRB Contribution to a Common Understanding, November 2009. Moldova only joined the Energy Community in May 2010 and therefore is not included in the overview.

3.1 ELECTRICITY

3.1.1 The acquis on electricity

The Energy Community Treaty requires the Contracting Parties to implement the following legislative documents:

1. Directive 2003/54/EC concerning common rules for the internal market in electricity establishes the main principles of electricity market liberalisation. This includes market opening, unbundling, third-party access to electricity networks, public service obligations, customer protection, the criteria and procedures for granting authorisations and tendering for new generation capacities, licenses for transmission, distribution and supply as well as requirements for system operation and development.

   The deadline for implementation of Directive 2003/54/EC expired by 1 July 2007. According to Annex I to the Energy Community Treaty, the electricity markets of the Contracting Parties have to be open for all non-household customers as of 1 January 2008 and for all households as of 1 January 2015.

2. Regulation (EC) 1228/2003 on conditions for access to the networks for cross-border exchanges in electricity establishes the main principles of electricity market liberalisation. The Regulation builds on Directive 2003/54/EC and lays down more detailed rules for cross-border electricity flows such as tariff principles, third-party access services, transparency requirements, balancing rules and imbalance charges, principles on capacity allocation and congestion management on interconnections including secondary markets for trading of the capacities rights. The guidelines on capacity allocation and congestion management annexed to Regulation 1228/2003 have been made part of the *acquis* by Decision 2008/02/MC-EnC of the Ministerial Council of June 2008. The implementation deadline for the common coordinated congestion management method and procedure for the allocation of capacity required thereunder expired on 31 December 2009.

3. Directive 2005/89/EC concerning measures to safeguard security of electricity supply and infrastructure investment establishes a common legal and regulatory framework within which the Contracting Parties shall define general, transparent and non-discriminatory security of supply policies compatible with the operation of a competitive internal electricity market. The Directive sets up measures to safeguard an adequate level for the security of electricity supply and encourage investment in generation, transmission, distribution and cross-border interconnection lines to maintain a sustainable balance between supply and demand. Roles and responsibilities of the competent authorities and network operators involved have to be defined to set, meet and monitor the quality of supply and network security performance objectives while contributing to the proper functioning of the regional and internal electricity markets. The deadline for the implementation of Directive 2005/89/EC expired on 31 December 2009.

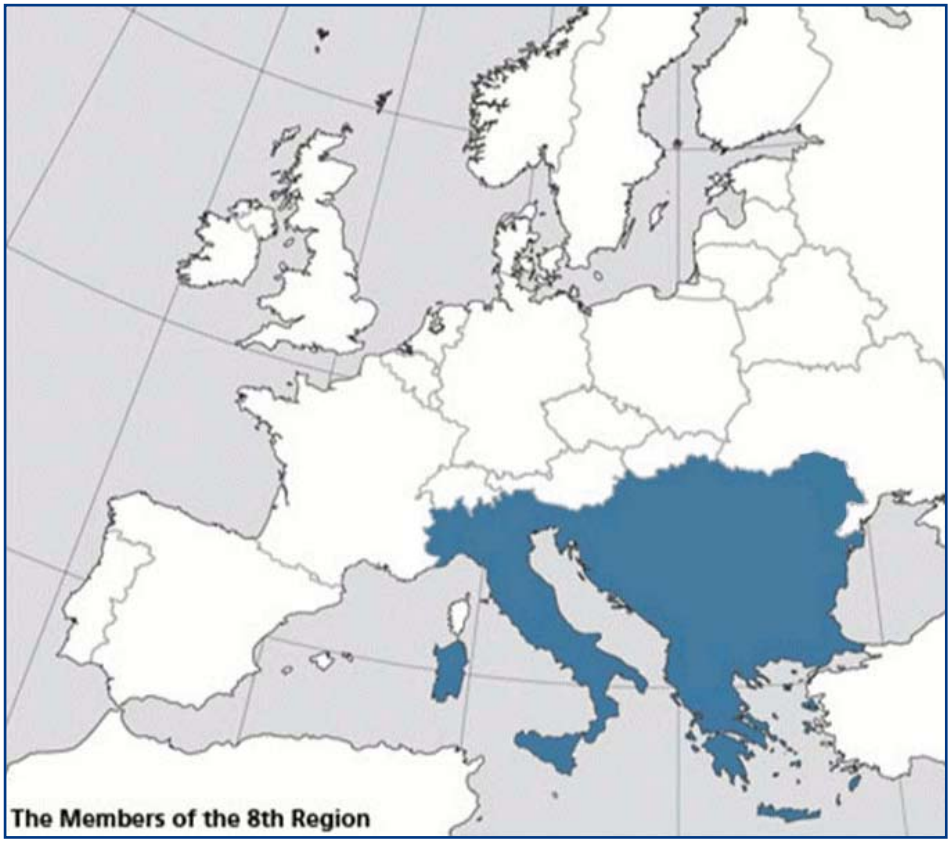
   In addition to the legally binding obligations a general list of technical standards for the electricity sector, mirroring the relevant standards on the European level - (e.g. the operational UCTE rules) has been adopted by the Ministerial Council in June 2007 under Article 21 of the Treaty as the so-called "List of Generally Applicable Standards". In that respect, more detailed implementation plans including concrete deadlines still have to be prepared and adopted by the Contracting Parties.

3.1.2 The 8th Region

Under the framework of the Energy Community, the so-called "8th Region" has been established by Decision of the Ministerial Council 2008/02/MC-EnC of 27 June 2008, with a view to implement the common procedure for electricity congestion management and transmission capacity allocation on a regional level, stemming from the guidelines annexed to Regulation 1228/2003. The concept of the 8th Region follows the model of the seven regions already established in Europe.

The 8th Region includes Albania, Bosnia and Herzegovina, Croatia, the Former Yugoslav Republic of Macedonia, Montenegro, Serbia, UNMIK, Bulgaria, Greece, Hungary, Romania, Slovenia and Italy (limited to interconnections between Italy and the Contracting Parties which to date do not yet exist). In the Secretariat's assessment, Moldova joined the 8th Region *ipso jure* by acceding to the Treaty.

The main legal consequence arising from the creation of the 8th Region is the obligation to apply a common coordinated congestion management method and procedure for the allocation of capacity to the market. In that respect, the approach taken and developed within the framework of ECRB is the establishment of a Coordinated Auction Office.



Source: Energy Community Secretariat

3.1 ELECTRICITY

3.1.3 Main Findings

The overall compliance with the *acquis* on electricity is, even after the deadlines for the implementation of all three parts of the electricity *acquis* have expired a while ago, still not satisfactory.

Based on a more detailed analysis of the individual Contracting Parties in chapter 5 the following overall picture can be drawn for the status of market liberalisation:

In 2009 and 2010, most of the Contracting Parties have finalised (Montenegro) or are in the process of finalising (Former Yugoslav Republic of Macedonia, Serbia, UNMIK) amendments to their primary electricity legislation, aimed to transpose the requirements of Directive 2005/89/EC and to increase compliance with Directive 2003/54/EC and Regulation 1228/2003. Moldova adopted an Electricity Law at the end of 2009, transposing Directive 2003/54/EC. It still has to implement Directive 2005/89/EC and Regulation 1228/2003 by the end of 2010. Croatia is already considering the transposition and implementation of the Third Energy Legislative Package, on account of its process towards accession to the EU. More substantial progress is expected from Albania and Bosnia and Herzegovina, as the process of amending the legislation and achieving compliance with the electricity *acquis* is still at an early stage.

The process of legal unbundling of transmission system operators was finalised in all Contracting Parties. Unbundling of distribution from supply and generation has to advance further in the vertically integrated utilities. Until then, the regulatory authorities have to properly monitor the process of unbundling of the accounts, so as to ensure the correct allocation of costs and returns on activities.

In addition to the formal adoption of the eligibility thresholds, the relevant preconditions for the market opening include the implementation of the third-party access principle through the approval of non-discriminatory, transparent network access tariffs. Transmission and distribution tariffs have been adopted by most of the Contracting Parties. However, lack of cost-reflectivity is the main drawback for the implementation. Thereby regulatory authorities and governments - to the extent they have the power to approve network tariffs - negatively affect investments in the networks needed to ensure the long term ability of the system to meet a reasonable demand for the transmission of electricity. Moreover, the policy of promoting renewable energy will require grid operators to reinforce or develop their networks to ensure the integration of renewable projects into their systems.

The rate of voluntary supplier switching is almost zero in most of the Contracting Parties, as the eligible customers have the right to be supplied by the incumbent supplier at regulated electricity prices, which are below the market price of imported electricity.

Security of electricity supply remains an issue of concern in the long term at the regional level, despite good hydrologic conditions in 2009 and 2010 combined with a drop in electricity consumption. The authorisation procedures for new generation capacities have to be adopted in most Contracting Parties and streamlined considering their limited size or potential impact in case of distributed generation. Tendering for new capacities must be used as an efficient tool to ensure security of the electricity supply as some of the Contracting Parties do not meet the requirements to have available reserve capacities for balancing purposes (Albania, the Former Yugoslav Republic of Macedonia, Montenegro and UNMIK). Provisions for balancing services have to be developed further.

None of the Contracting Parties is in compliance with the requirement of Regulation 1228/2003 to establish a regionally coordinated capacity allocation and congestion management procedure (Point 3.2 of the Congestion Management Guidelines). The deadline for implementation expired on 31 December 2009. The setting up of a Coordinated Auction Office is not explicitly required by Regulation 1228/2003. However, no other concept for a regionally coordinated capacity allocation and congestion management has been tabled and seriously discussed.

If at all, only bilaterally coordinated auctions are applied. Discussions on establishing a Coordinated Auction Office for South-East Europe for meeting the legal requirements were so far blocked by evident inconsistencies between the support given to the project from the high-up political level, including the Ministerial Council on several occasions, and the lack of an adequate follow-up on the operative levels in the Contracting Parties' ministries. Regulatory authorities as well, which together with the governments are responsible for their transmission system operators' compliance with the legal requirements have failed to take a strong position, both on the national and regional level. While a certain lack of regulatory independence may be an explanation for regulatory passivity, it does not release regulatory authorities from their responsibilities.

3.2 GAS

3.2.1 The acquis on gas

The Treaty requires the Contracting Parties to implement the following legislative documents:

1. Directive 2003/55/EC concerning common rules for the internal market in natural gas, establishing the main principles of gas market liberalisation. This includes market opening, unbundling, third-party access to gas infrastructure; public service obligations, customer protection, the criteria and procedures for granting authorisations and licenses for transmission, distribution, supply and storage, as well as requirements for system operation and development.

   The deadline for implementation of Directive 2003/55/EC expired on 1 July 2007. According to Annex I to the Energy Community Treaty, the gas markets of the Contracting Parties have to be open for all non-household customers as of 1 January 2008 and for all households as of 1 January 2015.

2. Regulation (EC) 1775/2005 on conditions for access to the natural gas transmission networks has been included in the binding set of *acquis* by the Ministerial Council Decision 2007/06/MC-EnC of December 2007, with an implementation deadline of 31 December 2008. The Regulation builds on Directive 2003/55/EC and lays down more detailed rules for access to the natural gas transmission network, such as tariff principles, third-party access services, transparency requirements, balancing rules and imbalance charges, principles on capacity allocation and congestion management including secondary market trading of capacities.

3. Directive 2004/67/EC concerning measures to safeguard security of the natural gas supply has also been included in the binding set of *acquis* by Decision of the Ministerial Council in December 2007, with an implementation deadline of 31 December 2009. The Directive establishes measures to safeguard an adequate level of security of supply, with a special focus on specific customers and a community mechanism. It requires the Contracting Parties to define general, transparent and non-discriminatory security of supply policies, compatible with the requirements of the competitive market together with the definition of the roles and responsibilities of market participants and the implementation of procedures to safeguard security of supply.

   In addition to the legally binding obligations, a general list of technical standards for the gas sector, mirroring the relevant standards on the European level has been adopted by the Ministerial Council in June 2007 under Article 21 of the Treaty as the so-called "List of Generally Applicable Standards". In that respect, more detailed implementation plans including concrete deadlines still have to be prepared and adopted by the Contracting Parties.

3.2.2 Main Findings

After the expiry of the deadlines for the implementation of all three parts of the gas *acquis*, overall compliance is still not satisfactory.

Only one Contracting Party (Croatia) is well in line with the legal requirements. The picture is different for the other Contracting Parties. Although progress has been made, full compliance with the *acquis* is still not ensured. On top of the insufficiencies in national primary and secondary legislation, the different implementation levels and varying progress between the Contracting Parties creates a barrier on the proper development of gas market opening in the region. In this respect, it is important to remember that a successful liberalisation process requires full implementation of *all* legal requirements, bringing about an interlinked set of measures. Similarly, only coherence between Contracting Parties can bring the benefits expected from regional market integration.

From the more detailed analysis of the individual Contracting Parties in Chapter 5 the following overall picture can be drawn for the status of gas market liberalisation:

Interestingly, the three Contracting Parties without a gas market (Albania, Montenegro, and UNMIK) have almost fully implemented Directive 2003/55/EC in their primary legislation, which can be seen as a sufficient basis for further gas market development. Going even further, Montenegro has implemented most of the provisions of Regulation 1775/2005 and Directive 2004/67/EC in its recently adopted Energy Law. Also Albania, and to a certain extent UNMIK, have made efforts to develop secondary legislation. For these three Contracting Parties further implementation of Regulation 1775/2005 and Directive 2004/67/EC will have to be adjusted to the level of market development.

On the contrary, those Contracting Parties that have a more or less developed gas sector (Bosnia and Herzegovina, the Former Yugoslav Republic of Macedonia and Serbia) still struggle with some of the crucial provisions of the basic Directive 2003/55/EC such as unbundling and third-party access exemptions for new Infrastructure. Keeping in mind the already existing structures, the level of market development and the fact that transmission system operators have been established for a long time, the poor level of implementation of Regulation 1775/2005 is hardly understandable in the case of Bosnia and Herzegovina and Serbia. Implementation of the Regulation remains an ultimate precondition for proper functioning of the market.

Network tariffs or respectively the regulatory approval of methodologies for tariff calculation are defined in all Contracting Parties except Bosnia and Herzegovina, where they exist only in one entity, but not on state level.

Market opening is not defined in line with the *acquis* in Albania, Bosnia and Herzegovina, and the Former Yugoslav Republic of Macedonia.

Non-compliance with the *acquis* exists in a number of Contracting Parties related to the treatment of cross-border transmission flows ("transit"), which are either treated differently from national transmission (Serbia) or not regulated at all (Bosnia and Herzegovina and partly Moldova). Additionally, the application of competition barriers, such as destination clauses in Serbia restricts market integration. In Croatia, the Former Yugoslav Republic of Macedonia and Serbia, the Secretariat is currently looking into certain issues of non-compliance in the respective inter-governmental agreements signed in the context of the South Stream project.

Provisions on security of supply are mostly implemented in line with Article 5 of Directive 2003/55/EC, including monitoring and definition of market players' responsibilities. However, existing legislation remains far from being in line with the requirements of Directive 2004/67/EC. Further efforts – especially related to the definition of major supply disruptions, measures to ensure security of supply for specific customers, emergency measures and procedures, reporting obligations, as well as cooperation mechanisms on Community level – remain to be made by all Contracting Parties with the exception of Croatia.

Moldova, as the "youngest" Contracting Party, provides an encouraging starting picture. Although Moldova benefits from implementation deadlines that are different from those applicable to the other Contracting Parties, Directive 2003/55/EC, except for rules on third-party access exemptions, has been almost fully implemented by primary legislation. The same is true for some basic provisions of Regulation 1775/2005. Implementation of both the Regulation and Directive 2004/67/EC has to be completed by the end of 2010.

Finally, the proper legislative framework is only one precondition for the functioning of the gas market. The second relates to the availability of interconnected infrastructure with sufficient capacity. Unfortunately, interconnectors in particular are poorly developed throughout the region. Huge efforts will be required in the future (see Chapter 4.2 of this report for the Secretariat's activities relating to this issue).

3.3 OIL

3.3.1 The acquis on oil

By Decision 2008/03/MC of the Ministerial Council in December 2008, the scope of the Energy Community Treaty was extended to a so-called "oil dimension", by including oil as part of the definition of "network energy". Firstly, this entails the applicability of the horizontal *acquis* related to, inter alia, environment, competition and the free movement of energy (Article 41 EnC), to oil. The Ministerial Council also decided to establish an Oil Forum as a regional consultation platform. Furthermore, the implementation of Directive 2006/67/EC on strategic oil stocks in the Energy Community was envisaged, but has not yet taken place.

In the meantime, the EU legal framework related to oil stocks was further developed by adoption of the new Council Directive 2009/119/EC on the obligation of Member States to maintain minimum stocks of crude oil and/or petroleum products. This Directive lays down rules aimed at ensuring a high level of security of oil supply through reliable and transparent mechanisms, maintaining minimum stocks of crude oil and/or petroleum products and putting in place the necessary procedural means to deal with a serious shortage. Countries have to ensure that their total oil supplies meet at least 61 days of average daily inland consumption or 90 days of average daily net imports (whichever of the two is greater). Countries also have to hold at least 30 days of stocks or a third of their stockholding obligation in the form of refined products. The Directive further sets out requirements for calculating stock levels and for enabling competent authorities to release quickly, effectively and transparently some or all of their stocks in the event of a major supply disruption.

The Permanent High Level Group in June 2010 decided to consider - following the conclusions and recommendations of the regional study on emergency oil stocks currently being commissioned - a proposal to the Ministerial Council on incorporating Directive 2009/119/EC in 2011.

3.3.2 Main Findings

The market for oil and petroleum products is characterized by the following key parameters:

- Oil is a key component of the energy mix in the Contracting Parties comprising 38%.
- Domestic oil production and export potential is likely to decline, while imports will increase. At the same time, oil demand increased by 53% within the last 9 years. Crude oil dependence in 2008 was around 84% and increased by 17% as compared to the level in 2000.
- Refineries in the Contracting Parties operate at 40%-42% of their nameplate capacity.
- Technical, environmental and quality improvements are required in order to achieve EU standards.
- The maximum capacity of storage tanks in the region amounts to around 3.2 million m3 (without knowledge about the technical condition of the tanks).
- The existing regional oil network infrastructure is limited. The start of operation of the envisaged new oil pipelines remains uncertain. Moreover, they are competing for the same sources of oil.

Following up on the Ministerial Council Decision, the Secretariat focused on the organisation of the first Oil Forum jointly organized with the International Energy Agency on 24-25 September 2009 in Belgrade. The Forum focused on several major issues such as the development of the oil dimension, the implementation of EU legislation on emergency oil stocks, the current situation with regard to the planned pipelines in the region, perspectives of downstream oil business, investment in refining, experience of Contracting Parties in exploration and production, and oil stocks policy in South-East Europe.

Based on a request by the Oil Forum, a first workshop on emergency oil stocks was organized in Zagreb at the end of May 2010. The workshop focused on lessons learned on the EU level; stockpiling experience in the region by Croatia and the Former Yugoslav Republic of Macedonia; the role of industry in stockholding and emergency response policies; the current legal and institutional framework, technical aspects, costs and funding and the role of the central stockholding entity according to Directive 2009/119/EC, as well as the composition of oil supplies and the development of emergency response policy.

The workshop indicated substantial differences between the Contracting Parties. In general and with minor exceptions, national stockholding systems are underdeveloped due to the lack of experience. Most of the Contracting Parties adopted some kind of legislation on emergency oil stocks according to which a majority of oil supplies are to be held by the industry. Other Contracting Parties have no policy yet in place on oil stocks. For these reasons, the imminent launch by the Secretariat of a regional study on emergency oil stocks was welcomed, as well as of the idea of a twinning project between EU Member States and the Contracting Parties on emergency oil stocks policies.

Similar to the gas, electricity and biofuels sectors, the Secretariat also identified potential barriers to the free movement of energy between the Energy Community for the oil sector. Related to these findings the Secretariat started investigations regarding conformity with Article 41 of the Treaty. In particular, this includes customs duties and quantitative restrictions or measures having equivalent effect. The review of national law and practice by the Secretariat is still at an early stage and may yield additional findings with respect to non-tariff barriers.

Based on the picture so far, however, it may be concluded that the market for oil and petroleum products in the Energy Community, irrespective of the high dependence on imports, is relatively open and competitive within most Contracting Parties, giving competing suppliers the possibility to enter the market and to have access to networks and storage facilities.

3.4 COMPETITION

3.4.1 The acquis on competition

Chapter IV of Title II of the Energy Community Treaty determines the *acquis* to be implemented by the Contracting Parties in the fields of competition and State aid. The competition *acquis* is modelled on the EU Treaty by incorporating what is now Articles 101, 102, 106(1) and (2) as well as Article 106 of the Treaty on the Functioning of the European Union (TFEU). Implementation should have occurred by the entry into force of the Treaty, i.e. by 1 July 2006, except for the public undertakings and undertakings to which special or exclusive rights have been granted (six months following the date of entry into force of the Energy Community Treaty). Since then, Contracting Parties are under a legally binding obligation to introduce, to the extent to which the trade of network energy between the Contracting Parties may be affected, a prohibition of cartels (agreements between undertakings, decisions by associations of undertakings and concerted practices), of the abuse of a dominant position and of State aid respectively. Even though the Treaty does not contain specific rules on mergers, it is to be noted that the case law of the Court of Justice of the European Communities applying what is now Article 101 and Article 102 TFEU to mergers is applicable to the Contracting Parties through Articles 18(2) and 94 of the Treaty. Finally, the lack of a specific Energy Community *acquis* on competition law enforcement (procedure, institutions, sanctions, remedy) is put into perspective by the fact that the Contracting Parties, pursuant to Article 6 of the Treaty, are obliged to ensure efficient implementation of their obligations under the Treaty, of which efficient enforcement of the rules on substance is an important aspect.

Between the three pillars of Energy Community competition policy, the distinction between cartel and abuse prohibition (restricting conduct of undertakings in the first place) on the one hand and State aid prohibition (restricting conduct of the State) on the other hand imposes itself and will be followed throughout this report.

3.4.2 Main findings

Competition and State aid law are of great importance in the energy sectors characterized by natural monopolies, a high degree of concentration and a high level of State intervention. The necessary progress towards full implementation of the electricity and gas *acquis* can only be achieved when competition and State aid law enforcement protect markets from distortion and enable market access by new entrants and foreign competitors. In this respect, the ex-post and case-related control by the competent authorities forms a natural complement to sector-specific regulation. Competition law can also play an important role in combating anti-competitive practices of public undertakings, which are rather common in most Contracting Parties. Besides, there is an obvious need for what is called competition advocacy, namely the review of energy legislation and regulation from a competition law perspective, as well as for comprehensive inquiries of the energy sectors from a competition law perspective. In all these aspects, full implementation of the Treaty relies on active, effective and independent enforcement authorities, as well as efficient procedures and deterring sanctions.

1 As regards Energy Community competition law, legislation transposing the *acquis* is available in all Contracting Parties. Hence, the Contracting Parties in general reached a relatively high degree of transposition, while the effectiveness of implementation/enforcement and the competition culture in general are still at rather different levels. Competition legislation in the Contracting Parties follows more or less closely the EU model based on the three pillars of a cartel prohibition, a prohibition of the abuse of a dominant prohibition and merger control. In terms of cartel prohibition, Contracting Parties increasingly shift to the self-assessment approach underlying the EU enforcement model since 2004.

The increasing alignment in terms of transposition of the competition *acquis* notwithstanding, the situation in the Contracting Parties still differs significantly. Albania is currently revising its competition law. Its competition authority stands out on account of its active involvement in the energy markets in terms of sector inquiries and individual case law. Bosnia and Herzegovina still needs to amend primary legislation to achieve full transposition. The competition authority is active in the energy sectors but, to the Secretariat's knowledge, has never interdicted an activity so far. Croatia reformed its competition law in 2009, thus achieving full compliance with the *acquis*. The competition authority is also very active in the energy sectors. In the Former Yugoslav Republic of Macedonia, the pending reform of competition legislation should achieve transposition of the *acquis*, rectifying existing shortcomings on the enforcement side. The competition authority has been active in energy in the past, but not all decisions would pass legal scrutiny. Moldova, which joined the Energy Community only recently, still needs to adopt a competition law in line with Articles 18 and 19 EnC. The competition authority, however, seems to be more active in the energy sectors than that deficiency might suggest. In Montenegro, both legislation and enforcement are still not in line with the standards required by the *acquis*, in particular as regards the institutional design and procedure. Serbia, through the adoption of a new Competition Law in 2009, now complies with Articles 18 and 19 EnC. First activities of the competition authorities in the gas sector are to be welcomed. In UNMIK, the effectiveness of both the legal framework and its enforcement still raises serious concerns.

2 With regard to State aid control, it must be assumed that non-transparent and selective grants of State aid account for one of the main reasons for market distortion in the energy markets of the Energy Community. In the absence of a central monitoring authority, it is up to each Contracting Party to ensure effective State aid control domestically. In this respect, the approach among the Contracting Parties with State aid legislation in force differs: some tasked the competition authorities, whereas others established government-internal bodies. The former approach seems more apt to ensure independence and effectiveness of enforcement. Key issues in monitoring the implementation of the State aid *acquis* remain transparency and publicity, as information about and access to information about State aid granted and its eventual monitoring does not exist in most Contracting Parties. In this respect, not only the monitoring authorities but also the authorities granting the aid should make available (on websites etc.) more and better information on individual cases. Regardless of the fact that some Contracting Parties seem to have started their State aid monitoring activities in the energy sectors, no objection has ever been raised according to the Secretariat's information.

The achievements made by the Contracting Parties so far differ very much. As of July 2010, three Contracting Parties (Bosnia and Herzegovina, Moldova and UNMIK) still do not have any State aid legislation at all. The Secretariat is currently preparing enforcement action against this evident failure to comply. Albania reportedly improved its legislation in 2009 and started its monitoring activities. Croatia also reported monitoring activities in the energy sector. In the Former Yugoslav Republic of Macedonia, no progress on new State aid legislation has been achieved by July 2010. Cases on State aid monitoring in the energy sectors do not seem to exist. Montenegro recently adopted a new State Aid Law, the effectiveness of which still needs to pass the test. A new State Aid Law in Serbia essentially transposes Article 18 EnC. Monitoring activities in the energy sectors have not yet started.

A study currently performed by the two law firms *Hunton&Williams* and *Eisenberger&Herzog* for the Secretariat will provide more insight with regard to the effectiveness of State aid enforcement in the electricity sector. The study will establish State aid inventories for seven Contracting Parties, and evaluate the effectiveness of State aid control and enforcement in each of them. Results are to be expected in autumn 2010.

3.5 ENVIRONMENT

3.5.1 The acquis on environment

The environmental *acquis communautaire*, as defined in Article 16 of the Treaty, consists of four pieces of legislation, namely (1) Council Directive 85/337/EEC of 27 June 1985 on the assessment of the effects of certain public and private projects on the environment, as amended by Council Directive 97/11/EC of 3 March 1997 and Directive 2003/35/EC of the European Parliament and of the Council of 26 May 2003 (the "Environmental Impact Assessment Directive"); (2) Council Directive 1999/32/EC of 26 April 1999 relating to the reduction in the sulphur content of certain liquid fuels and amending Directive 93/12/EEC (the "Sulphur in Fuels Directive"; (3) Directive 2001/80/EC of the European Parliament and of the Council of 23 October 2001 on the limitation of emissions of certain pollutants into the air from large combustion plants (the "Large Combustion Plants Directive") and (4) Article 4(2) of Directive 79/409/EEC of the Council of 2 April 1979 on the conservation of wild birds (the "Wild Birds Directive"). Besides, the Contracting Parties, under Article 14 of the Treaty, committed themselves to endeavouring to implement Council Directive 96/61/EC of 24 September 1996 concerning integrated pollution prevention and control whereas Article 13 of the Treaty invites the Contracting Parties to accede to the Kyoto Protocol. In general, the environmental *acquis* is applicable only to the extent that network energy is concerned.

According to Annex II to the Treaty, the Environmental Impact Assessment Directive and the Wild Birds Directive were to be implemented upon the entry into force of the Treaty, i.e. by 1 July 2006, whereas the Sulphur in Fuels Directive and the Large Combustion Plants Directive are to be implemented by 31 December 2011 and 31 December 2017, respectively. The present report limits itself to monitoring the implementation of the former two pieces of legislation. In the following, their main features are summarized:

1. The Environmental Impact Assessment Directive aims at identifying and assessing environmental consequences of projects before a building or operation permit is granted. Projects falling within the scope of the Directive are specified in the annexes to the Directive. In terms of network energy, Annexes I and II to the Directive include projects both in energy generation and transmission/distribution as well as gas storage. The key document within the environmental impact assessment procedure is the environmental impact statement to be compiled and submitted by the developer to the competent authorities for review. The procedure itself can be divided into four main parts, namely (1) *screening*, i.e. the determination of whether an environmental impact assessment is required for a specific project covered by Annex I (mandatory) or Annex II (non-mandatory); (2) *scoping*, i.e. the identification of the issues to be covered by the environmental impact study; (3) the elaboration and submission of an *Environmental Impact Study* by the developer; (4) a *review* of the study by the competent authorities and the adoption of an *authorization decision*, before which (domestic) authorities likely to be concerned by the project, the public concerned and other Parties likely to be significantly affected by projects with a trans-boundary impact are to be consulted.

2. The main aim of the Wild Birds Directive is the long-term conservation of all species of naturally occurring wild birds in the territory of the European Union. The Directive focuses on two major issues: the *protection of birds' habitat* and the establishment of *rules for their management, control and exploitation* (hunting, capture, killing and sale). Article 4 of the Directive is a central element in that respect, as it foresees the establishment of a network of *Special Protection Areas* (SPAs) scientifically identified as critical for the survival of particularly vulnerable species of birds listed in Annex I of the Directive. Furthermore, similar measures are envisioned for migratory birds. Article 4(2) in particular requires the establishment of a legal protection regime for *regularly occurring migratory species*, taking into account their areas of breeding, moulting, wintering and their staging posts along the migratory routes.

3. With regard to the Sulphur in Fuels Directive, in March 2010 the Secretariat presented implementation guidelines as an assistance tool for early stocktaking and structuring of the pre-implementation process in order to achieve timely and coordinated implementation by the end of 2011. The Permanent High Level Group agreed to use the guidelines as basis of their pre-implementation activities and invited the Secretariat to take a similar approach with respect to the Large Combustion Plants Directive. The latter was examined at a Secretariat Workshop in 2009; both Directives will be further discussed at a Secretariat Workshop in October 2010. Furthermore, the Secretariat commissioned a study on emissions from power generation in the Energy Community from *SEEC Belgrade*, the results of which are to be expected in October 2010.

3.5.2 Main findings

Regarding the implementation of the Environmental Impact Assessment Directive, it should be noted that domestic legislation often dates back to before the entry into force of the Treaty. Furthermore, the motivation of Contracting Parties for swift implementation is high, given the strong link to investment in particular from public donors. Despite the fact that legislation exists in all Contracting Parties, however, there are still shortcomings to be noted.

1. With regard to environmental impact assessment, legislation in the Contracting Parties basically follows the Directive's model. However, only Croatia and Serbia are close to full transposition, whereas all other Contracting Parties still need to improve the legislative framework both in terms of primary and secondary law. As regards implementation, the Secretariat started to look into individual projects and has provided assistance in that respect.

2. As regards the implementation of Article 4(2) of the Wilds Birds Directive, it must be noted that a coherent and comprehensive monitoring of the implementation of all activities required to protect (migratory) birds is barely possible with respect to the energy sectors alone. Furthermore, obtaining the necessary data and information by the Contracting Parties proves to be rather difficult due to the lack of cooperation in some of them. That said, the Secretariat's assessment indicates that none of the Contracting Parties has achieved the full level of protection of wild birds required by the Directive.

3.6 RENEWABLE ENERGY

3.6.1 The acquis on renewable energy

The requirements regarding the promotion of renewable energy under Article 20 of the Treaty consisted in submitting a plan to the European Commission on how to implement Directives 2001/77/EC and 2003/30/EC. The plans were prepared by all Contracting Parties (except Moldova, which is under an obligation to submit a plan by 31 December 2010). Consequently, the obligation according to Article 20 of the Treaty was considered fulfilled at the Ministerial Council meeting in June 2007.

1. Directive 2001/77/EC fosters the use of electricity produced from renewable energy sources in the internal electricity market with the aim of diversifying and securing energy supplies, increasing environmental protection and providing sustainable development. The Directive requires the adoption of indicative national renewable energy targets to achieve these goals and the introduction of support and certification schemes, streamlined administrative and grid access rules to incentivise the investments in renewable energy projects.

2. Directive 2003/30/EC aims at promoting the use of biofuels or other renewable fuels to replace diesel or petrol for transport purposes, with a view to contributing to objectives such as CO_2 emission reduction and environmentally friendly security of supply. The Directive calls for indicative national targets to be set as reference values of energy content of all diesel and petrol for transport placed on the market, namely 2% by the end of 2005 and 5.75% by the end of 2010. Fulfilment of the targets has to be ensured by different measures, such as public promotion, incentives for production and/or consumption of biofuels and monitoring of the effects of the use of biofuels in diesel blends above 5% by non-adopted vehicles. Monitoring and reporting obligations are also defined.

3.6.2 Main findings

Regarding the status of the implementations of the adopted plans, it has to be noted that the Contracting Parties have started to take steps towards the implementation of the two Directives. However, the progress is not equal and the legal frameworks are not complete in most of the Contracting Parties. The Secretariat continued the monitoring of the achievements in the plans of each Contracting Party.

Following the adoption of Directive 2009/28/EC on the promotion of the use of energy from renewable energy sources in the EU, the Energy Community institutions commenced activities with the ultimate aim of incorporating the new Directive into the Energy Community *acquis*. Directive 2009/28/EC sets an overall EU target of 20% of renewable energy in total final energy consumption by 2020 and introduces cooperation mechanisms to meet the targets for each Member State. The Directive also stipulates that a share of 10% energy from renewable energy sources (biofuels) be used in transport.

At its meeting in June 2009, the Ministerial Council established a Renewable Energy Task Force to assist the work of the Permanent High Level Group in the analysis required for the incorporation of the new Renewable Energy Directive. In March 2009, the Secretariat launched a study aiming at assessing the impact and the modalities of possible inclusion of Directive 2009/28/EC into the Energy Community *acquis*. The study, commissioned to a consortium of IPA *Energy and Water Economics* and *EPU-NTUA* was finalised and published on the Secretariat's website in June 2010.

The study identified that compared to EU-27, the Energy Community Contracting Parties used almost twice as much renewable energy in their total energy consumption in 2005. This is mainly due to the electricity produced by hydro power plants and the traditional use of biomass for heating. Given, however, the problems with regard to the availability of reliable data, inconsistency in data collection and measurement methods across the region related mainly to biomass (wood used in households for heating), mandatory renewable energy targets could not be established. Consequently, the European Commission at this point proposes to the Ministerial Council a recommendation rather than a decision on the implementation of Directive 2009/28/EC in the Energy Community.

1 With regard to electricity produced from renewable energy sources, all of the Contracting Parties have made this one of the top policy priorities in recent years. At the same time, the legal, regulatory and administrative frameworks lack consistency and clarity in pursuing this objective. Most of the flaws may be removed with the adoption of new laws, amendments to existing energy laws, and completion of the secondary legislation which many Contracting Parties currently consider.

Few Contracting Parties have introduced national indicative targets in their legislation; only Croatia, Serbia and UNMIK set such targets. In 2007 Moldova adopted even a 20% RES target for 2020, which will barely be possible to achieve. Albania set an obligation for 2% of the electricity generated from new power production (larger than 100 MW) to come from RES, without setting a proper RES target in accordance with Directive 2001/77/EC. Half of the Contracting Parties have implemented support schemes for electricity produced from renewable energy sources (Croatia, the Former Yugoslav Republic of Macedonia, Serbia, UNMIK) while the others have planned technical assistance to help the adoption of support schemes. Even where good support schemes are in place, the administrative procedures, authorisation rules or grid system access are far from being consistent, correlated or harmonised among all the authorities involved in all the Contracting Parties. The donors expressed concerns about the overall cost increase of financing renewable energy projects in the Contracting Parties due to a lack of streamlined processes hindering investments in the region.

Finally, certification schemes for the electricity produced from renewable energy sources have yet to be implemented in almost all of the Contracting Parties. Most Contracting Parties, however, already assigned issuing bodies for guarantees of origin.

2 With regard to biofuels, the realisation of the adopted plans varies greatly among the Contracting Parties. Only two Contracting Parties have adopted appropriate legislation (Albania, Croatia), a majority set at least the targets (Former Yugoslav Republic of Macedonia, Serbia, UNMIK and even Moldova), and two Contracting Parties did not make significant progress since 2007 (Bosnia and Herzegovina and Montenegro).

Setting the targets is a first step. More important and demanding activities are related to the establishment of measures aimed to reach these targets. In this regard, it can generally be stated that almost all Contracting Parties are at the very beginning of the implementation of Directive 2003/30/EC. Even Croatia, the most advanced Contracting Party with regard to biofuels, has to further develop the existing measures and make a greater effort regarding the promotion of biofuels and the fulfilment of the targets.

It has to be underlined that the implementation of Directive 2003/30/EC should be used to develop domestic potential with regard to biofuels production rather than just as a framework for the import of and trade in biofuels. A proper implementation, beneficial to all Contracting Parties, requires good and timely cooperation between different stakeholders, especially authorities responsible for energy, economy, environment, agriculture, transport and fiscal policies.

Directive 2009/28/EC upgrades Directive 2003/30/EC as it introduces sustainability criteria for biofuels and defines a target of 10% of energy content for all diesel and petrol for transport placed on the market by 2020. The provisions on promotion, incentive measures, monitoring and reporting, however, are already stipulated by Directive 2003/30/EC.

3.7 ENERGY EFFICIENCY

3.7.1 The acquis on energy efficiency

At the meeting on 18 December 2009, the Ministerial Council adopted Decision 2009/05/MC-EnC on the implementation of certain directives on end-use energy efficiency, namely Directive 2006/32/EC on energy end-use efficiency and energy services, Directive 2002/91/EC on the energy performance of buildings and Directive 92/75/EEC (as well as the Implementing Directives) on the indication by labelling and standard product information of the consumption of energy and other resources by household appliances. In May 2010, a recast of Directives 92/75/EEC and 2002/91/EC was adopted within the European Union. The Energy Community Ministerial Council is expected to adopt the recast Directives in September 2010.

The overall deadline for the transposition of Directives 2006/31/EC, 2002/91/EC and 92/75/EEC is 31 December 2011, except for the National Energy Efficiency Action Plans (NEEAP), where a first NEEAP is to be prepared no later than 30 June 2010; a second NEEAP no later than 30 June 2013 and a third NEEAP no later than 30 June 2016.

3.7.2 Main findings

The work of the Secretariat in the area of energy efficiency was strongly backed up by the work of the Energy Efficiency Task Force established in 2008. The Task Force's four tasks focus on the implementation of the adopted energy efficiency *acquis*, namely:

- Finalization of the first National Energy Efficiency Action Plans;
- Monitoring of the implementation of the NEEAPs;
- Preparation of a road map for transposition and implementation of Directive 2006/32/EC, Directive 2002/91/EC, Directive 92/75/EEC and the associated Implementing Directives;
- Implementation of a communication and awareness raising campaign plan.

In order to enhance the work in this area, the Contracting Parties' members of the Task Force (with the exception of Bosnia and Herzegovina) prepared road maps in the second quarter of 2010, which improves confidence that the transposition and the implementation is progressing and will be monitored and reported to the Secretariat regularly.

The Contracting Parties are also in the process of finalization of the first NEEAPs, as well as preparation of a label design (translated into the respective official languages). The Secretariat reviewed the draft NEEAPs and the draft road maps and made recommendations on how to improve these in order to be in compliance with the Directives.

The Contracting Parties are currently at different stages of transposition and implementation of the *acquis*. Regarding primary legislation, Croatia is most advanced, followed by Montenegro which adopted its Energy Efficiency Law in April 2010. Albania, the Former Yugoslav Republic of Macedonia, Serbia and UNMIK have laws in the drafting phase that are expected to transpose the Directives. However, in Bosnia and Herzegovina no progress is visible.

During 2010 and beyond, efforts will have to be made to fully transpose the Directives and implement the NEEAPs, using the technical assistance and the funds made available by the international financial institutions through different regional initiatives and also using best practices from EU Member States.

3.8 SOCIAL ISSUES

3.8.1 The social acquis

The Treaty does not foresee the adoption of a specifically defined set of social *acquis*. However, several articles from various other energy directives that are part of the *acquis* indicate the importance of the social dimension in the context of the energy sector reforms.

While the Treaty's core objective is to lay the foundations for a successful reform of the energy sector that will increase market efficiency and will contribute to the improvement of living and working conditions of the people, it is acknowledged that this may also have an impact on energy affordability, especially for vulnerable residential costumers, in the transition phase.

Therefore, and in order to complement the Treaty, in October 2007 the Contracting Parties signed the Memorandum of Understanding on Social Issues in the Context of the Energy Community. The Memorandum indicates the political intent of the signatories to take due account of the social dimension, and outlines the principles and the context for a social dialogue in the energy sector at both the national and regional levels.

Moreover, the Ministerial Council at its meeting in December 2007 decided that the Energy Community shall organize a Social Forum every year, as a platform for discussion of the progress with the implementation of the Memorandum.

3.8.2 Main findings

Based on the Memorandum of Understanding on Social Issues, all Contracting Parties - with the exception of Moldova that only joined the Energy Community in May 2010 - have prepared Social Action Plans and have started to transpose some EU *acquis* on social aspects into their national legislation. Moldova will follow with the same approach.

The main areas of the Social Action Plans include:

- *Public Service Obligations:* Focusing attention on vulnerable customers,
- *Social Partners:* Promoting the social dialogue with the social partner,
- *Management of Change:* Promoting the development of specific employment, training and support services, and
- *Social Dimension,* with a focus on the following key areas: workers' fundamental rights; improved working conditions and standards of living; improved working environment with respect to the health and safety of workers; equal opportunities.

The most beneficial result of the Plans is the creation of a platform (plans and working groups) that would allow further and stronger cooperation of multiple stakeholders, including the social partners.

On the other side, a common characteristic of the Plans seems to be a too general approach to implementation through concrete activities, and an overoptimistic timeframe.

The treatment of vulnerable household customers remains a key topic for discussion throughout the region. Appropriate mechanisms are so far broadly missing in the Social Action Plans, with the exception of the Former Yugoslav Republic of Macedonia and (partly) also Moldova. Vulnerable customer groups exposed to potential energy poverty are to a large extent supported via regulated gas and electricity prices, which are questionable in the approach applied by the Contracting Parties.

4

INVESTEMENT REPORT

A NEW APPROACH

PROGRESS WITH INFRASTRUCTURE INVESTMENTS IN THE ENERGY COMMUNITY

CONCLUSIONS

4. INVESTMENT REPORT

4.1 A NEW APPROACH

The Treaty establishing the Energy Community places emphasis on the issue of investments in energy infrastructure. Article 2 highlights the need to *"create a stable regulatory and market framework capable of attracting investment in gas networks, power generation, and transmission and distribution networks, so that all Parties have access to the stable and continuous energy supply that is essential for economic development and social stability..."*.

Against this background, in December 2007 the Ministerial Council endorsed a list of priority investment projects to be monitored by the Secretariat. The Secretariat reported at the following two Ministerial Council meetings on the progress of these projects, as well as on the actions undertaken to facilitate the investment process.

In spite of the prioritization proposed by the Contracting Parties with the assistance of the Secretariat, some of the projects did not make enough progress between 2007-2009 to justify their priority status. In parallel, new investments appeared to be more actively pursued by the Contracting Parties.

One of the reasons for the slowdown in investments was that the financing environment was getting tougher, the final demand for energy was weakening and the cash flows were falling. The energy supply infrastructure was affected by the financial and economic crisis in several ways. Firstly, energy companies find it more difficult to obtain loans for both ongoing operations and new projects; in some cases, the cost of capital has risen in absolute terms, making marginal investments uneconomic. Secondly, profitability of new power generation investments has become lower. Thirdly, there is less need for capacity with the falling demand for energy caused by the economic downturn.

Based on discussions in the Permanent High Level Group and Ministerial Council meetings in December 2009, as well as in the Permanent High Level Group meeting in March 2010, a much more focused priority projects list was identified, with a more concrete approach towards implementation. The approach proposed includes the identification of a maximum of ten projects from both the gas and electricity sectors, based on the following criteria:

- Increased security of energy supply to customers as well as safety/reliability of the energy networks;
- Contribution to the development of the regional, competitive electricity and gas market;
- Importance for electricity interconnection and trade;
- Importance for the gasification of the Energy Community (pipelines) and merits as new gas anchor loads are needed for further gasification;
- Listed as priority in the SECI project transmission planning or the UCTE/ENTSO reports, the GIS study, etc.;
- Link with other regional interconnections (gas and electricity) already being built;
- Maturity status;
- Contribution to reduce congestion in electricity;
- Contribution to improving the environmental conditions in the energy sector.

For the projects thus identified, joint meetings between the project sponsors (companies), the donors' community (chaired by the European Commission) and the Secretariat are organized, possible obstacles in financing and project implementation are identified and solutions to remove these are sounded out and implemented together with the actors involved. The Secretariat will in each case follow up the progress and report to the donors' community and the Permanent High Level Group.

4.2 PROGRESS WITH INFRASTRUCTURE INVESTMENTS IN THE ENERGY COMMUNITY

4.2.1 Electricity infrastructure

The priority projects selected so far are:

1 Interconnection between the Former Yugoslav Republic of Macedonia and Albania

A 400 kV OHL interconnection between Bitola (Former Yugoslav Republic of Macedonia) and Elbasan (Albania) was proposed by both transmission system operators and the respective ministries responsible for energy. The main benefits of building the interconnection included the creation of regional trading opportunities, whereby economic exchange of power among the countries can take place, reserve capacity sharing (which will also contribute to a better security of supply of both power systems faced with capacity shortage), emergency support in case of power shortage and higher reliability of system operation. The project requires the construction of approximately 128 km of 400 kV OHL, of which 65 km is in the Former Yugoslav Republic of Macedonia and 63 km is in Albania. The estimated cost is around € 30 million.

In April 2010, the Secretariat organized in Vienna a joint meeting between representatives of the two transmission system operators: *OST* (Albania) and *MEPSO* (Former Yugoslav Republic of Macedonia), the EBRD and the European Commission. Both TSOs re-confirmed their interest in the investment and continuation of joint activities. Both EBRD and KfW expressed interest in financing the investment if the feasibility study shows that the investment is economically valid. Milestones jointly agreed comprise an update of the feasibility study made in 2007 including an environmental and social impact assessment study possibly financed by the Western Balkans Investment Framework: the studies are expected to be finalized during the fourth quarter of 2011. EBRD and KfW expressed interest in financing of the interconnection, including substation facilities.

2 Interconnection between Serbia and Romania

A new 400 kV OHL interconnection between Pancevo (Serbia, 55 km) and Resita (Romania, 80 km) was proposed by both transmission system operators. A system study conducted in 2007 proposed three options to be further investigated. The estimated cost is at € 22 million on the Serbian side and € 37 million on the Romanian side. In Serbia, a feasibility study was prepared at the end of 2009. A preliminary design study and an environmental and social impact assessment study are expected to be finished in September 2010. In Romania, *Transelectrica* commissioned a feasibility study, the deadline for which is October 2010. In March 2010, both TSOs decided on the cross-border point and other technical details.

In order to facilitate the progress, in June 2010 the Secretariat organised a meeting between representatives of the two transmission system operators, *Transelectrica* (Romania) and *EMS* (Serbia), with the participation of the European Commission and EBRD to discuss the current status of the project and future action. The milestones jointly agreed by the stakeholders include that the Romanian TSO will apply for structural funds under the electricity interconnection window by the third quarter of 2010 and that a new joint meeting will take place once the two feasibility studies are final. EBRD expressed interest in financing this interconnection.

3 New generation capacity HPP *Zhur* in UNMIK

This hydropower plant was presented as a priority project in 2008. The HPP has a planned installed capacity of 305 MW and is expected to be developed with a private investor. The estimated investment cost is € 330 million. The commissioning term is 2015. Kosovo pursuant to UNSCR 1244 is currently importing approx 8% of its consumption and bases its domestic production largely on two lignite fired power plants requiring major retrofit and life extension. Therefore, a new HPP will not only contribute to the power balance, but also improve the power generation energy mix using renewable energy. The HPP will be utilized as a peak load plant with large storage capacity; this will offer flexibility and reliability in UNMIK and the region.

The World Bank provided financing for the review of the project pre-feasibility study and pre-environmental and social impact assessment study in June 2009. In June 2010, the Ministry of Energy and Mining announced a Call for Interest for HPP *Zhur* and tendering procedures for transaction advisors.

After the tender has been launched and the responses from investors will have been received, the Secretariat will advise the authorities on the potential contentious issues which may not be in line with the Energy Community *acquis*. Tentatively in the third quarter of 2010, the Secretariat will organise a joint meeting with the company and the respective Ministry representatives involved, the IFIs and the European Commission to discuss the results of the expression of interest and the possible bottlenecks.

4.2.2 Gas Infrastructure

In the case of gas infrastructure, a regional approach to investments is a key, as countries planning to rely on gas-fired power generation capacity need to be confident that neighbouring countries also follow this regional priority, rather than pursuing self-sufficiency through non-gas power generation. The large investments required by gas transmission systems will not be justified in the absence of a sufficient base load (anchor loads). The 2009 South-East Europe: Regional Gasification Study, financed jointly by the World Bank and the German KfW, proposed the concept of an "Energy Community Gas Ring". The Energy Community Gas Ring would link currently ungasified areas with mature gas markets, facilitating supply diversity and providing favourable prospects for security of supply, including through providing access to regional underground storage facilities.

In December 2009, the Secretariat organized a donors' meeting with the aim of drawing attention to three gas infrastructure projects of regional value and of interest for the Energy Community Gas Ring:

1 Interconnection Serbia and Bulgaria

To facilitate the project to interconnect Serbia (Nis–Dimitrovgrad) and Bulgaria (Sofia/Dupnica), a first meeting took place in December 2009. A second meeting in January 2010 was attended by representatives from *Srbijagas, Bulgartransgaz,* the Ministry of Economy, Energy and Tourism and the Ministry of Regional Development and Public Works (Bulgaria), the EBRD, EIB/JASPERS, the European Commission, and the Secretariat. In March 2010, a joint statement was signed by the energy ministers of the two countries, expressing the will to realise the project. In May 2010, the first meeting of the working group, established by *Srbijagas* and *Bulgartransgaz* took place to discuss technical aspects of the interconnector.

At these meetings the preparation of solid feasibility studies for both sides of the interconnector was identified as a priority action. In March 2010, *Srbjiagas* submitted an application for a feasibility study to the Western Balkans Investment Framework which was approved in June 2010. *Bulgartransgaz* will apply for funding of the study from other sources open to EU Member States. *Bulgartransgaz* already received structural funds approved by DG REGIO for the Bulgarian side of the interconnector. The Parties involved have also proposed a timetable for further activities under the project.

2 Ionian Adriatic Pipeline (IAP)

The IAP is foreseen to run from Croatia (Ploce) to Albania (Fieri) with a diameter of 800-1000 mm/ and a pressure of 75 bar with reversed flow capability from north to south. The IAP will be part of the Gas Ring once this will be constructed. Two versions of the IAP are being analyzed. The first version includes a section in Croatia with a DN 500 mm and 2.5 bcm/y capacity, a section in Montenegro of DN 700 and in Albania of DN750, with a joint capacity of 5.0 bcm/y. This option will cost around € 0.9 billion. The second version foresees a single DN 800 pipeline from Croatia (Bosiljevo) to Albania (Fieri) with a total capacity of 7 bcm/a, of which 4.5 bcm/a are in Croatia and Montenegro. The cost is estimated at approx. € 1 billion.

An Intergovernmental Declaration for IAP was initially signed by Albania, Croatia and Montenegro in September 2007. In December 2008, Bosnia and Herzegovina signed the Declaration as well. A Memorandum of Understanding on the implementation of this project between the Swiss company *EGL* and *Plinacro* of Croatia was also signed in September 2007.

In Croatia, several sections of the network, which may become part of the IAP, are in progress. The pipeline Bosiljevo–Split with a capacity of 5 bcm/y is being built; the section up to Split is under construction. The pipeline is financed by *Plinacro* through an EIB loan as part of the investment plan 2007-2011, and its own funds. Furthermore, in 2008, the pre-feasibility study for the entire IAP was completed. The hydraulic study and cost comparison for the section Bosiljevo-Split-Ploce was finished in 2009. For the section Ploče–Dobreč (at the Montenegro border), studies on routing, mapping, spatial planning documentation, geology survey and hydrology survey were also performed.

The Secretariat organized a meeting in Zagreb in March 2010, attended by representatives of the European Commission, *Plinacro*, EBRD and the Secretariat; at which the plans of the signatories of the Intergovernmental Declaration for IAP were assessed. In April 2010, a questionnaire which was sent to Albania, Bosnia and Herzegovina, Croatia and Montenegro included questions related to these Contracting Parties' plans to develop the IAP pipeline on their respective territories, as well as their plans to gasify these and build potential gas anchor loads. A second meeting in June 2010 involved representatives of Albania, Bosnia and Herzegovina and Croatia, the European Commission and the Secretariat. Further milestones include the preparation of a comprehensive feasibility study to include all signatories' markets, a strategic environmental impact assessment; to set up an interstate committee steering the project and the evaluation of the findings of a gas market study commissioned by *Plinacro*.

3 LNG terminal in Croatia

The project is located on the island of Krk in Croatia, on an unused petrochemical site. Its re-gasification capacity is 10 to 15bcm/year and it is planned to be started in 2014. The structure of the shareholders' consortium is *E.on Ruhrgas, OMV, Total, Geoplin* with 75% and Croatian companies (reserved) with 25%. In June 2010, Croatia announced the establishment of *LNG Hrvatska* (with *Plinacro* and *HEP* as equal shareholders) participating with 11% in the consortium; while *INA* has to decide on its 14% share independently of the Croatian authorities. In 2009, the project company finalized the environmental and social impact assessment study and held public consultations. Croatia granted it the status of a project of State interest.

In order to facilitate implementation of the project, the Secretariat organized a meeting in March 2010 attended by representatives of the Adria *LNG* company, EBRD, the European Commission and the Secretariat. At this meeting, it was agreed that the Croatian authorities need to prepare a new Grid Code for gas quality that would allow the re-gasified LNG to be used on the Croatian market. The transmission system operators of Croatia and Slovenia, *Plinacro* and *Geoplin Plinovodi*, established a working group to prepare a proposal for relevant changes of the Network Rules, ensuring access and transmission of gas with a wider scope of characteristics, i.e. gas from different sources re-gasified at the terminal. The working group is expected to deliver a proposal before summer 2010 for comments to the Secretariat. The Secretariat will also organize a second meeting related to the LNG Krk project in the second half of 2010.

4.3 Conclusions

Based on the meetings held so far, the following conclusions on the main barriers to investments may be drawn:

- Incumbent companies appear to be genuinely interested in investments but clearly lack the financial means to engage in large scale investments. International financing institutions are in many cases interested in financing, but the companies' creditworthiness or their borrowing capacity based on their current debt levels is fairly low;
- The governments' preferred model for investments appears to be through tendering procedures, for which in almost all legal frameworks provisions exist. Under the *acquis* the tendering for new capacity should be used only if an authorization procedure is not enough to achieve the investments;
- The tenders do not always go as smoothly as planned, and reasons for this include the lengthy preparation of project documentation (pre-feasibility study, feasibility study, environmental impact assessment, strategic environmental assessment, etc). Often, by the time this is approved, the figures are no longer valid and an update is needed. Moreover, the model of communication and decision-making, mainly in the case of interconnections appears to be "stop and go" with large time gaps between individual phases. Finally, the tender documentation is frequently not well enough prepared which leads to very lengthy and sometimes unsuccessful tenders.
- The treatment of CO_2 emissions is not clear within the Energy Community. This raises many concerns with regard to coal-fired power plants;
- The regulatory framework, although in progress, is not fully in line with the *acquis* especially with regards to capacity allocation and third party access;
- In some Contracting Parties there are still import and export fees on energy that together with the treatment of VAT interfere with trade and make energy more expensive;
- The treatment (incentives) of investments done by one TSO in another country is not clear and hence should be further discussed. An ECRB paper in this respect was prepared and was presented at the PHLG meeting in June 2010, as a starting point for future relevant discussions.

The Secretariat will continue its assistance to the Contracting Parties to remove some of the barriers mentioned above by regular follow-up meetings on all projects, monitoring the progress and signalling delays or bottlenecks, working with the Contracting Parties to better prepare applications for technical assistance, with an emphasis on the Western Balkan Investment Fund, working with the donors' community to identify the best source of financing for each project, reviewing the tender documentation for compliance with the *acquis* prior to its public announcement based on the request by the Contracting Parties, regular monitoring of the implementation of the Treaty, and taking enforcement action against instances of non-compliance hindering the advancement of investments.

5

IMPLEMENTATION OF THE ACQUIS IN THE CONTRACTING PARTIES

ALBANIA

BOSNIA AND HERZEGOVINA

CROATIA

FORMER YUGOSLAV REPUBLIC OF MACEDONIA

MOLDOVA

MONTENEGRO

SERBIA

UNMIK

5. IMPLEMENTATION OF THE ACQUIS IN THE CONTRACTING PARTIES

5.1 ALBANIA

5.1.1 Electricity

a. Electricity in Albania

The unbundling of the electricity system of Albania reached its current status in 2008, resulting in three separate legal entities – the national transmission system and market Operator *OST*, the national distribution system operator and retail public supply company *OSSH* and the incumbent generation company *KESH*, which at the same time performs the role of the wholesale public supplier under the market model. In 2009, Albania sold 76% of its shares in *OSSH* to the Czech energy utility *CEZ*. The electricity sector operates under the regulatory supervision of the Energy Regulatory Authority (ERE), established in 1995.

The reliability of the electricity system in Albania remains fragile. As much as 98% of the domestic electricity generation is produced in hydropower plants and is largely dependent on hydrological conditions. After the severe drought in 2007, which drove imports to above 50% of consumption in addition to 17% of load shedding, the supply has gradually improved reaching the level of 12% of imports in 2009. The overall consumption of 6.6 TWh is partially covered by the domestic production of 4.5 TWh on average. The oil/gas-fired TPP Vlore of 97 MW installed capacity will provide a moderate contribution to the overall hydro capacity of 1.446 MW

Another challenge to the electricity supply is the level of losses in the distribution system of up to 34% (17% are recognized by ERE and included in the tariff) which, together with the average collection rate of 76%, brings the overall efficiency of payment close to 50%. In practical terms the DSO is compelled to import electricity on the level of 2.0 TWh annually only in order to cover the losses.

The interconnection of the electricity system of Albania with the neighbouring systems (of 400 kV with Greece and of 220 kV with Montenegro and UNMIK) is barely sufficient to provide for operational security. Over the last several years Albania has been struggling to fulfil the conditions for UCTE membership.

The electricity sector in Albania operates under the Power Sector Law of 2003, as revised and amended in 2008, along with the Law on Energy of 1995 and the Law on Regulation of the Electricity Sector of 1995. A set of regulatory rules has been adopted and applied by ERE, including the Grid Code and Market Rules, as well as main tariff methodologies for transmission, distribution, public generation and sales to captive customers.

Pursuant to a Decision by ERE, since December 2007 all customers except household customers are granted the status of eligible customers. In practice, however, there have been only two active eligible customers who have accessed the market. There are eight registered traders, out of which six are also licensed as qualified retail suppliers for eligible customers.

b. Progress made in 2009/2010

In late 2008 a set of amendments to the Power Sector Law, Market Rules and Grid Code were implemented along with other regulatory measures aimed to consolidate the investment climate and electricity supply conditions in Albania, and to carry out the privatization of the distribution company *OSSH*. As a part of the transaction package, a regulatory statement was issued by ERE supporting a gradual decrease of losses from the level of 32% (2008) by a total of 17% over the following three regulatory periods starting with 2010, in order to reach the targeted level of 15% losses to be recognized by ERE at the end of 2014. The new level of tariffs (2010) including a re-assessment of the level of losses and treatment of bad debts in the regulated asset base are currently the basis for a dispute (lawsuit) between *OSSH/ CEZ* and ERE.

The share purchase transaction for the privatization was completed in 2009. The new majority shareholder *CEZ* committed to reduce the level of technical and non-technical losses to 15% during the first five years of operation by means of investments of approximately € 200 million.

The distribution system operator started a programme to increase the collection rate and the results are reported as promising. Also, the installation of meters in the distribution network has advanced – no meters are missing and no collective metering is applied any more. Within its master plan for investments the new owner initiated a set of measures for diversification of energy sources, construction of new renewable capacities (small HPPs) and energy efficiency measures.

The overall market structure enforced in 2008 included a transitory market model designed primarily to improve the hampered electricity supply and increase the security in an environment of deficient generation and approaching privatization. Currently, there are endeavours to move ahead with the development of the legal and regulatory framework in 2010 and 2011. The Ministry of Economy, Trade and Energy is considering bringing the Power Sector Law to full compliance with the *acquis* related to electricity, eventually including the Third Internal Market Energy Package, and upgrading the market model. An expert team of representatives from relevant authorities in the electricity sector has been appointed and the initial draft proposal for a new law is soon expected. Further steps should include the collection of comments from the stakeholders and from the Secretariat.

The market model is subject to consideration by ERE as well, targeting in the first place improved access to the electricity market, increased number of public suppliers and applicable switching platform. Feasible options are being considered for gradual reduction of the market share of the wholesale public supplier and the implementation of customer switching procedures based on the existing metering system.

Regarding the implementation of security of supply measures, Albania has been moving towards its targets identified in the updated Security of Supply Statement. Main policy targets include an improvement of the investment climate, attraction of investments in new generation capacities and an increase of the electricity system efficiency. New infrastructure projects in power generation have been contracted to ensure future additional generation capacities. A new 400 kV OHL transmission line for interconnection with Montenegro is in advanced stages of development, a similar OHL interconnection is financially supported by KfW, the new dispatch centre is under construction and the SCADA system is in the final stage of development. Other new transmission projects are contemplated, which should significantly consolidate the supply conditions in Albania and support the electricity trade in the neighbouring region.

c. State of compliance

The legal and regulatory framework related to the electricity sector of Albania has undergone significant developments over the past few years and the structural reforms in the electricity sector have been continuously advancing.

Some intrinsic obstacles for faster progress in the implementation of the *acquis* could be located in the inherited low level of payment discipline and insufficient or inadequate metering, an inadequate generation structure and relatively low reliability of the base load and an underdeveloped transmission infrastructure. The country's struggle to give priority to these issues and its substantial effort for attracting investments aimed to compensate such shortcomings has started to yield results and finally allowed the development policy to be placed on the right track.

However, Albania still needs to undertake substantial steps in several areas in order to bring it to the level of full compliance.

The main focus of the reforms in the forthcoming period needs to be set on further development of the market model. ERE needs to take a proactive role in the revision of the existing market structure and to reconsider the wholesale public supplier function within the incumbent generation company in order to allow further opening of the market. The existing option for eligible customers to remain supplied under regulated tariffs that are not fully cost-reflective, and the lack of transmission capacity released to the market are among the main factors impeding the effective market opening. In addition, further unbundling of accounts for supply activities from distribution system operation and between supply to eligible and non-eligible customers in the distribution company *OSSH* still needs to be done.

Although Albania actively participates in the project for establishment of a Coordinated Auction Office in South-East Europe, the applied criteria do not completely reflect the applicable level of compliance. In practical terms, there are reserved capacities on the existing interconnections to the benefit of the wholesale public supplier (25%) and the retail public supplier (50%), leaving only 25% for the market according to the Market Rules approved by ERE in June 2008. Although ERE can revise the reservation clause every year in November, in 2009 it has not used this option. Such capacity reservations contravene the non-discrimination principle in Directive 2003/54/EC and need to be reconsidered and abolished; transmission capacity on interconnections needs to be allocated on market based procedures. *OST* has to develop the rules on capacity allocations in compliance with Regulation 1228/2003.

Network tariffs are supposed to become cost reflective and to allow for a proper return on capital of the needed investments to increase the security of electricity supply and to provide integration of new renewable energy projects.

The TSO position has to be strengthened further. It has to perform all its duties as one of the institutional pillars of the electricity market. No significant progress could be registered related to compliance with Regulation 1228/2003. The power of ERE to monitor and to steer the change of the existing non-compliant rules still needs to be enforced. Publication of information on interconnection capacities (as requested in Article 5 of Regulation 1228/2003 and Point 5 of its Annex) has not yet taken place. The required transparency of information for the access to cross-border capacities has to be ensured by *OST* and monitored by ERE. In addition, the published documents of ERE do not provide evidence of the TSO's compliance with requirements related to the congestion management method and its monitoring (as required in Point 1(10) of the Annex to Regulation 1228/2003). Balancing procedures and consideration of ancillary services costs still require more work to be done.

There has been no significant progress in the past amendments of the Power Sector Law with respect to transposition of Directive 2005/89/EC. Although some of the provisions are practically applied, it is still necessary to apply a more systematic transposition and enforcement in the legal framework.

5.1.2 Gas

a. Gas in Albania

The commercial production and consumption of natural gas in Albania started in the 1960s. During the 1980s, gas production peaked at almost 1 bcm and since then has decreased to 0.01 bcm. Gas, which was used in the past mainly in the industrial sector (but never in the household sector) is currently used only for technological purposes (i.e. oil production and refining (on-site facilities). Space heating uses mainly electricity and LPG. It must be concluded for these reasons that today Albania is one of currently three Contracting Parties without a gas market.

Nevertheless, the Natural Gas Sector Law, in force since June 2008, has transposed almost the entire Directive 2003/55/EC.

b. Progress made in 2009/2010

After the adoption of the Natural Gas Sector Law, Albania has followed-up very actively with the development of secondary legislation. The following items are under preparation: the *Natural Gas Sector Rules and Procedures on Licensing, Modification, Partial/Full Transfer and Renewal of Licenses; Regulation on Procedures for Licensees Assets Transfer; Regulations Pertaining to the Refusal of Third-Party Access to Natural Gas Systems and Derogations in Relation to Take-or-Pay Commitments.* All drafts have been discussed in detail with the Secretariat. The same goes for the gas market model.

c. State of compliance

The main principles of Directive 2003/55/EC have been transposed by the Natural Gas Sector Law.

However, the provisions on market opening are not in line with the Treaty. Instead of making all non-household customers eligible, eligibility is still determined by the type (generation of electricity and heat) and level of consumption (as defined by the national regulatory authority ERE). If the rules on market opening were brought in line with the Treaty, the legal background for an initial development of the gas market would be properly set. Furthermore, non-compliance with respect to market opening can be rectified relatively easily and quickly, by an ERE decision according to Article 38 of the Law in force (*"In setting the amount of natural gas consumed during a year for the status of eligible customer, ERE shall take into consideration the technical possibilities of the natural gas system and the international commitments of Albania"*).

Most of the provisions of Regulation 1775/2005 have been transposed by the Law (third-party access, tariffs, balancing, congestion management and capacity allocation, some transparency requirements). Further progress in its implementation should be made in line with the gas infrastructure development.

Security of supply is defined by the Natural Gas Sector Law in line with Articles 5 and 26 of Directive 2003/55/EC. Directive 2004/67/EC, however, has not yet been transposed. This must be further considered in line with the gas market development.

5.1.3 Oil

a. Oil in Albania

Exploration of hydrocarbons in Albania commenced before World War II. Many important oil fields in lime- and sandstone have been discovered since then. Albania has produced around 52 million tons during that time, while the remaining oil in place is estimated at around 380 million tons. The current oil production is around 580,000 tons/year.

So far, Albania has not been dependent on crude oil. The country has recently started to import crude oil for further processing in the refineries. Two refineries exist in Albania. They were privatized in August 2008 and sold to AMRA Oil which owns 85% of the shares of ARMO, a former state-owned company. Meanwhile 15% of shares remain with the Albanian government represented by the Ministry of Economy, Trade and Energy. The total nameplate capacity is 1.5 million tons/year. The refineries provide more than 10 types of products for the Albanian market and the region. The tank farm consists of approximately 214,000 m3 of crude oil, half-products and finished products. Furthermore, seven over-the-ground reservoirs with a storage capacity of 35,000 m3 exist in the Vlore Import-Export Branch. ARMO satisfies the demand for almost 50% of the oil products in the country, whereas its market share for gasoil is at approximately 25%. It is also the sole market supplier of bitumen. The refinery sector has approximately 1,600 employees.

Albania is currently not connected to any international oil pipeline. Two oil terminals exist in Vlore Bay (with a capacity of 89,000 m3) and in Porto Romano-Durres (with a capacity of 80 000 m3).

There are 164 private companies operating in the wholesale and around 1,035 operating in the retail oil market. The policy on petroleum products pricing is determined by the government which can impose temporary restrictions on maximum or minimum retail prices. Such intervention has not taken place so far.

The Petroleum Law governing the organization and functioning of the oil sector in Albania dates back to 1993. In 1994, the Law on the Fiscal System in the Hydrocarbons Sector (Exploration/Production) was adopted. Processing, transporting and trading of oil and petroleum products is governed by the Law on Refining, Transportation and Trading of Oil, Gas and their By-Products of 1999. The same Law also covers the maintenance, management and reporting of crude oil and petroleum product stocks. Additionally, a Council Minister Decision of 2004 also deals with the maintenance and management of emergency stock for oil, gas and their products. From 2007 until 2010, emergency stocks have remained at the same level equivalent to the average sales of 60 days. As of 2010, the security reserve will equal the average sales of 90 days.

b. Progress made in 2009/2010

In terms of exploration, Albania signed a production sharing contract for Block ‚F' with *Bankers Petroleum* in April 2010 for a seven-year term with three exploration periods. Another seven-year production sharing contract covering three exploration blocks was signed with *Sky Petroleum* in June 2010. The PSC has three exploration periods. Furthermore, a consultancy contract to advise the sale of *Albpetrol* was signed with Washington-based law firm *Patton Boggs* in June 2010. Consultancy services will include due diligence on *Albpetrol*, the proposal of a privatization method and international marketing during the privatization period. Finally, a development plan with the Canadian firm *Stream Oil and Gas* was signed in April 2010. The project concerns the re-activation and re-development of three oil fields and a gas/condensate field in Albania.

c. State of compliance

With regard to Article 41 EnC, the market of crude oil and petroleum products can be considered open to private and foreign companies. There is no preference given to domestic oil and petroleum products over non-domestic ones. Local companies are treated no different than foreign companies vis-à-vis taxation.

However, Albania levies a customs duty of 10% on the import/export of crude oil. Even though the main petroleum products such as gasoline, diesel and fuel oil are not subject to customs duty; such duty is levied on some petroleum products which do not have a large consumption in the country like aviation gasoline and kerosene-type jet fuel with 10%, lubricants from 2% to 10%, bitumen 10% and coke 2%. These customs duties are in violation of Article 41 EnC and need to be removed.

5.1.4 Competition

a. Competition and State aid in Albania

1 Competition law in Albania is governed by the Law on Competition Protection of 2003. The Law provides for a *prohibition of cartels* with possible (individual) exemptions to be granted *inter alia* for horizontal and vertical agreements. Exemptions depend on prior notification of the competent authority. Block exemptions do not exist. The Law also stipulates a *prohibition of the abuse of dominant positions*. A separate provision defines criteria for the establishment of dominance. The Law further equates *"public and local administration bodies, as well as public authorities and entities"* with undertakings to the extent they *"engage in economic activity"*.

The authority enforcing the Law on Competition Protection is the Competition Authority (ACA). ACA is independent and consists of the Commission as the decision-making body and the Secretariat as the supporting body with monitoring and investigating functions. The Law further establishes procedural rules as *lex specialist* to general administrative law. The Competition Authority may impose fines in the range of 2% to 10% of the annual turnover for infringements. The Competition Authority has adopted EC Regulations 1/2003 and 773/2004 as by-laws.

2 State aid control in Albania is governed by the Law on State Aid in force since 2006 and amended in October 2009. The Law stipulates a prohibition in principle of State aid along the lines of Article 107(1) TFEU. The Law covers aid granted to both private and public undertakings. The aid does not necessarily have to affect trade between Contracting Parties within the meaning of Article 18(1) of the Treaty. Per se exemptions apply to aid mentioned in Article 107(2) TFEU. Aid corresponding to the list in Article 107(3) TFEU, regional aid and aid for undertakings faced with difficulties may be exempted from the general prohibition. Furthermore, regulations on regional aid and rescue and restructuring aid have been adopted. In 2008, secondary legislation concerning horizontal aid and guidelines on aid in the form of compensation for public services has been adopted. Additionally, secondary legislation concerning, inter alia, environmental aid was adopted in June 2009.

As regards enforcement of state aid Law, the Law establishes the State Aid Commission (SAC) as an *"operationally independent"* decision-making body. The chairman of that Commission, which is comprised of five members, is the Minister for Economic Affairs. The other members are appointed by the Council of Ministers. The Commission is supported by a State Aid Department within the Ministry of Economy, Trade and Energy which in particular drafts decisions and guidelines. The Department is supposed to be independent from the SAC. State aid shall be reported to the State Aid Department and is subject to approval by the SAC. Before approval, the aid shall not be put into effect. Aid put into effect without prior approval granted by the SAC is subject to recovery. Decisions taken by the Commission may be appealed to the District Court of Tirana.

b. Progress made in 2009/2010

1 In terms of legislation, the Law on Competition Protection is currently being revised. The draft Law has not been provided to the Secretariat. In December 2009, ACA issued two guidelines concerning the evaluation of non-horizontal and conglomerate agreements as well as on horizontal concentrations.

In terms of case law, in November 2009 ACA opened an in-depth investigation procedure on the behaviour of the company *ARMO* which has a dominant position in the market of production, wholesale and retail of diesel. ACA is reviewing ARMO's practice of selling the same product at different prices to various wholesale companies from the perspective of Article 102(c) TFEU. There are further allegations of a margin squeeze. ACA is currently assessing the results of the investigations and hearings. A final decision is to be expected soon.

Furthermore, in February 2010 ACA started a preliminary investigation of the service market of loading, unloading and storage of liquid gas. ACA suspects that the exclusive concession granted to the company *Petrolifera* for the construction and use, within the "Vlora-1" port, of a terminal for the storage of oil and gas in the Bay of Vlora may constitute an abuse of dominant position. Based on these concerns, ACA adopted an interim decision obliging Petrolifera to offer the service of loading-unloading and depositing to all interested importers. The preliminary investigation is currently in its final phase. Another preliminary investigation is underway in the gas market following the structural changes in the gas removal and storage market segment, which have given a dominant position to some operators.

In December 2009, ACA also issued recommendations to ERE, the regulatory authority, on the prices and tariffs to be applied in 2010 by the utility *KESH*, the transmission system operator *OST* and the distribution system operator *OSSH*. ACA recommended a cost based approach to tariffs and a capital return ratio. They were not taken into account by ERE.

ACA is also monitoring the electricity market. An interim report has been completed and will be discussed with ERE and the Ministry of Energy. Following such consultations, recommendations on the opening of the market might be made.

2 The State Aid Law was amended in October 2009. The amendments have not been shared with the Secretariat. Reportedly, the amendments transpose the General Block Exemption Regulation 800/2008.

c. State of compliance

Articles 18 and 19 EnC have been properly transposed into Albanian law.

1 With regard to the implementation of competition law, it should be noted that ACA has been remarkably active in the energy sectors, with respect to both cases and competition law advocacy, thereby setting an example for competition authorities in the other Contracting Parties to follow.

For instance, ACA carried out a general investigation in the energy markets in 2007-2009. With respect to electricity, in October 2008 the authority recommended the *"real opening"* of the electricity market in accordance with Directive 2003/54/EC and made further detailed recommendations to the Ministry, the regulatory authority and the TSO. In cooperation with ERE, ACA recommended to the legislator the liberalization of production and distribution operations of the electricity sector, as well as the application of a market-oriented tariff setting approach.

Following up on the investigation in the hydrocarbons market, in May 2009 the responsible body did not find clear evidence for the existence of coordinated behaviour by the market participants in the market for motor fuels. Simultaneously, ACA recommended to the Parliament amendments to the legislation applicable to hydrocarbons because of their anti-competitive effects on the wholesale markets. In December 2008, the authority had already recommended to the government to withdraw a decision on the quality of fuels produced from refining Albanian crude oil due to its restrictive effects on imports.

In line with the initiatives started in 2009/2010, in October 2008 ACA authorized the purchase of 85% of shares of *ARMO*, the State-owned oil refining company, by AMRA, an Albanian and international consortium. In May 2009, ACA also approved the sale of 76% of State-owned DSO *OSSH* to *CEZ* under the merger rules, as well as the sale of *BP Greece* to Hellenic Petroleum. ACA furthermore exempted an exclusive agreement between *Tirana International Airport* and *AIR BP Albania* on securing, depositing and trading fuel for aircraft at Mother Teresa Airport.

2 With regard to the implementation of State aid law, the Secretariat understands that SAC is active in reviewing and assessing new and existing aid schemes. The Secretariat has been informed of two decisions relating to the energy sectors, one (2007) concerning VAT for electricity imported by KESH and one (2008) concerning exemptions from excise duties for fuel oil used for electricity generation. These decisions have not been provided to the Secretariat.

5.1.5 Environment

a. Environment in Albania

1 With regard to environmental impact assessment, the Law on Environmental Protection of 2002 lays down the basic principles of the procedure upon which the Environmental Impact Assessment Law of 2003 elaborates in more detail. Furthermore, a national methodology for the impact assessment procedure has been adopted in 2007 and 2008.

With regard to *screening*, the Environmental Impact Assessment Law differentiates between a "profound" assessment for mandatory projects listed in Annex I, in protected areas or marine environment, and a mere "summary" assessment for other projects as listed in Annex II, unless significant impact on the environment is established. The competent authority, the Regional Environment Agency takes a *screening* decision, unless the developer submits information fulfilling the criteria of a „profound" assessment. With respect to *scoping*, the Environmental Impact Assessment Law empowers the minister to establish a list of documents to be attached to the application. The methodology covers that subject. Depending on whether the environmental impact assessment to be carried out is a "profound" or a "summary" review, the *environmental impact statement* will be a "profound" or a "summary EIA report". The statement is to be compiled by licensed experts chosen by the developer. The course of action in the *decision-making* phase is as follows: The Regional Environmental Agency issues an opinion after having notified the Ministry, the authority issuing the construction/operation licenses and the local authorities and having consulted with local government units and urban and tourism development organs. Subsequently, a Commission of Requests Review, established by the Ministry, issues a final report including a proposal for a decision. In order to prepare this report, the Commission consults with external specialists and with sector-specific bodies, urban and tourism development organs, local government organs as well as specialized environmental impact institutions. The Environmental Impact Assessment Law also provides for a public debate to be held. Further participation of the interested public as well as of NGOs is provided for in that Law; the corresponding secondary legislation has not been made available to the Secretariat. The Environmental Protection Law also deals with trans-boundary cases, making explicit reference to the Espoo Convention. Finally, the Ministry of Environment issues a decision granting or denying an environmental declaration/permit as a precondition for the construction permit. This decision may be appealed by the developer to a court.

2 In terms of the protection of wild birds, the legislative framework includes a Law on the Protection of Wild Fauna and a Law on Hunting. They have not been provided to the Secretariat in English. An assessment of the presence of birds species listed in the Wild Birds Directive and of suitable sites for designation of special protection areas has been initiated, as well as an evaluation of possible conservation measures. Albania has further designated protection sites under the RAMSAR Convention.

b. Progress made in 2009/2010

1 There is no progress to be reported in the area of environmental impact assessment. During the last reporting period, Albania announced that amendments to the Environmental Impact Assessment Law of 2003 would be adopted in 2010. Up until now, the Secretariat has not been informed whether this has been the case.

2 With regard to the protection of wild birds, a Law on the Protection of Wild Fauna was reportedly adopted in October 2009 and a Law on Hunting was adopted in May 2009. In spite of several requests, the Secretariat was not provided with copies of that legislation.

c. State of compliance

Overall, the Albanian legislation still falls short of fully implementing the environmental *acquis*.

1 In terms of transposition, domestic legislation follows the structure and substance of the Environmental Impact Assessment Directive. Its implementation and enforcement, however, remain weak. In 2009, the Secretariat provided assistance to the Albanian authorities in receiving training tailored for the environmental impact assessment as part of the permitting procedure for a coal-fired power plant.

2 The transposition of the *acquis* on wild birds is at an early phase, full transposition is envisaged only for 2012. The assessment is being complicated by the fact that the relevant acts adopted in 2009 have not been made available to the Secretariat.

5.1.6 Renewable Energy

a. Renewables in Albania

The main renewable energy resources in Albania are hydro and biomass. Close to 100% of domestic electricity generation comes from hydropower plants. However, only 35% of Albania's hydropower potential is currently exploited. Albania has still significant potential with biomass (12.8 TWh/year), hydro (3.2 GW) wind (1.4 GW) and solar (33 MW).

1 Related to the implementation of Directive 2001/77/EC, Albania has already taken several steps. As regards renewable energy targets, the Power Sector Law of 2003, as amended in 2006, 2007, 2008 and 2009, obliges new electricity producers with an installed capacity higher than 100 MW to produce electricity no less than 2% of their total generation from RES. This obligation can also be fulfilled through purchase of electricity from domestic sources or from import, based on certifications issued in the country of origin.

Incentives to support the development of RES include power purchase agreements of up to 15 years for small HPPs (less than 15 MW) based on concession agreements or feed-in tariffs adopted by the regulatory authority. The purchase prices for old and new small HPPs are set based on the import price of electricity in the previous year, adjusted with an inflation index and approved annually by the regulatory authority, ERE. Proper feed-in tariffs for renewable energy sources must still be developed to boost investors' confidence. Another support measure, as prescribed in the *Law Facilitating the Construction of new Renewable Electricity Capacities* of 2002, consists in a customs duty exemption for the equipment and machinery for new RES facilities with an installed capacity of less than 5 MW. Small HPPs are not obliged to pay for water or State property fees.

There are no restrictions related to access to the grid of new renewable electricity capacities. The TSO and DSO are obliged to grant grid access to RES producers. The status of a privileged producer is granted by ERE and includes power plants with a capacity of up to 25 MW, for HPPs of up to 10 MW and for cogeneration plants of up to 100 MW. The privileged producers enjoy priority access to the transmission network.

2 As regards biofuels, Albania adopted a Law for the Production, Transport and Trade of Biofuels and other Renewable Fuels in Transport in February 2008. The Law deals with the functional and organizational aspects of production, transportation and trade in biofuels. Albania set a national indicative target of a minimum share of 5% biofuels by 2010. Some incentives to support the competitiveness of biofuels and renewable fuels on the market have been identified (e.g. special tax advantages for machineries, equipments and materials necessary for the construction and commissioning of biofuels plants etc.).

b. Progress made in 2009/2010

A Law on Renewable Sources has been drafted at the end of 2009. The Law aims to implement some of the key principles of the new EU Directive 2009/28/EC. The scope of the draft is limited to electricity production from renewable energy sources and does not include provisions related to the energy for heating and cooling. Despite also mentioning biofuels in its scope, the provisions of the draft Law make no reference to biofuels, or to the existing Law for Production, Transport and Trade of Biofuels. It is envisaged that national RES targets will be adopted by the Council of Ministers. The draft also foresees the appointment of an institution to implement a system for guarantees of origin. The draft was presented to the Secretariat for further comments.

c. State of compliance

Albania submitted its plan to implement Directives 2001/77/EC and 2003/30/EC to the Ministerial Council in June 2007, as was required by the Treaty.

1 The draft Law on Renewable Sources, currently under discussion, is to be welcomed as it shows the willingness to act proactively in implementing Directive 2009/28/EC even before a decision is reached by the Ministerial Council.

The Secretariat recommended the revision of the provisions related to support schemes and certification schemes for energy produced from RES based on guarantees of origin. There is concern regarding the introduction of mixed support schemes based on feed-in tariffs and a quota obligation for electricity produced from renewable energy sources. The certification schemes have to include the heating and cooling from renewable energy sources for compliance with Directive 2009/28/EC.

Proper support schemes for new RES projects have yet to be developed. The adopted power purchase prices for electricity produced in hydro power plants in the year 2010 have decreased compared with 2009 due to the lower price of imported electricity, therefore increasing the risks of new HPP projects.

The TSO and DSO have to set and publish their standard rules related to the costs of connection to the grid or grid reinforcement which are necessary to integrate new RES producers. The administrative procedures related to authorization for all new RES capacities have to be coordinated regarding deadlines, reception and treatment of application between different institutions involved, and be made available to applicants.

2 Concrete achievements with regard to fulfilment of the biofuels target as set by the Law of 2008 have not been reported to the Secretariat.

As regards the draft Law on Renewable Sources, the link to biofuels and other forms of renewable energy for transport should be clarified by amending the relevant parts of the draft, and by referring to the Law for Production, Transport and Trade of Biofuels and other Renewable Fuels in Transport (which might also require amendments). If biofuels are to be excluded from the scope of the new Law, this should be made clear.

5.1.7 Energy Efficiency

a. Energy Efficiency in Albania

A general Law on Energy Efficiency was adopted by the Albanian Parliament in 2005 (i.e. prior to the entry into force of Directive 2006/32/EC). The Law includes provisions concerning the National Energy Efficiency Program, energy audits, the Energy Efficiency Fund, etc. Nevertheless, the Law was not implemented, as the implementing norms were not adopted; the main reason was the financial constraints on the public budget to set up an Energy Efficiency Fund.

Besides the general Law on Energy Efficiency, a Law on the Conservation of Thermal Energy in Buildings of 2002 establishes the necessary legal basis for setting up the rules and taking mandatory action for the conservation of thermal energy in buildings. This Law stipulates that the design and construction of buildings shall meet the prescribed technical parameters for conservation, saving and efficient use of energy. Based on this Law, the Council of Ministers sets norms, rules and design and construction conditions, and guidelines for heat generation and conservation in buildings. In particular, in 2003 the government adopted the Building Code, which contains norms, rules and conditions for the design and construction of buildings as well as the production and conservation of thermal energy in buildings. The so-called "Councils of Regulatory Adjustment" in municipalities or counties is only then obliged to issue construction permits when the designs meet the requirements of this Code. However, the Building Code needs to be updated to reflect the current technical progress, changes in consumer behaviour, construction materials, etc.

The Law on Planning Territory of April 2009 imposes, in Article 25 on building regulations, an obligation on investors to comply with energy efficiency standards.

The Law on the Indication by Labelling and Standard Product Information of the Consumption of Energy and Other Resources by Household Appliances of April 2009 transposes Council Directive 92/75/EEC. The Law stipulates the obligation of suppliers regarding the provision of information to consumers related to the consumption of electric energy, other forms of energy and other essential resources through a fiche and a label attached to household appliances offered for sale, hire, hire-purchase or which are displayed to end-users. The implementing Directives will be further transposed through decisions of the Council of Ministers.

b. Progress made in 2009/2010

In line with the work programme of the Energy Efficiency Task Force, Albania prepared a Roadmap for the implementation of the energy efficiency directives in May 2010, as well as the draft for the 1st National Energy Efficiency Action Plan (NEEAP). In line with Articles 4 and 14 of Directive 2006/32/EC, the NEEAP needs to be amended, taking into account the Secretariat's comments, and re-submitted to the Secretariat by 30 June 2010, with some possible delay. According to the NEEAP, the institution responsible for monitoring and verifying energy savings will be the National Agency of Natural Resources (AKBN). For the proper implementation of the NEEAP, the legal framework needs to be completed, as well as the cooperation and responsibilities of institutions involved need to be strengthened.

The Ministry of Economy, Trade and Energy is currently preparing a new Law on Energy Efficiency aimed to transpose the directives included in the Ministerial Council Decision No. 2009/05/MC-EnC. The Law will also include rules on

certification of the energy performance of buildings, currently not in place.

Pursuant to the Law on the Indication by Labelling and Standard Product Information of the Consumption of Energy and Other Resources by Household Appliances, the Albanian Council of Ministers will issue decisions in 2010 which further transpose the relevant implementing directives. In these decisions the details relating to the label and the fiche for each type of appliance foreseen in the Law will be determined.

Several information campaigns have been launched in the last few years, focusing on energy efficiency in buildings and energy labelling. They were accompanied by workshops attended by builders, architects, construction material producers, traders, consumers, and representatives from small banks, municipalities, custom offices etc. Training of energy auditors has been started and will continue throughout the remainder of 2010.

Model contracts for the financial instruments for energy efficiency measures will be introduced in 2010 by using EU templates, and will be available to existing and potential purchasers of energy services and other energy efficiency improvement measures in the public and private sectors. Special provisions will be also included in the draft of the new Law on Energy Efficiency.

c. State of compliance

As the deadline for implementing the energy efficiency directives only expires in December 2011, the state of compliance is currently not assessed.

5.1.8 Social Issues

a. Social issues in Albania

Even if the social *acquis* is not mandatory under the Treaty, the government was encouraged to transpose some of it on a voluntary basis. At this stage, the Secretariat has not received any information on the transposed directives.

The Albanian legal framework related to the social *acquis* includes the following primary legislation: The Labour Code of 1996, the Power Sector Law of 2003, the Law on the Ratification of the Treaty establishing the Energy Community of 2006, the Law on Gender Equality of 2008, the Law on the Labour Inspection and the State Labour Inspectorate of 2006, the Law on Safety and Health at Work of 2010 and the Law on Protection Against Discrimination of 2010.

The Decision of the Energy Regulatory Agency on the Determination of the Electricity Tariffs of 2008 establishes, for the protection of vulnerable customers, a regulated two-block tariff for households of 7 lekë/kWh for up to 300 kWh/month and 12 lekë/kWh for above 300 kWh/month. There is no specific definition of an energy vulnerable consumer. The definition used is the one introduced by the Ministry of Labour and Social Affairs for social assistance support.

b. Progress made in 2009/2010

A working group set up with multiple stakeholder representation has prepared a *Social Action Plan* in accordance with the MoU.

The Plan follows the structure of the MoU and envisages activities in the areas of *public service obligations* (ensuring economic, social and territorial cohesion, universal access, and a high level of consumer rights); *social partners* (promoting the social dialogue with the social partners - introduction of effective mechanisms for information and consultation of social partners); *management of change* (promoting the development of specific employment, training and support services) and *social dimension* (focusing attention on the following key areas: workers' fundamental rights, improved working conditions and standards of living, an improved working environment concerning the health and safety of workers, and equal opportunities).

Albania reported plans to reduce the threshold used for the block tariffs to 200 kWh to better target the recipients, but has not specified a deadline. The government still needs to adopt the Plan and prepare its implementation.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.2 BOSNIA AND HERZEGOVINA

5.2.1 Electricity

a. Electricity in Bosnia and Herzegovina

One crucial feature of Bosnia and Herzegovina is its intrinsic complexity. The market is split along the borders of the two political entities (Republika Srpska and the Federation of Bosnia and Herzegovina) which share the responsibility to also supply the customers in a separate independent small administrative unit (Brcko District). On top of that there are three incumbent utilities *(Elektroprivreda, EP)*, of which two *(EP BIH and EP HZ-HB)* operate in the Federation and one *(EP RS)* in Republika Srpska. Each of the utilities is engaged in a specific process of unbundling with a different pace of progress and a different result. Both utilities in the Federation are completing the unbundling of their accounts along their main activities of generation, distribution and supply of electricity and planning further steps towards legal unbundling. Both utilities remain 90% State owned. In Republika Srpska, *EP RS* has advanced and since 2005 accomplished legal unbundling into a holding structure of five generation companies and five utilities for distribution and supply of electricity. The *Elektroprivreda* holding is 100% State owned while its subsidiaries are 65% owned by the holding.

The electricity transmission system is carved out in a separate corporate structure consisting of two companies – an Independent System Operator *(NOS BIH)* and a transmission company *(Elektroprenos–Elektroprijenos)* which incorporates the transmission infrastructure assets. Both are operated under a separate legal framework adopted on the State level. The ownership title over the transmission infrastructure belongs to the transmission company (Elektroprenos-Elektroprijenos). The management of interconnections with the neighbouring TSOs is performed by *ISO- NOS BiH.*

The regulatory powers derive from the level of political competences and result in three separate regulatory authorities. The State Electricity Regulatory Commission *(DERK)* operates on the State level. However, its competences are limited to electricity transmission system operation including the cross-border capacity market and cross-border trade of electricity. Since 2010, DERK is entitled to regulate the generation, distribution and supply of electricity in the Brcko District. The two entity regulators are the Federal Electricity Regulatory Commission *(FERK)* in the Federation of Bosnia and Herzegovina and the Energy Regulatory Commission of Republika Srpska *(RERS)*, both of which are empowered to regulate the generation, distribution and supply of electricity in their jurisdictions. The entity regulatory authorities establish tariffs and carry out tariff proceedings in their respective jurisdictions, including the setting of the end-use prices for captive customers and distribution network tariffs.

In the same context, another particularity of Bosnia and Herzegovina consists in the fact that it is the only Contracting Party with a significant capacity for export of electricity. The surplus of indigenous generation complies with fundamental conditions for easy entry to the electricity market and may provide strong back-up for the process of its liberalization. Most of the excessive generation is located in Republika Srpska. Despite the fact that the market is administratively open for all non-household customers, the exchange of electricity supply happens only on the wholesale level, among the utilities and between utilities and traders.

The total electricity consumption of Bosnia and Herzegovina is around 12.2 TWh with an annual growth rate of around 4.4% (2008), while overall production reached nearly 14.0 TWh, of which thermal, coal-fired power plants provided 8.9 TWh, large hydro provided 4.8 TWh and small hydro power plants provided 0.2 TWh of electricity. Roughly 10% of this energy, or 1.36 TWh, is produced in the 792 MW total hydropower capacity of the utility *EP NZ-HB*. At the same time, this utility's consumption reached 2.43 TWh, the 56% offset was purchased on the domestic market and from imports (15%). The utility *EP BiH* is the largest utility. It operates 1,682 MW of generation capacity, 30% of which is hydro, and generates 53% of the electricity in Bosnia and Herzegovina. The same utility's customers consume 63% of its own generation and the rest is sold on the market. *EP RS* covers the remaining 37% of the indigenous generation in Bosnia and Herzegovina, employing a total of 1,348 MW installed capacity. Production is equally divided (50%) between thermal (coal-fired) and hydropower generation. The total production of 5.09 TWh (2008) covers the domestic consumption of 2.89 TWh and the consumption of the Brcko District of 0.27 TWh while the remaining electricity is traded on the market.

Undertakings operating in the electricity sector of Bosnia and Herzegovina are, depending on their seats, licensed by the regulatory authority of the respective entity. Licenses however are valid throughout the territory of Bosnia and Herzegovina. The electricity market of Bosnia and Herzegovina is formally open for all categories of customers except households, which could allow for a nominal level of 57.5% of the demand. In practice, the single active eligible customer is the aluminium industry *(Aluminij)* absorbing 20% of the total consumption in Bosnia and Herzegovina – but only 12% under market conditions – which is the actual scale of effective market opening.

The complexity of the legislative and political structure in Bosnia and Herzegovina is followed by the level of competence and responsibility and has a bearing on the energy policy in the country. The legislative framework is spilt into several layers of primary legislation. The State is responsible for transmission system operation, and the entities of Republika Srpska and the Federation of Bosnia and Herzegovina are both responsible for energy matters in their own jurisdiction. Furthermore, the Brcko District is an autonomous administrative unit.

On the State level, primary legislation is composed of the Law Establishing an ISO (2004), the Law Establishing the Transmission Company (2004) and the Law on Transmission, Regulator and System Operator in Bosnia and Herzegovina (2002, as amended in 2002 and 2009). Pursuant to this framework, DERK has adopted corresponding rules, in particular Licensing Rules (2005); Rules on Tariff Proceedings (2005); Tariff Pricing Methodology for Services of Electricity Transmission, Operation of the ISO and Ancillary Services (2005 as amended in 2007 and 2009); Rules on Allocation of the Rights to Use Cross-border Transmission Capacities (2010) and Decision on Market Opening (2006 as amended in 2009). NOS-BIH developed and DERK further approved the Market Rules (2006) and the Grid Code (2006).

The main laws of the Federation of Bosnia and Herzegovina are the Electric Power Law (2002, as amended in 2005 and 2009) and the Law on Implementation of the Tariff System (2004). Additionally, FERK has adopted Rules on Hearing Procedures and Resolving Appeals and Complaints (2005); Rules on Protection of Confidential Information (2005); Licensing Rules (2005); Rules on Tariff Methodology and Tariff Proceedings (2005); Rules on Obtaining Eligible Customer Status (2006) and General Conditions for Electricity Supply (2008, as amended in 2010).

In Republika Srpska, the Law on Energy (2009) and the Electricity Law (2008, as amended in 2008 and 2009) are in place. RERS adopted a Rule Book on Tariff Methodology and Tariff Procedure (2005); a Rule Book on Methodology for Determination of the Fee for Connection to the Distribution Network (2008); General Conditions for Delivery and Supply of Electricity (2006, as amended in 2008 and 2010); a Rule Book on Licenses (2007, as amended in 2009 and 2010); a Rule Book on Reporting (2007); a Rule Book on Acquiring the Status of Eligible Customer (2006, as amended in 2010); a Rule Book on Confidential Information (2007); Rules on Public Hearings and Settlements of Disputes and Complaints (2005). RERS also approved the Distribution Grid Code (2008).

In the Brcko District, a Supervisory Decision on Transmission Assets was issued in 2009. In addition, pursuant to corresponding Decisions of the OHR (2009) amending the Law on Electricity of the Federation of Bosnia and Herzegovina, the Law on Electricity of Republika Srpska, The Law Establishing the Company for Transmission of Electric Power and the Law on Transmission of Electric Power, Regulator and System Operator of Bosnia and Herzegovina, the security of electricity supply and the regulatory rule for the Brcko District are enforced through the existing legislative framework on the State and entity level.

b. Progress made in 2009/2010

After serious problems in the operation of the transmission company occurred, the Law on Transmission was amended in September 2009 to ensure smoother operation. A working group has been established to work along the conclusions reached at the meeting with the Secretariat. Despite having promised to solve the bottlenecks in the operation of the transmission operator, no outcome or progress has been reported so far.

In 2009, the State Regulatory Commission adopted a new form of standard contract on the responsibility of balancing and the ISO has initiated the procedure to make some amendments related to scheduling, metering, the integration of wind farms into the system, cooperation and reporting.

Congestion management on interconnections was substantially changed by mid 2010, when the State regulatory authority (DERK) approved the auction rules based on market principles, removing "pro rata" allocation of capacity rights. The procedure envisages yearly, monthly, weekly and daily allocations. The intra-day allocation is made on a first-come-first serve basis for the available capacity. The capacity rights except for daily allocation can be transferred to other participants, however only with the approval of the ISO. The pricing method is the marginal price for the capacity rights, and the failure to nominate the capacity to the ISO by the deadline is not compensated (the "use-it-or lose-it" principle applies). The holder of the capacity rights will enter into a contract with the transmission operator and the use of the income from capacity allocations according to Regulation 1228/2003 is determined by the transmission company and reported to DERK.

Since July 2010, *ISO-NOS BiH* has introduced monthly and daily allocations split 50-50 with the neighbouring TSOs. The auction rules and the current monthly and daily results since July 2010 are published on the *ISO (NOS BiH)* website.

During 2009, RERS of Republika Srpska determined the fees for connection of final customers to the distribution network, as well as the tariff rates for supply of tariff customers. The cross-subsidies between the second and third customer group within the commercial customer class have been decreased.

c. State of compliance

Primary legislation transposes the main part of the *acquis*, namely market opening, public service obligations, tasks of TSO and DSOs, unbundling requirements, regulatory competences, customer protection, technical standards, operational network security, third party access and congestion management and confidentiality protection. Although the eligibility thresholds for market opening were not adequately transposed in the entity laws, the laws provided for regulatory competences to adjust these thresholds and thus ensured the achievement of formal compliance.

The following items are still not adequately transposed:

- universal service is not adequately defined,
- information by the supplier on the fuel mix and environmental impacts is not required,
- procedures and conditions for tendering procedures are not adequately transposed,
- responsibilities related to reporting on the security of supply and measures necessary for maintaining long-term balance between supply and demand and the availability of generation capacity are not consistently assigned,
- responsibility to report on market dominance, predatory and anti-competitive behaviour is not assigned,
- regulatory competence related to methodologies for the provision of balancing services assigned to the State Regulatory Commission have proved not adequate to impose on the ISO the proper implementation.
- there is a lack of power to establish a methodology and to fix or approve terms and conditions for connection and access to the distribution network, as well as distribution tariffs in the Brcko district,
- the procedure for exemption for new interconnectors has not been transposed.

In terms of implementation, the recent amendments to the Law on Transmission of Electric Power, Regulator and System Operator in Bosnia and Herzegovina, as well as the amendments to the Electricity Law in the Federation and the Electricity Law in Republika Srpska of 2009 need to be scrutinized. The entities' laws extend an obligation on two energy undertakings (*Elektroprivreda BiH* and *Elektroprivreda RS*) to supply all customers in the entities, contrary to Article 32 of the Treaty and Article 3.1 of Directive 2003/54/EC. A similar obligation to supply all customers in the Brcko district at regulated prices is imposed on two undertakings, thus denying those customers their eligibility rights under Article 21 of Directive 2003/54/EC.

Given the shortcomings in primary legislation, secondary legislation promulgated in the prescribed procedure by the relevant State or entity administration, regulatory authority or energy undertaking is consequently imperfect. An example for this may be the competence to establish a binding methodology and fix or approve terms and conditions for the provision of balancing services under Article 23(2)(b) of Directive 2003/54/EC, which has not explicitly been given to the regulatory authorities. However, the State Regulatory Commission in its methodology (amended in 2009) stated that it will set the price for imbalances, even though the prices have not been established yet.

Furthermore, in a decision from April 2010, the State Regulatory Commission established a fee for the declared export (to be paid by holders of the license for international trade in electricity) contrary to Article 41 of the Treaty and 4(4) of Regulation 1228/2003. The Secretariat will follow up on this.

Finally, implementation would include establishing a legally binding obligation on the ISO to coordinate its congestion management methods and procedures in the way described in Regulation 1228/2003 and its Annex, as well as to ensure the required level of transparency. Moreover, attention needs to be paid to the level of tariffs, in order to allow the necessary investments in the network and to ensure their viability.

5.2.2 Gas

a. Gas in Bosnia and Herzegovina

Bosnia and Herzegovina does not have its own natural gas sources. Its supply is exclusively from one source of natural gas (from Russia) through the transport systems of Ukraine, Hungary and Serbia. The gas is mainly consumed by a few big industrial consumers (58%), whereas the household consumption share is 17% (which should be considered 17% with central heating).

There is no legislative framework for the gas sector on the State level but only on the level of the entities. The Law on Gas in Republika Srpska and the Decree on Organization and Regulation of the Gas Sector in the Federation of Bosnia and Herzegovina are both in force since autumn 2007. Two transmission system operators, one in each entity, have been established by those entities' laws. Besides, one more transporter, (only) one supplier (which is still bundled with transmission system operation) and four distribution companies are participating in the gas market.

Furthermore, in Republika Srpska the Tariff Methodology for Transport, Distribution, Storage and Supply of Natural Gas has been defined by the regulatory authority in 2009. However, so far only the tariffs for distribution and prices for supply of natural gas have been approved by the regulatory authority. In another entity, the Federation of Bosnia and Herzegovina, network tariffs for natural gas are still not regulated. Even worse, the tariffs for network services are still bundled with the prices of gas as a commodity. In practical terms, this means that the prices for transmission-supply and for distribution-supply are proposed by the companies and approved by the respective cantonal Ministry.

b. Progress made in 2009/2010

An expert group was established in 2007 in order to develop and propose the proper framework for the gas sector in Bosnia and Herzegovina in line with the requirements of Directive 2003/55/EC. The work of the group did not yield any concrete results by February 2010, when the three ministers in charge for energy visited the Secretariat. One of the conclusions of that meeting was to resume the work of the expert group, with the same (still unfilled) tasks. The group has held three meetings since February 2010. The results, to be presented to the ministers and to the Secretariat, may be expected anytime soon. The main improvement seems to be related to the approach applied to the regulatory authority's jurisdiction on the State level. However, the proposal by the expert group has still not been presented formally. In case it leads to tangible results, it should be accepted by the ministries and swiftly implemented by amending the legislation and by establishing the necessary structures.

c. State of compliance

Both entities have transposed some of the provisions of Directive 2003/55/EC, albeit not always the same provisions. Thus, the gas market is governed differently in the different entities of Bosnia and Herzegovina, and not in line with the EU *acquis*. In summary, the crucial non-implemented provisions at the State level include: the regulatory authorities' tasks and responsibilities, unbundling requirements, third-party access and market opening. There is no regulatory authority with jurisdiction over the entire State, and one entity has not yet established a regulatory authority responsible for gas. The unbundling requirements vary across the State from account unbundling only to certain arrangements not allowing for true independence criteria and to be implemented only by 2012. Third-party access and market opening are also defined differently by the two entities, which thus establish different rules for market participants on the same gas market.

The implementation of Directive 2004/67/EC is still pending as well. Even the provisions of Directive 2003/55/EC related to the security of supply have not been transposed by the existing legislation. Both directives could be implemented by revision of the existing legislation and/or the development of a new legislation on the State level.

Further substantial incompliance must be stated in relation to the implementation of Regulation 1775/2005. Just as even basic network access elements as required by Directive 2003/55/EC (network codes, TPA, tariffs) are still not in place, almost none of the provisions of Regulation 1775/2005 have been transposed on the State level. This is even more alarming considering the number of participants in the domestic gas market (two transmission system operators, three transporters and four distribution system operators), as well as several planned interconnectors.

It needs to be summarized that, despite having a relatively developed gas sector and having had four years time, Bosnia and Herzegovina has still not properly implemented any of the three gas legislative acts required by the Treaty. The Secretariat will have to follow up on this deficiency in the near future.

5.2.3 Oil

a. Oil in Bosnia and Herzegovina

In Bosnia and Herzegovina there is no domestic production of crude oil. Crude oil dependency is at 100%. The crude oil is mainly sourced from Russia.

Oilfield exploration, which took place extensively before 1991, was stopped due to the war. No concrete activities have been reported on the continuation of oil field exploration since 1991. According to results of the exploration done before 1991 in several locations in the north-north eastern, central and southern parts of the country, it is estimated that Bosnia and Herzegovina has significant oil reserves. The oil reserves in several locations in the north-eastern part of the country are estimated at 50 million tons. For further activities in this direction, significant financial resources are needed. The government of Republika Srpska authorized the Bosanski Brod refinery to conduct exploration activities on the territory of Republika Srpska. Currently, no such activities have been observed. In the Federation of Bosnia and Herzegovina, the concession process for exploration to a domestic company is currently underway.

Bosnia and Herzegovina has around 800,000 m^3 of storage capacity. There is only one oil terminal in the port of Ploce (Croatia) with a storage capacity of around 84,000 m^3.

The Bosanski Brod oil refinery is the only refinery in the country. It stopped its regular operation in 1991, when supply through the JANAF oil pipeline was interrupted due to military operations. The refinery resumed its operation in 1995, but only on an *ad hoc* basis until it stopped operating again in 2005. In 2007, the entity government of Republika Srpska privatized the refinery. In November 2008, it started operating again. In the period of 2000–2005, the refinery operated at very low capacity. The nameplate capacity is 4.3 million tons/year to be reached in 2013, but the actual capacity is 1.3 million tons/year.

The total number of wholesale trade companies in Bosnia and Herzegovina is 160, and the number of retail companies is 550. The annual petroleum products consumption in the last few years was around 1 million tons.

There is no particular legislation for exploration and production of crude oil in Bosnia and Herzegovina. One State and two entity Laws on Concessions exist. Furthermore, State Laws on Foreign Trade Policy and on Customs Policy are in place. There are Laws on Trade at the level of both entities, and a Law on Oil and Oil products in Republika Srpska. Legislation on fiscal policies in the hydrocarbon sector is governed by the (State) Laws on VAT and on Excise Duty. A Decision on Quality of Liquid Petroleum Products in Bosnia and Herzegovina is part of the legislation for standards and the regulation of petroleum products. There is no legislation covering maintenance, management and reporting requirements of oil stocks.

b. Progress made in 2009/2010

After the privatization of the *Bosanski Brod* oil refinery, the *Modrica* lubricants refinery and the *Petrol* distribution company, a number of achievements can be reported.

This includes the fact that the refinery now produces only euro diesel of EURO 4 and EURO 5 quality. The maximum content of sulphur is below 50 mg/kg and 10 mg/kg (50 ppm and 10 ppm) respectively, all other parameters are in line with EN 590. In December 2009, domestic production of leaded petrol was stopped. The sale of leaded petrol has been forbidden since 1 January 2010. Meanwhile, the export of petroleum products has increased. The lubricants refinery increased its production output, and in April 2010 for the first time it achieved a level of production equal to the one in 1990. A number of petrol stations have even been reconstructed.

Furthermore, the State Ministry of Foreign Trade and Economic Relations is currently preparing an analysis on the possibilities of establishing compulsory oil stocks.

In 2010, the regulatory authority of the Republik Srpska adopted a new Licensing Rulebook which includes also the oil sector. Procedures for licensing of undertakings operating in oil derivatives production, as well as storage of oil and oil derivatives are currently being prepared.

c. State of compliance

The oil and petroleum products market in Bosnia and Herzegovina has been fully opened and liberalized since 2000. Governments do not have any major influence on the operation of any oil company operating in Bosnia and Herzegovina, and do not have the power to regulate the price of products. Prices are formed by the oil companies. A licensing procedure is not yet in place.

There is no customs duty on the import/export of crude oil. The customs duty is at 10% on petroleum products, but it is not applied in cases where bilateral free trade agreements exist such as the CEFTA Agreement or the Stabilization and Association Agreement with the EU. Based on the bilateral free trade agreements with EU countries, customs duty is reduced every year and will be at 0% by the end of 2011. It needs to be further scrutinized if this scheme effectively exempts also all transactions between the Contracting Parties from customs duties. To the extent this is not the case, Article 41 EnC is violated.

Tax components in the final price of the petroleum products vary from 45% to 54%. There is no different treatment of local companies vis-à-vis foreign companies regarding taxes.

5.2.4 Competition

a. Competition and State aid in Bosnia and Herzegovina

1. Competition law in Bosnia and Herzegovina is governed by the federal Act on Competition in force since 2005. The Act provides for a prohibition of cartels which generally corresponds to Article 101 TFEU. Individual exemptions may be granted by the competent authority upon application. If the authority fails to take a decision within four months, however, the agreement in question is deemed to be exempted. Block exemptions inter alia cover horizontal and vertical agreements. The prohibition of the abuse of dominant positions is modelled on Article 102 TFEU. A separate provision as well as a regulation adopted by the Council of Competition define the notion of a dominant position. The establishment of a case of abuse depends on the decision by the competition authority. The Act extends the notion of undertakings covered by it to *"state and local self-government units directly or indirectly participating in or having influence on the market".*

   The federal authority enforcing the Act on Competition is the Council of Competition established in 2004. Within the Council, an Expert Unit is in charge of the operational work, in particular the preparation of decisions. Decisions by the Council may be appealed by way of an administrative dispute to the Court of Bosnia and Herzegovina. The Act also establishes procedural rules complementing general administrative law. The Council of Competition shall impose fines on undertakings violating the provisions on the substance of up to 10% of the total annual income. Fines may also be imposed on the persons responsible for the undertaking in question. The Act and a regulation on the procedure for granting immunity from fines define the Council's leniency policy.

2. Bosnia and Herzegovina still does not have a federal State Aid Law or monitoring infrastructure. Minister *Zirojevic* announced at a meeting in Vienna that a Law was to be adopted by 1 July 2010. Despite repeated requests, the Secretariat never received a draft of this Law.

b. Progress made in 2009/2010

The Secretariat is not aware of any new primary or secondary legislation in the field of competition. Despites repeated requests no information on any progress in 2009/2010 has been brought to the attention of the Secretariat.

c. State of compliance

Articles 18 and 19 EnC have been only partly transposed into the law of Bosnia and Herzegovina.

1. Despite following the EC model in principle, however, competition legislation still requires legislative efforts in order to achieve full compliance with the *acquis*. This relates to both law on substance and procedure.

   With regard to the implementation of competition law in the energy sectors by the Council of Competition, the Secretariat took note of several approvals of and non-objections against mergers in the markets for oil, oil derivatives and lubricants (namely the takeover of *Energopetrol* by *INA* and *MOL* in 2006, the takeover of refineries by the Russian company *Neftegaz* in 2007 and the merger between *MOL* and *INA*), as well as in the electricity sector (approval of the majority purchase of the Albanian State-owned TSO *OSSH* by *CEZ* in June 2009). In July 2009, the Council apparently gave an opinion on a draft decision on the *"size, conditions and time schedule of opening the electricity market in Bosnia and Herzegovina"* which has not been made available to the Secretariat.

2. Regarding State aid, Bosnia and Herzegovina is in a state of non-compliance with the Treaty due to the lack of primary legislation. The Secretariat will have to follow-up on this issue.

5.2.5 Environment

a. Environment in Bosnia and Herzegovina

1 With regard to environmental impact assessment, there is no legislation at the federal level on environmental impact assessment. No information has been provided as regards the applicable law in Republika Srpska. In the Federation of Bosnia and Herzegovina, the Law on Environmental Protection deals with several aspects of environmental impact assessment, namely definition, public participation, access to justice and procedure.

With regard to *screening*, that Law differentiates between mandatory environmental impact assessment (to be defined by secondary legislation which has not been submitted to the Secretariat) and non-mandatory environmental impact assessment, based on a case-by case decision by the competent authority. Significant changes of existing projects, namely an increase of over 25% in production, energy use, water consumption, territory use, emission or waste production are also to be subjected to an environmental impact assessment. The developer shall first apply for a "Prior Impact Assessment", upon which a *scoping* decision is to be made by the competent Ministry after consultation with other authorities and "concerned subjects". This decision shall be made in line with so-called "EIA Guidelines" which are not available to the Secretariat. Together with the scoping decision, the competent Ministry assigns a contractor to prepare the *environmental impact study*, a draft of which is to be presented to the public and the respective other entity within Bosnia and Herzegovina or other States in transboundary situations. The *environmental impact study* is to be approved or rejected by way of a *decision* by the competent authority. Approval is to be denied, inter alia, where the statement is not in line with *"international environmental legal responsibilities of the State"*. An approved environmental impact study is a precondition for being granted a building permit etc. The public concerned may take the decision to court.

2 Regarding the protection of wild birds, Bosnia and Herzegovina has ratified the UN Convention on Biodiversity, CITES, the Berne Convention on the Conservation of European Wildlife and Natural Habitats and the Aarhus Convention. According to the information received, in the Federation of Bosnia and Herzegovina the implementation of Article 4 of the Wild Birds Directive has yet to begin. In Republika Srpska, transposition is at an early stage. Two protection sites have been established under the RAMSAR Convention (one in each entity); however a specific assessment of regularly occurring migratory species (not listed in Annex I of the Wild Birds Directive) and wetlands of international importance is still to be carried out.

b. Progress made in 2009/2010

The Secretariat has not received updated information regarding the implementation of the two directives covered in this report.

c. State of compliance

Bosnia and Herzegovina's preparations in the field of environmental protection remain at an early stage. With the Secretariat's requests for information not being answered, a proper assessment cannot be carried out.

1 Overall, the transposition of the Environmental Impact Assessment Directive in the Federation of Bosnia and Herzegovina still requires substantial effort. Central elements of the procedure are still underdeveloped or unclear. The Secretariat has still not been informed about Republika Srpska. Procedures do, however, take place within the entire territory of Bosnia and Herzegovina.

2 According to the information received by the Secretariat in the last reporting period, the implementation of Article 4(2) of the Wild Birds Directive in the Federation of Bosnia and Herzegovina has yet to begin. In Republika Srpska, transposition is at an early stage. The adoption of a law, presumably amending the current Law on Nature Protection, is expected to ensure full transposition of the Wild Birds Directive by 2013. This Law, or any draft, has not been shared with the Secretariat.

5.2.6 Renewable Energy

a. Renewables in Bosnia and Herzegovina

1 In terms of renewable energy sources, Bosnia and Herzegovina produces about 45% of its total electricity consumption from hydro power. Biomass used for heating was at a level of 182 ktoe in 2005 according to IEA

statistics, although the volume of wood used in households is significantly higher based on recent consumption surveys.

The country's renewable energy potential is estimated at 6.8 GW in small and large HPPs, 2 GW wind, 33 MW solar and 18 TWh/y biomass. According to estimates the State's geothermal potential is the second largest in the Energy Community (at about 40 GWh/y).

There is no legislation at the State level covering the promotion of renewable energy sources. However, the Federation of Bosnia and Herzegovina and Republika Srpska both have laws governing the electricity sector and regulatory requirements. The coverage of RES, however, remains marginal. There are no specific laws for RES on the entity level.

The Energy Law of Republika Srpska covers incentives to RES and requires the government to issue a decree on RES targets. The decree shall set indicative RES targets of gross energy consumption and the measures to achieve them. The regulatory authority shall set out in secondary legislation a system of incentives for energy from RES. The adoption of the decree is expected by the end of 2010, as well as the adoption of feed-in tariffs.

2 As regards biofuels, there is legislation in force in Republika Srpska, namely the Regulation on Type, Content and Quality of Biofuels of 2008, which enables the setting of targets and support measures. A decree on incentives for consumption of biofuels is allegedly under preparation. There is no legislation covering the entire territory of Bosnia and Herzegovina.

b. Progress made in 2009/2010

There is no concrete progress to be noted with regard to the implementation of Directives 2001/77/EC and 2003/30/EC.

c. State of compliance

Bosnia and Herzegovina submitted its plan to implement Directives 2001/77/EC and 2003/30/EC to the Ministerial Council in June 2007, as required by the Treaty. Following the adoption of the plan, however, Bosnia and Herzegovina did not undertake any major steps on the State level to implement the two Directives.

Despite some steps undertaken on the entity level in terms of the adoption of incentives to support electricity produced from RES and co-generation by the Regulatory Commissions, there is no indicative target set or strategy adopted at the national level. The complexity of the organisational structure and decision-making system hinders the effective promotion of renewable energy at the State level. During 2008, technical assistance was provided by Spain in order to solve some institutional and legislative barriers related to the promotion of renewables. The consultancy was supposed to result in a proposal on national indicative targets to be set, and the development of a RES strategy. Unfortunately, neither indicative targets nor a strategy for the promotion of renewable energy including biofuels in Bosnia and Herzegovina have been adopted thus far.

Proper support schemes for all RES, as well as a certification system based on guarantees of origin have yet to be defined and to be harmonised at the national level. Grid access (mainly at the distribution level) and administrative procedures have to be ensured in coordination and harmonisation at the State level, in order to create a favourable investment climate for RES projects.

5.2.7 Energy Efficiency

a. Energy Efficiency in Bosnia and Herzegovina

Based on publicly available information, Bosnia and Herzegovina's progress on the way to meet the requirements in the area of energy efficiency remains at an early stage.

Bosnia and Herzegovina does not have energy efficiency legislation in place on the State or entity level (an exception is the Energy Law in Republika Srpska which includes certain provisions on energy efficiency). There is also no energy efficiency policy in place in either of the entities.

Bosnia and Herzegovina is also lacking the relevant energy efficiency institutional framework. The entities are expected to initiate all activities related to energy/energy efficiency, while the role of the Ministry of Foreign Trade and Economic Relations (Department for Secondary Energy and Projects Development) is limited to coordinating this work as well as to developing and implementing international programmes.

b. Progress made in 2009/2010

There has been little progress reported over this period. Compared to the other Contracting Parties, Bosnia and Herzegovina is lagging behind in meeting the requirements in the area of energy efficiency.

During 2008-2009 Bosnia and Herzegovina has not been actively participating in the work of the Energy Efficiency Task Force and fulfilment of its Work Programme. As a result, there is no visible progress in developing the National Energy Efficiency Action Plan and Roadmap for the implementation of the relevant energy efficiency directives. This was also brought to the attention of the energy ministers of the two entities and the Foreign Trade and Economic Relations Minister at the occasion of their meeting with the Secretariat in February 2010. The recent re-nomination of the Task Force member representing MOFTER should ensure proper and adequate representation as well as fulfilment of the obligations in line with the agreed Task Force Work Programme.

Work on the formulation of energy strategies is reportedly underway. The strategies are expected to be strongly linked to the obligations of Bosnia and Herzegovina to transpose and implement the *acquis* on energy efficiency.

Many existing and planned grants and loans (EU, GTZ, EBRD, UNECE, UNDP, USAID, WB etc.) are available to support Bosnia and Herzegovina in the transposition and implementation of the energy efficiency directives, and the preparation and implementation of the energy efficiency projects. The IPA project *"Technical assistance support to meet the requirements of the Energy Community Treaty for SEE"* was planned to start in June 2010 and includes, among others, capacity building and development of a legal and institutional framework for energy efficiency at the State and entity level.

c. State of compliance

As the deadline for implementing the energy efficiency directives expires only in December 2011, the state of compliance is currently not assessed.

In line with the Work Programme of the Task Force, Bosnia and Herzegovina was asked to prepare a draft for the 1st National Energy Efficiency Action Plan (NEEAP). According to Articles 4 and 14 of Directive 2006/32/EC, the draft NEEAP needs to be amended, taking into account the Secretariat's comments, and re-submitted to the Secretariat by 30 June 2010. As not even the draft for an Energy Efficiency Action Plan has been sent yet, the Secretariat does not expect this requirement to be met.

5.2.8 Social Issues

a. Social issues in Bosnia and Herzegovina

Even if there is no mandatory social *acquis* in place, the government was encouraged to transpose some of the relevant directives on a voluntary basis. At this stage, the Secretariat has not received any information on transposed directives.

b. Progress made in 2009/2010

Bosnia and Herzegovina prepared a very extensive Social Action Plan in a well concerted cooperation with the principal stakeholders at the entities and State levels. This was adopted in March 2010 by the Council of Ministers of Bosnia and Herzegovina and published in the Official Gazette in May 2010.

A Working Group met in June 2010 to prepare the implementation steps.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.3 CROATIA

5.3.1 Electricity

a. Electricity in Croatia

Croatia has applied a thorough legal unbundling of all market-related activities from network operation in its electricity sector, with the exception of the distribution system operator who, along with its core function, also operates as a supplier of electricity to captive customers under public service obligation. The State-owned *Hrvatska Elektroprivreda (HEP-Group)* holding is the sole holder of the bundled assets of several dominant energy utilities with horizontally and vertically correlated activities in the energy sector, including electricity network operation, electricity supply and electricity generation. The Croatian Energy Regulatory Agency (HERA) has been operational in the current setup since 2004 and is empowered to regulate the matter of public interest in electricity, thermal energy, gas and oil/oil derivatives.

The overall demand of electricity consumers in Croatia is approximately 18.0 TWh with an average growth rate of 4.1% (2000-2006). Losses are relatively low compared to the region, at 2.1% in the transmission system and 7.2% in the distribution (2008). Close to 20% of the consumed electricity comes from imports. NPP *Krshko* (owned and used at 50% by *HEP*) generates another 17%. The remaining 63% is provided by indigenous power generation sources in Croatia which amount to 4.326 MW of the total installed capacity. In 2008, around 46.2% of the electricity was produced in HPPs, 0.4% came from wind generation and the remaining 53.4% from TPPs, of which around 64% of the capacity is gas-fired. As much as 89% of the engaged generation capacity and 89% of the electricity production (2008) are attributed to the State-owned company *HEP-Proizvodnja*, a subsidiary of *HEP-Group*. The Croatian TSO *HEP-OPS* operates the Croatian electric power system, which is relatively well interconnected with the neighbouring systems. Average Net Transfer Capacity (NTC) amounts to 4.8 MVA for import and 3.7 MVA for export (2008).

The main legislative framework for the electricity sector of Croatia consists of several energy laws such as: the Act on the Regulation of Energy Activities of 2004 (as amended in 2007), the Energy Act of 2001 (as amended in 2004, 2007 and 2008) and the Electricity Market Act of 2004 (as amended in 2007 and 2008). In addition, the government issued an Ordinance on Licences for Carrying out Energy Activities in 2007 and a Directive on the Validity Period for Licences for Carrying out Energy Activities in 2009.

The HERA operates pursuant to the corresponding Act and the Government Decision on the Amount of Fees for Carrying out the Regulation of Energy Activities of 2008 (as amended in 2009) which sets the terms for financing the Agency's activities as a percentage of the total annual income of the energy operators and a fee for issuing licences, acknowledging the status of eligibility and dispute settlement activities. HERA reports on its operation to the Parliament.

b. Progress made in 2009/2010

Amendments were made to the Energy Act and the Electricity Market Act in the beginning of 2009. Several important steps were taken then, aimed to foster the state of compliance and the operation of the electricity market. A clear distinction was made between activities of trading and supply to final customers. The criteria for switching the supplier were improved, as well as the aspects of transparency and reciprocity.

In November 2009, HERA approved and *HEP-OPS* adopted updated Rules on Allocation and Use of Cross-Border Transmission Capacities. The Rules fix a 50:50 ratio for sharing the interconnection capacity, enforce bilateral coordination of the methods for its allocation with a neighbouring TSO, rule out any asymmetrical or non-market allocation methods or capacity reservation save in case of force majeure, support secondary trading principles and the transfer of rights, and outline the framework for yearly, monthly and daily auctions as well as for intra-day capacity allocation. In practice, *HEP-OPS* performs coordinated auctions with MAVIR for the whole NTC on the border with Hungary. Auctions are also applied for the Croatian portion of the NTC on the borders with Serbia, Slovenia and Bosnia and Herzegovina.

Earlier in the same year, HERA adopted amendments to the Methodology on Providing Balancing Energy Services in the Electric Power System, related to the setting of a unit price of electricity for the supplier of last resort.

In October 2009, the Croatian Assembly adopted a new Strategy for Energy Development of the Republic of Croatia for the period until 2020, aiming to provide a balanced system of development relations between security of energy supply, competition and protection of the environment, and promoting quality, security, accessibility and sufficiency of energy. The growth of electricity demand is projected to be 3.7% including extensive application of energy efficiency measures and substitution of electricity.

c. State of compliance

Croatia has achieved an advanced level of compliance of its legal and regulatory framework in most of the areas covered by the *acquis*. The outstanding scope of reforms in the electricity sector has shifted to improvements and enforcement of specific provisions and monitoring of the competitive market. In line with the endeavours in the process of accession to the EU, the energy policy focus is gradually turning towards the requirements of the new EU legislative energy package (the "Third Package").

In spite of the relative advancement, further progress should still be considered with respect to several aspects of implementation of the Energy Community *acquis* into the legal and regulatory framework and/or electricity market structure in Croatia, as outlined in the following section.

Legal unbundling of key energy activities including the TSO *(HEP-OPS)* has been implemented within the *HEP-Group*. *HEP-ODS*, however, still performs a dual function in the retail market – as a DSO and at the same time as a supplier of the customers under public service (households and small enterprises) and a supplier of last resort for eligible customers. The accounts are unbundled, and compliance programs are applied (both for *HEP-OPS* and *HEP-ODS*) and regularly monitored by HERA. There is still room for achieving a more effective and transparent (legal) independence of the DSO and higher level of compliance.

Customer protection is well transposed and progressing in the area of protection of socially vulnerable customers and quality of service and transparency. In the past two years, the government partially subsidized the increase of tariffs for households applying a consumption-sensitive scheme financed from the State budget.

The development of the environment for the integration of Croatia into the regional market is comparably advanced but still not all *acquis* provisions regulating the access to cross-border transmission network capacity and congestion management are equally well applied. Particular importance should be attributed to the regional coordination of capacity allocation. The measure currently applied by Croatia provides this only on a bilateral level.

Since July 2009, the electricity market has been legally open for all customers, ahead of the required schedule, and implemented both with respect to the legal framework and to most of the practical aspects of electricity supply. In the domain of end-user supply, an efficient switching platform is implemented. However, no significant competitive behaviour of the licensed suppliers can be registered yet. Some of the obstacles for opening of the wholesale market are in the domain of balancing. Overall electricity trading and market activities are administered by the independent Croatian Energy Market Operator (HROTE). Market Rules provide the framework for basic market activities and for the initial steps toward opening up the wholesale market. However, the developed operational trading platform is still not available.

The state of compliance and efficiency of the market environment could be improved by further enforcement of the independence and competences of HERA, in particular with respect to unbundling, transparency and market concentration. This is to be seen against the background of the ownership structure of the *HEP-Group*, spreading over a major part of the energy sector, on the one hand, and the applied legal framework providing to some extent only indirect powers to HERA, relatively complex procedures and regulatory competences shared with the government, on the other hand.

In general terms, and regardless of the provisions of the Third Energy Package, another aspect of further compliance relates to the obligations for monitoring and reporting, which still need to be properly addressed.

5.3.2 Gas

a. Gas in Croatia

The supply of natural gas in Croatia comprises domestic resources (on-shore Panon) and off-shore (production fields in the Adriatic Sea), as well as imports (40% of total demand), which is in a long-term contract with Russia based on constant quantities. Household customers participate with almost 50% of the total consumption of 3.3. bcm/a. Underground storage facilities of 0.55 bcm working capacity are also in operation.

For the time being, wholesale supply is provided by only one company. The transmission system has been operated by one single TSO, fully unbundled and 100% State-owned since 2002. A storage system operator was established in 2009. Meanwhile, 38 distribution companies operate the distribution system and supply to household customers. The only distribution company has split supply and distribution system operation into two separate entities, thus complying with legal regulations set in place for operators with more than 100.000 customers.

The gas market in Croatia is governed by the Energy Law of 2001, as amended in 2004, 2007 and 2008, the Law on Regulation of Energy Activities of 2004, as amended in 2007, and the Gas Market Law of 2007, as amended in 2008 and 2009.

The Gas Market Law requires a substantial number of provisions in the secondary legislation to make the system operational. The provisions have been in place since April 2009, by the adoption of several acts, namely the Regulations on the Organization of Natural Gas Market; Network Rules of the Gas Distribution System; Network Rules of the Transport System; Terms of Use of Gas Storage and General Conditions for the Supply of Natural Gas.

Access to the networks has been defined through the tariff systems, namely the Tariff System for the Storage of Natural gas, with no tariff items; the Tariff System for the Supply of Natural gas, with the exception of eligible customers, with no tariff items; the Tariff System for the Distribution of Natural gas, with no tariff items and the Tariff System for Natural gas Transportation without tariff items. All systems were approved by the Energy Regulatory Agency, whereas tariff items were approved by the government.

Directive 2004/67/EC has been transposed by the Regulation on Security of Natural Gas of 2008, as amended twice in 2009.

b. Progress made in 2009/2010

The latest package of secondary legislation was approved in April 2009 and effectively implemented in the Gas Act.

c. State of compliance

The gas *acquis* under the Treaty has been transposed by Croatia. The focus now should be placed on the implementation in practice and the efficient functioning of the gas market. One may note in this respect that investors raise questions regarding the distribution tariffs.

5.3.3 Oil

a. Oil in Croatia

In Croatia, around 830,000 tons of oil is produced per year from 35 oil fields. The annual imports in recent years vary from 3.5 - 4 million tons (crude oil dependency of 80%). The remaining oil in place in Croatia is estimated at around 191 million tons. *INA-Industrija Nafte d.d. Zagreb* is the holder of all the approvals for exploration of energy mineral raw materials, the approvals for exploitation of fields of energy mineral raw materials and concessions for exploitation of energy mineral raw materials in the Republic of Croatia. Currently, exploration of energy mineral raw materials in the Republic of Croatia is carried out both off-shore and on-shore. The transport of crude oil is carried out by the 622 km JANAF pipeline from the tanker and terminal port of Omišalj to domestic and foreign refineries in Eastern and Central Europe. The storage capacity at the Omišalj, Sisak and Virje terminals equals 900,000 m^3. The ports' locations and maximum capacity of storage tanks are in Rijeka 1,216,000 m^3, (out of it Omišalj 820,000 m^3), Zadar 97,000 m^3, Split 77,000 m^3, and Ploče 100,000 m^3.

Two refineries, Rijeka and Sisak, exist in Croatia, with a nameplate capacity of 8 million tons/year and an average utilization rate of 64%. Domestic production of petroleum products is around 4.5 million tons, while around 2 million tons are imported. The total consumption of petroleum products in 2008 was 6.5 million tons, which is a decrease by 7.2% compared to the previous year, with the exception of LPG where consumption increased by 10.3%. Altogether, 18 companies have obtained an oil products wholesale license, while 19 companies have a license for oil and oil products storage.

The legislative framework on oil in Croatia includes the Mining Act of 2009, the Oil and Petroleum Products Market Act of 2006, the Act on Excise Duty on Mineral Oils of 2002, as amended in 2003 and 2006, the Regulation on the Rates of Excise Duty on Oil Products of 2007, the Excise Duty Act of 2009, and the Regulation on the Quality of Petroleum-derived Liquid Fuels of 2006, as amended in 2008.

Compulsory oil stocks are established by the Act on Oil and Petroleum Products Market of 2006, which provides for the establishment of a Croatian Compulsory Oil Stocks Agency. The Act defines the time frame for the creation of compulsory oil stocks at the level of a 90-day consumption and defines the quantity of stocks to be held by producers and importers of petroleum products.

b. Progress made in 2009/2010

In December 2009, the government approved the Action Plan for the establishment of 90-days compulsory stocks of crude oil and petroleum products by 31 July 2012. The Action Plan is based on the Oil and Petroleum Products Market Act of 2006. In line with the Action Plan, the Ministry of Economy, Labour and Entrepreneurship in 2009 adopted a Plan for Securing, Establishing Dynamics and Renewal of Compulsory Oil and Oil Products Stocks, Storage Organization and Regional Distribution.

In parallel, *HANDA* (the Croatian Compulsory Oil Stocks Agency) continued the process of increasing the level of compulsory stocks to: 86 days for motor spirit, 45 days for diesel oil, 44 days for gas oil, 64 days for jet fuel and 71 days for fuel oils.

c. State of compliance

The oil and petroleum market in Croatia is open, in principle, to private and foreign companies. No preference is given to domestic oil and petroleum products over non-domestic ones. There is no government intervention in price determination.

There are no customs duties on import/export of crude oil and petroleum products for EU countries and CEFTA countries.

5.3.4 Competition

a. Competition and State aid in Croatia

1 Competition law in Croatia is governed by the Competition Act in force since 2003. The Act establishes a cartel prohibition in line with Article 101(1) and (2) TFEU. With respect to the exemptions following Article 101(3) TFEU, the Act differentiates between block exemptions issued by the government (covering, inter alia, horizontal and vertical agreements), and individual exemptions to be granted by the Competition Agency upon request. The abuse of a dominant position is prohibited in correspondence with Article 102 TFEU. The notion of dominance is defined separately. The Act applies also to public undertakings, i.e. legal persons owned by the State or local and regional self-government units. The Act further includes legal and natural persons entrusted with the operation of services of general economic interest or exclusive rights *"… in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them"*. Whether and to what extent this includes the proportionality test required by Article 106(2) TFEU is, however, unclear.

In operation since 1997, the authority applying and enforcing the Act is the Croatian Competition Agency (CCA). The CCA's decision-making body is the Competition Council consisting of five members appointed by Parliament. The CCA may institute proceedings upon complaint or on its own motion. The Act calls on the CCA to apply the law in conformity with its application within the EU to the extent trade between Croatia and the EU may be affected, as required by Article 70 of the Stabilization and Association Agreement. In this context, the CCA strives to follow the "more economic approach" underlying modern EU competition policy. Undertakings violating competition law in substance will result in the company being fined up to 10% of its total annual turnover. However, the imposition of a fine currently still requires an application by the CCA to the courts, namely the competent Misdemeanour Court. Decisions of the Council may currently be challenged before the Administrative Court of Croatia. The existing Act further spells out procedural rules complementing general administrative procedural law.

2 State aid control in Croatia is governed by the State Aid Act in force since 2005. The Act defines the notion of State aid and lays down a general prohibition of State aid modelled on Article 107 TFEU. It includes possible exemptions reflecting Article 107(2) EC and part of the *Altmark* jurisprudence. Rules on *de minimis* aid and rules on environmental aid have been adopted. By-laws adopted in the domain of State aid also include rules for the compensation of the costs from the liberalisation of the electricity market in the form of a Government Decision of 2008.

As regards enforcement of State aid law, the Act tasks the Competition Agency with authorizing and monitoring State aid grants. Its Expert Team also comprises a State aid division. The State aid control procedure basically envisages that drafts for legislation containing rules for granting State aid are to be provided to the CCA for review and opinion or authorisation respectively. Decisions granting State aid are also subject to notification and prior authorisation. Unlawful aid, i.e. aid not authorised, is to be recovered. The compatibility assessment is governed more specifically by the Regulation on State Aid of 2006. Decisions taken by the Agency are subject to appeals to an administrative court.

b. Progress made in 2009/2010

1 In the area of competition law, Croatia made significant progress by adopting the new Competition Act in June 2009 which will enter into force on 1 October 2010. The improvements in the 2009 law as compared to the previous law from 2003 mainly concern procedural issues such as empowering the CCA to impose fines directly, establishment of a leniency programme, dawn raids, interim measures etc. CCA decisions can now be appealed directly (i.e. without administrative appeals) to only one court, the Administrative Court of Croatia. The new law further provides for *ex officio* assessment of agreements and opening of the proceedings in cases of abuse of a dominant position, the issuance of a statement of objection, as well as the right to propose commitments. The new Competition Act also abolishes individual exemptions from the cartel prohibition and thus shifts towards a self-assessment approach in line with the current EU model.

According to the new Competition Act, the general law on administrative procedure is to be applied subsidiarily. A new General Administrative Procedure Act was entered into force in January 2010. The Act stipulates basic procedural principles including the protection of the rights of parties, access to data, enforcement etc.

Further by-laws, inter alia on market definitions, block exemptions, *de minimis* cases, methods for setting and calculation of fines and leniency have been announced. In its annual plan 2010/2011, CCA also announced market monitoring and market investigations which hopefully will include the energy sectors.

The CCA also issued two opinions in April 2010 on draft proposals of secondary legislation in the energy sector, namely on the Ministry of Economy's draft proposals for measures to speed-up energy sector reforms, and for the determination of the interest of the Republic of Croatia in the construction of power plants/energy facilities. The CCA declared both proposals as being in compliance with the Competition Act.

2 No changes have been made to primary or secondary legislation in the area of State aid. There were no new decisions taken in the area to be brought to the attention of the Secretariat.

c. State of compliance

Articles 18 and 19 EnC have been properly transposed into Croatian law.

1 The new Law on Competition which will enter into force in the course of 2010 brings Croatian competition law largely in line with the *acquis* on competition, in particular in procedural terms.

With regard to the implementation of competition law by the CAA, the Secretariat notes that the CCA has developed a well-established body of case law. In the field of energy, in 2004 the Agency, without taking formal decisions, closed three cases concerning oil derivatives before the entry into force of the Treaty (*MOL AGRAM/MOL* on franchise agreements, *Anonymous Buyers/INA* on distribution agreements and *TIFON/Croatian Highways* and *INA* on refusal to supply). Another case of unfair pricing in distribution of natural gas (*HEP-PLIN/INAINDUS-TRIJA* in 2004) was referred to the Energy Regulatory Council. After the entry into force of the Treaty, several mergers in the markets for oil derivates were approved. (*MOL /TIFON* in 2007, *Slovenska Petrol/Euro-petrol* in 2008). In June 2009, CCA conditionally approved the *MOL/INA* merger, imposing both structural and behavioural measures. Besides several opinions in advocacy cases concerning bills on natural gas as well as on the oil and oil products market, the CCA also gave an opinion in 2006 on long-term power purchase agreements between *HEP Toplinarstvo* and the *Clinic and Hospital Centre Zagreb* where it did not raise concerns. Other opinions by the CCA in 2006 and 2008 respectively concerned the rebate and price policy of the oil company INA and the draft sales agreement between the companies INA and Crobenz, in which INA holds the majority of shares.

The most recent cases in the area of energy include the *Proplin* case concerning exclusive purchase agreements on the lease of containers for gas and agreements on the sale of gas concluded between Proplin and different undertakings, as well as natural persons for the period of 10 years. The CCA concluded that the duration of the agreements could lead to the closure of the market for competitors of Proplin and represent a barrier to entry for new suppliers by tying the buyers to Proplin. In 2008, the CCA accepted commitments by Proplin to change all the agreements on the lease of containers for gas to a duration not exceeding five years, and the agreements on the sale of gas to a duration of one year instead of ten years.

By decision of December 2008, the CCA in the case *SEDAM PLIN and BRALA TRADE/PROPLIN* held that by non-transparent and discriminatory application of its rebate policy to its buyers, Proplin abused its dominant position in the market for the sale of liquified petroleum gas (LPG) by applying dissimilar conditions to equivalent transactions with other undertakings, thereby placing them at a competitive disadvantage (Article 102(c) TFEU). Furthermore, Proplin abused its dominant position by imposing unfair trading conditions by requiring the buyer in the sales agreement to purchase LPG exclusively from Proplin.

In June 2009, CCA conditionally approved the *MOL/INA* merger, involving the markets for refining and production of oil products, exploration for and exploitation of oil and gas deposits, distribution of fuels and associated products through a chain of retail outlets, refining and production of oil products through refineries, and trading in crude oil and petroleum products. CCA imposed both structural and behavioural measures.

2 The State Aid Act basically transposes Article 107 TFEU, as required by Article 18 EnC. From an Energy Community perspective, however, it is to be noted that the purpose of the Act is to *"set out general conditions and rules for the authorisation, monitoring of the implementation and recovery of State aid for the purpose of the implementation of the international commitments undertaken by the Republic of Croatia, arising under the Stabilisation and Association Agreement between the Republic of Croatia and the European Communities"* (Article 1(1)). The notion of State aid as well as the State aid prohibition is also limited to the extent the aid *"may affect the international commitments undertaken by the Republic of Croatia referred to in Article 1"*. In a future revision, the scope of applicability of the State aid law should be broadened so as to explicitly include the Treaty.

With regard to the implementation of State aid law, the Secretariat understands that in 2006 the CAA approved individual aid granted to an undertaking (outside the energy sector) in the form of free electricity supply at a value of € 236,897.26 *(Town of Novi Marof/BBS)*; that aid was exempted as aid to SME and based on the equivalent to Article 107(3)(c) TFEU. Another case of individual aid concerned the conversion of an undertaking's *(Petrokemija)* gas debt into equity (value of € 31,644,938.20). In 2006, the agency decided that this did not constitute State aid. Furthermore, CCA's most recent (2008) report mentions State guarantees for, inter alia, the construction and maintenance of gas pipelines as well as the energy utility HEP, which again was not considered to be State aid.

5.3.5 Environment

a. Environment in Croatia

1 With regard to the environmental impact assessment, the Directive has been transposed into national law by the Environmental Protection Act which has been in force since 2007. Furthermore, a Regulation on Environmental Impact Assessment and a Regulation on Information and Participation of the Public and Public Concerned in Environmental Matters are in place.

The procedure may be summarized as follows: with regard to *screening*, the Environmental Protection Act differentiates between projects for which an environmental impact assessment is mandatory, and projects subject to evaluation of the need for an environmental impact assessment. The two respective lists are annexed to the Regulation on Environmental Impact Assessment, which also contains details of the *screening* procedure. The evaluation in the case of non-mandatory projects shall be made upon application by the developer and based on a case-by-case analysis and/or criteria detailed by the Regulation on Environmental Impact Assessment. Projects not subject to an environmental impact assessment shall, in principle, be subjected to an environmental protection study. The developer may submit a request for a *scoping* opinion to the Ministry or the competent administrative body in the county or the City of Zagreb. The *environmental impact study* itself is to be submitted by the developer together with the request to carry out an environmental impact assessment or an environmental impact assessment *screening* procedure. The *environmental impact statement* shall be developed by an authorised legal person. An advisory expert committee appointed for each project shall prepare an opinion on the study. The competent authority will review and make the final *decision* on the environmental acceptability of the project. Depending on the category of the project, the authority will be the Ministry or the competent administrative body in the county or the City of Zagreb. According to the Environmental Protection Act, the following shall be taken into account: results of the environmental impact study, opinions of the bodies and/or persons designated by special regulations; objections, proposals and opinions of the public and public concerned, as well as results of any trans-boundary consultations. As regards public consultation, the Regulation on Information and Participation of the Public and Public Concerned in Environmental Matters provides further details. The decision on environmental acceptability is a precondition for a location permit for project implementation or other project approvals. Against the decision, an administrative dispute may be initiated, without determination of standing.

2 The Wild Birds Directive has been transposed by the Nature Protection Act of 2005 and by the regulations and ordinances adopted pursuant to it. The Ministry of Culture, Directorate for Nature Protection is responsible for the implementation of the Nature Protection Act. In accordance with that act, the government has designated the ecological network with the system of ecologically important sites and ecological corridors (Regulation on Proclamation of the Ecological Network of the Republic of Croatia of 2007). Through that Regulation, Croatia implements the Wild Birds Directive (SPA sites) as well as the Habitat Directive (SAC sites), on which grounds the EU ecological network NATURA 2000 is defined. The ecological network is composed of sites important for the conservation of species and habitat types on the national and international level, including potential NATURA 2000 sites. Croatia has designated RAMSAR sites that are part of the national ecological network and for which regularly occurring migratory species not listed in Annex I of the Wild Birds Directive are qualified species.

Furthermore, the Croatian Ordinance on Nature Impact Assessment of 2007 provides a mechanism for the assessment of projects which are likely to have a significant impact on the ecological network. A nature impact assessment (NIA) is mandatory for all projects that individually or in combination with other projects may have a significant impact on the ecological network. The Ministry of Culture carries out the assessment procedure.

b. Progress made in 2009/2010

1 The Secretariat has not been informed about any development in the area of environmental impact assessment since the last reporting period.

2 In terms of wild birds protection, Croatia adopted an Action Plan for the Conservation of Biological and Landscape Diversity in June 2009. Reportedly, the Nature Protection Act was amended to ensure further alignment with the *acquis*. However, the Secretariat did not achieve any information on this.

Furthermore, in May 2009 Croatia adopted a Regulation on the Proclamation of the Ecological Network (Fourth National Report to the Convention on Biological Diversity). It takes stock of, *inter alia*, threats for the protection of biological diversity and the progress achieved in implementing the National Strategy and Action Plan.

c. State of compliance

1 The Environmental Impact Assessment Directive has been transposed into Croatian law.

2 Article 4(2) of the Wild Birds Directive has been partly transposed into Croatian law. Any further assessment is made difficult by the lack of direct information.

5.3.6 Renewable Energy

a. Renewables in Croatia

Among all Contracting Parties, Croatia takes the most consistent approach to the promotion of renewable energy sources.

1 Croatia transposed the requirements of Directive 2001/77/EC and is already at an advanced stage regarding the implementation of Directive 2009/28/EC. It is currently preparing the National Renewable Action Plan to be submitted by 30 June 2010, together with the EU Member States. More than half of the electricity production in Croatia comes from hydropower. Several (other) renewable energy projects are already operational: 69 MW in wind farms, 2 MW biomass, 2 MW waste disposal gas generation facilities and 50 KW demonstration photovoltaic installations.

2 As regards biofuels, Croatia adopted an Act on Biofuels for Transport in 2009. Targets were defined for each year, even before the Act entered into force, i.e. for 2007 and 2008. The share of 5.75% biofuels for transport has to be achieved by 31 December 2010. Several biodiesel production plants in Croatia contribute to the fulfilment of the targets.

b. Progress made in 2009/2010

1 As part of the negotiations for EU accession, Croatia agreed to a mandatory national target for renewable energy of 20% in gross final energy consumption in 2010. The Energy Development Strategy adopted in 2009 also includes a strategic objective of a 35% share of renewable energy in total electricity generation (including large HPPs) by 2020.

2 In April 2010, an Ordinance on the Measures for Promotion of Use of Biofuels was adopted. The Ordinance specifies the method for preparation of the programme and the plan of the party liable for placement of biofuels on the market, the method of keeping the registry of parties liable for placement of biofuels on the market and the method of keeping records about placement of biofuels on the market. The Ordinance constitutes one of the final steps in achieving full compliance with the *acquis* regarding biofuels and the adopted plan on the implementation of Directive 2003/30/EC. Other required by-laws are in the final stage of preparation.

Besides, Croatia has prepared a National Renewable Energy Action Plan, including biofuel requirements in line with the new Directive 2009/28/EC, as part of the EU accession process, regardless of the eventual adoption of the Directive within the Energy Community.

c. State of compliance

Croatia submitted its plan to implement Directives 2001/77/EC and 2003/30/EC to the Ministerial Council in June 2007, as required by the Treaty.

1 Croatia set a target of 5.8% of incentivised electricity (excluding HPPs over 10 MW) to be generated from renewable energy by 2010, starting from a 0.7% share in 2007. The share of RES in total electricity consumption is monitored annually by the Ministry of Economy, Labour and Entrepreneurship.

The support scheme used to incentivise RES producers is feed-in tariffs. Different levels of support based on capacity and/or technology are adopted for various RES, including cogeneration. The market operator HROTE is obliged to buy the electricity produced from eligible RES producers, the status of which is granted by the Croatian energy regulatory authority. TSO and DSO are responsible for grid access. The shortcomings of the grid code related to renewable energy have partly been overcome by the transmission system operators HEP-OPS' "Additional Technical Conditions for the Connection and Operation of the Wind Power Plant" adopted in 2008.

The administrative procedures, namely authorisation or licensing constitute the main barriers to the development of renewable energy projects. The procedures are not suited for small or mid-range renewable projects and could take more than four years for completion. Besides, there are some limitations for wind projects along the Adriatic coast due to environmental reasons.

2 The existing legislative framework on biofuels is in compliance with the adopted plan and with Directive 2003/30/EC. However, further activities to implement all measures and to fulfil the defined targets beyond 2010 will be needed.

5.3.7 Energy Efficiency

a. Energy efficiency in Croatia

The legal framework on energy efficiency is well developed and consists of the following primary and secondary legislation:

The Act on Energy End-Use Efficiency was adopted in 2008 and transposes Directive 2006/32/EC. This Act regulates the energy end-use efficiency, adoption of programmes and plans for energy efficiency improvement and their implementation, energy efficiency measures (especially activities of energy services and energy audits), obligations of the public sector, energy subjects and large consumers as well as consumers' rights with regard to the application of energy efficiency measures.

Directive 2002/91/EC on the Energy Performance of Buildings has been transposed by the Act on Physical Planning and Construction of 2007 and amended in 2009, as well as by a Technical Regulation on Heating and Cooling Systems for Buildings of 2008, a Technical Regulation on Rational Use of Energy and Thermal Protection in Buildings of 2008 as amended in 2009, an Ordinance on Certification of Energy Performance of Buildings of 2010 and an Ordinance on the Requirements and Criteria to be met by Energy Auditors and Energy Certifiers of Buildings of 2008, as amended in 2009.

Directive 92/75/EEC and the implementing Directives on the indication by labelling and standard product information of the consumption of energy and other resources by household appliances have been transposed through the Energy Act of 2001, as amended in 2004, 2007 and 2008, and the Ordinance on Energy Efficiency Labelling of Household Appliances of 2007. A State Inspectorate is responsible for ensuring compliance with the legislation and regulation.

The Act on Public Procurement of 2007, as amended in 2008, determines energy efficiency as one of the possible criteria in public tenders. Public procurement guidelines on how to apply energy efficiency criteria have not yet been developed, although the National Energy Efficiency Action Plan (NEEAP) envisages this activity. Within the UNDP project *"Removing barriers to energy efficiency in Croatia"*, the procurement guidelines on green public procurement issued by ICLEI are translated into Croatian and presented to the national and local public authorities. It is expected that the newly established Central Office of Public Procurement will take further steps in 2010 regarding this matter in cooperation with the Ministry of Economy, Labour and Entrepreneurship (MoELE).

The MoELE is responsible for overall monitoring of energy efficiency policy implementation and reporting, in close cooperation with the Ministry of Environmental Protection, Physical Planning and Construction (responsible for buildings) and the Environmental Protection and Energy Efficiency Fund.

Pursuant to the Act on the Environmental Protection and Energy Efficiency Fund of 2003, the Environmental Protection and Energy Efficiency Fund was established in 2003, with the aim to finance programmes and projects in the field of environmental protection, energy efficiency and renewable energy. It is also responsible for monitoring of the NEEAP and verifying achieved energy savings.

Within the framework of the *"Intelligent Energy for Europe Program"* supported by the European Commission several energy agencies (four regional and one local) were set up.

The Energy Service Company HEP ESCO, which was established in 2003 with funding from the World Bank and Global Environmental Facility and national financial contribution, prepares, carries out and finances energy efficiency projects on a commercial basis in Croatia.

b. Progress made in 2009/2010

Energy efficiency continues to play an important role in Croatian energy policy and significant progress can be reported during 2009/2010.

A National Energy Efficiency Programme for the period 2008-2016 was adopted by the government in April 2010. The Programme determines the national indicative energy saving target of 9% (for 2016) in accordance with Directive 2006/32/EC, and also determines an intermediate target of 3% for the first three year period (2008-2010). In addition, the 1st National Energy Efficiency Action Plan was developed, based on the above Programme, and adopted in April 2010.

In accordance with the NEEAP currently three main projects are implemented by the UNDP and MoELE in line with the *"Removing Barriers to Energy Efficiency"* project, namely:

- *"House in Order"*: a project focusing on enhancing energy efficiency in all central government buildings;
- *"Systematic energy management in cities and counties"*, targeting buildings at the local and regional level;
- An info-educational campaign on energy efficiency (including marketing activities and cooperation with media, various workshops, public discussions, training seminars, professional meetings and conferences, support for Energy Efficiency Info Offices and Energy Efficiency Corners etc.).

Croatia is also actively taking part in the Energy Efficiency Task Force, with the Croatian representative acting as the Chairman of the Task Force.

Pursuant to the Work Programme of the Energy Efficiency Task Force, in May 2010 Croatia submitted to the Secretariat a Roadmap for implementation of the energy efficiency directives.

Further work on secondary legislation will continue during 2010. This is said to include an Ordinance on a Unique Information System for Energy Efficiency; an Ordinance on Energy Audits and an Ordinance on Authorisations for Performing Energy Audits. Training on energy audits was carried out, and more than 500 specialists passed the auditors' exam.

c. State of compliance

As the deadline for implementing the energy efficiency directives does not expire until December 2011, the state of compliance is currently not assessed. Croatia has fulfilled its obligations under Articles 4 and 14 of the Energy Services Directive. The Energy Efficiency Action Plan was already adopted by the Government in April 2010.

Croatia advances quickly on the path towards full implementation of the energy efficiency *acquis* and may be regarded as a model country for other Contracting Parties. One of the risks for future successful promotion of energy efficiency might be the insufficient institutional capacity (i.e. the lack of a specialized Energy Efficiency Agency) to lead the complex process of the NEEAP implementation. Further efforts are required to support the establishment/capacity development of the energy efficiency units within all main players: State and local authorities, Environmental Protection and Energy Efficiency Fund etc.

5.3.8 Social Issues

a. Social issues in Croatia

Based on the report of the Ministry of Economy, Labour and Entrepreneurship, no less than 51 EU directives related to social and labour law issues are transposed or were planned to be transposed by the end of 2009 into national legislation. To list them all here would go beyond the scope of this report.

b. Progress made in 2009/2010

Croatia prepared the Social Action Plan (SAP) approved by the government in December 2009. The SAP was prepared by a working group consisting of the representatives of the Ministry of Economy, Labour and Entrepreneurship, the Ministry of Health and Social Issues, the Croatian Energy Regulatory Agency and the Union of Autonomous Trade Unions of Croatia.

The SAP includes activities focused on achieving the following specific goals:

- Ensuring of vulnerable consumers' protection in line with the sustainable and competitive energy market;
- Strengthening information and consultation mechanisms of social partners in the energy sector;
- Improvement of the organisation of work and qualifications structure of employees;
- Improvement of working conditions and living standard, workers' rights, and safety at work in the energy sector.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.4 FORMER YUGOSLAV REPUBLIC OF MACEDONIA

5.4.1 Electricity

a. Electricity in the Former Yugoslav Republic of Macedonia

The electricity sector of the Former Yugoslav Republic of Macedonia has been largely unbundled since 2004, at least compared to most of the Contracting Parties. The transmission system operator *MEPSO* is legally unbundled, while the distribution company, i.e. the distribution system operator and public supplier *EVN Makedonija* is unbundled from all other activities. It was privatized in 2005 by selling 90% of its shares to the Austrian utility company *EVN*. Most of the remaining incumbent generation is still concentrated in a single State-owned company, *ELEM*. The Energy Regulatory Commission (ERC) has been operational since 2003. It is empowered to regulate the electricity sector and monitor the electricity market in the country.

The electricity system of the Former Yugoslav Republic of Macedonia is characterized by a relatively high level of imports. The overall amount of electricity required to cover the demand amounts to 8.64 TWh (2008). The domestic generation in the same year reached the level of 5.83 TWh, covering 67.6% of the demand, while the remaining 32.4% are supplied from imports. As much as 5.00 TWh or 86% of the indigenous electricity was generated in lignite/oil-fired thermal power plants, with an overall installed capacity of 1,010 MW, representing 64% of the total installed capacity. The hydropower capacity amounts to 528 MW.

The electricity market is open for all customers supplied on 110 kV or higher voltage levels by a decision of the government. This is not in compliance with the requirements and the timetable for the market opening according to the Treaty.

The transmission system is interconnected with Serbia, Bulgaria and Greece.

The energy sector, including the electricity sector in the Former Yugoslav Republic of Macedonia is governed by the Energy Law of 2006, as amended in 2007 and in 2008.

Besides that, secondary legislation was introduced by the relevant authorities. It includes a Tariff System for Electricity, issued in 2010 by ERC. ERC also adopted Rulebooks on: the Method, Conditions and Procedure for Issuing, Changing, Extension and Suspension of Licenses (2009); the Method and Conditions for Regulation of Electricity Prices (2008), the Method and Conditions for Setting and Approving a Privileged Tariff for Electricity from RES (rulebook for small HPP, wind, photovoltaic, geothermal, biomass, biogas from biomass, - in the period between 2007 and 2010); the Conditions of Supply (2009 as amended in 2010); the Conditions, Method and Procedure to obtain the Status of Eligible Customer (2006). ERC further approved the Transmission Grid Code (2007) and the Distribution Grid Codes (2008 for *EVN*, and 2010 for *ELEM*).

b. Progress made in 2009/2010

In 2009 and with a view to, *inter alia*, complying with the Secretariat's Reasoned Opinion in Case ECS 2/08 (see below), the government adopted an action plan to bring its legislative framework in line with the energy *acquis*. Based on this, a draft Energy Law has been finalized and commented upon several times by the Secretariat during the drafting. It has been announced that the final proposal would be sent to the Secretariat for comments in June 2010. However, the new Law has not been adopted by 1 July 2010, as envisaged by the action plan.

In terms of secondary legislation, the development of a Rulebook on a Tariff System for Electricity in 2010 marks a step towards the development of cost reflective supply prices. This has to be extended to cover network tariffs too, so as to start establishing the formal conditions for market opening on the distribution level.

Some of the data required by Regulation 1228/2003 are publicly available, but only in the local language. The rules for allocation of interconnection capacity for 2010 are published, as well as results of annual, monthly and weekly auctions. The method for capacity allocation is explicit auctions split 50:50, whereby the price is set as "pay as bid" on all borders. Day-ahead auctions are not implemented. Allocated capacity is not transferable but has to be returned to *MEPSO* (use-it-or-lose-it). The maintenance plan of interconnections and internal lines for 2010 is published.

Pending tasks include the finalization of the Market Rules pursuant to the new Energy Law, reviewing the non-compliant Rulebook on the Method and Conditions for Regulation of Electricity Prices and the adoption of methodologies to establish transparent and non-discriminatory network tariffs, and finally setting of an adequate tariff system for use of the transmission network and for use of the distribution network. The draft Market Rules are published on the TSO's web page for comments. A revised version, based on ERC's comments is expected to be submitted to ERC for approval by the end of August 2010.

c. State of compliance

The existing Energy Law has some major flaws in terms of implementation of the energy *acquis*. Some of these issues of non-compliance are addressed in the Reasoned Opinion issued by the Secretariat in July 2009 in pending Case ECS-2/08. The case addresses the failure by the Former Yugoslav Republic of Macedonia to open the market for non-household customers in accordance with Article 21 of Directive 2003/54/EC, the non-compliance with the tasks assigned to the regulated generator in accordance with the Treaty's rules on free movement of goods and competition as well as the lack of cost-reflectivity of distribution tariffs.

Furthermore, the current Law refers to transit of electricity as a separate activity and requires licensing of transit as an energy activity. This is not compliant with Directive 2003/54/EC and may raise an additional administrative barrier on energy undertakings wishing to access the network for "declared transit".

The existing legal framework does not provide for exemptions for new interconnectors (the so-called merchant lines).

There are a number of aspects related to cross-border transmission capacity allocation and congestion management where the Law is not in compliance with the *acquis*. The TSO is not obliged to closely cooperate with neighbouring TSOs and other TSOs affected by physical flow conditions, and to coordinate the congestion management method. Common coordinated congestion management method and compatible congestion management procedures have yet to be adopted. The rules for the auctioning of annual interconnection capacity allocation grants rights for capacity use only to bidders who would use the capacity to supply customers in the Former Yugoslav Republic of Macedonia: This is in breach of Art 6 of Regulation 1228/2003 and the principle of non-discrimination. Furthermore, bidders have to pay an administrative fee for auctioning (ranging from € 4,500 for annual to € 300 for weekly auctions). Such administrative barriers contravene Art 41 of the Treaty. Generally, the use of congestion income including the revenues from auction fees is not explicitly defined in ERC rules and is not made available online by *MEPSO*.

Moreover, legislation related to regulatory powers for the provision of balancing services is missing. The same is true for secondary legislation required for market opening. The terms and conditions for the provision of balancing services and network tariffs, such as development of methodologies to establish terms and conditions for access to the network and transmission and distribution tariffs, requirements related to the provision of information by the supplier on the fuel mix and environmental effects and transparency of operation in general need to be established.

MEPSO is applying charges to users connected to its system based on bilateral contracts, and these are not set or approved by the regulator. This constitutes a breach of the principle of regulated third-party access.

The notion of "direct consumers" and "indirect consumers" in the Law and in secondary legislation is not consistently applied. The term "direct customer", as somebody who is directly connected to the high voltage transmission network, should be avoided as it unduly mixes technicalities with market opening requirements.

The current tariff system for the use of the network relates to the bundled cost of service required only for determination of the regulated revenue of the service provider (i.e. the network operator). This is not transparent enough, does not provide adequate price signals and does not ensure non-discrimination between tariff and eligible customers.

5.4.2 Gas

a. Gas in the Former Yugoslav Republic of Macedonia

The gas market in the Former Yugoslav Republic of Macedonia is currently rather small: an average of 0.1 bcm is consumed per year and exclusively by industrial customers. The entire gas supply is provided by sources from Russia, through Ukraine, Moldova, Romania and Bulgaria. There is only one wholesale supplier in the country. The transmission system operator was established in 2006. The ownership over the transmission network is still not clear and is subject to a dispute between the State and the private company *Makpetrol*. The dispute has a noticeable impact on the functioning and further development of the gas market.

In legal terms, the gas sector is governed by the Energy Law of 2006, as amended in 2007 and 2008.

Access to the network has been defined by secondary legislation, namely the Rulebook on the Method and Conditions for Regulating Prices for Transport, Distribution and Supply of Natural Gas, the Tariff System for Transport of Natural Gas and the Tariff System for Selling Natural Gas to Tariff Customers. Since March 2009, a Grid Code for the Transmission of Natural Gas has been in place.

The Rulebook of the Conditions, Method and Procedures for Obtaining and Ceasing the Status of Eligible Customers of Natural Gas defines the terms of market opening.

b. Progress made in 2009/2010

In 2010, a draft for a new Energy Law was presented in several versions to the Secretariat. According to the action plan submitted by the government, the new Energy Law should be approved by 1 July 2010.

The Rulebook on the Method and Conditions for Regulating Prices for Transport, Distribution and Supply of Natural Gas has been amended at the end of 2009. Some crucial elements relevant for the tariff determination are still set out in an insufficiently transparent manner.

c. State of compliance

Several crucial provisions of Directive 2003/55/EC are still not transposed by the primary legislation in force: the unbundling requirements in terms of legal form, TPA exemptions for new infrastructure, combined operators, and refusal of access. Furthermore, the provisions on market opening are still not in line with the Treaty. Eligible customers are suppliers of retail tariff customers and all customers with an annual consumption above 10 mcm, i.e. not all non-household customers as required after 1 January 2008.

Regulation 1775/2005 has been transposed, with the exception of the provisions on secondary markets, by the Grid Code for Transmission of Natural Gas. However, to make the Grid Code fully operational, some crucial provisions as described above still have to be transposed into primary legislation.

The existing Energy Law deals with security of supply only with respect to Directive 2003/55/EC. The entire Directive 2004/67/EC still needs to be implemented.

If the new draft Energy Law, as presented to the Secretariat, were to enter into force, the state of compliance of the Former Yugoslav Republic of Macedonia would be significantly improved. At this point in time, however, the Secretariat cannot speculate on when and which provisions will be adopted. It also has to be noted that, upon the approval of the new primary legislation, the existing secondary legislation will have to be harmonized accordingly.

5.4.3 Oil

a. Oil in the Former Yugoslav Republic of Macedonia

There is no domestic production of crude oil in the Former Yugoslav Republic of Macedonia.

The only oil refinery in the country, *OKTA* in Skopje, is owned by a subsidiary of *Hellenic Petroleum* from Greece. *OKTA* was connected in 2002 with the Thessalonica port in Greece through the 21.6 km long oil pipeline Thessalonica-Skopje with a capacity of crude oil flow of 360 m^3/h.

The current consumption of petroleum products is around 820,000 tons and anticipated to increase by 5% in 2010. Of the currently 320 petrol stations operating in the country *Makpetrol* owns 44%, the *OKTA* refinery 14%, *Lukoil Macedonia* 4%, and the remaining 38% belong to several small privately owned domestic companies.

The oil sector in the Former Yugoslav Republic of Macedonia is governed by a set of laws and secondary legislation including the Mineral Resources Law; the Energy Law, and the Law for Transport of Dangerous Substances in Road and Railway Transportation.

Compulsory oil stocks are regulated by the Law on Compulsory Reserves of Oil and Oil Derivatives of 2008 as well as by the Decree on the Method for Determining, Calculating, and the Payment of the Fee for the Compulsory Reserves.

Setting petroleum product prices lies in the competence of the Energy Regulatory Commission (ERC). The calculation of the adjusted ex-refinery price in relation to the cost of the crude oil is done by reference to the average International Brent price. The prices of petroleum products are calculated every 14 days in accordance to the stock's movement of crude oil and petroleum products.

b. Progress made in 2009/2010

In February 2010, the government adopted a medium-term programme for the establishment of compulsory reserves of oil and oil derivatives for the period of 2010-2015. In March 2010 the Directorate for Compulsory Reserves of Oil and Oil Derivatives adopted an annual programme for the establishment of compulsory reserves of oil and oil derivates for 2010.

The establishment, management and financing of the compulsory reserves for oil and oil derivatives shall be done with funds from a fee included in the price of oil derivatives to be paid by the importers and producers of oil derivatives. The medium-term programme envisages the maintenance of 70% reserves for petroleum products and 30% reserves in the form of "tickets". In the case of distortion of the energy safety, the government shall take a decision on the type, quantity and price of oil derivatives to be sold.

c. State of compliance

The market of oil derivatives in the Former Yugoslav Republic of Macedonia is fully liberalized. The conditions are generally equal for all companies participating in the oil market.

A 1% customs duty applies to the import of crude oil. For petroleum products, customs duties are as follows: duties on imports from non-EU countries are 20%, mainly for gasoline, diesel and mazout (heavy fuel oil), while for imports from EU countries, the customs duty is 4%. These customs duties are violations of Article 41 EnC and need to be removed. Customs duties on products of EU origin are planned to be abolished starting 1 January 2011.

5.4.4 Competition

a. Competition and State aid in the Former Yugoslav Republic of Macedonia

1 Competition law in the Former Yugoslav Republic of Macedonia is governed by the Law on Protection of Competition applicable since 2005 and amended in 2006 and 2007. The prohibition of cartels follows closely the wording of Article 101 TFEU. Without notification being mandatory, individual derogations may be granted by the competition authority (Article 11), a possibility which has never been used. Block exemptions are foreseen by law and by regulations for, *inter alia*, certain horizontal and vertical agreements. The Law also prohibits abuses of a dominant position. As compared to Article 102 TFEU, two explicit examples for an abuse are added (refusal to deal and refusal to grant access to essential facilities). According to the Law, the existence of an abuse and its remedy shall be determined by the competition authority. With a view to implementing Article 106 TFEU, the Law covers public undertakings owned by the State or municipalities as well as undertaking entrusted with *"performing services of general economic interest or granted with special and exclusive rights or concessions, except in cases when the application of the provisions of this Law would prevent the performance of competencies stipulated by the law or for the purpose of which those entities are established"*. Whether and to what extent this includes the proportionality test required by Article 106(2) TFEU is, however, not apparent in the Law.

The competent authority under the Law is the five-member Commission for Protection of Competition (CPC). As regards competition procedure, the Law establishes rules as *leges specialis* to the general administrative procedure. The Commission since 2007 has the authority to fine undertakings violating competition law by initiating a misdemeanour procedure. As regards violations of the substantive provisions of the Law, fines of up to 10% of the annual turnover may be imposed on undertakings, as well as up to 10,000 € and a temporary ban on professional performance on the natural persons responsible for the undertaking. A leniency policy does not exist. Decisions taken by the Commission may be appealed to an administrative court. The misdemeanour decision on fines may be challenged separately. The Law also provides for the possibility of obtaining compensation of damages for victims of competition law violations.

2 Control of State aid is governed by the Law on State Aid entered into force since 2004. The Law contains a State aid prohibition and rules on the notion of compatible aid in accordance with Articles 107(2) and (3) TFEU. The Law makes an exemption for *de minimis* aid.

The competent monitoring authority is also the Commission for Protection of Competition. The operational work is performed by a Unit on State Aid Control. The Commission shall be notified in advance of plans of providing aid. The procedure before and the notification to the Commission is determined by a regulation on the procedure and forms of notification to the Commission. The Commission's subsequent decisions are binding. Appeals against these decisions by the provider of the aid and interested parties are governed by the Law on Protection of Competition.

b. Progress made in 2009/2010

1 A draft Law on Protection of Competition has been prepared and is expected to enter into force by the end of 2010. As regards the cartel prohibition, the draft proposes a shift to a legal exemption regime in principle, giving, however, CPC the competence in the public interest to adopt exception decisions. Similarly, the dependence of an abuse on a decision by the CPC has been erased. In terms of the procedure, the draft Law strictly differentiates between misdemeanour matters (for sanctions) and administrative matters. It includes rules on evidence (information and investigation rights), the calculation of fines and leniency.

As to the enforcement of competition law, the CPC on 18 December 2009 approved a merger in the oil market *(Hellenic Petroleum S.A./BP Hellas S.A. Oil Trading).*

2 No new developments can be reported with respect to transposition or implementation of the State aid *acquis*. A new Law on State aid is still under preparation and is currently being considered by the government. It, however, has not been submitted to the Secretariat. According to the internal plans, adoption of the new Law is envisaged by 31 August 2010. The Secretariat is not aware of cases before the Commission for Protection of Competition in the energy sectors.

c. State of compliance

Articles 18 and 19 EnC have been partly transposed into the law of the Former Yugoslav Republic of Macedonia.

1 Despite following the EU model in principle, competition legislation still requires further legislative efforts in order to achieve full compliance with the *acquis*, mainly on the enforcement side. Moreover, homogeneous application of competition law in accordance with EU rules and practice is limited to cases under Article 69 of the Stabilisation and Association Agreement, namely where trade between the Former Yugoslav Republic of Macedonia and the EU may be affected. This should also be corrected from the perspective of the Energy Community Treaty. Otherwise, the new draft considerably increases the degree of compliance with the EU model on substance and procedure.

With regard to the implementation of competition law in the energy sectors by the Commission for Protection of Competition, three decisions are worth mentioning, namely (1) the approval of the take-over by *EVN* of *ESM* in 2006, based on the grounds that the company had and would have a dominant position in the relevant product markets for electricity distribution, electricity distribution system management and retail electricity supply to tariff customers before and after the merger, and consumers could expect benefits from the concentration; (2) the 2006 opinion that the planned takeover of *TPP Negotino* by *EVN* would constitute a significant restriction of competition on the markets for electricity distribution, electricity distribution system management and retail

electricity supply to tariff customers markets for electricity generation and distribution by giving EVN a considerable share of the electricity generation market; and (3) in 2007, the determination of an abuse of a dominant position (unfair selling prices) by *EVN-ESM* on the market for retail supply of electricity for tariff costumers by charging those customers a handling fee. The Administrative Court, based on procedural deficiencies, quashed the latter decision in 2009.

2 The scope of the Law on State Aid is also unduly limited to cases where *"the aid may affect trade between the* [Former Yugoslav] *Republic of Macedonia and the European Community"*. From an Energy Community perspective, the scope of applicability of State aid law needs to be broadened.

With regard to the implementation of State aid law in the energy sector by the Commission for Protection of Competition, the Secretariat has been notified of two decisions: (1) In 2007, the Commission approved individual State aid in form of a grant in the amount of 14,754,098 € to the State-owned transmission system operator *MEPSO*. The grant was used to purchase oil for the operation of TPP *Negotino* as a response to a shortage of electricity supply stemming from an increase in demand by large consumers and the close-down of NPP *Kozloduj* in Bulgaria. The Commission declared the aid to be compatible in accordance with the clause corresponding to Article 107(3)(b) TFEU of the Law on State Aid. (2) In April 2008, the Commission found that individual State aid in the form of 530,065,880 kWh electricity supplied at discounted price by *MEPSO* to the ferro-silicon producing company *SILMAK* in the period from 1 January to 30 September 2006 worth 2,194,676 € in accordance with the clauses corresponding to Article 107(3)(a) and (b) TFEU of the Law on State Aid. In both decisions, fulfilment of the criteria for an area where the standard of living is abnormally low or where there is serious underemployment (Article 107(3)(a) TFEU) and the existence of a serious disturbance in the economy of a Party (Article 107(3)(b) TFEU) were not further reasoned.

5.4.5 Environment

a. Environmental issues in the Former Yugoslav Republic of Macedonia

1 Environmental impact assessment is covered by the Environmental Law of 2005, as amended in 2007. Furthermore, several pieces of secondary legislation ("ordinances") are in place which spell out further the provisions of the Law. With regard to *screening*, the Law mandates the government to specify projects for mandatory environmental impact assessment, define criteria for non-mandatory projects and changes to existing projects. The manner and the procedure of environmental impact assessment screening procedures for projects, as well as the form and the content of EIA screening is set out in secondary legislation. The necessity for an environmental impact assessment for non-mandatory projects is to be decided on a case-by-case basis. In exceptional cases, an alternative environmental impact assessment procedure shall apply, the method of which is to be determined by the government. Upon notification of the intent for implementing a project, the competent authority is to carry out a *screening* procedure and adopt a decision upon notification of the developer which shall include an assessment on the need for an EIA. The screening decision is to be published and may be subject to appeal to the so-called Second Instance Commission. Furthermore, a *scoping* opinion may be requested by the developer. The scope is to be determined by the competent authority after consultation with the developer and the public. The *environmental impact study* is to be submitted to the competent authority by the developer, making use of licensed experts. As regards the review of the study presented in the *decision-making* phase, the Law calls for a consultation with municipalities, other authorities and the public following publication. A public hearing is to be held. The Law also lays down rules on environmental impact assessment in trans-boundary cases for projects located inside and outside the country. Finally, the competent authority or external experts are to establish an adequacy report. Based on this report, the competent authority grants or denies consent to the project implementation. This consent is a prerequisite for the project implementation permit and shall be published. The public concerned is eligible to appeal the environmental impact assessment decision to the Second Instance Commission of the government, and to a court for interim measures.

2 The Ministry of Environment and Physical Planning and the Ministry of Agriculture, Forestry and Water Economy are in charge of implementing the Wild Birds Directive. The 2004 Law on Nature Protection, as amended in 2007 and 2010, as well as the Law on Hunting from 1996, as amended in 2004 and 2009, aim to transpose the Wild Birds Directive. The former Law provides for a natural impact assessment procedure and sets rules on conservation measures for wildlife in general and endangered animals in particular (protected and strictly protected wild species). The Law also sets the basis for the designation of special protection areas (SPA), including water habitats (wetlands).

An initial assessment of areas important for regularly occurring migratory species has reportedly been carried out. The Law on Nature Protection further explicitly requires that electrical lines, technical components and windmills producing electric power shall not endanger birds with power shocks and mechanical injuries and/or killings. Existing power-line poles and technical components endangering birds need to implement measures of protection against electric shock.

b. Progress made in 2009/2010

1 There has been no progress reported in the implementation of the Environmental Impact Assessment Directive.

2 In terms of the protection of wild birds, the Secretariat has been informed that the Law on Hunting was amended in 2009. This Law has not been made available to the Secretariat. Currently transposition efforts have been undertaken to amend the Law on Nature Protection, as well as drafting secondary legislation to transpose the Directive. The Secretariat has not received any drafts so far.

c. State of compliance

1 With regard to the implementation of the Environmental Impact Assessment Directive, the Environmental Law as amended in 2007 and a number of by-laws follow closely the structure and content of the Directive. The Directive has largely been transposed into national law.

2 The Laws on Nature Protection and on Hunting only partially transpose the Wild Birds Directive. In order to achieve full transposition of the Directive, more efforts are still required. The schedule submitted to the Secretariat in that respect includes (a) carrying out an assessment of Annex I bird species and regularly occurring migratory species by the end of 2010, (b) identifying and designating special protection areas (SPAs) by the end of 2011, (c) establishing measures to ensure that bird populations are maintained at appropriate levels, both inside and outside SPAs by the end of 2012, (d) taking special conversation measures to protect the habitats of Annex I species and regularly occurring migratory species by the end of 2011, (e) establishing a general system of protection for all wild bird species by the end of 2011, (f) establishing a system of authorisations for any derogation by the end of 2011, (g) establishing measures to ensure that hunting of Annex II species does not jeopardize conservation efforts by the end of 2011, (h) prohibiting certain types of capture/killing by the end of 2009 (no further information available to the Secretariat), (i) establishing an effective inspection and enforcement system by the end of 2011 and (j) establishing information systems to enable reports to be sent to the Commission by the end of 2012. Evaluation as to whether special conservation measures are required to protect the habitats of vulnerable or rare species has not yet been done in a comprehensive manner.

5.4.6 Renewable Energy

a. Renewables in the Former Yugoslav Republic of Macedonia

The policy on renewable energy sources is defined by the Strategy for the Exploitation of Renewable Energy Resources, which was adopted recently by the Government, and, by the Strategy for Energy Development until 2030 which was adopted in 2010. The Strategies provide a review of available renewable energy resources in the Former Yugoslav Republic of Macedonia, and stipulate the targets of renewable energy in the final energy consumption of 21% by 2020 and 27% by 2030.

1 The total installed capacity in hydro power plants represent 33.3% of the total generating capacity and consist of 7 large HPPs and several small HPPs, with a combined capacity of 500 MW. Production of electricity in hydro power plants is highly variable due to the climate conditions. The existing potential for large and small hydro power plants is 1.8 GW. Meanwhile, wood is primarily used for household heating. The 2005 statistics indicate a share of up to 10% in total final energy consumption. Other significant renewable energy sources are geothermal and solar power, while the potential of wind power has not been mapped so far.

An indicative target for electricity produced from RES in total electricity consumption has not yet been set. However, a few steps have been taken toward the achievement of the submitted plan. Secondary legislation has been developed mostly in 2006-2008 to promote renewable energy. Feed-in tariffs for wind, small hydro, biomass/biogas and photovoltaic installations have been set, as well as a certification system based on the guarantees of origin. The market operator established within the transmission system operator MEPSO is obliged to buy all the electricity produced from RES. However, there is currently no Market Code adopted.

2 Indicative targets (5.7% by 2010 and 10% by 2020) for biofuels were already set in 2006 by the Rulebook for the Quality of Liquid Fuels and by the Energy Law in 2008. There are facilities in the country for the production of biofuels, but imports play a significant role.

b. Progress made in 2009/2010

1 The draft Energy Law currently under preparation envisages the transposition of Directive 2001/77/EC. Proper transposition will be needed as a basis for the completion of the secondary legislation to support full implementation. In 2009, a decision on defining the eligibility of RES producers to obtain the status of privileged producers and receive feed-in tariffs has been adopted.

2 The new draft Energy Law introduces more concrete provisions regarding biofuels. Those provisions will enable introduction of obligatory targets in the future. The Rulebook for the Quality of Liquid Fuels has also been revised during the reporting period. The main changes are related to the obligatory blending ratio.

c. State of compliance

The Former Yugoslav Republic of Macedonia submitted its plan to implement Directives 2001/77/EC and 2003/30/EC to the Ministerial Council in June 2007, as required by the Treaty.

1 A RES target remains to be set in accordance with Directive 2001/77/EC. Allegedly, the recent activities of the Energy Community related to the implementation of Directive 2009/28/EC delayed the decision on the adoption of a RES target.

The Grid Code provides no reference for renewable energy. The provisions related to the connection to the grid are applicable to all types of producers, stipulating that all applicants are requested to bear the costs of connection. The national regulatory authority has not required priority dispatch for the electricity produced from renewable sources, although it has that power according to the Energy Law, and the Grid Code makes no exceptions for covering frequency fluctuations.

Renewable energy projects face administrative barriers due to inefficient, uncoordinated and non-streamlined approaches in all public institutions involved with promoting RES. More capacity building in terms of human resources and training is needed for all institutions that are responsible for creating a proper environment that fosters investments in renewable energy projects.

One major obstacle in promoting RES further is the price of electricity for the end-users which is heavily subsidized and not cost-reflective. This status could be changed as the draft of the new Energy Law provides the mechanism for RES integration into the market and allocation of costs on all customers.

2 Due to the voluntary approach of the Treaty, very few activities have been undertaken towards the realization of the indicative target set up in 2006 for biofuels.

The regulatory authority ERC is responsible for the determination of biofuel prices. The methodology should be reconsidered carefully in order to avoid distortion of competition, and remain in line with the new Energy Law once it is adopted.

Once the new Energy Law is adopted, many provisions of Directive 2003/30/EC will need to be further transposed by way of secondary legislation.

5.4.7 Energy Efficiency

a. Energy efficiency in the Former Yugoslav Republic of Macedonia

There is no energy efficiency law in force in the Former Yugoslav Republic of Macedonia. The current Energy Law (as amended in 2008) includes a Chapter on Energy Efficiency and Renewable Energy Sources and additional provisions for the labelling of household appliance. The draft for a new Law envisages clearer provisions on energy efficiency and aims at transposing the *acquis* on energy including energy efficiency. In 2005, an Energy Agency was established which deals with energy efficiency.

The Directive 2002/91/EC on the energy performance of buildings has been partially transposed into the national legislation through adoption of the Rulebook for Energy Efficiency in Buildings of 2008. The Rulebook's entry into force has been postponed to January 1, 2011. However, a new Rulebook for Energy Efficiency in Buildings will be prepared in 2010.

b. Progress made in 2009/2010

A first (draft) National Energy Efficiency Action Plan (NEEAP) was prepared and submitted to the Secretariat in May 2010, in accordance with the Energy Efficiency Task Force Work Programme. The Secretariat commented on the draft version of the NEEAP and prepared a preliminary assessment, so that the final version would fully comply with the requirements of Directive 2006/32/EC. A final NEEAP was submitted to the Energy Community Secretariat before the deadline of 30 June 2010.

In the second quarter of 2010, the Former Yugoslav Republic of Macedonia prepared a detailed Roadmap for the implementation of the energy efficiency *acquis*. The Secretariat is confident that the transposition and the implementation are progressing.

c. State of compliance

As the deadline for implementing the energy efficiency directives does not expire until December 2011, the state of compliance is currently not assessed. Compliance with Articles 4 and 14 of the Energy Services Directive was met, as the Energy Efficiency Action Plan was sent to the Secretariat before 30 June 2010.

With adoption of the new Energy Law and preparation of the new Rulebook for Energy Efficiency in Buildings, the full transposition of the Buildings Directive including the recast is possible.

5.4.8 Social Issues

a. Social issues in the Former Yugoslav Republic of Macedonia

Even if there is no mandatory social *acquis* under the Treaty, the government transposed some directives on a voluntary basis and indicated plans to transpose even more in a paper sent to the Secretariat.

b. Progress made in 2009/2010

The government adopted a Social Action Plan (SAP), in accordance with the MoU in September 2009. The SAP follows the structure of the MoU and envisages activities in the areas of public service obligations (ensuring economic, social and territorial cohesion, universal access, and a high level of consumer rights), social partners (promoting the social dialogue with the social partners, introduction of effective mechanisms for information and consultation of social partners), management of change (promoting the development of specific employment, training and support services) and social dimensions (focusing attention on the key areas of workers' fundamental rights, improved working conditions and standards of living, improved working environment concerning the health and safety of workers, equal opportunities). The implementation started in the fourth quarter of 2009.

Moreover, in September 2009 the government also adopted an Action Plan for the Reduction of Energy Poverty that will introduce social protection for the poorest categories of energy consumers.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.5 MOLDOVA

5.5.1 Electricity

a. Background

The electricity sector of Moldova has gone through substantial reforms. The transmission network is legally unbundled and operated as part of the IPS/UPS electricity system. The Moldovan Transmission System Operator *Moldelectrica* performs transmission and dispatch activities, including basic market administration. Currently, there are three distribution system operators/suppliers active in Moldova, *RED Nord*, *RED Nord-Vest* and *RED Union Fenosa*. The latter is the largest one and merged with the former *RED Sud*, *RED Centru* and *RED Chisinau*. *RED Union Fenosa* covers 70% of the overall demand. It has been privatised and sold to the Spanish utility company *Union Fenosa*. The remaining two utilities are State-owned.

Generation capacities are just sufficient to cover the demand with no significant need for imports except for balancing purposes. As much as 70% of the supply is provided by a single, gas/oil fired thermal power plant (*Kuchurgan*, 2,520 MW installed capacity) owned and operated by the Russian utility company *RAO UES* and located in the region of Transnistria. The remaining 30% is provided from several indigenous gas-fired CHP and very few hydro power plants of an overall installed capacity of 440 MW. The system is practically balanced by the Ukrainian system. One feature of the system is its almost complete dependence on imports of primary energy (natural gas) for the production of electricity.

Overall consumption of electricity reached 5.8 TWh (2008) with a very slow growth of less that 1% annually. The supply is roughly secured and no systematic load shedding is applied. Total losses in the electricity sector amount to approximately 16%, out of which 3% occur in the transmission networks.

The electricity market is in its early stages of development and mostly regulated. There are nine independent suppliers licensed to supply electricity at non-regulated prices in the electricity market. However, only three large industry customers connected to the high-voltage grid are currently eligible, of which one purchases electricity at non-regulated prices.

In 1997 the Energy Regulatory Agency (ANRE) was established. It regulates the activities in the gas, electricity and heating sectors. ANRE has the power to issue and monitor licences, develop tariff methodologies and approve transmission tariffs. A methodology for setting the distribution tariffs has not yet been established. ANRE also adopts regulated prices in the electricity sector. The regulatory framework also includes monitoring of the quality of supply from the distribution companies. Under the existing Energy Law, ANRE may adopt a quality of supply regulation.

Moldova acquired the status of a Contracting Party to the Energy Community on 1 May 2010. In terms of legislation, in December 2009 the Parliament of Moldova adopted an Electricity Law aimed to transpose the requirements of Directive 2003/54/EC, including a timetable for opening of the electricity market following the Accession Protocol for membership in the Energy Community. Further legislation includes the Law on Conducting Licensed Activities (2001), the Law on Public Service (2002, as amended in 2006), the Law on Customer Protection (2003), the Law on Basic Principles for Regulating Entrepreneurial Activity (2006) and the Concession Law (1995 – currently under revision).

The regulated price of electricity has constantly increased since 2007. The devaluation of the local currency, however, led to a decrease of regulated electricity prices expressed in € in 2009. In terms of regulated electricity supply tariffs for households, ANRE does not apply a uniform tariff policy throughout the whole country, but reflects the technical characteristics of the distribution network and the number of customers per km of lines which resulted in higher tariffs for the State-owned utilities.

b. Progress made in 2009/2010

The adoption of the Electricity Law in December 2009, motivated by the accession to the Energy Community, represents a great step forward towards the implementation of the electricity *acquis* and market opening. Although a number of basic features required for opening of the electricity market, such as unbundling of the sector and establishment of an operational regulatory authority, were already implemented, another major achievement introduced by the new Law was the possibility for customers to switch their suppliers. Additional substantial steps, however, are still needed in order to fully implement the electricity market *acquis* and Directive 2005/89/EC.

In March 2010 the government also adopted a plan for implementation of the Directives in accordance with the Accession Protocol.

ANRE has raised regulated electricity prices twice during 2010, namely in January and May. The actual regulated price for electricity supply to household customers is about 9.0 ¢€/kWh for the State-owned suppliers (RED Nord and RED Nord-Vest), and about 8.4 ¢€/kWh for RED Union Fenosa. The new tariffs represent effective steps for eliminating the existing cross-subsidies between classes of customers.

The actual transmission tariff adopted in May 2010 is about 4.2 €/MWh. The tariff is higher compared to January, to partially offset the impact of the devaluation of the local currency from the beginning of the year.

In its 2009 Annual Report, ANRE set benchmarks for the quality of supply indicators.

Together with the Ukrainian TSO, *Moldelectrica* has applied for ENTSO-E membership and synchronization with the ENTSO-E grid. Another option considered for synchronization of the network of Moldova is achievable by separation of several blocks of the Kuchurgan power plant, and their synchronisation (together with the remaining generation capacity) with the ENTSO-E network. This depends, however, on the owner of the plant. In any case such a step, together with the proposed projects for construction of new interconnections between Moldova and Romania, would connect Moldova to the South-East European electricity market.

c. State of compliance

According to the Accession Protocol, Moldova was supposed to implement Directive 2003/54/EC by the end of 2009, Regulation 1228/2003 and Directive 2005/89/EC by the end of 2010, and to ensure that all non-household customers would be eligible from 1 January 2013 and all customers from 1 January 2015.

Moldova has taken serious steps towards implementation of the electricity *acquis* through the adoption of the Electricity Law. Since 1997, transmission and distribution system operations have been legally unbundled from generation and supply activities. The Electricity Law adopted at the end of 2009 transposed the requirements of Directive 2003/54/EC related to unbundling, third-party access, strengthened of the power of the regulatory authority, tasks and duties of the TSO and DSOs, as well as authorisation and tendering for new generation capacities. The calendar of the electricity market opening has been transposed in accordance with the Accession Protocol.

Furthermore, the institutional development and regulatory framework is well advanced for a new Contracting Party and is, in most respects, comparable to other Contracting Parties. In the coming period, special attention has to be paid to a revision of the 2003 methodology in order to set a cost-reflective transmission tariff, to adopt the methodology for setting the distribution tariff, and to eventually adopt new distribution tariffs.

The existing transmission tariff methodology should be revised to warrant a proper return on capital to allow the reinforcement and new investments in the grid. This revision is part of the 2010 annual work program of ANRE. *Moldelectrica* will reportedly perform a revaluation of assets in accordance with the requirement of the existing legislation.

As regards the missing methodology for distribution tariffs, ANRE has not yet envisaged a defined timeframe. The tariffs for distribution network access have to be separated from supply and include approved costs of required investments, regulated costs of energy to include the appropriate treatment of losses, and cost-reflectivity for the supplied electricity including costs of transmission and the balancing/ancillary services.

Furthermore, rules for the opening of the market and switching of supplier need to be developed. This should include an adequate definition of the supply function putting the emphasis on the supply to eligible customers in addition to public supply, and including the supply of last resort which is missing. The next step of unbundling of the distribution network from such supply is also pending. Also, the cross-subsidies between household and non-household customers should be eliminated.

Moldova has until the end of 2010 to implement Directive 2005/89/EC concerning measures to safeguard security of electricity supply and infrastructure investments. Among other things, it is important to address demand forecast and long-term planning of generation capacity, including sustainable means of balancing electricity, to maintain efficient authorization procedures and to adopt a framework of measures for gradual increase of security of the transmission (including implementation of the ENTSO-E criteria) and the distribution networks.

Full implementation of Regulation 1228/2003 also requires the development and implementation of coordinated, market-based capacity allocation procedures for interconnection on all borders connected to the ENTSO-E grid.

5.5.2 Gas

a. Gas in Moldova

Domestic gas production is insignificant in Moldova and covers only 0.1% of domestic consumption. Hence in practical terms, supply to Moldova comes from Russian imports through Ukraine. There is no storage capacity for the time being, although a feasibility study on storage development has been carried out.

Before the 1990s, Moldova's gas consumption was about 5 bcm/year. After the collapse of the USSR, and as a consequence of the economic crises in the post-Soviet era, natural gas consumption fell significantly below 1 bcm. The consumption has recovered in 2008 to the level of 3 bcm in the entire territory of Moldova.

Gas consumption is not distributed equally, both in territorial and consumption terms. Chisinau consumes about 60% of the gas supplied to Moldova. Beside the fact that Chisinau is the biggest city in Moldova, the combined heat and power plants are located there. In general, the heat sector consumes 42% and households account for 27% of total natural gas consumption in Moldova.

Most of the activities in the gas market (supply, transit, transmission, distribution) are performed by one vertically integrated company, *Molodovagaz*, and by its subsidiaries, two transmission system operators (*Moldovatransgaz* and *Tiraspoltransgaz*) and 19 distribution companies. *Moldovagaz* was established in 1999. Its shareholders are *Gazprom* (50%), the Republic of Moldova (36%), the regional authority of the Transnistria region (13%), and its employers (1%).

It should be noted that Moldova is an important transit country for Russian natural gas on the route to European countries. The State territory is crossed by two systems of major natural gas supply pipelines: to the south, the transit route to Romania, Bulgaria and Turkey, including branches to Greece and the Former Yugoslav Republic of Macedonia, and to the north, the transit route to Ukraine and Slovakia.

b. Progress made in 2009/2010

To adopt a gas act in line with Directive 2003/55/EC was the decisive condition that the Ministerial Council requested Moldova to fulfil before achieving the status of a Contracting Party. Moldova started drafting its gas law in early 2009 with the support of the Secretariat. The Natural Gas Act was adopted in December 2009. The Act has transposed most of the provisions of Directive 2003/55/EC.

c. State of compliance

According to the Accession Protocol, Moldova is under an obligation to implement Directive 2003/55/EC by the end of 2009, whereas the implementation deadline for Regulation 1775/2005 and Directive 2004/67/EC is 31 December 2010.

The most important issue, which is still not appropriately covered by the Natural Gas Act, concerns the rules on new infrastructure, i.e. exemptions from third-party access for new infrastructure, in line with Directive 2003/55/EC. Furthermore, the authorization procedure for new infrastructure investments should be clarified in more detail. The Natural Gas Act includes a procedure for concessions which are financed from the State budget only. It is not clear how these provisions have to be read in relation to private investment in new infrastructure.

Unbundling provisions are in place, but their implementation in practical terms needs to be further scrutinized.

ANRE, the regulatory authority, approves national transmission and distribution network tariffs. However, they are not explicitly shown on the bill to the final consumer as individual components.

5.5.3 Oil

a. Oil in Moldova

Moldova has no oilfields apart from a very small field in the southern part of the country with very heavy crude oil. The annual production is around 15,000 tons, i.e. a daily production of around 40 tons. However, currently no exploration activities are performed and there is no oil pipeline in the country.

Moldova disposes of a very small refinery with a nameplate capacity of 100,000 tons. However, the actual capacity is less than 20% and is not profitable. Hence, Moldova is a net importer of petroleum products, whereas crude oil has been imported only once. The petroleum products are mainly imported from Romania, Belarus, Greece, Russia, and Ukraine. The import figures in 2009 were as follows: 220,800 tons of gasoline, 309,200 tons of diesel, and 60,500 tons of LPG. The largest importers of petroleum products are: *Petrom-Moldova, Lukoil-Moldova* and *TIREX*, importing more than 65% of the domestic demand. *Dominic LLC* and *Lukoil Moldova* dominate the supply of the LPG market for more than 55% of the demand.

There is no particular legislation for exploration and production of crude oil. Moldova also has no law dealing with emergency oil stocks. Emergency oil stocks are held by the State Reserves of Moldova. The State Reservoir Law will be translated and sent to Secretariat soon.

There is no information provided about the amount of petroleum products maintained for emergencies, but the available petroleum product stock capacity is more than 150,000 tons, including State and industry storage capacities, but excluding the army's capacities (confidential).

According to current legislation, the industry does not have any legal obligation for maintaining petroleum stocks. For their own business purposes, however, they keep stocks in warehouses of importers and petrol stations. Currently, Moldova's petroleum industry keeps stocks of around 30 days consumption of the main petroleum products (gasoline, diesel and LPG).

The national energy regulatory authority provides importers with three different licenses (for wholesale, distribution and retail).

b. Progress made in 2009/2010

No progress can be reported concerning the legislative framework.

c. State of compliance

The petroleum market is open in principle to domestic and foreign companies. No preference is given to domestic petroleum products. There is no government intervention in price determination. The price is based on the quotations of PLATT's regional market. However, retail companies are not allowed to have a profit higher than 10 % of the price provided by wholesale companies. No customs duties are applied on the import of petroleum products.

5.5.4 Competition

a. Competition and State aid in Moldova

1 Competition law in Moldova is governed by the Law on Protection of Competition of 2000. It prohibits "anti-competitive agreements" between undertakings as well as abuses of dominant positions. The cartel prohibition, however, depends on a minimum market share of 35% by the participating undertakings. As regards the abuse of a dominant position, the law categorically excludes market shares of less than 35% from the notion of dominance. To which extent the law includes the activities of public undertakings is unclear. The activities of *"State entities and natural monopolies"* are explicitly subjected to different legislation *"with the exception of cases when the activity of such entities leads to a limitation of competition in product markets"*. Furthermore, the State enjoys the full right to price-setting in non-competitive markets and may, *"in order to protect domestic consumers, to satisfy State needs in the most important forms of production, or to develop competition", take "temporary protectionist or stimulating measures."*

The authority enforcing competition law is the National Agency for the Protection of Competition (ANPC) established in 2007. It consists of seven members appointed by Parliament. ANPC is supposed to be independent and has the competence to adopt decisions for violation of competition law. Whether this includes the direct imposition of fines or whether imposing penalties is the prerogative of the courts is not clear from the law. Liability of undertakings and their management is governed by general administrative law. Investigation rights do exist, but there are no leniency rules in place. Where an undertaking abuses its dominant positions two times or more, the ANPC may request divesture under certain conditions by the courts.

2 The control of State aid is currently not regulated in the Republic of Moldova.

b. Progress made in 2009/2010

1 In the area of competition law, the ANPC prepared a new Law on Protection of Competition which, however, the President refused to promulgate in 2008. Currently, ANPC is drafting a new Law with the help of the competition authorities of Austria and Lithuania to develop a new Law on amending the Law on Protection of Competition. The draft has not been submitted to the Secretariat.

2 The ANPC also drafted a Law on State Aid with the help of experts from Romania. The Law has not yet been adopted.

c. State of compliance

Articles 18 and 19 EnC have not yet been properly transposed into Moldovan law.

1 With respect to competition law, the limitations to 35% in both the cartel and abuse clauses are not in line with EnC law. Furthermore, the full application of competition law to the public sector is highly questionable. It should be noted however, that Article 19 only needs to be transposed from six months following the date of accession according to the Accession Protocol.

As regards competition law enforcement, the Secretariat was informed of several cases in the energy sector, including a decision on the abuse of a dominant position by *Chisinau Gaz* related to the compulsory purchase by customers of one particular brand of meters, as well as another, non-specified case involving the companies *Orhei-Vit* and *Moldovagaz*, which apparently led to a settlement. Furthermore, the ANPC approved the merger between *Ungheni-Gaz* and *Asociatia de locatari Marinescu*.

2 In the absence of a law governing State aid control, Moldova is currently not in compliance with the Energy Community *acquis*.

The draft Law on State Aid submitted to the Secretariat establishes ANPC as the State aid control authority and sets procedural rules. In terms of substantive law, it is not yet fully in compliance with the *acquis*. The draft does not contain a general prohibition of State aid mirroring Article 107(1) TFEU, but lists compliance grounds such as State aid for the provision of services of general economic interests or environmental aid which are lacking the degree of differentiation inherent in EU case law or secondary legislation.

5.5.5 Environment

a. Environment in Moldova

1. The Ministry of Ecology and Natural Resources is the responsible authority for State policy and development in the environmental sector. The main legislative acts related to environmental impact assessment are the Law to Safeguard Environment of 1993 and the Law on Ecological Expertise and Environmental Impact Assessment of 1996. The latter specifies the principles, criteria and administrative procedures for environmental protection and basic rules of the environmental impact assessment. With regard to *screening*, the Law describes the principles of project selection which are subject to an assessment. The Law also contains a list of projects. With respect to *scoping*, the Law empowers the special State authority in the field of environmental protection and natural resources to perform the environmental impact assessment procedure. The requirements for the *environmental impact study* are provided in the Annex to the Law. The study shall be developed by the license holder to develop guidelines for the design and renovation of various urban planning projects. The *decision-making* procedure includes the adoption of a final consent and rules on publicity.

2. With regard to the implementation of the Wild Birds Directive, the Ministry of Ecology and Natural Resources informed the Secretariat during its recent mission that laws on protected areas and on animal protection exist and are in the process of being amended. The new laws will establish criteria for habitat protection. Furthermore, a law on the protection of wetlands exists. Neither law has been submitted to the Secretariat.

b. Progress made in 2009/2010

1. The Ministry of Ecology and Natural Resources prepared a new draft Law on Environmental Impact Assessment, which is currently only available in Moldovan and Russian. The draft Law which aims for full transposition of the Environmental Impact Assessment Directive is a major achievement. This new Law is planned to be submitted to the Parliament by the end of the first half of 2010. Approval and entry into force of the Law is expected by the end of 2010. The Secretariat submitted comments on the draft.

2. The laws pertaining to the protection of wild birds are currently being amended. The respective drafts have not been made available to the Secretariat.

c. State of compliance

According to its Accession Protocol, Moldova needs to implement both Directives under assessment in this report by the end of 2010.

5.5.6 Renewable Energy

a. Renewables in Moldova

Moldova has little potential of renewable energy resources in hydro, solar, wind and geothermal power, estimated at about 2.7 Mtoe. Currently, two hydro-power plants with a total install capacity of 64 MW exist (HPP *Costesti* (16 MW) and HPP *Dubasari* (48 MW), the latter is situated in the region of Transnistria). An additional ten small HPPs are owned by the sugar industry. Biomass and waste is used for heat production, and fuelwood is extensively used for household heating.

A Law on Renewable Energy has been in force since 2007. The Law stipulates renewable energy targets of 6% until 2010, and a 20% share of energy from renewable sources in total energy provided by 2020. Ambitious biofuel targets were also set at 6% until 2010 for ethanol fuel mixed with gasoline within total gasoline consumption, and 5% for biodiesel in the diesel mix. The Law also sets a 20% target of biofuels in the total fuel mix until 2020.

The Law also introduces support schemes based on approved tariffs set by the national regulatory authority ANRE for 15 years, as well as certification schemes on guarantees of origin issued by the grid operators. As the TSO and DSOs are mandated to certify the electricity produced from RES, a total of four issuing bodies exist in the country. The Law also established an Energy Efficiency Fund to promote and support energy efficiency and renewable energy projects. A few provisions on grid system and administrative or licensing issues are also provided for.

b. Progress made in 2009/2010

Plans on the implementation of Directives 2001/77/EC and 2003/30/EC are currently under preparation.

The Law on Renewable Energy is envisaged to be revised in 2010, but only in relation to the timeframe for biofuel targets (to be extended until 2013 instead of 2010), and a revised role for the regulatory authority in relation to the contracts for network access and market integration of RES. The revision should be used for a more comprehensive review of the Law.

c. State of compliance

According to the Accession Protocol, Moldova has to submit a plan to implement Directives 2001/77/EC and 2003/30/EC by the end of 2010. The deadlines for the implementation of measures in the plans will reflect the later date of Moldova's accession to the Energy Community.

1. As regards the provisions of the Law on Renewable Energy, some amendments are still needed. The targets are not properly set in compliance with Directive 2001/77/EC, as reference is made to the total energy generated, but not consumed. Moreover, the 2020 targets for energy and biofuels are both set at unrealistic levels and beyond what is required by both RES Directives.

   Adequate feed-in tariffs for all types of RES have yet to be developed by the regulatory authority. The existing tariffs are imposed by the Law and need to be determined anew every year, a measure that does not provide for investor confidence. ANRE asked for technical assistance to support the development of proper feed-in tariffs for various RES.

   Guaranteed or priority access to the networks, as well as priority dispatching, are not stipulated by the Law as required by Directive 2001/77/EC. Moreover, the contractual system established by the Law does not provide a clear indication if and how the costs of RES projects will be borne by all energy customers.

2. The envisaged change of the timeframe to three more years with regard to biofuel targets shows that the targets set have not been fulfilled. The Secretariat has not been informed about the real achievements so far.

5.5.7 Energy Efficiency

a. Energy efficiency in Moldova

The information on the state of play of energy efficiency in Moldova originates mainly from public sources, such as the web page of the Ministry of Economy of the Republic of Moldova, and the UNECE Publication *"Republic of Moldova: National Energy Policy Information for Regional Analysis"* of September 2009, as well as the Secretariat's country mission in June 2010.

The Ministry of Economy and within that Ministry, the General Department for Energy Security and Energy Efficiency, is responsible for energy efficiency in Moldova.

In 2007, Moldova adopted an Energy Strategy until 2020. The Strategy acknowledges energy efficiency as one of the priorities for the national economy and for the energy sector. Energy efficiency has also been declared as a key objective under the EU-Moldova Action Plan (Objective 66).

Furthermore, energy efficiency is addressed in the National Program for Energy Conservation of the Republic of Moldova 2003-2010 and in its follow up, with an on-going biannual update. The National Programme sets out quantitative targets for efficiency improvements at a macroeconomic level, priority areas for energy conservation and efficiency interventions as well as indications for activities to be carried out in order to achieve the above stated objectives.

The Law on Renewable Energy of 2007 has established an Energy Efficiency Fund to promote and support energy efficiency and renewable energy projects.

The Law on Energy Conservation of 2000 is outdated and will be soon repealed by a new law on energy efficiency.

b. Progress made in 2009/2010

A draft Law on Energy Efficiency was approved by the government of Moldova in April 2010. The Law is currently in the second reading in the Parliament. It is expected to be passed in first half of 2010. The draft Law sets the basic principles of State policy and identifies the government's roles in energy efficiency. It also provides for the development and implementation of specific programmes to improve energy efficiency and renewable energy.

According to the draft Law, Moldova will establish an Agency for Energy Efficiency, to be created through the reorganization of the existing National Agency for Energy Conservation. The draft also establishes a new Energy Efficiency Revolving Fund.

In February 2010, EBRD launched a new energy efficiency credit line in Moldova. The Moldovan Sustainable Energy Financing Facility (MoSEFF) will offer € 20 million through local partner banks to private companies wishing to invest in energy efficiency and renewable energy. Loans provided to the private sector range from a few thousand Euros to a maximum of € 2 million. Each loan has a grant component (5-20% of the loan) for projects implemented successfully.

Moldova is part of the USAID-supported Municipal Network for Energy Efficiency (MUNEE) programme, which was created to help cities in transitional countries meet the challenge of world-market energy prices through enabling greater energy efficiency. USAID also supports the development of energy efficiency action plans, the Energy Efficiency Revolving Fund Operational Manual, the implementation of energy audits and development of the energy efficiency investment projects and demonstration projects, communication strategies etc.

Certain technical assistance projects in the area of energy efficiency are currently in the pipeline and will be launched with the financial support from the Swedish International Development and Cooperation Agency (SIDA). They include the rehabilitation and extension of CHP-1 and CHP-2 in Chisinau and CHP-North in Balti; the implementation of certain energy efficiency projects at the Mother and Child Health Centre in Chisinau and Pulmonology Centre for children in the village of Tirnova; institutional capacity building assistance for the newly-created Energy Efficiency Agency etc.

Moldova is a member of the Central European Initiative and thus has the opportunity to participate in their Know-How Exchange Programme (KEP). This programme is a funding facility created in 2004. One of the priority areas of funding for 2010 is know-how transfer in the areas of energy efficiency, renewable energy sources, clean energy and climate change.

The focus of activities of the Energy Community Secretariat in the coming period will be the integration of Moldova as a new Contracting Party in the Energy Efficiency Task Force activities, as well as working on further harmonization of the legislation with the Energy Community *acquis* on energy efficiency.

c. State of compliance

As the deadline for implementing the energy efficiency directives does not expire until December 2011, the state of compliance is currently not assessed. Nevertheless, compliance with Articles 4 and 14 of the Energy Services Directive is expected to be met before the end of 2010, as the Energy Efficiency Action Plan for buildings was already prepared with the assistance of the SYNENERGY Programme.

5.5.8 Social Issues

a. Social issues in Moldova

Even if there is no mandatory social *acquis* under the Treaty, the government of Moldova has adopted some legislation for the protection of energy vulnerable customers.

In 2000, a Law concerning the social protection of certain categories of the population includes provisions for payment of cash compensation for communal services, such as electricity, gas and other heating sources, and water. In addition, a Law adopted in 2010 and concerning social compensation for the cold season of 2010 gives additional cash-in-hand to socially vulnerable parts of the population; however, without indicating the use (e.g. for the payment of utilities bills).

b. Progress made in 2009/2010

Moldova became a Contracting Party to the Energy Community only on 1 May 2010 and has not yet signed the Memorandum of Understanding. It has therefore not yet prepared Social Action Plans.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.6 MONTENEGRO

5.6.1 Electricity

a. Electricity in Montenegro

The unbundling of the electricity sector in Montenegro started in mid 2009. The transmission system operator was legally unbundled from the vertically integrated utility, *EPCG*, in April 2009 and received the operation licenses in July 2009.

In September 2009, *EPCG* underwent a tendering process to attract a financial investor for the company. Subsequently, 18% of the shares were bought by the Italian company *A2A*, which also acquired the contract for the management of the company. *A2A* can reach 34% after a capital increase, or 45% combined with the *acquis*ition of shares from all minor shareholders. The rest of the shares will remain in State ownership.

The total installed generation capacity in Montenegro is 868 MW, out of which 658 MW (76%) is generated in hydro power plants. Thermal Power Plant Plevljia has a capacity of 210 MW.

Total gross electricity consumption in 2008 was 4,584.5 GWh, out of which only 2,686.9 GWh (or 58%) has been domestically produced. There is a long-term cooperation agreement between *EPS* (Serbia) and *EPCG* (Montenegro) related to the use of HPP Piva (342 MW) to supply peak electricity in the Serbian power system and to receive base load electricity in compensation.

The transmission system consists of 1200 km high voltage lines of 400 kV, 220 kV and 110 kV and a total installed transmission capacity of 2,800 MWA in 19 substations. In 2008, transmission losses were 2.6% and distribution losses amounted to 23%.

With regard to market opening, the Energy Law of 2010 envisages all household customers to become eligible in 2015, as stipulated in the Treaty. Non-household customers are eligible to switch suppliers. However, they maintain the right to be supplied by the incumbent supplier at regulated tariffs until then.

The legal framework for electricity in Montenegro is set out mainly by the Energy Law adopted in April 2010. In terms of secondary legislation, the government's Rulebook on Technical Conditions for Connection of Small Hydropower Plants to the Distribution Network of 2007 and the Guidelines to set the Prices for Purchase of Electricity from Small Hydropower Plants of the same year may be mentioned. Secondary legislation by the national regulatory authority REGAGEN includes the Licensing Rules of 2004; Tariff Rules for Electricity of 2005, as amended in 2007 and 2009; Rules for Unbundling of the integrated undertaking EPCG of 2004; Rules for Third-Party Access to Transmission and Distribution Networks of 2007; the Decision on the Market Model in Montenegro of 2007 etc. Other secondary legislation was approved by REGAGEN, including the Rules on Supply of Electricity of 2005; the Provisional Grid Code of 2005; and the Provisional Distribution Grid Code of 2005.

The allocation of interconnection capacity is conducted in accordance with the auction rules adopted by the TSO in 2008 and published on the TSO webpage however it is available only in the local language. The allocation of the capacity on interconnections is split 50:50 and the domestic supplier will get first priority compared with traders that are using the capacity for transits. Unused capacity is to be paid, along with a penalty imposed on suppliers based on the marginal auction price. Capacity rights are allocated applying the "use-it-or-lose-it" principle and may be traded among participants.

b. Progress made in 2009/2010

The most important development during the reporting period was the adoption of the new Energy Law in April 2010. The Secretariat assisted by reviewing the draft Law and commenting it extensively during 2009.

The implementation of the new Energy Law will require the adoption of substantial new secondary legislation, including the completion of the regulatory framework for the market design, supplier switching, appointment of a supplier of last resort, methodologies for network tariffs as well as, the authorisation procedure for new capacities, network codes, or balancing rules. Efficient tools for enforcement should also be of the highest priority.

c. State of compliance

By and large, the Energy Law adopted in 2010 transposes the electricity *acquis* under the Treaty. The Energy Law transposes the main principles of Directive 2003/54/EC, Directive 2005/89/EC, Regulation 1228/2003, assigns increased powers to the regulatory authority and tasks for the network operators.

The requirements related to the unbundling of vertically integrated undertakings and unbundling of accounts have been properly transposed. Despite the changes in the ownership structure in 2009 of the vertically integrated utility, the generation, distribution and supply are still bundled and the monitoring of the unbundling of activities and accounts has to be properly enforced by the regulatory authority. The secondary legislation will have to be adjusted to reflect changes in the primary legislation.

Unlike transposition, the current state of compliance in terms of implementation and enforcement is far from being satisfactory: major open issues relate to the preconditions for market opening, while the legal obstacles have been removed by the new Energy Law. These include: discriminatory terms and conditions based on the types of customers for access to the networks including tariffs, balancing of services and third-party access.

Further remaining issues of concern are related to the existing methodologies to establish types, level and structure for the use of network charges, unbundling of accounts and congestion management issues.

The adopted network tariffs are discriminating against network users and do not provide appropriate conditions for further market opening. The tariff design for transmission and distribution network tariffs, as applicable to eligible customers connected to the networks, is not sufficiently transparent to comply with the requirement of Article 20(1) of the Directive 2003/54/EC.

Network tariffs have to be reviewed to ensure cost-reflectivity and an adequate level of return on capital, in order to allow for the necessary investments in the networks.

The method used for the congestion management on interconnections is not compliant with the requirements of Regulation 1228/2003.

5.6.2 Gas

a. Gas in Montenegro

There is currently no gas consumption or infrastructure in Montenegro. However, there are plans to develop domestic off-shore production and to join the gas infrastructure projects discussed and implemented in the region.

The lack of a gas market notwithstanding, the *acquis* has been transposed by the Energy Law approved in April 2010.

b. Progress made in 2009/2010

During 2008 and the first half of 2009, a draft Gas Law, was developed. Subsequently, the approach was changed and the provisions related to gas were incorporated in the draft of the new Energy Law to replace the one which was in force since 2003. During the reporting period, the new Energy Law was drafted, analysed and commented on several times by the Secretariat and finally approved by the Parliament in April 2010.

c. State of compliance

The new Energy Law transposes most of Directive 2003/55/EC, most of the provisions of Regulation 1775/2005 as well as Directive 2004/67/EC. At this moment, the legal basis, defined by the new Energy Law is to be considered an appropriate and sufficient legal basis for the initial development of a gas market. The next activities should focus on capacity-building within the regulatory authority related to the gas sector, as well as the development of secondary legislation.

5.6.3 Oil

a. Oil in Montenegro

Montenegro has no domestic crude oil production. There are also no refineries for crude oil processing, nor oil pipelines. The current petroleum products consumption is around 320,000 tons. Storage capacity is around 175,000 tons.

Licenses for oil activities are provided by the regulatory authority. *Jugopetrol AD Kotor* is the dominant company in the Montenegrin oil market. The majority shareholder is *Hellenic Petroleum International*. The main business activities of the company include retail, wholesale, supplying, storage and distribution of petroleum products, as well as exploration of hydrocarbons in the Adriatic undersea area.

The current legal framework is comprised of the new Energy Law, the Mining Law, the Geological Exploration Law and the Concession Law. Law on Prospection, Exploration and Exploitation of oil and gas is adopted in July 23, 2010. The secondary legislation in place includes the Rulebook concerning Licenses in the Energy Sector of Montenegro of 2004, as amended in 2009, on commercial transport, storage and distribution, sale and supply of petroleum products; and a Decree on the Method of Setting Maximum Retail Prices for Petroleum Products.

The new Energy Law defines a way of ensuring strategic reserves of oil and petroleum products in a total quantity equal to 90 days of average domestic consumption in the previous year. Management of strategic reserves is a public service which shall be carried out by a legal person established by the government. A fee for establishing, maintenance, and management of strategic reserves will be charged in accordance with the Government Regulation. Strategic reserves of oil and petroleum products may be stored in Montenegro or in other countries.

b. Progress made in 2009/2010

The new Energy Law was adopted by Parliament in April 2010. Based on this Law, the government shall specify deadlines and conditions for beginning, and the timeline for establishing of strategic reserves of oil and petroleum products, and a corresponding methodology governing the setting of a maximum retail sale price for products; deadlines and conditions (including financial) relating to the management and maintenance of the strategic reserves in line with international commitments; deadlines and conditions for storage including requirements and conditions relating to the location of storage capacities; deadlines and conditions for quality checks and replenishing of reserves; compensation and a method of payment of compensation for the establishment, storage and management of the strategic reserves. For that purpose, a working group was set up and started to prepare the secondary legislation.

A Law on Prospection, Exploration and Exploitation of Oil and Gas has been adopted in July 2010. Secondary legislation is under development, and a first tender is expected for 2012.

c. State of compliance

The prices of oil and petroleum products are established by the State, according to the Decree on the Method of Setting Maximum Retail Prices of Petroleum Products.

Fiscal obligations applicable to petroleum products include customs duties, excise duties, VAT and eco-tax. The customs duty applied to imports of petroleum products is 1% on gasoline and diesel D-2, and 2% on heating oil. These customs duties are in violation of Article 41 EnC and need to be removed.

5.6.4 Competition

a. Competition and State aid in Montenegro

1 In terms of competition law, Montenegro has a Law on Protection of Competition in place since 2006. The cartel prohibition comprises provisions similar to Article 101(1) and (2) TFEU as well as exemptions corresponding to Article 101(3) TFEU. Agreements that do not fall within the scope of a block exemption or the *de minimis* rule must be reported to the competition authority. It may grant individual exemptions for a certain period of time. Furthermore, a government regulation on block exemption is in place. The Law also stipulates the prohibition of abuses of dominant positions, defining the notions of dominance and collective dominance separately. The market share above which a dominant position is presumed is as high as 50%. Aside from determining a case of abuse, the competent body may also issue a decision on the non-existence of an abuse. As regards public undertakings, the Law is applicable to *"State administration bodies and local self-government bodies, when directly or indirectly engaged in economic activity and trade of goods or services"*. Undertakings providing services of public interest do not fall within the scope of the Law if its application would obstruct the performance of the entrusted activities. Whether and to what extent this includes the proportionality test required by Article 106(2) TFEU is, however, not apparent from the Law.

As of November 2007, the body in charge of enforcing competition law is the Competition Protection Administration. The procedure of and before the authority is governed by general administrative procedural law to the extent the Law on Protection of Competition does not provide otherwise.

2 A Law on State Aid Control is in force since 2009 containing a definition of, as well as a general prohibition of State aid. The Law furthermore explicitly lists cases not considered State aid and instances where State aid is considered compliant.

The Law establishes a State Aid Control Commission consisting of eight members from various State institutions and the employers' association, as well as a chairman from the Ministry of Finance. The Ministry of Finance is tasked with preparing the Commission's work on procedure and substance. The Commission monitors and controls the use of State aid *ex ante* and *ex post*. Individual State aid schemes are to be reported and require approval for any provider of State aid. The Commission, within 30 days, shall then approve or reject the aid.

b. Progress made in 2009/2010

1 A new Law on the Protection of Competition is currently under preparation and is expected to be adopted in the course of 2010. The draft has not been submitted to the Secretariat. Apparently, it will improve the situation as to investigation rights, fines and leniency. The new Law is also supposed to replace the existing Competition Protection Administration by a new Agency for Protection of Competition with increased independence.

Under the generally applicable Law on Competition, until recently, Montenegrin legislation included some features of sector-specific competition regulation in the Energy Law of 2003. The aforementioned provisions are not featured anymore in the new Energy Law of April 2010. From a point of view of clarity and consistency, this development is to be welcomed.

2 A new Law on State aid Control was adopted in November 2009 and replaced the former version of that Law. The Secretariat is not aware of any decisions taken in the energy sectors.

c. State of compliance

Articles 18 and 19 EnC have only been partly transposed into the law of Montenegro.

1 Despite following the EC model in principle, competition legislation still requires legislative efforts in order to achieve full compliance with the *acquis*. This concerns mainly institutional and procedural issues. Firstly, to what extent the Competition Protection Administration is independent of the government cannot be established at this point. Secondly, the procedures suffer from several shortcomings. Among others, there are no appropriate rules on the investigation powers of the authority. Furthermore, the Law determines a very tight timeframe of four months in cartel and abuse proceedings. Fines from 200 to 300 x the national minimum wage may be imposed in cartel and merger cases, but not in cases concerning abuses of a dominant position. In the cases covered, the Law also foresees personal liability from 10 to 20 x the national minimum wage. Sanctions further exclude structural remedies. A leniency policy has not been established. The new Law should correct the shortcomings of the existing legislation, in particular as regards the status of the competition authority, competition law procedures and fines.

With regard to the implementation of competition law in the energy sectors, the Secretariat has been informed that the Competition Protection Administration has issued a decision on approval of a concentration in the field of gas in 2006 and a decision in the area of electricity in 2009. They are, however, not public, which in itself is deplorable.

2 Despite having been adopted only in 2009, the Law on State Aid still suffers from several shortcomings. Firstly, the definition of the State aid is not in line with Article 107 TFEU, nor are the compliance criteria. Secondly, the scope of applicability of the Law is limited to aid affecting trade between Montenegro and the European Union as well as CEFTA members. Thirdly, it would be preferable from the Secretariat's point of view to task an independent authority such as dealing with competition law with State aid control.

To the Secretariat's knowledge, to this date no decisions have been issued by the Commission concerning State aid to the energy sectors.

5.6.5 Environment

a. Environment in Montenegro

1 Environmental impact assessment in Montenegro is governed by the Law on Environmental Impact Assessment in force since 2008. To the extent that issues of general nature are not covered by that Law, the Law on General Administrative Procedure applies. Furthermore, four by-laws entered into force together with the Law. In 2008, an Environmental Protection Agency was established with the competence for carrying out environmental impact assessment procedures. Following the adoption of a Rulebook on Internal Organization, it became operational in March 2009.

With regard to *screening*, the Law on Environmental Impact Assessment differentiates between mandatory and non-mandatory environmental impact assessment in accordance with lists encompassed in a regulation. The need for environmental impact assessment in non-mandatory cases shall be established case-by-case. The developer shall apply to the competent authority (a State authority or local self-government) for a screening decision only for projects where an environmental impact assessment is not mandatory. Upon the application, the competent authority shall inform and consult with other authorities, the public concerned and other States participating in trans-boundary projects before issuing a screening decision. The developer may appeal such a decision to the so-called head administrator. The developer may further apply for a *scoping decision*. If he/she chooses to do so, an "Impact Assessment Committee" set up by the competent authority shall make a proposal for that decision. The competent authority shall inform and consult with other authorities, the public concerned and other States in trans-boundary situations before taking the scoping decision. The *environmental impact study* is to be submitted by the developer to the competent authority, together with an application for approval of the study. The study may be elaborated on by registered experts. Its review in the *decision-making* phase requires consultation with other authorities, the public concerned, and other States in trans-boundary situations. A public debate is to be held. The review is to be carried out by the Impact Assessment Committee which reports and proposes the final decision. This decision, approving or rejecting the environmental impact statement, is to be taken by the competent authority. Approval is a prerequisite for commencing project implementation. Other authorities, the public concerned as well as other States in trans-boundary situations are to be informed of the decision. The decision may be appealed to the Head Administrator, without mentioning standing.

2 Wild birds protection falls in the scope of the Law on Nature Protection adopted in August 2008. The Law provides for the protection of ecologically significant areas for endangered and rare species. This covers, *inter alia*, migratory routes, resting places and natural breeding sites. However, such areas shall only be established *"until the accession of Montenegro to the European Union."* Furthermore, the Law provides for specific bird protection measures such as prohibition on killing or capturing, destroying or removing of eggs and nests, disturbing of nesting birds, etc. In particular, *"poles and engineering components of medium and high voltage cables shall be constructed in such a manner to protect birds from electric shocks and mechanical injuries. Necessary measures to protect birds from electrical shock shall be undertaken on poles and electrical components constructed before this Law entering into force posing a high level of threat for birds, within one year from this Law entering into force."*

b. Progress made in 2009/2010

1 In December 2009, a memorandum of cooperation between NGOs and the Ministry for Spatial Planning and Environment was signed. This document was prepared in the context of participation of NGOs in the process of the environmental impact assessment procedure.

2 According to information provided to the Secretariat, secondary legislation concerning the further implementation of the Wild Birds Directive is currently under preparation by the Ministry for Spatial Planning and Environment. In particular, a monitoring tool on the inventory of wild birds was introduced. The Secretariat has not received any information on the details or drafts.

c. State of compliance

1 The Law on Environmental Impact Assessment follows the structure and content of the Directive. On top of this Law, the Law on Environment defines the principles of access to information and public participation in which everyone shall have the right to be informed about the state of the environment and shall participate in the decision-making process which may affect the environment.

2 Article 4(2) of the Wild Birds Directive is partially transposed into national legislation by the Law on Nature Protection.

5.6.6 Renewable Energy

a. Renewables in Montenegro

In Montenegro, domestic electricity is mainly generated by hydropower. Currently, 658 MW or 76% of the installed generating capacity in Montenegro is in HPPs, of which only 9 MW is in small HPPs. As Montenegro needs significant electricity imports to cover its consumption, the contribution of renewable energy in total final electricity consumption is much lower (30-35%) depending on the hydrology.

There is one pilot project for wind energy with 500 kW installed, and solar installations used for hot water or heating of about 5.5 MW.

After the tender for the concession of 8 small HPPs in 2008, the government announced the successful bidders for another 5 watercourses with capacities of up to 10 MW each based on a DBOT scheme. In September 2010 the next bidding round is planned for another 10 small HPPs on the rivers located in the north of the country.

In July 2010, a 20 years land lease agreement was signed by the Montenegrin government for the construction of a 46 MW wind farm in Mozura.

Montenegro still has abundant resources in hydropower estimated at 2 GW, mostly for large HPPs as well as for small HPPs. Wind (400 MW), solar (33 MW) as well as biomass (4.2 TWh/y) power also have significant potential.

The importance of promoting renewable energy can be implicitly derived from the Montenegrin *Constitution*, stipulating that Montenegro is an "ecological State".

The Energy Development Strategy up to 2025 set a target of 20% RES in primary energy consumption to be achieved between 2020-2025. It also provides plans for installing new RES capacities, namely 80 MW in small HPPs, 60 MW in wind, and 10 MW in energy from waste.

The new Energy Law adopted in April 2010 includes a special chapter on renewable energy. It specifies that a RES target will be adopted by the government. The Law determines the relations, rights and obligations of all participants in the energy sector, gives priority access to the network for the privileged producers of RES, introduces support schemes for RES to be adopted by the government, defines guarantees of origin and assigns the national regulatory authority to issue them. The Law also transposes several requirements from the Directive 2009/28/EC, namely the definition of the RES target in total energy consumption for electricity, heating and cooling and guarantees of origin to be issued for electricity produced from RES and from high-efficiency cogeneration plants.

b. Progress made in 2009/2010

1. The adoption of the Energy Law in 2010, which includes a special chapter on renewable energy and defines the roles and tasks of the institutions in promoting RES, constitutes a major step forward towards the implementation of the requirements of Directive 2001/77/EC. Feed-in tariffs for small HPPs, wind and biomass are currently under development.

2. There is no progress to be reported in relation to biofuels. This holds true not only for the reporting period, but also in general for the period since 2007, when the implementation plan was adopted.

c. State of compliance

Montenegro submitted its plan to implement Directives 2001/77/EC and 2003/30/EC to the Ministerial Council in June 2007, as required by the Treaty.

1. As regards Directive 2001/77/EC, support schemes have to be introduced for all types of RES and secondary legislation has to be developed further.

2. Following the adoption of the implementation plan in 2007, no single activity related to the implementation of the Biofuels Directive 2003/30/EC can be noted. Targets have not been set. The new Energy Law, despite aiming at implementing Directive 2009/28/EC, fails to address biofuels altogether in its scope.

5.6.7 Energy Efficiency

a. Energy efficiency in Montenegro

In April 2010, the Parliament of Montenegro adopted a new Law on Energy Efficiency. The Law is meant to be the basis for transposition of the Treaty's energy efficiency *acquis*. The Secretariat commented on the draft Law twice. Most of the comments were incorporated into the final proposal to the Parliament.

The Law on Energy Efficiency assigns the monitoring role for its implementation to the Ministry of Economy, and in particular to its Department (so called "Sector") for Energy Efficiency which was established at the end of 2009 (including a new position - Deputy Minister for energy efficiency heading the Department). The Law also envisages the adoption of further secondary legislation. The required by-laws need to be developed within 12 months after the adoption of the Law, i.e. by May 2011, by the Ministry of Economy.

Furthermore, a Law on Spatial Development and Construction of Structures was adopted in September 2008. It introduces basic concepts and provisions for energy efficiency in two main areas. Firstly, the Law concerns spatial development and sets energy efficiency requirements to be fulfilled during the development of different spatial/urban plans and studies. Certain guidelines on how to implement this part of the Law are still missing. Secondly, the Law concerns the construction of new buildings, where it imposes an obligation to prepare a specific technical documentation ("elaborate") to also include energy efficiency, as a precondition for the issuance of building permits by the responsible Ministry (for building areas larger than 3,000 m^2) or local administration authorities (for building areas smaller than 3,000 m^2). Norms for the preparation of the so-called "Elaborate" on energy efficiency are currently being prepared.

b. Progress made in 2009/2010

Concrete progress was achieved with the adoption of the new Law on Energy Efficiency in 2010. The main weakness of the Law is the absence of a specialized implementing body (i.e. Agency for Energy Efficiency) and an Energy Efficiency Fund, although the first draft Law on Energy Efficiency provided for both.

The implementation of the Buildings Directive remains a challenge. As it is a joint obligation of both the Ministry of Economy and the Ministry for Spatial Planning and Environment, the Secretariat proposed an inter-ministerial working group to be established in order to better coordinate the implementation process.

The by-laws currently under preparation include a Methodology for Calculating Indicative Energy Savings Target as well as Rulebooks on Energy Performance of Buildings, on Energy Efficiency in Buildings, and on Energy Certification of Buildings. This is a very challenging task keeping in mind that in accordance with the new Law on Energy Efficiency approximately 20 pieces of secondary legislation should be prepared and adopted within 12 months.

A draft of the First National Energy Efficiency Action Plan (NEEAP) was prepared and submitted to the Secretariat in December 2009 in accordance with the Energy Efficiency Task Force Work Programme. The Secretariat sent back a preliminary assessment of the draft NEEAP in May 2010, and made some recommendations, with a view to ensure that the final version of NEEAP fully complies with the requirements of the Energy Services Directive. The final version of NEEAP was amended and submitted to the Secretariat beginning of July 2010..

To complete its activities, the Ministry of Economy is supported by the EU IPA project *"Technical Assistance for the Implementation of the Energy Community Treaty"* (TA-EnCT) which started in February 2010 and has a planned duration of 18 months. TA-EnCT also advises the Ministry of Economy (Department for Energy Efficiency) on secondary legislation for the transposition of the *acquis*.

Montenegro currently also focuses on awareness-raising activities. The energy efficiency awareness-raising campaign implemented in 2008-2009 through the national project *"Year of energy efficiency"* yielded good results. A new campaign starting in 2010 is based on the three-year Information campaign plan supported by the GTZ ASE project and co-financed by the Government of Norway.

Training on and implementation of energy audits started in 2008 and will continue in 2010. This includes the creation of the specialized energy auditing teams.

c. State of compliance

As the deadline for implementing the energy efficiency directives does not expire until December 2011, the state of compliance is currently not assessed.

The final version of NEEAP was amended and submitted to the Secretariat beginning of July 2010. Its assessment is pending, but it might be expected that Montenegro's NEEAP is in compliance with the Energy Services Directive.

The main risk for future developments in the area of energy efficiency in Montenegro is absence of a specialized implementing bodies (i.e. Agency for Energy Efficiency), and an Energy Efficiency Fund.

5.6.8 Social Issues

a. Social issues in Montenegro

According to the information provided by Montenegro, part of the EU social *acquis* has already been transposed into national law:

The Labour Law adopted in July 2008 allegedly transposes Council Directives 98/59/EC, 2001/23/EC and 2000/78/EC. The amendments to the Law on the Protection of Workers of 2004 is said to partly transpose Council Directive 89/391/EEC and 92/57/EEC. Finally, the Law on Employment and Unemployment Insurance of March 2010 should have transposed Directives 96/71/EC, 2002/73/EC, 2006/54/EC as well as Council Directives 2000/78/EC and 76/2007/EEC.

b. Progress made in 2009/2010

In May 2010, Montenegro prepared the Social Action Plan, which is now pending approval by the government. The Plan analyses the current situation including the legal framework, and proposes improvements, together with deadlines and responsible institutions. Many measures are listed to require further technical assistance for implementation.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.7 SERBIA

5.7.1 Electricity

a. Electricity in Serbia

The electricity sector of Serbia is gradually progressing in its process of unbundling. Since 2005, the electricity transmission system operation and the electricity market operation have been performed by a separate public enterprise *EMS*. The remaining activities are performed within the vertically integrated public enterprise *EPS*, which consists of 11 subsidiary economic units, five for generation of electricity (one generation company also performs coal mining), one for coal mining and five for distribution system operation and supply. Trading of electricity is performed by the parent company *EPS*. The holding structure is 100% State ownership. The Energy Regulatory Agency (AERS), entitled to exercise regulatory powers in the electricity sector and monitor the electricity market, is established and operational since 2005.

The gross electricity consumption in Serbia in 2008 was 33.7 TWh, and final energy consumption 27.3 TWh. In the same time, the domestic electricity generation reached the level of 35.0 TWh and registered an average annual growth rate of 1.9% without any new installed capacity. As much as 10.0 TWh or 29% (2008) was produced in the hydropower plants. The total installed capacity operated by EPS rounds up to 7.124 MW out of which roughly 40% is hydropower, 55% is coal-fired thermal power and 353 MW or 5% is gas-fired CHP plants.

Serbia is well interconnected across most of its borders and electricity exchanges with its neighbouring systems are significant, i.e. on the level of 8.7 TWh in each direction (2008). As a transit hub in South-East Europe, all interconnectors on its eight borders are usually congested.

The electricity market of Serbia is formally open for all non-household customers who are allowed to acquire eligibility status starting from February 2008, pursuant to a Decision of AERS. Theoretically, such customers can freely choose their electricity supplier, which potentially opens the electricity market by 47%. In practical terms, no such customers have exercised an eligibility option yet, mainly due to the significant difference between average market price and regulated tariffs for the electricity provided by *EPS*.

The energy sector in Serbia is still governed by the comprehensive Energy Law (2004), which predates the entry into force of the Treaty and is not sufficiently developed to transpose the provisions of the related *acquis*. Public service obligation and customer protection are partially supported and supplemented in the Law of Public Utilities (2005). Authorisation for construction and refurbishment of generation facilities is enforced through the Energy Permit Code (2006) issued by the Ministry. The Energy Law allows tendering for new capacity on the grounds of security of supply, while applicable tendering criteria are stipulated in the Concession Law (2003).

The Energy Sector Development Strategy up to 2015 (2005) as well as implementation programmes in 2007 and 2009 have been adopted by the government. The Strategy and the programmes are enforced by the Energy Law and have to be updated regularly.

In terms of secondary legislation, the government or the Ministry of Mining and Energy adopted, inter alia, a Decree on the Conditions for Electricity Supply of 2005; a Rulebook on the Requirements regarding Professional Staff and Terms of Issuing and Revoking of Energy Licences of 2005, as amended in 2006; a Decree on the Requirements for obtaining the Status of the Privileged Electric Power Producer, and the criteria for assessing fulfilment of these requirements (2009).

AERS has adopted several regulations of relevance for the implementation of the electricity *acquis*, on topics such as the access to and the use of electricity transmission system charging methodology (2006, as amended in 2007 and 2008); access to and use of electricity distribution system charging methodologies (2006, as amended in 2007 and 2008); methodology for setting tariff elements for pricing electricity for tariff customers (2006, as amended in 2007 and 2008); tariff system for electricity transmission system access and utilisation (2007); tariff system for electricity settlement for tariff customers (2007, as amended in 2008 and 2009); electricity transmission and distribution system connection charging methodology (2006, as amended in 2006, 2007 and 2009); decision determining minimum electricity consumption for acquiring eligible customer status (2008). AERS also approved the Transmission Grid Code (2008) and five Distribution Grid Codes (2010).

b. Progress made in 2009/2010

Since 2007, Serbia has been reviewing its outdated Energy Law of 2004, making very slow progress. In 2009, a draft version of new amendments to the Energy Law was submitted to the Secretariat for assessment and comments. Progress was registered in the powers of the regulatory authority, transposition of the requirements from Directive 2005/89/EC and from Regulation 1228/2003. However, AERS will not yet be empowered to adopt electricity and networks tariffs, a competence which still remains with the government until 2015. It has been announced that the revised draft Law will be sent for consultation with the Secretariat in autumn.

Recent progress in the process of unbundling was registered with the implementation of accounting unbundling of distribution system operation from the supply activities within the five distribution utilities of *EPS* and with setting distribution network tariffs. The process is still undergoing regulatory adjustments; however it can be considered as a significant step in development of the market framework. Tariffs for the use of the distribution system have been implemented as of March 2010.

Specific progress has also been achieved in the development of the regulatory competences. In this respect a mandatory reporting scheme is established by AERS to monitor the quality of supply – including respective performance indicators of license holders. A protocol on cooperation between AERS and the Commission for Protection of Competition was signed in February 2010, although with little explicit reference to shared duties related to the energy markets. AERS will continue to monitor unbundling and transparency.

Due to non-compliance with the Energy Law, AERS refused to approve the Market Code submitted by the Market Operator *(EMS)*. A revised Market Code may be submitted by *EMS*. Rules on the provision of balancing services will be included in the Market Code.

The transmission system operator *EMS* abolished transfer fees and auction fees related to the allocation of interconnection capacity at the beginning of 2010. *EMS* also updated its Grid Code in order to integrate electricity produced from renewable sources into the system and adjusted the scheduling accordingly.

EMS performs yearly and monthly allocation of available interconnection capacities split 50:50 with the neighbouring TSOs. Further on, *EMS* allocates the unused capacity following the first-come-first-served principle for intra-day allocation, without any fee. The data are published on daily basis. There are discussions with the Hungarian, Romanian and Croatian TSOs to agree on common procedures for bilaterally coordinated allocation of capacity on the interconnections.

c. State of compliance

The main source of incompliance is the current Energy Law, which does not adequately transpose the electricity *acquis*. To some extent the same applies to secondary legislation based on this Law. Among other issues not adequately covered in the existing legislation is the assignment of tasks regarding security of supply, regulatory competences related to monitoring and reporting and mandatory obligations imposed on the system operator regarding the use of interconnections and congestion management.

Furthermore, important missing provisions in the legislative framework include:

- definition of supply of electricity (to the eligible customers) as an energy activity and consistent use of terms for electricity supply in wholesale and retail markets including missing requirements for unbundling of accounts for supply of eligible customers and supply of tariff customers;
- requirements for legal unbundling and compliance monitoring and reporting by vertically integrated or related undertakings;
- universal service obligation and adequate scope of public service obligation in the context of a liberalized electricity market including adequate framework for switching procedures for eligible customers;
- monitoring security of supply and related enforcement of the electricity market as an element of the supply policy including transparency/confidentiality issues in compliance with Directive 2005/89/EC;
- powers of the regulatory authority related to monitoring, the management and allocation of interconnection capacities, supplier's transparency and provision of information to the customer including data on fuel mix, imposition of penalties.

The level of unbundling is another substantial prerequisite for effective development of the market. While legal unbundling of generation and distribution activities has been concluded, *EPS* has only taken preliminary steps in legal unbundling of distribution and supply. A compliance programme needs to be applied and closely monitored.

The provision of balancing services is not sufficiently enforced within the scope of the Law. In practical implementation, AERS has developed mechanisms aiming to establish an adequate methodology. Nevertheless, an appropriate balancing mechanism on market-based criteria remains to be applied.

Despite the insufficiency of the Law, some provisions of the *acquis* are addressed implicitly through secondary legislation. This is the case with regard to the eligibility threshold, whereas AERS declared eligibility for all non-household customers and introduced an eligibility threshold of 200,000 kWh of annual consumption for household customers.

The procedure and method applied to determine the rate of return on employed capital provides an insufficient guarantee that the calculated tariffs are covering the costs of operation and an adequate return for necessary new investments. Furthermore, as the government is authorised to exercise its discretion for final approval of the tariffs, it is necessary to enforce the effective application of a proper tariff methodology and maximum level of transparency.

The network development plans of *EMS* are regularly updated. Actual problems with financing partially arise from the flaws of the existing Energy Law, according to which the connected distribution network is not defined as a transmission system user and from the inconsistent separation of assets between the TSO *(EMS)* and the DSO *(EPS). EMS* is working on the criteria for clear allocation of a part of the substations to the TSO or DSO. Such measures need to be agreed to among all the parties involved.

Transparency criteria applied by *EMS* are quite advanced. In accordance with the *EMS* confidentiality clause, there is no restriction to publish data required by Regulation 1228/2003, and investment and maintenance plans are available online. Assessment of system adequacy, investment plans and system forecasts are within *EMS'* competences and updated regularly.

Currently, the price for congested capacity is set using a "pay-as-bid" method for 50% of the interconnection capacity on all borders. This is justified as a better option in the initial stage to prevent gaming. However, this method is not applied by any of the TSOs in the EU and different pricing methods for the same product send non-economic signals to the market. In addition to that, any potential bilateral coordination of the capacity allocation mechanism would still be short in its compliance since Regulation 1228/2003 and the Congestion Management Guidelines stipulate the requirement for a regionally coordinated capacity management mechanism.

5.7.2 Gas

a. Gas in Serbia

Gas consumption in Serbia is around 2.3 bcm/a. 92% of the demand is satisfied by imports from Russia, through Ukraine and Hungary. The remainder is covered by domestic production and by using the only storage facility in Serbia (in operation since 2009). The main consumption categories are industry (52%), district heating (17%) and household customers (16%).

The main players in the domestic gas market include one supplier on the wholesale market, one transmission system operator (still not unbundled from supply activities), one company in charge of transmission (but not as an operator) and 38 distribution companies. A storage system operator has not been established yet.

In legal terms, the gas market is governed by the Energy Law in force since 2004. There has been three tariff methodologies adopted, namely the Tariff System for Natural Gas Transport System Access and Utilization of 2007, the Tariff System for Natural Gas Distribution System Access and Utilization of 2007 and the Tariff System for Natural Gas Settlement for Tariff Buyers of 2007 as amended in 2008.

The status of market opening corresponds to the Treaty since February 2008, when the regulatory authority AERS passed a decision by which all non-household customers are eligible regardless of their annual consumption.

b. Progress made in 2009/2010

At the beginning of November 2009, the draft amendments to the Energy Law were submitted to the Secretariat for comments. The comments were also discussed during an expert mission. Since then, there has been no progress to report, except the oral assurance that preparations are ongoing.

c. State of compliance

Although there were several attempts to amend the existing Energy Law (with the latest one still ongoing), the Law has remained unchanged since 2004 and is still not harmonized with Directive 2003/55/EC (not to mention Regulation 1775/2005 and Directive 2004/67/EC, as its upgrading). The existing Law is largely non-compliant with the *acquis*. The most serious instances of non-compliance relate to: the lack of unbundling of even the transmission system operator, the lack of TPA exemptions for new infrastructure and cross-border mechanisms and codes for all existing infrastructure. As mentioned before, both, Directive 2004/67/EC and Regulation 1775/2005, have not yet been transposed.

In May 2010, the Secretariat sent a letter to the responsible minister expressing concerns related to certain provisions in the inter-governmental agreement between Serbia and Russia on the so-called South Stream pipeline project, for, *inter alia*, excluding third-party access *per se*.

5.7.3 Oil

a. Oil in Serbia

The Serbian domestic production in 2009 was around 647.000 tons. Imports were around 2.27 million tons, mainly from Russia. More than 75% of the crude oil is imported by the *Oil Industry of Serbia (NIS)*. Annual domestic petroleum products procession is around 2.8 million tons (diesel accounts for 33% of this figure, whereas the motor gasoline is around 21%). Imported petroleum products are around 900,000 tons with *Evro Gasoil* accounting for more than 60%.

NIS has two refineries in operation in Pančevo and Novi Sad. Pančevo is designed for a throughput of max. 4.8 million tons/year, while Novi Sad is designed for a throughput of max. 2.5 million tons/year. In 2008, *Gazprom-Neft* acquired 51% of the shares. *NIS* is the only company in Serbia with an integrated and balanced system of exploitation, processing and sale of petroleum and petroleum products and natural gas exploitation, thus playing an important role in maintaining energy security of the country. The company has its own retail network of 480 petrol stations and oil storage, and is a leading supplier of oil products in the Serbian market (supplies about 75% of the entire Serbian market). *NIS* exports motor fuel, benzene, toluene, construction and industrial bitumen to the EU, Ukraine, Croatia, Montenegro and Bosnia and Herzegovina.

Currently there is only one pipeline for crude oil in place, with a total length of 154.4 km. It is divided into two sections, DN-1 of 63.4 km from Sotin (Croatia) to Novi Sad, and DN-2 of 91 km from Novi Sad to Pančevo. There is no pipeline for the transport of petroleum products, but it is foreseen that one will be built (around 400 km), mainly for motor fuels (gasoline and diesel). Transport of crude oil and petroleum products via pipeline is considered an activity of public interest in accordance with the Energy Law of 2004. Pipelines are considered natural monopolies but third-party access to the pipelines is possible.

Companies must obtain a license issued by the national regulatory authority of Serbia.

The complex legal framework for the oil sector in Serbia includes the Energy Law, the Mining Law, the Geological Research Law, the Law on the Establishment and Classification of the Reserves of Mineral Raw Materials and Display Data, the Decree on Conditions and Manner of Import and Processing of Crude Oil and Oil Products, the Excise Tax Law, and the Decree on the Prices of Petroleum Products.

The oil reserves in Serbia are regulated by the Commodity Reserves Law and by the Energy Law. In accordance with the Commodity Reserves Law, the Directorate for Commodity Reserves takes care of all commodity reserves which include oil reserves. It has been announced that the new Commodity Reserves Law will regulate these activities in line with the EU *acquis*.

b. Progress made in 2009/2010

In accordance with the SPA between Serbia and *Gazprom*, the construction of a Mild Hydrocracking Complex (MHC) and Hydrofinishing in the Pančevo refinery will modernize the oil sector and will enable it to reach European standards of fuel production. Operation is planned for the third quarter of the year 2012. Regarding the fuel quality, it seems possible that from 2011 onwards, Serbia will produce only unleaded fuel.

As envisaged by the Energy Law of 2004, AERS approved the Oil Transportation Grid Code upon request by the transportation system operator *Transnafta* in May 2010. The Oil Transportation Grid Code includes technical conditions for connecting to the oil transportation grid, technical conditions for safe grid functioning, emergency procedures, rules on third-party access to the natural oil transportation grid, functional requirements and information on the accuracy class of measuring devices, the method of measuring oil and other transportation arrangements.

In 2009, the Directorate for Commodity Reserves bought 25,000 tons of crude oil worth € 8,283,600 in order to eliminate possible consequences of a potential gas crisis. Another € 9,000,000 has been earmarked for purchasing oil derivatives.

The second and third phases of the construction of four reservoirs with a total capacity of 20,000 m^3 have been completed.

c. State of compliance

A customs duty is applied to the import of crude oil and petroleum products in accordance with the Custom Tariff Law. There is no export customs duty rate on crude oil and petroleum products. The current customs duty rate on import of crude oil is 1%, but this does not apply to EU countries, CEFTA countries, the Russian Federation and Belarus. For the import of petroleum and diesel fuel this duty is 1% while for heating oil it is 0%. The customs duty rate on the import of petroleum products with EU countries, CEFTA countries, Russian Federation and Belarus is 0%. The treatment of local companies and foreign companies in the oil sector in regards to tax payment regulations is the same.

5.7.4 Competition

a. Competition and State aid in Serbia

1 In Serbia, competition law is governed by the Law on Competition in force since November 2009. It contains a cartel prohibition following Article 101(1) and (2) TFEU. Individual exemptions depend on a decision by the competition authority. The Law further envisages block exemptions to be adopted by the government. The provision on the prohibition of abuses of a dominant position is modelled on Article 102 TFEU. Furthermore, the Law also applies to public undertakings, entrusted with the operation of public services *"…except if through the application of this law, they are prevented to perform activities of public interest or tasks assigned to them"*. To what extent this involves the proportionality test required by Article 106(2) TFEU is unclear.

As for the enforcement of competition law, the competent authority is the Commission for Protection of Competition, an *"independent and autonomous organization"* consisting of a President and four members elected by Parliament following an open competition. Procedures for violation of the competition law may be initiated *ex officio* or upon request and result in a decision to be published. The investigation procedure includes information and inspection rights by the Commission, which may impose sanctions, including behavioural and structural remedies. Fines imposed may be up to 10% of the annual turnover. Appeals against decisions by the Commission are presented to the Administrative Court. The Law also contains a provision on the Commission's leniency policy and rules allowing for private damage claims. Finally, the Commission may also carry out sector inquires.

2 State aid law is governed by the Law on State Aid Control in force since 1 January 2010. The Law contains the definition and the general prohibition of State aid. The provision explicitly refers to *"internationally ratified treaties"*.

Any State aid will have to be notified in advance to the authority to be established for that purpose, a five-member and "operationally independent" Commission for State Aid Control. That body has been set up by the government and is chaired by a representative of the Ministry of Finance. The operational work is performed by the Group for State Aid Control within the Ministry of Finance. The Commission adopts binding decisions and conclusions on the compatibility of State aid (in *ex ante* and *ex post*-control cases), following a procedure which eventually may include recovery. The decisions are subject to an appeal under administrative law. Further procedural details are set forth in the Regulation on Rules for State Aid Granting and in the Regulation on Rules and Procedures for State Aid Notification (incl. notification form).

b. Progress made in 2009/2010

1 The year 2009 brought significant progress in the implementation of the Treaty's competition *acquis*. The Law on Protection of Competition of 2006 has been replaced by the new Law on Competition which entered into force on 1 November 2009. The Law has been upgraded in terms of substance by reducing the number and complexity of its provisions and giving more flexibility to secondary legislation and case law.

Most notably, however, the procedural aspects of the Law have been improved, such as the institutional framework of the Commission for the Protection of Competition, a competition procedure modelled on EC law, including inspection rights, rights to impose fines, leniency etc. Furthermore, the thresholds for merger control are now high enough to release capacities from concentration cases to cartel and abuse cases. In all these respects, the new Law constitutes a milestone in alignment with the competition *acquis*. The secondary legislation adopted under the new Law, however, has not been made available to the Secretariat.

2 In terms of State aid, the progress achieved was at least equally important. For the first time, a Law on State Aid Control is in force in Serbia as of 1 January 2010. The Commission for State Aid Control was set up in December 2009. It became operational upon entry into force of the procedural by-laws in March 2010.

c. State of compliance

Articles 18 and 19 EnC have been properly transposed into Serbian law.

1 The new Law on Competition brings Serbian competition law largely in line with the *acquis* on competition.

When it comes to the implementation and application of competition law in the energy sector, the Secretariat has taken note that the Competition Commission in 2010 warned the natural gas company *Srbijagas* for refusing third-party access to its network by companies other than *Jugorosgas*, the joint venture between *Srbijagas* and *Gazprom*. The attempt of *Srbijagas* to justify the refusal by the lack of network codes was rejected.

2 The Law on State Aid Control essentially transposes Article 107 TFEU, as required by Article 18 EnC. With regard to the implementation of State aid law, the effectiveness and degree of independence of the Commission for State aid Control remains to be seen. According to information submitted by the government, the Commission so far has decided on 27 notifications (25 decisions and two conclusions). Another seven notifications are currently pending. In the energy sectors, the Commission has decided on three notifications from the Provincial Secretariat for Energy and Mineral Resources of the Autonomous Province of Vojvodina. The Secretariat has not reviewed these decisions

5.7.5 Environment

a. Environment in Serbia

1 Environmental impact assessment in Serbia is governed by the Law on Environmental Impact Assessment of 2004.

With regard to *screening*, the distinction between mandatory and non-mandatory environmental impact assessment is to be made based on a regulation adopted by the government in 2005 and amended in November 2008. As regards energy projects, this regulation is in line with Annex 1 to the Directive. As a principle, "historic" cases have to undergo an EIA as well. The need for an environmental impact assessment in non-mandatory cases shall be established according to pre-defined criteria encompassed in a ministerial regulation. For projects where an environmental impact assessment is not mandatory, the developer shall apply to the competent authority (i.e. the Ministry of Environmental Protection, a provincial authority or a local self-government authority) for a *screening* decision following guidelines established by the Ministry. The competent authority shall inform and consult with other authorities, the public concerned, and, in trans-boundary situations, other States before taking a screening decision. The developer may appeal the screening decision to the competent authority of second instance. Application for a *scoping* decision by the developer is mandatory and shall be made in accordance with guidelines established by the Ministry. Before taking such a decision, the competent authority shall inform and consult with other authorities, the public concerned in trans-boundary situations, and other States. The developer and the public concerned may appeal the scoping decision to the competent authority of second instance. In the next phase, the developer submits an *environmental impact study*, as an integral part of documentation required to obtain a permit to the competent authority, and to apply for approval of the study.

The study may be conducted by registered experts. The Law creates the position of an "environmental inspector" to supervise the developer as regards compliance with his obligations under the Law. As regards decision-making, the environmental impact study is to be reviewed by a Technical Committee, established by the competent authority, which issues a report and a proposal for decision. In this context, consultation with other authorities, the public concerned, and other States in trans-boundary situations is to take place. The Law also provides for a public debate to be held as defined in a separate regulation. The final decision approving or rejecting the EIS is to be taken by the competent authority. Approval is a prerequisite for commencing project implementation. Other authorities, the public concerned and other States in trans-boundary situations are to be informed of the approval. An appeal of the decision by the developer and members of the public concerned to the administrative court is envisaged.

2 The Wild Birds Directive, has been largely transposed into Serbian law by the Law on Environmental Protection of 2004 (as amended in 2009), as well as by the Law on Game and Hunting of 2010 which repealed the former Law on Hunting Management, and a new Law on Nature Protection of 2009. The competent authorities for transposition and implementation of the Wild Birds Directive are the Ministry of Environmental Protection and the Ministry of Agriculture, Forestry and Water Management. In addition, the Institute for Nature Protection performs tasks related to research and studies in the domain of nature protection in order to implement regimes of protection, preparation of project reports concerning nature protection and assessment of natural values.

The Law on Game and Hunting contains provisions on the protection of wild birds. Bird species are protected and regimes of strict protection have been determined, i.e. prohibitions against killing, disturbing, catching, hunting, destroying nests, and killing hatchlings. The new Law on Nature Protection enables the establishment of an ecological network, and the identification of areas of special conservation interest. The protection of wild species is accomplished by carrying out measures and activities for the preservation of the species, their populations and habitats, ecosystems and the corridors connecting them. More particular, important sites of global bird conversation (Important Bird Areas) were identified with a view to implementing, *inter alia*, the Wild Birds Directive. Serbia has also established RAMSAR Sites.

b. Progress made in 2009/2010

1 With regard to the environmental impact assessment, the Law on Environmental Impact Assessment was amended in May 2009. The amendments have not yet been submitted to the Secretariat.

2 In May 2009, Serbia adopted a new Law on Nature Protection. The Law on Game and Hunting was adopted in March 2010. Additionally, the Institute of Nature Protection of Serbia and other scientific institutions also adopted a Rulebook on the Proclamation and Protection of Strictly Protected and Protected Wild Species of Plants, Animal and Fungi in February 2010. This Rulebook contains lists of protected wild species of plants, animal and fungi, also including the birds listed in Directive 79/409/EEC.

c. State of compliance

1 The Environmental Impact Assessment Directive has been largely transposed into Serbian primary and secondary legislation.

2 As regards wild birds protection, the new Law on Nature Protection in particular furthers the level of harmonization with the Wild Birds Directive.

5.7.6 Renewable Energy

a. Renewables in Serbia

1 Hydropower contributes about 27% of the total electricity production of Serbia (2008). The installed capacity is 2,831 MW in large and small HPPs. There are no other generation capacities based on RES currently installed, but Serbia has promising potential. This includes a large untapped hydro potential, mainly for mid and small HPPs, at about 4.6 GW, 2.3 TWh/y in wind, 50 MW in geothermal and 33 MW in solar energy. Biomass from wood and agricultural waste has the most significant potential in Serbia, with an estimate of 19 TWh/y.

The Serbian Energy Development Strategy up to 2015 adopted in 2005 also covers the promotion of renewable energy sources. The legal framework for the promotion of RES set by the 2004 Energy Law was only completed in 2009 and 2010, with several governmental decrees addressing the shortcomings in attracting investment in RES projects.

The Decree amending, for the period of 2007-2012, the implementation of the Energy Sector Development Strategy set an interim renewable target for 2012 at an increase of 2.2% for the electricity produced from RES compared with the RES share of the final electricity consumed in 2007.

The regulatory authority adopted a methodology for calculation of the cost of connection to the transmission and distribution networks. A "shallow approach" (cost of connection excluding the reinforcement of the grids) is applied for midsize and small producers, including RES.

2 Regarding biofuels, Serbia introduced a blending obligation through the Decree amending, for the period of 2007-2012, the implementation of the Energy Sector Development Strategy. In the same document, the biofuels targets are specified as the share of fuels in transport for the years 2010 (0.76%), 2011(1.52%) and 2012 (2.28%).

b. Progress made in 2009/2010

1 A Governmental Decree on Criteria for Privileged Power Producers was adopted in September 2009. In November 2009, the government adopted two Decrees, one amending a regulation on the Energy Development Strategy Action Plan, targeting an increase of 2.2% in electricity produced from renewables until 2012 compared with 2007 and the second, setting feed-in tariffs as support schemes for electricity produced from RES. The 2009 Decree adopting the feed-in tariffs introduces support scheme limitation for solar up to 5 MW and wind capacity up to 450 MW. However, the threshold for wind power can be increased by 10% of the total new conventional capacities connected to the grid for balancing purposes.

The Energy Law currently under revision also envisages the establishment of an Energy Efficiency Fund to promote renewable energy projects.

In April 2010, the Ministry of Mining and Energy presented a draft contract between the privileged power producers and the buyer of electricity (currently EPS, the vertical integrated generation, distribution and supply company).

In July 2010, Serbia adopted a Biomass Action Plan aimed at defining a strategy for biomass utilization. One of the main tasks of the Action Plan is to indentify bottlenecks in the process of biomass utilization, as well as the actions required to overcome them. The Plan focuses on short term activities (by the end of 2012) with some additional recommendations for long term actions.

2 According to the information presented to the Renewable Energy Task Force, future priorities include the development of sustainability criteria on biofuels to be in line with the requirements of the new Directive 2009/28/EC.

c. State of compliance

The plan to implement Directives 2001/77/EC and 2003/30/EC was submitted to the Ministerial Council in June 2007, as required by the Treaty.

1 A new Energy Law is under preparation and will eventually transpose the requirements of Directive 2001/77/EC and even consider some provisions from Directive 2009/28/EC.

Currently, there is no correlation between the validity of the adopted feed-in tariffs (until the end of 2012) and the duration of electricity buy-out contracts (for 12 years). The government announced to adopt new feed-in tariffs for the period starting 2013 during 2012. These new feed-in tariffs will not affect previously signed agreements valid over 12 years.

As new electricity suppliers enter the market and eligible customers switch suppliers, the actual market model of RES integration will have to be revised to accommodate the allocation of costs for promoting RES to all electricity customers. The certification system for RES and the appointment of the issuing body for the guarantee of origin still need to be addressed.

Furthermore, the procedures for authorisation, licensing and network connections need to be streamlined. They remain the greatest barriers to the development of RES projects. The institutional setting related to RES is extensively developed, however, the first RES projects still have to be financed and developed.

2 Targets for biofuels have been set as described above, but not in line with Directive 2003/30/EC. Furthermore, many other provisions of Directive 2003/30/EC are still to be transposed, as well as the obligation to report on the achievement of the defined targets.

5.7.7 Energy Efficiency

a. Energy efficiency in Serbia

The Energy Law of 2004 defines energy policy objectives and the instruments for its implementation. The three instruments for implementation of the Serbian energy policy set in the Energy Law are: the Energy Sector Development Strategy of 2005, the 2010 Programme for the Implementation of the Strategy, and the Energy Balance.

The Energy Sector Development Strategy of the Republic of Serbia is to be implemented until 2015. It recognizes energy efficiency as one of its five priorities. The Programme for the Implementation of the Energy Sector Development Strategy for the period 2007-2012, as amended in 2010, dedicates separate chapters to energy efficiency in energy consumption, and to the establishment of an Energy Efficiency Fund.

While there is a clear strategic focus on greater promotion of energy efficiency, Serbia still does not have a comprehensive legislative framework on energy efficiency in place. The Energy Law as well as the current draft for a new Law, however, includes provisions for the setting-up of an Energy Efficiency Agency (done) and Fund.

The Ministry of Mining and Energy is currently preparing a Law on the Rational Use of Energy planned to be adopted by the end of 2010. The development of the related secondary legislation is expected in 2011. This Law and the supporting secondary legislation are said to transpose the directives on energy end use efficiency and energy services, energy labelling and partly on energy performance of buildings (part not covered by the Law on Construction and Planning).

The Law on Construction and Planning of 2009 forms the legal basis for the introduction of norms and standards related to energy efficiency in buildings. Additional energy efficiency standards and norms are yet to be established by the Law on Rational Use of Energy.

The key governmental institutions active in the field of energy efficiency, besides the Ministry of Mining and Energy, are the Ministry of Environment and Spatial Planning, the Serbian Energy Efficiency Agency, and the five Regional Energy Efficiency Centres.

b. Progress made in 2009/2010

Aiming at the removal of the main obstacles to increasing energy efficiency, Serbia initiated during 2009-2010 several important activities, namely the creation of the basic legislative framework for energy efficiency (in terms of a draft Law on the Rational Use of Energy and Rulebooks), the preparatory activities for establishment of the Energy Efficiency Fund, preparation of the National Energy Efficiency Action Plan (NEEAP) and the development of an energy management system.

The legal basis for the establishment of the Energy Efficiency Fund (planned by the end of 2010) will be either included in the amended Energy Law or in the Law on Rational Use of Energy. The Energy Efficiency Fund will be established to support and co-finance priority activities/projects/programmes aiming to increase energy efficiency in both the production and consumption sectors, as well as increasing the utilization of renewable energy.

Pursuant to the work programme of the Energy Efficiency Task Force, Serbia submitted in May 2010 a Roadmap for implementation of the energy efficiency directives to the Secretariat. The draft of the 1st NEEAP of Serbia has been prepared and submitted to the Secretariat in February 2010, in accordance with the Task Force's Work Programme. The Secretariat commented on the draft NEEAP to ensure full compliance of the final version with the requirements of Directive 2006/32/EC. The final version of the first NEEAP was adopted in July 2010 and was submitted to the Secretariat on 18 August 2010. An entity to have the overall control and responsibility for NEEAP implementation in Serbia has been assigned.

The preparation of Energy Efficiency Plans is also defined in the Programme for the Implementation of the Energy Sector Development Strategy as amended in April 2010. The most important projects in this field are the following:

- A project on the introduction of energy management and energy planning in municipalities, which includes among others various training activities and brochures entitled *"Guide for preparation of municipal energy balances" and "Preparation of the energy efficiency projects";*

- Cooperation with Germany to introduce ESCO services in the public sector of Serbia, with the aim of preparing a model contract for ESCO services and implementing a pilot project for these services;
- A study for the introduction of an energy management system in energy consumption sectors in Serbia with the financial and technical assistance from *JICA* (Japan) which should propose an energy management system, as well as a plan for its implementation and support schemes;
- Implementation of the Serbia Energy Efficiency Project, dealing with the improvement of heating energy efficiency in public buildings, improvement of the functional and health environment for the users and reduction of the environmental impact of the use of dirty fuels for heating in Serbia, all financed with two loans provided by the World Bank;
- Increasing public awareness and education. Among other programmes, the Energy Efficiency Agency started a programme in cooperation with the Ministry of Education, which considers the introduction of energy efficiency and renewable energy as subjects in the *curriculum* of primary and technical secondary schools.

c. State of compliance

As the deadline for implementing the energy efficiency directives expires in December 2011, the state of compliance is currently not assessed.

5.7.8 Social Issues

a. Social issues in Serbia

Serbia adopted a number of acts with relevance for the social *acquis*, namely a Labour Law, an Employment and Employment Benefit Law, a Disability and Anti-Discrimination Law, a Law on Amicable Resolution of Labor Disputes, an Occupational Safety and Health Law, a Pension and Disability Insurance Law, a Social and Economic Council Law and a Law on Strikes.

Following the National Programme for EU Integration the Ministry of Labour and Social Policy aims to align domestic labour law with the relevant EU *acquis* by the end of 2011.

b. Progress made in 2009/2010

The Government of Serbia adopted in 2009 the Social Action Plan prepared by a working group. The Plan includes chapters on the *protection of vulnerable consumers* (including tasks such as setting criteria and indicators to define the category of vulnerable energy consumers and defining an integral assistance programme for socially vulnerable energy consumers), *promotion of social dialogue in the energy sector* (including tasks such as the development of the capacity of social partners, the development of a social dialogue at the local self-government level in the energy sector, the promotion of peaceful settlement of labour disputes in the energy sector); *change management* (including tasks such as ensuring conditions for the efficient operation of energy companies and determination of the optimum number of workers and measures for redundant workers), *improvement of working conditions and living standards* (including tasks such as the promotion of a legal framework and efficient labour inspection in the energy sector). The Social Action Plan also has a chapter on monitoring its implementation.

Furthermore, the Ministry of Trade and Services prepared a draft Law on Consumer Protection to be adopted by the end of 2010. The chapter on services of general economic interest covers also consumer protection in the energy sectors, including the protection of vulnerable customers.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

5.8 UNMIK

5.8.1 Electricity

a. Electricity in UNMIK

Total annual consumption of electricity in UNMIK is around 5 TWh (2008) with an average annual growth of 8%. This consumption figure includes a high level of losses which amount to 4.56% in the transmission and 42.8% in the distribution network (2008). The two domestic lignite-fired power plant units generate about 900 MW effective net capacity providing close to 98% of the indigenous electricity generation, which in turn covers almost 92% of the total net consumption. Maximum cross-border transmission capacity (NTC) is in the order of 1,400 MW. The missing less than 10% of the consumption is covered by imports. The demand, however, is not fully satisfied – there is regular load-shedding through a collection-sensitive reduction scheme periodically updated by the national regulatory authority ERO. In addition, 330 kWh per month are subsidized by the government for 32,000 socially vulnerable households.

The electricity sector in UNMIK has been partly liberalized since 2006. The publicly owned transmission system operator *KOSTT*, which is also responsible for balancing services, and essential market functions has been unbundled. The remaining public and vertically integrated utility *KEK* still dominates generation and supply, performing the core activities of coal mining, electricity generation, distribution system operation and supply, including imports, for all captive customers. The regulatory authority (ERO) has been established and functional since 2004.

The legal framework of UNMIK for the electricity sector is structured in three basic acts, the Law on Energy, the Law on the Energy Regulator and the Law on Electricity. All three date back to 2004 and are currently under revision.

ERO adopted or approved a comprehensive set of rules and other regulatory acts (some of them prepared by the network operators), as well as methodologies for the determination of tariffs. They include the transitional Market Rules, the Transmission Grid Code of *KOSTT*, the Distribution Grid Code and Metering Code of *KEK*, Rules on the Authorization Procedure for Construction of new Generation Capacities etc.

In 2008, *KOSTT* complained to the Secretariat about being barred by the Serbian transmission system operator from the ITC system and performing capacity allocation/congestion management on the interconnectors with neighbouring Contracting Parties. Since then, a series of negotiations under the auspices of the Secretariat has taken place. Compromise solutions proposed by the Secretariat have been rejected.

b. Progress made in 2009/2010

Draft amendments to the three basic legal acts in the energy sector – the Law on the Energy Regulator, the Law on Energy, and the Law on Electricity – were developed in September 2009. The Secretariat reviewed and commented on the drafts repeatedly. All three draft Laws are currently pending in the Assembly.

The process of transformation and legal/functional/account unbundling of the vertically integrated utility *KEK* is underway and said to be completed by the end of 2010. In this respect, the legal unbundling of distribution system operation and supply from all other activities, and its transformation into a new corporate structure has been enforced through a Government Act. Another Act stipulates the intention of the government to privatize the newly incorporated company.

Notwithstanding the delay in the adoption of primary legislation, considerable progress has been registered in bringing the secondary rules and regulations into compliance. During this reporting period, ERO approved the Generation Adequacy Plan 2009–2015 and a Distribution Network Development Plan 2009-2011. ERO also approved the Transmission Connection Charging Methodology. In the meantime, *KOSTT* requested an amendment to that document on procedures, cost and certain obligations.

The Energy Strategy 2009-2018 was approved by the Assembly in March 2010.

Furthermore, the transitional Market Rules in force are currently undergoing revision. The new Transmission Network Development Plan 2010-2013 has been submitted to ERO for approval. Furthermore, *KOSTT* submitted for approval a ten year Transmission Network Development Plan 2010-2019. *KOSTT* also prepared a list of New Transmission Capacity Interconnection Lines 2009–2015, as required by the Law on Electricity. A new Methodology for Connection to the Distribution Network (for customers and small generators) as well as Standards for Quality of Supply and Quality of Service are under development.

Ongoing developments also include the signature of an Interconnection TSO Agreement between *KOSTT* and the transmission system operator of Albania. *KOSTT* is also negotiating with the Montenegrin TSO on a similar agreement. *KOSTT* and *KEK* have signed an Ancillary Service Agreement. *KOSTT* and *KESH* of Albania also signed an Ancillary Services Agreement, to provide on third of available capacities for secondary regulation. Procedures and rules of operation are under development with the declared aim to pave the way for accession of *KOSTT* to ENTSO-E.

An increase of revenue collection was reported during 2009 (relative to the invoiced electricity).

c. State of compliance

The legal framework provided a solid ground for the reforms implemented in the past in UNMIK. However, in the present situation, the legal framework should be considered outdated. It falls short of complying with the *acquis*. The swift revision/adoption of the pending amendments should be of the highest priority.

The current Law on Energy and the Law on Electricity aim to complement each other in creating the framework for the electricity sector. They fail to properly implement several aspects of the *acquis* such as:

- Rules related to public service obligation, which have not been transposed, in particular with respect to universal service, customer protection, contractual terms etc.;
- The structure of the electricity sector, which is non-compliant with respect to definitions and tasks (sup plier, eligible customer), unbundling (unbundling in general, DSO, compliance programmes, monitoring of accounts), responsibilities of the operator (dispatching, balancing);
- Third-party access, which is incompletely implemented with regard to the stipulation of the right in general, treatment of refusals, transparency, rules on direct lines, access to interconnections as well as all issues specified in Regulation 1228/2003;
- Market opening, where the legal framework does not provide for a timely implementation of Article 21 of Directive 2003/54/EC and Annex I to the Treaty;
- Security of supply is not adequately covered (rules on monitoring of supply, reporting, implementation of Directive 2005/89/EC are missing), the framework for strategic planning and development instruments are not coherent with the market liberalization policy, authorization procedure and criteria for new capacity tendering are insufficiently covered by the Law.

Pursuant to a Government Act of 2009, the electricity market is declared open for all customers except households. This Act has not been implemented, the main reasons include the inappropriate market model, the underdeveloped balancing market, the lack of sufficient secondary enforcement for switching, the lack of payment discipline, the extreme level of losses (covered by the State-owned utility), the high level of concentration on the generation side and lack of transparency and competition in the wholesale trading environment, and high market prices compared to the tariffs.

5.8.2 Gas

a. Gas in UNMIK

UNMIK is one of the Contracting Parties without an existing gas market. However, Directive 2003/55/EC was transposed entirely by the Law on Natural Gas adopted in 2009.

b. Progress made in 2009/2010

The Law on Natural Gas was adopted during the reporting period. Furthermore, an Administrative Instruction on Security of Supply in the Natural Gas Sector is under preparation.

c. State of compliance

The existing basic legal framework for gas enables UNMIK to participate in the development of the regional gas network. Nevertheless, further efforts are required in capacity building for the gas sector in both ERO and in the Ministry.

The implementation of Regulation 1775/2005 is still pending. This may, however, be tackled in parallel with a future development of a gas infrastructure. Equally, the transposition of Directive 2004/67/EC needs to be considered in parallel with the development of a gas market.

5.8.3 Oil

a. Oil in UNMIK

UNMIK is a net importer of oil. Petroleum products imported in 2009 amounted to around 520,000 tons of which diesel accounts for more than 55% and gasoline around 24%. 32 private companies operate in wholesale and more than 550 in retail oil supply. Imported petroleum products are transported 40% by rail and 60% by trucks.

The main law governing the oil sector is the Law on Trade of Petroleum and Petroleum Products of 2004, amended in 2009, which includes provisions encouraging free and fair competition; payment of tax liabilities and fiscal duties; and which ensure the quality, safety and security of supply. The Law applies to the wholesale and retail supply, transport, storage of petroleum and petroleum products.

The market structure is controlled by the Ministry of Trade and Industry through Administrative Direction No. 01/2010 which regulates the organization and functioning of the Licensing Office for Regulation and Monitoring of the Oil Sector.

Emergency oil stocks are defined in the amended Law on Trade of Petroleum and Petroleum Products as stocks reserved for use in cases of natural and social disasters or technical and technological catastrophes. All petroleum and petroleum product storage facilities and points-of-sale are obligated at any time to possess reserves of at least 5 % of their storage capacity for State emergency purposes. In case of market disorganization, the Minister of Trade and Industry through special legal acts can determinate the highest percentage for emergency reserves.

b. Progress made in 2009/2010

From January 2010 on, the Licensing Office became part of the Ministry of Trade and Industry. This office has three main objectives, namely licensing, market regulation and monitoring of the petroleum sector. The Licensing Office has started to implement the amended Law and is also finalizing Administrative Directions/Instructions in accordance with the Law.

A draft Law on Emergency Oil Stock Reserves has been prepared and should be adopted by the Assembly during 2010. Furthermore, a number of Administrative Directions implementing the Law on Trading of Oil and Oil Products have been adopted during 2010.

c. State of compliance

The law gives no preferences to domestic or non domestic oil and petroleum products. However, a 10% customs duty is applied to imports of petroleum products, LPG, and lubricants and bitumen from all countries, apart from countries parties to CEFTA. These customs duties are in violation of Article 41 EnC and need to be removed. The 10% customs duty for heating oils (Mazut) was abolished during 2010.

5.8.4 Competition

a. Competition and State aid in UNMIK

1 Competition law in UNMIK is governed by the Law on Competition of 2004. The cartel prohibition is modelled on Article 101(1) and (2) TFEU. As regards the exemptions, the situation is different. *Per se* exemptions apply to agreements within concerns and agreements with the purpose of effecting a merger. The competent authority may, upon request, exempt agreements on the uniform application of standards or business terms. Exemptions may, under certain conditions, also be granted to agreements dealing with the rationalisation of economic activities through specialisation or through *"increasing the efficiency or productivity of the participating undertakings in technical, commercial or organisational respects"*. Finally, the authority has the power to exempt agreements contributing to the *"improvement of the development, production, distribution, procurement, return or disposal of the items concerned"*. Restrictions of vertical agreement are subject to a separate prohibition. The abuse of a dominant position is prohibited. The definition of an abuse deviates from the wording of Article 102 TFEU. The Law applies to all undertakings including public enterprises, i.e. *"a public authority or an undertaking owned, controlled or administered, in whole or in part, by a public authority, if such public authority is engaged in the conduct of economic activity"*.

The Competition Commission (KCC) is the competent authority for competition law monitoring and enforcement. It reportedly started its work in February 2009. In cartel and abuse cases, sanctions include fines for undertakings of up to 100,000 € and personal fines for managers involved in the trust of up to 25,000 € (cartels) and 20,000 € (abuses) respectively. A leniency policy has not been established. Decisions taken by the KCC may be appealed to a Review Committee. That Committee's decision may be challenged before the district court. The Law also sets out special rules for private enforcement of competition law before the district court.

2 There is still no State aid law or an independent State aid authority in place in UNMIK.

b. Progress made in 2009/2010

1 KCC has developed a new draft Law on Competition, and has submitted it to the government. The draft has not been shared with the Secretariat.

2 A Law on State Aid has been drafted by the Ministry of Economy and Finance. The draft Law contains a State aid prohibition. However, the notion of State aid is not yet fully in line with Article 107 TFEU. The draft Law also establishes a State Aid Commission of ministry representatives, chaired by the Minister of Economy and Finance. The bill has not yet been sent to the government for approval but is planned to enter into force on 1 January 2011.

c. State of compliance

Articles 18 and 19 EnC have not been properly transposed into the law of UNMIK.

1 Competition legislation does not strictly follow the EU model and still needs some improvement on substance, in particular as regards the provisions concerning the abuse of dominant positions. An update of the Law should rectify these shortcomings. Furthermore, the Secretariat has no information on the independence and effectiveness of the KCC. In particular, the Secretariat has no information on decisions applying competition law to the energy markets in UNMIK.

Further to the general applicability of the Law on Competition, competition in the energy markets in UNMIK is affected by the Law on Energy of 2004 which contains a different set of provisions prohibiting cartels and abuses of dominant positions than the Law on Competition. The Energy Regulatory Office is tasked to enforce them. The relation between the two laws on substance is unclear, which is regrettable as they diverge considerably. Nor does energy legislation answer the question of how an energy regulatory authority shall perform tasks and carry out procedures for which competition authorities are normally much better equipped. The draft for a new Law on Energy still contains provisions modelled on Articles 101 and 102 TFEU and tasks both the Energy Regulatory Office and the Competition Commission with applying their respective legal framework to the energy sectors.

However, the draft Law also confers important tasks on ERO related to monitoring the overall effectiveness of competition and the occurrence of restrictive contractual clauses.

2 In the area of State aid, UNMIK is in a state of non-compliance with the Treaty due to the lack of primary legislation. The Secretariat will follow up on this within the next months.

However, the authorities regularly submit to the Secretariat a list of grants made in the energy sector, information which is very valuable in particular for the upcoming State aid study.

5.8.5 Environment

a. Environment in UNMIK

1 Environmental impact assessment in UNMIK is governed by the Law on Environmental Impact Assessment adopted in February 2009. It replaced the Administrative Directive on Environmental Impact Assessment of 2004.

With regard to *screening*, projects listed in Annex I to the Law are subject to a full environmental impact assessment, whereas projects listed in Annex II to the Law will be selected based on their review, case by case, for an environmental impact assessment. As regards *scoping*, the Law empowers the Ministry of Environment and Spatial Planning to establish and apply procedures. The Ministry shall provide, upon request, the necessary data and information of significance for the identification and assessment of direct and indirect impacts of the project on environment. The *environmental impact study* or Environmental Impact Assessment Report is the core document of the process. The Report shall be signed and submitted by its compiler and the applicant. As regards *decision-making*, the Ministry shall review remarks and opinions coming out of public debate, and decide to grant or refuse an environmental consent. The applicant is entitled to file an appeal in accordance with the Law within thirty days of the date of acceptance of the decision for environmental consent. Appeal shall be made to the Ministry.

2 The Wild Birds Directive is partly transposed by the Law on Nature Conservation of 2006 and the Law on Hunting. The Law on Nature Conversation sets the basic rules for nature conversation and for its sustainable utilization. The protection measures envisaged under the law comprise the protection of wild animals and the protection and conservation of habitats and species of wild fauna. Intentional capture or killing of specimens of wild animals is prohibited as is the intentional disturbance, especially during the period of breeding, rearing of young, hibernation or migration. The Law on Hunting also lays down protection measures for wild animals.

b. Progress made in 2009/2010

1 As regards environmental impact assessment, the Law on Environmental Impact Assessment was only adopted in February 2009. In May 2010, the Parliamentary Commission already approved a new draft Law on Environmental Impact Assessment. The Secretariat has not received a copy of this draft. Its adoption is foreseen for the end of 2010. Furthermore, secondary legislation necessary for the enforcement of the new Law should be introduced within 12 months after the entry into force of this legislative act. In February 2010, an Administrative Instruction on the information, participation of public and public concerned in EIA procedures has been adopted. Again, this document has not been shared with the Secretariat.

2 With respect to the protection of wild birds, UNMIK initiated the adoption of the new Law on Nature Protection. The new draft Law on Nature Protection was approved by the government in March 2010 and has been submitted to the Assembly. It is expected to be approved until September 2010. The draft Law defines the procedure for designating special areas of conservation (SAC) and regulates aspects of intervention in nature through the application of Environmental Impact Assessment for all public and private projects.

c. State of compliance

1 With the most recent legislation not been submitted to the Secretariat for review, it is currently not possible to assess UNMIK's state of compliance with the Environmental Impact Directive.

2 The transposition of the Wild Birds Directive has still not been fully achieved under the current legal framework. The designation of Special Protected Areas (SPA) and Special Area for Conservation (SAC), as envisaged by the Law on Nature Conservation, is not yet completed. General conservation measures are also provided for in the Law on Nature Conservation, but have not yet been taken in practical terms.

5.8.6 Renewables Energy

a. Renewables in UNMIK

1 Out of 970 MW of available generation capacity, only 43 MW is in hydro power plants. UNMIK has some potential for hydro (400 MW) and wind (50MW) power. Fuel wood is extensively used for residential heating. During 2008 and 2009, several surveys led to a re-assessment of the biomass contribution in the final energy consumption of about 27%. The total potential for renewable energy resources (mainly hydropower, biomass and solar) is estimated at about 1.7 TWh/y.

The Energy Strategy for 2009-2018, adopted in 2010 by the Assembly, recognises the importance of using renewable energy sources for electricity generation and heating, as well as the necessity to adopt a legal and regulatory framework to stimulate investments in RES projects.

In 2007, the Ministry of Energy and Mining adopted 7.78% RES targets for 2016 for both electricity and heat, including also annual indicative targets.

Feed-in tariffs have been adopted by the regulatory authority, ERO, for small HPPs (based on capacity) and wind farms. A Government Decision stipulates a five years buy-out contract for electricity produced from RES and cogeneration, with the possibility for extension. The Regulator is also empowered by the Law on the Energy Regulator to issue guarantees of origin for electricity or heat produced from RES.

2 The legislative basis for biofuels is still being drafted. There were no activities going beyond the Plan for the implementation of Directive 2003/30/EC, with the exception of draft targets for the period 2010-2015.

b. Progress made in 2009/2010

1 The drafts for three energy laws submitted to the Secretariat for comments included transposition of the main remaining Articles of Directive 2001/77/EC previously not considered. The laws have not yet been adopted.

2 A Decision on the Use of Biofuels in Transport was drafted in June 2009, transposing some basic provisions and setting up the yearly targets from 2010 (2%) until 2015 (5.75%). To date, no information is available on the adoption of the Decision.

c. State of compliance

The Plan to implement Directives 2001/77/EC and 2003/30/EC was submitted to the Ministerial Council in June 2007, as required by the Treaty.

1 The legal and regulatory framework for promotion of electricity produced from RES is almost completed. The focus for implementation shifts to the effectiveness of the measures already in place. The feed-in tariffs for other RES than wind and hydro power have to be adopted. The extensive use of biomass (reportedly from illegal logging) for heating has to be properly addressed by the institutions involved in forest management.

2 The adoption of the Decision on the Use of Biofules in Transport would be the first step for the implementation of Directive 2003/30/EC. Further promotion and development of incentive measures for biofuels is needed, especially with regard to the sustainability criteria in Directive 2009/28/EC.

5.8.7 Energy Efficiency

a. Energy efficiency in UNMIK

Under the existing legislation energy efficiency is, to a certain extent, covered by four laws in force in UNMIK, namely the Law on Energy, the Law on Electricity, the Law on the Energy Regulator and the Law on Construction. This set of legislation is supplemented by a set of secondary legislation on energy efficiency in the form of administrative instructions.

In an effort to align its legislation closer with the energy efficiency *acquis*, UNMIK adopted in 2008 an Administrative Instruction on Promoting Efficient Consumption of Energy by End-Users and Energy Services, following Directive 2006/32/EC without fully transposing it. Its implementation needs to be strengthened by the adoption of the Energy Efficiency Action Plan.

In 2008, UNMIK also adopted an Administrative Instruction on Labelling of Electric Household Appliances transposing Framework Directive 92/75/EEC. Full transposition of the set of implementing directives is planned for 2010, with the adoption of the (currently draft) Technical Regulation on the Form and Content of Household Appliance Labels.

Another Administrative Instruction on Energy Auditing was adopted in 2008. It regulates the auditing process including testing and certification of audits.

The Law on Construction was already adopted in 2004. Pursuant to its Article 12, the Ministry of Environment and Spatial Planning (MESP) adopted a Technical Regulation on Thermal Energy Saving and Thermal Protection in Buildings. The Regulation does not yet incorporate the requirements following from Directive 2002/91/EC on the energy performance of buildings.

Since 2005, energy efficiency is under the responsibility of a special unit within the Department of Energy in the Ministry of Energy and Mining (MEM). The establishment of an Energy Efficiency Agency is one of the priorities in the area of energy efficiency.

b. Progress made in 2009/2010

UNMIK submitted its draft Roadmap for the implementation of the *acquis* on energy efficiency in February 2010 to the Secretariat. Following the Secretariat's comments on the draft, the final Roadmap was submitted in June 2010.

A draft Law on Energy Efficiency was prepared and is planned to be adopted during 2010. The Law aims to regulate energy efficiency in greater detail, including the development of the National Energy Efficiency Plan (NEEAP), Municipal Energy Efficiency Plans, public sector energy management, energy auditing etc. The Energy Efficiency Law will also determine the role of different administrative bodies, organizations and agencies dealing with energy efficiency, including the Energy Efficiency Fund. The establishment of the Energy Efficiency Agency is one of the declared priorities.

On top of its 2008 Administrative Instruction on Labelling of Electric Household Appliances, UNMIK drafted a Technical Regulation on the Form and Content of Household Appliance Labels. This Regulation aims at creating a label design based on the template annexed to the respective Implementing Directives and translated into the official languages. The design was submitted to the Secretariat for comments in June 2010. Adoption is planned by the end of 2010.

MEM also submitted the first draft of NEEAP to the Secretariat in March 2009 for review and comments. The Secretariat's comments were incorporated into the final NEEAP submitted in June 2010.

The implementation of the Directive on the Energy Performance of Buildings remains one of the main challenges, since it is a joint obligation of both the MEM and the MESP. The new Law on Construction is in the drafting phase and will incorporate main requirements of Directive 2002/91/EC. It will also serve as a legal basis for future regulation on energy certification of buildings, modification of the existing Technical Regulation on Thermal Energy Savings and Thermal Protection in Buildings etc. Some requirements under the Directive, e.g. on energy audits, provisions on obligatory inspection of boilers and air-conditioning systems etc. will be incorporated into the draft Energy Efficiency Law and the relevant secondary legislation. An inter-ministerial coordinating committee will be established in order to better coordinate the drafting process.

During 2007-2009, the energy efficiency activities undertaken were based primarily on the Energy Efficiency and Renewable Energy Resources Programme (KEERERP), developed by the MEM with support from the EAR. Major activities were: application of energy efficiency measures in certain public sector facilities; implementation of the awareness raising campaign related to citizens' knowledge and energy efficient behaviour; capacity building programmes for central and local governments and universities on energy management; initial basic trainings on energy audits and auditing processes etc.

An EU funded programme managed by the European Commission Liaison Office during 2010 aims to train the trainers of energy audits and to create a certification board for energy auditors, as well as to provide training programmes for municipal energy planning including the development of several Municipal Energy Plans (MEPs) in selected municipalities. This activity will be followed up by the establishment of a sustainable training programme for energy auditors.

In 2009, the MEM prepared a three-year communications strategy for an energy efficiency campaign. The project is under implementation and currently covers 2010, while for 2011 the financial resources still need to be secured. The campaign includes a set of awareness-raising activities of informative and educational character, training of journalists etc.

c. State of compliance

As the deadline for implementing the energy efficiency directives does not expire until December 2011, the state of compliance is currently not assessed.

The required update and modification of the NEEAP and its submission to the Secretariat was completed by 30 June 2010.

5.8.8 Social Issues

a. Social issues in UNMIK

A large number of laws and by-laws regulating the energy sector and addressing social issues have been developed in UNMIK. They include the Law on Energy, the Law on the Energy Regulator, the Law on Electricity, the Law on Heating, the Law on Social Assistance Scheme, the Law on the Status and Rights of Martyrs' Families, KLA War Veterans and Invalids and Civilian Victims' Families, the Law on Pension for People with Disabilities, the Energy Strategy 2009-2018, the Law on Gender Equality and the Law against Discrimination.

b. Progress made in 2009/2010

In 2010, UNMIK finalised its Social Action Plan. The approval by the government is pending.

The main activities foreseen in the Social Action Plan include an evaluation of the social and economic effects of energy enterprise restructuring and/or the privatization process; the implementation of a legal and regulatory framework for protection of consumers in need, the development of a social dialogue at all levels, the improvement of work conditions and living standards of employees, the improvement of the working environment regarding health and safety measures for employees in energy sectors, the development of programmes and definition of implementing mechanisms, the identification of training needs according to labour market demands and monitoring of the Plan's implementation.

c. State of compliance

As no mandatory *acquis* exists in the social area, the state of compliance is currently not assessed.

Energy Community Secretariat
Am Hof 4
1010 Vienna
AUSTRIA

Tel:+ 43 1 535 2222
Fax:+ 43 1 535 2222-11

Internet: www.energy-community.org
E-mail: contact@energy-community.org