



**MEMORANDUM**

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**RE:** The Third Liberalisation Package to BiH

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**Executive Summary**

This memorandum reviews the changes wrought by the Third Liberalisation Package,<sup>1</sup> issued on September 3, 2009, and addresses their effect on the structure of the energy sector of BiH. The Third Package changes in both electricity and gas occurred primarily in five areas, and these changes are summarized in the memorandum. A sixth area is discussed that concerns only natural gas -- access to storage and LNG facilities. At the end of each section, the impact on the changes discussed on the situation in BiH is discussed.

1. Unbundling Regime. Motivated by the vertical foreclosure of market entrants, an unbundling regime was prescribed that provided choices of legal unbundling, and Independent System Operator (ISO) and a new structure, the Independent Transmission Operator (ITO). The ISO structure involves an owner of transmission lines only being responsible for liability insurance and investment financing, while the ISO fully operates

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<sup>1</sup> The Third Liberalisation Package is a set of energy Directives and Regulations as follows:

- Regulation (EC) No 713/2009 of the European Parliament and of the Council of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulators (hereinafter ACER Regulation.)
- Regulation (EC) No 714/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the network for cross-border exchanges in electricity and repealing Regulation (EC) No 1228/2003 (hereinafter Cross-Border Exchange Regulation).
- Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005 (hereinafter Gas Transmission Access Regulation.)
- Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC (hereinafter Gas Directive.)
- Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (hereinafter Electricity Directive.)

the transmission system. The ITO can sit in a vertically integrated utility; but a “Chinese Wall” must be built between it and the generation/supply functions, and the regulator is involved in detailed monitoring the ITO. Only TSOs situated inside a vertically integrated utility can choose an ISO or ITO structure. The deadline for application of the rule is 3 March 2012.

2. Stronger authorities of National Regulatory Authorities. The competencies of the national regulator authorities are substantially strengthened in multiple areas. The independence of the regulators is spelled out in detail, clearly prohibiting interference by a government or other public or private entity. Regulators’ can impose a penalty of up to 10% of an energy undertaking’s turnover for any regulatory violations. The regulators are charged with ensuring general compliance with European Union law. Finally, the regulators’ monitoring duties are greatly expanded, particularly regarding consumer protection in the retail market.
3. Retail Markets. The Third Package contains extensive new provisions that emphasize customer protection. In addition, new detailed guidelines (Annex I) are attached to both Directives.
4. European Network of Transmission System Operators (ENTSO) and European Network of Transmission System Operators Gas (ENTSOG). Under new regulations, the TSOs are required to cooperate in new organizations that are charged with the development of multiple network codes and ten-year network development plans.
5. Agency for Cooperation of Energy Regulators (ACER). A new EU-level regulator has been established by another new regulation. Representatives of the Member State regulators form the Board of Regulators. Although the jurisdiction of this regulator has been controversial, but the authorities granted to ACER are broad enough that it will have an impact on the energy markets.
6. Gas Storage and LNG Facilities. Third party access principles apply to both gas storage and LNG facilities, based on the facilities, not the identity of the party requesting storage or the portfolio in question.

## **Introduction**

The source of the Third Liberalisation Package was the Energy Sector Inquiry that started in 2005 and culminated in the Commission’s Communication dated 10 January 2007.<sup>2</sup> The Energy Sector Inquiry focused on identifying areas where competition was less than satisfactory, which were: market concentration/market power; vertical foreclosure (mostly, inadequate unbundling of network and supply), lack of market integration (including lack of regulatory oversight for cross-border transactions; lack of transparency, price formation, downstream markets, balancing markets and liquefied natural gas. The Final Report found

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<sup>2</sup> <http://ec.europa.eu/competition/sectors/energy/inquiry/index.html>

that priority was to be given to four areas: ”(1) achieving effective unbundling of network and supply activities, (2) removing the regulatory gaps (in particular for cross border issues), (3) addressing market concentration and barriers to entry, and (4) increasing transparency in market operations.<sup>3</sup>

Importantly, on 24 September 2010, the Ministerial Council of the Energy Community Treaty, *recommended* adoption of the Third Liberalisation Package. In the recitals to the Recommendation, the Ministerial stated that the directives and regulations identified as the “*acquis communautaire on energy*” were repealed and replaced by the Third Liberalisation Package and that, “Under Article 79 of the Energy Community Treaty, the relevant adaptations shall be proposed, as appropriate, by the European Commission.” It can be concluded from this provision that, whereas BiH is not presently mandated by the Treaty to comply with the Third Liberalisation Package, it is just a matter of time before the new directives and regulations are incorporated into it. Since the Third Liberalisation Package will go into effect in the EU on 3 March 2011, it can be assumed that this requirement to comply will be proposed by the European Commission in the near future. It is important that BiH understand the components of the Third Liberalisation Package because it will be required to comply with it. In the meantime, where BiH can comply with the Third Liberalisation Package in, for example, the ongoing process of market opening, it should.

Only the important *changes* to the energy directives are discussed in this Memorandum. This memorandum does not address issues from the Directives and Regulations that did not change from the Second Package to the Third.

## **1. Unbundling Regime**

### New Regime for Unbundling Transmission System Operator

The most extensive (and controversial) provisions of the Third Liberalisation Package were those with regard to unbundling Transmission System Operators (TSOs).<sup>4</sup>

While there are very detailed provisions regarding unbundling in both Directives, in summary, the three types of possible unbundled structures for TSOs are:

1. Ownership unbundling. A TSO that is part of an integrated undertaking must functionally and legally unbundle so that the same person or persons (a term that includes a Government or other public body) are entitled neither to exercise control over an undertaking performing generation or supply and directly or indirectly exercise any right over a TSO or transmission system; nor the converse –the same person or persons (including a Government or other public body) are not entitled to exercise direct or indirect control over a transmission system operator or transmission system and an undertaking performing generation or supply; nor can the same person

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<sup>3</sup> Communication from the Commission, Inquiry pursuant to Article 17 of Regulation (EC) No 1/2003 into the European gas and electricity sectors (Final Report), p. 3.

<sup>4</sup> Chapters IV and V of the Electricity Directive, and Chapters III and IV of the Gas Directive.

be a member of the supervisory board, the administrative board or bodies legally representing the undertaking of both an undertaking performing generation or supply and a TSO or transmission system.

2. Independent System Operator (ISO). Where a transmission system belongs to a vertically integrated undertaking, but instead of unbundling ownership of the system, an independent system operator is appointed to act as a transmission system operator. The ISO grants and manages third party access, including the collection of access charges, congestion charges and payments under the inter-TSO compensation mechanism. The ISO also operates, maintains and develops the transmission system, having full responsibility for ensuring the long-term ability of the system to meet reasonable demand through investment planning. The owner has no responsibility and no prerogatives as regards granting and managing third party access; its duties are to provide liability coverage relating to the network assets and finance the investments decided by the ISO. If the owner does not care to finance, then it must give its agreement to financing of the investments by any interested party, including the ISO, which may result in the network owner not becoming the owner of the new parts of the network.
3. Independent Transmission Operator (ITO). Under this model, the TSO may remain part of a vertically integrated undertaking; however, there are numerous rules ensuring true unbundling, requiring what could be termed micro-monitoring by the regulatory authority to ensure that no conflicts of interest exist.<sup>5</sup>

While the provisions for these unbundling options are numerous, what is particularly interesting are the restrictions on the choice of model:

1. The ISO and ITO models can only be chosen for a specific TSO if on entry into force of the Directives (3 September 2009), the transmission system belonged to a vertically integrated undertaking.<sup>6</sup> It is not possible to go from a situation of ownership unbundling to an ISO or an ITO if on entry into force of the Directives the on the date the Directives went into force the transmission system did not belong to a vertically integrated undertaking. For countries having several TSOs, only in situations where the transmission system was part of a vertically integrated undertaking on entry into force of the directives can the ISO or ITO model be chosen. New transmission systems that did not exist on 3 September 2009, must be ownership unbundled.
2. Where a Member State has opted for ownership unbundling, either in general or as regards a specific TSO, the vertically integrated undertaking does not have the right to set up an ISO or ITO. A Member State having several TSOs is free to opt for several models for different TSOs. However, once a choice has been made for a specific TSO to apply one of the unbundling models, all the elements of that model have to be complied with. Elements cannot be mixed to create a new unbundling model not provided in the Directives.

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<sup>5</sup> Interpretative Note on Unbundling,

[http://ec.europa.eu/energy/gas\\_electricity/interpretative\\_notes/interpretative\\_note\\_en.htm](http://ec.europa.eu/energy/gas_electricity/interpretative_notes/interpretative_note_en.htm).

<sup>6</sup> Article 9(8) in both the Electricity and Gas Directives.

How these rules are applied in practice will be clear several years in the future. By 3 March 2011, the rules of unbundling TSOs must be transposed, and the rule must be applied by 3 March, 2012.<sup>7</sup>

### Impact on Situation in BiH

*In 2004, Bosnia and Herzegovina unbundled its transmission system into a Transmission Company and an Independent System Operator, owned by the two Entities proportionately with the value of the facilities conveyed to the Transmission Company. The transmission sector satisfies the requirement of being legally unbundled.*

## **2. Stronger Authorities of National Regulatory Authorities**

The provisions in the Directives that comprise the Third Liberalisation Package that concern the regulatory authorities have been substantially expanded and elaborated to three expanded articles from the one article in the 2003 directives.<sup>8</sup>

The 10 January 2007 Commission's Communication found that both TSOs and regulators tend to consider short term national concerns over contributing to the integrated EU market. *Regulators lack the appropriate powers and discretion, and regulators are under the direct or indirect influence from national governments.*<sup>9</sup> [Emphasis added.]

### Designation of a Single Regulatory Authority.

The Directives (Article 39(1) of the Electricity Directive and 35(1) of the Gas Directive) state that "Each member State shall designate a single national regulatory authority at national level."

This is interpreted to mean that Member States may no longer designate one regulatory authority to deal with some of the regulatory duties and a different (regulatory or other) authority to deal with another duty of the regulatory authority. Specifically, the core duties of the regulatory authority cannot be split between the regulator and the Ministry.<sup>10</sup>

Notwithstanding this general rule, however, there is a provision for a derogation for ". . . the designation of other regulatory authorities at regional level within Member States, provided that there is one senior representative for representation and contact purposes at the

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<sup>7</sup> Interpretative Note on Unbundling, *op. cit.*, p. 6.

<sup>8</sup> Both the electricity and gas directives contain the same provisions for National Regulatory Authorities. The three articles for the regulators concern independence, general objectives and duties and powers, in that order. In the Electricity Directive, the three Articles are Articles 35, 36, and 37; and in the Gas Directives, the Articles are 39, 40, and 41.

<sup>9</sup> EU Energy Law, Vol. 1, The Internal Energy Market, The Third Liberalisation Package, Claeys & Casteels, 2010, at p. 218.

<sup>10</sup> Interpretative Note, The Regulatory Authorities, 22 January 2010,

[http://ec.europa.eu/energy/gas\\_electricity/interpretative\\_notes/interpretative\\_note\\_en.htm](http://ec.europa.eu/energy/gas_electricity/interpretative_notes/interpretative_note_en.htm).

Community level within the Board of Regulators of the Agency in accordance with Article 14(1) of Regulation (EC) No. 713/2009.”<sup>11</sup> This provision has been further discussed and explained by way of a derogation applied in countries like Belgium, where in addition to the national regulator, three regional regulators had been set up for the three federal regions.<sup>12</sup>

### Independence of National Regulatory Authority

Article 35(4) requires that member States guarantee that the regulator exercises its powers impartially and transparently. The Interpretative Note on The Regulatory Authorities states that the concept of impartiality is aimed at the regulator making decisions in a neutral way, based on objective criteria and methodologies. As an indication of how serious the Commission takes this requirement, the Note clearly states that, “In the view of the Commission’s services this requirement means that Member States must provide for dissuasive civil, administrative and/or criminal sanctions in case of violations of the provision on impartiality.”<sup>13</sup>

Article 35(4)(a) of the Electricity Directive and Article 39(4)(a) of the Gas Directive state, “the regulatory authority is legally distinct and functionally independent from any other public or private entity.” This means that the regulatory authority must be separate and distinct from any Ministry or other government body; even sharing personnel and offices is no longer in line with these articles.

Importantly, Article 35(4)(b) of the Electricity Directive and Article 39(4)(b) elaborate independence of regulatory authorities further by stating that they will act independently from any market interest and “*do not seek or take direct instructions from any government or other public or private entity when carrying out the regulatory tasks. This requirement is without prejudice to close cooperation, as appropriate, with other relevant national authorities or to general policy guidelines issued by the government not related to the regulator power and duties. . .*” [Emphasis added.] The Interpretative Note on Regulatory Authorities specifically states that these provisions are targeted at ensuring that regulatory decisions are not affected by political and specific economic interests. When making decisions, regulators and staff should *only* consider the general interest.<sup>14</sup> This provision prohibits regulators and staff from seeking or taking direct instructions from any government or other public or private entity. As stated, in the Interpretative Note, an instruction includes the use of pressure of any kind of regulator’s staff or on the persons responsible for its management. The European Commission thinks this is serious enough to require that member States provide for dissuasive civil, administrative and/or criminal sanctions in case of violations. It should be noted, however, that the Third Liberalisation Package does *not* deprive the government of the possibility of establishing and issuing its national energy

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<sup>11</sup> Electricity Directive, Article 35(1)(1).

<sup>12</sup> EU Energy Law, *op. cit.*, p. 220.

<sup>13</sup> Interpretative Note, Regulatory Authorities, *op. cit.*, p. 5.

<sup>14</sup> *Ibid.*, p. 6.

policy, but this policy should not interfere in any way with the regulatory authority's independence and autonomy.<sup>15</sup>

Other qualifications on the independence requirements include the ability of regulatory authorities to, as appropriate, consult transmission system operators and other national regulatory authorities. Indeed, regulatory authorities have the duty to closely consult and cooperate with each other and with the Agency for Cooperation of Energy Regulators, especially on cross-border issues.

Important are the specific provisions with regard to the regulator's accountability for its decisions. According to Article 35(5) of the Electricity Directive and Article 39(5) of the Gas Directive, ". . . decisions of the regulator are immediately binding and directly applicable without the need for any formal or other approval or consent of another public authority or any other third parties. Moreover, the decisions by the regulator cannot be subject to review, suspension or veto by the government or the Ministry. This, of course, does not preclude either judicial review nor appeal mechanisms before any other bodies independent of the parties involved and of any government."<sup>16</sup>

This does not mean that the regulatory authority is not legally accountable for its decisions, and indeed, it must be possible to introduce legal actions against a regulators' decisions. According to the Interpretative Note, in urgent cases, a court can be given the power to suspend a regulator's decision (typically via summary proceedings);<sup>17</sup> and, it is suggested, where a government does not agree with a regulatory decision, it can make use of the same procedures. The power to suspend regulatory decisions belongs only to the courts and judges or appeal mechanisms before any other bodies independent of the parties involved and of any government.<sup>18</sup>

### Duties of the Regulatory Authority

Whereas Article 36 of the Electricity Directive and Article 40 of the Gas Directive set forth the objectives of the regulator, they do not create the general duties and authorities of the regulator – Articles 37(1) of the Electricity Directive and Article 41(1) of the Gas Directive do that.

An important development results from the provision that charges the regulatory authority with "ensuring compliance of transmission and distribution system operators and, where relevant, system owners, as well as of any electricity undertakings, with their obligations under this Directive and other relevant Community legislation, including as regards cross-

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<sup>15</sup> *Ibid.*, p. 7.

<sup>16</sup> *Ibid.*, p. 9.

<sup>17</sup> BiH has such procedures prescribed: the BH Law on Administrative Disputes (OG BiH 19/02, Articles 8-18), the Federation law on Administrative Disputes (OG FBiH Articles 8-17) and the RS Law on Administrative Disputes (OG RS; Articles 7-14).

<sup>18</sup> Interpretative Note, Regulatory Authorities, *op cit.*, p. 20.

border issues.”<sup>19</sup> According to the Interpretative Note, this provision grants a general competence and duty to ensure general compliance with European Union law, with the cited provisions given the regulators the power to ensure compliance with the entire sector-specific regulatory *acquis communautaire* relevant to the energy market, vis a vis any energy undertaking.<sup>20</sup>

The core duties are:

- *Tariffs*. Fixing or approving fix or approving, in accordance with transparent criteria, transmission or distribution tariffs or their methodologies.<sup>21</sup>
- *Compliance*. Ensure compliance with Directives by TSOs and DSOs, including regarding cross-border issues.
- *Cross Border*. Cooperation on cross-border issues with concerned regulators and the Agency for Cooperation of Energy Regulators.
- *Unbundling*. Ensure there are no cross-subsidies between transmission, distribution, LNG, storage and supply activities.
- *Monitoring Duties* regarding the general oversight of energy companies.
- *Contracts*. Respecting contractual freedom with regard to interruptible and long-term supply contracts so long as they are compatible with Community law and policies.
- *Consumer protection measures*. Ensure such are effective and enforced, publishing recommendations regarding supply prices and ensuring access to customer consumption data and ensure provision of optional data at the national level for consumption data and prompt access for all customers to that data.

The provisions on tariffs and monitoring are extensive and discussed in more detail below:

### *Tariffs.*

In addition to the core task requirement to fix or approve transmission or distribution tariffs or their methodologies, further assignment of duties regarding tariffs is contained later in the respective Article(s).<sup>22</sup> The regulators must also approve at least the methodologies used to calculate or establish the terms and conditions for connection and access to national networks, provision of balancing services and access to cross-border infrastructures. According to the Interpretative Note, this language gives the regulators the duty of fixing or approving not only network tariffs or their methodologies but also methodologies used to calculate or establish the terms and conditions for connection and access to national networks, the provision of balancing services and access to cross-border infrastructures.<sup>23</sup>

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<sup>19</sup> Article 37(1)(b) of the Electricity Directive and Article 41(1)(b) of the Gas Directive.

<sup>20</sup> Interpretative Note, Regulatory Authorities, *op. cit.*, p. 15.

<sup>21</sup> Article 37(1)(a) of the Electricity Directive and Article 41(1)(a) of the Gas Directive. The Interpretative Note states that this is a duty “in relation for access to transmission and distribution networks,” p. 13, which is true under Article 37(6)-(7) of the Electricity Directive and Article 41(6)-(7) of the Gas Directive.

<sup>22</sup> Article 37(6)-(7) of the Electricity Directive and Article 41(6)-(7) of the Gas Directive.

<sup>23</sup> Interpretative Note, Regulatory Authorities, *op. cit.*, p. 13.

Regarding tariffs and/or their methodologies for connection and access to transmission and distribution networks, allowances should be made for the necessary investments in the networks to be carried out in a manner allowing those investments to ensure the viability of the networks.<sup>24</sup>

### *Monitoring.*

Article 37(1) of the Electricity Directive and Article 41(1) of the Gas Directive lay down a long list of monitoring duties for regulators, which generally include monitoring access to networks and infrastructure, monitoring markets and the development of competition, and monitoring consumer protection measures. Notwithstanding that the Directives provide that the monitoring duties can be delegated to an authority other than the regulator (and if so, the data must be shared as soon as possible with the regulatory authority),<sup>25</sup> the compliance provisions in Article 37(1)(b) of the Electricity Directive and Article 41(1)(b) of the Gas Directive guarantee that the regulators have the power to ensure compliance sector-specific regulatory *acquis communautaire* relevant to the energy market vis a vis the TSOs, DSOs and any electricity or gas undertaking.<sup>26</sup>

### *Powers Enabling Carrying Out of Duties.*

Articles 37(4)(d) of the Electricity Directive and Article 41(4)(d) of the Gas Directive give the regulator the power to impose effective, proportionate and dissuasive penalties on electricity and gas undertakings not complying with their obligations under the Directive or any relevant legally binding decisions of the regulator or of the Agency.<sup>27</sup> Pursuant to the Directives, Member States can assign the power to impose penalties to the regulator or give the regulator the power to propose to a competent court (not to any other public or private body) that it impose such penalties. The amount of the penalty can be up to 10% of a company's turnover.<sup>28</sup>

### *Impact on Situation in BiH*

*To remedy what the European Commission considered to be undue influence on the regulators, the regulator's role has been defined in further detail and greatly expanded. This was done to limit Governments' influence on the regulators in their day-to-day function. At the same time, the Third Liberalisation Package makes very clear that general energy policy guidelines generated by Governments remain acceptable.*

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<sup>24</sup> Article 37(6)(a) of the Electricity Directive and Article 41(6)(a) of the Gas Directive.

<sup>25</sup> Article 37(2) of the Electricity Directive and Article 41(2) of the Gas Directive.

<sup>26</sup> See, Footnote 27.

<sup>27</sup> This is in addition to the powers to issue binding decisions; carry out investigations into the function of markets and decide on any necessary measures to promote effective competition and proper functioning of the market; and require any information deemed relevant. Article 37(4) of the Electricity Directive and Article 41(4) of the Gas Directive.

<sup>28</sup> Interpretative Note, Regulatory Authorities, *op. cit.*, p. 18.

*With the new emphasis on regulator independence, the need for a carefully crafted and considered energy policy is a critical task for the BiH Governments. The policy will guide the actions of the regulator, while still allowing the enhanced independence and authorities of the regulators provided in the Third Package.*

*The requirement of regulator transparency is emphasized in the Third Liberalisation Package. The BiH regulatory commissions have generally followed their procedural rules and conducted their proceedings in a transparent way.*

*The general rule that Member States may no longer designate one regulatory authority to deal with some of the regulatory duties and a different (regulatory or other) authority to deal with another duty of the regulatory authority could be interpreted as impacting the three regulatory authorities in BiH. However, the conditions allowing derogation so that regulatory authorities can be designated at regional level within Member States, provided that there is one senior representative for representation and contact purposes at the Community level within the Board of Regulators of the Agency, are met in BiH. BiH is analogous to Belgium in this case. SERC presumably being the representative of BiH in the Agency for Cooperation of Energy Regulators and SERC's having jurisdiction over the Transmission Company and ISO, while the Entity regulators have jurisdiction over Distribution (and Generation), should meet the requirements for the derogation .<sup>29</sup>*

*Finally, the penalty provisions in the current versions of the Electricity Laws fall far short of the expanded regulatory ability to impose “effective, proportionate and dissuasive penalties on electricity undertakings” or to propose the same to a court. The penalty amount provided in the new Electricity Directives for energy undertakings not complying with their obligations under the Directive or any relevant legally binding decisions of the regulator or of the Agency is up to 10% of a company's annual turnover. The current penalty amounts provided in the Electricity Laws fall far below the amounts provided in the new Package.<sup>30</sup> At most, the SERC can impose of fines of at most 5,000-40,000; RSERC 5,000 – 15,000; and the FERC 5,000-30,000 KM. Given the healthy revenues of the regulated undertakings,<sup>31</sup> these penalties are far from effective, proportionate and dissuasive.*

### **3. Retail Markets**

The Third Liberalisation Package contains multiple new provisions with regard to retail markets that address the subject in some detail. When assembled together, the Third Package indicates a strengthened emphasis on encouraging the opening of retail markets and ensuring the protection of customers. The particularly relevant articles concern (i) the Articles

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<sup>29</sup> EU Energy Law, *op. cit.*, p. 222.

<sup>30</sup> Federation Electricity Law, Article 82; Republika Srpska Electricity Law, Article 102, and Act on Transmission of Electric Power, Regulator and System Operator for Bosnia and Herzegovina, Article 9.3.1

<sup>31</sup> From Annual Reports for 2009: EPRS 405.824.249 KM, EPHZHB 23,343,901 KM, and EPBiH 944,000,000 KM. From the SERC decision on approved revenues for ISO and Transco, dated April 27, 2010: Transco 123,548,981 KM and ISO 6,182,071 KM.

specifically entitled “Retail Market;”<sup>32</sup> (ii) Article 3 of both Directives on public service obligations and consumer protection;<sup>33</sup> (iii) the Directives’ Annex I that defines in some detail required Measures on Consumer Protection;<sup>34</sup> and (iv) the expanded provisions on regulators’ authority.<sup>35</sup>

### Retail Markets Provisions

The specific retail market provisions in the Directives address the need for rules to define the roles and responsibilities of TSOs, DSOs, supply undertaking, customers and other market participants regarding contractual arrangements, commitment to customers, data exchange and settlement rules, data ownership and metering responsibility. These rules will be public and be designed to facilitate customers’ and suppliers’ access to networks. They will be subject to regulatory review. The Directives further address these customer issues in Article 3 and the Annex I provisions.

### Public Service Obligations and Customer Protection – Article 3

The provisions from the Second Package regarding the public service obligation and universal service remain the same in the Third Package. However, in the Third Liberalisation Package, Article 3 is substantially expanded to address customer protection in more detail:

- Customers are entitled to be supplied by a supplier registered in another country, so long as the supplier follows the applicable trading and balancing rules. 3(4).
- A change of supplier must be effected by the operator(s) within three weeks, and customers are entitled to receive all relevant consumption data. 3(5).
- The vulnerable customer provisions are expanded: Member States are required to define the concept of vulnerable customers to refer to energy poverty and, *inter alia*, to the prohibition of disconnection of electricity to such customers in critical times. 3(7). Further, national energy action plans should ensure that social security systems ensure electricity supply to vulnerable customers or support is provided for energy efficiency improvements. 3(8).
- A high level of consumer protection must be ensured, particularly regarding the transparency of contractual terms and conditions, general information and dispute settlement mechanisms. Eligible customers must be able to easily switch suppliers. Regarding household customers, these measures shall include those set out in Annex I. 3(7).
- Electricity suppliers must specify in or with bills, fuel source labeling. Suppliers must also reference sources with information on the environmental impact of the electricity produced and information regarding customer rights regarding the means of dispute settlement available. Regulators must ensure that the information provided is, at a national level, clearly comparable. 3(9).

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<sup>32</sup> Article 41 of the Electricity Directive and Article 45 of the Gas Directive.

<sup>33</sup> Article 3 in both the Electricity and Gas Directives.

<sup>34</sup> Annex 1 to both the Electricity and Gas Directives.

<sup>35</sup> Articles 36 and 37 of the Electricity Directive and Articles 40 and 41 of the Gas Directive.

- Energy efficiency/demand-side management measures and the means to combat climate change, and security of supply, are required to be included, where appropriate. These measures may also include adequate economic incentives for the maintenance and construction of the necessary network infrastructure, including interconnection capacity. 3(10). Mention has been made of the fact that the inclusion of the words “as appropriate” weaken the provision.<sup>36</sup>
- To promote energy efficiency, the regulator shall strongly recommend that the use of electricity be optimized, for example by providing energy management services, developing innovative pricing formulas or introducing smart meters or smart grids, where appropriate. 3(11).
- Member States shall ensure the provision of single points of contact to provide consumers with all necessary information concerning their rights, current legislation and dispute settlement. 3(12).
- An independent mechanism, such as an energy ombudsman or a consumer body shall be put in place to ensure efficiency treatment of complaints and out-of-court dispute settlement. 3(13).
- An energy consumer checklist regarding energy consumer rights will be developed. 3(16).

### Annex I. Measures on Consumer Protection

Article 3 references Annex I, which expands provisions on customer protection even further, such as requirements on:

- listing the information that must be included in a contract with an electricity services provider;
- notice of an intention to modify contractual conditions with the right to withdraw;
- receipt by consumers of transparent information on applicable prices and tariffs and standard terms and conditions;
- offering a wide choice of payment methods , with any difference in terms and conditions reflecting the costs to the supplier of the different payment systems;
- not charging customers for changing supplier;
- provision of simple and inexpensive procedures to resolve complaints, in particular, customers having the right to a good standard of service and complaint handling by the electricity service provider. Disputes should be handled within three months;
- informing customers receiving universal service of their rights;
- consumers having access to their consumption frequently enough to regulate usage and be able by explicit agreement and free of charge give any registered supplier access to the metering data; and
- receipt by customers of a final closure account no later than six weeks after the change of supplier.

The Annex also addresses smart metering systems, stating first that intelligent metering systems shall be implemented to assist consumers. However, the implementation of these

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<sup>36</sup> EU Energy Law, *op.cit.*, p. 429.

systems may be subject to an economic assessment of all the long-term costs and benefits to the market and the individual consumer or determine which type of smart meter is economically reasonable and cost-effective and which timeframe is reasonable for their distribution. Even so, the Annex states that 10 years should be the target for implementation of the smart metering systems. Further, where it is determined that smart meters are desirable, then 80% of customers must be equipped with them by 2020. The metering systems within a State's territory have to be interoperable.<sup>37</sup>

### Impact on Situation in BiH

*There is much activity in BiH with regard to retail markets. The regulators have organized the Market Working Group, which is tasked to examining the BiH market to determine, inter alia, market impediments, work on the possibility of a Wholesale Market, and the development of rules for the Supplier of Last Resort and Default Supplier. A policy paper has been drafted that addresses the most important impediments to the market in BiH.*<sup>38</sup>

*At the present time, BiH is just beginning to establish the retail market. The provisions of the Third Liberalisation Package are far more detailed than those of the Second Package, which BiH is following currently. Even so, it would be a simple matter when implementing rules for the market, to incorporate the requirements of the Third Package.*

*Note that there is a substantial expansion of the vulnerable customer protection concept in that Member States are required to define the concept of vulnerable customers in a way to refer to energy poverty and, among other things, the prohibition of disconnection of electricity to such customers in critical times. At the present time, the Federation has no energy-related vulnerable customer program (Republika Srpska has a vulnerable customer program). It is imperative that appropriate vulnerable customer programs be instituted throughout BiH. Without such programs, it is difficult to open markets, which is exactly why there is a strong emphasis and elaboration of the concept in the Third Liberalisation Package.*

*The Directives and their Annexes I include a new topic: smart meters in preparation for a smart grid. The ability to perform cost-benefit analyses is included in the provisions; and if it is determined that the benefits outweigh the costs, then 80% of the customers must be equipped with the smart meters by 2020. The BiH EPs are currently in the process of replacing meters. The rapidity with which measurement technology develops indicates that it is important that decisions be carefully made by the EPs so that technology does not outrun their investments. For this reason, the regulators should be involved in the decision-making for metering, particularly in light of the clear intent by the EU to encourage smart meters and grids.*

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<sup>37</sup> Annex I, Para. 2, of the Electricity and Gas Directives.

<sup>38</sup> In the draft policy paper, the BiH market participants collectively identified eight impediments to the BiH Market: Metering/measurement, Unbundling, Cost-based tariffs, Generation deregulation, Vulnerable customer plans, Supplier of last Resort and Default Supplier/Customer Switching; Contracts and clarification of processes; and Procurement Law revisions.

#### **4. European Network of Transmission System Operators (ENTSO) and European Network of Transmission System Operators Gas (ENTSOG)**<sup>39</sup>

The two cited regulations require that all TSOs in electricity and gas cooperate at the Community level through ENTSO and ENTSOG to promote the completion and functioning of the internal market and cross-border trade and to ensure the optimal management, coordinated operation and sound technical evolution of the European electricity transmission network.<sup>40</sup> Both organizations are tasked to establish a number of network codes, which, other than a few sector-specific differences, are the same:

- Network security and reliability rules
- Network connection rules
- TPA rules
- Data exchange and settlement rules
- Interoperability rules
- Operational procedures in an emergency
- Capacity allocation and congestion management rules
- Rules for trading
- Transparency rules
- Balancing rules
- Rules regarding harmonized transmission tariff structures
- Energy efficiency regarding gas networks

In addition, ENTSO and ENTSOG must develop ten year network development plans and plans for electricity generation and gas supply every two years.<sup>41</sup> These plans are currently drafted and comprise non-binding Community-wide ten year network development plans.

In its ten year network development plan, ENTSOE finds that some 35,000 km of new transmission lines and 7,000 km of existing line upgrades are necessary. This involves almost 500 investment projects in 34 European countries, worth €23-28 billion in the first five years. This is much less than the up to one trillion Euro that the Commission saw as necessary in network and generation capacity by 2030.<sup>42</sup> ENTSOG, on the other hand, finds it necessary to increase European pipeline import capacities by 19%, increase European entry capacity from LNG terminals by 47%, an increase of European storage deliverability of 34%, an increase of an indicative measure for the development of interconnection capacities within Europe of 11%, and an increase of the sum of the aggregated figures for pipeline import capacity, LNG import capacity, national production deliverability scenarios and storage deliverability scenarios of 17%. Meanwhile, ENSOG has found a decrease of European

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<sup>39</sup> For electricity: Regulation (EC) No. 714/2009, 13 July 2009, on conditions for access to the network for cross-border exchanges in electricity and repealing Regulation (EC) No. 1228/2003; and for gas: Regulation (EC) No. 715/2009, 13 July 2009, repealing Regulation (EC) No. 1775/2005.

<sup>40</sup> Articles 4, both above-cited Regulations.

<sup>41</sup> Article 22 of both the Electricity and Gas Directives, and Article 8 of both Regulation 714/2009 on conditions for access to the network for cross-border exchanges in electricity and Regulation 715/2009 on conditions for access to the natural gas transmission networks.

<sup>42</sup> <https://www.entsoe.eu/index.php?id=232>.

indigenous national production deliverability of 24%, with an increase of European aggregated peak day demand of 12%.<sup>43</sup>

### Impact on Situation in BiH

*The ISO belongs to ENTSO-E. ENTSO-E and ENTSOG are tasked with developing a number of network codes, all of which will affect South East Europe. The BiH energy sector should take care to at least review for comment the network codes as they are developed, so that when they are implemented, there will be no surprises for market participants in BiH.*

## **5. Agency for Cooperation of Energy Regulators (ACER)<sup>44</sup>**

After it became clear that improved cross-national cooperation between National Regulatory Authorities was needed to make the internal market function effectively, in 2003, the European Regulator Group for Electricity and Gas (EREG) was formed. Even so, it was evident that a body that could manage internal market grid rules and the ability to make decisions on cross-border regulatory issues was needed. The European Commission came to the conclusion that a Regulatory Agency needed to be established.<sup>45</sup> Thus, the Regulation to establish the Agency for the Cooperation of Energy Regulators (ACER) was developed.<sup>46</sup>

The ACER is comprised of an Administrative Board, a Board of Regulators, a Director and a Board of Appeal. The tasks of the Agency concern:

- TSO Cooperation. The Agency is tasked with providing an opinion to the Commission on the formation of ENTSO and ENTSOG (gas) and the formulation of network codes, a draft annual work program, and a draft Community-wide network development plan. The Agency is tasked with considerable involvement in formulation of the network codes and monitoring their implementation. Further, the Agency is tasked to monitor progress as regards the implementation of projects to create new interconnector capacity, the implementation of the Community-wide network development plans, and the regional cooperation of TSOs.<sup>47</sup>
- National Regulatory Authorities. The Agency may issue decisions as provided in the Third Liberalisation Package, including making recommendations to assist national regulator authorities and market players in sharing good practices, and providing a framework within which national regulatory authorities can cooperate. The Agency shall provide an opinion at the request of a regulator on whether a decision taken by it complies with the Guidelines or other relevant provisions of the Third Liberalisation

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<sup>43</sup> ENTSOG European Ten Year Network Development Plan 2010-2019, 23 December 2009, Ref. 09ENTSOG-02.

<sup>44</sup> The Agency for Cooperation of Energy Regulators was established pursuant to Regulation (EC) No. 713/2009 of the European Parliament and of the Council, 13 July 2009, establishing an Agency for the Cooperation of Energy Regulators.

<sup>45</sup> EU Energy Law, *op cit.*, pp. 257-259.

<sup>46</sup> Regulation (EC) No. 713/2009 of the European Parliament and of the Council of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulations.

<sup>47</sup> Regulation (EC) 713/2009, Article 6.

Package. When the regulator encounters difficulties applying Guidelines, it may request the Agency for an opinion. The Agency also shall decide on the terms and conditions for access to and operational security of electricity and gas cross-border infrastructure.<sup>48</sup>

- Cross-Border Infrastructure. ACER can decide regulatory issues that fall within the competence of national regulatory authorities, which may include the terms for conditions of access and operational security only where the competent regulators have not been able to reach agreement within six months or upon a joint request from the regulators. The terms and conditions shall include a procedure for capacity allocation, a time frame for allocation, shared congestion revenues and levying charges on the users.<sup>49</sup>
- Exemptions and Opinions. The Agency in limited circumstances may decide on exemptions of interconnecting infrastructure (see above bullet) and can provide an opinion upon request by the Commission on decisions by national regulatory authorities on certification (unbundling of TSOs).<sup>50</sup>
- Monitoring and Reporting. The Agency shall monitor the internal markets in electricity and natural gas, in particular the retail prices of electricity and natural gas, access to the network, including access of electricity produced from renewable energy sources, and compliance with consumer rights. An annual report shall be issued on the results of the monitoring.

### Impact on Situation in BiH

*Even though BiH will not be a member of ACER's Board of Regulators, there will be an impact in the country from this European regulator, which is indicated by the numerous references to "national regulatory authorities.". At a minimum, decisions will be issued that impact BiH with regard to European network codes, certification of TSO unbundling applications and other matters. The activities of ACER should be carefully followed by the regulators and market participants.*

## **6. Natural Gas – Storage and LNG Facilities**

New provisions were added to the Regulation for access to the natural gas transmission networks regarding third-party access to storage and LNG facilities, the principles of capacity allocation mechanism and congestion-management procedures for storage and LNG facilities, and transparency requirements concerning the same.<sup>51</sup>

- Capacity Allocation and Congestion Management. The maximum LNG and storage facility capacity shall be made available to market participants, and the operators shall implement procedures that are compatible with the network access systems and the market, including spot markets and trading hubs. LNG and storage contracts shall

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<sup>48</sup> *Ibid.*, Article 7.

<sup>49</sup> *Ibid.*, Article 8.

<sup>50</sup> *Ibid.*, Article 9

<sup>51</sup> Regulation 715/2009 on conditions for access to the natural gas transmission networks, Articles 15, 17 and 19.

include measures to prevent capacity-hoarding by offering unused LNG facility and storage capacity on the primary market without delay (for storage facilities on a day-ahead and interruptible basis), and entitling LNG and storage facility users who wish to re-sell their contracted capacity on the secondary market to do so.<sup>52</sup>

- Third-Party Access Services. LNG and storage system operators are required to offer services on a non-discriminatory basis and make relevant information public. Storage facility capacity must be provided on a firm and interruptible third-party access bases, long term or short, bundled or unbundled service, along with injectability and deliverability. Contract limits on the required minimum size of LNG and storage facility capacity are required to be justified on the basis of technical constraints, permitting smaller storage users to gain access.
- Transparent Information. Operators must make public detailed information regarding the services it offers and the conditions applied, along with the technical information necessary for the facility users to gain effective access to the LNG and storage facilities. Contracted and available capacity shall be made available on a regular and rolling basis in a user-friendly standardized manner. Further, the amount of gas in each storage or LNG facility or group of storage facilities, inflows and outflows and the available storage and LNG facility capacities shall also be made available. Where a storage system is used by only one user, that user may make a reasoned request to the regulator for confidential treatment of the data

The Regulation makes clear that both storage and LNG facilities must operate on a non-discriminatory basis so that the same service is offered to different customers on equivalent contractual terms and conditions. Further, it is clear here that the criteria for third-party access are to be determined according to the type of storage or per storage facility, not per storage user or portfolio.

### Impact on Situation in BiH

*Even though BiH has no storage or LNG facilities to which the expanded provisions for third party access to them would apply, it is quite possible that BiH will in the future want to use other countries' facilities. A summary of these provisions has been included into the instant Memorandum with this possibility in mind.*

## **7. What BiH Must Do to Comply With the Third Liberalisation Package.**

*While BiH is not mandated to comply with the Third Liberalisation Package at this time, as explained in the introduction to this memorandum, it clearly will be under such obligation at some time in the future. Since the Third Liberalisation Package expands significantly the previous liberalisation policies, a thorough analysis and transposition effort must take place to bring BiH primary and secondary legislation in line with the Third Package's requirements. What is also needed before BiH can implement the Third Liberalisation*

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<sup>52</sup> Ibid., Article 17.

*Package is a decided and coordinated effort by the market participants to determine how to implement the provisions.*

*That work began with the Market Working Group's consideration of impediments to the BiH market, accomplished in cooperation with the market participants. To be efficient, as BiH creates its rules and regulations for the market, for example, it should comply with the Third Liberalisation Package now, rather than having to amend the rules in the near future.*

*The material that comprises the Third Liberalisation Package is voluminous. An immediate effort should be undertaken to be sure that all market participants can acquaint themselves with it in local language.*

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