

REPORT ON IMPLEMENTED ACTIVITIES FOR THE PURPOSE OF HARMONIZATION OF THE GAS SECTOR OF THE REPUBLIC OF SERBIA WITH INTERNATIONAL COMMITMENTS

The Energy Development Strategy until 2025 with projections until 2030 determines the strategic goals of the Republic of Serbia, namely: ensuring secure supply of the domestic market with natural gas, establishing the domestic and regional market of natural gas and diversification of sources and directions of natural gas supply.

In order to create a stable regulatory and market framework, capable of attracting investments in gas networks, electricity and transmission network production, and the creation of a regional energy market, which is essential for economic development and social stability, the Republic of Serbia has decided to start the process of international energy integration, by signing the Energy Community Establishment Treaty between the European Community and the Republic of Albania, the Republic of Bulgaria, Bosnia and Herzegovina, the Republic of Croatia, the Former Yugoslav Republic of Macedonia, the Republic of Montenegro, Romania, the Republic of Serbia and the United Nations Interim Mission in Kosovo in accordance with the United Nations Security Council Resolution 1244.

By signing this agreement, the Contracting Parties have undertaken to implement the relevant *acquis communautaire* on energy, environmental protection, competition and renewables.

In order to fulfill the obligations assumed by the Treaty on the Establishment of the Energy Community of Southeast Europe in December 2014, the National Assembly of the Republic of Serbia adopted the Law on Energy harmonized with the "third energy package". This law, in accordance with Directive 2009/73/EC, prescribes the conditions that must be met by the natural gas transmission system operator in terms of its organization.

The Law on Amendments to the Law on Energy from 2021 additionally opens the natural gas market by introducing a new participant in the natural gas market and enabling companies that are not registered in the Republic of Serbia to perform these activities on the market of the Republic of Serbia.

Also, this law in the field of gas creates the legal basis for the transposition into Serbian legislation of EU Regulation 1227/2011 on wholesale energy market integrity and transparency, EU Regulation 347/2013 on guidelines for trans-European energy infrastructure, EU Commission Regulation 2015/703 on establishing a network code on interoperability and data exchange rules, EU Commission Regulation 2017/459 establishing a network code on capacity allocation mechanisms in gas transmission systems, Commission Regulation EU 2017/460 on the establishment of a network code on harmonized transmission tariff structures for gas and Commission Regulation EU 312/2014 establishing a Network Code on Gas Balancing of Transmission Networks.

According to the assessment of the Secretariat of the Energy Community from the Report on harmonization for 2020, the Republic of Serbia has largely transposed the gas regulations into its legislation, but implementation of these regulations is at a low level.

This assessment was made primarily due to non-compliance of transmission system operators (Transport gas Serbia Ltd and Jugorogas transport Ltd) with the prescribed provisions of the Energy Law, lack of their certification and licensing in order to perform transport energy activities and transport system management.

Also, the report notes that the company Gastrans, owned by Gazprom and JP Srbijagas, was certified as an operator of the natural gas transportation system in accordance with the

decision on the exemption of the new interconnector for natural gas, issued by the Energy Agency of the Republic of Serbia and that the opinion of the Secretariat of the Energy Community was not taken into account.

The report especially emphasizes that The Republic of Serbia needs to correct its long-standing violations of the European Union's gas acquis. Without an open market, the Republic of Serbia will not be able to carry out cost-effective decarbonisation of the energy sector.

The Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Serbia, of the other part, in Article 109. Energy, paragraph 1, defines that cooperation will focus on priority areas related to the acquis communautaire in the field of energy, as well as that cooperation will be based on the Treaty establishing the Energy Community and will be developed with the aim of gradual integration of Serbia into the European energy market.

Accordingly, the harmonization of the gas sector with the acquis is one of the conditions for opening negotiations on Chapter 15 - Energy.

PE Srbijagas, - Transportgas Srbija Ltd

In order to fulfill international obligations, prevent the introduction of measures against the Republic of Serbia by the Ministerial Council of the Energy Community and remove obstacles to the opening of Chapter 15, a Plan for activities to reorganize PE "Srbijagas" Novi Sad was prepared. After considering the matter of property and possible risks related to resolving the issue of property and relations with creditors, a model of unbundling of the transmission system operator has been proposed, which in the first phase includes separation according to the ISO (independent system operator) model in accordance with Article 227. of the Law on Energy, and then at a later stage ownership unbundling in accordance with Article 224. of the Law on Energy In this regard, it is necessary that PE "Srbijagas" Novi Sad and the company "Transportgas Serbia" Ltd Novi Sad implement the prepared Action Plan

of Jugorosgaz jsc, Jugorosgaz - Transport Ltd.

Jugorosgaz ad Belgrade was established in accordance with the Law on Ratification of the Agreement between the Federal Government of the Federal Republic of Yugoslavia and the Government of the Russian Federation on Cooperation in the Construction of Gas Pipelines in the Federal Republic of Yugoslavia (Official Gazette of the FRY - International Agreements, No. 4/96).

In order to harmonize with the provisions of the Energy Law from 2011 and create conditions for certification and licensing of transmission system operators, a subsidiary Jugorosgaz Transport Ltd Nis was formed.

Agreement on entrusting activities 05 number 512-3660 / 2013-2 from 07.06.2013. Jugorosgaz Transport Ltd Niš is entrusted with performing energy activities of general interest in transport and transport system management.

Acting upon the request of "Jugorosgaz - Transport" Ltd on December 12, 2016, the Energy Agency of the Republic of Serbia made a preliminary decision on the certification of "Jugorosgaz - Transport" Ltd Nis.

Pursuant to Article 241. The preliminary decision of the Law on Energy was submitted to the Secretariat of the Energy Community, for an opinion.

By the act of April 22, 2017, the Secretariat submitted an opinion and pointed out that based on the information given in the Preliminary Decision and all other information obtained during the procedure, "Jugorosgaz - Transport" Ltd Nis does not meet the conditions related to unbundling.

By the decision of the Council of the Energy Agency of the Republic of Serbia dated June 20, 2017, "Jugorosgaz - Transport" Ltd Nis was issued a certificate as an independent system operator, under the conditions determined by that decision, i.e. to fulfill the established conditions within twelve months from the day the decision was made (i.e. by June 20, 2018).

On June 15, 2018, "Jugorosgaz - Transport" Ltd Nis addressed the Agency with a request to extend the deadline for fulfilling the conditions for certification by at least twelve months.

The Agency evaluated the submitted documentation, as well as the seriousness of the intention of "Jugorosgaz - Transport" Ltd Nis, expressed through a series of activities in order to obtain the missing documentation, and positively resolved the request and passed the Decision of 13 July 2018, by which "Jugorosgaz - Transport" Ltd Nis is given an additional deadline of 12 months to meet the requirements for certification.

Jugorosgaz - Transport Ltd Nis on April 30, 2019, in the procedure of regular reporting, informed the Agency that the shareholders of "Jugorosgaz" jsc Belgrade made a Decision on the adoption of an action plan for certification according to the model "independent transport operator" - ITO model in accordance with the Law on Energy (Article 232-238. of the Law on Energy).

Considering that "Jugorosgaz - Transport" Ltd Nis was issued a certificate as an independent system operator (ISO model) The Council of the Energy Agency of the Republic of Serbia passed a decision on July 15, 2019, that revokes "Jugorosgaz - Transport" Ltd Nis the certificate issued by the Decision of the Energy Agency of the Republic of Serbia from June 20, 2017.

In order to create conditions for certification of Jugorosgaz Transport Ltd Nis according to the model "independent transport operator" - ITO model, an initiative was launched to amend the Agreement between the Federal Government of the Federal Republic of Yugoslavia and the Government of the Russian Federation on cooperation in gas pipeline construction in the Federal Republic of Yugoslavia, which is in the process of harmonization between the parties, and the main change of which is that the owner of the gas pipeline system can be besides Jugorosgaz ad its subsidiary (in the case of Jugorosgaz Transport Ltd).

The plan for implementation of activities for the purpose of certification of Jugorosgaz Transport Ltd Nis (Annex 1 Plan for implementation of activities for the purpose of certification of Jugorosgaz - Transport Ltd according to the model of independent transport operator (ITO), which is an integral part of this report) defines activities to be undertaken by the Ministry responsible for energy affairs, Jugorosgaz ad Belgrade and Jugorosgaz Transport Ltd Nis, in order to create conditions for certification of Jugorosgaz Transport Ltd Nis.

Gastrans Ltd

Gastrans Ltd was founded on November 28, 2011 by the company SOUTH STREAM SERBIA AG from Switzerland, whose founders are PE Srbijagas (49%) and Gazprom (51%). The subscribed capital of this company is around EUR 250 million.

The Energy Law, which is fully in line with Directive 2009/73/EC on a common code for the internal market in natural gas, stipulates in Article 288, paragraph 1 that new infrastructure facilities of the gas pipeline system, i.e. interconnectors or natural gas storage facilities, may be request exempted from the application of Article 224 of this Law (*ownership unbundling*), as well as the right of access referred to in Article 283, paragraph 1 of this Law (*free third party access and the application of regulated prices*), under the following conditions:

- 1) that investment in a new infrastructure facility increases market competitiveness and security of supply;
- 2) that the risk of investing in new infrastructure facilities is such that there will be no investment unless an exemption is granted;

- 3) that the new infrastructure facilities must be owned by a natural or legal person operating in another legal entity separate from the system operator within which the new infrastructure facilities will be built;
- 4) that the users of the new infrastructure facility bear the costs for the use of that facility;
- 5) that the exemption does not impede competition, the efficient functioning of the internal market in natural gas and the efficient operation of the regulated system with which the new infrastructure facilities are connected.

Accordingly, on February 2, 2018, Gastrans Ltd submitted to the Energy Agency a request for exemption of the future gas interconnector from the obligation of ownership unbundling from Article 224. Of the Law on Energy and exemption of the future gas interconnector from the access of a third party and the application of regulated prices from Article 283, paragraph 1. of the Energy Law, for a period of 25 years.

In October 2018, the Council of the Energy Agency of the Republic of Serbia adopted the Preliminary Exemption Act. This act, in accordance with the Law on Energy, was submitted to the Secretariat of the Energy Community for opinion. The opinion was given on February 2, 2019 and was the basis for the Council of the Energy Agency of the Republic of Serbia to adopt the final act on exemption in March 2019. The Energy Agency of the Republic of Serbia has approved the exemption of the new interconnector Gastrans Ltd from the obligation of ownership unbundling, and a partial exemption from the obligation to approve third party access and application of regulated prices, for a period of 20 years. In the final act on exemption, the Council of the Energy Agency of the Republic of Serbia took into account the opinion of the Secretariat of the Energy Community to the greatest possible extent.

In the act on exemption of the Energy Agency of the Republic of Serbia, it implemented the following conditions from the Opinion of the EnC Secretariat:

- The maximum amount of capacity that can be allocated in the binding phase to project investors and third parties has been accepted, so that:
 - a) approved priority distribution to investors in the amount of:
 - 70% of technical capacity at the entrance (interconnector Bulgaria - Serbia)
 - 55% of technical capacity at exit points in Serbia
 - 75% of the technical capacity at the Horgos exit (interconnector Serbia-Hungary)
 - b) approved distribution to all third parties in the following percentage:
 - 20% of capacity on the interconnector Bulgaria-Serbia
 - 35% at exit points in Serbia
 - 15% at the Horgos exit points (Serbia-Hungary interconnector)
 - c) approved to reserve at least 10% of the technical capacity for short-term allocations (after the construction of the pipeline), provided that at least 10% of the technical capacity is provided in case the investor decides to change the technical design of the project.
- The request of the EnC Secretariat that 10% of the technical capacity reserved for short-term distributions be increased, before each distribution, for all the agreed capacity, but not nominated for the next day, and for all agreed capacity that users return to Gastrans for distribution was accepted
 - The application of contractual congestion management provisions has been accepted
 - The request of the EnC Secretariat to accept the capacity allocation in the obligatory phase by applying the auction method and ranking the bids according to the so-called criterion "willingness to pay" if the requirements for long-term capacities are higher than the offered capacities, was accepted.
- All requests of the Secretariat regarding the method of transport system management have been accepted (capacity allocation and congestion management after the construction of the gas pipeline)

- The obligation to offer for distribution and contracting has been accepted: commercial return capacity on the interconnector Hungary-Serbia, Serbia-Bulgaria and to provide physical flow of gas in the opposite direction Serbia-Bulgaria in case of gas shortage.

The Agency did not accept the following conditions from the Opinion of the EnC Secretariat:

- that, in case all capacity is not allocated to "third parties" in the binding phase, all unallocated long-term capacity intended for third parties is reserved for short-term allocations (after construction of the pipeline) and thus the already reserved 10% from subclause c) be increased.

- that this decision conditions the exemption by the obligation of PE Srbijagas to implement the legal unbundling of Transprotgas Srbija

- to introduce the Gas Release Program as a measure to ensure the protection of competition in the market

Also, in March 2019, the Council of the Energy Agency of the Republic of Serbia approved a set of acts adopted by Gastrans Ltd, which was ordered to adopt them in the final act on exemption. The adoption of these documents was a condition that had to be met before the implementation of the binding phase of long-term capacity allocation on the new interconnector.

In accordance with the Law on Energy from 2014 and the final act on exemption ("Official Gazette of RS", no. 15/19), Gastrans Ltd submitted an application for certification in June 2019. The Council of the Energy Agency of the Republic of Serbia adopted a preliminary act by which Gastrans Ltd was conditionally certified as an independent transport operator, with the obligation to submit use permits or register ownership of natural gas transmission system facilities, as well as to submit evidence of independent operation and transmission system operation, in accordance with the exemption act, within 6 months from the beginning of the operational work. In December 2019, the Secretariat of the Energy Community gave an opinion on the preliminary decision and in February 2020, the Council of the Energy Agency of the Republic of Serbia adopted the final act on certification. Gastrans Ltd Novi Sad is conditionally certified as an independent natural gas transport operator, with the same obligations set out in the preliminary act.

The issue of certification of Gastrans Ltd is fully within the competence of the Energy Agency of the Republic of Serbia as an independent regulatory body. During the accession negotiations, the regulatory regime of Gastrans needs to be reviewed in view of compliance with EU legislation.