

ENERGY SECTOR

CURRENT SITUATION

Electricity

The legal framework for electricity in Serbia is set out under the 2014 Energy Law, which for the most part transposes the European Union's (EU) Third Energy Package.

The main authorities responsible for this sector are: (i) the Serbian Government; (ii) the Ministry of Mining and Energy (the **"Ministry of Energy"**); and (iii) the Energy Agency.

State-owned enterprises Elektromreža Srbije (EMS) and Elektroprivreda Srbije (EPS) remain the dominant players in the sector. EMS is the transmission system operator. EPS is engaged in the production, wholesale and supply of electricity. EPS's subsidiary EPS Distribucija carries out the distribution and operates the distribution system.

The electricity market is fully liberalized on paper. Households and small consumers remain, for the time being, entitled to opt to be supplied under regulated prices (unlike other consumers which do not have the right to regulated prices). There is an intention to phase out the regulated supply of electricity, but the Energy Agency has taken the position that there is still a need for the regulation of electricity prices. On the other hand, the Energy Agency has allowed an increase of regulated prices - starting from the latest increase was in December 2019. The experts agree that this increase is insufficient and that new increases should be expected.

Despite the liberalisation, EPS remains the single most dominant supplier with around 98% of market participation.

The day-ahead market is operated by the joint-stock company South East European Power Exchange (SEPEX). SEPEX has not yet introduced intra-day market.

Renewables

The incentives package finalized in 2017 is available only to the entities that obtained the privileged power producer status or preliminary privileged power producer status (subject to reaching the final status during validity of the preliminary status) by the end of 2019. This incentives package was the result of the notable efforts to make consistent, comprehensive and bankable framework for supporting renewable energy.

With this package expiring in the end of 2019, Serbia has requested the assistance of the European Bank for Reconstruction and Development (EBRD) in the preparation and implementation of new incentives package based on competitive renewables auctions. Although it was expected that the Serbian Government would pass a new scheme by the end of 2019, the new scheme is not likely to be in place before the end 2020, or, even more realistic in 2021.

In preparation of the new incentives scheme, the decision makers should ensure that the new scheme envisages a competitive process for awarding incentives, rather than the first-come-first-serve system that Serbia has historically employed. The incentive scheme should also follow other criteria set out in EBRD and Energy Community joint policy guidelines.

There is still no indication whether the new scheme would envisage the support through feed-in tariff or contract for difference. The stakeholders expect that the mechanics itself is of less importance if the support scheme follows the bankability criteria.

Energy Efficiency

No major changes in the legislation regulating energy efficiency have been made in the previous year.

The Law on Efficient Use of Energy, adopted back in 2013, explicitly defines the energy services company (ESCO) and sets rules for energy performance contracting in line with the EU acquis, with the aim to provide a comprehensive legal framework for energy efficiency arrangements.

To enable the implementation of these general possibilities, the Rulebook on Model Energy Service Contracts for the Implementation of Energy Efficiency when Users are from the Public Sector (ESCO By-Law) was finally adopted in May 2015.

The ESCO By-Law prescribes two models of ESCO agreements, one for public buildings and one for public lighting. It requires public-private partnerships (PPP) to be established between the relevant public partner (e.g. a municipality, a public company, the state) and the relevant private partner (i.e. an ESCO company) on a long-term basis.

The energy efficiency market is still developing. Energy performance contracting (EnPC) projects in the area of public lighting have been initiated in a significant number of local municipalities, while the market is yet to see a successful cooperation between the public and private sector

in the area of public buildings.

The energy supply contracting (ESC) has also started functioning recently, primarily with public sector facilities such as schools and hospitals being the main point of interest. However, some of the implementation aspects, such as public budgeting, remain a point of misunderstanding for the public sector.

Unlike EnPC, ESC arrangements are still not governed by any by-law, nor is there a prescribed model available. The most notable difference between ESC and EnPC is in that EnPC implies backing the project with guaranteed savings, unlike the ESC, which focuses on a renewed arrangement regarding energy supply where the private partner guarantees the continuous provision of a certain minimum amount of energy. It is expected that, once the ESC model is regulated too, a much needed certainty will be brought into the sector, allowing for successful cooperation between the public and private sectors.

COVID-19

Electricity

COVID-19 has not particularly affected this sector.

Renewables

A few days after the declaration of the state of emergency, EPS invoked Force Majeure regime under power purchase agreements (PPA) with privileged power producers. Accordingly, effects of the PPA were suspended during the state of emergency.

This invocation of Force Majeure was arguably ungrounded and sent negative signal to the stakeholders in terms of reliability and predictability. Part of the sector perceived this also as a signal that EPS has notable liquidity issues.

Energy Efficiency

COVID-19 has not particularly affected this sector, except by general slow down in work process of administration due to rules that limited the number of persons i.e. employees in enclosed space.

POSITIVE DEVELOPMENTS

Electricity

SEEPEX membership grew to 21 members.

Renewables

A number of renewables projects, including large-scale wind power plants, reached commercial operations and started production in 2019.

Energy Efficiency

The number of awarded and initiated projects in the energy efficiency market has continued to grow, which is surely a positive step towards the further development of the energy efficiency market. In 2019, the competent Ministry published two tenders for award of funds from the Budget Fund. Based on the first tender, funds have been allocated to 24 projects, while funds from the second tender are still to be awarded.

The successful awarding of several energy performance contracting projects to private investors in the area of public lighting throughout Serbia continued during the previous year.

Energy supply contracting has also started to function, although it is still of somewhat limited scope. Several PPP contracts in this sub-sector have been awarded to private investors, with the projects typically relating to the heating systems of public utilities. Even so, private-to-private arrangements continued to grow, although existing practices are rather diverse and of different contracting quality.

REMAINING ISSUES

Electricity

Coal remains dominant resource for electricity generation – more than 70% of annual production comes from the coal-fired power plants.

Coal mines are in a relatively poor shape and in need of extensive modernisation in order to meet demand. Some major thermal power facilities will also need to be phased out or overhauled. It is not clear whether Serbia will have enough funds for these investments.

It can often be heard that an electricity price increase in Serbia would be justified, but vulnerable customers must be protected.

Renewables

The market does not seem to be mature enough to see a large-scale renewable projects realized solely on market basis, including on the basis of the corporate PPA. The customers are not currently driven to look into direction of corporate PPAs

as the prices for the electricity coming from EPS are still rather low and currently it would be hard to argue in favour of the need to ensure supply on the basis of the corporate PPAs.

In that sense, the lack of the incentive scheme for new projects seems to be the critical immediate factor obstructing further expansion of the RES projects.

Energy Efficiency

As to energy performance contracting (EnPC), apart from the need to have consistent practices in the formal preparation of projects fully in line with the ESCO By-Law and the PPP legislation, the challenges ahead also include the need to reduce subsidies, which keep energy prices on an artificially low level, and to introduce further sector-specific incentives for energy efficiency projects in the relevant regulations (notably, real estate and tax-related regulations) as well as the need to further raise financiers' awareness of the practical feasibility of ESCO projects.

As to energy supply contracting (ESC), the adoption of a model contract by the relevant authority (i.e. the Ministry of Mining and Energy) would be very helpful in addressing projects involving both the public and private sectors and removing

the existing ambiguities. The public sector is still overly careful in considering prospective projects, while the understanding of this concept and its practical implementation is still lacking on the authorities' side. This specifically relates to an absence of understanding of public budgeting procedures, with some important projects involving hospitals and schools in Serbia still lagging behind as a result thereof. Even though the Ministry started working on a model ESC contract which would allow for a greater transparency and feasibility of projects on the market, the relevant model has not yet been adopted.

The challenges ahead relating to both EnPC and ESC arrangements remain the same and require continuous work:

- capacities of the PPP Commission to be improved (including better understanding of EnPC and ESC projects' specifics);
- sharing of knowledge and existing know-how among various public entities to be strengthened and supported (especially in the case of minor Serbian municipalities);
- practical implementation of the rules relevant to determining the value of projects that are PPP-specific and of the rules of public budgeting needs to be improved, and the capacities of the public sector to be strengthened.

FIC RECOMMENDATIONS

Electricity

- Regulation of electricity prices to be abandoned (but vulnerable customers to be protected), allowing new investments in the modernisation and revitalisation of coal and electricity production. (3)
- Intra-day market to be introduced. (2)
- Consider introducing carbon pricing instruments. (3)
- Introduce grid connection reservation security mechanism e.g. bank guarantee or cash collateral by developers in order to avoid existing grid queues holding up capacity; (3)

Renewables

- Incentive system to be tailored to accelerate investments in the renewables sector and follow the EBRD and Energy Community policy guidelines. (3)
- To improve the provisions of the Law on Agricultural Land pertaining to the utilization of the state-owned agricultural land for non-agricultural purposes, such as the development of renewable energy projects, in a way to regulate in more detail the conditions for granting the public agricultural land to renewable energy investors." (2)

Energy Efficiency

- Adoption of a functional model contract to govern energy supply contracting. (3)
- Improvement of capacities of the PPP Commission and other notable public stakeholders with respect to both energy performance contracting and energy supply contracting projects involving the public and private sectors. (2)

TELECOMMUNICATIONS

The activities in 2020 triggered by the coronavirus pandemic were marked by the synergy between the Government of the Republic of Serbia and the electronic communications operators. The results of such activities had a significant impact on the entire society and economy of the Republic of Serbia by enabling successful functioning in the conditions of the state of emergency that was declared on March 15, 2020 on the territory of the entire country.

COVID-19

The operators supported all measures imposed by the state and made their resources available for general interest and to help facilitate the functioning of the entire society affected by the coronavirus. In a short period of time, the operators provided short codes free of charge and free calls to citizens of the Republic of Serbia, for the needs of the National COVID-19 Call Center within the Ministry of Health. The operators also provided the necessary devices for recording the content of the primary and secondary school curriculum, which was broadcast on the channels of the public media service and on RTS Planeta digital platform. In addition, students were provided with free data transfer to the digital platform RTS Planeta and Moja škola during online lessons in the Republic of Serbia. In this context, free internet access for video conferencing such as Microsoft Teams and Zoom was provided, which made it possible for the lessons to retain their interactive property in digital form. In cooperation with the competent ministry, a large number of students were provided with internet access, and within the same initiative, this was made possible for students from socially vulnerable families for each month until the end of the year. At the end of April 2020, for the purpose of online mock final exam for 8th grade elementary school students, using the Tesla EDU digital platform, for a period of three months mobile telephony operators provided a dona-

tion of over 1000 smart mobile phones with appropriate SIM cards for internet access.

On the other hand, the competent ministry and the regulator provided a considerable support to the industry and the Council commends their timely and adequate response during the crisis period. Owing to the strong support of the Ministry of Trade, Tourism and Telecommunications, it was possible to perform works on the development of additional network capacities and maintenance of the current capacities during the curfew, which enabled the continuous quality of services for the customers. We also appreciate the fact that during this period, RATEL worked continuously and provided maximum efficiency, while their announcement on the importance of the role of mobile operators contributed to raising citizens' awareness in recognizing false news about the alleged connection between 5G technology and the epidemic.

Although the state of emergency was lifted by the National Assembly of the Republic of Serbia on May 6, 2020, the need for greater digitalization in all areas of life and work is still present and is expected to grow even more in the coming period. Thus, the appearance of the COVID-19 virus further encouraged a faster and more comprehensive digital transformation of the society, compared to the planned transformation in ordinary circumstances. Mobile telephony operators, as holders of critical telecommunication infrastructure necessary for connecting and functioning of the entire public system and the work of the economy in the "remote" and „WFH" mode, have proven to be the main pillar of the process of digitalization of the entire society.

Also an important moment in the state of emergency is the sudden increase of national traffic that exceeds the existing capacity of the operators, as a result of which one of the main priorities was significant investment in the network to ensure the expansion of capacity for all types of traffic