



**REGULATORY COMMISSION FOR ELECTRICITY
OF REPUBLIC OF SRPSKA**

**ANNUAL REPORT
FOR 2005**

Trebinje, August 2006

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APPENDIX 1 - REFORM OF THE ELECTRIC POWER SECTOR IN THE EUROPEAN UNION

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Preamble

Regulatory Commission for Electricity of Republic of Srpska (hereinafter "Regulator") was founded pursuant to Law on electricity of Republic of Srpska ("Official Gazette of Republic of Srpska" number 66/02, 29/03, 86/2003 and 111/04) in order to regulate monopolistic behavior and provision of transparent and non-discriminatory position of all participants at the electricity market in Republic of Srpska.

The Annual Report of the Regulator was prepared pursuant to Article 31 of the Law on electricity of Republic of Srpska which provides that the Regulator is obliged to inform the National Assembly of Republic of Srpska about its work at least once a year.

In the first part of the Report, it was described the work and key activities of the Regulator in 2005, method of financing with the financial report while in the second part of the Report there are observations which are of importance for the electric power market development, the electric power system situation and electricity market in Republic of Srpska and Bosnia and Herzegovina.

National Assembly of Republic of Srpska adopted the Annual Report of REERS for 2004, along with the financial report, in its 30th regular sessions which was held on 15 November 2005.

In 2005, Regulator undertook and carried out a range of activities within its competences defined by the Law on electricity. All activities were carried out in a public and transparent way.

Until the beginning of 2005, Regulator held nineteen regular sessions and consequently a range of documents and decisions, important for its future work and of special importance for the electric power sector, were made.

In its work, Regulator was cooperating and harmonizing its activities with the State Regulatory Commission (SERC) and Regulatory Commission for electricity in Federation of BiH (FERC).

Preliminary annual report of the Regulator in 2005, with the estimate for the budget realization, was presented to the National Assembly of Republic of Srpska on 14 December 2005 while considering and adopting the Budget for 2006.

For the purposes of continuation of its regular work and meeting legally defined obligations, Regulator submits this Annual report for 2005 to the National Assembly of Republic of Srpska for adoption.

A. ANNUAL REPORT OF THE REGULATORY COMMISSION FOR ELECTRICITY

1. Introduction

The reform process of the electric power sector in Republic of Srpska was initiated by signing Statement on the electric power policy beginning of 2000. End of 2002, it was made the Study of restructuring and privatization of the electric power sector in Republic of Srpska, based on which it was made the Action plan for restructuring of the electric power sector in Bosnia and Herzegovina for Republic of Srpska. The same year, it was made the Law on electricity of Republic of Srpska and Law on transmission, regulator and independent system operator of electricity in Bosnia and Herzegovina and accordingly legal framework for implementation of the reform of the reform of the electric power sector in Republic of Srpska. Having adopted the Independent system operator for transmission of electricity in BiH in 2004, Bosnia and Herzegovina actually initiates the reform of the electric power sector.

National Assembly of Republic of Srpska passed Law on electricity ("Official Gazette of Republic of Srpska", number 66/02, 29/03, 86/03 and 111/04) in order to create condition for rational and cost-effective development of generation and distribution of electricity in the region of Republic of Srpska and promote the companies offering public services for normal supply of customers with electricity.

Law on electricity of Republic of Srpska (hereinafter "Law"), as the basic entity law for the electric power sector in Republic of Srpska, establishes the rules for generation, distribution, supply and trade of electricity, including regulation of these activities by establishing Regulatory Commission for electricity of Republic of Srpska and defining its authorizations and competences.

Regulator was founded pursuant to the Law as a specialized, independent and non-profitable organization in order to regulate monopolistic behavior and provide for transparent and non-discriminatory position of all participants at the electricity market.

Since the Law tends to the gradual liberalization of the national electricity market, it is the role of Regulator in that part very important. The activities related to the market opening are necessary to be harmonized at the level of Bosnia and Herzegovina, through the direct cooperation of the regulatory commissions.

There were significant activities and a step forward in development of the regional energy market in 2005, while the most important energy event of the year was signing of the Energy Community Treaty in South East Europe.

Activities related to creation of the Energy Community of the South East Europe started in 2002 signing the Memorandum on Understanding about the regional energy market and its integration in the internal market of the

European Community (Athens Memorandum) and were continued by signing the Athens Memorandum dated 2003.

The Athens Memorandum was arranging the policy and objectives aimed at establishment of the regional energy market in South East Europe and gradually ensuring its integration in the internal market of energy of the European Union. Political will of the countries signatories to the Memorandum resulted in signing the Contract on establishment of the Energy Community of the South East Europe. This Contract which was signed in Athens on 25 October 2005 between EU and participants to the Athens Memorandum¹ enables gradual creation of the internal market for electricity and gas accompanied by active participation of the member countries of the European Union and participants. The aim of this Treaty is creation of the stable regulatory and market framework, which may attract investments in the sector of electricity and gas in the region and provide for long-term safety of supply with these energy items.

2. Legal framework of regulation of the electric power sector and electric power activities

Regulatory Commission for electricity of Republic of Srpska was acting in 2005 pursuant to the provisions of the Law on electricity of Republic of Srpska as well as the accompanying secondary legislation as follows:

- Decision on appointment of the president and members of the Regulatory Commission for electricity of Republic of Srpska ("Official Gazette of Republic of Srpska" 90/03 and 93/03),
- Statute of the Regulatory Commission for electricity of Republic of Srpska ("Official Gazette of Republic of Srpska" number 41/04),
- Ethic code for members and staff of the Regulatory Commission for electricity of Republic of Srpska ("Official Gazette of Republic of Srpska" number 49/04),
- Rule on work, internal organization and job systematization of the Regulatory Commission for electricity of Republic of Srpska ("Official Gazette of Republic of Srpska" number 49/04)
- Procedural Rules ("Official Gazette of Republic of Srpska" number 96/04).
- Decision, number 01-1009/04 about the budget adoption of the Regulatory Commission for electricity of Republic of Srpska for 2005 made by the National Assembly of Republic of Srpska ("Official Gazette of Republic of Srpska" number 6/05)
- Decision on the regulatory fee for the companies dealing with generation, distribution and trade of electricity resulted from the approved budget for 2005 ("Official Gazette of Republic of Srpska" number 23/05)
- Rule book for issuance of licenses and permits ("Official Gazette of Republic of Srpska", number 52/05),

¹ Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Romania, Turkey, Serbia, Montenegro, Macedonia and UNMIK

- Decision on the amount of the one-off regulatory fee ("Official Gazette of Republic of Srpska", number 60/05),
- Rule book on tariff methodology and tariff proceeding ("Official Gazette of Republic of Srpska", number 61/05),
- Decision on content and form of template in the tariff proceeding ("Official Gazette of Republic of Srpska", number 65/05),
- Decision on initiating the first tariff proceeding ("Official Gazette of Republic of Srpska", number 65/05),
- Rule book on public hearings and settlement of disputes and complaints ("Official Gazette of Republic of Srpska", number 71/05).

3. Key activities

The activities performed by the Regulatory Commission were determined by the Law, Statute of the Regulator and secondary legislation which are made pursuant to the Law on electricity of Republic of Srpska.

Competences of the Regulator are:

- supervision and regulation of relationships between generation, distribution and buyers of electricity including traders of electricity,
- prescription of the methodology and criteria for determination of the price of electricity supply for non-eligible customers,
- determination of the tariff rates for distribution systems' licensees and tariff rates for non-eligible customers,
- issuance or revocation of the licenses for generation, distribution and trade of electricity,
- determination of general conditions for the electric energy delivery

Realizing its competences and carrying out its functions and pursuant to them, Regulator is also responsible to:

- improve effectiveness, reliability and cost-effectiveness for generation, distribution and exchange of electricity;
- improve the competitiveness;
- encourage effectiveness, cost-effectiveness and safety in the electricity consumption;
- regulate quality of services and tariffs and profitable prices taking into account the interests of customers and needs of companies for delivery of electricity;
- provide fairness in the electricity supply;
- provide transparent and non-discriminatory behavior at the electricity market;
- provide that the electric power activity on the territory of Republic of Srpska does not have an adverse impact on health, safety and protection of the environment;

- supervise effectiveness of mechanisms and procedures which provide system middle and long-term balance between consumption and delivery of electricity;
- create conditions for development of the electric power system (generation and distribution);
- make measures for prevention of misuse of the monopolistic behavior of the licensee issued by the Regulator;

In 2005, Regulator held 19 regular sessions and 28 internal meetings. In these regular sessions it was discussed and determined documents within regulatory competence pursuant to the law-prescribed authorizations, while at the internal meetings, it was discussed and adopted the documents of the organizational-administrative nature. In the following table, there are statistical data from the mentioned regular sessions and internal meetings.

Regular sessions	
Type of documents	number
Minutes of the sessions	19
Decisions adopted	14
Rulings adopted	24
Conclusions adopted	7
Press releases	6
Drafts adopted	3
Rule books adopted	3
Rationales adopted	1
Explanations adopted	1

Internal meetings	
Type of documents	number
Minutes of the meetings	30
Decisions adopted	39
Rulings adopted	7
Rule books adopted	1

Apart from the mentioned, in 2005, Regulatory Commission for electricity of Republic of Srpska held 38 public hearings and 4 working seminar of the consulting nature related to making general normative documents, determining prices of electricity in the first tariff proceeding and issuing the licenses for electric power activities. All proceedings led by Regulator are open for public and information about hearings in the proceedings led before Regulator is published in newspapers. Regulator intends, in the proceeding related to making rules and regulations within its competence, as well as in the proceedings led at the request of the companies dealing with electric power activities and beneficiaries of their services, to have the public fully and timely informed and according to the procedural rules it invites stakeholders and professionals to participate in the public hearings. In the following table, it is given the number of public hearings per types:

Type of public hearing	Rules and regulations	Issuance of licenses	Tariff proceeding	Total number of the hearings held
General public hearing	6	11	-	17
Technical hearing	4	-	-	4
Formal hearing	-	-	10	10
Preparatory hearing	-	-	8	8

3.1. Issuance of licenses

3.1.1 Rule book on issuance of licenses and permits

The Law prescribes the competence of the Regulator for issuance and revocation of licenses for electric power activities, for construction of the electric power structures and electric power permits.

Article 58 of the Law provides that all existing legal subjects within generation, distribution, supply and trade of electricity are obliged to submit an application for the license.

Having in mind that Regulator, pursuant to the Law, is in charge of issuance of the licenses for electric power activities, for construction of the electric power structures and electric power permits, it undertook in 2004 immediately after the legal establishment, all activities to develop and make necessary secondary legislation in order to receive and treat applications and decide on issuance of licenses for the electric power structures.

In order to provide rules and clear guidelines regarding issuance of licenses and permits for all facilities in the electric power sector in Republic of Srpska, Regulator made Rule book for issuance of licenses and permits in its 12th regular session which was held on 28 April 2005 ("Official Gazette of Republic of Srpska", number 52/05). Draft document was determined in December 2004 while its making was accompanied by the public hearing which lasted for several months, having 5 public hearings held (3 general public hearings and 2 technical public hearing).

Regulator issues the electric power permits for the electric power facilities intended for generation of electricity which capacity is above 10 MVA and voltage exceeding 20 kV, while for other structures the mentioned permits are issued by Distributor.

Criteria for making decision on issuance of licenses, license requirements and contents have been separately prescribed for each type of license and permit.

Pursuant to provisions of the Rule book, Regulator issued the following licenses and permits:

- license for generation of electricity in the hydro power plants, thermal power plants and other plants,
- license for distribution of electricity,
- license for supply of tariff customers with electricity,
- license for trade and supply of electricity on the territory of Bosnia and Herzegovina,
- license for construction of a new or large-scale reconstruction of the existing generation or distribution electric power capacity (facility),
- initial electric power permit for connection of distribution and generation electric power structures to the distribution network,
- permanent electric power permit for connection of the distribution and generation electric power structures to the distribution network

It was analyzed, in the Rule, the procedure related to issuance of licenses and permits, starting from the application filing along with accompanying documents, checking whether the application is complete, press releases about the

application, data checking, creation of the license draft and collection of the public comments until decision on issuance or revocation of license is made.

Rule book prescribes the content of the application for issuance of license while forms of application for all types of licenses and permits are its integral part.

3.1.3. Procedures related to issuance of licenses

Pursuant to the Rule book for issuance of licenses and permits, which became effective on 4 June 2005, the existing electric power companies were obliged to file an application for issuance of the initial license within 90 days from the effective date of this Rule book.

Applications for issuance of the initial license for realization of generation, distribution, supply of tariff customers and trade and supply on the territory of BiH, in accordance with the deadline defined by the Rule book on issuance of licenses and permits, were submitted to Regulator in September 2005 by 20 applicants. Having checked that these applications and their amendments made by the applicant are correct in a sense of its form and content, Regulator informed the public about their submission in order to encourage the public and all stakeholders to give comments.

In the 22nd regular session which was held on 18 November 2005, Regulator determined drafts of 19 initial licenses, while the procedure related to the issuance license was stopped for one license at the request of the applicant. The public and interveners were informed about the possibility to submit comments until 9 December 2005 on each license draft published at the website of Regulator, as well as about the possibility to take part in general hearings which are for that purpose organized in Visegrad, Pale, Bijeljina, Ugljevik, Doboj, Banja Luka, Mrkonjic Grad, Gacko and Trebinje. Upon completion of the public hearings on draft licenses and analyses of the comments received, and according to the foreseen Activity plan, Regular made, in its 25th regular session which was held on 27 December 2005, Decision on issuance eighteen initial licenses for electric power activities for the following electric power companies:

License type	Licensee
Initial license for generation of electricity	<ol style="list-style-type: none"> 1. "Hidroelektrane na Drini", a.d. Visegrad, 2. "Hidroelektrane na Vrbasu", a.d. Mrkonjic Grad, 3. "Hidroelektrane na Trebisnjici", a.d. Trebinje 4. "Rudnik i termoelektrana Ugljevik". a.d Ugljevik, 5. "Rudnik i termoelektrana Gacko", a.d. Gacko 6. "Elektrodistribucija" a.d. Pale 7. "Elektrobijeljina", a.d. Bijeljina
Initial license for distribution of electricity	<ol style="list-style-type: none"> 8. "Elektrodoboj", a.d. Doboj 9. "Elektrokrajina" a.d. Banja Luka

	10. "Elektrodistribucija", a.d. Pale 11. "Elektrobijeljina", a.d. Bijeljina 12. "Elektrohercegovina", a.d. Trebinje
Initial license for supply of tariff customers with electricity	13. "Elektrodoboj", a.d. Doboj 14. "Elektrokrajina", a.d. Banjaluka 15. "Elektrodistribucija", a.d. Pale 16. "Elektrobijeljina" a.d. Bijeljina 17. "Elektrohercegovina", a.d. Trebinje
Initial license for trade and supply of electricity on the territory of BiH	18. "Elektroprivreda Republike Srpske", a.d. Trebinje

The application for issuance of the license for trade and supply of electricity on the territory of BiH was filed by "Elektrobijeljina" a.d. Bijeljina in September 2005, and has not been solved so far. "Elektroprivreda Republike Srpske" a.d. Trebinje appeared as Intervener asking not to issue the licenses of this kind to legal entities within the system of holding company "Elektroprivreda Republike Srpske". Procedure continued in 2006.

Until the end of 2005, Regulator received one more application for issuance of the license for trade and supply, submitted by the "Energy Financing Team". Itd Trebinje. The license was issued in 2006.

Small HPP Strpci filed an application for issuance of the license for generation of electricity on 19 May 2005. The applicant is the owner, Petar Lalovic, registered as the physical person dealing with generation of electricity. The application was amended several times while processing because of lack of complete information. Procedure continued in 2006. Having submitted complete documents, it was confirmed that the applicant did meet requirement to enter the court register for generation of electricity, so the request was rejected.

REERS keeps the register of the licenses and permits issued, while it regularly updates the Sum overview of the licenses issued as well as the List of the received applications for issuance of licenses in an email form at its webpage.

3.2. Regulation of the electricity prices and electric power services

Regulator carries out the tasks related to regulation of the electricity price in Republic of Srpska. The aims of economic regulation in the electric power sector are based on improvement of the market principles pursuant to the Law based on the generally-accepted international standards in the area of electricity and it tends to promote gradual liberalization of the national electricity market whereby, the Law follows the principles of non-discrimination and equalization of persons and property.

The gradual approach in introduction of liberalization is firstly related to the generation function which will be the regulated activity with regulated prices in its first phase. The foundation of market institutions and development of market

mechanisms will enable introduction of competition in the electricity generation and the customers will be enabled to freely choose their supplier.

The Regulator is entitled by the Law to the following:

- supervision and regulation of relationships between generation, distribution and buyers of electricity, including traders of electricity (Art 23 of the Law),
- prescription of methodology and criteria for determination of prices of the electricity supply for non-eligible buyers (Art 23),
- determination of tariff rates for distribution systems' licensees and tariff rates for non-eligible buyers (Art 23),
- determination of the price structure and total price of electricity at the plant threshold and separately for the price of distribution of electricity (Art 115),
- Pursuant to Article 30 of the Law, Regulator makes tariff system for the electric energy selling.

3.2.1. Rule book on tariff methodology and tariff proceeding

Draft Rule on tariff methodology and tariff proceeding with an accompanying set of documents was discussed and determined by Regulator in its sixth regular session which was held on 24 December 2004. For the purposes of better understanding of the tariff methodology and to encourage the public to give their comments, Regulator also prepared the document entitled Concept of tariff methodology which was presented to the public in a set of documents accompanying Draft.

Among several approaches in creation of methodology providing determination of revenue requirement for the regulated companies, the proposed initial tariff methodology calculates total revenues, i.e. revenue requirement using the regulatory base of assets and justified costs of operation. Methodology of the regulatory base for determination of the revenue requirement was combined using the marginal costs to create tariffs.

Making this Rule was preceded by two general hearings: one in Istocno Sarajevo on 2 February 2005 and one in Banja Luka on 9 February 2005. REERS also held two technical hearings in Banja Luka on 26 January 2005 and in Trebinje on 28 January 2005 whereby experts from the electric power sector were invited to participate and the comments received were carefully analyzed.

Since the comments and proposals, which were received during the public hearing, required more considerable amendments of the Rule, REERS made, taking into account the public opinion and according to the Article 42 of Procedural rules, revised draft of this Rule which was adopted at the 14th regular session which was held on 19 May 2005. Stakeholders might have submitted written comments to the revised draft Rule from the date the information was published until the deadline for submission of comments, 1 June 2005, expired.

Rule on tariff methodology and tariff proceeding was adopted by REERS in the 15th regular session which was held on 3 June 2005 ("Official Gazette of Republic of Srpska", number 61/05), which formally enabled regulation of prices and approval of tariffs for electricity in Republic of Srpska pursuant to the adopted legal principles.

Rule on tariff methodology and tariff proceeding determines the process based on which tariffs in Republic of Srpska are determined, basic assumptions of the tariff system: tariff elements, categories of consumption and groups of customers as well as the way for determination of prices and tariff rates. Application of the methodology ensures that the approved tariffs are transparent, non-discriminatory and based on justified costs of operation and maintenance, to encourage energy efficiency, create stable relationships at the electricity market, encourage development of the regulated activity, respect protection of environment and reflect the standards which are common in the international practice.

Regulator is entitled and obliged to check its tariff methodology and harmonize it with changes occurred in the electric power sector in the market opening process.

The tariff proceeding rules provide the bases of proceeding for the application consideration for approval of prices and tariffs, filing an application by the regulated companies or at REERS initiative.

3.2.2. The first tariff proceeding

Decision on initiating the first tariff proceeding, as well as Decision on content and form of the template in the tariff proceeding were made at the 16th regular session on 21 June 2005 ("Official Gazette of Republic of Srpska", number 65/05). Adopting these two documents, it was actually initiated the first tariff proceeding for approval of prices and tariffs which shall be applicable in 2006; deadlines for submission of applications by the regulated companies dealing with electric power activity were defined as well as the form and contents of the application template and prescribed data and documents accompanying the application.

Decision on initiating the first tariff proceeding by REERS enabled the regulated companies to file an application for approval of tariffs and prices for 2006; concurrently it was determined the timetable for submission of applications depending on the activity:

- applications for the price approval at the plant outlet for generation companies were submitted until 15 August 2005,
- applications for the tariffs approval to use distribution systems were submitted by distribution companies until 15 September 2005

- applications for the price approval for supply of non-eligible (tariff customers) were submitted by the companies for supply of tariff customers (distribution) until 10 November 2005

Some companies filed an application even a month later than the established deadlines. Acting according to the Rule book on tariff methodology and tariff proceeding, the professional sectors of REERS checked the applications which were filed in a sense of form and content; the applicants were asked to amend application in the information on failures of the submitted applications for approval of prices and tariffs for generation, distribution and supply of electricity.

REERS kept its right of estimate, according to the Rule on tariff methodology and tariff proceeding, for the documents, data and information which were asked but not received.

The application for the price approval at the plant outlet was filed by seven regulated companies (JP "Hidroelektrane na Trebisnjici", a.d. Trebinje, "Hidroelektrane na Drini", a.d. Visegrad, "Hidroelektrane na Vrbasu", a.d. Mrkonjic Grad, "Elektrodistribucija" a.d. Pale, EDP "Elektro-Bijeljina" a.d. Bijeljina, "Rudnik and termoelektrana Ugljevik", a.d. Ugljevik, JP "Rudnik i termoelektrana Gacko", a.d. Gacko).

Application for approval of tariffs for distribution system users were submitted by five regulated companies (EDP "Elektrobijeljina" a.d. Bijeljina, "Elektrodistribucija" a.d. Pale, AD "Elektrodoboj" Doboj, "Elektrokrajina" a.d. Banjaluka, "Elektrohercegovina", a.d. Trebinje).

Application for approval of tariff rates for sale of electricity to non-eligible (tariff) customers were submitted by five regulated companies (EDP "Elektro-Bijeljina" a.d. Bijeljina, "Elektrodistribucija" a.d. Pale, AD "Elektrodoboj" Doboj, "Elektrokrajina" a.d. Banja Luka, "Elektrohercegovina" a.d. Trebinje).

The formal hearing procedure for approval of tariffs started making Decision on holding formal hearings for the price approval at the plant outlet at the 19th regular session of Regulator which was held on 21 September 2005 ("Official Gazette of Republic of Srpska", number 87/05). Press release on formal hearing holding, with summary of applications, criteria to get a status of intervener, as well as the methods for submission of the public comments was published in newspapers on 23 September 2005 and at the website of Regulator. Determining the price at the plant outlet, it was held 7 preparatory hearings and 8 formal public hearings (with each applicant separately and one consolidated hearing) whereby the participants to the proceeding presented evidences and gave their testimonies on some issues related to determination of prices.

Decision on holding formal hearings in the proceedings related to approval of tariff rates for distribution system users was made in the 21st regular session which was held on 16 November 2005 ("Official Gazette of Republic of Srpska"

number 105/05). For the purposes of solving issues which are the same for all 5 submitted applications, but are primarily related to allocation of costs of the distribution system for tariff elements, categories of consumption and groups of customers, Regulator consolidated applications in this proceeding and held a formal hearing on 1 December 2005 (and two preparatory hearings). Press release on formal hearing with summary of applications, criteria for getting a status of intervener and method of submission of public comments were published in newspapers on 30 November 2005 and at the webpage of REERS.

Decision on holding formal hearings in the proceedings for approval of tariff rates for supply of non-eligible (tariff) customers was made on 13 December 2005 at its 23rd regular session ("Official Gazette of Republic of Srpska" number 114/05) while the formal hearing with participants to the proceeding was held on 26 December 2005. The public was informed with the contents of applications of the electric power companies through the information published in the daily newspapers on 26 December and at website of REERS which enabled all stakeholders to timely address their comments.

Apart from REERS staff all these hearings were attended by the authorized representatives of applicants and interveners as active parties to the proceeding. Regulator approved the status of intervener to the company of "Elektroprivreda Republike Srpske" a.d. Trebinje which submitted an application for participation in all tariff proceedings as intervener.

There were no other interveners in the formal hearings of the first tariff proceeding.

3.3. Public hearings and settlement of disputes and complaints

3.3.1 Rule book on public hearings and settlement of disputes and complaints

Within the competences of the Regulator, pursuant to Article 27 of the Law, it is to make the rules and procedures and accordingly to resolve disputes between the participants at the electricity market of Republic of Srpska. Regulator determines costs of disputes between the participants and its decision is binding for the parties to the dispute. It resolves the disputes regarding:

- right for the electricity supply,
- right for the access to the distribution network,
- obligation to deliver electric energy,
- tariffs at which the electricity will be delivered,
- interruptions in the electricity supply,
- denial of the electric energy delivery,
- quality of the electricity supply;

The electric energy generator, i.e. eligible buyer of electricity, who is denied the access to the network or is not satisfied with the access conditions, can lodge a complaint to the Regulator. The valid regulations define basic conditions under

which one can be denied the access to the network which are mostly related to restriction of technical or operational possibilities.

Apart from the above mentioned Regulator makes decisions on complaints related to resolving applications for getting the electric power permit for connection of end users to the distribution network.

Pursuant to Article 27 paragraph 1 of the Law and Article 51 paragraph 7 of the Procedural rules of the Regulatory Commission for electricity of Republic of Srpska, REERS is obliged to make Rule book on public hearing and settlement of disputes and complaints which provide rules and procedures and accordingly conduct hearings and settle disputes and complaints between participants at the electricity market.

In 2005, Regulator developed and passed Rule book on public hearings and settlement of disputes and complaints. The basic reason for making this Rule is to define the procedure of conducting all kinds of public hearings and the way Regular shall act on the application filed by the party for settlement of disputes mentioned in Article 28 of the Law and complaints in those cases envisaged by the Law.

This Rule provides rules and procedures and accordingly is proceedings conducted and disputes and complaints settled between participants at the electricity market.

The aim of making Rule is to determine and provide transparent, effective and cost-effective public hearing procedure while making rules and regulations, settlement of disputes and complaints and make as better proposal of the general document as possible and justified decision.

This Rule determines type of public hearings (general, technical and formal) and the way the hearing is conducted when Regulator decides to conduct it.

Common characteristic of these hearings is their transparency, i.e. the public is allowed to attend each of them. The public is informed about each hearing in some newspapers, summarizing the issues that are to be considered.

Draft of this document was determined in the 7th regular session which was held on 12 January 2005. Press release for collection of comments and public hearing holding is timely published in newspapers.

REERS held one general hearing in Bijeljina on 1 February 2005 and one technical hearing in Banja Luka on 9 February 2005 which were attended by the invited experts within the area of legal matters.

Having conducted the public hearing procedure, analyses and comments summarizing collected in the period of public consideration of the draft Rule, REERS adopted the Rule on public hearing and settlement of disputes and complaints in its 17th regular session which was held on 1 July 2007 ("Official Gazette of Republic of Srpska", number 71/05).

3.3.2 Settlement of disputes

In 2005, Regulator received and solved 11 objections of end users which are mostly related to termination of delivery of electricity due to non-payment, calculation of consumption, quality of service and connections.

Introducing regulation to this area, it is encouraged the policy of active protection of customers and communication between different participants at the electricity market was established at the electricity market, particularly between end users and Regulator.

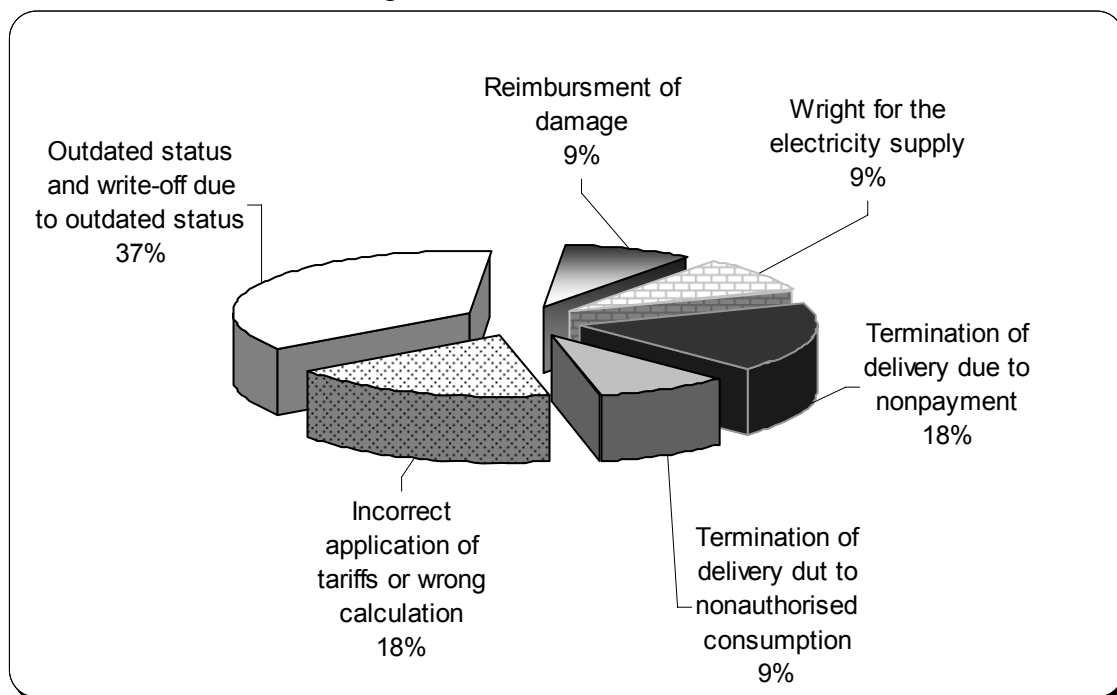


Figure 1: Structure of the solved objections in 2005

3.4 Protection of customers

Pursuant to the Law on electricity, the method of work of the Regulator related to protection of consumers and electric power structures is firstly directed to realization of his competences regarding:

- regulation of quality of the service, tariffs and profitable prices taking into account interests of the buyers and needs of the companies for delivery of electricity;
- provision of transparent and non-discriminatory behavior at the electricity market;
- making measures for prevention of misuse of the monopolistic behavior of the licensees issued by Regulator;
- participation in reaching agreement between buyers and suppliers of electricity;
- provision of other indirect aims of protection of customers while prescribing conditions for usage of licenses to perform certain electric power activities;

3.5 General conditions for delivery and supply of electricity

Pursuant to Article 23 and 30 of the Law, Regulator is obliged to make general conditions for delivery of electricity. According to the Activity plan for 2005, activities related to creation of the draft General conditions for delivery and supply of electricity in Republic of Srpska started in April 2005. The first working version of this document was made in August 2005.

The aim of making these General conditions is to improve the effectiveness, safety and fairness in delivery and supply of electricity, as well as provision of transparent and non-discriminatory behavior of the structures in the electric power sector.

General conditions for delivery and supply of electricity provide that supply and delivery of electricity, connection of structures of end users and generators to the distribution network in Republic of Srpska as well as other relationships between end users, licensee for distribution of electricity, licensee for supply of tariff customers with electricity, licensee for trade and supply of electricity and licensee for generation of electricity which structures are connected to the distribution network, in particular:

- Conditions and way for connection of structures owned by end users or generators to the distribution network, including:
 - issuance of electric power permits,
 - submission of application for connection, criteria and conditions for connection of structures owned by end user or generator to the electric power network and
 - method and deadlines to conclude contract on connection to the electric power network, contract on access to the network and contract on supply with electricity,
- quality of delivery and supply of electricity,
- the way on which the consumed electricity is metered, read, invoiced and charged,
- requirements related to accuracy of the metering devices,
- conditions, way, measures and timetable of terminations of delivery of electricity, in case of general shortage of electricity,
- conditions and way under which delivery of electricity to end user may be terminated,
- the way of informing end users in case of termination and limitation in delivery of electricity,
- conditions under which delivery of electricity is not terminated to users, including the cases when the consumed electricity is not paid as well as way mutual obligations in such cases are regulated,
- measures undertaken in case of damages in the electric power system as well as protection measures of the electric power system against excessive consumption,

- the way of determination of quantity and capacity of the electricity which is not legally consumed, as well as the way of invoicing and charging those quantities of electricity,
- conditions and way for connection of the site and temporary structures

3.6 Market opening

One of the basic aims of the market opening is to enable equal, transparent and impartial conditions for supplies of electricity to supply the buyers and vice versa, the right of buyers to choose the supplier. In Article 1 of the Law, it was prescribed that it "tends to promote gradual liberalization of the national electricity market", following the non-discriminatory principles and equality of persons and property.

Bosnia and Herzegovina is included in the Athens process which members are countries of the South East Europe, European Union and European Commission-joined countries, for the purposes of the electricity market opening pursuant to principles and standards which are applicable in the European Union, and which were determined by the European Union directives on electricity market, protection of environment, competition and renewable energy. Within that framework, "generally accepted international standards within electricity sphere" based on which Law on electricity is founded.

Monopolistic activities, such as control of transmission and distribution network and provision of ancillary services for the effective operation of the electric power system are the subject of full regulation of the respective body. Generation of electricity as well as trade and supply of end users with electricity have been gradually liberalized by introducing market mechanisms.

Introduction of competition at the electricity market of BiH and liberalization of that reform require preparation and adoption of some secondary legislation by some regulatory bodies in BiH.

SERC and entity regulatory commission have coordinated commencement of activities related to creation of regulations which shall enable initial opening of the electricity market in Bosnia and Herzegovina end of 2005, and are related to preparation to regulations on volume, requirements and timetable of the market opening, as well as draft rule book for getting a status of eligible customer of electricity and non-discriminatory enabling access to the network for third parties. Public hearing and adoption of the mentioned documents shall take place in 2006, which also means beginning of the realization of all obligations of BiH, after signing the Energy Community Treaty.

Beginning of establishment of the competitive market for customers with the annual consumption of electricity exceeding 10 GWh is foreseen for January 1, 2007. After that, small industrial and commercial customers should be entitled

to choose supplier and all customers end of 2015, including end users from the category of household.

Starting from the framework prescribed by the Law, and pursuant to commitments of Bosnia and Herzegovina under circumstances of gradual establishment of the energy market of the South East Europe, for the purposes of its integration in the European market, Regulator shall prescribe criteria and conditions for getting a status of eligible customer which shall be adopted in 2006. Market opening dynamics are determined according to realization of key assumptions, which are, apart from establishment of the system operator and issuance of licenses for trade and supply, making of market rules, grid tariffs and tariffs for ancillary services, following the guidelines and deadlines from the adopted and signed documents within the process of establishment of the Energy Community for South East Europe.

Regulator considers rules on status of eligible customer that shall enable gradual changes in trade and supply of electricity, in order that the wholesale market opening and right of switch do not have an adverse effect on safety of supply of end users of electricity in Republic of Srpska in the transitional period until it is defined and established electricity market in Bosnia and Herzegovina.

3.7. Renewable sources of energy

The whole process which was initiated by the Athens Memorandum on Understanding signing about the regional electricity market in the Southeastern Europe as well as the activities related to creation of the Energy Community of the Southeastern Europe which followed, represent significant guidelines which have impacts on development of the electric power system in Bosnia and Herzegovina and Republic of Srpska. The renewable sources of electricity play more and more significant role particularly in that surrounding because the mentioned documents affirm the Kyoto Protocol which was signed in 1997. That Protocol commits the countries signatories to take part in reduction of the carbon dioxide emissions in the atmosphere.

Most European countries have already committed themselves to put plans of significant usage of the renewable resources of energy into their strategies and to adapt the legislative framework in which those plans will apply. According to those initiatives, there was a Directive on promotion of electricity from renewable resources (2001/77/EC) made, which asks for increase of participation of the renewable resources in the electricity generation.

Bosnia and Herzegovina, signing the Energy Community Treaty committed itself to apply EU Directives on renewable energy sources (energy of wind, hydro energy, solar energy, biomass and waste, biogas, geothermal energy) and it should try to comply with Kyoto Protocol. Plan for implementation of Directive 2001/77/EK shall be submitted by Bosnia and Herzegovina to the European Commission within a year from the effective date of the Energy Community Treaty.

Usage of renewable resources was put in the Law on electricity of Republic of Srpska. It was prescribed by Article 30 of the Law that the Regulator was obliged to make subsidies for resources which use the waste or co-generation of heat-electricity while Article 37 determines that the company which in its single generation structure generates electricity using the waste or renewable sources of energy in a cost-effective way and pursuant to protection measures of environment, may get a status of eligible generator following the conditions prescribed by the Regulator.

In order to realize the mentioned legal guidelines, Regulator has initiated a range of activities related to development and making some secondary legislation on getting a status of the eligible generator which adoption is planned for 2006.

This document should prescribe terms and conditions for usage of the renewable energy sources, qualify the facilities which use the renewable energy sources, define individual rights and obligations of the participants at the energy market and determine the ways of providing incentives for generation from the renewable sources. Position of the eligible generator should enable benefits which stimulate capacity building, while subsidies and other types of incentives for usage of the renewable sources of energy according to the energy policy and EU Directives. REERS faced the fact that there was no Power policy in Republic of Srpska which may define mechanisms of the state incentives for the capacity building and usage of electricity from the renewable energy sources per priorities of certain sources and available technology.

European Union Directives prescribe that the countries members should establish indicative target values of shares of the renewable energy sources in total consumption of electricity, so that Regulator while making regulations related to this sphere, should rely on relevant elements of the energy policy.

REERS activities related to making rules on requirements for getting a status of eligible generator, regarding subsidies and other incentive mechanisms for renewable sources depend on formulated power policy of Republic of Srpska.

3.7.1. Rule book on getting a status of eligible generator

In order to determine and provide single requirements for getting a status of eligible generator of electricity, rapid, efficient and cost-effective procedure of submission and processing of application, making fair decision per the submitted application, Regulator planned creation of this Rule.

This Rule shall prescribe: criteria and conditions which generator has to meet in order to get a status of eligible (privileged) generator, types of eligible generators of electricity and their position, procedure for making Decision per application, contents of the application with necessary documents as well as the procedure, transfer and cancellation of status of eligible generator.

In 2005, it was made draft of this Rule, and there are activities related to finalizing draft rule in order to make it available for the public pursuant to the Regulator rules of work.

3.8. Cooperation

3.8.1. ERRA - Energy Regulators Regional Association

Energy Regulators Regional Association (ERRA) is an association of regulators of Central and East Europe, former Soviet Union Countries and Turkey based in Budapest. ERRA has 21 full members and 5 associated members. Aims of ERRA are improvement of regulating energy activities in the countries-members, encouragement of development of independent and stable regulators, improvement of cooperation between regulators, exchange of information, research work and experiences between members, better approach to information about the world experience in regulating energy activities.

State Regulatory Commission for electricity of BiH (SERC) has been a full member of ERRA since 19 May 2004. REERS plans, in the forthcoming period, for file an application for getting a status of the associate membership to this Association having in mind that full members can only be State Regulatory Commissions, according to the ERRA Statute.

Members and staff of Regulatory Commission for electricity of Republic of Srpska have been actively participating in the work of this association as well as in its permanent committees and working groups through the SERC. In the period from 10 to 13 April 2005, REERS representative took part in the ERRA Conference on Regional investment, held in Budapest.

3.8.2. ECSEE - Energy Community of the South-Eastern Europe

Establishment of the Energy Community of the South-Eastern Europe has firstly been initiated by the European Commission for the purposes of strengthening cooperation between the countries of this region within the energy field. This initiative should result in application of rules of the European Union in the South-Eastern European countries that has been in principle accepted by signing Memorandum on Understanding about the Regional Energy Market and its integration into the internal market of the European Community from 2002 and 2003 (the Athens Memorandum) by Bosnia and Herzegovina. Having signed these documents, there have been negotiations between the European Commission and the South-Eastern European countries regarding the Energy Community Treaty of the South-Eastern European countries. The Contract which was signed in Athens on 25 October 2005 enables establishment of the internal market for electricity and gas with effective participations of 34 parties: 25 countries-members of the European Union and Bosnia and Herzegovina, Croatia, Serbia, Montenegro, Albania, Macedonia, Romania, Bulgaria and UNMIK Kosovo.

The aim of this Contract is creation of stable regulatory and market framework which can attract investments in the electricity and gas sector in the region and provide long-term security of supply with these products.

Concluding the Contract, the countries-signatories commit themselves to establish the common electricity and gas market which will function applying the standards and rules of EU electricity market that it will integrate with. The contract established the dynamics of application of appropriate directives and regulations of EU taking care of particularities of some countries. It is achieved by gradual taking of parts of, so called *acquis communautaire* of EU regarding energy, protection of environment and renewable energy sources.



The work of Regulatory Commission for electricity of Republic of Srpska, within the process of establishment of the Energy community of the South-East Europe, was marked in 2005 with appropriate cooperation with the Ministry of Foreign Trade and Economic Affairs of BiH, then with appropriate participation in realization of different projects which function for the purposes of the Energy Community establishment.

Apart from the above mentioned, the members and staff of Regulator took part in the Athens Forum work. At the invitation of the Agency (Direkcija) for energy of the European Commission, in 2005, representatives of REERS participated in:

- 6th Athens Forum within the 5th Energy Week in Skopje from 8-11 June 2005
- Mini-Forum in Athens from 4-7 October 2005,
- 7th Athens Forum in Belgrade from 24-25 November 2005

3.8.3. Cooperation with other regulatory commissions

Regulatory Commission for electricity of Republic of Srpska in its past work realized successful cooperation with the State Regulatory Commission for

electricity (SERC) based in Tuzla and Regulatory Commission for electricity in Federation of Bosnia and Herzegovina based in Mostar (FERC). Apart from the common participation in trainings and workshops, all three commissions were harmonically cooperating on making rules and regulations within their competences. There were full cooperation and contacts between employees of the regulatory commissions who mutually exchange experiences and knowledge from some spheres of the regulatory work.

3.8.4. Participation in the work of trainings, conferences and workshops

Regulatory Commission for electricity of RS, in cooperation with USAID and Pierce Atwood organized a whole day-seminar on the subject "Prospects of the regulated company" which was held on 6 April 2005 in the hotel "Leotar" in Trebinje.

It was attended by representatives of JMDP Elektroprivreda RS and other power companies from Republic of Srpska and representatives of the State regulatory Commission.

REERS staff presented to participants of this seminar Power sector directives as well as obligations of REERS and power companies resulted from the Law on electricity.

USAID and Pierce Atwood provided participants of two eminent experts in this seminar from USA: Mr. Roger Kovack and Stan Graves who have great knowledge about the electric power sector and operation of the regulated companies which were while working in the fourth electric power company in the USA.

In 2005, it was realized considerable participation of members and staff of Regulator in seminars which were of educational nature. Seminars and trainings which were organized by the consulting company Pierce Atwood, and financed by USAID, were of great importance.

Knowing that REERS staff is expecting implementation of a range of formal hearings in the first tariff proceeding, in cooperation with the Consulting company Pierce Atwood - USAID, there was a training in Sarajevo on 12-13 October 2005, on the subject "Conduct of the formal hearing process".

For the needs of more professional education of REERS staff, it was organized by the same organization the training on the subject "Supervision and implementation" on 9-10 November 2005 in Tuzla. The expert from the Hungarian office for energy, Mr. Arpad Vajvodich presented his experiences in supervision of licenses issued for generation, transmission, distribution and supply of electricity. Special attention is given to legal framework for implementation of procedures of the Commission and establishment of internal procedures for supervision of the license requirements.

Apart from the above mentioned, representatives of REERS actively participated in the work of seminars related to the power sector:

- JUKO CIGRE seminar on Zlatibor,
- BiH Committee of CIGRE seminar in Neum from 26-29 September 2005

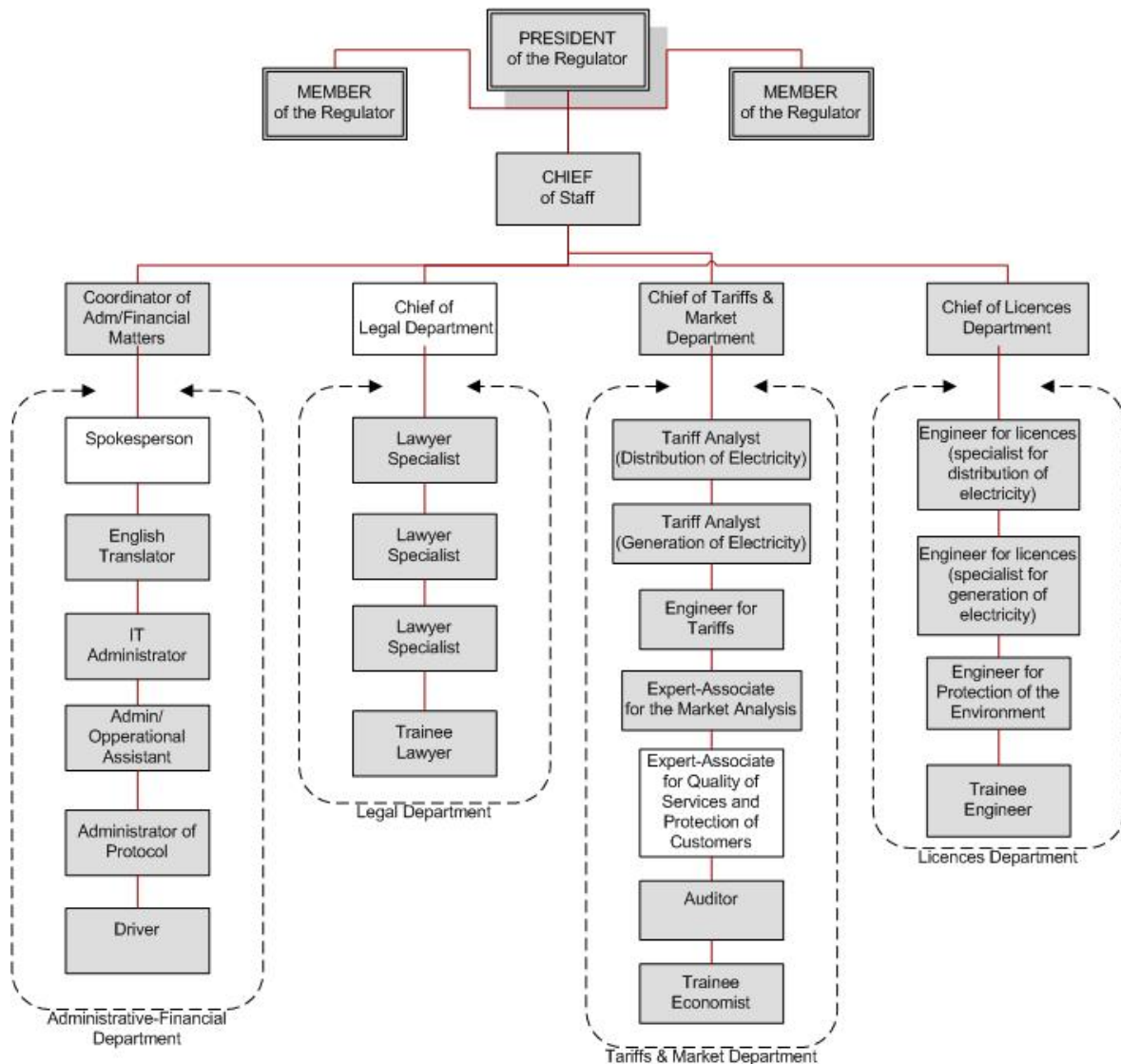
Participants to the training "Regulation of the electric power sector", in the Austrian agency for electricity E-control, Wien, organized by USAID Wordllearning in 2004, were delivered certificates for successfully completed training in Sarajevo on 29 October 2005 by USA Ambassador in BiH, Mr. Douglas McElhaney. This ceremony was also attended by Mr. Howard Sumka, director of the USAID mission in Bosnia and Herzegovina.

Regulator intends to, in the forthcoming period, follow the work of important seminars, conferences and trainings within the scope of the electric power regulation, because, in that way it contributes to improvement of the regulatory field rules and harmonizes in the process of the energy market liberalization, according to the general movements of the EU and region.

3.9. Staff, organization and transparency of the work

3.9.1 Staff and organization of the work of the Regulatory Commission

Regulatory Commission for electricity of Republic of Srpska has three members, one of which is the president. At the proposal of the Government of Republic of Srpska, the National Assembly of Republic of Srpska, in its ninth session, held on 9 October 2003 appointed the president, Mr. Milenko Cokorilo for the period of 5 years and two members of Regulator: Mr. Milan Baros for the period of 4 years and Mrs. Slobodanka Milasinovic for the period of 3 years. Decisions on appointment were published in the "Official Gazette of Republic of Srpska" number 90/03 dated 6 November 2003, and 93/03 dated 14 November 2003.



Picture 1. Organizational scheme

In 2005, Regulator made necessary staff amendments and employed 10 persons successively in 2005. Total number of employees is 26 including the Regulator members.

All employees in Regulator were employed in the procedure which was open for the public, having published the needs and prescribed conditions of the Regulator for employment. All employees in REERS meet the prescribed requirements.

3.9.2 Transparency of work of the Regulatory Commission

Pursuant to the Law, obligation of Regulator is to ensure transparency of work and provide transparent and non-discriminatory behavior at the electricity market. In order to be successful in implementation of duties which were assigned to it by the Law, Regulator initiated a range of activities to ensure transparency of its work which are realized through the transparency of its sessions for the public and media, publishing documents, information, decisions, resolutions, conclusions and

opinions at the official website (www.reers.ba) and in the Official Gazette of Republic of Srpska.

All sessions of the Regulator are open for the public and information about their holding is published on time.

Finally, transparency of the work is also reflected in timely reporting and publishing notices, documents and decisions in the mass media.

3.10. Financing of Regulatory Commission

3.10.1. Financing

The Law and Statute of Regulatory Commission for electricity of Republic of Srpska prescribes the financing from fees and taxes from the companies dealing with generation, distribution and trade of electricity, fees for licenses which are issued pursuant to the Law as well as donations from foreign governmental and non-governmental organizations.

Regulator determined the Budget for 2005 in the session which was held on 24 November 2004 while the National Assembly of Republic of Srpska adopted the budget of Regulatory Commission for electricity of Republic of Srpska for 2005 in the session which was held on 28 December 2004 with Decision number 01-1009-04. ("Official Gazette of Republic of Srpska", number 6/5 dated 22 January 2005).

Regulatory Commission made Decision on the regulatory fee for the companies dealing with generation, distribution and trade of electricity which resulted from the approved budget for 2005 in the 8th regular session which was held on 28 February 2005 ("Official Gazette of Republic of Srpska" number 23/05 dated 16 March 2005) and in the 15th regular session, it made Decision on the amount of the one-off regulatory fees ("Official Gazette of Republic of Srpska" number 60/05) which defined amounts of the stated fees and it was stated that the revenues based on them make the Regulator budget.

I EXPENDITURES		Adopted Budget 2005	Realization of the budget 2005	Percentage of realization (4/3)
1	2	3	4	5
A	CURRENT EXPENDITURES			
1.	Salaries and compensation of fees of staff			
1.1.	Gross salaries and compensations			
1.1.1	Net salaries and compensations			
1.1.2	Taxes and contributions on salaries and compensations			
2.	Costs of materials and services			
2.1.	Traveling costs			
2.2.	Energy costs			
2.3.	Costs of municipal services			
2.4.	Purchase of material			

2.5	Costs for services of transport and fuel			
2.6.	Rent of property and equipment			
2.7.	Costs of regular maintenance			
2.8	Costs of insurance and banking services			
2.9.	Contracted and other services			
B	CAPITAL EXPENDITURES			
1.	Purchase of equipment			
A+B	TOTAL EXPENDITURES			
	II REVENUES			
1.	Revenues from Elektroprivreda RS			
2.	Paid and non-spent means			
3.	One-off fees paid for applications			
3.	Other revenues			
	TOTAL REVENUES 2005			

In 2005, total expenditures in relation to the adopted budget were realized with 85.01%, including procurement of the fixed assets as well (capital expenditures).

Revenues were realized with 81.98% i.e. 1,061,239 BAM and are related to the regulatory fee from the licensed electric power structures within Elektroprivreda Republike Srpske in the amount of 1,013, 761 BAM, one-off regulatory fees based on the applications submitted by the regulated companies for issuance of licenses for activities in the amount of 40,000 BAM and revenues in the amount of 7,478 BAM.

Total amount approved by the budget for the regulatory fee was 1,294,500 BAM while it was paid 1,251,045 BAM in 2005. Paid but not spent means in the amount of 189,806 BAM were booked as pre-payment based on the regulatory fee for 2006 and licensees were reduced the obligation for that amount of money for 2006. The amount of 90,933 BAM which were planned by Budget but not paid in 2005 were not requested from Elektroprivreda Republike Srpske.

This analysis of the Budget realization for 2005 was adapted to the form based on which the Budget was adopted.

3.10.2.Audit report

The Statute of Regulatory Commission for electricity of Republic of Srpska provides that the annual audit of financial reports is compulsory.

Public invitation for selection of the independent auditor, pursuant to the Law on procurement of BiH was made on 6 March 2006.

Upon the conducted procedure on 11 April 2006, the independent auditor was selected - VRALAUDIT, ltd Banja Luka which, following the contracted dynamics

made an audit of financial report and submitted the report on 26 May 2006, from which we present the Balance sheet, Profit and Loss Statement and Audit opinion.

STATEMENT OF THE AUTHORIZED AUDITOR

We carried out the audit of Balance Sheet and Profit and Loss Statement for **"Regulatory Commission for electricity of Republic of Srpska", Trebinje** for the year ending on 31 December 2005. Members of the Regulatory Commission are responsible for the financial reports. Our responsibility is to according to the completed audit make our statement on the presented financial reports.

The audit was carried out pursuant to the Law on accounting, Rule book on audit of financial reports, Audit standards of Republic of Srpska and Ethic Code. These regulations require that the audit is planned and carried out in a way to make sure, in a reasonable manner, that the financial reports do not contain wrong information of material importance.

The audit includes testing of evidences, on the basis of random samples checking which support objectivity of information given in the financial reports. Audit also includes the estimate of applied accounting estimates made by the management of important estimations carried out by the management, as well as the general estimation of presentation of financial reports. We think that the audit, which we carried out, provides solid basis for our statement.

In our opinion, the enclosed financial reports objectively and truly regarding all important issues, present the state of property, capital and liabilities of Regulator on 31 December 2005 as well as the business results for the year ending that day, pursuant to the accounting standards and other regulations of Republic of Srpska.

Banja Luka, May 2006 године



БРАЛАУДИТ д.о.о.

Благојевић Зоран, дипл.инж
Овлашћени ревизор

PROFIT AND LOSS STATEMENT
for the period 31.12. 2004 - 31.12.2005

in BAM

Remark 31.12.2004 31.12.2005

REVENUES

-Assets from the
public revenues
-Revenues from contributions,
fees, donations, gifts and
assistance
Financial revenues

EXPENDITURES

Costs of the material
Costs of fuel and energy
Depreciation costs
Costs of salaries and contributions
Costs of generation services
Costs of non-generation services
Intangible costs
Costs of taxes

SURPLUS OF REVENUES - PROFIT

BALANCE SHEET

for the period 31.12.2004 - 31.12.2005

Remark 31.12.2004 31.12.2005

Assets
Cash and cash equivalents

TOTAL ASSETS

LIABILITIES

Non-allocated surplus of revenues - profit
Liabilities towards suppliers
Liabilities for salaries and taxes and
contributions on salaries
Paid means but not spent

Total liabilities **102.296**

3.11. Information system of REERS

Infrastructure of the information system of the Regulatory Commission for electricity of Republic of Srpska is based on the local computer network, servers, user working stations, network printers and appropriate accompanying equipment.

In August 2005, the information system was improved by enlargement of the existing computer network, procurement of the additional computer equipment and program packages. Regulator employees are enabled to carry out their activities efficiently no matter whether they are in the business premises of Regulator or far way which is often necessary due to the business nature.

Program packages which are in use are intended for realization of the standard office duties but also for fulfillment of the specific service requirements within the computer system (program packages for exchange of electronic mail, anti-virus server and client-based packages, etc). For all program packages requiring so, user licenses are regularly renewed. It is planned design and creation of the Regulator data base for 2007 which is meant by procurement of appropriate software as well.

Since transparency is the basic principle that the Regulator operation is based on, end of 2004 it was created Internet page of Regulator (www.reers.ba); since then all documents relevant for proper and full provision of information for the public have been regularly published.

All employees may be informed about basic rules of behavior in Internet and Internet surrounding, using internal guides, as well as about the way of keeping and filing electronic documents. This is also meant by the obliged confidential treatment of all input and output information which are considered a part of the Regulator information base.

B. REFORM OF THE ELECTRIC POWER SECTOR AND ELECTRICITY MARKET IN REPUBLIC OF SRPSKA

1. General remarks

The first important activity which related to the reform of the electric power sector in Bosnia and Herzegovina is preparation of the Statement on the electric power policy during 1999 and beginning 2000. The Statement was "a white book" i.e. guidelines of reform of the electric power sector in Republic of Srpska and BiH; it was prepared on the basis of the Study which was made by the English Consulting house "NERA". Proposal of the "Statement" was amended by certain amendments that were related to creation of the single transmission company in BiH, establishment of the regulatory body at BiH level for regulation of the transmission activity and obligation to offer the majority parcel in the privatization process of "Elektroprivreda". End of 2002 there was a Study on restructuring and privatization of the electric power sector in Republic of Srpska made based on which the Action plan for restructuring of the electric power sector in BiH for Republic of Srpska was made. The same year there was the Law on electricity and Law on Transmission, ISO and SERC passed and in that way there was a legal framework made for implementation of the reform of the electric power sector in RS.

2. Laws on electricity and application

The Law on electricity of RS, as the basic entity law for the electric power sector in Republic of Srpska regulates the activities of generation, distribution, supply and trade of electricity, including regulation of these activities through establishment of the Regulatory Commission for electricity of RS and defining its authorizations and competences.

Electric power transmission of electricity and control of the electric power system in BiH (System operator) and regulation of these activities were defined at BiH level by the Law on Transmission, ISO and SERC. Establishment of the company "Elektroprivreda Bosne i Hercegovine" and Independent System Operator of BiH were regulated by special laws (Law on establishment of the Transmission and Law on establishment of ISO).

Application of the Law which regulates functioning of the electric power sector in Republic of Srpska and BiH is slowed down by slow implementation of the Action plan for restructuring of the electric power sector in BiH for Republic of Srpska, while the Action plan for restructuring of the electric power sector in BiH for BiH Federation was adopted only in 2005.

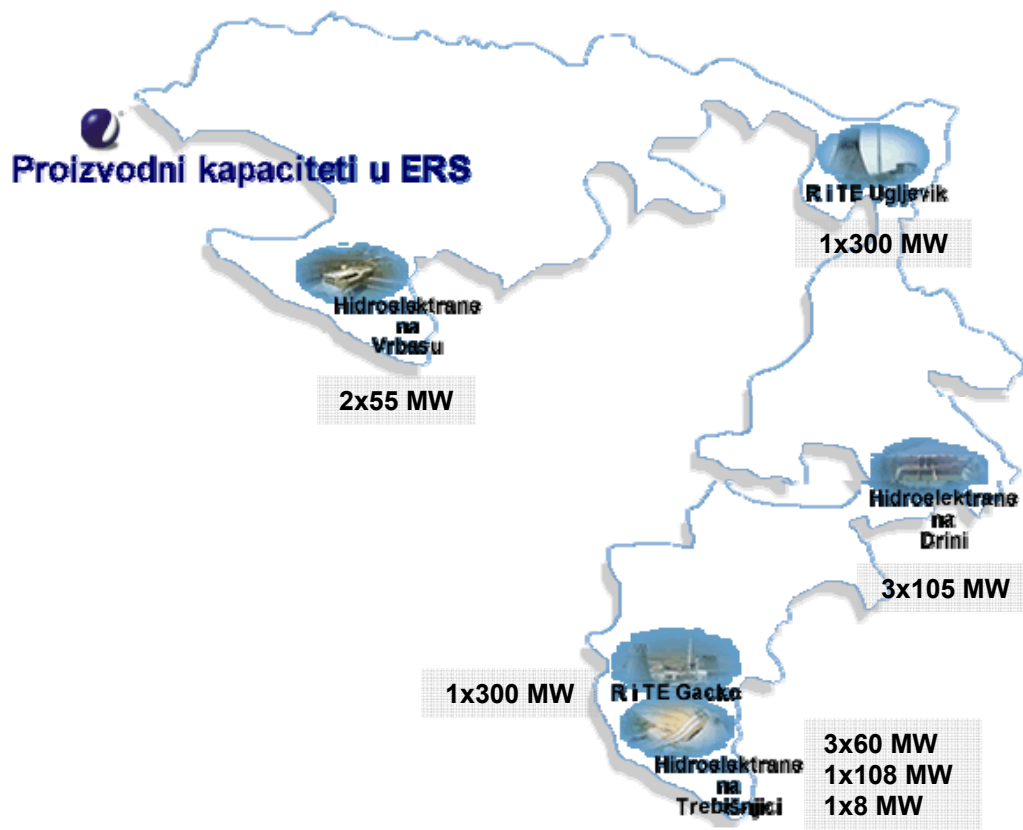
Inconsistency of some provisions of the Law on electricity, need for harmonization with other laws in Bosnia and Herzegovina as well as obligation of harmonization with provisions of the Energy community Treaty of South-Eastern Europe imposes the need for review of the Law on electricity of RS. The experience of the European countries in transition and EU countries show that changes of national energy legislations were needed after 3 to 6 years of application of the initial reform laws.

3. Electricity market and public services

Electric power activities can be done as public or market services. However, obligations of the energy subjects do not differ according to that criterion but according to the way prices are created (free or regulated).

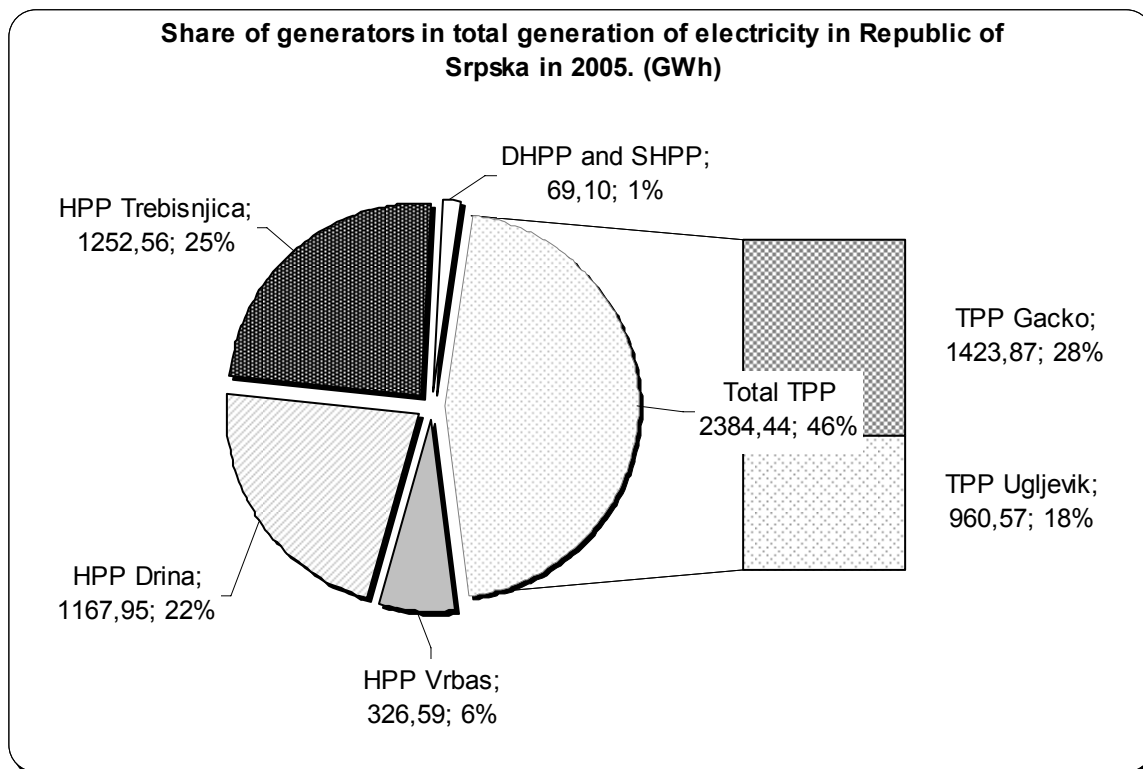
3.1. Generation of electricity

Generation of electricity, i.e. selling of the electricity generated is an activity which is carried out in the market competition. When the electricity market is open, the generation prices are completely "free" apart from some exceptions which are related to the renewable sources and co-generation and also in case of emergency. During the market opening process, generation prices are also regulated at the very beginning usually by the regulatory body. In Republic of Srpska, pursuant to Article 115 of the Law, Regulatory Commission for electricity determines the price of electricity at the outlet of each plant. Generation of electricity for tariff buyers is the public service obligation while generation of electricity for the eligible buyers in Republic of Srpska, BiH and in export, is the generation for the market.



Picture 2, Generation capacities in Republic of Srpska

Generation of electricity in Republic of Srpska is carried out in five generation companies and four small hydroelectric power plants within two distribution companies. The realized generation in 2005 was 5200,64 GWh. Picture number 2 presents generation capacities in RS, while Picture number 3 presents the structure of electricity in 2005.

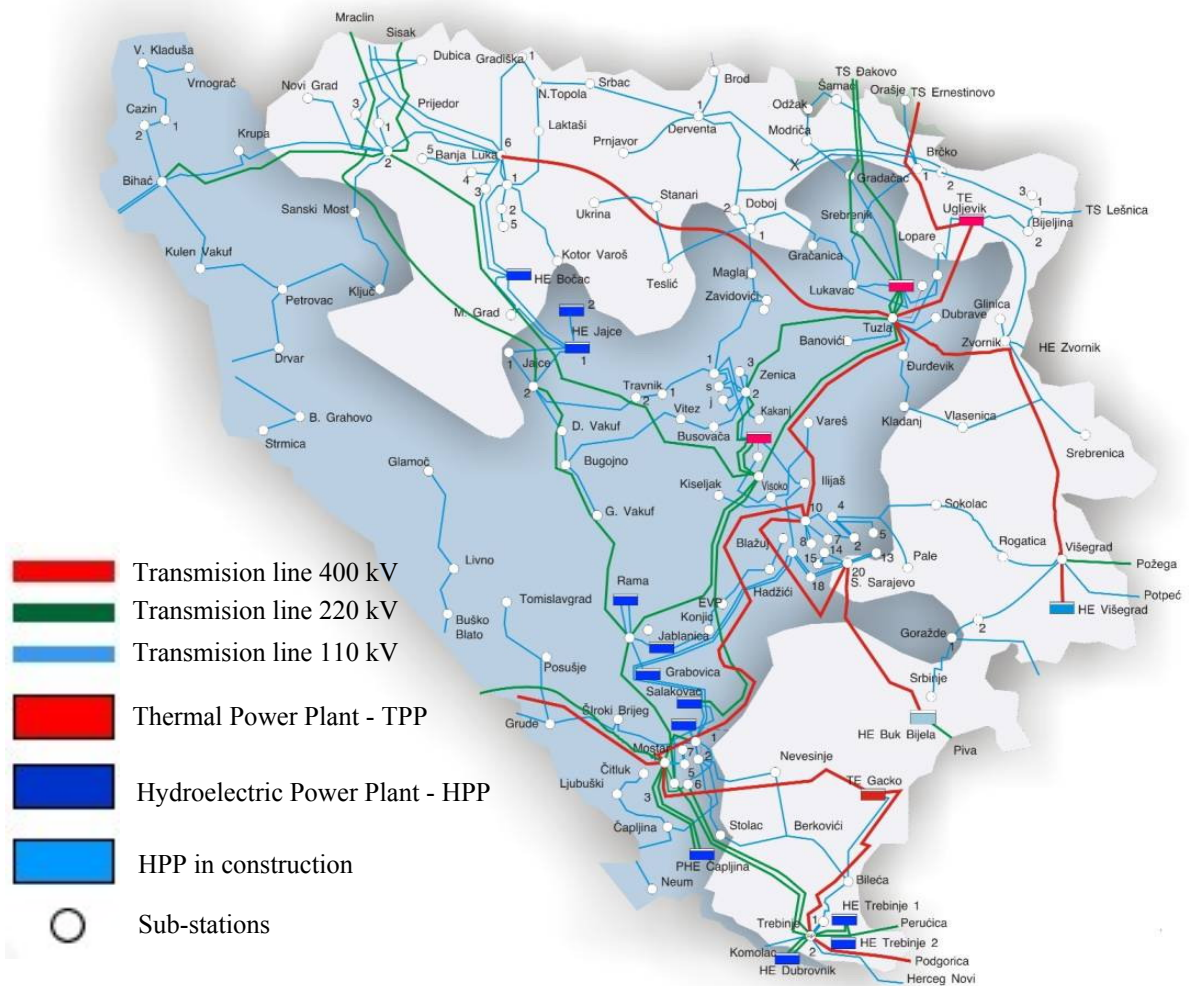


Picture 3, Structure of electricity generation in 2004

3.2. Transmission of electricity

Transmission of electricity is a monopolistic activity and that is why it has to be regulated in order to provide usage of the network for all users in equal and transparent way at regulated prices. It is of special importance that the transmission activity is separated from other electric power activities in special companies (managerial and legal unbundling) in order to provide impartiality in offering services. The transmission activity in Republic of Srpska was organized at the level of BiH within a special company "Elektroprenos Bosne i Hercegovine". Regulation of the transmission activity is within the competence of SERC.

Picture number 4 gives a map of the transmission network of Bosnia and Herzegovina. The network was considerably damaged during the war and it was divided in two parts one of which belonged to the First I synchronous UCTE zone (Federation BiH and a smaller part of Republic of Srpska) and another to the Second II synchronous zone (major part of Republic of Srpska), but it was completely reconstructed and joined again. Namely, from 10.10.2004 when reconnection of two synchronous zones (I synchronous zone which covered the West and Central Europe and II which covered the South-East Europe), the electric power network of Republic of Srpska has been an integral interconnection part of a big European UCTE network (UCTE - Union for coordination of transmission of electricity).



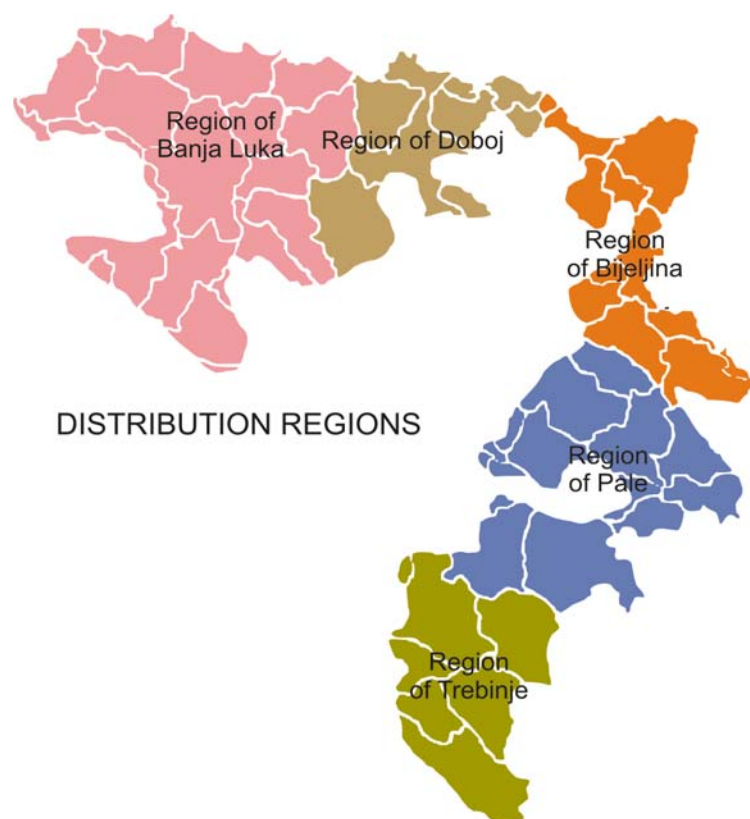
Picture 4, Transmission Network of Bosnia and Herzegovina

3.3 Distribution of electricity

Distribution of electricity is transmission of electricity at middle-voltage and low-voltage network for the purposes of delivery to end users and is, as it is the case with transmission at high-voltage network a monopolistic activity and being like that it should be regulated in order not to misuse the monopolistic behavior of distribution companies which possess capacities to perform these activities in certain area. When it is about unbundling of distribution activity from other commercial activities (generation and supply), it is also being imposed as the condition of impartiality in offering services, but the national legislation of European countries and EU legislation as a roof for its parties allows a lot of exceptions and time delay of the unbundling obligation of three years in relation to the transmission activity.

Distribution activity in RS is performed in five distribution companies (Picture number 5) within "Elektroprivreda RS" with franchising rights of delivery of electricity in certain geographic areas and it was regulated by the Regulatory Commission for electricity of RS. Tariffs for the distribution network use, which cover the distribution network costs and all transferred costs calculated for services at the transmission network, all end users connected to the distribution network are approved by REERS.

Distribution companies also perform the electricity supply for tariff buyers. Although the distribution and supply of electricity in Republic of Srpska are performed in the system of the public service obligation, it will be necessary to apply appropriate unbundling of these activities in case that they are performed within the same legal structure (in the beginning accounting and later on managerial-functional) in order to disable subsidizing between regulated and non-regulated activities.



Picture 5, Distribution Regions in Republic of Srpska

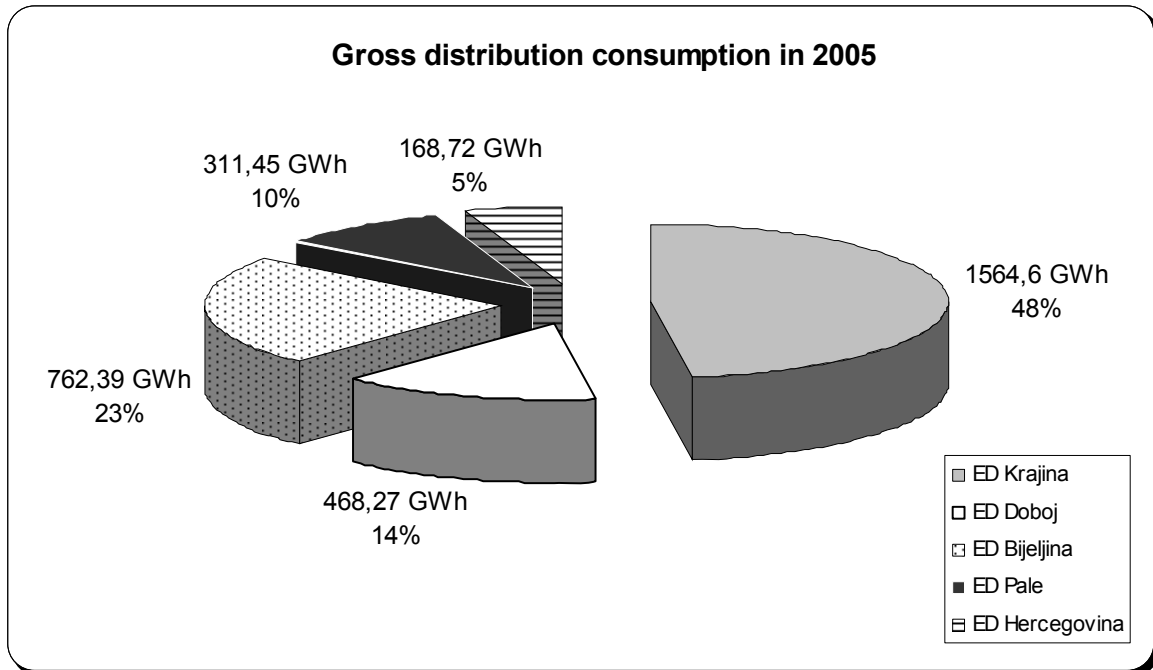
3.4 Supply of electricity

Supply of electricity is, in a principle, a commercial activity which is performed under circumstances of free competition when it is about the developed markets. Amount of transparency of some market is measured by freedom of buyer to choose its supplier of electricity.

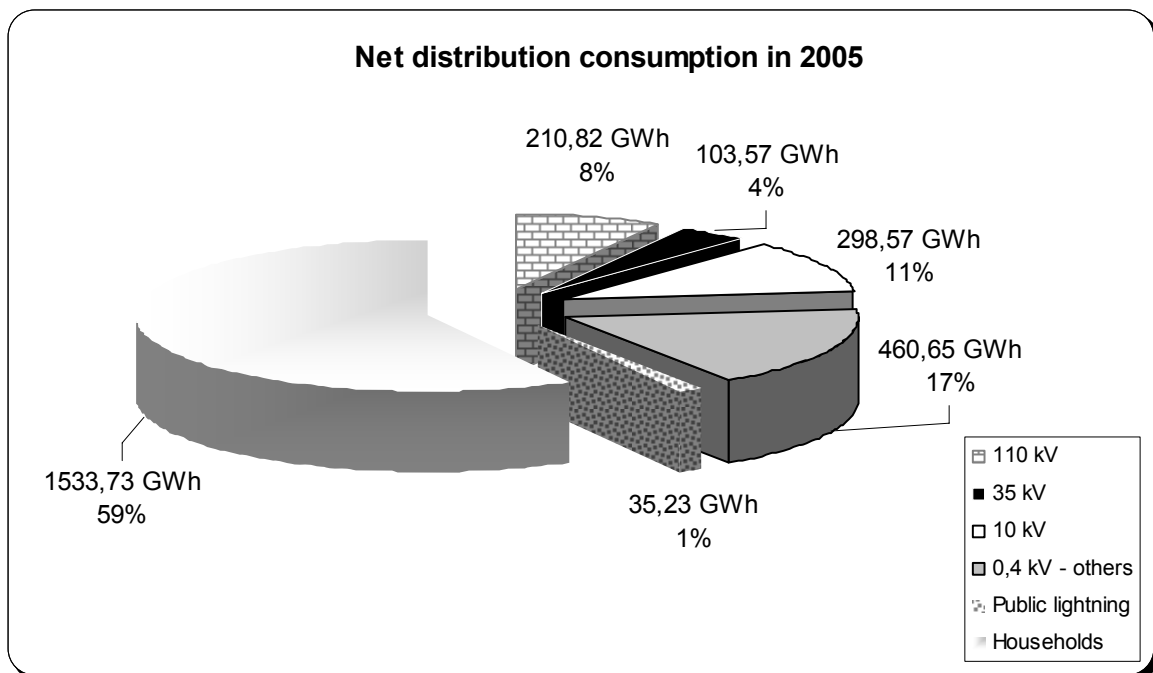
According to that principle, buyers are divided into two categories: eligible (free choice of supplier) and non-eligible (tariff) buyers. Supply of non-eligible (tariff) buyers in RS is a regulated activity, so that Regulatory Commission for electricity

in RS determines tariffs for sale of electricity to non-eligible (tariff) customers at which they are supplied by the supply licensee. Supply licensee of tariff buyers in certain tariff area should be, in the beginning, regional distribution company but, having in mind that it is about the same legal structure, it is obliged to make the accounting unbundling of the supply from the "classical" activity of distribution.

Picture number 6 presents gross distribution consumption at distribution companies (regions), while the picture number 7 presents the structure of total consumption of electricity in Republic of Srpska per categories of consumption (voltage levels and groups of buyers).



Picture 6, Gross Distribution Consumption of Electricity in 2005



Picture 7, Structure of Total Consumption in 2005

3.5. System operators

System operator is an electric power subject which is in charge of control of certain electric power system (offering and provision of system services). Transmission system operator (TSO) is often an integral part of the transmission company while distribution system operator (DSO) is as a rule within the distribution company. System services offering by the system operator should also be regulated and supervised, both regarding prices of its services and transparency and impartiality toward beneficiaries of its services. TSO obtains a part of the services from other electric power structures (ancillary services), usually under the market competition in a transparent way, while costs of the purchase of such services are transferred to its beneficiaries pursuant to already established and approved rules.

Function of the transmission system operator is, for Republic of Srpska, and for transmission as well, organized on the level of BiH within a special non-profitable company "Independent system operator for BiH" (ISO) which is regulated by SERC.

3.6. Dynamics of the market opening

Level of transparency of the electricity market is defined as a share of consumption of buyers who are free to choose the supplier, i.e. consumption of eligible buyers in the total consumption of all buyers. The threshold to get a status of eligible buyers in some countries has been defined in different ways: by the annual consumption, connection capacity or voltage levels of the connection.

The Law on electricity (Article 49) provides that all buyers of electricity in Republic of Srpska that have total consumption of more than 10 GWh may get a status of eligible buyer. Conditions and criteria for getting a status of eligible buyer are prescribed by Regulatory Commission for electricity of RS.

Activities related to the market opening are necessary to be harmonized on the level of Bosnia and Herzegovina, through direct cooperation of regulatory commissions, although these problems have not been completely regulated in both entity laws on electricity and Law on Transmission, ISO and SERC. Market opening implies making the opening plan, necessary rules and preparation of institutions in a way that the market can function in the single market area of Bosnia and Herzegovina and join the regional market of the South-Eastern Europe. The Energy community Treaty of the South-Eastern Europe signed, should be a binding document for countries-signatories to it, which means that its energy legislation has to be mutually harmonized both, regarding establishment of necessary market subjects and respect of deadlines for realization of conditions which are necessary for functioning of the fair electricity market in the region.

3.7. Safety of supply

Safety of supply is an issue which is getting more and more important with the market opening. It implies establishment of the institution of responsibility for safe supply and mechanisms to remove possible causes of insecurity in the network or unavailability of generation or purchase of electricity. In order to ensure satisfactory level of the supply safety, it is necessary to provide sufficient generation capacities, appropriate transmission and distribution system and

effective control. This issue can often be solved in a more effective way on the regional level, although so far, until the common solution is found, even EU countries determine their own procedures and make special measures in order to ensure safe supply of electricity.

3.7.1. Construction of generation facilities of electricity

In order to provide safety of supply it is necessary to define the procedure for construction of new generation capacities which means that the procedure and its implementation should comply with objective, clear and impartial, already publicly published criteria. This procedure is called the license issuance procedure for construction of generation capacities or the authorization procedure. Applicants for construction of the facility, in case that they do not get the license for construction have to be informed about reasons for the license denial. The applicant should also be enabled to lodge the complaint in case of denial of application for construction of the generation facility.

If sufficient generation facilities are not provided through the process of approval (authorization) for safe supply of buyers, i.e. if there isn't market interest for construction of new generation facilities, there might be invitation for bids open for construction of additional generation capacities which should be based on publicly published criteria.

Construction of generation facilities on the basis of renewable sources and for the concurrent generation of heat and electricity (co-generation) is additionally regulated.

3.7.2. Safety of the electric power system and electricity market

In order to ensure safety of an electric power system it is necessary to provide, at least the following activities:

- making and regular annual update of long-term estimates of the transmission network development by the system operator in cooperation with the transmission company;
- making and regular annual update of long-term estimate of the electricity market development;
- creation of appropriate estimates of supply safety for buyers of electricity on the basis of estimates of development of the market and transmission network, and submitted applications for issuance of approvals for construction of generation facilities;
- creation of plans of necessary measures to ensure necessary safety of the electric power system;

Safety of the electric power system in Republic of Srpska and Bosnia and Herzegovina, apart from the fact that the installed generation capacities go far beyond the need of electricity consumption for both energy and capacity and that the transmission network has been completely restructured to the extent which was before the war, was consistently resolved neither regarding legal and regulatory framework nor clear defining the procedures and institutional responsibility. Laws on concession, environmental laws and regulations, energy laws and other regulations require full harmonization in order to overcome possible

misunderstandings during the process of construction of new and reconstruction of existing electric power structures.

3.8 Prices of electricity in Republic of Srpska

The electricity prices in Republic of Srpska for 2005 were determined on the basis of Tariff system and tariff rates which were made by Government of Republic of Srpska in December 2004 pursuant to amendments of the Law on electricity. Apart from the fact that individual tariff rates were amended (unit prices of tariff elements for respective categories of consumption and groups of customers in certain daily and seasonal intervals, the tariff system was partly amended regarding the method of determination of the capacity charge for end users from the category of households.

The tariff system, which was applicable in 2005, has the following characteristics:

- prices of electricity are different for different categories of consumption and groups of buyers and they depend on the season and part of the day when the electricity is used;
- the basic division of buyers of electricity on categories of consumption on the basis of voltage level which the electricity is taken from accompanied with division on low voltage on the categories of household and other buyers (commercial structures i.e. companies, trade and others);
- winter season lasts from 01.10 to 31.03 and summer from 01.04 to 30.09;
- high season tariff (HT) is from 6 to 22 hours, i.e. in summer time from 7 to 23 hours; low season tariff (LT) is from 22 to 6 hours, i.e. in summer time from 23 to 7 hours. Low tariff comprises also days of weekend from Friday at 22(23) to Monday at 6(7) hours;
- Calculation elements which make the total price are: active energy, capacity charge and excessively taken reactive energy.

3.8.1. Households

Pursuant to the tariff system which was applicable in 2005, calculation of the electricity consumed by end users in the category of household was carried out in the following way:

- all households are calculated the active energy at middle tariff except households which have the calibrated two-tariff device and tariff switch clock inserted provided that they submitted the application for such calculation;
- Capacity for households is calculated in the following way: 1 kWh of capacity charge is calculated at each initiated 200 kWh of consumption of electricity, while 6KW of capacity charge is calculated for consumption of over 1000 kWh.

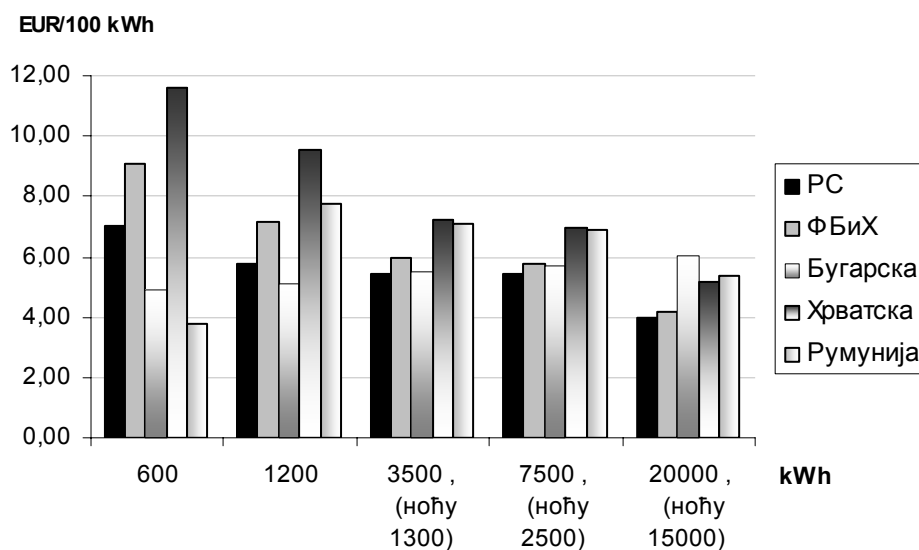
The following table presents the average prices of electricity in Republic of Srpska for users within the category of households, of certain consumption characteristics according to the EUROSTAT principles in 2005, along with the benchmarking values of three countries in the region (Bulgaria, Romania and

Croatia) which data were available in the EUROSTAT report and with data on the electricity prices for the same volume and structure of consumption in the Federation of Bosnia and Herzegovina.

Table 1 - Benchmarking prices of electricity for households in 2005

Annual consumption of energy in households	RS	FBIH	Bulgaria	Croatia	Romania
	(EUROSTAT 01.07.2005) without VAT Euro/100 kWh				
600 kWh	7,04	9,08	4,91	11,63	3,75
1200 kWh	5,76	7,16	5,11	9,58	7,74
3500 kWh, at night 1300 kWh	5,44	5,97	5,47	7,25	7,09
7500 kWh, at night 2500 kWh	5,41	5,74	5,73	6,98	6,91
20000 kWh, at night 15000 kWh	3,97	4,19	6,03	5,20	5,37

Graph 1 - Benchmarking prices of electricity for households in 2005



According to EUROSTAT data, electricity prices in 2005 in EU countries, including the countries candidates were increased for 4,6% for end users from the category of households.

Standard, i.e. referent customer from the category of consumption according to EUROSTAT methodology is an end user who consumes 3500 kWh of electricity annually.

Average customer from the category of household with one-tariff device in Republic of Srpska consumes 3,240 kWh, and with two-tariff device it is 5,050 kWh; out of which 2560 kWh at night (i.e. at low tariff), so the price at which

these customers used to pay electricity in 2005 was 5.62 EUR/100 kWh (one-tariff), i.e. 4.98 EUR/100 kWh (two-tariff).

3.8.2 Industrial and commercial customers

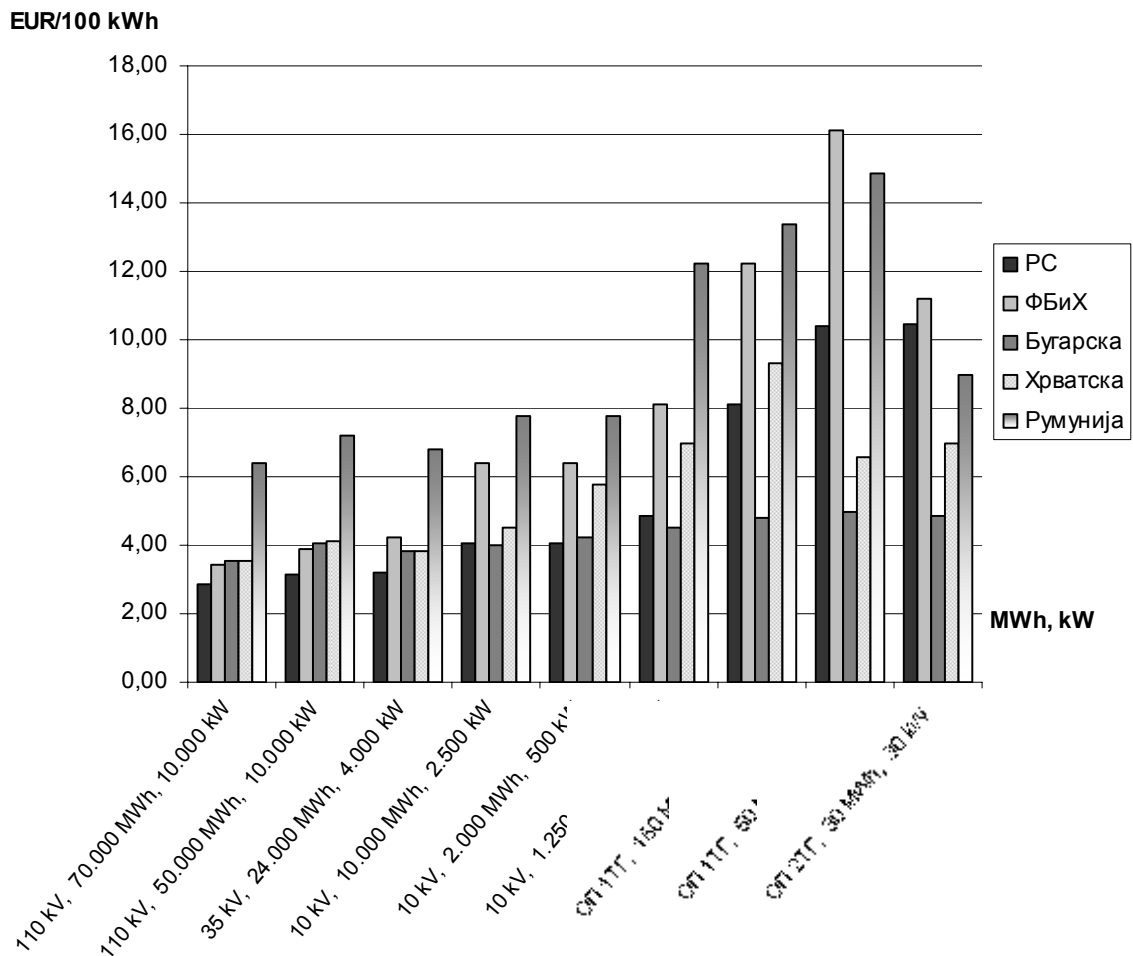
Prices of electricity for industrial and commercial customers, comparing to the countries in neighborhood, calculated per tariff rates which were applicable in 2005 in the average price of electricity for the end user of respective characteristics of consumption depending on volume and way of consumption of electricity, are given in the following table:

Table 2 - Benchmarking prices of electricity for industrial and commercial customers in 2005

Characteristics of consumption			RS	FBiH	Bulgaria	Croatia	Romania
Category of consumption ² (in RS)	Annually in MWh	Maximum capacity in kW	EUROSTAT (01.07.2005.) without VAT and tax				
			U EUR / 100 kWh				
110 kV	70000	10000	2,86	3,41	3,53	3,56	6,38
110 kV	50000	10000	3,14	3,90	4,04	4,10	7,18
110 kV - average customer ³	38057	5060	3,06				
35 kV	24000	4000	3,22	4,25	3,83	3,83	6,80
35 kV - average customer	4356	778	3,49				
10 kV	10000	2500	4,04	6,41	3,99	4,51	7,79
10 kV	2000	500	4,04	6,41	4,24	5,75	7,79
10 kV	1250	500	4,85	8,14	4,50	6,98	12,21
10 kV - average customer	751	195	4,38				
Groups of customers at low voltage:							
1 TG	160	100	8,09	12,22	4,81	9,30	13,36
1 TG	50	50	10,39	16,10	4,96	6,57	14,86
Average customer at 0.4 kV with capacity metered	127	39	6,10				
2 TG	30	30	10,43	11,20	4,86	6,98	9,00
Average customer at 0.4 kV without capacity metered	6,3	5	10,50				

² Categories of consumption are related to Republic of Srpska and Federation, while there are no categories of consumption stated in the EUROSTAT Report for other countries

³ Data on the annual consumption and maximum capacity of the average customer are related to Republic of Srpska and were taken from the regulated companies' reports in the proceeding for the tariff approval



Graph 2 - Benchmarking prices of electricity for industrial and commercial customers in 2005

According to the EUROSTAT data, prices of electricity in 2005 in the European Union countries, including the countries candidate, were increased for 15.5% for industrial customers in relation to the previous year.

APPENDIX 1

REFORM OF THE ELECTRIC POWER SECTOR IN THE EUROPEAN UNION

CURRENT SITUATION OF THE INTERNAL ENERGY MARKET IN THE EUROPEAN UNION - PROGRESS IN KEY AREAS AND FAILURES

1. Making regulations in the spirit of new Directives

Countries members were obliged to apply provisions of the Directives in the own legislation until 1 July 2004. However, until the end of 2005, it was not conducted complete harmonization of the state legislation with Directive provisions, not in formal but practical sense.

The basic subject of delay in application is related to the stipulated conditions and allowed exceptions for unbundling of the transmission and distribution system operators. Unbundling of distribution system operator from the supply has been neither harmonically and properly stipulated nor conducted in the whole Union.

2. Market integration

Directive 2003/54/EC on internal energy market aims at creation of the single European market with higher level of competition in the whole Union, and it shall reflect the competitive prices for the welfare of end users.

However, the level of integration is not satisfactory which is implied by two basic indicators of the market integration:

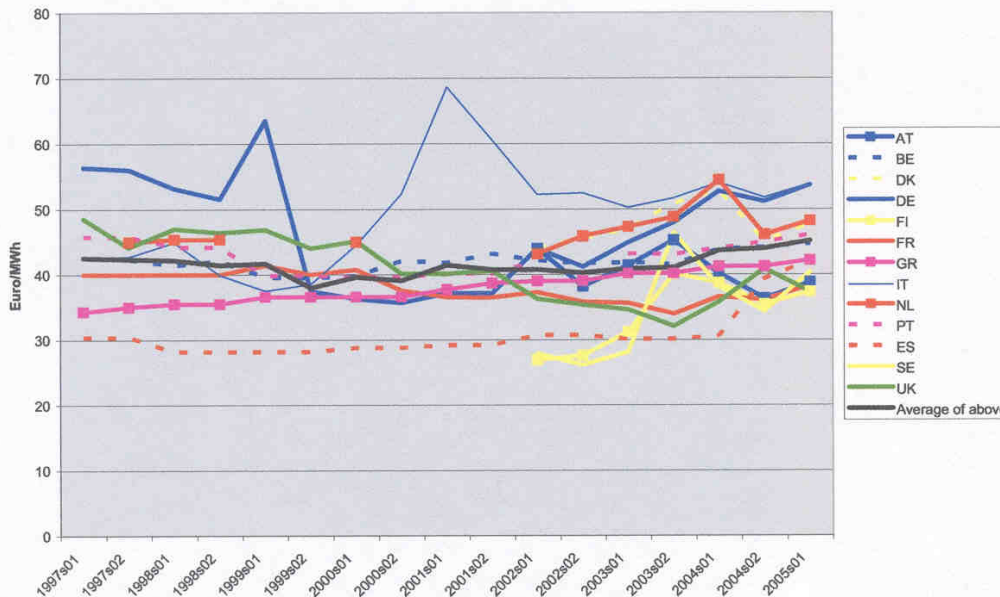
- considerable differences in the level of prices in the internal market
- low level of the cross-border trade

Main obstacles to establish the European electricity market are still:

- high level of concentration and a possibility of market domination, particularly at national markets which, from its side, opens a possibility for big players to manipulated with wholesale and balance prices
- insufficient integration of the national markets,
- major part of energy is still the subject of direct trading between generators and suppliers through the long-term fixed contracts, and only a small part at the organized wholesale market,
- non-harmonized approach to unbundling of electric power activities in the vertically integrated companies

Establishment of the liquid internal electricity market within the European Union is not supported by differences in the level of electricity price at some markets and limited capacities for the cross-border trading.

Differences in the electricity prices for industrial customers between countries members are up 100%, but it is also noticed the trend of gradual approaching of levels of the wholesale prices in neighboring countries, which can be found among Nordic countries, connected through Nordpool. These differences may be best noticed in the following examples:



Graph 1 - Retail prices for big industrial customers (up to 50 MW of peak capacity)

Source: European Commission with the EUROSTAT data

The price of electricity for industrial end users has had major changes in Germany, Ireland and Italy, while at the Union level it is established the trend of prices' approaching which goes within the range of 40 - 55 EUR/MWh.

For end users which are grouped in the category of middle industrial customers, differences in the level of prices are higher and they are from 60 - 80 EUR/MWh, but generally changes of the price levels are lower.

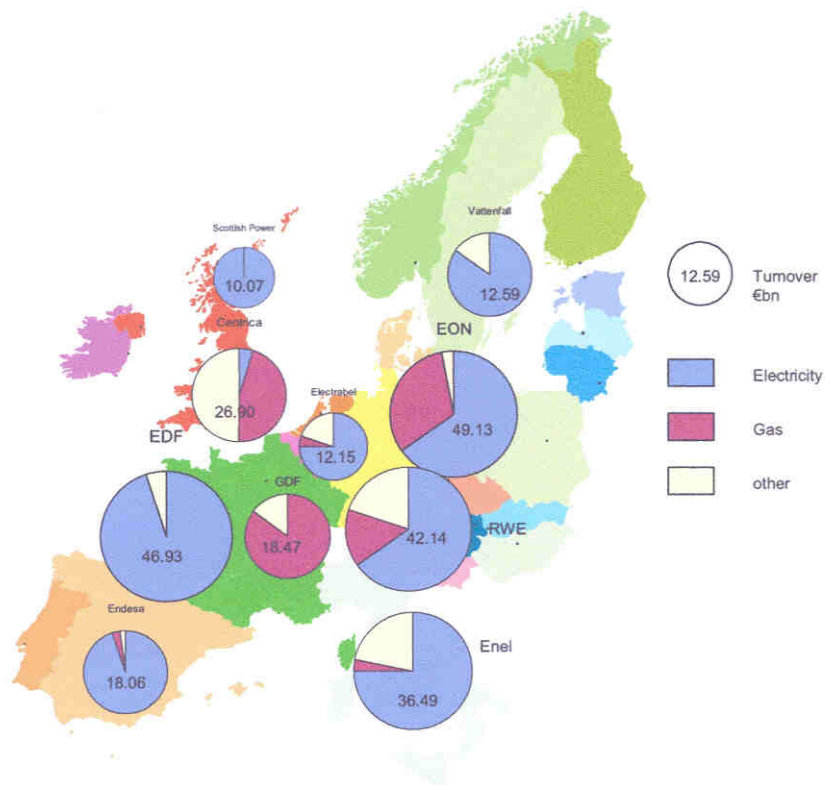
The biggest deviation in the level of the electricity prices between the EU countries is with small industrial and commercial customers, and the prices are from 60 - 150 EUR/MWh, the price statistics is made for groups of countries with high, middle and low prices.

3. Concentration and consolidation of the activity

Most EU countries started with the electricity market opening, where there was a monopolistic and oligopolistic market structure. Even though the Directive and

regulations harmonized with it, provided a legal framework for competition, it is not achieved to the preferred extent. The concentration still exists, but, apart from that, where is further consolidation (merging) of participants accompanied by the market opening.

The electricity market remained mainly national, although regional markets are being developed within the Union with a new market structure and competition at the level of regional market (e.g. Nordic market).



Picture 1: Structure of shares of major companies at the national markets

It is estimated that the fear is justified regarding market concentration at the wholesale market. Entry of new participants to the national markets make difficult and limit transmission capacities.

New participants at the national markets almost as a rule appear by the contract on taking or long-term contract with generator of electricity.

The number of real new participants who enter the national market started to decrease while the companies that the allocated the monopoly before the market opening (or they actually acted as monopoly) still have major share in the projects of construction of new plants.

Analysis of acquisitions in the energy field indicate that the number of the cross-border taking of companies is increasing, as well as increasing vertical integration in the activities of generation and supply.

Table 1 - Concentration at the wholesale national electricity markets

	Number of companies with 5% share in the total generation capacity	Share of 3 major generators in total generation	Liquidity - multiply spot trades/total consumption	Liquidity - multiply term trades/total consumption
Countries	Number of companies with 5% share in the total generation capacity	Share of 3 major generators in total generation	Liquidity - multiply spot trades/total consumption	Liquidity - multiply term trades/total consumption
Austrija	5	54%	3%	-
Belgija	2	95%	-	-
Danska	10	40%	42%	450%
Finska	10	40%	42%	450%
Francuska	1	96%	3%	-
Njemačka	5	72%	11%	64%
Grčka	1	97%	-	-
Irska	2	93%	-	-
Italija	5	65%	21%	-
Luksemburg	1	88%	4%	43%
Holandija	4	69%	12%	37%
Portugal	3	76%	-	16%
Španija	3	69%	92%	-
Švedska	10	40%	42%	450%
Velika Britanija	8	39%	6%	210%
Norveška	10	40%	42%	450%
Estonija	1	95%	-	-
Latvija	1	95%	-	-
Litvanija	3	92%	-	-
Pojska	7	45%	1%	44%
Republika Češka	1	76%	1%	206%
Slovačka	1	86%	-	-
Mađarska	7	66%	-	-
Slovenija	3	87%	2%	-

Source: data of EU Regulators

Remark:

1. Data for Sweden, Norway, Denmark and Finland are related to the whole Nordic market

Table 2 - Concentration at the retail national markets

Countries	Companies with more than 5% of the market share	Number of totally independent suppliers (without branches)	Market share of 3 major companies (big industrial customers)	Market share of 3 major companies (small and middle companies)	Market share of 3 major companies (small customers/ households)
Austrija	5	4	60%		
Belgija	3 / 2	14 / 6	100%/ 92%	100% / 99%	94% / 100%
Danska	-	3	-	-	-
Finska	5	< 5	-	35-40 %	
Francuska	1	5	91%	97%	96%
Njemačka	4	13	-	-	-
Grčka	1	10	97%	97%	100%
Irska	3	7	99%	99%	99%
Italija	6	119	33%	12%	93%
Luksemburg	4	4	94%		95%
Holandija	3	18	-	-	83%
Portugal	2	4	98%		
Španija	5	11	82%	86%	85%
Švedska	3	-	50%		
Velika Britanija	6	3	65%	66%	59%
Norveška	4	5	95%	33%	31%
Estonija	1	0	95%	95%	95%
Latvija	1	0			
Litvanija	3	5	100%	100%	100%
Poljska	6	20	50%	48%	47%
Republika	3	0	95%		
Slovačka	1	1	86%	100%	100%
Mađarska	7	0	7%	43%	51%
Slovenija	6	6	67%	75%	77%
Kipar	1	0	100%	100%	100%
Malta	1	0	100%	100%	100%

In order to prevent limit of the competition through integrations and misuse of dominant position, European Commission carefully examines the integration processes in the electric power activities, pursuant to regulations on competition.

4. Reaction of end users

Natural indicator of the efficient competition is a number of customers who change their supplier.

There is no doubt that big customers (mostly industrial ones) are more in favor to switch, while commercial customers and households that are entitled to, hesitate to use that right. There are more reasons for that. Very often the reason is the fact that the customer has no competitive bid, or the bids are so similar that they actually do not represent a real possibility of choice. When it is added dominant position of the previous monopolist and insufficient unbundling

of activities, particularly at the distribution level, end user considers often changes of supplier as a risky action.

Table 3 - Volume of consumption of electricity of customers who switched per groups of customers

Countries	Big customers	Small and middle industrial customers	Small companies and households
Austrija	29%	29%	4%
Belgija	oko 20%	10%	
Danska	>50%	oko 15%	
Finska	>50%	82%	30%
Francuska	15%		0%
Njemačka	41%	7%	5%
Grčka	2%	0%	0%
Irska	56%	15%	9%
Italija	60%		-
Luksemburg	25%	3%	0%
Holandija	-	-	11%
Portugal	16%		
Španija	25%	22%	19%
Švedska	>50%	-	29%
Velika Britanija	>50%	>50%	48%
Norveška	>50%	>50%	44%
Estonija	0%	0%	0%
Latvija	0%	0%	0%
Litvanija	15%	0%	0%
Poljska	19%	0%	0%
Češka Republika	5%	1%	0%
Slovačka	-	0%	0%
Mađarska	32%		0%
Slovenija	8%	2%	0%
Kipar	0%	0%	0%
Malta	0%	0%	0%

Source: data of Regulator

Remark:

1. Data for Belgium are related only to Flam region (customers who abandoned the regulated tariff: 40% industrial, 53% small companies/households)
2. Ireland, including switch on ECB (independent)
3. Italy, Spain include all customers that abandoned regulated tariffs (i.e. including re-negotiating)

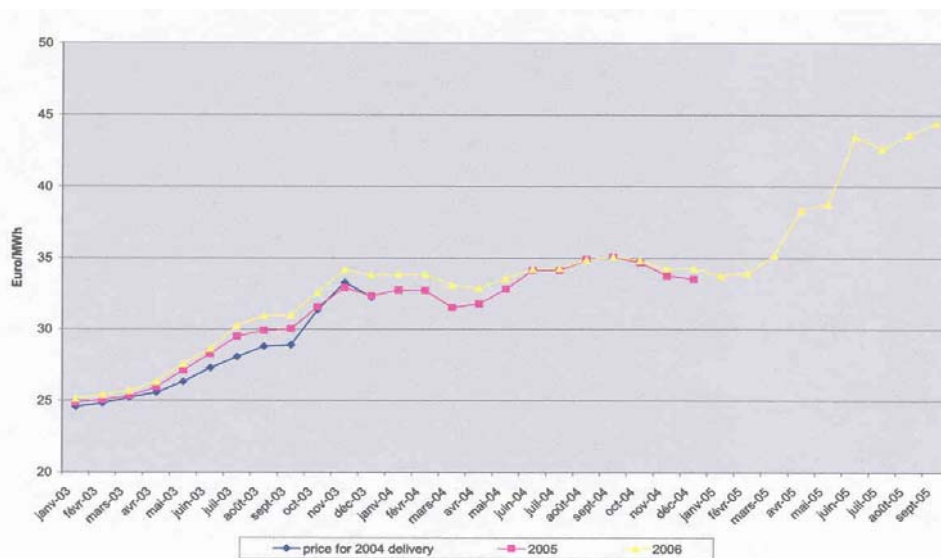
5. Trends of the electricity prices

General trend of changes of the electricity prices in the European Union, since the beginning of the reform of the electric power sector, has been declining. According

to data of the European Commission, stated in the Report on progress in development of the internal market, in the period 1997-2005, prices for end users decreased for 10%, which means 4% for big industrial customers, 5% for middle industrial customers and 12% for commercial customers and households.

Application of Directives on protection of environment and trade of certificates for emission CO₂, without any doubt, affected occasional drastic price changes at the wholesale market, which resulted in direct insertion of all prices in the forward contracts for band energy.

Wholesale prices of band energy (energy of the constant capacity) per contracts for the period 2004-2006 have had major increase, which can be seen in the following graph:



Graph 2 - Prices of band energy for the calendar year 2004-2006 (EEH Leipzig)

Source: Eurostat Market prices, DTI Quarterly Energy Prices

Retail prices are reflected on this general trend depending on the category of consumption, so that the change of the wholesale prices does not affect big customers, which is logical taking into account a share of the wholesale price in the total price for customers at high voltage level.

6. Independency of the system operator

Directive 2003/54 EC prescribes legal and functional unbundling of the system operator from generation and/or trade and supply, while regulations providing implementation of this provision are different in EU countries.

While 12 countries prescribe legal unbundling as minimum, 12 countries prescribe compulsory ownership unbundling of the transmission system operator from other activities, consequently creating assumptions for creation of the wholesale market.

Unbundling of the distribution system operators, particularly from supply, has not been uniformly solved in the EU countries. Most countries included in their legislation, exception which is allowed by Directive for distributors with less than 100,000 beneficiaries.

In practice, it resulted in different solutions whereby some countries impose the requirement of legal unbundling but the ownership unbundling is not required and it was only conducted in Great Britain. Legal unbundling of the distribution system operators was not conducted in most countries. According to the European Commission Report⁴, functional unbundling was not applied in the spirit of Directive. Accounting unbundling and audit of unbundled accounts was prescribed as an obligation and it is conducted in most countries (with exception of Ireland, Spain, Estonia, Poland, Czech, Slovakia and Slovenia).

In Spain, Italy, Portugal and Hungary, distributor is at the same time compulsory supplier (for tariff customers).

Table 4 - Unbundling of the distribution network operator

countries	Legal unbundling conducted	Management unbundled (Y/N)	Corporate acting unbundled (Y/N)	Regulatory accounts with guidelines unbundled (Y/N)	Audit of the unbundled accounts (Y/N)	Publication of unbundled accounts (Y/N)	Special Board of Directors without members from other	Grading (possible 6)
Austrija	no	N	partly	N	Y	Y	partly	3
Belgija	da	Y	Y	Y	Y	Y	N	5
Danska	da	partly	partly	Y	Y	Y	partly	4
Finska	da	N	N	Y	Y	Y	N	3
Francuska	no	N	N	N	N	N	N	0
Njemačka	no	N	N	Y	Y	N	Y	3
Grčka	no	N	N	N	Y	N	N	1
Irska	no	N	Y	Y	Y	Y	N	4
Italija	see remark	N	N	Y	Y	N	N	2
Luksemburg	no	N	N	N	partly	partly	N	1
Holandija	da	N	Y	Y	Y	Y	N	4
Portugal	see remark	Y	N	Y	Y	Y	N	3
Španija	see remark	N	Y	N	N	N	N	1
Švedska	da	N	N	Y	Y	Y	N	3
Velika Britanija	da	partly	partly	Y	Y	Y	partly	5
Norveška	da	N	partly	Y	Y	Y	N	4
Estonija	da	Y	Y	Y	Y	Y	Y	6
Latvija	no	N	N	Y	Y	N	N	2
Litvanija	da	Y	Y	Y	Y	Y	Y	6
Poljska	no	N	N	N	N	N	N	0
Češka R.	no	N	N	Y	N	N	N	1

⁴ Report on progress on development of the internal market of gas and electricity dated 15.11.2005 and Technical Annex accompanying the Report

Slovačka	no	Y	Y	N	N	N	N	2
Mađarska	see remark	N	N	N	Y	Y	N	2
Slovenija	no	N	N	Y	Y	Y	N	3
Kipar	no	N	N	Y	N	N	N	1
Malta	no	N	N	ongoing	N	N	N	1
Complete acceptance	9	7	11	17	19	15	6	

Source: Regulator data

Remark:

1. In Spain, Portugal and Hungary, distribution companies are also incumbent suppliers. However, suppliers of non-regulated (eligible) customers have to be legally unbundled.

There are considerations on regarding audit of the unbundling requirements of the vertically integrated companies, and equalizing criteria for obligatorily unbundling of the electric power activities in domestic legislation of the countries members.

7. Effective regulation and independent regulatory authority

Regulator for electricity exists in all countries EU members. Organization and competence of the Regulator were differently defined, so that, with some countries, the competences are divided between regulators, entities in charge of the competition control and ministries as long as they exist and states with some regulators functioning at regional and state level.

Regulatory bodies were established at the EU level such as the Council of the European Energy Regulators (CEER), while in 2003 the European Commission founded the European Regulatory Group for electricity and gas (ERGEG).

Through these bodies and Firenze Forum, which is a permanent forum for regulatory issues for electricity, there are initiatives given for improvement of the regulator operation which refers to the following:

- members countries should provide implementation of directives, both spiritually and practically, first of all those provisions on unbundling and non-compliance shall be punished;
- countries members shall provide that Regulator may make prudent decisions in a flexible way in order to improve the market competition, independently from the interest of electric power activities;
- regulator shall enforce their efforts to solve key problems in the market integration, where there are already considerable authorizations regarding provision of fair and non-discriminatory conditions for the access to the network and balance rules;
- countries members and regulators shall commit themselves for increase of interconnections between the countries members, either through investments or in some other way;

- countries members and regulators shall provide appropriate protection for end users and stimulate the reaction of customers, in that way, it is necessary to analyze the appropriateness of methods of the price control referred to Article 3 of Directive;

The regulation level within the scope of the electricity price is indicated by the following table:

Table 5: Existence of the price control

Countries	ELECTRICITY		
	Regulated tariffs Industrial customers	Regulated tariffs Small companies	Regulated tariffs Households
Austrija	N	N	N
Belgija	N	N	Y
Danska	Y	Y	Y
Finska	N	N	Y*
Francuska	N*	Y	Y
Njemačka	N	Y	Y
Grčka	Y	Y	Y
Irska	Y	Y	Y
Italija	Y	Y	Y
Luksemburg	N	N	Y
Holandija	N	N	N
Portugal	Y	Y	Y
Španija	Y	Y	Y
Švedska	N	N	N
Velika Britanija	N	N	N
Norveška	N	N	N
Estonija	Y	Y	Y
Latvija	Y	Y	Y
Litvanija	Y	Y	Y
Poljska	Y	Y	Y
Češka Republika	N	N	Y
Slovačka	N	N	Y
Mađarska	Y	Y	Y
Slovenija	N	N	Y
Kipar	Y	Y	Y
Malta	Y	Y	Y

Source: Regulator data

Remark:

1. Finland D* means that there is ex-post control
2. Germany, ex-ante approval of domestic and SME of the end user tariff by Lander shall be effective until 1 July 2007

The European Commission attempts to develop the instruments for complete practical application of Directive 2003/54 EC, which shall include regular checking and practical volume of the legislative and regulatory measures of the countries members.

The European Commission developed the Study and made recommendations regarding more precise competences of the regulatory body, aiming at improvement of the existing practice.

8. Protection of customers and public service obligation

Taking into account the basic aim of Directive - to maintain and improve the position of end users, the European Commission follows and estimates the level of services offered to customers, so that the introduction of competition does not result in reduction of their level.

In that sense, regulatory bodies and state bodies make regulations and measures to protect the rights of customers.

Special attention is paid to socially vulnerable customers. For that purpose, there were special guidelines made and it is considered justification of making regulations of the European Union.

APPENDIX 2

INFORMATION ON CHANGES IN THE ELECTRIC POWER SECTOR AND ACTIVITIES OF REGULATOR IN 2006

1. Introduction

Implementing regulations within the scope of competence of Regulator pursuant to the Law, in 2006, the conditions for de-regulation of the electric power sector and electricity market liberalization were created.

In 2006, State Regulatory Commission for electricity in BiH approved the Grid Code, which regulate conditions based on non-discriminatory position at the transmission network and Market rules that enable prescription of rules and arrangement of relations between the participants to the electricity market in the initial phases of the market opening.

Issuance of licenses to new participants to the market, making rules and regulations within the regulatory competence enabling the end users to choose the supplier and other decision, measures and actions considered, made and undertaken by Regulator with other authorized bodies in Republic of Srpska and Bosnia and Herzegovina imply the commencement of the process of opening and liberalization of the electricity market. As far as competitive activities are concerned, Regulator is in charge of regulation and control of realization of activities in the system related to public service obligation, in order to improve quality of the service in the electric power system for welfare of end users and stability of business environment for the structures dealing with the electric power activity.

2. Legal framework of regulation of the electric power sector and electric power activities

2.1. Market opening

The political will of countries signatories expressed by signing of the Athens memorandum was enforced in the legal obligation when the Energy Community Treaty of South East Europe became effective and it happened on 1 July 2006 after ratification of 6 parties-signatories. Presidency of Bosnia and Herzegovina made Decision on ratification of the Treaty on 27 June 2006.

Having ratified the Energy Community Treaty of South East Europe, Bosnia and Herzegovina accepted the application of Directives of the European Union about the energy market, protection of environment, competition and renewable energy per timetable stipulated by the Treaty. According to the adopted laws and internationally taken obligations, Bosnia and Herzegovina is joining other countries in the region which have already opened their markets.

State Regulatory Commission for electricity (SERC) made Decision on volume, conditions and timetable of the market opening in BiH, in 2006, according to the Law on transmission, regulator and system operator of electricity in BiH, while REERS and FERC should provide criteria for getting a status of eligible customer which shall create conditions for gradual market opening in Bosnia and Herzegovina.

REERS determined draft Rule for getting a status of eligible customer, which gives a possibility for end user to freely choose supplier, regulate terms and criteria for getting a status of eligible customer, his rights and obligations, rights and obligations of the supplier, particularly during the transitional period of the gradual market opening, taking into account the requirement for harmonization with new conditions and provision of the safety of supply with electricity for customers.

Starting from the framework prescribed by the Law, and pursuant to obligations of Bosnia and Herzegovina within circumstances of gradual establishment of the energy market of South East Europe for the purposes of its integration to the European market, Regulator is led, in the process of the market opening, by guidelines and terms from the adopted and signed documents within the process of establishment of the energy community for South East Europe.

Regulator considers rules on getting a status of eligible customer which shall enable gradual changes in trade and supply of electricity, so that the retail market opening and right of the supplier to choose do not have an adverse impact on the safety of supply of end users with electricity in Republic of Srpska in the transitional period, until the electricity market in Bosnia and Herzegovina is not fully defined and established.

2.2. Renewable energy sources

At the request of Ministry of economy, energy and development in the RS Government, Regulator gave its Opinion on electricity prices from small plants, capacity up to 5 MW.

Regulator initiated, through the respective Ministry, the need to define a share of renewable sources in total consumption, timetable of priorities of some sources and applied technologies, as well as the elements of the power policy made by the Government of RS pursuant to the Article 5 of the Law, which complies with the requirements taken by the Energy Community Treaty of South East Europe.

In order to determine and provide single conditions for getting a status of eligible producer of electricity, rapid, efficient and cost-effective procedure for submission and treatment of application, making fair Decision per the submitted application, Regulator has properly developed this Rule on getting a status of eligible generator.

This Rule shall prescribe: terms and conditions which generator of electricity should fulfill in order to get a status of eligible (privileged) generator, types of

eligible generators of electricity and their status, the procedure for making Decision per application, content of the application with necessary documents as well as procedure, transfer and cancellation of status of eligible generator.

REERS activities related to making rules on conditions for getting a status of eligible generator as well as subsidies and other mechanisms of incentives for renewable sources depend on the formulated electric power policy of Republic of Srpska.

Regulator plans making of this document in the second half of 2006.

3. Licenses and permits

3.1. Issuance of licenses

Regulator, in its 33rd regular session which was held on 16/06/2006, made Decisions on issuance of the license for trade and supply on the territory of Bosnia and Herzegovina to the Service and trade company "Energy Financing Team", Ltd Trebinje. The application for issuance of this license was submitted on 27 December 2005 and four times amended and after that REERS published Notification on the complete application on 11 April 2006. In its 30th regular session, which was held on 27 April 2006, it was determined the draft license, while the general hearing on the draft license was held on 10 May 2006 in Trebinje.

In 2006, REERS received the application for issuance of the license for electricity generation in the small hydro power plant Divic, Kotor Varos. Notification that the application was complete was published on 9 August 2006.

3.2. Supervision over the license requirements' compliance

In the process of supervision over the license requirements' compliance, in 2006, Regulator initiated the activities of regular and extra checking of the regulated companies.

Two extra check-ups were made which resulted in orders to undertake the measures for removal of the practice which is contrary to requirements of the issued license. It was about the method of calculation of the electricity consumed and calculation of the interest for delay in settlement of the financial obligations and acting per the objection of end users.

Regulated companies acted pursuant to the order of Regulator for realization of the measure and informed Regulator accordingly, which was confirmed by the regular monitoring.

There were three regular monitoring actions and reports were made on the condition determined with recommendations for removal of the found failures.

Regulator plans to carry out monitoring process till the end of 2006 regarding the compliance with requirements of all issued licenses for the electric power activities.

4. Regulation of the electricity price

4.1. The first tariff proceeding

Decision on initiating the first tariff proceeding as well as Decision on content and form of the template in the tariff proceeding were made in the 16th regular session on 21 June 2005 ("Official Gazette of Republic of Srpska", number 65/05).

Upon completion of formal hearings in January 2006, parties to the proceeding and intervener were submitted Final reports of the presiding officer (seven Presiding officer reports for the price approval at the plant outlet and one consolidated Presiding officer report for approval of tariffs for distribution system users and tariff rates for sale of electricity to non-eligible customers). The reports included detailed technical and economic analyses of revenue requirement and justified costs of the applicant. All parties to the proceeding were given a possibility to give their comments on the submitted Presiding Officer reports. Presiding officer reports with the proposed price at the plant outlet, tariff rates for distribution system users and tariff rates for non-eligible (tariff) customers, were published at the website of REERS in order to collect additional comments on the proposed prices and tariff rates before their final adoption.

Regulator made, in its 28th regular session which was held on 22 March 2006, Decisions on the price approval at the plant outlet, tariff system for sale of electricity in Republic of Srpska, tariff rates for distribution system beneficiaries in Republic of Srpska, tariff rates for non-eligible customers in Republic of Srpska. The prices and tariff rates made were applicable as of 1 April 2006.

4.2. Electricity prices in Republic of Srpska

The prices which were determined by "Elektroprivreda RS" in agreement with RS Government were valid until 31 March 2006. The tariff system and tariff rates for sale of electricity to non-eligible customers made by REERS became effective on 1 April 2006.

In spite of the fact that individual tariff rates (unit prices of tariff elements for the respective categories of consumption and groups of customers in certain daily and seasonal intervals) were changed, it was partly changed the tariff system regarding the method of determination of the capacity charge for end users within the category of households.

The tariff system which has been applicable since 1 April 2006, prescribed by Regulator upon the first tariff proceeding, starts from the classification of tariff elements, categories of consumption and groups of customers and periods of

consumption which were applicable in the past. Allocation of the accompanying costs based on this classification was made applying the marginal analysis (the analysis of marginal costs) which resulted in modification of tariff rates comparing to those valid in 2005.

The tariff system and tariff rates approved by Regulator upon completion of the tariff proceeding were based on costs to such an extent in which those available necessary data on consumption, system load and costs, so according to the available data it was made calculation of costs for provision of the necessary capacity for respective groups of customers based on metered or estimated peak load of each respective group.

Definition of the tariff system and determination of tariff rates based on the marginal analysis is meant by commencement of Regulator activities of gradual elimination of cross-subsidies between categories of consumption and groups of customers and connection of the electricity price with costs of the electric power system caused by consumption under respective circumstances.

If Regulator intends to carry out its task, it is necessary that regulated companies improve their systems of the cost analysis per type and place of occurrence as well as to carry out necessary analyses of load and consumption of different groups of customers.

Regulator did not have necessary data available for the analysis of possible justification to introduce new categories of consumption and tariff groups of customers within the existing ones, based on costs which their way consumption causes to the electric power system.

In the forthcoming period Regulator expects the regulated companies to conduct complete analysis of load and consumption for the purposes of more fair allocation of costs following the casualty principle.

In the following table there are average prices of electricity in Republic of Srpska and Federation BiH based on the calculated average consumption of customers and average capacity charges of the respective categories of end users:

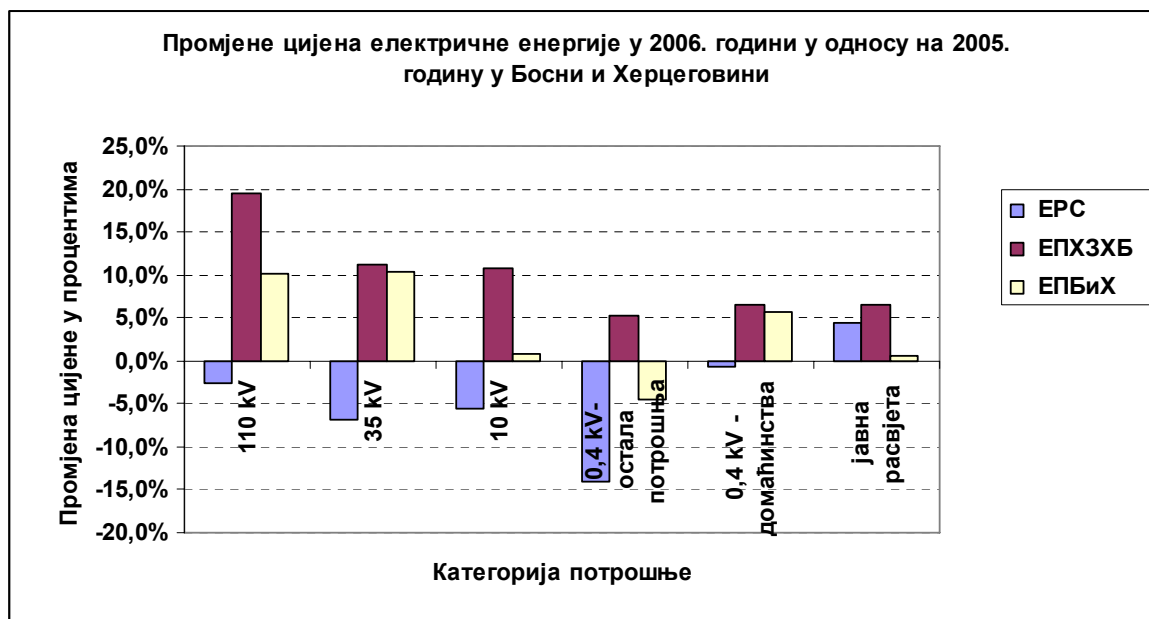
Table 1- Average prices of electricity in BiH in 2005 and 2006

	ERS		EPHZHB ⁵		EPBiH	
	2005.	2006.	2005.	2006.	2005.	2006.
Categories of consumption						
110 kV	5,99	5,83	6,16	7,36	7,13	7,86
35 kV	6,83	6,37	10,00	11,11	8,43	9,30
10 kV	8,57	8,09	11,36	12,59	11,63	11,73
0,4 kV - other consumption	17,85	15,33	20,02	21,07	19,56	18,66

⁵ Подаци за ЕПХЗХБ и ЕПБиХ из ФЕРК-а

0,4 kV - households	10,28	10,21	11,00	11,72	11,18	11,82
Public lightning	12,00	12,53	15,65	16,68	15,40	15,50

Graph 1 - Changes of the average electricity prices in BiH



It is obvious that there is reduction of the average price for end users in Republic of Srpska, while tariffs and tariff system have been designed with the aim to effectively use resources of the electric power system.

Large end users who use electricity in a rational and effective way, i.e. whose consumption corresponds to the engagement of peak capacity in the period no shorter than 8 hours realize more significant reduction of total price.

5. Protection of customers

5.1. Regulatory framework of the customer protection

The problems of the customer protection in Bosnia and Herzegovina were regulated by the Law on protection of customers ("Official Gazette of BiH" number 25/06) which initiated the procedure of application of the European standards regarding informing and protection of customers itself.

Apart from the above mentioned, protection of customers is still on of considerable issues of the regulation policy in all countries in which there are ongoing processes of de-regulation and liberalization of the energy sector. For that purpose, regulatory bodies are assigned with more and more duties and the task to analyze at the open electric power market, the issues of protection of customers, protection of the electric power structures and environment through in a transparent and impartial way of solving issues related to regulation.

Acting pursuant to the Conclusion of the National Assembly of Republic of Srpska, number 01-404/06 dated 12 April 2006, made in the 33rd regular session which was held on 12 April 2006, Regulator made, in its 33rd regular session which was held on 11 May 2006, Conclusion regarding calculation of interests on receivables based on the electricity delivered which, among other things, determined liabilities for the companies dealing with distribution and supply of end users with electricity regarding calculation, invoicing and collection, including the obligation to check already calculated interests.

Conclusions were submitted to the National Assembly of Republic of Srpska and Government of Republic of Srpska.

These measures resulted in correction of calculation with the companies which calculated the interest against positive regulations.

Conclusions of the Regulator were additionally supported by the Government of Republic of Srpska regarding handover of activities which were ordered by Conclusions of the National Assembly.

5.2. Settlement of disputes and complaints

Having introduced the regulation in this branch, it was initiated the policy of active protection of customers and established the communication between different participants at the electricity market and particularly end users with Regulator, which was particularly obvious in 2006.

In 2006, Regulator was filed 74 applications for settlement of disputes regarding regulatory competence, out of which 64 were settled.

Due to many objections of the customers for delay of liability toward the regulated companies that turned to Regulator to initiate the dispute, Regulator held a special technical hearing with representatives of the companies in charge of calculation, invoicing and collection of receivables from end users, associations of end users and experts from the sphere related to the obligation relationships. Disputes related to issues of delay are not within the regulatory competence, but Regulator initiated the hearing for regulated companies to approach these problems in a way which is based on law and without discrimination of customers.

Report from the technical hearing was published at the website of Regulator, and conclusions were adopted in which Regulator expressed its standpoint regarding these disputes.

5.3. General conditions for delivery and supply of electricity

Pursuant to provisions of Article 23 and 30 of the Law, and according to the Activity plan for 2005, Regulator initiated, in April 2005, activities related to

drafting General conditions for delivery and supply of electricity in Republic of Srpska, and the first draft was this document was made in August 2005.

Draft of this document was determined in the 29th regular session which was held on 20 April 2006. Information for the public for collection of comments and information about the public hearing was timely informed in newspapers, while draft General Conditions with Rationale was submitted to stakeholders independently and might have been handed over in the seat of Regulator. Interested legal and physical persons as well as invited experts submitted written comments on the draft General conditions in the period of five days from the day the information was published until expiry day for submission of comments on 25 May 2006.

In the procedure of public consideration of the draft General conditions, REERS held three general and two technical hearings. In the procedure of public consideration of the draft General Conditions, REERS held two technical (Trebinje 16 May 2006 and Banja Luka 24 May 2006) and three general hearings (Pale 18 May 2006, Bijeljina 19 May 2006 and Doboje 23 May 2006).

REERS held one more technical hearing on 14 June 2006 in Trebinje which subject was the revised draft of General conditions which contained the comments of the public, accepted by the professional departments of REERS.

The mentioned text of the draft General conditions with Summary of comments and proposals for amendment of the draft General Conditions was published at the website of REERS so that all those interested might have participated in the procedure related to development of General conditions, within the prescribed deadline until 14 June 2006.

General conditions for delivery and supply of electricity were published in the "Official Gazette of Republic of Srpska", number 66/06.