

**RECOMMENDATIONS
REGARDING
THE REFORM OF THE
ENERGY COMMUNITY
TREATY**

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PREFACE

The Energy Community Treaty was signed in Athens, Greece, on 25 October 2005, and entered into force on 1 July 2006. The contracting parties to the Treaty are Albania, Bosnia & Herzegovina, Kosovo¹, Macedonia², Moldova, Montenegro, Serbia and Ukraine.

On 24 October 2013, the duration of the Treaty was extended for an additional 10 year-period by a decision of the Ministerial Council of the Energy Community.

This extended timeline provided an opportunity to reflect on the past experience in achieving the objectives of the Treaty and on possible improvements to the functioning of the Energy Community, including changes to the current Treaty.

The Ministerial Council of the Energy Community established a High Level Reflection Group (HLRG) chaired by Jerzy Buzek and including Walter Boltz, Vesna Borozan, Fabrizio Donini-Ferretti, Volodymyr Makukha and Goran Svilanović as members.

The Group was mandated by the Ministerial Council to carry out an independent assessment of the adequacy of the institutional set-up and working methods of the Energy Community, and to make proposals for improvements to the Ministerial Council in June of 2014.

This document represents the agreed position of the undersigned Civil Society Organisations towards the Energy Community in respect of its future work and should be seen as complementing the work of the HLRG.

- *SEE Change Net Foundation*, Bosnia and Herzegovina
- *Client Earth*, Poland
- *Front 21/42*, Macedonia
- *CAN Europe*, Belgium
- *Analytica*, Macedonia
- *Advocacy and Training Resource Center – ATRC*, Kosovo
- *CEKOR*, Serbia
- *Public Interest Advocacy Center – CPI*, Bosnia and Herzegovina
- *Center for Environment*, Bosnia and Herzegovina
- *DOOR*, Croatia
- *Environmental Center for Development, Education and Networking – EDEN*, Albania
- *Ekolevizja*, Albania
- *Eko-Svest*, Macedonia
- *Forum for Freedom of Education – FSO*, Croatia
- *Fractal*, Serbia
- *Green Home*, Montenegro
- *MANS*, Montenegro
- *World Wide Fund For Nature*, MedPo, Italy
- *CEE Bankwatch Network*, Czech Republic
- *Health and Environment Alliance – HEAL*, Belgium

1. According to the UN, Kosovo is “under the United Nations Interim Administration Mission in Kosovo (UNMIK) established pursuant to Security Council Resolution 1244.” In this paper it is referred to as “Kosovo”.

2. According to the UN, the official name for Macedonia is “The former Yugoslav Republic of Macedonia”. In this study it is referred to as “Macedonia”.

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EXECUTIVE SUMMARY

In the 2009 Notre report examining the feasibility of a European Energy Community, Jacques Delors wrote:

“Europe faces several major crises: an energy crisis, with human activity consuming more resources than nature can provide; an environmental crisis, with climate change calling for a radical shift in the way we produce and consume energy; and an economic and financial crisis that limits our ability to find solutions quickly.”

In the few years since this report was written we have experienced the Fukushima Daiichi nuclear disaster, crude oil prices averaging more than USD 110 per barrel for two years in a row, the BP Deepwater Horizon disaster in the Gulf of Mexico and the current energy concerns provoked by the crisis in Ukraine.

The recent flooding of homes, coal mines and power plants across the Balkans combined with the certainty³ that unchecked climate change will lead to more frequent catastrophic – and hugely expensive⁴ - climate events, have all demonstrated that energy is a crucial component of security as well as sustainability and that the current ways of doing business make our region and indeed the whole world extremely vulnerable.

The extension and reform of the Energy Community Treaty therefore represents a golden opportunity to meet these weighty challenges with a united approach and a sense of common purpose.

If it is to do so, the Energy Community needs to be strengthened by the redoubled commitment of its members to an enhanced legal framework and to the EU’s long-term goals such as decarbonisation and environmental protection. There is also an urgent need to address systemic failures, e.g. dysfunctional governance and structural flaws in decision-making, lack of transparency, as well as high-level corruption amongst the signatory states.

As one element of its work, the Energy Community Secretariat has made greater efforts to include the views of Civil Society Organisations (CSOs) in recent times, and we encourage it to continue and formalise greater public participation in the functioning of the Treaty. The EU’s own position on this matter supports such a move when it states, that *“an empowered civil society is a crucial component of any democratic system and is an asset in itself. It represents and fosters pluralism and can contribute to more effective policies, equitable and sustainable development and inclusive growth... They embody a growing demand for transparent and accountable governance.*

While states carry the primary responsibility for development and democratic governance, synergies between states and CSOs can help overcome challenges of poverty, widening inequalities, social exclusion and unsustainable development⁵”.

3. https://unfccc.int/files/meetings/warsaw_nov_2013/application/pdf/cop19cmp9_opening_ipcc_pachauri_powerpoint.pdf
4. <http://www.bloomberg.com/news/2014-05-11/power-decarbonization-cost-rises-22-to-44-trillion-iea-says.html>
5. “The roots of democracy and sustainable development: Europe’s engagement with Civil Society in external relations” – Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions (2012)

RECOMMENDATIONS

In concrete legal terms, the challenges outlined above require the following improvements to the Energy Community Treaty:

1. RULE OF LAW AND TRANSPARENCY

Public Procurement Directive 2004/18/EC

The Directive's provisions are crucial not only to the energy sector, but also to unification of the of the Energy Community Contracting Parties' legislation and economies and strengthening the rule of law.

Competition and state aid rules (Article 108 of the TFEU)

Inclusion of Article 108 into the Energy Community Treaty and equipping the Secretariat with strong investigative and decision-making powers regarding state aid issues and aid measures would help to build a transparent aid procedure in the energy sector.

Directive 2001/42/EC on the assessment of the effects of certain plans and programmes on the environment according to which a Strategic Impact Assessment is obligatory for plans/programmes, inter alia those prepared for energy sector, and which sets the framework for future development consent of projects listed in the Environmental Impact Assessment Directive.

2. ENVIRONMENTAL STANDARDS AND CLIMATE ACTION

While energy and environmental policies are inextricably linked, harmonizing environmental standards and combatting climate change is crucial for sustainable development of the region. Unfortunately in the context of poor transparency, social and environmental concerns are often discounted or postponed.

Therefore the Treaty's environmental *acquis* needs to be expanded in order to ensure that the countries of the Energy Community are moving in a planned and incremental way towards EU goals and targets in respect of a low-carbon, energy-efficient, renewables-based society.

The climate and energy targets are an essential part of the European Union's strategy for 2020, 2030 and 2050. Introducing provisions of European Union's targets will help to ensure a balance in energy trading and also give the necessary lead in and planning time for the countries of our region to meet the long term goal of decarbonising the electricity sector in a manageable, step by step approach.

The following EU environmental legislation is also crucial and closely related to energy planning and investments:

Chapter II of Directive 2010/75/EU on industrial emissions according to which, industrial installations must use the "best available techniques" to achieve a high level of environmental protection.

The Directive ensures a level playing field in energy generation in the EU and Energy Community and prevents the danger of emissions leakage.

Directive 2008/50/EC on ambient air quality and cleaner air for Europe which, defines objectives for ambient air quality designed to avoid, prevent or reduce harmful effects on human health and the environment as a whole.

Directive 2008/105/EC on environmental quality standards in the field of water policy which sets environmental quality standards for surface waters (rivers, lakes, transitional and coastal waters). The impact of power plant operation on water quality should be minimized by implementing this Directive.

Directive 2006/21/EC on the management of waste from extractive industries and amending Directive 2004/35/EC which applies to waste resulting from the extraction, treatment and storage of mineral resources. The Directive is clearly relevant to mining supplying the energy sector in the Energy Community countries.

Directive 2000/60/EC on the management of waste from extractive industries which establishes a framework for action on water policy. The Directive identifies priority substances and obliges states to monitor the level of those substances and to achieve good status of water quality. It also requires the non-deterioration of water bodies' status.

Directive 92/43/EEC on the conservation of natural habitats and of wild fauna and flora, known as the Habitats Directive, designed to help maintain biodiversity in by defining a common framework for the conservation of wild plants and animals and habitats of Community interest. This Directive plays a significant role in energy investments, particularly in the hydropower or wind sector, which can have a serious impact on natural habitats, flora and fauna.

3. IMPLEMENTATION

There is a clear need to increase the Secretariat's capacity to monitor and enforce the Treaty by equipping it with stronger investigative and decision-making powers.

The existing enforcement mechanism does not fulfil this role adequately and should be strengthened by enhancement of the dispute settlements mechanism as well as democratization of decision-making processes.

In this context we also request non-voting CSO participation in all bodies and activities of the Energy Community up to and including the PHLG and the Ministerial Council.

THE REPORT

CONTEXT

The Energy Community was established in 2005 to create an effective regulatory and market framework in order to ensure a stable and continuous energy supply in the region, as an essential precursor for economic development and social stability. In the first decade of its existence the Energy Community was deemed to be a successful example of regional cooperation, which has also contributed towards solidarity, mutual trust and peace in this formerly fragile region.

*“Europe faces several major crises: an energy crisis, with human activity consuming more resources than nature can provide; an environmental crisis, with climate change calling for a radical shift in the way we produce and consume energy; and an economic and financial crisis that limits our ability to find solutions quickly. However, these crises also offer opportunities. The development of alternative, sustainable energy sources and green technologies is the key to a new industrial revolution based on sustainable development and new technologies that will help us emerge from the economic crisis. Will Europe choose to play a proactive role in the next industrial revolution, or will it be content to follow the lead set by others?”*⁶

The question posed by Jacques Delors is very relevant to the Energy Community. The Energy Community Treaty is an attempt to extend the ‘European regulatory space’ for the internal market to non-EU countries, under which they commit to adopt the *acquis* on energy, environment, competition while taking into account social issues.

The first assessment report on the Energy Community published by the European Commission in March 2011 verified that *“the Energy Community has grown into a mature organization, which provides a solid institutional framework for cooperation, mutual support and exchange of experiences and therefore serves as a model for regional cooperation on energy matters.”* In fact since its creation the Energy Community has encouraged the full and timely implementation and enforcement of the EU *acquis*, as well as assisting in removal of technical barriers towards an Energy Community-wide energy market.

However even the Secretariat admits that *“the current implementation efforts in the Contracting Parties are not sufficient to achieve the comprehensive sector reform and the regional integration pursued by the Treaty.”*⁷

6. A call for European Energy Community by Jacques Delors in Notre Europe’s paper “towards a European Energy Community: A policy Proposal (2010)

7. “An Energy Community for the Future – the Secretariat’s View”

More deeply concerning are the emerging global and regional impacts we have experienced in recent times including the Fukushima Daiichi nuclear disaster, crude oil prices averaging more than USD 110 per barrel for two years in a row, the BP Deepwater Horizon disaster in the Gulf of Mexico and the current energy concerns provoked by the crisis in Ukraine.

The recent flooding of homes, coal mines and power plants across the Balkans combined with the certainty⁸ that unchecked climate change will lead to more frequent catastrophic – and hugely expensive⁹ - climate events, have all demonstrated that energy is a crucial component of security as well as sustainability and that the current ways of doing business make our region and indeed the whole world extremely vulnerable.

Now that there is a decision to extend the Treaty and an assessment of the adequacy of the current institutional set up and working methods has been decided upon, it is more important than ever to agree on a clear set of future goals .

Given the fact that many Energy Community Contracting Parties are also countries acceding to the EU, combined with the fact that most investments in the energy sector lock in capital for several decades, the Energy Community will in the future need to ensure that the countries of the Energy Community are not left even further behind in the transformation to an energy-efficient, renewable-based society.

The extension and reform of the Energy Community Treaty therefore represents a golden opportunity to meet these weighty challenges with a united approach and a sense of common purpose.

8. https://unfccc.int/files/meetings/warsaw_nov_2013/application/pdf/cop19cmp9_opening_ipcc_pachauri_powerpoint.pdf

9. <http://www.bloomberg.com/news/2014-05-11/power-decarbonization-cost-rises-22-to-44-trillion-iea-says.html>

RECOMMENDATIONS

In concrete legal terms, the challenges outlined above require the following improvements to the Energy Community Treaty:

1. RULE OF LAW AND TRANSPARENCY

There is an urgent need to address systemic failures, e.g. dysfunctional governance and structural flaws in decision-making, as well as an abundance of reported corruption cases. In order to address these issues, clear commitments need to be undertaken in the extended Treaty on public participation and the rule of law, which can then be subject to the same dispute settlement procedure as the energy and environment acquis within the Energy Community. We recommend the inclusion of:

a. **Public procurement (Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts)**

Directive 2004/18/EC sets out the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts creates the criteria used by the contracting authorities in awarding their public contracts. The first criterion is the lowest price. However, if the contract is awarded to the most economically advantageous tender, the contracting authorities use other criteria (like quality, price, technical merit, aesthetic and functional characteristics, environmental characteristics, etc.), which should be specified and have relative weight.

These conditions aim to check the suitability of economic operators tendering for contracts on the basis of criteria relating to their economic and financial capacity, and their technical and professional knowledge or abilities. The conditions for participation also aim to effectively combat fraud and corruption. The awarding of contracts concluded in the Member States must also comply with the European principles of the free movement of goods, the right of establishment and the freedom to provide services. Moreover, when public contracts exceed a certain amount, Community coordination of the national procedures for awarding these contracts is necessary in order to ensure maximum competition and full benefit to be made of the internal market.

The provisions of the Directive should be introduced to the Energy Community Treaty in order to ensure that public tenders take place in the construction of energy infrastructure. In fact the Commission's own report on the Energy Community identified the shortcoming of impact of the Energy Community Treaty on investments, which could be resolved with applying systematic solutions. The application of public procurement rules would help to solve the problem of corruption and strengthen the rule of law in the energy sector. The Directive's provisions are crucial not only to the energy sector, but also to unification of the of the Energy Community Countries' legislation and economics.

b. The Competition and State Aid rules (Article 108 of the TFEU)

In accordance with Article 107 of the Treaty on the Functioning of the European Union (TFEU) on notification of State Aid, any public aid, which distorts or threatens to distort competition by favouring certain undertakings or certain energy resources, is incompatible with internal market. However, there are some kinds of aid, which may be considered to be compatible with the common market:

- aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned,
- aid to make good the damage caused by natural disasters or exceptional occurrences;
- aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division;
- aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State
- aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;
- aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest;
- such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission may be considered to be compatible with the common market.

A decision by a state on whether aid is compatible with the common market, may lead to abuse of state interventions through the unlawful use of public resources. Thus, according to Article 108 (ex-Article 88) of the TFEU, *“the Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States (...). If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the internal market having regard to Article 107, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission”*. Inclusion of Article 108 into the Energy Community Treaty with adjustments to equip the Secretariat with strong investigative and decision-making powers regarding state aid issues and aid measures would help to build a transparent aid procedure in the energy sector.

c. Directive 2001/42/EC of the European Parliament and of the Council of 27 June 2001 on the assessment of the effects of certain plans and programmes on the environment

The public plans and programmes covered by this Directive are subject to an impact assessment during their preparation and before their adoption. This assessment includes the introduction of an environmental report (detailing the likely significant environmental effects and reasonable alternatives), as well as carrying out consultations (with the public, the authorities with environmental responsibilities and other States in the case of significant cross-border effects). **According to the Directive the Strategic Impact Assessment is obligatory for plans/programmes which are inter alia prepared for the energy sector and which set the framework for future development consent of projects listed in the Environmental Impact Assessment Directive.** The Directive provides members of the public with opportunities to participate on the permitting and on-going regulation of certain categories of activities. These are provided through consultation on certain key documents. By ensuring public participation the Directive favours the rule of law principle.

The SEA Directive plays a very important role in terms of assessing cumulative environmental impacts at strategic levels. The SEA Directive requires the consideration of: ‘the likely significant effects (...) including cumulative and synergistic effects on the environment (...)’ which is very important in terms of energy development planning and investments. With reference to development plans, cumulative effects can occur from the combined impacts of policies and proposals on specific areas or sensitive receptors. Many environmental problems result from the accumulation of multiple small and often indirect effects, rather than a few large and obvious ones. Examples include loss of tranquillity, changes in the landscape, loss of heathland and wetland, and climate change. These effects are very hard to deal with on a project-by-project basis. It is at the strategic level that they are most effectively identified and addressed.

2. WE RECOMMEND THE INCLUSION OF ADDITIONAL ENVIRONMENTAL STANDARDS AND CLIMATE ACTION GOALS

The limited scope of the environmental acquis within the Treaty is currently inadequate to protect the environment and public health from the impacts of the energy sector. Environment-related EU commitments need to be adopted, with equal weight given to all policy areas, meaning that the environmental acquis must be seen as having equal importance as the energy acquis. Moreover, the implementation of the environmental acquis will help to ensure a level playing field for the common energy market of the EU and Energy Community and avoid imports of electricity from environmentally damaging sources.

a. International and EU approach to climate change and its relevance for the Energy Community

Since 2006, the EU's climate, energy and environment policies have evolved and experienced significant changes. In addition, climate change negotiations under the United Nations Framework Convention on Climate Change (UNFCCC) have advanced and are expected to lead to a Global Climate Agreement in 2015. The recently released Fifth Assessment Report (AR5) of the Intergovernmental Panel on Climate Change (IPCC) confirmed that climate change is already happening; its impacts have been observed on all continents, with Europe and countries of the Energy Community being no exception. Once again, AR5 confirmed that the increase in concentration of greenhouse gases in the atmosphere resulted from growing combustion of fossil fuels in the energy sector.

The IPCC has stressed that there is no more time to delay action if we are to avoid the devastating effects of climate change, and the current Contracting Parties of the Energy Community, as well as potential future members¹⁰, will be highly vulnerable to climate change: countries of southern Europe are likely to experience rising temperatures and declining levels of precipitation, as well as increased extreme weather events: droughts, floods and forest fires. This will further affect their already fragile economies and their main sectors – agriculture, energy and tourism. In addition, a regional study¹¹ on climate change vulnerability in southeast Europe showed that climate change will have adverse effects on human health too.

Little has been done in the Contracting Parties to quantify the costs of climate change impacts or mitigation potential. Data¹² from Montenegro give us some indications: estimated potential damage from climate change in tourism amount to substantial EUR 33 to 68 million per year, while losses in revenue from the Piva hydropower plant alone could amount to EUR 7 million per year already as of 2030. For such a small economy, this is significant damage.

Tackling climate change is still largely seen by Contracting Parties as too expensive and an impediment to development. However, the Stern Review showed already in 2006 that without any climate action, the overall costs of climate change will be equivalent to losing at least 5% of GDP each year from now on. This estimate could rise to 20% of GDP or more, if a wider range of risks and impacts were included. In 2013 Stern stated that his analysis had been too conservative and that the real situation looks much worse¹³. However, in his report Stern projected that mitigation efforts would take only 1% of global GDP. Thus, it is clear that benefits of early action significantly outweigh the costs of inaction.

Decisions made today – if unsustainable - may backfire in the very near future, through the impacts of climate change, our image in the international political arena and in the EU, and through additional costs and non-compliance penalties in the process of

10. Countries of the Southern Mediterranean are often referred to as EU strategic partners in the energy sector and prospective members of the Energy Community.

11. South East European Forum on Climate Change Adaptation (2012): Regional climate vulnerability assessment – synthesis report.

12. Ministry of Sustainable Development and Tourism of Montenegro (2012): Technology needs assessment for Climate Change Mitigation and Adaptation for Montenegro. National Strategy and Action Plan.

13. <http://www.theguardian.com/environment/2013/jan/27/nicholas-stern-climate-change-davos>

accession, as complying with the EU acquis at a later stage would in all probability be more expensive.

In the EU accession process, climate policy is simply another side of the energy policy coin. Current EU climate and energy policy is centred around three targets that need to be achieved by 2020 - 20% greenhouse gas emissions reductions from 1990 levels, 20% share of renewable energy sources in EU energy consumption and 20% improvements in energy efficiency. The renewable energy targets have been adjusted for the Contracting Parties and energy efficiency targets of 9 percent by 2018 have been adopted¹⁴. However, despite the fact that most of the Contracting Parties are striving to become EU members in the next decade¹⁵ and are generally committed to the Kyoto protocol and the UNFCCC process, none of the countries has adopted greenhouse gas emissions reductions targets.

In 2011 the European Commission launched a Roadmap for moving to a competitive low-carbon economy in 2050 and an Energy Roadmap 2050, which show the longer term perspective of the European energy sector. The Energy Roadmap 2050 reflects the EU's goal of reducing greenhouse gas emissions by 80-95% below 1990 levels by 2050 as part of the effort needed by developed countries.

The 2030 policy framework currently under discussion for climate and energy aims to reduce the EU's domestic greenhouse gas emissions by 40% below the 1990 level by 2030. To achieve the overall 40% target, the energy sector would have to reduce its emissions by 43% compared to 2005. Moreover, the share of renewable energy must increase to at least 27% of the EU's energy consumption by 2030.

It is therefore essential that the EU's medium and long term visions, presented through the *Resource efficiency initiative* of the Europe 2020 Strategy, the planned EU 2030 framework on climate and energy policies, as well as the *Roadmap for moving to a competitive low-carbon economy in 2050* need to be taken into account when strategically planning the future of the Energy Community. The long-term vision of the EU means 80-95% greenhouse gas reductions by 2050 and almost complete decarbonisation of the energy sector, and should be applied to raise awareness of the Contracting Parties that they need to develop their energy sectors in line with this trajectory.

Therefore, we propose more ambitious energy efficiency targets than the ones currently adopted by the Energy Community as well as a commitment to GHG emission reduction targets in the revised Treaty, to enable the Contracting Parties to meet their obligations from the EU accession process. The Energy Community could contribute to facing this challenge by assisting countries with developing energy efficiency and decarbonisation scenarios that could significantly reduce the need for fossil fuels, especially as there is a significant amount of existing installed hydropower capacity in the region that can help to balance fluctuating electricity generation

14. In line with Directive 2006/32/EC on energy end-use efficiency and energy services and repealing Council Directive 93/76/EEC

15. Montenegro and Serbia have already opened negotiations and aim to join by 2020 and 2022, respectively, while other countries are expected to follow soon.

from renewable energy sources such as solar and wind. This would make maximum use of indigenous renewable energy resources and energy efficiency potential.

The EU Emissions Trading System (ETS) is part of the EU's effort to combat climate change by putting a cap on emissions from installations covered by the Scheme and aiming to accelerate low-carbon transition in the power generation and manufacturing sectors. The Scheme has been operational since January 2005. It covers almost 12,000 installations including oil refineries and steel, aluminium, other metals and cement plants.

From 2008 the economic recession and a massive inflow of international offset credits led to the accumulation of a huge surplus of allowances on the EU's carbon market. The surplus has undermined the Scheme's proper functioning. At the same time over-allocation of free permits to sectors being prone to a risk of carbon leakage, resulted in unjustified windfall profits and misuse of public assets. Furthermore lack of obligatory earmarking of auctioning revenues to support investments in energy efficiency and renewable energy has led to a situation where some of the EU Member States do not foresee greening of revenues and plan to spend auctioning funds for different, non-climate related purposes.

There are varying views within civil society whether incorporating the EU ETS Directive into the Energy Community legal framework would significantly contribute to bringing the Contracting Parties into line with the EU's decarbonisation objectives.

We recommend that, if implemented, the Energy Community's emissions trading scheme should be governed by a **tight cap** with **full auctioning** as the most cost-efficient, simplest, fairest, and most transparent way to allocate emission allowances as well as **mandatory earmarking of auctioning revenues** for climate investments, especially energy efficiency and support for small scale renewable projects. Moreover emission reductions should be realised through domestic abatement, instead of offsetting in third countries.

The problems of windfall profits and over-allocations, if not avoided or dealt with, will lead to serious problems in the functioning of emissions trading system and prevent such a system from achieving its goals.

b. Environmental acquis to be included in the revised Energy Community Treaty

Chapter II of Directive 2010/75/EU of the European Parliament and of the Council of 24 November 2010 on industrial emissions (integrated pollution prevention and control)

Chapter II of Directive 2010/75/EU on industrial emissions introduces obligations, which should be met by any industrial installation from the listed activities in Annex I to the Directive. Preventive measures must be taken against pollution; the best available techniques (BAT) should be applied; waste should be reduced, recycled or disposed of in the manner which creates least pollution; energy efficiency should be maximised; accidents should be prevented and their impact should be limited; significant pollution should not be caused; and sites should be remediated when the activities come to an end.

The Directive also creates permitting conditions, rules on environmental inspections, access to information and public participation in the permit procedures and access to justice.

In the “best available techniques”, the emphasis is placed on pollution prevention techniques rather than end-of-pipe treatment. The Directive requires the use of advanced technologies, the use of low-waste technology and the use of less hazardous substances, as well as the recovery and recycling of substances. The energy sector uses a range of different combustion systems, techniques and fuels. However, emissions to air carry the most significant risks to the environment and health in the sector. The emission of transboundary air pollutants - mainly by combustion installations - has impacts at global, regional and local levels. The energy sector impacts the environment not only through emissions, but also by the consumption of natural resources. Thus, environmental impacts can be somewhat reduced by increasing the efficiency of energy production, particularly during fuel storage and handling or combustion of solid and liquid fuels. The Directive requires innovation and decreases the possible gap in technology between the EU and the Contracting Parties, thus helping to prevent a “race to the bottom” between states.

The Directive is crucial for Energy Community countries, because investments made now will lock in the energy sector for several decades to come, so it is crucial that the standards are the highest possible. The best available techniques in energy sector would also minimize local, long-distance and transboundary pollution. The implementation of Chapter II of the Directive will also strengthen the rule of law by ensuring public participation in the permitting process. Thus, the provisions of the Chapter II of the Directive should be an essential part of the Energy Community Treaty.

Directive 2008/50/EC of the European Parliament and of the Council of 21 May 2008 on ambient air quality and cleaner air for Europe

Directive 2008/50/EC on ambient air quality and cleaner air for Europe is designed to avoid, prevent or reduce harmful effects on human health and the environment as a whole. It sets legally binding limits and targets for concentrations of major air pollutants: sulphur dioxide, nitrogen dioxide and oxides of nitrogen, lead, benzene, carbon monoxide, and ozone in outdoor air. Moreover, in order to help combat air pollution and nuisance, the Directive sets out measures for the assessment of ambient air quality and methods of obtaining information on ambient air quality. Due to the fact that air pollution mainly comes from the emission of gases such as carbon dioxide, nitrogen oxides, and sulphur dioxide, the Directive has a positive influence on the energy sector, especially on coal. **The energy sector contributes greatly to overall air pollution, because emissions are released through the entire spectrum of energy activities, from upstream emissions during fossil fuel extraction and production to end-use emissions.**

The Directive is important for Contracting Parties because it helps to achieve better cooperation between states in reducing air pollution, which undoubtedly has a transnational character. Secondly, it stipulates common methods for assessing air quality and ensuring that information on ambient air quality is made available to the public. It is important on a regional level, because it regulates standards for the combustion of coal, which is the main reason for the air pollution in places like Pristina, Tuzla and Pljevlja.

The Directive consists of six chapters, all of which should be included in the Energy Community Treaty. This will reduce the harmful effects of energy production on human health and the environment and develop the rule of law through dissemination of information on air quality and ensuring public participation in creating air quality plans.

Directive 2008/105/EC of the European Parliament and of the Council of 16 December 2008 on environmental quality standards in the field of water policy

Directive 2008/105/EC on environmental quality standards in the field of water policy, also known as the Priority Substances Directive, sets environmental quality standards for substances in surface waters (rivers, lakes, transitional and coastal waters). It establishes limits on concentrations in surface waters of 33 priority substances and 8 other pollutants, including cadmium, lead, mercury, nickel and its compounds, benzene, polycyclic aromatic hydrocarbons (PAH) and Total DDT. The Directive also requires the establishment of an inventory of emissions, discharges and losses of forbidden substances.

One of the main threats to water quality is from chemical substances, most of which are emitted by the energy sector. The impact of

power plant operation on water quality, including impacts on fish and other aquatic life by cooling water intakes, thermal impacts of heated water discharge, and pollution from power plant effluent as well as impacts of fossil-fuel production, such as the water pollution hazards created by coal mining should be minimized. Coal-fired plants produce vast amounts of fly ash combustion residuals, which contain heavy metals and radioactive material, while surface mining gives rise to water pollution when coal with high sulphur content and other impurities is exposed to air and water.

The Directive requires the achievement of good chemical status and no deterioration of water quality, but leaves the states flexibility as to how they achieve them. The Directive reduces the costs of treating drinking water and improves the quality of waterborne organisms and livestock drinking water.

Control over chemical emissions is hampered by the limited amount of available information. The Directive helps to build a system of information exchange and strengthens the cooperation between Contracting Parties of Energy Community. Since the objective of this Directive, namely that of achieving of good surface water chemical status, cannot be sufficiently achieved by single states and can be better achieved at Energy Community level, the Directive should be an essential part of the Energy Community Treaty.

The Directive is especially important to Energy Community countries, because all of them are Contracting Parties to the Ramsar Convention on Wetlands signed in 1971.

Directive 2006/21/EC of the European Parliament and of the Council of 15 March 2006 on the management of waste from extractive industries and amending Directive 2004/35/EC - Statement by the European Parliament, the Council and the Commission

Directive 2006/21/EC on the management of waste from extractive industries applies to waste resulting from the extraction, treatment and storage of mineral resources and the working of quarries. This particular extractive waste must be managed in specialized facilities in compliance with specific rules in order to limit risks to public health and the environment, inter alia by applying the concept of “best available techniques”. According to the Directive no extractive industry waste facility may operate without a permit issued by the competent authorities. The public must be informed about requests for permits, which gives the opportunity for the public to participate in the assessment procedure for authorization requests and increases public buy-in and acceptance of such facilities.

The Directive is especially important in the long-term perspective, e.g. in deciding on locations of new investments, because it requires the sustainability of location of facilities. Facilities must be insured and soil, air and water pollution prevented, and they must be monitored and inspected by competent persons. Moreover, arrangements must be made for the closure of the facility, the

rehabilitation of the land and the post-closure phase. The Directive ensures an appropriate exchange of scientific and technical information on how to carry out an inventory of closed waste facilities at Member State level. It also ensures the exchange of information within and between states on the best available techniques.

Directive 2006/21/EC is clearly relevant to mining related to the energy sector in the Energy Community countries, which have already left significant legacy damage. It is necessary to lay down minimum requirements in order to prevent or reduce as far as possible any adverse effects on the environment or on human health, which are brought about as a result of the management of waste from the mining industry. The Directive would strengthen also the rule of law principle and increase public buy-in by ensuring public participation in the permit issuance procedure.

Due to the fact that mismanagement of such waste may cause transboundary pollution, the Directive can help to ensure a minimum level of safe and responsible management and waste recovery throughout the region, which cannot be achieved by Contracting Parties acting alone.

Under the polluter pays principle it is necessary, *inter alia*, to take into account any damage to the environment caused by waste from the energy sector, and different national applications of that principle may lead to substantial disparities in the financial burden on economic operators. Moreover, the existence of different national policies on extractive industry waste management hampers the aim of ensuring a minimum level of safe and responsible management of such waste and maximising its recovery throughout the Energy Community. Therefore, by reason of the scale and effects of this Directive, its objective can be better achieved at the Energy Community level than by waiting for country-by-country adoption during EU accession.

Directive 2000/60/EC of the European Parliament and of the Council of 23 October 2000 establishing a framework for Community action in the field of water policy

The Directive 2000/60/EC aims to achieve good ecological and chemical status of surface freshwater (lakes, streams and rivers), groundwaters, groundwater dependent ecosystems, estuaries and coastal waters out to one mile from low-water. **The Directive has an important influence on the energy sector, because water plays a crucial role not only in hydropower production, but also in extraction, cooling and processing in coal power.** Undoubtedly, the energy sector has significant impacts on the quality and health of water bodies, notably: biological, ecological and chemical status, water temperature, flow regime, hydromorphological alterations. The Directive identifies the priority substances and obliges states to monitor the level of those substances and to achieve good status of water quality. It also requires the non-deterioration of water bodies' status.

Chemical pollution of surface water presents a threat to the aquatic environment with the effects such as acute and chronic toxicity to aquatic organisms, accumulation in the ecosystem and losses of habitats and biodiversity, as well as a threat to human health.

The reduction of water pollution levels would bring several direct economic benefits to the Energy Community's Contracting Parties:

- Reducing treatment costs for major water users, in particular drinking water and process water for industry.
- Cleaner sediment in water treatment plants, which will reduce inputs of harmful substances and hence cheaper management of waste. Triggering the development and commercialization of environmental friendly technologies.
- Improving the quality of fish, which is particularly important in the fishing industry. Cleaner water will improve productivity and reduce the accumulation of dangerous substances in fish tissue, thereby reducing human exposure to hazardous substances.

Additionally, the Directive will bring several environmental and social benefits, e.g. protection of biodiversity, improved amenity value, reduced exposure during water activities, etc.

Directive 92/43/EEC of 21 May 1992 on the conservation of natural habitats and of wild fauna and flora

Directive 92/43/EEC on the conservation of natural habitats and of wild fauna and flora, known as the Habitats Directive, was designed to help maintain biodiversity by defining a common framework for the conservation of wild plants and animals and habitats of Community interest. The main part of the Directive is establishing the NATURA 2000 network, which is the largest ecological network in the world and represents around 18 % of the European Union's terrestrial territory. Special areas of conservation and special protection areas have been designated by Member States, whose aim is to protect the habitats and species listed in Annexes of the Directive. States must take all necessary measures to guarantee the conservation of habitats in special areas of conservation, and to avoid their deterioration and the significant disturbance of species. Especially, the Member States should encourage the management of features of the landscape which are essential for the migration, dispersal and genetic exchange of wild species; establish systems of strict protection for those animal and plant species which are particularly threatened and study the desirability of reintroducing those species in their territory; prohibit the use of non-selective methods of taking, capturing or killing certain animal and plant species.

The Directive is the most important part of EU nature conservation policy. The preservation, protection and improvement of the quality of the environment, including the conservation of natural habitats and of wild fauna and flora, are an essential objective of general interest pursued by the European Union. Unfortunately, natural habitats are continuing to deteriorate and an increasing

number of wild species are seriously threatened, including by poorly-sited energy facilities such as hydropower plants, thermal power plants and wind farms. As the threats habitats and species are often of a transboundary nature, it is necessary to take measures at regional level in order to conserve them. **For the energy sector, the Directive is especially important in land-use planning and development policies.** In view of the threats to certain types of natural habitat and certain species, it is necessary to introduce the Directive into the Energy Community Treaty at an early stage.

The Directive plays a significant role in energy investments, particularly in the thermalpower, hydropower or wind sectors, which can have a serious impact on natural habitats, flora and fauna. The provisions of the Directive ensure that energy installations are not built at the expense of the natural value of the region. Poor siting of energy investments can cause irreversible changes in natural environment and increase public opposition, legal challenges and therefore project costs, and therefore, the principles of the Directive should be a key element of the Energy Community Treaty.

3. IMPLEMENTATION

The effective enforcement of the Energy Community *acquis* is crucial for the proper functioning of the Energy Community. Contracting Parties' compliance with the *acquis* must be assessed not only on the basis of transposition of the *acquis* into their national legislation but also on the basis of effective implementation. The existing enforcement mechanism does not fulfill its role and should be strengthened by enhancement of the dispute settlement mechanism as well as democratization of the decision-making processes. The Energy Community's role should be enhanced in this direction so it can identify problems regarding implementation. The Energy Community should have at its disposal suitable tools to ensure that transposition and implementation deadlines are met.

a. Aligning with the European Union

The Energy Community needs to send a very strong and clear message to its members about Europe's future goals. Setting defined goals and ambitions with equal rules that ensure sustainable market development will guarantee that all members compete on a level playing field. We would like to point out the necessity of regulatory framework that ensures creation of a single energy market encompassing both the EU and the Energy Community. **Creating a situation where the regulatory framework sets different obligatory rules for its members is a conflict "double-edged sword" situation that might disturb the path towards a level playing field or even result in electricity market distortion.**

Improvement of the environmental state in relation to energy issues means incorporating the environmental *acquis* and the goals of the EU environmental policy in the region. The current situation, in which only a small portion of the *acquis* has been adopted by the Energy Community countries mean that there is a danger of "emissions leakage"¹⁶ or "energy grabbing"¹⁷.

16. Some of the energy from planned coal power plants is planned for export to the EU rather than used for domestic consumption eg. Burshtyn, Dobrotvir (UKR); Pljevlja II (Montenegro)
17. Italy plans, through its Renewable Energy Action Plan, to import from Albania no less than 2/3 of the amount of electricity generated annually in Albania in 2009, along with smaller amounts from Montenegro, Bosnia and Herzegovina and Serbia.

In the Western Balkans countries and even in some new EU member states, legislation implementation failures and lack of investment are linked with dysfunctional governance and structural flaws in decision-making, as well as an abundance of corruption, and these urgently need to be addressed. In order to overcome this situation Energy Community needs to address these issues with clear regulatory rules that reflect the main goal of the Energy Community itself – creating wider European stable and regulatory market framework. Also, there are tangible problems with investments, mostly related to poor planning and overly high levels of ambition. The Energy Community could assist more with is ensuring that its Contracting Parties develop realistic energy strategies with realistic demand projections, that take into account current and future EU obligations and are properly publicly consulted. The Energy Community may also be able to play a role in doing a reality check of governments’ expectations about becoming energy exporters or energy hubs. It is often said that it is up to the Contracting Parties to decide on their energy mix, but at the same time they have committed to renewables targets and need to keep decarbonisation in mind when doing energy planning. This can be achieved if the EU targets 2020; 2030 and 2050 are also the targets of the Energy Community parties.

b. Institutional changes (openness of the Energy Community bodies, increasing the Secretariat’s capacity)

“An empowered civil society is a crucial component of any democratic system and is an asset in itself. It represents and fosters pluralism and can contribute to more effective policies, equitable and sustainable development and inclusive growth. It is an important player in fostering peace and in conflict resolution. By articulating citizens’ concerns, civil society organisations (CSOs) are active in the public arena, engaging in initiatives to further participatory democracy. They embody a growing demand for transparent and accountable governance. While states carry the primary responsibility for development and democratic governance, synergies between states and CSOs can help overcome challenges of poverty, widening inequalities, social exclusion and unsustainable development. CSOs’ participation in policy processes is a key for ensuring inclusive and effective policies. CSOs therefore contribute to building more accountable and legitimate states, leading to enhanced social cohesion and more open and deeper democracies.”¹⁸

The formal inclusion of CSO as non-voting representatives in the institutions of the Energy Community would lead to better understanding by citizens of its decisions as well as ensuring openness and transparency of procedures and public participation. It would also follow the path of openness and transparency established by the EU through its common practice of including NGOs representatives in other high-level bodies.

18. “The roots of democracy and sustainable development: Europe’s engagement with Civil Society in external relations” – Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions (2012)

Moreover the Energy Community should commit to full transparency in terms of publishing reports, strategies and analysis *before* decisions are made based on them. Publicizing clear and concise annual balance score cards for each signatory party would also help to identify where members stand in terms of their commitments to the Treaty obligations.

There is also a need to increase the Secretariat's capacity to monitor and enforce existing commitments by equipping it with strong investigative and decision-making powers regarding: introducing reporting obligations of the Contracting parties regarding the transposition and implementation of the *acquis*; introducing automatic opening of dispute settlement mechanism procedures in cases when the *acquis* is not transposed in a timely manner; linking the fulfilling of the obligations deriving from Energy Community Treaty with the accession process; strengthening the consequences of non-compliance by introducing financial penalties and linking bilateral financial assistance to the respect of commitments under the Energy Community Treaty.

c. Financial and technical assistance

The Energy Community should support countries with their energy strategies, bearing in mind long-term EU climate and energy goals, in order to ensure that only appropriate investments leading to decarbonisation and the sustainable use of renewable resources are encouraged. This can be done through coordination of technical assistance/grants from EU governments and the EBRD to make sure the studies and consequent energy strategies are conducted professionally and to increase public participation in their preparation.

Incentives for the implementation of the *acquis* should be introduced through conditioning of disbursement of EU funds and facilities on compliance. Moreover, it is crucial not to just promote investments per se, but carefully chosen ones. This means that the Energy Community needs to have increased monitoring and enforcement capacity to ensure that countries' investments do not infringe the EU *acquis* or risk being regrettable in the medium-long term.

The Energy Community has attempted to link the implementation of the *acquis* to the PECIS' projects by stating that if the PECIS are found to be infringing the *acquis*, they can be removed from the list. One additional principle that could be adopted is that the Energy Community should not lend its support to any new generation projects unless the host country is on track to meet its energy efficiency targets. As for indicators for success in investment, an important prerequisite must be a project's inclusion in a good-quality energy strategy, which is in line with EU legislation and short- and long-term policies (eg. 2050 targets) and which is based on realistic demand scenarios.

d. Dispute settlement mechanism (court issue)

If the existing dispute settlement mechanism is strengthened by establishing a Court of Justice, to enhance the current rather ineffectual dispute settlement mechanism, we would insist – without prejudice to the above - that any such Court should be founded upon the principles of:

- Impartiality – the majority of judges should come from countries outside the region and represent the highest level of competence
- Comprehensiveness – the whole legal framework ie. all parts of the Treaty should be treated with the same level of importance
- Openness - access to justice and participation of civil society representatives within the court proceedings should be assured

A Court of Justice, if it is established, should ensure that Contracting Parties comply with the Energy Community acquis within infringement procedures regarding acts of omission, violation of Energy Community law and non- or inadequate transposition/implementation of the acquis. It should also settle questions of interpretation the Energy Community acquis rules to make sure that they are understood and applied in the same way in all Contracting Parties and ensure that the Energy Community bodies do not act illegally.

