

Standard Summary Project Fiche

Project Number LI 9910.01

1. Title

Transposition, implementation and enforcement of the Energy *Acquis*

2. Geographical Location

Ministry of Economy, Energy Agency, JSC Lithuanian Energy, and JSC Lithuanian Gas

3. Objectives

The objective of this **3.25 MEUR twinning and investment project** is to assist in the modernisation of the Ministry of Economy's Energy Agency and the two major energy utilities (JSC Lithuanian Energy and JSC Lithuanian Gas) by ensuring that a policy, regulatory and monitoring system is in place with a legal foundation based upon EC requirements.

The specific objective for the Ministry of Economy is to ensure that the policy and legal basis for the regulation of the energy sector is in place. Particular attention will be paid to three critical and strategic areas:

- Review the transposition of energy directives into Lithuanian legislation and the government's policy, technical criteria and strategies to implement the directives, with special attention being paid to establishing the operational mandate for the utility companies;
- Setting the legal and technical criteria and ensuring that the supervision and regulatory authority has adequate powers and authority; and
- Establishing the policy, legal framework, procedures and systems for establishing compulsory oil stocks (COS) and oil crisis management (OCM).

The need for COS and OCM is demonstrated by the following information: Lithuania's annual consumption of primary energy resources is about 9 Mtoe, including 3.5 Mtoe of oil. Indigenous oil resources are very scarce, with only 0.2Mt production per year. The country's economy is fully dependent on imported oil and oil products. Approximately 90% of oil and oil products are imported from Russia and some other countries of the CIS. To ensure stable and reliable energy production and energy resources supply Lithuania is seeking to form stocks of oil products. Stocks available at the moment are very small. This component will build on the transformation process of EC directives and develop policy and an implementation strategy for oil crisis management. It will include the following activities, assisting in the preparation of:

- Legal basis in compliance with the EC requirements to have 90 days oil products stocks;
- System of information collection, processing and supply to the EC and IEA related to compulsory oil stocks (COS); and
- System for oil crisis management (OCM).

The specific objective for the two energy utilities is to develop strategies to implement government's mandate, policy and technical criteria established during the first twinning component. These strategies will be supplemented by the development of western management techniques and information systems. This process will include establishing management information criteria for decision making and the unbundling of the accounts of the two utilities, to achieve this objective, a number of specific activities are planned:

- Develop management criteria and information systems to help control the performance and efficiency of the Lithuanian Utilities. It will also satisfy the European Union directives' requirements for unbundling the accountancy of their businesses while complying with the Lithuanian Laws and International Accounting Standards.
- Position Lithuanian Utilities to successfully meet the ongoing requirements for reporting by activities, in order to identify the actions required to improve results, providing the following:
 - Financial information by major cost centres.
 - Balance sheets, statements of operations and cash flows per activity.
 - Statements of operations and cash flows per operational unit.
- Permit Lithuanian Utilities to identify critical management performance criteria, through the development of Management Information Systems (MIS) and associated training. These MIS will also properly allocate all costs and revenues to their activities through the establishment of the appropriate parameters and criteria.

4. Institutional Framework

Ministry of Economy

The Ministry of Economy is responsible for the implementation of the *Acquis* in Energy sector. In the process of integration with the EU, Lithuania is seeking to meet harmonisation requirements, as required by the Directives 98/30/EC and 96/92/EC concerning common rules for the internal market in gas and electricity sectors. The legal obligation to maintain oil reserves is recorded in the Energy Law of the Republic of Lithuania No. I-828 adopted on 28 February 1995. Certain aspects were also transposed by the Law on ensuring strategic interest of the State under emergency situation in providing the country's economy with oil and oil products No. VIII-229, adopted on 29 May 1995. The requirements of the Directives 68/414/EEC, 68/416/EEC, 72/425/EEC need further transposition into the national legislation.

The Ministry's priority is to align its legislation, regulatory and institutional framework to become EC-compliant. The most important legislation in relation to the energy utilities is the Energy Law, which is being reviewed with assistance from the 1997 Phare programme and will lead to the establishment of an independent power sector regulator. The existing law was passed in 1995 and it establishes a regulatory framework for the electricity, heat, petroleum and gas industries in the Republic of Lithuania. Pursuant to current legislation, the Ministry of Economy executes regulatory powers in developing the energy sector. The Law on Energy prescribes that rates for energy are based on costs of fuel, generation and transportation of energy. The Law does not establish a special methodology for determining electricity prices. The transposition of the Electricity and Gas Directives has also begun and is being supported by the 1998 Phare programme and will be reviewed during this twinning programme.

The draft law on State Reserves is under development by the Ministry; this draft law will need amendments to achieve full compliance with the Directives' requirements and this will be provided by this twinning project. The Ministry's Energy Resources Department has prepared the necessary institutional structures and framework to introduce COS and OCM. In the process of integration in the EU, Lithuania is seeking to make oil products reserves equal to 90 days consumption, as required by the Directives 68/414/EEC, 68/416/EEC, 72/425/EEC and foreseen in Lithuania's NPAA. Regulation procedures of oil stocks available are not in line with these directives and with the Agreement on an International Energy Programme (AIEP). A summary of the main responsibilities and tasks of the Energy Resources department is given in Annex 9 and its organisation chart and staffing in Annex 8.

State Commission for the Control of Prices of Energy Resources and Energy Activities

A State Commission for the Control of Prices of Energy Resources and Energy Activities (the “Commission”) approves retail energy rates following discussions with the respective utilities and is in effect the energy Regulatory Authority. The Minister of Economy must approve their Board of Directors requests for change in retail energy rates, prior to submission to the Commission. The Commission, established in 1996, also deals with Lithuania’s state investment strategies in the utilities sector and with establishing a methodology for rate setting. The Commission is designated as the permanent regulatory authority under the supervision of the President of Lithuania. The President of Lithuania appoints the Commission’s five members for a five-year period. The role of this regulatory authority will be reviewed during this twinning programme, recommendations will be made to ensure its independence, and that it operates effectively. The current Phare funded review may see the Commission given more responsibilities and powers.

Energy utilities

An overview of the structures and activities of the two energy utilities Lietuvos Energija (Electricity), and Lietuvos Dujos (Gas) is given in the following paragraphs and then there is a discussion of the scope of the twinning support to them. Organisation charts are appended in Annex 8.

Lietuvos Energija was established in 1995 and the company is made up of shareholders (86% Government owned), and employs 11,500 people. The activities of the company are divided amongst four main power plants, seven electricity utility (transmission, distribution and delivery) companies and eight service and construction subsidiaries. 58% staff are employed in the utilities, 20% in the subsidiaries, 18% in production, and 4% in administration.

Generation of electricity is mainly supplied from the Ignalina Power Plant (over 80% of supply) with 8% supplied from two heat and power plants, and a small percentage coming from the two hydro-power plants. The company is also involved in some ten associated companies with diverse range of activities covering geothermal power, power maintenance in Lithuania, Latvia and Kaliningrad, energy conservation, electricity meter repair, construction and health complexes.

The company has a substantial investment programme including measures designed to reduce the environmental impact from conventional power plants, reconstruction of transmission lines, upgrading the distribution network, upgrading power plants and improving the telecommunication and dispatch control systems.

Immediately after the restoration of the country’s independence in 1990 the Lithuanian Government recognised that the utilities were one of the major strategic industries in Lithuania. There was a need to restructure the industry to make it more efficient, environment-protecting, and operating in line with the main EC directives applicable for the industry. As part of the Lithuanian Government accession programme Lietuvos Energija is being restructured; for example there are several alternative proposals to rationalise the company’s distribution network. The preferred structure should be implemented this year, following Government approval, and would allow a rational reorganisation based upon EU experience of the whole management structure, its strategies and procedures.

The company is also currently undertaking a Phare management audit project, which aims to better position the company to commercial environment and improve its efficiency and effectiveness. The desirable outcome of this project would be detailed analysis of its accounting systems and unbundling of accounting and management through the respective business areas (generation and transmission).

The power systems of the Baltic States were developed as part of the bulk Unified Power system of the former Soviet Union; despite this unified system there are some problems for autonomous

operation of Estonian, Latvian and Lithuanian power systems. All these systems are strongly integrated and are dependent on CIS. However, no power system in the Baltic States meets the requirement of a control area because it cannot directly control its generation and continuously balance its interchange nor can it regulate and stabilise the interconnection's alternating frequency. The Baltic's 330 kV grid is a part of a large high voltage network loop that goes from Estonia via St. Petersburg, Moscow and Smolensk in Russia, then Belarus and through Lithuania into Latvia. The Baltic power systems thus operate interconnected with the CIS system with the frequency regulation continuing to be the responsibility of the Central Dispatch Office in Moscow.

The creation of common power grid is an opportunity for the regional co-operation in the Baltic electricity market. However, there is a need to establish a common transmission system operator, harmonised grid codes and another legal documents for this common grid to work efficiently and effectively.

Lietuvos Dujos was established in 1995 and the company is made up of shareholders (92% Government owned), the Board, Management with four administration departments and finally four branch operations. The four administration departments with their divisional responsibilities are:

- Economics Department (Economics, finance and bookkeeping)
- Technical Department (gas system maintenance & technology, and information)
- Commerce Department (gas flow management, sales and trade)
- Construction Department (gas system development & construction and procurement)

There are also legal and personnel, audit and training divisions.

The four branch operations cover gas transmission, distribution (seven companies), liquid petroleum gas (LPG) production, distribution, and production of gas equipment.

The company employs over 4,000 in the various departments and operations, of which nearly 60% are employed in distribution, 30% in the LPG sector, 9% in transmission, only 2% at headquarters and 1% in producing equipment.

The Government has regulated prices since independence and since 1997 the company has been allowed to set prices in conjunction with the Commission. The company has developed two key policies to help position the company more competitively; the first covers expansion of the supply network, and this involves building new high-pressure transmission pipelines. The second policy is of a more technical nature concentrating on improving the reliability and safety of the gas supply. The elements of this policy include an inspection, repair and modernisation programme, establishing codes and standards, upgrading the metering system and improving customer service.

Preparing for the transposition of EC Directives

Directives and regulations operative in the European Union encourage electricity and gas vertically integrated companies to analyse the cost elements and revenue generation for each line of business. Subsequently, the two Lithuanian utility companies have been encouraged to unbundle and separate their operations into generation (where applicable), transmission and transportation and distribution businesses, with the objective to develop their businesses through an operational and accountancy differentiation of these activities. This is a particular challenge to the Lithuanian Utilities as they are intensively vertically integrated companies. In preparation for future root and branch reorganisation there is a need to enhance their current reporting process through unbundling the financial and operational information of their businesses in order to generate unbundled financial statements for each of the activities and provide management with a useful tool for the decision making process.

The EC Directives calls for price transparency, and non-discriminatory formation of internal markets. Recognising the need to comply with these directives the Lithuanian Government stresses that the most important tasks for the industry in this respect are accounts and management,

unbundling and transparent pricing system. In the process of integration with the EU, Lithuania is seeking to meet harmonisation requirements, as required by Directives concerning common rules for the internal markets.

To assist in this reorganisation, both utility companies are in process of implementation of SCALA accounting system. Both companies have management audit projects sponsored by Phare. These projects aim to better position companies to commercial environment and improve their efficiency and effectiveness. The desirable outcome of this project would be detailed analysis of their accounting systems and unbundling of accounting through the respective business areas.

5. Description

This twinning project will consist of three distinct, but strategically related components:

- Policy and Regulatory support to the Ministry of Economy, particularly in establishing the operational mandate for the energy utilities and define a policy and strategy for compulsory oil stocks (COS) and oil crisis management (OCM);
- Restructuring of Lietuvos Energija (JSC Lithuanian Energy) through the introduction and development management techniques, specific management information criteria for decision making and the development of tailored management information system (MIS), including accounts unbundling software;
- Restructuring of Lietuvos Dujos (JSC Lithuanian Gas) through the introduction and development of modern management techniques, specific management information criteria for decision making and the development of tailored MIS, including accounts unbundling software.

In support of these twinning initiatives a limited amount of equipment and local software development expertise will be procured, following normal DIS procedures, to support the development of the management information and accounting systems and the OCM information system. A description of the details of these projects is given in the following sections.

Policy and Regulatory support to the Ministry of Economy

- A Pre Accession Adviser (PAA-A) will provide policy and strategic advice to senior officials of the Ministry of Economy and its Energy Agency. The PAA-A will take responsibility for assisting the Ministry to setting the mandate for the energy utilities, he/she will also liaise and co-ordinate the activities of various short-term advisers (STAs) and liaise with the PAAs in the two energy utilities. This policy and strategic advice will focus on the implementation the requirements of EC Directives in the electricity and gas sectors. The issues that need to be addressed include, *inter alia*: energy sector regulation principles, legislation, and management. The PAA-A will also assist the Ministry in defining the operation environment of the energy utilities' activities and ensuring their managerial independence.
- Another adviser, PAA-B is expected to focus on COS and OCM and prepare the specifications, tender documents and participate in the evaluation for the procurement of equipment and software development services.
- There are seven STAs providing specific inputs; the four key ones will provide support to the general policy and legislation, transposition of the Electricity and Gas Directives and reviewing heating and combined heat and power (CHP) policy and legislation. The remaining STAs will provide support to the system analysis and the development of OCM information system.

The indicative inputs from the PAAs and STAs will cover the following stages, activities summarised in the table below, and each activity is described in subsequent paragraphs.

Title	Area/activities	Duration
PAA-A	Establish utility mandate, legal & regulatory advice & co-ordination	12
PAA-B	COS and OCM	12
STA-C	Electricity directive, policy & regulation	6
STA-D	Gas directive, policy & regulation	6
STA-E	OCM systems analysis	3
STA-F	OCM systems development	6
STA-G	Training	6
STA-H	Heating/CHP policy & legislation	6

General Policy, Co-ordination and Strategic Advice

There are two current projects focusing on the transposition of the electricity and gas directives into Lithuanian laws and regulations, they also are reviewing and preparing the basis for an energy regulation authority, energy policy and introduction of new legislation. PAA-A will build on these activities by assisting the Ministry in establishing the mandates for the energy utilities, with the view to ensuring their future managerial independence; this is a prerequisite to the provision of twinning assistance to the two energy utility companies. The PAA-A will also be responsible for co-ordinating the whole twinning programme in the sector. The legislation should be in place by the end of 1999; therefore, the PAAs and the specialist STAs will be responsible for reviewing, and developing where necessary, the legislation, government policy and their implementation and enforcement strategies. In addition, attention will need to be paid to the development of a heating/CHP policy. The PAA-A's specific activities will include assistance to the Ministry of Economy on the following issues:

- Assistance in drafting and preparing for implementation of new legislation for electricity and gas sectors following the EC Energy Acquis;
 - Assistance in defining the energy market regulation principles and methods, improving operation of the market regulators;
 - Assistance when drafting restructuring and reorganization programmes for the energy utilities;
 - Assistance for improvement of principles for the financial securing of the investment and operational programmes for the energy utilities;
 - Assistance in representing State capital interests in management of the energy enterprises;
- Assistance in updating of the National Energy Strategy and implementation of issues related to the introduction of the energy market aspects.

Preparation of a legal basis for COS and OCM

The existing legal basis for COS and OCM does not comply with the requirements of the EC and AIEP and are insufficient to cover these issues. The existing legal basis needs to be revised and a new one prepared; PAA-B will assist in the process. This part can further be subdivided into the following components:

- *Revision of the existing legal basis:* The Energy Law, Law on National Stocks and governmental decisions regarding Compulsory Oil Stocks (COS) and Oil Crisis Management (OCM) should be revised in order to identify those provisions which are not in line with the requirements of the EC and of the Agreement on an International Energy Programme (AIEP).
- *Preparation of a model legal basis for the regulation of COS and OCM:* On the basis of related legal acts and taking into account Lithuania's legal system and experience of the EU member

states recommendations should be made on what laws and legal acts governing COS and OCM have to be prepared.

- *Preparation of new legal acts and amendments to the existing ones:* Based on conclusions concerning activities of above new legal acts governing COS and OCM (laws and governmental decisions) need to be prepared and/or amendments to the existing ones made so they meet the requirements of the EC and IEA. Responsible institutions, information channels and responsibilities of companies should also be identified.

Preparation of a system of COS information collection, processing and supply to the EC and IEA:

The existing legal acts of Lithuania do not provide for collection and processing of efficient information on oil products stocks and consumption. The Department of Statistics collects and processes this information on a yearly basis, whereas the EC and IEA require it to be done on a monthly basis. Legal provisions to collect and process this information as well as the appointment of responsible institutions should be developed and the PAA-B will assist in this process. This part of the project should include:

- *Preparation of table/report forms:* Table/report forms need to be prepared for companies in charge of the accumulation and storage of COS to provide information on available stocks to a responsible institution. Besides, table/report forms should be prepared to provide information on COS to the EC, IEA and other related institutions.
- *Preparation of information processing software:* For the processing of information referred to the activity above, all necessary software should be arranged, including preparation of the ToR and software as well as installation and adjustment. Further maintenance of software should be ensured. Software explanatory notes should be given in the Lithuanian language. A software manual has to be prepared.
- *Specialist training:* A specialist group should be set up to undergo training in information collection and processing. After software referred to above is prepared specialists need to receive training to be able to work with it. A full-scale training is required so people were able to work on their own.
- *Hardware purchase:* To ensure full operation of the information system corresponding hardware needs to be purchased. All users should be equipped with hardware. The number of users should be identified when preparing the second phase of the project.

Oil crisis management.

A legal basis for oil crisis management should be prepared in the first phase of the project with the assistance of the PAA-B. During this phase attention should be given to the preparation of practical processes of OCM and readiness to manage oil crises. This part of the project should include:

- *Preparation of OCM procedures:* In this phase practical procedures for OCM should be worked out, including their implementation stages and concrete measures; besides, responsible institutions should be appointed and plans for each stage of OCM prepared. The number of specialists to undertake permanent jobs in this stage has to be identified.
- *Software preparation:* For the implementation of OCM procedures foreseen above, corresponding computer software needs to be prepared allowing for information processing and output. The ToR for software and the volume of software will be defined during the process of work. Software notes should be in the Lithuanian language. Further maintenance has to be ensured and a software manual prepared.
- *Staff training:* A specialist group is needed for oil crisis management. After responsible institutions and the required number of specialists are identified, specialists should receive training in making oil market analysis, crisis forecasts, and information collection and processing. A training programme should include co-operation procedures with relevant institutions of the EC and IEA. A visit to relevant institutions of the EC and IEA responsible

for OCM is required to receive first-hand and practical knowledge about their work as well as to establish relations.

- *Hardware purchase:* All users should be equipped with hardware that meets the requirements of software installation. Therefore sufficient computer hardware and off-the-shelf software will need to be purchased at the beginning of the project to allow the development of the pilot unbundling system. The State budget will fund the purchase of necessary hardware for the roll-out of the system to the branches and regional offices, as dictated by the Ministry's Information Strategy.
- *Software development put out to local tender:* Bespoke software will need to be developed for the pilot unbundling system; a local tender will be launched to recruit a suitable software house. The State budget will fund rollout, maintenance and training of the system according to Ministry's Information Strategy.

The services and support provided by the PAAs and STAs will be accompanied by the procurement of software services for the analysis development of the OCM information system, by the provision of associated translation and interpretation services and by the procurement of software and hardware to support the PAA and STAs and the development of the pilot OCM information system (3 local tenders as part of the twinning component).

Restructuring of Lietuvos Energija (JSC Lithuanian Energy)

EC Directives call for electricity price transparency, and non-discriminatory formation of internal electricity markets. Recognising the need to comply with these directives the Lithuanian Government stresses that the most important tasks for the electricity industry in this respect are accounts, management unbundling, and transparent pricing system. In the process of integration in the EU, Lithuania is seeking to meet harmonisation requirements, as required by the Directive 96/92/EC concerning common rules for the internal market in electricity.

This twinning assignment will assist management to analyse possible alternatives of responding to the Ministry's implementation of the EC Electricity directive. It will also help develop management and staff capacity and integrate Lietuvos Energija's electronic data processing (EDP) and accounting systems into a Management Information System (MIS). The assistance will work closely with management to prepare recommendations and implement the procedures needed to enable Lietuvos Energija to:

- Determine certain directions of reorganising internal market of electricity.
- Participate in creating the integrated energy market of the three Baltic States with interconnection to European energy market.
- Satisfy the European Union directives for unbundling the accountancy of their businesses while complying with the Lithuanian Laws and International Accounting Standards.
- Meet the ongoing requirements for reporting by activities, in order to identify the actions required to improve results, providing financial information by major cost centres, balance sheets, statements of operations and cash flows per activity and statements of operations and cash flows per operational unit.
- Identify and properly allocate all costs and revenues to their activities through the establishment of the appropriate parameters and criteria.

A Pre Accession Adviser (PAA-I) will provide policy and strategic advice to senior management of Lithuanian Energy over a two-year period with at least 20 person-month input. The PAA-I should place particular emphasis on the Electricity directives and their relevance to the company and dispatching issues and the introduction of accounting and management reforms. The PAA-I will also have responsibility to assist in advancing general management, staff development and accounting functions within the company, putting together a human resource development

programme with the assistance of the company training department and short term inputs (STA-N). The PAA-I will also liaise and co-ordinate the activities of various short term advisers (STAs) and prepare the specifications, tender documents and participate in the evaluation for the procurement of equipment and software development services for the Management Information System.

Another PAA-J will be responsible for the advising the company on the technical implications of the company's operation of the electricity network and reorganisation along resolving issues of maintenance and regional co-operation. It is expected that the adviser would have considerable experience from a career in a Member State Power Company.

The PAAs and the team of STAs will be expected to work towards the following guaranteed outputs:

- Design and implementation of the separate accountancy management system for each Business Unit complying with the Lithuanian Laws and International Accounting Standards feeding into the company MIS.
- Prepare regulations and perform structural changes, enabling the organisation of company's activities in accordance with EC standards.
- Improve reporting by activities on: financial information by major costs, balances sheets statements of operations and cash flows per activity and statements of operations and cash flows per operational unit.
- Practical procedures for company management in market conditions.
- Specialised software for company accounts management.
- Training for specialist involved in company and companies accounts management. The necessary computer hardware, telecommunication systems and equipment for physical security purchased under the separate investment project and installed.

The PAAs will co-ordinate the twinning programme, liaise with the PAAs in the Ministry of Economy and will ensure that the following stages are covered:

- Solving institutional building questions (including internal audit and staff development and training),
- Creating Baltic electricity market (resolving the various technical issues, i.e. dispatching and pricing, with assistance STA-O and P) with long-term goal of interconnection with West European grids and
- Analysis of possible alternatives of EC directive requirements, with options for reorganisation.

The advantages and shortcomings as well as costs and ways of implementation and execution of each alternative shall be determined. Following the official decisions, appropriate legal documents, complying with laws and equivalent to EC directives and rules as well as international agreements should be prepared. These issues are discussed in more detail in Annex 6.

The indicative inputs from the PAA and STAs will cover the following stages, activities summarised in the table below, and each activity is described in subsequent paragraphs.

Title	Area/activities	Duration
PAA-I	General management advice on electricity directive & company policy, staff development etc.	24
PAA-J	Electrical network issues	12
PAA-K	MIS design & project management	12
STA-L	Accounts analysis & internal audit	6
STA-M	MIS systems analysis	6
STA-N	MIS systems development	6
STA-O	Training	6

Strategic planning and implementation process and human resource development (PAA-I and STA-O):

The PAA should assist in the formulation and implementation of implementation company, utility and functional level strategies. He/she should assist the company in development human resource development strategy and programme following a detailed review of the organisational structure and procedures of the electricity utilities. This should include, *inter alia*:

- Job analysis and preparation of a methodology for preparing job descriptions covering the whole profile of the managerial and labour forces. Worked examples should be produced for each grade and level of the company.
- Review and make recommendations for the division of responsibilities and authority in the company with particular emphasis on the organisational departmental structure and accountability.
- A study of labour specialisation, with recommendations for streamlining both management and labour forces.

Analysis and evaluation of information available (PAA-I, PAA-K, STA-L and P):

Analysis of the Lithuanian Energy charts of accounts should be performed in order to identify issues for allocation to the Business Units specific management information criteria and accounts. It is most likely that two main business activities are included – generation and transmission. The result of this stage should be the identification of the information required to realise the Unbundling.

Analysis, review and assistance on technical issues relating to the electrical network (PAA-J):

A review of the generation and transmission assets of the company will be required leading to advice on future investment and maintenance programmes aimed at improving the reliability and safety of the network. The company's ability to be a link in the regional transmission network should be reviewed and a strategy developed to maintain and build on the company's strategic position. Among the issues the PAA-J will be expected to address are:

- Peculiarities of operation of electric equipment with SF₆ gas isolation and security equipment.
- General operation management of high voltage substations and switchyards.
- Application of IEC standards to high voltage equipment, manufactured in compliance with GOST.
- Principals of substation design, build and operation.
- Principals of drafting specifications while ordering equipment.

Analysis of the accounting system (STA-L):

The procedures (fixed assets, accounts payable, accounts receivable, etc.) of the accounting system should be analysed in order to evaluate the information present in the accounting system of the Lithuanian Energy (existence and quality). The result of the step should be the identification of the relevant information for the MIS criteria and Unbundling objectives and to design the implementation required managing the information to be utilised for the MIS and Unbundling Systems.

Design of the MIS and Unbundling System (PAA-K, L and M):

Analysis should be performed in order to design the Unbundling system based on the information flow in the Lithuanian Energy. The result should be a design of flexible system able to:

- Model and set specific management information criteria
- Separate accounting balances;
- Manage accounting information;
- Arrange financial statement for all business units, corporate and other services.

Implementation of the MIS and Unbundling System (PAA-K, STA-L, M and N):

A plan should be prepared to define how to manage the activities to be performed in order to realise the MIS and Unbundling System and be followed by the training how to use the new MIS and Unbundling System. Due to complexity, development of a new accounting system for managing the unbundled data generally needs at least 2 years time period. In order to obtain reliable unbundled data and to develop a continuous improvement process the following different systems are likely to be identified:

- *Static System*, which works on accounting balances at the date of financial statements, providing the attribution of the transactions that compose the balance of a specific Business Unit based on the information available in the accounting and management information system. This system does not allow managing “*non allocable*” items (primarily financial flows, and equity). This system should be effective until implementation of Dynamic System.
- *Dynamic System* provides separate accounting systems for each Business Unit and allows managing separate criteria, financial flows, fiscal items and equity. It provides also for the allocation of a common costs based on internal contracts made to rule the supply of specific services between different Business Units and energy transferred among generation and transmission business units on the basis of specific internal transfer prices.

Three local tenders for intangible supplies and services will augment the services and support provided by the PAA and STAs. The first for software services for the analysis development of the MIS, the second for the provision of associated translation and interpretation services in support of the PAA and STAs and the third for bespoke software and hardware to support the PAA and STAs and the development of the pilot MIS.

Equipment tendering (PAA-K) and Software development put out to local tender:

Sufficient computer hardware and off-the-shelf software will need to be purchased at the beginning of the project to allow the development of the pilot unbundling system. The State budget will fund the purchase of necessary hardware for the rollout of the system to the branches and regional offices, as dictated by Lietuvos Energija’s Information Strategy. Bespoke software will need to be developed for the pilot MIS and unbundling system; a local tender will be launched to recruit a suitable software house. The State budget will fund rollout, maintenance and training of the system according to Lietuvos Energija’s Information Strategy.

Restructuring of Lietuvos Dujos (JSC Lithuanian Gas)

A Pre Accession Adviser (PAA-Q) will provide policy and strategic advice to senior management of Lithuanian Gas over a two year period with at least a 18 person-month input, with particular emphasis on the Gas directive and its relevance to the company. The PAA will also liaise and co-ordinate the activities of various short term advisers (STAs) and prepare the specifications, tender documents and participate in the procurement of equipment and software development services.

This twinning assignment will be analyse the actual JSC Lithuanian Gas electronic data processing (EDP) systems in order to prepare recommendations and implement the procedures needed to:

- Enable Lithuanian Gas to satisfy the European Union directives for unbundling the accountancy of their businesses while complying with the Lithuanian Laws and International Accounting Standards.
- Position Lithuanian Gas to successfully meet the ongoing requirements for reporting by activities, in order to identify the actions required to improve results, providing financial information by major cost centres, balance sheets statements of operations and cash flows per activity and statements of operations and cash flows per operational unit.
- Permit Lithuanian Gas to identify and properly allocate all costs and revenues to their activities through the establishment of the appropriate parameters and criteria.
- Assist the JSC Lithuanian Gas in preparation of long term gas supply contracts

The JSC Lithuanian Gas is in the process of implementation of SCALA accounting system. The company have recently implemented management audit project sponsored by Phare, the proposals and suggestions of which are currently being analysed and discussed within the company. This project aims to better position the company to commercial environment and improve its efficiency and effectiveness. The desirable outcome of this project would be detailed analysis of its accounting systems and unbundling of accounting and management through the respective business areas (transmission and distribution).

This twinning assignment is designed to produce the following outputs:

- Design and implementation of the separate accountancy management system for each Business Unit complying with the Lithuanian Laws and International Accounting Standards feeding into the Company Management Information System (MIS).
- Prepare regulations and perform structural changes, enabling the organisation of company's activities in accordance with EC standards.
- Improve reporting by activities on: financial information by major costs, balances sheets statements of operations and cash flows per activity and statements of operations and cash flows per operational unit.
- Develop practical procedures and other enterprise implications for company management in market conditions.
- Specialised software for company accounts management.
- Training for specialist involved in company and companies accounts management. The necessary computer hardware, telecommunication systems and equipment for physical security purchased under the separate investment project and installed.
- Gas supply pricing: long-term gas supply contracts (or drafts available for finalisation with gas suppliers)

The PAA with his/her twinning team of STAs will lead a twinning programme consisting of the following stages:

- Solving institutional building questions
- Creating Baltic gas market and the gas-interconnection
- Assistance in preparation of long term gas supply contracts
- Analysing possible alternatives of EC directive requirements, whereof certain directions of reorganisation could be chosen. The advantages and shortcomings as well as costs and ways of implementation and execution of each alternative shall be determined. Following the official decisions, appropriate legal documents, complying with laws and equivalent to EC directives and rules as well as international agreements should be prepared. These issues are discussed in more detail in Annex 7.

The indicative inputs from the PAAs and STAs will cover the following stages, activities summarised in the table below, and each activity is described in subsequent paragraphs.

Title	Area/activities	Duration
PAA-Q	General management advice on gas directive & company policy, staff development etc.	24
PAA-R	MIS design & project management	12
STA-S	Accounts analysis & internal audit	6
STA-T	MIS systems analysis	6
STA-U	MIS systems development	6
STA-V	Training	6
STA-W	Pricing	6
STA-X	Ad hoc technical inputs	6

Analysis and evaluation of information available:

Analysis of the Lithuanian Gas charts of accounts should be performed in order to identify issues for allocation to the Transmission and Distribution Business Units and specific management information criteria and accounts. The result of this stage should be the identification of the information required to realise the MIS and the Unbundling system.

Analysis of the accounting system:

The procedures (fixed assets, accounts payable, accounts receivable, etc.) of the accounting system should be analysed in order to evaluate the information present in the accounting system of the Lithuanian Gas (existence and quality). The result of the step should be the identification of the relevant information for establishing the criteria for the MIS and the Unbundling objectives and to design the implementation required managing the information to be utilised for the MIS and Unbundling System.

Design of the MIS and Unbundling System:

Analysis should be performed in order to design the Unbundling system based on the information flow in the Lithuanian Gas. The result should be a design of flexible system able to:

- Model and set various management information criteria
- Separate accounting balances;
- Manage accounting information;
- Arrange financial statement for all business units, Corporate and other services.

Implementation of the MIS and Unbundling System:

Plan should be defined how to manage the activities to be performed in order to realise the MIS and Unbundling System and be followed by the training how to use the new MIS and Unbundling System. Due to complexity, development of a new accounting system for managing the unbundled data generally needs at least 2 years time period. In order to obtain reliable unbundled data and to develop a continuous improvement process the following different systems are likely to be identified:

- *Static System*, which works on accounting balances at the date of financial statements, providing the attribution of the transactions that compose the balance of a specific Business Unit based on the information available in the accounting and management information system. This system does not allow managing “non allocable” items (primarily financial flows, and equity). This system should be effective until implementation of Dynamic System.

- *Dynamic System* provides separate accounting systems for each Business Unit and allows managing separate management criteria, financial flows, fiscal items and equity. It provides also the allocation of:
 - Common costs based on internal contracts made to rule the supply of specific services between different Business Units.
 - Energy transferred among Transmission and Distribution Business Units on the basis of specific internal transfer prices.

Equipment tendering:

Sufficient computer hardware and off-the-shelf software will need to be purchased at the beginning of the project to allow the development of the pilot unbundling system. The State budget will fund the purchase of necessary hardware for the rollout of the system to the branches and regional offices, as dictated by Lietuvos Dujos's Information Strategy.

Software development put out to local tender:

Bespoke software will need to be developed for the pilot MIS and unbundling system; a local tender will be launched to recruit a suitable software house. The State budget will fund rollout, maintenance and training of the system according to Lietuvos Dujos's Information Strategy.

6. Budget (in MEUR):

	Investment	Institution Building	Total Phare (I+IB)	Recipient	IFI	TOTAL
General legal and institutional framework for implementing the energy directives and oil crisis management		1.00	1.0	0.15		1.15
Restructuring of Lithuanian Energy through accounts unbundling		1.50	1.5	0.25		1.75
Restructuring of JSC Lithuanian Gas through accounts unbundling		0.75	0.750	0.1		0.850
TOTAL		3.25	3.25	0.5		3.75

7. Implementation arrangements

Responsibility for the administration related to the procedural aspects of procurement, contracting and accountancy will rest upon the CFCU. Responsibility for the administration related to the preparation, technical control and implementation will rest with the Energy Agency at the Ministry of Economy. All three projects will be implemented through Twinning arrangements with Member State's energy administration, power and gas companies as appropriate. The equipment part of the twinning components will be tendered by the CFCU according to DIS rules.

8. Implementation schedule

	<i>Start of project activity</i>	<i>Completion</i>
(Ministry)	2Q 2000	3Q 2001
(Energy)	4Q 2000	3Q 2002
(Gas)	4Q 2000	3Q 2002

9. Equal opportunity

The institutions involved in the project execution will observe equal opportunity of men and women in its recruitment and human resources development. The beneficiaries will ensure equal access of men and women to the project activities and results

10. Environment

n/a

11. Rates of return

n/a

12. Investment criteria

n/a

13. Conditionally and sequencing:

Support to the energy sector is conditional on the adoption of a National Energy Strategy in line with the Accession Partnership priorities and the confirmation of the date for closure of Ignalina NPP Unit 1 in conformity with the Lithuanian obligation under the Nuclear Safety Account Agreement.

The project is conditional to the approval by the Ministry of Economy of the respective parts of the Action Plan for the implementation of the National Energy Strategy and substantial progress with the transposition of the energy directives.

The Member state's twinning experts in the Energy Utilities should only start once the new contractual operational and management relationship between the Ministry of Economy and the state-owned energy utilities has been agreed by the parties concerned.

Logframe Matrix

Annex 1

Transposition and implementation of the Energy <i>Acquis</i>		Project Number: LI9910.01	Date of Drafting 5/99
		Contracting period Expires: 31/10/2001	Disbursement Period Expires: 31/10/2002
		Total Budget 3.75 MEUR	Phare contribution: 3.25 MEUR
Wider Objective	Indicators of Achievement	Sources of Information	Assumptions and Risks
Implementation of the NPAA in the Energy Sector and development & implementation of National Energy Strategy (NES)	Progress with the implementation of the NPAA and the NES Reports on the activities performed	NPAA implementation deadlines checked by the Government and EU	Project will assist to the positive developments of the energy sector and integration into EU
Immediate Objectives	Indicators of Achievement	Sources of Information	Assumptions and Risks
Prepare legal basis for EC requirements compliance for 90 days oil product stocks; Prepare information collection system, processing and supply to the EC and IEA related to compulsory oil stocks (COS); Prepare oil crisis management system (OCM). Assist in commercialisation of the energy utilities, design & implement account unbundling within each energy utility.	Law on emergency oil stocks drafted/ revised COS information system designed OCM system designed. Reports on assistance performed. Separate account systems introduced for each business unit of the energy utilities.	Ministry of Economy, Energy Agency and CFCU will check progress of the work and the results according the reports.	Competent Pre-accession adviser selected; Competent implementation team contracted; Financial constrains; Speed of reforms; Possible lack of competent staff. Low interest of Member States.
Outputs	Indicators of Achievement	Sources of Information	Assumptions and Risks
Legal and institutional framework for State oil reserves and oil crisis management procedures; Separate accounts introduced for different business units of the energy utilities	Draft law submitted to Seimas, institutional framework & reporting procedures designed; Energy utilities able to operate in a competitive environment.	According to the work programme reports will be checked by the responsible Government Officials;	All tasks successfully completed; Financial, economical and administrative constrains in the enforcement stage;
Inputs			
Man power from the Ministry of Economy staff allocated to the project; Man power from the energy utilities staff allocated to the project	Necessary manpower and co-financing secured.	Information provided by Ministry of Economy, Energy Agency and energy utilities.	Timely start and smooth implementation;

Cumulative Quarterly Contracting and Disbursement Schedule (in MEUR)**LI 9910.01****Cumulative Quarterly Contracting Schedule (MEUR)**

Component	3Q 99	4Q 99	1Q 00	2Q 00	3Q 00	4Q 00	1Q 01	2Q 01	3Q 01	4Q 01	1Q 02	Total
Restructuring of JSC Lithuanian Energy through accounts unbundling						1.50						1.50
Restructuring of JSC Lithuanian Gas through accounts unbundling						0.75						0.75
General legal and institutional framework for implementing the energy directives and oil crisis management				1.00	1.00	1.00						1.00
Total				1.00	1.00	3.25						3.25

Cumulative Quarterly Disbursement Schedule (MEUR)

Project	4Q 99	1Q 00	2Q 00	3Q 00	4Q 00	1Q 01	2Q 01	3Q 01	4Q 01	1Q 02	2Q 02	3Q 02	Total
Restructuring of JSC Lithuanian Energy through accounts unbundling					0.50	0.70	0.90	1.10	1.20	1.30	1.40	1.50	1.50
Restructuring of JSC Lithuanian Gas through accounts unbundling					0.20	0.30	0.40	0.50	0.60	0.60	0.60	0.75	0.75
General legal and institutional framework for implementing the energy directives and oil crisis management			0.25	0.50	0.65	0.80	0.95	1.00	1.00	1.00	1.00	1.00	1.00
Total			0.25	0.50	1.35	1.80	2.25	2.60	2.80	2.90	3.00	3.25	3.25

Detailed Implementation Chart – LI 9910.01

Year	1999			2000												2001												2002											
	O	N	D	J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S			
3 Twinning and Training Packages for the Energy Sector																																							
- Launch Twinning Request to Member States (after Management Committee – 23 July 1999)																																							
- Selection of Member State(s) for Twinning	X																																						
- Elaboration of Twinning Covenant	X	X	X	X	X																																		
- Submit Twinning Covenant to the Commission & Steering Committee for Approval				X	X	X																																	
Implementation of Twinning Packages :																																							
Policy & strategic advice to Ministry of Economy							X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X																	
Restructuring Lietuvos Energija													X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X			
Restructuring Lietuvos Dujos													X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X			

Detailed Cost Breakdown – LI 9910.01

	2000/01			Total
<i>Component</i>	National Budget	Phare	Other	
<i>Institution Building</i>				
A. TA				
B. Twinning				3,75
(1)	0,15	1,00		
(2)	0,25	1,50		
(3)	0,10	0,75		
C. Other				
<i>Investment</i>				
A. Studies				
B. Financial Support				
C. Equipment				
D. Other				
Total	0,50	3,25		3,75

Relation of Project with previous Phare activities and ongoing projects financed from other sources

LI 9910.01

The Legal Harmonisation Work Programme for Lithuanian energy sector was drafted in April 1998 and presented to inter-ministerial legal harmonisation commission “Energy”. This programme is based on the previous screening exercises performed both by foreign and local experts. The following approach is suggested:

1. Analysis of EC law and its requirements;
2. Detailed analysis of current situation;
3. Determining national choices;
4. Determining how national law will be implemented and enforced;
5. Drafting a strategy for EU accession in the Energy Sector;
6. Defining a schedule for implementation;
7. Actual drafting of legislation.

The Phare national programme is already financing from the 1997 budget two projects related to the implementation of the Legal Harmonisation Work Programme. First project comprises the training element and second one assists with the implementation.

The Energy Emergency Planning issues have been analysed in the Phare financed study for EBRD performed by Lahmeyer International in 1997. Recommendations from the said study have been used to define the scope for the Twinning activities under the 1999 Phare budget in order to set up a legal and institutional framework for oil crisis management in Lithuania.

Several studies have been financed earlier by Phare programme for Lithuanian Power and Gas companies on restructuring, management and accounting issues. Both utility companies (Lithuanian Energy and Lithuanian Gas) are in process of implementation of SCALA accounting system.

The study “Restructuring and Management Consultancy performed by Price Waterhouse in 1996 for Lithuanian Energy provided recommendations on restructuring, corporate planning, accounting and management information issues. Some recommendations are already implemented by separating the District Heating activities from Lithuanian Energy and transferring it to municipalities in 1997.

The study “Performance Management Audit” for Lithuanian Gas Company performed by PANDREX Phare framework contractor provided recommendations on management improvement issues in a commercial environment in late 1998.

The present project is a logical continuation of the previous activities. It concentrates on legal and institutional development and enforcement of Oil Crisis Management legislation, aims to position companies to take advantage of their commercial environment and improve their efficiency and effectiveness.

Lietuvos Energija: Issues to be resolved

LI 9910.01

The key issues that the twinning team should help the company address are:

- Dispatching
- Pricing
- Internal audit
- Unbundling systems

The following sections discuss these issues in detail below.

Dispatching:

Following the current and pre-planned analysis of post-restructured electric power system structure, competitiveness, reliability, organisation and means of dispatching within the system it is important to determine the most acceptable central dispatch control scheme for Lithuania.

The main criteria to ensure the transparency and non-discrimination of power plant, transmission and distribution network dispatch control should be defined.

The conditions of access to transmission network and order of supply to consumers, consumer power plants, regular power plants should be defined.

Harmonised rules of organising the internal and international electric energy market should be developed.

Public, departmental and government institutional projects of dispatch control accounting should be defined.

Limits of dispatch control competence and its relations with electric power market participants, operators of power plant and network, government institutions, Regulator, etc.

The adviser is expected to:

- help in creating the structure and functions of national dispatch centre within the conditions of energy market, transmission from present to projected structure
- assist in preparing activity rules of system (as well as market) operator and other participants of energy market
- demonstrate energy market models, presently used in practice, make a detailed presentation of NORDPOOL model, consult and organise training in creating energy pools, Transmission System Operator (TSO), Independent System Operator (ISO)
- organise training in transition pricing and application of different methodologies
- organise training in static and dynamic stability of energy systems
- consult on annual, quarterly, monthly, 24-hour reports and information systems of NDC, publicised and non-publicised information
- recommend necessary changes within Lithuanian energy system, aiming to create an independent control area for interconnecting with European energy system (UCPTE)
- present requirements for new electric energy sources, national dispatch centres and transmission companies
- help define relations of NDC with electric energy distributors and generators, other power systems and companies within the market conditions

- propose short and long term planning programs, used by NDC, planning and implementation of power system balance and reliability and effectiveness of national transmission grid
- present requirements and planning for primary and secondary control within market conditions
- assist in defining of legal and economic requirements for primary and secondary control
- organise consultations on functions, requirements and work assessment of system operator

Pricing: Electricity pricing in the high voltage (transmission) network within the liberalised and competitive electricity market:

- pricing methods for transmission, transit, capacity reserve;
- pricing for electricity transmission in interconnected systems, taking into consideration the requirements of the EC Directives for not discriminative and transparent prices;
- Pricing methods for the ancillary services provided by the transmission network.
- Enhancement of electric power contracts with industry, commercial and residential consumers in accordance with EC document.

An adviser for pricing issues will help in analysing advantages and shortcomings of current regulation, demonstrate patterns of pricing in West and EU countries according to three positions indicated previously; help the staff solve specific issues evolved while pricing, organise training while inviting appropriate specialists and consulting companies, evaluate and analyse local procedures; help execute regulation documents, meeting requirements of EC directives. The detailed plan will be developed upon consultation with adviser, having assessed the situation on the spot.

Expected outputs: development of regulation documents for issues of pricing and co-ordination of it with Lithuanian legislation and EC directive requirements.

Analysis and implementation international standards of the internal audit;

Consultations while preparing samples of internal audit documents, used in practice by EU, drafting long-term work plans, preparing audit tests and training the personnel to work in compliance with international standards.

The adviser is expected to work with internal audit staff and Management to:

- Upgrade the existing audit system in areas such as
 - audit mandate and policies
 - audit programme
 - audit organisation, staffing and resources
 - audit methodology, information, tools and documentation
 - audit reporting and follow-up
- Train audit staff in the use of the upgraded processes; work with auditors in the first new applications of the new audit process
- Identify ongoing audit needs, including specialised audit skills such as EDP and dealing audit, and develop a plan for meeting them

Unbundling system:

Analysis and evaluation of information available: Analysis of the "Lietuvos Energija" charts of accounts should be performed in order to identify issues for allocation to the Business Units specific

accounts. It is most likely that two main business activities are included – generation and transmission (split into three components - Use of System Services, Ancillary Services and Other). In the process of analysis the following steps should be performed:

- Collect, analyse and evaluate information available at "Lietuvos Energija" in order to identify information required for the unbundling system.
- Evaluate the actual "Lietuvos Energija" charts of accounts to identify the appropriated allocation of investments, incomes, expenses, etc. to the Business Unit specific account needed for the unbundling system.

The result of this stage should be the identification of the information required to realise the Unbundling.

Analysis of the accounting system: In the process of analysis the following steps should be performed:

- Evaluate and analyse the procedures (fixed assets, account payables, account receivables, etc.) of the actual accounting system to evaluate the information present in the accounting system of the company in order to identify relevant information for the unbundling.
- Review the "Lietuvos Energija" internal costing allocation criteria and policies for indirect expenses, if available.
- Analyse the actual structure, if any, for transfer pricing among the different activities and cost centres.
- Review the allocation of the "Lietuvos Energija" fixed assets, receivables and payables to the two major activities mentioned above.

The result of the step should be the identification of the relevant information for Unbundling objective and to design the implementation required managing the information to be utilised for the Unbundling System.

Design of the Unbundling System: Analysis should be performed in order to design the Unbundling system based on the information flow in the "Lietuvos Energija". During its execution the project team will:

- Clarify reporting requirements of management, Lithuanian and European Union regulations.
- Analyse the advantages and disadvantages of the static unbundling model (financial statements reflected in the accounting records at a given date) versus the dynamic unbundling models (economic events reflected in the accounting records are assigned to the related activities).
- Analyse the most important impacts of unbundling on the organisation and administration structures and on the administrative procedures and resources.
- Analyse the logical flow and methodology of the actual EDP systems in order to proceed to the unbundling.
- Study the implications, advantages and disadvantages of legal/corporate unbundling. Organisation and management structures, tax, labour legal and economic aspects of the process to take place.
- Analyse the impacts of unbundling on the data processing systems. Prepare a list of recommendation of the required changes in the organisations and data inputs.
- Issue a report with the consultant recommendations for the required supply of hardware and necessary software.

The result should be a design of flexible system able to:

- separate accounting balances;
- manage accounting information;
- Arrange financial statement for all business units, Corporate and other services.

Implementation of the Unbundling System: Plan should be defined how to manage the activities to be performed in order to realise the Unbundling System and be followed by the training how to use the new Unbundling System.

Due to complexity, development of a new accounting system for managing the unbundled data generally needs at least 2 years time period. In order to obtain reliable unbundled data and to develop a continuous improvement process the following different systems are likely to be identified:

- *Static System*, which works on accounting balances at the date of financial statements, providing the attribution of the transactions that compose the balance of a specific Business Unit based on the information available in the accounting and management information system. This system does not allow managing “*not allocable*” items (primarily financial flows, and equity). This system should be effective until implementation of Dynamic System.
- *Dynamic System* provides separate accounting systems for each Business Unit and allows managing separate financial flows, fiscal items and equity. It provides also the allocation of:
- Common costs based on internal contracts made to rule the supply of specific services between different Business Units.
- Energy transferred among Generation and Transmission Business Units on the basis of specific internal transfer prices.

Lietuvos Dujos: Issues to be resolved - LI 9910.01

The key issues that the twinning team should help the company address are:

- Pricing
- Internal audit
- Unbundling systems

The following sections discuss these issues in detail below.

Gas Pricing:

- pricing methods for transmission, transit, distribution;
- pricing for gas transmission in interconnected systems, taking into consideration the requirements of the EC Directives for not discriminative and transparent prices;
- Enhancement of gas contracts with industry, commercial and residential consumers in accordance with EC document.

Analysis and implementation international standards of the internal audit;

Design of management performance evaluation and assessment system. (As a continuation of above mentioned Performance Management Audit project). Assistance in preparation of samples of internal audit documents, used in practice by EU, drafting long-term work plans, preparing audit tests and training the personnel to work in compliance with international standards.

Analysis and evaluation of information available: Analysis of the Lithuanian Gas charts of accounts should be performed in order to identify issues for allocation to the Business Units specific accounts. It is most likely that two main business activities are included – transmission and distribution. In the process of analysis the following steps should be performed:

- Collect, analyse and evaluate information available at Lithuanian Gas in order to identify information required for the unbundling system.
- Evaluate the actual Lithuanian Gas charts of accounts to identify the appropriated allocation of investments, incomes, expenses, etc. to the Business Unit specific account needed for the unbundling system.

The result of this stage should be the identification of the information required to realise the Unbundling.

Analysis of the accounting system: In the process of analysis the following steps should be performed:

- Evaluate and analyse the procedures (fixed assets, account payables, account receivables, etc.) of the actual accounting system to evaluate the information present in the accounting system of the company in order to identify relevant information for the unbundling.
- Review the Lithuanian Gas internal costing allocation criteria and policies for indirect expenses, if available.
- Analyse the actual structure, if any, for transfer pricing among the different activities and cost centres.
- Review the allocation of the Lithuanian Gas fixed assets, receivables and payables to the two major activities mentioned above.

The result of the step should be the identification of the relevant information for Unbundling objective and to design the implementation required managing the information to be utilised for the Unbundling System.

Design of the Unbundling System: Analysis should be performed to design the Unbundling system based on the information flow in the Lithuanian Gas. During its execution the project team will:

- Clarify reporting requirements of management, Lithuanian and European Union regulations.

- Analyse the advantages and disadvantages of the static unbundling model (financial statements reflected in the accounting records at a given date) versus the dynamic unbundling models (economic events reflected in the accounting records are assigned to the related activities).
- Analyse the most important impacts of unbundling on the organisation and administration structures and on the administrative procedures and resources.
- Analyse the logical flow and methodology of the actual EDP systems in order to proceed to the unbundling.
- Study the implications, advantages and disadvantages of legal/corporate unbundling. Organisation and management structures, tax, labour legal and economic aspects of the process to take place.
- Analyse the impacts of unbundling on the data processing systems. Prepare a list of recommendation of the required changes in the organisations and data inputs.
- Issue a report with the consultant recommendations for the required supply of hardware and necessary software.

The result should be a design of flexible system able to:

- Separate accounting balances;
- Manage accounting information;
- Arrange financial statement for all business units, Corporate and other services.

Implementation of the Unbundling System: Plan should be defined how to manage the activities to be performed in order to realise the Unbundling System and be followed by the training how to use the new Unbundling System. Due to complexity, development of a new accounting system for managing the unbundled data generally needs at least 2 years time period. In order to obtain reliable unbundled data and to develop a continuous improvement process the following different systems are likely to be identified:

- *Static System*, which works on accounting balances at the date of financial statements, providing the attribution of the transactions that compose the balance of a specific Business Unit based on the information available in the accounting and management information system. This system does not allow managing “*non allocable*” items (primarily financial flows, and equity). This system should be effective until implementation of Dynamic System.
- *Dynamic System* provides separate accounting systems for each Business Unit and allows managing separate financial flows, fiscal items and equity. It provides also the allocation of:
 - ◆ Common costs based on internal contracts made to rule the supply of specific services between different Business Units.
 - ◆ Gas transferred among Transmission and Distribution Business Units on the basis of specific internal transfer prices.
 - ◆ Assistance in preparation of long term gas supply contracts

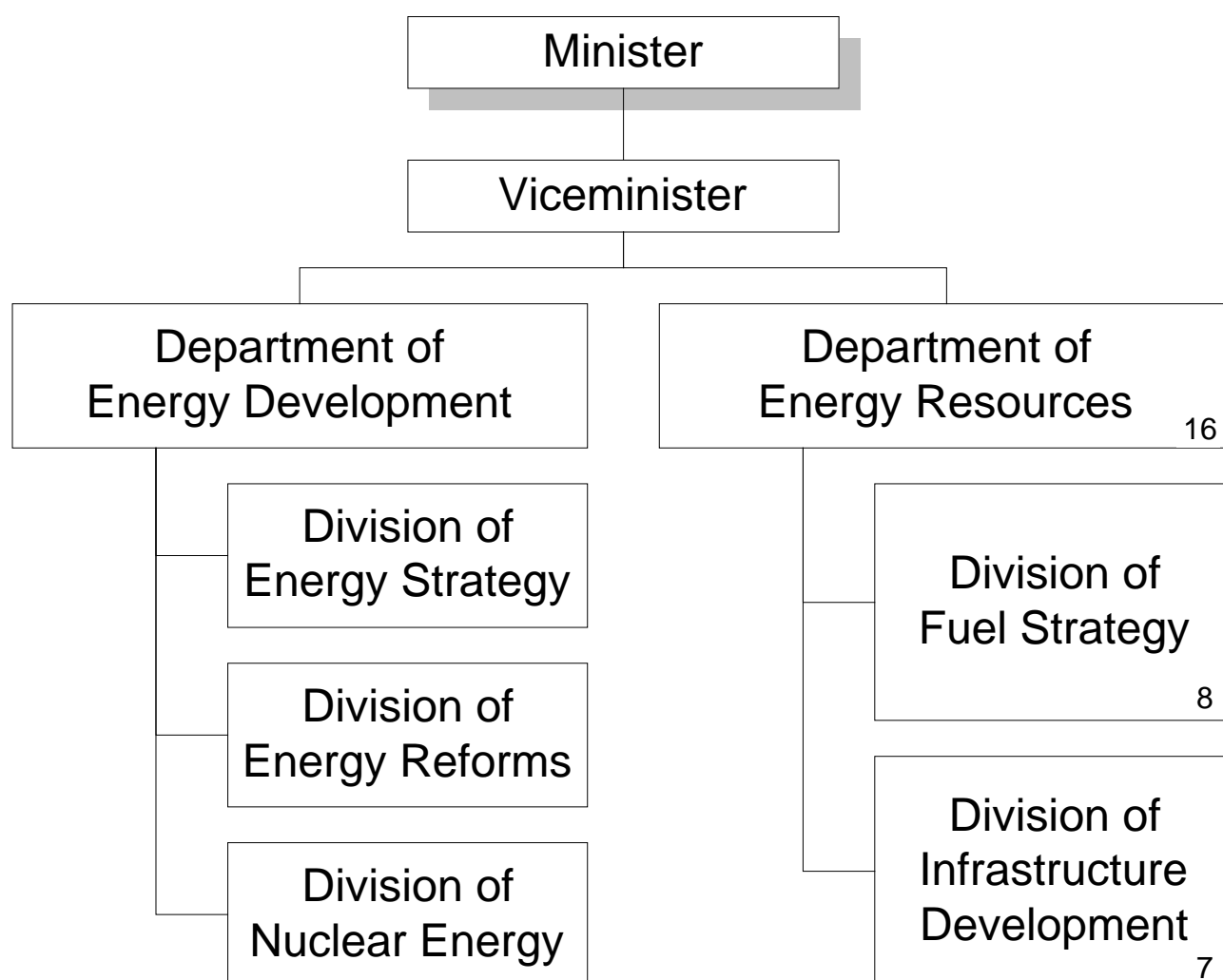
Analysis and evaluation of information available: Analysis of the Lithuanian Gas supply contracts and existing negotiation procedures with gas suppliers in order to identify obstacles in setting long term gas supply contract (LTC). The result of this stage should be the identification of the information required to prepare and negotiate LTC.

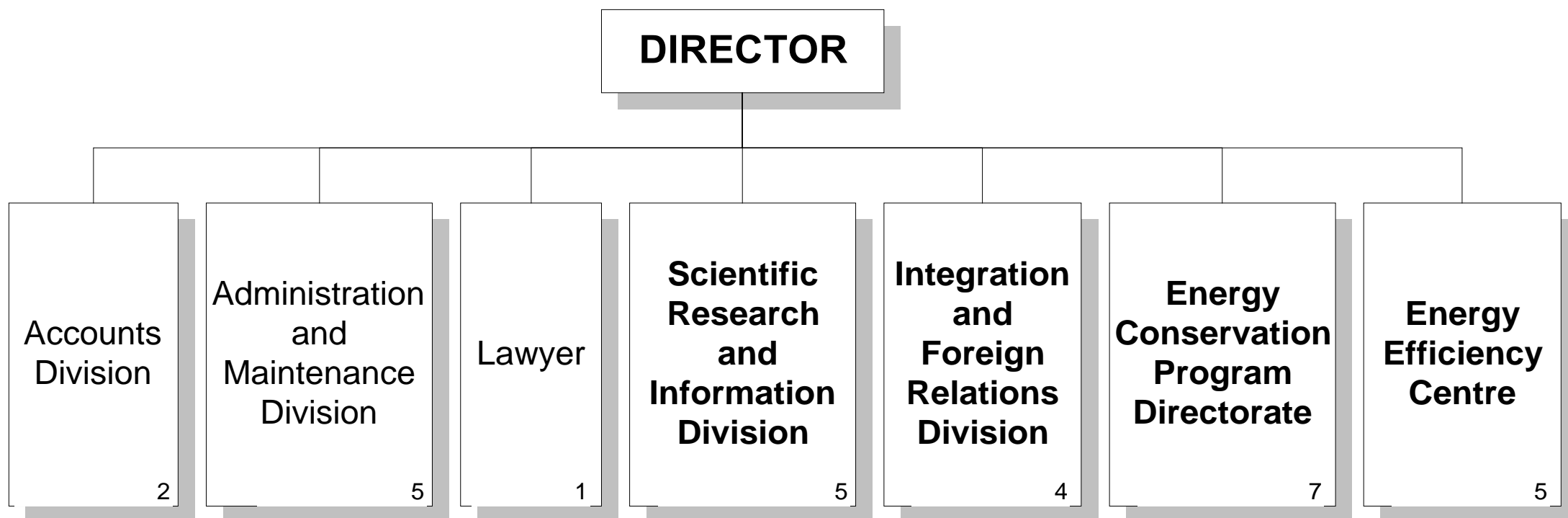
Analysis of the gas price setting system for LTC: The procedures used of the gas price setting systems that are in practise in Western European countries should be analysed. Possibilities of introducing alternative fuel price factor should be analysed. The result of the step should be the identification of the relevant information for establishing the criteria for the setting acceptable gas price calculation principles, gas price calculation formula.

Draft and Negotiation of LTC: Analysis should be performed in order to prepare draft long-term gas supply contract. The result should be a few versions of LTC. Permanent advisory activity including personal participation in the negotiation group should take place. Due to complexity of the development of a new understanding and bargaining of new LTC generally needs at least 2 years time period.

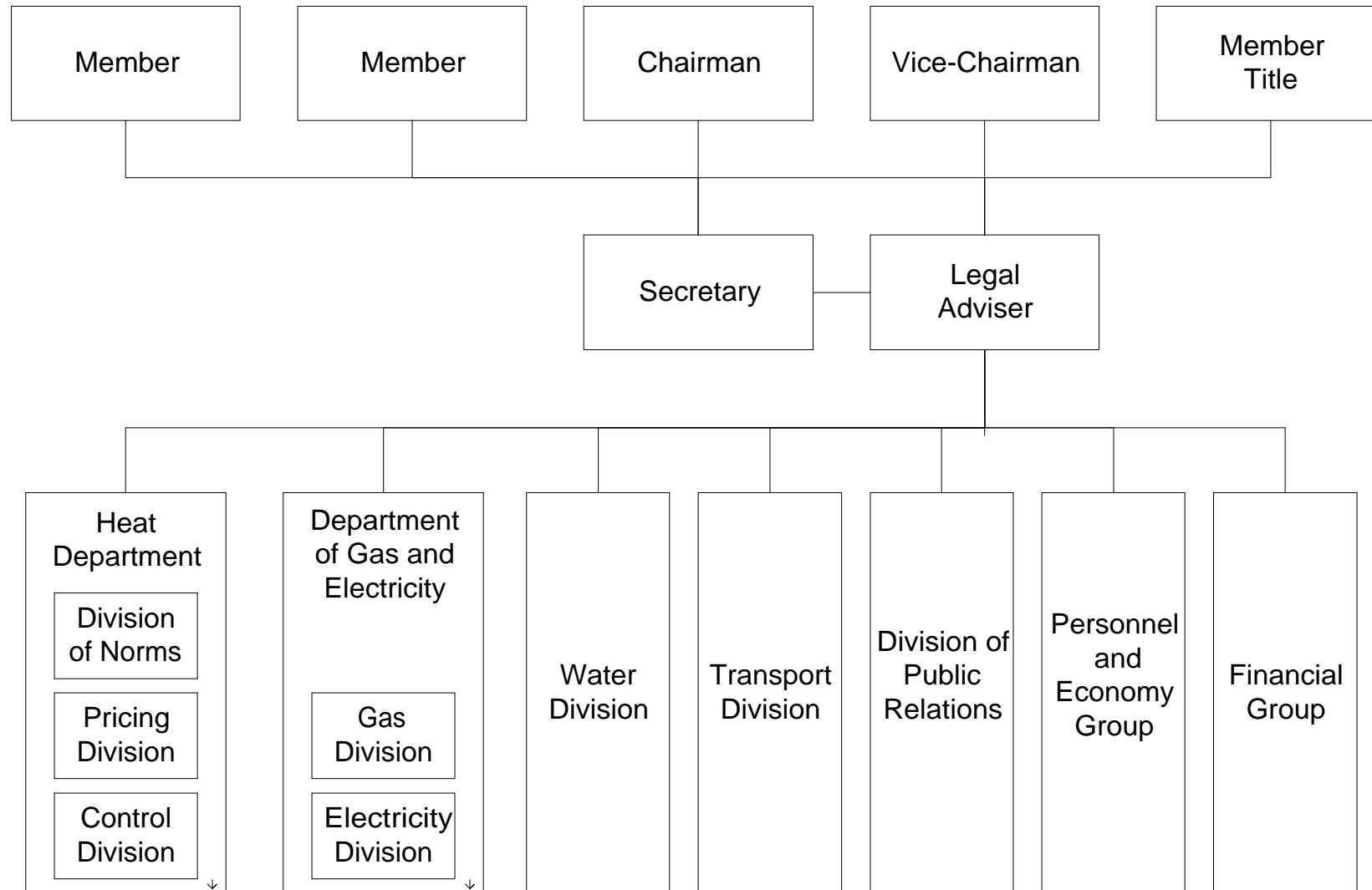
Organisation Charts for the Ministry and Energy Commission – LI 9910.01

MINISTRY OF ECONOMY
(Energy part)

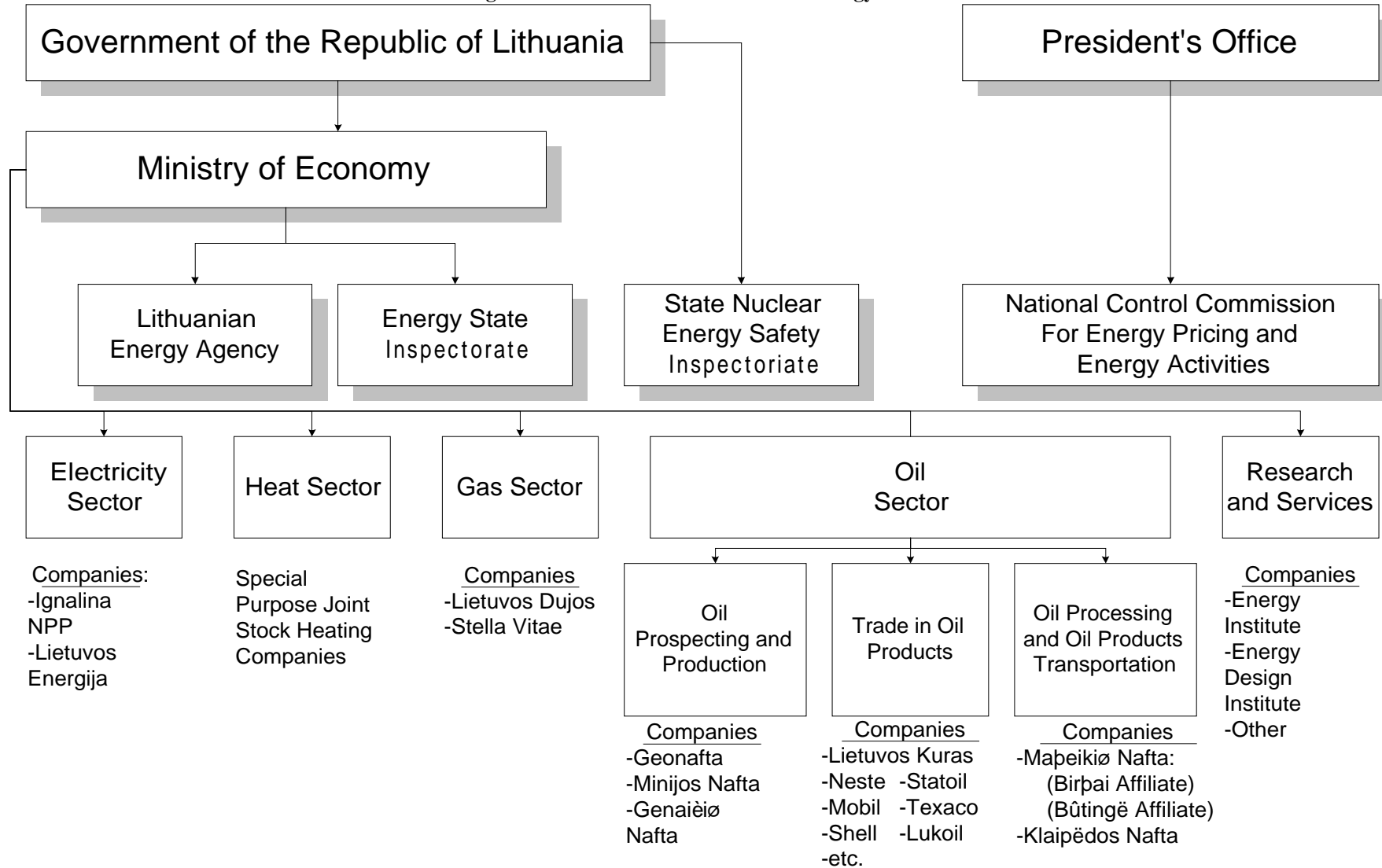




State Commission on Prices and Energy Activity Control



Management Structure of the Lithuanian Energy Sector



Ministry of Economy

ENERGY RESOURCES DEPARTMENT

REGULATIONS

The main tasks of the Energy Resources Department shall include:

- formulation and implementation of the strategy of the energy resources (gas, oil, oil products, other types of fuel) sector as part of the national energy strategy;
- preparation of measures ensuring reliable provision of the country's economy with energy resources;
- preparation of the policy and means for the energy infrastructure development and improvement;

When implementing its tasks the Department shall:

- study priorities and objectives of the Lithuanian energy resources sector, participate in the preparation of its development strategy and programmes, draft legal and other provisions for their implementation;
- harmonise legal acts drafted by other departments of the Ministry of Economy and other institutions, the provisions of which have impact on the country's provision with energy resources;
- together with other ministries and state institutions prepare forecasts of economic development for the energy resources sector;
- analyse development trends, changes in the market, prices of the domestic and foreign energy resources sector;
- within its competence participate in the carrying out of feasibility studies of investment projects and programmes in the energy resources sector;
- participate in the preparation of restructuring programmes for energy utilities;
- participate in the formation of the technical and informational policy in the field of energy resources;
- together with other departments prepare forecasts of energy resources demand;
- within its competence draft laws and other legal acts necessary for the regulation of the energy resources sector;
- within its competence take part in the preparation of means ensuring reliable fuel supply in emergency situations and implement them;
- within its competence participate in the preparation of energy resources consumption balances;
- within its competence co-ordinate activities related to the preparation of restrictive measures of energy resources consumption in emergency situations;
- within its competence submit proposals to the Minister concerning the introduction of restrictive measures of energy resources consumption and use of state stocks of energy resources;
- solve issues related to the development of energy infrastructure;
- within its competence participate in the approval of the energy part and designing provisions concerning major energy projects of territorial and urban master plans;
- prepare and harmonise normative documents in the field of energy: rules, standards, regulations, etc., maintain accounting of these documents;
- together with other institutions involved prepare rules and procedures for maintenance and technical supervision systems and consumer connection to the energy network;
- within its competence support and promote the use of local and renewable energy resources, participate in the preparation of related means and implement them;

- prepare and approve obligatory quality requirements for fuel sold in the Lithuanian market;
- within its competence take part in the preparation of the strategic directions of local oil prospecting, production and use;
- within its competence take part in the preparation of legal acts providing for the procedure for import, export, transit and trade of energy resources;
- within its competence and following the established procedure maintain relations with foreign and international institutions and organisations;
- participate in the preparation of international co-operation agreements on the provision with energy resources;
- analyse the EC legal acts regulating the energy resources sector;
- participate in the preparation of the EU integration programme in the field of energy resources, prepare proposals concerning the approximation of the corresponding Lithuanian legal acts with those of the EC;
- within its competence participate in consultancy conferences, seminars and negotiations with international and other organisations;
- within its competence provide informational material to the mass media;
- Within its competence organise seminars, conferences and other events.