NGOs' vision of the new EBRD Energy Policy (2005)

"Simply put, energy efficiency must go up and greenhouse gas emissions must go down in the countries east of the EU."

Jean Lemierre, EBRD President, International Herald Tribune, Dec 12, 2003

Overall goal

The overall long-term goal of the EBRD Energy Policy should be to promote and bring about a transition of the energy sector in Eastern Europe and Central Asia from the current dependency on fossil fuels and nuclear energy towards more sustainable energy sources. In the process of achieving this goal the EBRD should put the emphasis on ensuring socially equitable, poverty reduction-driven energy and natural resource development.

The Revised Energy Policy Should:

- **Conduct a Strategic Environmental Assessment of the draft Energy Policy.**
- **An assessment of the success in implementing the previous policies is needed.**
- **Increase emphasise on energy efficiency and set up gradually increasing targets for investments into energy efficiency requiring 50% of investment in the power sector to be for energy efficiency by 2008.**
- **Set targets for the financing of sustainable renewable energy.**
- **Projects that include Waste to Energy Plants or the use of Refuse Derived Fuel should not be eligible for financing.**
- **Over the next 5 years the EBRD should phase out investments in fossil fuel**
- **Transition impacts' monitoring must be based on a set of clear indicators and should include social impacts.**
- **Involve only projects where the Production Sharing, Host Country and other similar agreements are able to demonstrate that national, regional and local benefits live up to best international practice.**
- **Include a set of requirements in order to ensure proper revenue and contract transparency in extractive industry projects.**
- **Ensure that there is an open and public planning process to distribute revenues in any extractive industry projects fairly.**
- **All extractive industries projects should ensure that emergency response plans are in place from the outset of a project and associated risks are adequately insured by an independent company.**
- **Financed projects should support only the use of safe, modern, and well-run vessels to carry oil, LNG or hazardous cargoes.**
- **Should not finance any oil, gas, or mining projects or activities (including technical assistance) that might affect existing World Heritage properties, current official protected areas, or critical natural habitat (as defined by the World Bank Natural Habitat Policy) or areas planned in the future to be designated by national or local officials as protected.**
- **All Joint Implementation (JI) and Clean Development Mechanism (CDM) projects must fulfil the Gold Standard.**
- **Based on the accounting of greenhouse gas (GHG) emissions caused by funded projects, EBRD activity in the energy sector should bring about a decrease in GHG emissions.**
- **Not support any projects that are aimed at the construction, completion or upgrading of nuclear power stations.**
- **Adopt clear guidelines and require, as a condition of financing, that there is provision for sufficient funds to be built up in the balance sheet for closure from the start of any new development,**
- **The Bank's operations in the energy sector have to be scrutinised in order to exclude those projects which promote different forms of "perverse subsidies" in the energy sector and/or support the replacement of state owned monopolies by private or public-private ones.**
- **Include provisions to effectively mitigate the possible negative institutional, social and environmental impacts of energy privatisation actively promoted by the EBRD.**
- **Project financed by Financial Intermediaries must be required to comply with national and international standards, equal to projects directly funded by the EBRD.**

Strategic Environmental Assessment of the draft Energy Policy

The EBRD should conduct a Strategic Environmental Assessment of the draft Energy Policy.

It is beyond any doubt that the Energy Policy – probably the largest of all the EBRD's sectoral policies and which will determine the EBRD's energy sector lending in the coming years - has a significant effect on the environment at both the local and global levels. Given the wide ranging impacts, it is difficult to comprehend why the proposed policy revision process does not reflect paragraph 39 of the EBRD's Environmental Policy – "In addition to EIAs on specific projects, the EBRD may also carry out strategic environmental assessments (SEAs) on the likely environmental consequences of proposed sector or country/regional plans or programmes which have the potential to significantly affect the environment." The EBRD should conduct an SEA of the draft Energy Policy that will be prepared after the current round of public consultations. In addition, the consultations should include a discussion regarding the scope of the SEA and the different alternative scenarios that should be assessed. For example, such an assessment should also take into account the long term contribution to climate change mitigation.

Implementation of previous policies

An assessment of the success in implementing the previous policies is needed.

There appears to be an implementation gap at EBRD in terms of delivering on both the overarching and specific objectives of the last revisions of the Energy and Natural Resources policies. For example, following the last revision of the Energy Policy in 2000, there have been very few renewable energy projects. The previous Natural Resources policy specifically outlined the need to conduct an SEA of the Sakhalin oil developments as a way of mitigating the environmental impacts of this huge development. The EBRD has not been able to deliver on this measure. The EBRD should explain why its previous policies and strategies have not been implemented, and consider how it can tackle these obstacles. The EBRD should also outline responsibilities for delivering on these areas. The decision-making structure should also be transparent. At present it is not clear how the client-driven project finance of the bank can be shaped to deliver on the strategic objectives of these policies. Lessons should then be applied to future actions. At present the Barents Sea is identified as a priority in the Environmental Policy, yet the significant proposed hydrocarbon developments in the Barents are not being addressed by the EBRD. The EBRD could provide significant input to improve the governance of these developments. It is willing to undertake an SEA of the nuclear decommissioning; a similar exercise is required for oil and gas.

Energy efficiency

The EBRD should emphasise energy efficiency and set up gradually increasing targets for investments into energy efficiency.

Given the low levels of efficiency in East European countries, the new policy should strongly emphasise energy efficiency across all sectors. Furthermore, the use of publicly specified targets is an important political instrument that signals the EBRD's priorities to borrowing countries. As such, an annually increasing lending target for energy efficiency should be set. By 2008, 50 percent of all lending in the power sector should be earmarked for increasing energy efficiency. To help reach this target, the use of Energy Service Companies and special energy efficiency credit facilities should be expanded. The EBRD should give priority to projects aiming to increase energy efficiency, for example by providing finance for highly efficient CHP power stations as well as end-user energy saving projects.

Furthermore, prior to the approval of any project, the EBRD should ensure that an energy audit is undertaken and that the project sponsor has given a written response to the audit's recommendations. Energy efficiency must be integrated into all of the EBRD's areas of operation and not be a niche activity.

Renewable energy

The Bank should set up targets for the financing of sustainable renewable energy.

Consistent with the principles of sustainable development, the EBRD should follow the practice of other international financial institutions and, as a minimum, adopt targets for lending for renewable energy. Therefore:

- In line with the European Investment Bank, 50 percent of all lending in the power sector in current or future EU Member States must be allocated to renewable energy by 2008.

- In all countries of operation there must a 20 percent increase in lending for renewable energy per year based on 1999 lending (the last year in which the EBRD made any significant finance available for renewable energy), in line with the target of the World Bank.

- Starting with the adoption of the new energy policy, the EBRD should accept only those projects that comply fully with the sustainable development principles set out in the EU Treaty and in the EU's international commitments on sustainable development and which are aimed at increasing the share of renewable energy. In the case of large dams, the EBRD should only support projects that meet international standards, including the recommendations of the World Commission on Dams.

Waste to energy generation

Projects that include Waste to Energy Plants or the use of Refuse Derived Fuel should not be eligible for EBRD financing under the new Energy Policy.

Energy generated from waste in various manners, such as waste to energy plants, refuse derived fuel or the use of landfill gas, cannot be classified as green, renewable or sustainable. Although it may be useful to exploit sources of energy that have not been utilised so far, these types of waste management should be considered as old-fashioned, end of pipe technologies that are inferior options in the EU waste hierarchy. Those types of projects which are disguised as clean sustainable energy projects should not be financed.

A special case is the use of landfill gas which has a major climate impact. Financing with money earmarked for climate issues should be supported.

Phasing out involvement in fossil fuel oriented investments

Over the next 5 years the EBRD should phase out investments in fossil fuel with the exceptions of efficiency improvements in existing power stations or the construction of highly efficient CHP power stations. In particular the EBRD should no longer provide funding for the extraction, processing and transportation of oil.

Clear indicators for the monitoring of transition impacts

Transition impacts' monitoring must be based on a set of clear indicators and should include social impacts.

There is an absence of publicly available empirical data on the transition impacts and benefits of EBRD financed projects. Furthermore the transition impacts - as they are presented as part of Project Summary Documents - are formulated in extremely general terms and usually do not contain the social impacts/benefits. Therefore the EBRD should adopt clear reporting guidelines for the measuring of the transition impact of projects that would include a set of measurable indicators, both quantitative and qualitative. In particular, regional and local impacts and benefits (including social ones) of EBRD investments should be monitored systematically and, if necessary, be mitigated.

The reporting of transition impacts - based on a set of determined indicators - should be locally driven and participatory; all information and ongoing assessments should be made publicly available in a timely manner.

The EBRD should clarify that it is seeking to produce local sustainable energy supplies to deliver transition and development, rather than prioritising the security of western energy supplies. Otherwise there is a risk of pushing countries down the road of oil dependence and the resource curse, increasing the risk of bribery and corruption. The EBRD should ensure that adequate governance measures covering economic, social and environmental issues are in place before considering investment in hydrocarbons. The timing of the EBRD's involvement is crucial in order to make sure adequate frameworks are in place.

Production Sharing, Host Country and other similar agreements

Some project sponsors – for example Sakhalin Energy (Shell, Mitsui, Mitsubishi) in the case of the Sakhalin II project – profit from unbalanced Production Sharing Agreements that are unfavourable to the host country. **The EBRD should be involved only in such projects where the Production Sharing, Host Country and other similar agreements are able to demonstrate that national, regional and local benefits live up to best international practice.**

Revenue and contract transparency

The EBRD's new Energy Policy should include a set of requirements in order to ensure proper revenue and contract transparency in extractive industry projects.

It is disappointing that the EBRD's evaluation of past performance in the extractive industries, recently carried out by the Independent Project Evaluation Department, does not provide any specific recommendations with regard to revenue and contract transparency. This is particularly concerning in light of efforts by other international financial institutions to vigorously pursue revenue transparency, such as the World Bank Group and the IMF.

The EBRD's new Energy Policy should clearly reflect the following revenue and contract transparency requirements:

- Public disclosure of all revenue payments (including royalties, taxes, commodity based payments, signing bonuses, etc.) made to governments and their agents by all extractive projects that receive the financial support of the EBRD, including those made via financial intermediaries;

- Public disclosure of all revenue payments received from the extractive industries by all governments receiving loans or technical assistance from the EBRD;

- Public disclosure of key contractual agreements (HGAs, IGAs, & PSAs) for all extractive projects funded by the EBRD; and

- Mandatory disclosure of the transparency-related requirements contained in EBRD loan agreements and investment contracts with sponsors (it should be noted that the Asian Development Bank requires public disclosure of its loan agreements). Furthermore, require the specification of acceptable disclosure mechanisms, including in what documents and locations the required information may be found.

Serving the interests of local communities

The EBRD should ensure that there is an open and public planning process to distribute revenues in any extractive industry projects fairly, whether this is provided for in the national legal framework or established on a project-specific basis. Further, the local communities affected by the project should have equal access to the information they need for meaningful participation in negotiation processes, in order to obtain free prior informed consent. The consent of locally affected communities should be a pre-condition for EBRD lending. This is particularly relevant with regard to Indigenous Peoples, considering that FPIC is already an internationally accepted standard for Indigenous Peoples. Projects must deliver measurable and clear social benefits for the region, such as increasing employment. Information on revenue, expenditure as well as environmental and social impact information should also be publicly available during project implementation.

The EBRD should only support extractive industry projects that have the agreement of indigenous peoples and locally affected communities. For indigenous peoples, agreement will be arrived at through their own customary decision-making processes and does not amount to an individual veto over development, but rather enhances indigenous peoples' self-development and overall development effectiveness. This process should include meaningful and good faith consultation with indigenous peoples and affected communities, and informed participation in the decision- making process. All agreements between relevant parties have to be made publicly available.

Emergency response

All extractive industries projects should ensure that emergency response plans are in place from the outset of a project, involving plans and procedures to establish good lines of communication to be able to warn local communities, sufficient recognition of potential impacts, and adequate monitoring and maintenance. **Project approval must also be subjected to obligatory insuring of associated risks** by independent insurance companies in adequate amounts and to the requirement of establishing a liability fund by the project sponsor. Information about the involved insurance companies, potential indemnities and procedures for compensation must be public.

High standards for shipping

EBRD financed projects should support only the use of safe, modern, and well-run vessels to carry oil, LNG or hazardous cargoes. Safety, age criteria and labour standards should be required for all such vessels, along with systematic and stringent inspections.

Establishment of No-go zones

The EBRD should not finance any oil, gas, or mining projects or activities (including technical assistance) that might affect existing World Heritage properties, current official protected areas, or critical natural habitat (as defined by the World Bank Natural Habitat Policy) or areas planned in the future to be designated by national or local officials as protected. In addition, any extractive industry projects financed within a known "biological hot spot" must undergo additional alternative development studies.

Under no circumstances should the EBRD support extractive projects in areas involved in or at high risk of armed conflict.

Gold Standards for Joint Implementation and Clean Development Mechanism projects

The EBRD should ensure all Joint Implementation (JI) and Clean Development Mechanism (CDM) projects are fulfilling the Gold Standard.

Gold Standards, the best practice benchmark system for CDM and JI projects that is supported by the NGO community, would allow the EBRD to balance its carbon footprint. It is already applied by several EU governments (e.g. Germany, Denmark) and also finds supporters among businesses. In the last few years the EBRD has increased its involvement in JI and CDM projects, a fact reflected in the new Environmental Policy where participation in JI and CDM projects is explicitly mentioned as one of the regional and global initiatives where the EBRD wants to participate. As the EBRD's environmental mandate incorporates "additionality" and "transition impacts" it is necessary that EBRD JI and CDM projects provide carbon credits of a high environmental quality, such as is guaranteed by the Gold Standard.

Gold Standard projects:

- are restricted to renewable energy and demand side energy efficiency projects because these technologies carry inherently low environmental risks;
- comply with an explicit 'additionality' test that is used to screen out projects that would have happened without the CDM;
- use a methodology deploying environmental and social indicators to check the contribution of a project to sustainable development.

GHG accounting for EBRD funded projects

Based on the accounting of greenhouse gas (GHG) emissions caused by funded projects, EBRD activity in the energy sector should bring about a decrease in GHG emissions.

The new EBRD Energy Policy should show a clear priority to switch from the financing of fossil fuel extraction towards the development of renewable energy and investments into energy saving. Towards this overall goal, the new policy needs an evaluation instrument which would allow measuring the contribution of a particular project to global climate change. All EBRD projects should be evaluated in terms of their direct and indirect greenhouse gas emissions. The accounting of GHG emissions should be done for the direct impacts of project activities as well as for the indirect effects. In other words, emissions from the extraction and transportation of fossil fuel should be taken into account as well as direct emissions from the combustion of fossil fuel. At the same time, emission mitigation by energy efficiency and renewable energy should be taken into account as well. The EBRD can set up a certain target for the balance of the project's contribution to global climate change. The total balance should show a decrease in GHG emissions as a result of EBRD activity in the energy sector.

The procedure of GHG accounting should be included into the environmental impact assessment procedure and the results of such accounting should be available to the public. As a starting point, the EBRD should use the Intergovernmental Panel on Climate Change's approved methodologies for GHG accounting. Furthermore, the development of EBRD-specific GHG accounting schemes should be done in an open manner where all interested parties including NGOs, academia and the private sector will be able to participate and provide comments. The accounting of GHG emissions should not become an instrument for the EBRD to take part in the international market of GHG emissions allowances; it should rather be an instrument to evaluate the overall quality of EBRD investments in the energy sector.

Exclusion of nuclear energy investments

The new EBRD Energy Policy should clearly state that the bank will not support any projects that are aimed at the construction, completion or upgrading of nuclear power stations.

The current policy regarding the completion of new nuclear units dates back to 1995 and allows the EBRD to finance nuclear projects only when it will lead to the closure of high-risk nuclear units. Today, only the Russian Federation still has high-risk units in operation with no binding closure schedule, and there has been no progress with regards to the closure of these units despite the EBRD provision of support (with the NSA programme) to the country in previous years.

No other international development bank provides support to nuclear projects. The EBRD's own experience with completing new reactors showed that these are not suitable investments for the EBRD or other IFIs as they are risky investments and are not competitive when compared to non-nuclear alternatives.

The many discussions regarding the K2/R4 project in Ukraine have clearly demonstrated that the project received support only because of its political background, rather than any banking principles. The EBRD should defend itself from similar political pressure that damages its environmental credibility and independence by closing the option with a policy which clearly excludes the completion and upgrading of nuclear units.

Closure (decommission) issues

The EBRD should adopt clear guidelines and require, as a condition of financing, that there is provision for sufficient funds to be built up in the balance sheet for closure from the start of any new development, including the decommissioning and clean up of polluted areas. This should be independently verified and annually updated, and the closure plans should be available to the public. These plans should also take social considerations into account.

Avoiding "perverse subsidies"

The Bank's operations in the energy sector have to be scrutinised in order to exclude those projects which promote different forms of "perverse subsidies" in the energy sector and/or support the replacement of state owned monopolies by private or public-private ones.

The fast-paced liberalisation of the energy market in Central, Eastern and South-Eastern European countries leads the governments to give up more and more restrictions in the fight to attract private investors. This process also includes the transfer of direct and in-direct benefits to potential investors –

benefits that go far beyond normal market incentives and often result in the enrichment of national or regional private monopolies. Part of these benefits come in the form of so-called “perverse subsidies” – various forms of state-owned loans or guarantees for private borrowers, long-term contracts for the buy-out of energy at fixed prices, low interest credits, fees for available installed capacities, budget funding for research and impact analyses, agreements for future privatisation on special conditionalities, lower pricing of already existing state-owned energy assets, state/municipality-funded energy infrastructure for particular projects, “patching” the project by keeping its “dirty” parts (such us environmental liabilities or liabilities for nuclear accidents) under public/budget funding, etc. All such subsidies – open or hidden – distort a future free market in the energy sector and predetermine a number of problems for consumers and taxpayers. At the same time, the use of “perverse subsidies” maintains a high ratio of fossil fuel and nuclear based energy, thus effectively blocking the growth of cleaner and safer forms of energy production.

Social and environmental aspects of energy privatisation

The new Energy Policy should include provisions to effectively mitigate the possible negative institutional, social and environmental impacts of energy privatisation actively promoted by the EBRD.

The EBRD has emphasised the role of privatisation within the energy sector. However, the important factor is not the ownership of a particular company but the independence, mandate and enforcement capabilities of the regulator. Experience has shown that privatisation can bring its own problems, in particular for the electricity sector with storage difficulties and constant demand. In many countries of operation, privatisation is being carried out in a hasty and non- transparent fashion that also leads to negative social as well as environmental impacts.

The new policy should include the requirement for conducting an SEA of privatisation projects prior to approval for funding. Rigorous assessment of potential social and environmental risks will help projects realise less environmental/social harm and more benefits. Along with making SEA a mandatory provision of the new policy, the Bank should acknowledge the fact that the privatisation of state-owned entities and sector deregulation brings heavy social/environmental impacts. In addition, the EBRD should create a set of measurable social and environmental indicators for project related transition impacts in order to gain a complete picture of total project impacts. Project finance should not be tied to the prescriptive liberalisation of energy sectors but instead should be linked to the improved governance of these sectors based on transparency, accountability and genuine public participation.

Financial intermediaries

Project financed by the Financial Intermediaries must be required to comply with national and international standards, equal to projects directly funded by the EBRD.

The new Energy Policy should reflect the proposal of the Project Evaluation Department with regards to the compliance with national and international standards (e.g., EU, WB, UN, etc.) of projects financed by Financial Intermediaries (FI). The EBRD should also prepare sub-sector guidelines for FI. FI should be included in any energy strategy and targets. The balance of the overall portfolio could be completely unsustainable if, for example, coal projects were to be financed through FI to escape central EBRD restraints. If renewables targets are to be achieved in country, then it is essential that FI are included in the strategy.