Heavy Footprint

The World Bank and Environment In Europe and Central Asia

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Edited by
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CEE Bankwatch Network, Budapest
2000.

ISBN 963 004206 1

This publication was supported by the Regional Networking Project, sponsored by Freedom House, with funding provided by the U.S. Agency for International Development.

The opinions expressed herein are those of the authors and do not necessarily reflect the views of Freedom House or USAID.

Cover design: Ekologika Bt.
Layout: Dénes Nagy
Illustration: János Fodor
Back cover photo: Stephen D'Esposito, Mineral Policy Center
Printed by Saluton Bt. Budapest, Hungary

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Preface and acknowledgements

This publication is a result of the common effort of the people, most of them associated with the CEE Bankwatch Network. Editors are grateful for their contribution, suggestions, and comments, which made this book possible. We are especially grateful to Roberta Harper and Dénes Nagy in editing the text and preparing the layout.

Special thanks to the Freedom House for supporting the publication as well as to the C. S. Mott Foundation, Wallace Global Fund, and Heinrich Boell Foundation for making possible activities of CEE Bankwatch Network in connection to the World Bank Annual Meeting in Prague.

Merits of the book are of many people, however the responsibility for possible mistakes and the opinions expressed rest only on the shoulders of the authors and editors of the publication.

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Radioactive Loan to Czech Republic

Introduction

In 1994, the World Bank gave a USD 246 million loan to the Czech Energy Enterprise (CEZ) utility company. The aim of the loan was to decrease negative impacts of the electricity production on the environment. At that time, the production was mainly based on outdated lignite-fired power plants. The modernization program, completed in 1998, put an emphasize on fossil fuel power plants.

Construction of the Temelin Nuclear Power Plant, which is situated in South Bohemia, started in 1985. The design is based on old Soviet VVER-1000/320 reactors, upgraded during the 1990s in cooperation with Westinghouse Corporation. A planned capacity is 2 000 MW (two reactors) with annual production of 11.3 TWh.

This combination of Soviet and Western technologies has never been tried before, meaning that the performance and safety are unpredictable. The pioneering nature of the project, which the Swiss consultant firm Colenco called "the most complicated nuclear project in the world," would be a challenge even for the best management. Unfortunately, the management of the Temelin can only be described as chaotic. During the 1990s, the entire decision-making structure of the Temelin site changed several times.

Since the Temelin project, the largest part of the CEZ investment portfolio has gone for nuclear projects. The CEZ's official investment plan for the period between 1999-2006 is to spend 69 percent of the two billion budgets on nuclear development projects. In fact, two out of five projects financed by the World Bank loan were directly connected to the highly controversial Temelin Nuclear Power Plant. Although the CEZ violated the financial conditions that were determined by the loan contract, the World Bank did not react. In other words, after the loan was signed and the Czech government gave a full loan guarantee to the World Bank (which secures the Bank from financial risks) the Bank simply ignored the way in which the money was spent.

The World Bank itself, in the 1992 report advised the Czech government not to proceed with the Temelin. After more than five years of accumulated delays and cost overruns, which have nearly tripled the overall budget, the plant is still under construction.

On The Surface, a Positive Project

The World Bank's ENERGY I loan of USD 246 million was designed primarily to decrease the environmental impacts of electricity production in the Czech Republic, that were at the time primarily caused by outdated lignite-fired power plants. The modernization program of fossil fuel power plants and the objective of the loan were officially completed in 1998- overall CEZ spent USD 1.5 billion for this purpose.

The North Bohemia region, located in the northeastern part of the country, provides 50 percent of the country's electricity, all from coal-burning power plants. The region has suffered from severe environmental pollution and landscape destruction mostly from coal mining and coal burning. Moreover, coal-mines have wiped out 113 towns and villages. Considering the environmental damage that the region has suffered, a loan for desulphurization seemed a blessing. However, emissions were reduced because of the decreased production not because of environmental reasons. The production cutbacks and potential shutdowns of newly upgraded plants made the investment in desuphurization useless.

To cut down the production, the CEZ did not need a loan since a very simple application of the emissions control technologies would have had an effect. Besides the CEZ had profits from cheap coal production since prices ignore the environmental and social costs. However, the CEZ did need loans for its hugely expensive Temelin Nuclear Power Plant project. Since loans for usually uneconomical nuclear projects are hard to get, the CEZ found it very convenient to purchase loans for the necessary environmental upgrades (the Clean Air Act required emissions reductions by 1998) and to use the profits for Temelin construction.

The CEZ is the major electricity utility in the Czech Republic, covering about 70 percent of the Czech electricity demand. Currently 75 percent of electricity is produced from coal, 23 percent from nuclear and two percent from hydro plants. Temelin will almost double the nuclear share. It is not surprising then, that since 1998, the largest part of the CEZ investment portfolio lies in nuclear projects: completing construction of the Temelin Nuclear Power Plant, modernizing of the Dukovany Nuclear Power Plant, and constructing a temporary storage facility for spent nuclear fuel. Although the World Bank denies the financial support for nuclear projects, loans from the Bank have, in fact, allowed nuclear development in the Czech Republic.

The World Bank Finances Nuclear Power

CEZ officially announced that the World Bank's loan was used for [1]:

[1] Source: CEZ Newsletter, March 30, 1998.

- desulphurization of the Prunerov II coal power plant;
- upgrades to increase efficiency at 12 coal fired generating blocks;
- training of corporate management;
- connecting the high-voltage transmission grid connection between Temelin and Chrast to the Prestice transforming station (2 lines each 400 kV); and
- audit examining of the Temelin Nuclear Power Plant's safety.

It is obvious that the two last projects financed by the Energy I loan was directly linked to the Temelin nuclear power plant project. Even with its scheme of shuffling financial flows to fund the Temelin project, the CEZ still needs this "environmental loan" to directly support the Temelin project.

CEZ‘s program to renovate coal power plants and reduce emissions – the main purpose of the Energy I loan - was successfully completed in 1998, the latest date possible under the Czech Clean Air Act. At that time, the CEZ had launched a large media campaign, proudly announcing that CZK 48 billion (USD 1.5 billion) had been invested for sulfur and nitrogen emissions reduction. As a result, the emissions of all power plants decreased by almost 90 percent.

As mentioned above, the CEZ investment program is mostly focused on nuclear power development. According to the plan for 2000, the CEZ will invest in:

- nuclear energy – CZK 13.4 billion (of this Temelin represents CZK 10.8 billion);
- desulphurization – CZK 0;
- transmission grid – CZK 1.2 billion;
- others – CZK 4.4 billion; and
- total – CZK 19 billion (USD 0.5 billion).

A nuclear program represents more than 70 percent and Temelin itself 57 percent of all expenses in 2000. The plan is similar for the following years (See Figure 1 and Table 1).

Figure 1. *Planned investments of CEZ between 1999 and 2006. The majority of total investments (69 percent) are planned to cover nuclear development projects (the bottom two sections in the graph). Numbers are in CZK billion.*

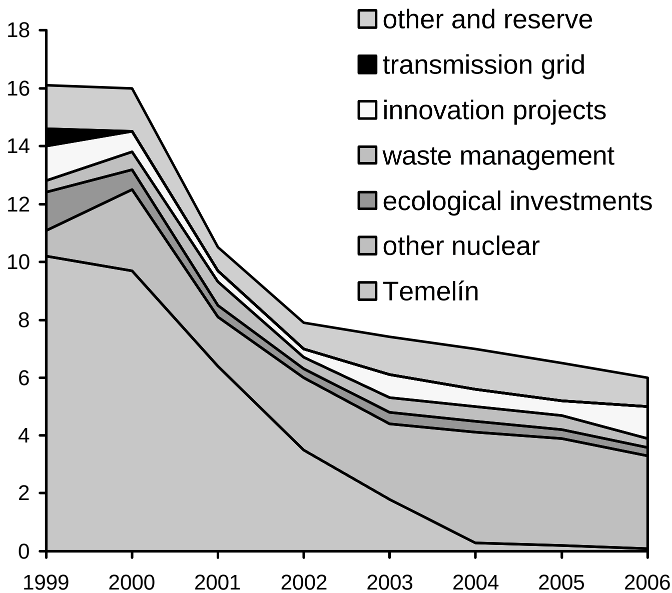


Table 1. *Planned investments of the CEZ between 1999 and 2006 (in CZK billion).*

Year	Temelin	Other nuclear projects	Ecology	Waste management	Innovation projects	Transmission grid	Others	Share of nuclear
1999	10.20	0.90	1.30	0.40	1.20	0.60	1.50	69 %
2000	9.70	2.80	0.70	0.60	0.70	0.00	1.50	78 %
2001	6.40	1.70	0.40	0.80	0.40	0.00	0.80	77 %
2002	3.50	2.50	0.30	0.40	0.30	0.00	0.90	75 %
2003	1.80	2.60	0.40	0.50	0.80	0.00	1.30	59 %
2004	0.30	3.80	0.40	0.50	0.60	0.00	1.40	59 %
2005	0.20	3.70	0.30	0.50	0.50	0.00	1.30	60 %
2006	0.10	3.20	0.30	0.30	1.10	0.00	1.00	55 %

The CEZ Violated Conditions of Loan

Not only has the loan been used for nuclear projects, which was against the World Bank's policy, but the CEZ has also violated the loan conditions. In 1999, the CEZ was not able to meet loan requirements (the corporate working ratio[2] and the debt service ratio[3]). According to its official business plan, the utility would not achieve those requirements until 2003.

[2] The Corporate Working Ratio is the ratio of total operational costs to the total operational incomes.

[3] The Corporate Debt Service Ratio is the size of net income compared to the debt service of that year (i.e. comparison of income to the amount of debt payments CEZ has to pay back in the given year).

Knowing that, the World Bank could have either cancelled the loan (according to the contract, such violations of the loan conditions enables the Bank to demand immediate repayment), or at least put a pressure on Czech politicians and on the CEZ, to shift theirs investment policy from nuclear power.

Figure 2. *Corporate Working Ratio. The required maximum value is 60 percent (dotted line). Values for the period between 1993 - 1998 are taken from CEZ annual reports. Values for the period between 1999 - 2006 are taken from the "CEZ Business Plan 2000-2006"*

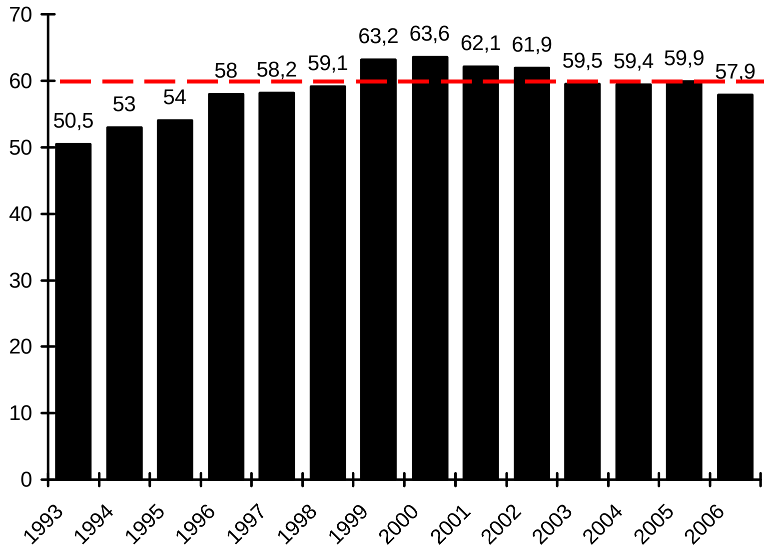
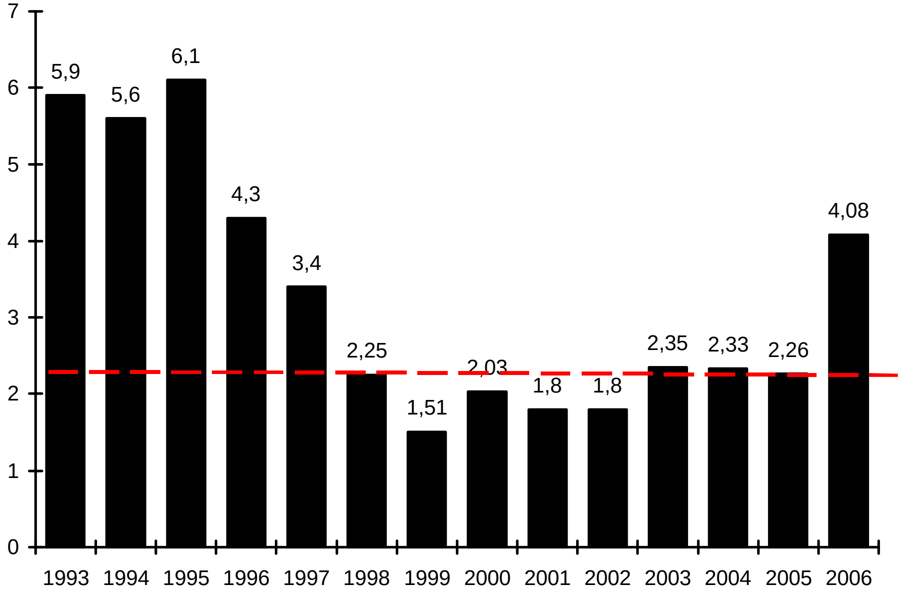


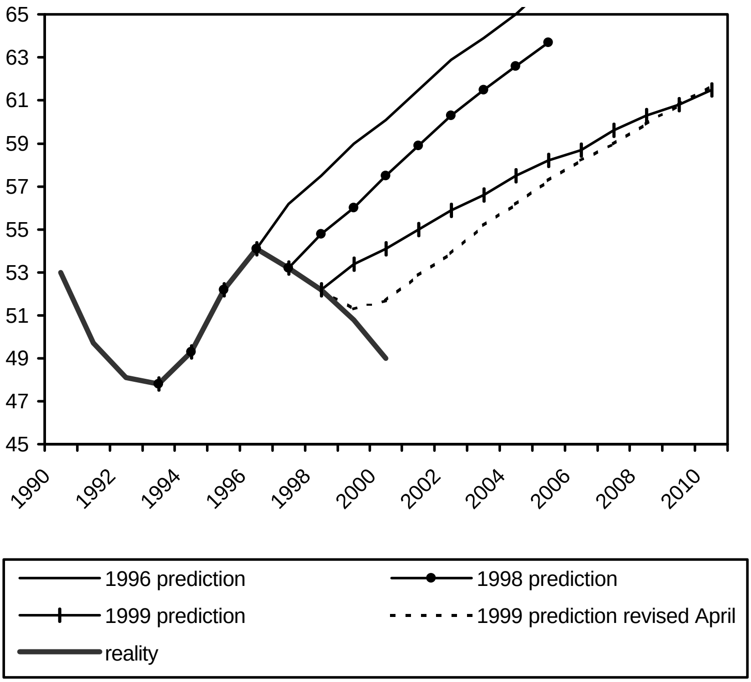
Figure 3. *Corporate Debt Service Ratio. The required **minimum** value is 2.2.*



False Figures Policy

Figures presented by the company are suspect. It seems that the estimation of the future electricity demand is far too optimistic. The graph (See Figure 4) demonstrates that the CEZ has been constantly wrong about its estimates. The company not only failed to predict the correct numbers, but also to estimate overall trends. As the graph shows, the CEZ has predicted a rapid growth from 1996, while the demand has been falling since then (as independent studies had correctly projected).

Figure 4. *Actual electricity demand compared to the CEZ's projections. The value for electricity demand in 2000 is the most recent estimate. Numbers are in TWh per year. Note the big difference between the two scenarios published for 1999. While the revised curve from April had to account for a further drop of demand in the first months of the year, its rate of growth was then artificially accelerated in order to meet the same level of electricity consumption by 2010 as in its previous prediction. (No figures were published in 1997.)*



Because of political reasons, the CEZ has been providing scenarios that supported a need for the large new nuclear capacity of Temelin (2000 MWe, 11.5 TWh per year) in the first decade of the 21st century. The company's predictions have been based on high-growth expectations that are incorrect for numerous reasons.

- The relatively rapid growth in consumption that occurred between 1993 and 1996 was only due to a major campaign that supported the use of electric heating in households. At that time the price was below production costs. Studies have shown that 60 percent of the increased demand during that period was due to the new electric heating systems. Since 1996, as the electricity price has rapidly increased, households began to switch away from electric heating systems. This trend is likely to continue as the prices go up. Due to price liberalization and subsidies removal prices will be 300 percent higher in 2006 than in the year of 1993.

- The Czech Republic, like other East European countries, suffers from very low energy efficiency. Compared to the EU average, the Czech Republic consumes 2.5 times more energy (as well as electricity) for the same level of economic output (calculated as purchase power parity). There are dozens of studies that demonstrate that the increased energy efficiency represents one of the most economical ways to meet energy needs. The World Bank itself, in a 1991 study, concluded *"Improved operating procedures and minor investments in industry, transport and public buildings could easily lead to a decline in energy use of 20 to 30 percent."* [4] To date, almost none of these measures have been undertaken.

[4] Czechoslovakia – Transition to a Market Economy, A World Bank Study, Washington, 1991.

Exports Are Not the Solution

Without the estimated growth in domestic demand, the CEZ faces a problem of overcapacity, even without Temelin. The only solution, apart from closing Temelin and shutting down even more newly upgraded coal power plants, is to significantly increase exports to the neighboring countries. The CEZ nearly doubled its exports in 1999, reaching 5.7 TWh, compared to 3.1 TWh in 1998, and in the first quarter of 2000 exports went up to eight to nine TWh.

Its plan to increase exports, however, is not likely to solve the CEZ's problems. The European Union has an overcapacity of at least 10 000 MWe, and the hard competition on the liberalized electricity market keeps the prices down at approximately CZK 600 per MWh (USD 16 per MWh). The Czech Company has been able to increase its exports only by selling electricity at CZK 560 per MWh,[5] which is well below production costs.[6] These prices may bring short-term profits – CEZ's variable costs are about CZK 455 per MWh[7]- but they are not sustainable in the long term. In addition, the CEZ will have to cover huge capital investments from the 1990s.

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[5] CEZ General Director Stanislav Svoboda said in an interview with the newspaper *Pravo* on January 24, 2000, that CEZ is selling electricity abroad for DM 30 per MWh, which is CZK 560 per MWh.

[6] CEZ overall production costs were CZK 780 per MWh in 1998: coal plants produced 73 percent at CZK 851 per MWh, Dukovany nuclear power plant produced 25 percent at CZK 570 per MWh, hydro plants produced two percent at CZK 852 per MWh.

[7] This value is for coal power plants. Temelin nuclear power plant will have, according to CEZ, variable costs around CZK 265 per MWh (while its overall costs are to be between CZK 900 and 1100 per MWh).

According to official figures[8], Temelin production costs (at current price levels) are CZK 900 per MWh (USD 25 per MWh). Although CEZ is now selling electricity to the domestic grid for CZK 1 150 per MWh – under which Temelin could be profitable – the opening of the Czech market and the energy sector's privatization would certainly force this price down. And, as it was already shown, Temelin's production will have to be exported to EU markets where the prices are even lower.

Temelin-Overflowing Budget, Overflowing Problems

The environmental impact assessment (EIA) has never been conducted. The EIA procedure was omitted partly because the project started under the communist's regime, before the EIA was mandatory. In spite of that, any changes within a project that could affect the environment, health, and safety require an EIA. Although the project has been changed, the CEZ and pro-nuclear government officials avoided an EIA procedure simply by not allowing access to the official documentation that could prove the project's negative impact on the environment.

In addition, the Temelin Nuclear Power Plant project has become a symbol of economic disaster in the Czech Republic. Originally budgeted at CZK 35 billion (USD one billion), a series of cost overruns has rocketed the price up to today's estimate of CZK 98.6 billion (USD 2.8 billion).

Since 1993, when the project was re-approved by the Czech government, its budget has risen by CZK 30 billion (USD 800 million). During the same period, it has accumulated delays of more than five years (See Table 2).

[8] Such as the complex report presented by Ministry of Industry to the Czech government in May 1999.

Table 2. *Projected budget and start-up date of the Temelin Nuclear Power Plant.*

Year of announcement	Total budget (billion CZK)	Year of start-up
1981	20	
1985	35	1991
1990	50	1992
1993	68	1995
1995	72	1997
1996	79	1998
1997	85	1999
1998	99	2001

With each price increase, the CEZ officials claimed it would be the last one pointing at a specific problem that has just been solved. Despite of that, promise of the "final price" has been broken more than ten times to date, each time with a new explanation. Even the World Bank warned the Czech government in 1992 that Temelin is not the best for the Czech energy sector. In its paper *Czech Republic Energy Sector Mission Aide Memoire*, the Bank stated:

"Implications of proceeding soon with Temelin Units 1 and 2, without electricity exports, would be... a heavy demand on the public budget, and an unnecessary increase in electric power prices to cover investment expenditures. This would not be in the interest of creditors or of Czech shareholders, neither the government shareholders nor new private shareholders. If the electricity generated by Temelin were not exported... it would result in large unemployment of miners and power plant operators. Possible solutions are: delay of Temelin until

domestic needs require it (for medium demand this would be after 2010), or arrange for export contracts for the Temelin generated electricity... a further option could be to convert the unfinished nuclear site to gas fired combined cycle operation."

The most recent evaluation of Temelin's economic status comes from the Independent Panel of Experts, established by the Czech Government in 1998. In February 1999, the Panel completed a large report making a strong case for abandoning the Temelin project. This report repeated and went beyond what the World Bank said before a renewed construction of the plant[9]:

- It is now without question that the decision made in 1993 by Prime Minister Klaus' government was wrong. If Temelin had been abandoned then, this clearly would have been the least cost scenario.
- Even today, if we consider past expenditures to be "sunk costs" and if we take into account only the budget yet to be spent, the economy of the project is highly questionable. Should the investment give full returns, this would require a scenario of high electricity prices maintained over the entire lifetime of Temelin, and sales at full capacity of Temelin's production. According to the Final Report, the likelihood of this scenario is very low. In fact, today's situation is the opposite: prices of electricity are low and Temelin's capacity is not needed at all. Should the investment in Temelin pay back enough to at least reach zero profit for CEZ, transition to the "optimistic"

[9] Final Report of the Team of Experts for Independent Evaluation of the Project to Complete Construction of the Temelin Nuclear Power Plant, Prague, February 28, 1999. The full English version of this study is available upon request.

(high costs, full consumption) scenario is necessary before 2006. This is also very unlikely.
- The Czech Republic already suffers from overcapacity, with several additional sources under construction by independent producers. As a result, there is no domestic market for Temelin's capacity until the year 2015. Even under a high-growth scenario, experts state that there are cheaper ways to secure electricity needs without Temelin. Because an overcapacity exists as well on the European electricity market, the situation may get even worse for Temelin after the Czech Republic joins the open EU electricity market.

There Are Alternatives

As the above discussion of exports made clear, Temelin’s capacity is not needed in the Czech energy market. In longer term, Czech Republic has other, more effective ways to cover its energy and electricity demands:
- First of all, to improve energy efficiency.
- To promote gas-fired co-generation plans. Several projects are currently under construction by independent companies, and this will further increase generation capacity in the Czech Republic.
- Renewable sources also provide reasonable potential - wind, small-scale hydro plants and biomass could cover about ten percent of Czech energy needs by 2010 or 2015 (their current share is 1.5 percent).

Citizen Opposition to Temelin

Concerned about the World Bank's loan and its purpose, local CEE Bankwatch member Friends of the Earth Czech Republic raised the issue with the Bank and asked them to cancel the loan or at least force the CEZ to abandon its nuclear program. The initial response of the Bank in 1998 was: "as far as we know, the money is going to modernization of the coal power plants." When the potential contract violations became apparent, Friends of the Earth decided to pursue the case more strongly, with a study that showed the World Bank's loan contribution to the Temelin project. This time, in a meeting with Petr Holbi, CEE Bankwatch Oil and Climate Coordinator, Bank staff responsible for the loan could not deny any of the findings, so they interpreted the same findings in a different manner. The Bank stressed that the project has been successful. The two projects directly linked to Temelin were explained as a necessary one that would have been done anyway.

The Temelin project in general has aroused active opposition both within the Czech Republic and abroad. Within the country, Temelin has been one of the most controversial environmental issues since the fall of Communism in 1989. The country's most influential environmental citizens' organization, Friends of the Earth, has organized a long-running campaign against the plant construction. Outside the country, Temelin has caused significant tensions between Czech Republic and Austria, since Temelin is only 60km from the border.

As the project drags on, the history of failed promises and forecasts (both by CEZ and politicians) cause stronger public rejection to the project construction. A year ago, even President Vaclav Havel made a highly critical statement about Temelin:
"Over the years I have come to the conclusion that I cannot henceforth be silent on this matter, that I cannot stand idly by… For decades we fought, or at least many of us fought,

against the totalitarian system and against the centralization of all power. I do not think that we fought against the Communist government in order to have it be replaced by some peculiar, more hidden and more inconspicuous dictatorship of a single company, even one as respected as CEZ… CEZ has deceived us nine times. Nine times they quoted us a price and start-up date for this power station which later proved to be false. I do not have any reason to believe CEZ. I have been lied to nine times. I do not know why I should believe them in the 10th case.” [10]

More recently, a coalition of more than 150 civil society groups, including national environmental groups, local historical heritage conservation associations, the country's largest humanitarian aid foundation and cancer-prevention advocates, demanded a national referendum on Temelin before the plant starts to operate. The Prime Minister had promised a referendum on Temelin before the last elections, but since taking power he and his cabinet have ignored the call for a referendum.

Conclusions

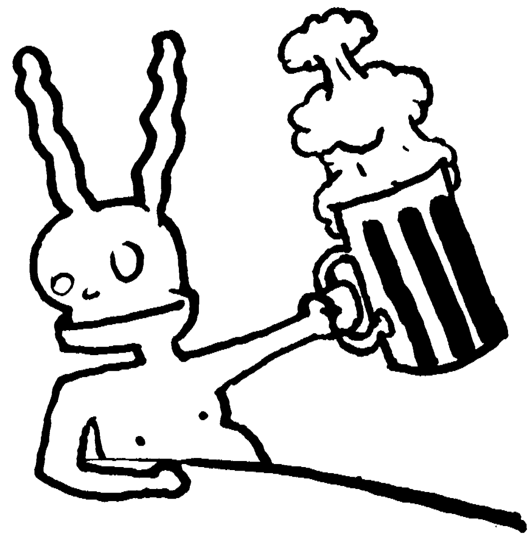
The World Bank has often been criticized by nongovernmental organizations (NGOs) and community activists over the years on blindly dishing out loan money without adequate controls on how its money is used. According to these critics some of the noble goals that the World Bank proclaimed have failed many times. The Temelin project is another case in point.

[10] Press conference of the President of the Czech Republic Vaclav Havel on the issue of Temelin, May 12th 1999.

Along with other loans that the CEZ received in recent years (and many of these lenders also claim that none of their money went toward nuclear projects) this World Bank's loan allowed the CEZ to push forward an investment plan that focuses on nuclear power. This nuclear-based energy strategy creates a safety threat for Czech citizens and those of neighboring countries, and leaves a legacy of nuclear waste for future generations. Just as seriously, it has sent the Czech economy backwards rather than forward onto a more modernized efficient path to economic development. This is something that the Czech economy can not afford after several years of recession, and with incorporation into the more competitive and efficient European Union market looming in the near future.

The World Bank would like to look at the Energy I loan as illustrating its potential to contribute positively to sustainable development. However, as this study shows, the Energy I loan clearly illustrates why the World Bank's good intentions often lead to disaster. This lesson is a crucial one in the present context, after the World Bank has spent much of the past decade developing policies and procedures attempting to be more open and to take social and environmental factors into account.

The World Bank claims that it does not support nuclear power. This ring empty if the Bank gives money to companies like CEZ whose main focus is obviously the development of nuclear power.



Leaking Pipeline

It is generally acknowledged that provision of the MDBs' financial resources to developing and transition countries helps shape the country's way of development. In Russia, a significant share of financial support from the World Bank has been directed to the oil industry. On the one hand, this financing has aimed to contribute to the economy's recovery, since the oil sector serves as the main source of income for the country. On the other hand, such support pre-defines further heavy dependence of the country on natural resource extraction and implies damaging consequences for the environment and, thus, local populations.

Sector background

The Soviet State was characterized by a strong economic and social dependence on the extraction industries such as oil, coal, and gold. This resulted in reliance of economy upon non-processing activities and supply of cheap raw materials abroad. The export of oil and gas has remained the main single contributor to the country's budget providing around half of the country's hard currency revenue[1].

The Soviet oil and gas industry performed according to the principle that represented the quantity as a good substitute for the quality. All efforts were directed towards short-term increase in production and export volumes at the expense of the future sector capabilities and the environment. In addition, discharge of oil through ruptured infrastructure has been, and still is a common practice in Russia. Currently, approximately

[11] Grigoriev, A. 1995. Russia: foreign investment in oil and gas. *Taiga News* (3).

eight to ten percent of produced oil (20-50 million tonnes) is released into the environment each year[2].

Generally, the oil industry of Russia, as of many former Soviet Union countries, is burdened with a number of acute problems related to non-sustainable resource depletion, the use of outdated equipment, inefficient management, bad practices, and absence of transparency and accountability. For the local populations and indigenous people this has turned into violation of the rights, resettlements, reduction of food stock, and a lack of compensation[3].

To keep the reputation of a multilateral development agency, the World Bank had to take the difficult task not only to mitigate environmental impacts of the future operations, but to address the existing problems in the Russian oil sector as well**.**

IBRD Lending

Since Russia joined the World Bank in 1992, the IBRD has provided only three loans to the oil industry out of 45 loans. However, the amount of financing for these three loans was quite significant. The three oil loans accounted for approximately 10 percent of total IBRD lending to Russia over the last nine years.

The first two loans were directed to oil rehabilitation in Western Siberia and will be considered together, since they

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[2]Lexin, V. and Andreeva, E. 1995. Regionalnaya politika v kontexte novoi Rossiyskoi situasii. Moscow: Sovremennik.

[3] Suliandziga, P. 1998. *Environmental problems affecting the traditional lifestyles of indigenous peoples in the Russian North*. Moscow: RAIPON.

have similar objectives. The third loan was committed for environmental purposes and will be discussed separately.

Oil Rehabilitation I

Amount of financing: USD 610 million
Approval: June 1993

Oil Rehabilitation II

Amount of financing: USD 500 million
Approval: June 1994

The oil rehabilitation loans had the following principal objectives:

- to strengthen Russia’s ability to earn foreign exchange in the near term through increased oil production and exports;
- to support sector reforms to catalyze the equity and loan finance and international participation;
- to transfer international, technical, environmental and managerial practice; and
- to promote a more efficient and environmentally sustainable use of Russia’s petroleum resources.

The first two objectives were implemented - a decline in oil production in Western Siberia stopped, which contributed to stabilization of Russia’s hard currency earnings. According to Bank approach, the stabilization and increase in oil production is linked to economic recovery and growth in the country. This way of thinking arises from the short-term approach that cures problems on the surface creating only temporary effects on the economy. According to the EBRD's Transition Report Update from 1999, the Russian economy showed 3.2 percent growth. However, this growth was largely due to the steep increase in the world oil prices and masked the lack of reform in the oil and other sectors.

For the sake of a near-term rise in oil revenues, the development of fuel mineral reserves, which implies accelerated depletion of resources, is the favored activity in the country. At the same time, long-term consequences are being ignored. The first evidence of inevitable reserve depletion has already been revealed. Approximately 56 percent of oil reserves in the Western Siberia are depleted, with the water content exceeding 90 percent. Simultaneously, the annual addition of oil reserves has not been compensating the annual production since 1994[4] Further support to increase the production would not correspond to the Bank's policy of promoting the sustainable use of the Russian petroleum resources.

Oil Rehabilitation projects had significant environmental dimension such as mitigation measures, reconstruction of the existing infrastructure, and strengthening the environmental capabilities of the operating oil associations. However, the whole idea to protect the environment seemed unfeasible because of the gap between goals and costs. According to OECD/EIA estimations[5], the investment of USD 6 billion would be needed for the rehabilitation of only one oil field in Western Siberia. Moreover, these estimates would increase significantly if clean-up measures became mandatory[6]. Thus, environmental concerns could not be considered essential parts of these projects, since the proposed amount of USD 1.1

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[4] Kaibysheva, L. 2000. U neftyanikov [With oil industry staff]. *TEK 1.*
[5] Organization for Economic Co-operation and Development (OECD), US Energy Information Administration (EIA). 1995. *Energy policies of the Russian federation.* Paris: OECD/EIA.
[6] Schmidt, E. 1996. *The World Bank and Russian oil: a dark future for man and climate.* Bonn: WEED.

billion is not sufficient to cover both the environmental component and production expenses. Therefore, the operations actually aimed to increase the production without paying proper attention to environmental issues.

It appeared that the Bank moved into the country with its first Oil Rehabilitation project without careful assessment of the situation in the sector. In addition, criminal activities and corruption affected the oil sector, which caused difficulties in project implementation as well[7]. Strict implementation measures were needed, but they were missing from the Bank's first agreement. Similarly, the environmental dimension of the project was not clearly defined. There were no time frames for the implementation of required measures such as reducing stress on the environment, monitoring, and enforcement. The absence of strict requirements caused a gap between the initial project goals and performance in practice.

Later on, another oil project in Western Siberia was to be implemented. Since the Petroleum Joint Venture aimed to increase the production, which would have caused further environmental degradation, NGOs strongly opposed to the project implementation. The increase of oil production would seriously affect the quality of life of people in the region[8]. Finally, the project was rejected, but largely due to withdrawal of the foreign partner Amoco from the operations.

More potential oil loans were canceled in the past due to the Bank’s requirements for procurement agreements. According to the Russian newspaper Segodnya (1996) Russian companies (Yuganskneftegaz, Tatneft, and Permneft) refused the Word

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[7] Karnaukhov, S. 2000. Neft and criminal [Oil and criminal activities]. *Neftegazovaya ertical* (2).

[8] Friends of the Earth. 1994. *Drilling for oil: a recipe for disaster in Russia.*

Bank credits mostly because of the Bank's condition, which allowed tender of equipment supply only to foreign companies. It should be stressed that Russian equipment that was sufficient to meet technical standards was available at that time at 40 percent lower price than of overseas facilities. Thus, the Bank's inclination towards dealing with foreign equipment suppliers seemed quite absurd and contradicted with the World Bank objectives to promote economic recovery. The engagement of domestic contractors could have increased both the amount of finance remaining within Russia and the number of jobs.

Emergency Oil Spill Recovery and Mitigation

Amount of IBRD financing: USD 99 million
EBRD co-financing: USD 25 million
Approval: April 1995

This loan has a primary environmental purpose with the following objectives:

- to prevent oil spills and to minimize the quantity of oil released during the runoff;
- to prevent the damage to the Pechora river basin;
- to stabilize oil in the spill area prior to spring thaw and to minimize the quantity of oil released during the runoff;
- to continue with the clean up activities;
- to increase a pipeline safety in the short term; and
- to consider a replacement of the pipeline in the long term.

The loan was provided only for environmental purposes with an emphasis on the clean up activities of the Komi Republic, which was affected with the 100 000 tonnes[9] oil spill. It is

[9] World Bank. 1995. *Oil spill recovery and mitigation project.* Project information document RUPA 40409.

worth mentioning that the amount of the loan for Spill Recovery and Mitigation project was more than five times lower in comparison with the impressive amounts directed to the oil production.

The World Bank and EBRD were indirectly involved in the oil spill of 1994 through their support to the oil joint ventures Polar Lights (IFC USD 60 million, EBRD USD 90 million) and KomiArcticOil (EBRD USD 80 million), since the operating companies were using the leaky pipeline that caused the devastating oil spill. However, neither of the banks committed soft loans for the clean-up, and the loan to the Russian Federation was to be paid back by the Russian citizens, some of which suffered damage from the spill.

The Komi project helped to overcome the environmental damage in the region after the spill. However, the Bank could have enhanced requirements on the project implementation and monitoring.

Being aware of a poor environmental behavior in the past and the insufficient capacity of the implementing agency KomiNeft, which is the owner of the infrastructure, to perform the clean up the Bank stipulated the involvement of the international management contractor Australian-American company Hartec. However, a management team within KomiNeft was put in charge to review, approve, and monitor the contractor’s activities[10], which actually meant the establishment of the KomiNeft's responsibility over the project performance.

The lack of continuous external supervision resulted in disposal of removed oil and snow mixture in sumps lacking

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[10] IBRD. 1995. *Oil spill recovery and mitigation project.* Technical annex T- 6578-RU.

hydro-insulation in the dangerous proximity from settlements. The selection of oil combustion in the open environment as the main method of clean-up also appeared doubtful from the environmental point of view, since burning of 7 000 tonnes of oil[11] caused substantial emission of various toxic substances threatening the health of local villagers and wildlife.

Five years after the oil spill, the locals remained unsatisfied with the quality of clean up activities. Meanwhile, the World Bank refused to provide the information about the progress of the mitigation, although its Pollution Prevention and Abatement Handbook proclaims the project progress awareness as a major condition of active public participation and high-quality monitoring.

Present IFC Financing

Russia became an IFC member in 1993, and the very first year of its official membership was opened by two oil sector loans. The IBRD ended its oil projects in Russia with the three loans, but the IFC has continued its financing of the oil industry up to date.

According to the new World Bank Group Country Assistance Strategy for the Russian Federation, the IBRD will shift its financing from energy and infrastructure, and the IFC will concentrate on „export-oriented areas where foreign investors see strong comparative advantages and lower country risks"[12] (oil and gas, gold and other mining).

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[11] Komineft, Hartec. 1995. *Plan szhiganiya nefti na razlivah nefti v Komi respublike* [Plan of oil combustion in the Komi Republic]. Internal document.
[12] World Bank Group. 1999. *Country assistance strategy for the Russian Federation 1999- mid2001*. Public information notice.

The IFC, as an institution oriented to the private sector, is strongly demand-driven. Therefore, if the loan recipient does not give a high priority to the environment, the IFC does not have the ability to influence the national policy framework or to promote green projects. In Russia, operating oil companies are orientated towards higher production to increase the profit. Low demand for environmentally friendly projects from the clients in the country has partly shaped the IFC behavior as well. To the present, not a single loan with primary or major environmental objectives such as clean up and recovery, remediation, significant mitigation, and infrastructure replacement has been provided to the Russian oil and gas sector. Instead, the IFC sponsored a number of projects directed to the expansion of existing operations or development of new reserves.

Polar Lights Project

Amount of financing: USD 60 million
Approval: 1993

This project includes the development of the Ardalin oil field in the Komi Republic, drilling of 24 wells, establishment of treatment facilities, and construction of a pipeline to connect the Ardalin complex to the main Russian pipeline.

Through this joint venture, the IFC became indirectly involved in the catastrophic Komi oil spill. Polar Lights was one of the numerous joint ventures established with the support of western companies. Timan Pechora Company was engaged in the Komi oil development and it was using the leaky infrastructure, which caused the devastating spill. Approximately 1 500 tonnes per day were pumped out through the pipeline[13]. According to the Greenpeace, the Komi spill was not an unexpected event – oil was released into the environment continuously from the January 1994, till the end of the year. Thus, if the operating companies had not ignored the leakage, the latter oil spill could have been prevented.

According to the IFC procedures, appropriate analyses of the site should be performed prior to the loan approval. This includes assessment of the state of existing facilities and infrastructure and potential impacts on the environment. The bank's involvement into this risky venture could be explained with inappropriate environmental analysis conducted by the project sponsor and with the consequent IFC's ignorance of infrastructure problems. Another explanation might be the Bank's ignorance of environmental safety in favor of financial benefits. Considering the poor environmental capabilities of Russian companies in 1994 and a long practice of misreporting, it is likely that sponsor did not perform adequate environmental analysis. However, this would testify the bank's entire reliance on the information provided by the project sponsor and its capabilities to undertake environmental studies.

Vasyugan Services Project

Amount of financing: USD 10 million, 1.5 million quasi-equity
Approval: 1993

The project consists of the increase in the oil and gas production from the wells in the Tomsk region. No detailed data on its objectives and outcomes is publicly available due to

[13] World Bank Group 1998. *Pollution prevention and abatement handbook*. Washington: World Bank.

non-retrospective nature of the IFC information disclosure policy.

The most recent IFC loans were provided with the main objective to support private sector hydrocarbon development through assistance to small independent companies in completion of their financing plans for the investment program.

Aminex Project

Amount of financing: USD 17 million, 3.05 million equity in 1997
Amount of financing: USD 0.12 million equity in 1999

The project aims to recover the crude oil from the Kyrtayel oil field in the Komi Republic for export to Western Europe.

Bitech Silur Project

Amount of financing: USD 17.5 million, 7.5-million equity
Approval: 1999

This project consists of full development of South Kyrtayel and Lekker oil fields in Timan-Pechora region (Komi Republic), installation of drilling and gas re-injection facilities, and the extended seismic studies as well as testing of non-producing Subor heavy oil field.

Bitech Silur and Aminex projects were assigned as environmental category B, since they are based on the existing facilities and fields that might have impact on the environment. It should be pointed out that the IFC's environmental procedures imply the reliance of the bank on the project sponsors in a case of B-category project implementation. The participation of an independent party in the environmental impact assessment and monitoring over the implementation are required only for A-projects, but the great majority of the IFC' projects do not fall into this category. There are no provisions that would ensure similar objectives for the B-category projects. The IFC stipulates that monitoring will be conducted on the basis of periodical site visits and annual reports prepared by the operating companies.

Current conditions in the Russian oil sector will most probably lower the quality of the project implementation, especially with the insufficient supervision. Site visits of the bank's specialists are time limited and organized by the operating companies. In respect to companies' responsibility for reporting, it should be noted that the World Bank marks the tradition of „incomplete accountability for performance and results, deliberate misreporting of environmental data" in Russia. Thus, existing procedures on supervision and monitoring do not guarantee the accuracy of data on project progress as well as the implementation of international practices and standards by Russian partners. Such situation does not contribute to insurance of environmental sustainability that is supported by the bank.

Conclusion

It has been revealed that the Russian oil sector was burdened with a number of bad practices, which may hinder successful implementation of the World Bank environmental policies and procedures. These environmental procedures are of little use if the strong control and enforcement measures are missing. Being aware of the current problems in the country's oil industry, the bank still provides loans to Russian oil industry.

The majority of the oil projects proposed by the World Bank Group in Russia had that environmental rating. The complete bank's reliance on the capability and objectivity of local operating companies in conducting environmental studies and reporting on the project progress cannot be justified in Russian conditions. There is an obvious need to involve independent parties in the EIA process, which would ensure unbiased consideration of alternatives and recommendations on the changes in project design. To ensure successful performance in the oil sector, the bank should develop a system of external supervision and adopt stronger requirements for monitoring, auditing, and reporting on the project progress.

Furthermore, there is a lack of providing information about the project implementation and progress. This practice, most often explained as business confidentiality, does not allow monitoring and participation of affected parties, although it could improve environmental and social quality of operations.

The World Bank Group approach to the expansion and growth of oil industry, as a prerequisite for recovery of the Russian economy should be reassessed. The focus should be shifted from the extraction industries in order to ensure sustainable development.

4.

Kumtor - the Poisoned Gold

Description of the Project

The Kumtor gold mine is located in Kyrgyzstan, along the northwestern slope of the Ak Shirak mountain ridge in the interior of the Tien-Shan Mountain, 60 kilometers from the Chinese border. The gold deposit, among the ten biggest in the world, was discovered in 1978, during the Kyrgyz geophysical expedition. During the communist time, the extraction of the deposit was considered an economic failure because of its location.

In 1992, the Canadian Cameco's geologists came to assess the potential of the Kumtor deposit, which resulted, with the signing of an initial agreement between Cameco and the Republic of Kyrgyzstan. In 1994, final agreements and a feasibility study approved the exploration of the Kumtor deposit. Kyrgyz Republic owns two-thirds of the gold mine, while Cameco owns one-third. However, the mine's operator, Kumtor Operating Company, is fully owned by Cameco.

In 1995, the initial financial package was approved. The mine is financed by loans and guarantees from private and public financial institutions along with Cameco's own fund of USD 167 million. The construction of the mine was completed in 1996, and commercial production started in 1997. The mine employs approximately 1500 people and it is the largest western managed mining project in the former Soviet Union.

The Public Investments are the Following:

- the European Bank for Reconstruction and Development provided USD 40 million loan;
- the International Finance Corporation provided USD 40 million loan;

- the Multilateral Investment Guarantee Association provided USD 45 million for political risk insurance;
- the Overseas Private Investment Corporation provided USD 192 million for political risk insurance; and
- the Export Development Corporation provided USD 50 million loan.

Along with the backing of public institutions, there are two eight-year loan packages provided by six banks led by the Chase Manhattan. In 1998, the leadership of the joint venture acknowledged a cost overrun and announced that, in fact, it was about USD 176 million over the budget.

It should be mentioned that the European Bank for Reconstruction and Development provided USD 30.1 million to the Kyrgyz Republic for the electricity net improvements that supplied the mine site with electricity.

According to the contract, the Kumtor Operating Company has a ten-year exemption on a tax from profit. The Company can freely export abroad and if the National Bank of Kyrgyzstan wants to exercise its first option on buying the gold it has to pay the full rate at the London bullion market rate. Cameco controls the venture’s gold account and determines the conditions of sale. The gold produced at Kumtor is to be refined at the Kara-Balta plant southwest of Bishkek. However, Cameco's officials claim that the Kara-Balta plant does not have sufficient capacities, and that gold should be refined abroad.

Description of the Mine

As the mine is situated in the altitude of 4 400 meters in a sub-zero temperature zone, the machinery operates at 70 percent capacity because combustion engines lack the oxygen. In addition, employees are working in hard conditions since there is a lack of oxygen.

The weak point of the mine is the long supply line - everything should be delivered to the mine by trucks or by airplane. For example, delivery of 17 tonnes of steel grinding balls consumed every day by the plan’s sag mill and two ball mills takes three to four months. Train and truck through Russia and Kazakhstan deliver equipment for mining and processing to Kyrgyzstan. The road path passes the giant Issyl-Kul Lake and a steep serpentine road 60 kilometers long. To prevent shortages due to logistic difficulties, Kumtor Operating Company keeps more than USD 20 million budget for supplies and spare parts in inventory.

The open pit mine is partially in an area that was under a glacier shield before the construction. The waste is disposed on the top of the glacier since it is assumed that the temperature below the freezing point would fix the material on the spot.

The gold extraction process results in large quantities of cyanide and heavy metal containing sludge, which is stored in the tailing pond (the mine uses more than ten thousand tonnes of sodium cyanide yearly). The KOC started to discharge treated effluent from the pond in 1999 to the river Kumtor, which is tributary to river Naryn.

In the vicinity of the mine there are five glaciers. One of them, the Lysyi Glacier, covers the upper part of the mineral deposit. Research suggests that these glaciers have a negative mass balance because they are melting. This fact is supported with the data that proves the increased melting process of glaciers in the Tien Shan Mountain over the last 40 years.

Problems of the Mine

Until now, the existence of the mine was haunted by several accidents, different in scale. The first one was a helicopter crash in 1995, when 15 people died while they tried to return from the site. In June 1996, a fatal construction accident happened and one of the employees was killed. In August 1997, a large quantity of nitric acid was spilt at the site.

Probably the most controversial accident is the truck accident from May 20, 1998. Eight kilometers from Barskoon village, the truck, transporting sodium cyanide[1], crashed. As a result, 20 tonnes of load fell from the bridge into the river Barskoon. Sodium cyanide was packed in special packing from synthetic material, polypropylene film, which was put in a wooden container. The container and some of the packages were damaged, which caused a sodium cyanide contamination of the Barskoon River. The contamination spread to the Issyk Kul Lake, the main tourist attraction in Central Asia.

Five hours after the accident, the container was lifted from the river and delivered to Kumtor. Samples taken downstream the river showed that the largest toxic release occurred when the

[1]Cyanide is the chemical-of-choice for mining companies to extract gold from crushed ore. Very low-grade ore, with minimal residues of gold, is crushed and piled on the ground, then sprayed with a cyanide solution. No mine has ever avoided leaking cyanide-laced water and waste into the ecosystem.
At one U.S. mine, Summitville, taxpayers have already paid USD 100 million over a few years for the EPA to simply contain – not clean up – contamination of local rivers. Meanwhile, a spill of billions of gallons of cyanide-laced waste from the Omai mine in Guyana caused the death of thousands of fish and scores of other animals downstream. A spill from the Baia Mare pretreatment facility in Romania eradicated life from a river and killed hundreds of tons of fish.

containers were lifted from the water. One of the explanations is that the efforts to lift up the containers caused the tearing of the packages.

According to some information, the population of Barskoon did not know anything about the accident for two days and they continued to use water. “The Ministry of Environmental Protection was informed about the accident by the regional department and the next day a special commission examined the impact of the sodium cyanide spill.

“According to their statement, 1 762 kg of cyanide was flown into the river after the accident. Based on the calculation made by the Ministry of Ecology ... it was found out that 566 to 863 kg cyanide flew into the Issyk-Kul lake, and 189 to 155 kg sodium cyanide got on the fields and individual plots of Barskoon and Tamga villages respectively, processes of natural decomposition not taken into account. “ (Kyrgyz Ministry of Ecology)

> “According to Dr. Owen Mathre, a former research chemist for E.I.DuPont, the dissolution of approximately 1,800 kg (about 2 tons) of solid sodium cyanide under given conditions would probably require several hours to complete. Since the pre-spill pH of the river was likely less than 9.0, most of the dissolved cyanide would have formed HCN, a toxic gas that would have escaped into the air. Within a few hours of the accident, sodium hypochlorite was applied to areas near the spill site to break down the cyanide. Application of this chemical, however, would likely result in the formation of cyanide and cyanogen chloride—cyanide-related compounds that are toxic to aquatic organisms. Cyanogen chloride is a heavy gas that could have traveled significant distances from the spill, and has been known to cause throat and eye irritation in mine workers. Therefore this compound, together with the presence of gaseous ammonia, may have contributed to some of the medical complaints of the local citizens.

> Water samples collected about 20 meters from the spill site (presumably downstream) within hours of the accident contained up to 79.5 mg/L of free cyanide, which was the only cyanide form reported. However, since standard cyanide analytical techniques fail to detect several forms of cyanide and cyanide-related compounds, the concentrations reported would not include cyanide from many of the stronger metal-cyanide complexes, nor would they include the toxic cyanide breakdown products in cyanides, thiocyanates, cyanogen, and cyanogen chloride, or indications of ammonia or chlorine concentrations. All of these compounds could have formed following the spill, and all are toxic to aquatic organisms.” (Robert Moran, Ph.D.; Cyanide Uncertainties, 1998.)

Effects on the Environment

The impacts of the accident are still under debate. The KOC denies any lethal poisoning resulting from the accident, while the newspapers' report prove that there were such cases. Similarly, there is a dispute over the accident's impact on the local population. News from May 28, 1998 says that: “more than 1000 residents of the southern Issyk-Kul area have been medically treated and at least 93 of them have been kept in a hospital. Two people died, while eight were in a serious condition."

The International Commission that examined the case did not find any lethal case, while the report of the Russian Ministry of Defense identifies one.

The serious health impacts of the toxic spill were magnified by the extensive use of sodium hypoclorite solution in order to neutralize the toxic compound. According to the EBRD, the KOC used only ten litters of the solution at the site, while the Kyrgyz authorities used approximately 6-700 kilograms of the solution to decontaminate the canals of Barskoon village. Other sources gave different information about the extent of the solution used by the KOC. People in the village have suffered, and still are, from the neutralization effort.

The assessment of the accident was completed fairly late, on June 9, 1998. Approximately 4 800 people were temporary relocated. In early July, independent mine experts from the US Mineral Policy Center were invited by the Kyrgyz parliament to visit a mine site and perform another assessment. However, the KOC did not provide access to the site during their visit.

Although there are some available reports, the most prominent is the Canadian-led exercise of the International Scientific Commission on the impact of the accident. However, this report fails to deliver a detailed analysis of possible impact of the accident and does not address properly the health impact of sub-lethal exposure to cyanide and cyanide complexes. It also limits its focus to the impact of cyanide compound but does not assess its possible interaction with the neutralizing agents used after the spill in wide extent. Cluster analysis and statistical data collected by Kyrgyz scientists shows a higher rate of mortality and morbidity in Barskoon village after the spill. According to the National Hospital doctor, Jengish Jylkybayeva, four years before the accident only 40 people died, while in the one year after the accident the number of deaths was 22.

An independent laboratory was set up to monitor the health status of the population that might have been affected by the accident. However, detailed results are not available yet. Along with the harm to human health, other life forms, especially fish, which are 1 000 times more sensitive to cyanide exposure than human beings and other aquatic organisms in the river Barskoon and lake Issil-Kul, were affected as well.

Apart from direct harm, the accident had large economic effects. People from the region were unable to sell their fruits and vegetables as they were contaminated. The tourist industry around the Issil Kul Lake suffered from the accident tremendously since tourists cancelled their reservations for the whole season. A number of trains from Bishkek and flights from Moscow to Bishkek were cut. Clumsy efforts by the Cameco and the Kyrgyz government did not succeed to prove that the lake was safe.

It is apparent that the KOC and the Kyrgyz authorities did not respond on time. There was a significant delay in the notification of the spill, which affected the local population. If the Russian border guards did not appear on the site of the accident, the delay would probably have been even longer. The other problem arises from the efforts to neutralize the impact of the accident. It is hard to get independent information on who and how much sodium hypoclorite was used. One thing is clear - the extensive use of this compound created more harms than good. This overextended use was obviously the sign of panic and a lack of proper information.

Road Safety

Another problem, which is connected to the accident, is the state of the roads and the bridges that lead to the mine site. The orientation of the bridge where the accident happened is a critical issue, as the drivers have to take a very sharp turn to enter the bridge. According to Kyrgyz MP Kadyrbekov, the KOC has used an old road, which was constructed in the 1950s. According to the contract between the Kyrgyz

Government and the KOC, USD 55,565900 should be spent for the road reconstruction. The KOC cancelled the agreement on road reconstruction in January 1995. The Kyrgyz Ministry of Transport appealed to the KOC and the Government several times to repair the road and bridges. All these requests were rejected. Kadyrbekov also said that the bridges were built in the 1950s and their weight capacity was around 13 tonnes. The truck that caused the accident carried 20 tonnes of cyanide compounds. Three people were charged with the Criminal Code of Kyrgyzstan concerning the accident; the driver of the truck, Murat Murtazin, and two managers of the KOC. One of the managers, a Canadian citizen, escaped from the country before the procedure started. All the other drivers who were transporting chemicals on the day of accident were fired by the KOC. The driver was sentenced to several years of imprisonment but was amnestied immediately. After the accident, four bridges were reconstructed on the road to the mine.

Compensation to Affected Population

As the company caused extensive damage the issue of compensation was obviously one of the crucial. According to the Kyrgyz Minister of Ecology, Kulubek Bokonbaev, the direct damage of the environment was around USD nine million. The KOC, together with Kyrgyzaltyn, the Kyrgyz State Gold Company, spent about USD 470 000 for compensation to 7 200 residents of Barskoon village and USD 3 600 to the residents of the neighboring Tamga village. Approximately USD 580 000 was spent for the compensation of tourist activities and USD 530 000 was spent for the construction running water system in Barskoon. About USD 105 000 was spent on reconstruction of the road to the mine and USD 80 000 for tourist advertisements.

In an arbitrated agreement between the Kyrgyz government and the Cameco, the compensation of USD 4.6 million was set, which included USD three million for the residents of the Issyk-Kul region. However, there were some troubles surrounding the distribution of the money to the population. It is indicated by the news that a year after the accident, in May 1999, local residents blocked the road to the Kumtor mine. 55 trucks of Kumtor could not get to the mine during these days and two trucks were completely destroyed. The KOC estimated the damage to USD 500 000. Five militiamen and two picketers were hospitalized and 34 picketers were detained. After this, the local residents captured three leading officials from the regional administrations, whom they accused of embezzling the compensation. The hostages were released when all the detainees' people were let go. Later, a criminal case was opened against the head of regional administration because of the money embezzlement.

Lack of Response

A crucial failure is the fact that there was no proper Emergency Response Plan on the place. The KOC staff as well as Kyrgyz authorities acted in panic, resulting in the late notification of the population impacted and inappropriate measures to neutralize the toxic effect of the spill.

After the spill, a new Emergency Response Plan was developed by the KOC, but it was not released to citizens. The KOC argues that the public release of the plan would mean a security risk for the mine operations. Basically the mine says ‘trust us’ - which is difficult after the spill.

There were several accidents since the cyanide spill in the mine, which means that new accidents can occur anytime. The latest accident that is reported happened in January 20, 2000, when a truck with chemicals overturned on a bridge along the road between the Barskoon village and the mine site. About 1 500 kilograms of ammonium nitrate were spilled. Although it is not a toxic chemical, the substance causes eutrohisation in watercourses. Similar accidents are likely to happen again since a large quantity of various chemicals is transported to the mine.

The large number of accidents/incidents connected to the mine can be the result of two causes. One is the difficult access to the place and the long path route while the other is a bad housekeeping practice. It is known that the OPIC's field mission found a serious problem during their visit at the mine but they were not willing to disclose details about it.

The secretive behavior of the mine leads to the problem of transparency. The mine tends to be very secretive while after the cyanide spill such behavior just fuels suspicions that something should be wrong if they try to seal their operations to such high extent.

As Cameco's spokesperson said in 1999, the cyanide accident turned into a major public relations nightmare, which is mostly due to the company's wrong strategy in dealing with the public. According to a group of Kyrgyz NGOs, the KOC tries to buy its improved public relations profile instead of engaging in a genuine dialogue with stakeholders.

Public Participation

In 1999, the EBRD initiated the Monitoring Advisory Group (MAG), which was supposed to address the lack of credibility of the monitoring data collected by Kumtor and the Ministries of the Health and Environment and the break-down of effective communication among various stakeholders. The MAG was to be an independent forum, funded by the UK Department of International Cooperation to facilitate an informed and credible stakeholder dialogue involving the local community, Kumtor, NGOs and other interested parties. Later on, the MAG was widened and its name was changed into the Community and Business Forum (CBF). Its mission was declared as *"To develop effective cross-sectoral collaboration between business and communities, to further encourage sustainable social, economic and environmental benefits in Kyrgyzstan*."

The widening of the process would not be a problem if it would not cause the watering down of the original stakeholder dialogue on Kumtor-related issues to general 'collaboration'. Local NGOs raised serious concerns about the usefulness of the process in this form. It is perceived by them that the forum is used to divide the NGO community with the tools of small grants and monopolize further the information flow concerning Kumtor as the KOC and Cameco refers information inquiries to the CBF, which is not legally responsible body and lacks adequate information to respond such requests in substance. The Steering committee of the CBF consists of nine people, six of them officials. The process turned very formal with withdrawing the meaningful content of dialogue from it.

The shadow of corruption also touched the mine as one of its stakeholders, Kyrgyzaltyn, was impacted by corruption. On

December 16, 1999, the Kyrgyz Assembly discussed corruption in Kyrgyzaltyn. The newly appointed head of Kyrgyzaltyn, Kamchybek Kudaibergenov, said that the former president of Kyrgyzaltyn, Dastan Sarygulov, cheated the government by using changes in the world price of gold.

Another concern that has not been addressed until now is the impact of long-term climate change on the fate of the tailing pond. It is not clear what will happen with all its highly toxic content when the melting of glaciers will increase. In addition, significant climatic changes are suspected for the years 2040-2050. The Environmental Impact Assessment of the mine site deals only with general terms such as decommissioning and takes the sub-zero temperature as an important factor for the eternal storage of toxic materials. It does not assess the possible climatic fluctuations and the change of precipitation and water flow from melting. If material from the tailing disposal basin would enter the watercourse via the Kumtor River, it would poison the main water resources of Central Asia, which are already under stress.

The case of the Kumtor mine is an example of bad communication with the public and NGOs. Both the mining firm and the lenders missed the opportunity to re-establish trust after the serious accident with their shortsighted behavior. There is still a chance to prove the quote from the Mark Twain: *"What's the definition of a Gold Mine? A whole in the ground owned by a Liar."*

The case also points out the risks and dangers of gold mining, especially under such difficult conditions, present at Kumtor. 78 percent of the worldwide gold consumption is for jewelry. Is it worth to produce jewelry with a price of heavy pollution?

5.

Micro-credits in Bosnia and Herzegovina

Background

The World Bank is one of the initiators and supporters of micro-credit activities and their development in Bosnia and Herzegovina. There are nine micro-credit organizations in Bosnia and Herzegovina that provide loans to low-income citizens giving them an opportunity to start their own business.

Local Initiatives Departments (LIDs)

Local Initiatives Departments (LIDs) were established in 1996 in the Federation of BiH and in 1997 in Republika Srpska to administer the Local Initiatives Project. Legally, the LIDs are departments of governmental Employment and Training Foundations (ETFs) established to administer three employment-related programs financed by the World Bank and other donors. The ETF/LID management is responsible to a Board of Trustees and ultimately to their respective Entity Governments. The Federation and Republika Srpska LIDs work in close cooperation and share certain functions and staff. The LIDs act like an apex or second tier institution channeling financial and technical assistance to the Micro-credit Organizations (MCO's) at the retail level.

The LIDs have four main roles:

- to provide and monitor financing to the MCO's;
- to evaluate the development of the MCO and provide them with technical assistance needed to manage their resources soundly and become independent financially viable institutions;
- to improve the legal framework for the micro-finance sector in BiH; and

- to disseminate information on micro-finance best practice to all micro-lending institutions in BiH and participate in local and regional professional micro-finance associations.

Both LIDs in Bosnia and Herzegovina have developed substantial capacity to channel financing, monitor and evaluate the MCO's performance from an institutional, financial and social perspective. Performance, monitoring and financial analysis are conducted on a quarterly basis.

Financing is based upon the success of performance. To remain eligible for financing, MCO are expected to meet mutually agreed Performance Standards. These provide clear targets and incentives for the development of high-performing institutions that reach large numbers of clients. MCO that meet the Performance Standards will be provided with the capital base that will further their growth. The final goal is to make MCOs strong and financially viable institutions that will increase the outreach to low-income clients. The LIDs also disseminated information to the entire micro-finance sector in 1999 through monthly newsletters.

Projects Financing

The Local Initiatives Project has a total budget of USD 21.8 million financed by the Governments of Austria, Italy, Japan, the Netherlands, Norway, Switzerland, UNHCR, UNDP and the World Bank.[1]

According to fund allocation, the highest amount goes to Micro-credit Loan Funds (USD 1,482 863 million in Federation and USD 1,890 008 million in Republic of Srpska).

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[1] In 2000, the Government of the Netherlands is providing an additional USD 0.6 million in financing to the Local Initiatives Project.

Management Fees for MCOs were USD 1,032 501 million, Technical Assistance USD 370 695 and Operational Costs of LIDs USD 325 117.
The World Bank, in partnership with the stakeholders, plans to review the status of the current project in July 2000, and develop a medium-term strategic framework and financing strategy for the micro-finance sector.

Overall Results

According to data from December 1999, the following results have been achieved:

- 35 400 loans have been disbursed with a total amount of USD 57 million.
- 15 000 micro-entrepreneurs are currently active borrowers with total loans of more than USD 16 million.
- 50 percent of borrowers are women, mainly war widows.
- 21percent of loans have been disbursed to displaced persons and five percent to returning refugees.
- Repayment rates are extremely high, with less than one percent of outstanding loans in default more than 30 days.
- Approximately 24 420 jobs were created and/or sustained in 1999 with 43 500 suppoerted jobs since the project start-up in 1997.
- The average amount of the loan has decreased over the last two years from DM 4 500 (USD 2 500) in 1997 to DM 2 918 DM (USD 1 621) at the end of December 1999. The latter amount represents 140 percent of annual GNP per capita, which is currently estimated at DM 2 000. This indicates that the micro-credit organizations are targeting low-income micro-entrepreneurs for whom the project was intended.
- The majority of clients operate in the trade and services sectors as is typical for low-income entrepreneurs (22

percent of loans disbursed were for agriculture or small-scale production).

- Seven of eight MCOs contracted by the LIDs are operationally sustainable. It is expected that they will reach full financial sustainability in year 2000. The institutional capacity of the MCOs has improved significantly during the course of the year.
- The government of the Federation of BiH has adapted the draft of the Law on Micro-credit Organizations which is now in the parliamentary approval procedure. The Ministry of Finance is still considering the Republika Srpska's proposal.

MCOs as Implementing Partners of the LID’s

There were 17 MCOs during 1998, but only eight of them renewed their contract with LID. Those institutions that did not renew the contract continued the work through partnerships with micro-credit organisations that have access to LID financing. This created a welcome consolidation in the micro-finance sector where over 30 NGOs were running micro-credit programs in 1998, many of them with limited potential for sustainability. LOK, Sarajevo has formed a partnership with NBRM Modrica, Plavi Most, Bihac, and Business Center Travnik; Sunrise, Sarajevo with Lori Orasje, and World Vision with Vrelo, Mostar.

During 1999, the Local Initiatives Project has been implemented through various organisations. Targeted clients in the Federaton were:

- small entrepreneurs and small enterprises, primarily displaced persons and returnees, families of soldiers who were killed in the war and demobilized soldiers;
- unemployed women with a monthly income per household member of less than DM 100;

- legal and physical persons with low income who do not have access to traditional loan sources;
- refugees, returnees in suburban areas, demobilized soldiers and those who are engaged in the manufacture of domestic products; and
- physical persons whose monthly income does not exceed DM 300 per a household member, legal persons whose capital amount does not exceed DM 30 000 or those who do not employ more than five full time employees.

In Republika Srpska:

- low income entrepreneurs, especially demobilized soldiers, returnees, war widows, and women;
- economically active low income population who have an opportunity to generate profit;
- existing micro, small and medium enterprises, shops and farms in the sectors of agriculture, production and services; and
- low income private entrepreneurs (priority - displaced persons, returnees, and minorities).

The year 1999, was a year of expansion for all institutions. The micro-credit organisations experienced an average annual growth of 130 percent in the number of clients and in loan portfolio. The institutions also expanded their operations geographically. Together, LID partner institutions have 44 branch or satellite offices that lend in 81 out of 87 municipalities in the Federation of BiH and 28 out of 64 municipalities in the Republika Srpska.

Client Survey

In 1999, the LIDs contracted out an independent Client Survey. The Economic Faculty of the University of Sarajevo, working in collaboration with the University of Banja Luka, won the bid for this survey.

The objective of the survey was to investigate:

- the characteristics of a typical client;
- the impact of micro-credit on household income, business growth and employment; and
- clients satisfaction.

Profile of the Clients

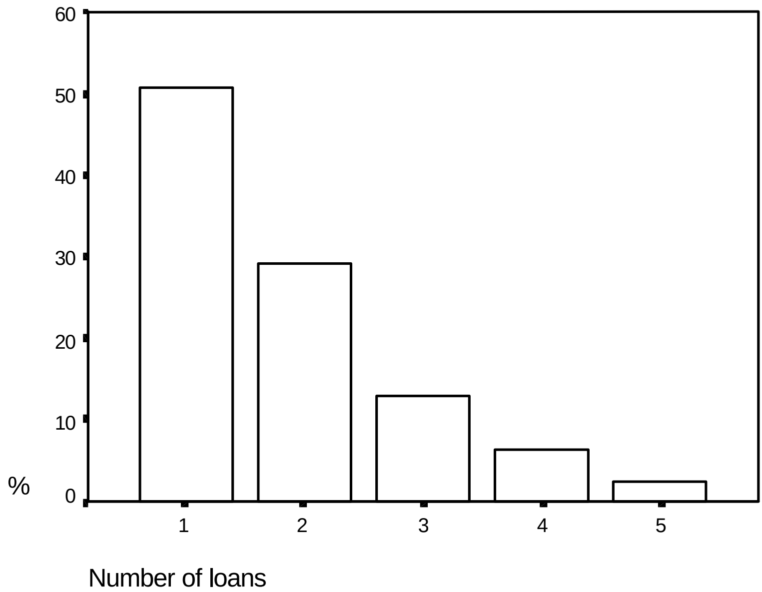
Most active clients work in the trade sector, which, together with services represents about 80 percent of loans. The majority of these business activities (57 percent) are unregistered. Registered activities are mostly individual (80 percent). Only 12 percent of clients represent start-up[2] activities. Among those that are not start-ups, about 48 percent have previously been employed, 21 percent have been unemployed, and ten percent have run another business. Previously employed clients have an average of 15 years of working experience.

Repayment of the loans appears to be quite regular, and over 97 percent of loans are repaid on time. However, approximately 47 percent of borrowers spend their own money to supplement the business. The average loan is about KM 3 361, with a range of between KM 200 to KM 25 000. The average number of loans per respondents is two, and average amount of money received is KM 5 600.

As a recommendation, more care should be given to younger clients and start-up activities, as well as more inroads in rural areas, production and agriculture as business activities.

[2] Start-up clients are those for whom this is the first business in their lives; they have not been employed or involved in any business before.

Figure 1: No of approved loans per client



Clients Profile Reviewed by MOCs

Three micro-credit agencies are mostly focused on clients from urban areas (LOK and Sunrise from Sarajevo and Mikrofin from Banja Luka). Benefit, Lukavica, Bospo and MC SEA from Tuzla are maintaining a balance between clients from towns and villages, while the other two agencies are on the level of sample average (72.2 percent of total clients are from urban area). Clients are predominantly domicile residents in six agencies. Only the Benefit has slightly more displaced persons than domiciles among clients.

Only the MC SEA has a relatively high percentage (about 17) of returnee clients. While the BOSPO is conceptually focused on female clients, other agencies keep the balance between males and females. The Sinergija is the only agency mainly male oriented (77.9 percent male clients).

There are no significant differences between the micro-credit agencies in the ages their clients. Approximately two out of three clients are between 31 and 50. The AMK is the only agency which is slightly more focused on clients younger than 30. The dominant education of the clients is secondary school in all agencies.

Sectoral Structure

Clients use loans for different types of businesses grouped in five categories-services, production, trade, agriculture and other. The biggest percentage of clients are working in trade sector in all MCOs (approximately 45 percent), then service sector (average 41 percent), production (11 percent), agriculture and other sectors.

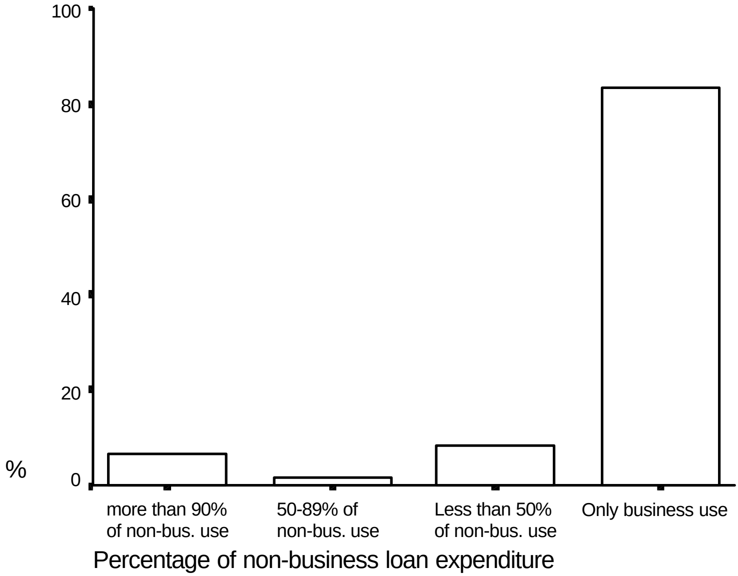
In all agencies, except the BOSPO (with more than 80 percent registered businesses), the number of unregistered businesses is approximately two times bigger than the number of registered ones. The dominant type of registered business is a single private enterprise, which on average employs between one and three persons. In all agencies, 70 percent and more borrowers are only engaged in their own businesses.

The number of approved loans to one client varies from agency to agency. Mikrofin is the agency that offers more credits to the same person than other agencies: 30 percent of Microfin's clients received only one credit and 45 percent received more than four credits. In the BOSPO and the AMK only a small number of clients received three credits (five percent). The total amount of money per client is also variable – from the BOSPO with the lowest average amount (KM 2 142) to Sinergija with the highest average amount (KM 10 625).

Effects on Clients

Only about 17 percent of respondents used a portion of the loan for non-business expenditures, 83 percent of clients used the complete loan for business purposes. Among those that are using a loan for non-business purposes, only about 8.5 percent are spending more than 50 percent of the loan for such purposes (mainly for buying food, clothes, and rebuilding homes).

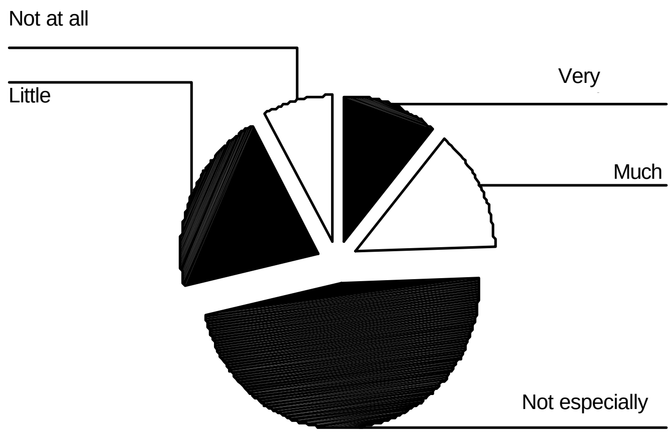
Figure 2: Business vs. non-business loan use



About 40 percent of clients said that the micro-credit had induced a new business. In terms of loan effects, 68 percent of respondents confirmed that the loan contributed to the increase in their business activities, but only 27 percent claimed that the loan also increased employment in their current business.

Household income was particularly affected by the loan. However, that did not positively affect purchasing power, social position, household health care and social security.

Figure 3: The change in clients life



Effects on Micro-credit Agencies

More than 50 percent of the loans are used for business purposes or as working capital. The greatest effects are on the increase of business (78 percent businesses are increasing) and on start- up businesses (43 percent of existing businesses initiate new ones). The lowest effect is on employment, only 29 percent.

It is obvious that loans significantly improved the economic position of clients in all agencies, judged through increased household income. Economic position of clients is low. More than 70 percent of clients in all agencies have less than KM 1

000 as household monthly income. MS/SEA has the biggest impact on household income (85 percent of clients have bigger household income now then before taking loans), and the lowest was AMK (only 40 percent).

Effects on the Quality of Service

Conditions of loans such as the repayment, collateral terms and interest charges were acceptable for most clients. Clients are also satisfied with the application procedure such as preparation of necessary documentation and performance of micro-credit organizations.

The agencies differ in the amount of time they need to release the loan and the money they need during the procedure. On average, clients have to wait 12 days (Mikrofin and Sinergija) to 29 days (BOSPO) to get the loan. The total amount of money spent on documentation varies from KM 2.30 (BOSPO) to KM 122 (Benefit). After the first contacts with the agency, clients needed 18 days (Sinergija) to 36 days (BOSPO) to get the loan. The time period between submitting the application form to receiving credit approval varies from ten days (Benefit) to 27 days (LOK). The number of days from approval to disbursement is rather low in each agency – from two to five days.

Treatment of clients in terms of availability for contact, kindness, providing the information, and care for clients, was evaluated as good or very good in all agencies.

Looking at the profile of micro-credit agencies from the type of service, it is obvious that all of them offer only financial support. About 90 percent of clients in each micro-credit agency received only financial support. And other type of services for certain number of clients was predominantly business advice.

Conclusion

The micro-finance sector in BiH has been developing remarkably quickly, particularly if we consider the post-war context. Today, BiH has one of the most vibrant micro-finance sectors in all of Central and Eastern Europe countries. Yet, the micro-finance institutions are still very young and reaching only a small percentage of potential clients. Many micro-entrepreneurs do not have access to capital that would help them increase their business and overall quality of life.

The main findings of the survey are the following:

- On average, clients are 40 years old and married (83 percent of total), living in urban areas (73 percent) with an average monthly household income between DM 500-900 (USD 275- 500).
- Clients mostly operate their businesses in trade and services with one to three employees.
- More than half of the businesses (57 percent) is unregistered. The main reasons are high business registration fees and taxes in BiH.
- 79 percent of clients state that the loan has significantly improved their economic situation.
- Impact is primarily on increased business production rather than increased employment.
- After the loan disbursement, the average monthly salary has grown from DM 351 to DM 444 (26 percent).
- 94 percent of clients are satisfied with the quality of service, especially with the speed and simplicity of loan application procedures.

- 75 percent of respondents believe that loan terms and conditions are well tailored to their business needs.
- Only 13 percent of respondents stated that they need business support services. These needs include business consulting (30 percent), market information (31 percent), and accounting (15 percent).

The survey highlights that outreach to rural areas is still relatively limited (27 percent of clients), as is the outreach to younger clients and start-up businesses. Returnees are also not well represented among the clientele. Therefore, activities for targeted outreach and product development are planned.

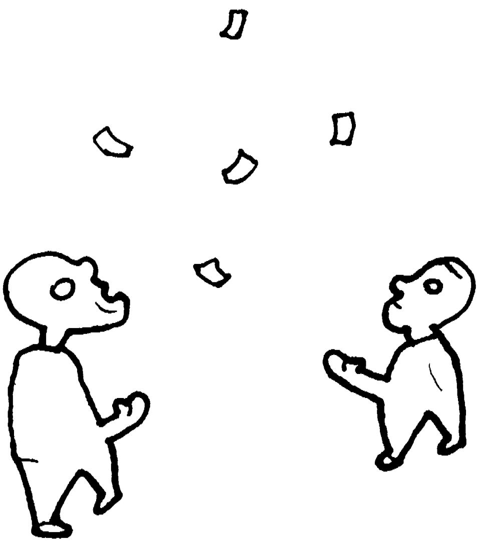
Future Perspectives

Micro-finance in BiH is now entering a second phase. With a solid institutional base and increased competition among credit providers, focus will be on managing growth in a sound and sustainable manner and on responding to client needs. Three main trends are characterizing this phase:

- Continued **consolidation and cost reduction** among the micro-credit organizations as they form strategic partnerships to increase their breadth and depth of operations and maintain their comparative advantage in the marketplace.
- **Product diversification** as micro-credit organizations start to experiment with new products and reach out to broader clientele, such as those involved in more productive and agricultural-based businesses.
- **Increasing integration with the formal financial sector** as micro-credit organizations increasingly reduce dependency on donor support and turn to commercial banks for financing and possibly explore partnerships as regards service delivery.

In 2000, the LIP has three main goals:

- Capitalization of the best performing micro-credit organizations so as to support continued growth and outreach to low-income clients.
- Adoption of laws to regulate the micro-credit organizations, and progress in developing legal amendments and policies to regulate other institutional forms.
- Development of a strategy for the long-term development of the entire micro-finance sector in partnership with all key stakeholders.



6.

"Shall not be built" -The Sofia Hilton and IFC

Introduction

Initially, this project involved the construction of 17-floors of top quality business hotel in the middle of the South Park of the capital of Bulgaria. The managing company of the hotel is Hilton International. The sponsors of the project include Sofia Municipality (SM), Glavbolgarstroy Ltd., Hilton International, FEAL International S.A (a subsidiary company of Compagnie Generale des Eaux (now Vivendi), France). At a later stage, the International Finance Corporation (IFC) of the World Bank Group was invited to financially support the project, becoming one of the project sponsors. The full cost of the project is USD 46.7 million in which IFC is involved with USD 22,3 million of which: mortgage loan – USD 10,80 million, quasi-equity – USD two million, and syndicated loan – USD 9,5 million.

Violation of Law

The main problem with the Hilton Hotel Sofia Project is that the IFC finances a construction, which will destroy and damage a part of one of Sofia's major parks – the South Park. The project was prepared in violation of the Bulgarian environmental legislation (including EIA legislation and right-to-know principle) and was in contradiction with the environmental policy of the World Bank. It is a destructive step towards filling the second part of the South Park with buildings, thus decreasing significally the city's green territories. The construction also affects the fresh airflow from Vitosha Mountain towards the city center. This will indirectly have a negative impact on the local residential and work environment. Another concern is that the high rise building presents a visual intrusion into the picturesque landscape of Vitosha Mountain from the city of Sofia.

Since Sofia Municipality and IFC (both of them public institutions) have never provided full documentation to interested NGOs, the following description is only based on fragmented information. A court case (No 238/98 in Regional Administrative Court) was started against Sofia municipality on their failure to provide information. There is no final verdict yet.

The history of the park and the hotel goes back for decades. The oldest document dates from 1973. It shows that, for a number of reasons, the green territories of Sofia and those of the South Park in particular, had been subject to protection.

> "Point 6: The foreseen hotel "Lux" (luxury category) shall not be built on the territory of [South] park."

This is a quotation from Order 63/31.03.1973 of the Bureau of the Council of Ministers of Bulgaria, which approved a preliminary project with a draft-statement of account of the "South Park". The Council of Ministers rejects the construction of a number of proposed buildings in the park's territory with the same Order. The Sofia municipality was obliged to research and project an extension of the park to the south, (as far as the ringroad of the city) and establish links with the Vitosha Mountain.

In the mid-1993, the Union of Architects opened a bidding procedure for "Preparing a new idea for spatial and functional organisation of the territory of the South Park, part II." From a letter of the Chief-Architect of Sofia, it was clear that one of the main driving forces for the "new idea" was a "displayed interest from investors". Public interests were not considered at this stage.

On 28/29 July 1993, the Sofia Municipality Council passed a Decision to build a five-star hotel complex in co-operation with a foreign investor.

In 1995, the Municipality decided to change the purpose of the park territory without any public consultation. Changes in town planning are regulated by the Law on Territorial and Urban Planning and regulations for its application. According to these regulations, the municipality has to announce changes, and citizens have the right to appeal. To avoid public consultation, the Municipality used a regulation that applies only to low rise building (one to three floors) construction, which does not require public consultation. According to the Environmental Protection Law, the investor is obliged to carry out an Environmental Impact Assessment (EIA) in a case of town plan alteration. In this case, the investor simply ignored and violated Bulgarian legislation.

Despite the law violation, the Ministry of the Environment and Waters and the Ministry of the Territorial Development and Urbanization supported the project, thus ignoring legal responsibilities. The Environmental Protection Law was interpreted according to Municipality wishes, which resulted in ignoring the EIA procedure. The Municipality did this, in spite of the fact that only courts can rightfully interpret disputed legal texts.

Furthermore, the financial assessment of the land area is not sufficient. The Municipality's proposal for the land price was USD six million, which was only a half of the price, of an evaluation given by a consulting company. In 1997, the price of the land was reduced to USD 4,390 million, despite the fact that during this time property prices in the area were rising.

According to the EBRD, the Bank rejected participation in the project in 1996, because it was estimated that a new luxury hotel in Sofia would not be cost effective. Bad financial results would jeopardize the owning consortiums ability to pay back the loan.

The first attempt to involve the International Financial Institutions in the Hilton construction was made in the early 90s (1993-1994) by the Sofia municipality. At that time, Sofia's major, who played a leading role in the project, announced his attempt to involve the EBRD in the project. The motivation for building a new five-star hotel was the EBRD's Annual Meeting in 1997.

Since the EBRD refused involvement in the project, the IFC became a new potential source of financing. Unfortunately, NGOs were provided only with the two IFC's documents; Environmental Review Summary, which was released on September 20, 1996, and the press release from December 11, 1997.

The IFC's decision to support the project was criticized on the following basis:

- the lack of EIA procedure and public participation in the project preparation; and
- ignorance of Bulgarian legislation.

Since 1996, the Municipality has been refusing to provide information about the project both to NGOs and citizens, thus violating one of the basic rights that are guaranteed by the Bulgarian Constitution. The only piece of information was provided to a Dutch NGO, the BothEnds after the Dutch Executive Director of the World Bank group, Mr. P. Stek, had asked for it. Some of the documents had been requested directly from the Sofia Municipality, but they were never provided to Bulgarian NGOs. Nevertheless, some parts of the World Bank information mislead both the NGOs and the Bank itself, since the legislative procedures and obligations of the Sofia Municipality were not clearly identified. For example, the Municipality misinterpreted the legislation about the EIA procedures. This illustrates different standards of application by the Bank and recipient country.

The Campaign for Change

Local citizens, together with national and international NGO's, started a campaign against this project in the following manner:

- A number of letters and declarations have been sent to the Mayor of Sofia, to the Speaker of the Municipality Council (who is in the same time the Chairman of the joint-venture company which runs the project), to the Minister of the Environment and Waters, and to the Director of the Regional Inspectorate on Environment. The requested information covered all aspects of the problem: (i) EIA procedure; (ii) procedure on the town plan change; (iii) information about the project costs, loan from the IFC, selection of the partners, assessment of the land price; and (iv) public participation. The answers were formal, sometimes deceptive, or there were simply no answers.
- A Copy of the letter, which requested information from the Speaker of the Municipality Council, was also sent to the IFC representative in Sofia.
- Two protest actions were undertaken on the spot – one of them with the international support and participation.

- More than 2000 signatures against the project were collected within a week.
- Many press conferences were organized.
- After the CEE Bankwatch Network lobbying in Washington, the IFC agreed to meeting with Bulgarian NGOs. Five NGO representatives met with Mr. Jyrki Koskelo, but the meeting was informal. It was another example of neglecting the NGOs' and citizen's opinion about the project.
- One letter was sent to James Wolfensohn on July 2, 1998, with the NGOs' demands.

NGOs demands were:

- to stop the construction of the Hilton hotel in the South Park and to find a new, more suitable place for the same purpose.
- to conduct a referendum for moratorium of the construction in the green areas of Sofia.

In 1998, "Za Zemiata" (For the Earth) started a court-case against Sofia municipality, because it ignored the right-to-know principle. This court-case has not finished yet. According to the Bulgarian legislation, the construction cannot start as long there is a court-case going on, but the hotel is almost finished.

Alternatives proposed by NGOs

NGOs suggested two alternatives:

- to build the hotel near the National Palace of Culture (NPC), which is 100 –150 meters away from the present “Hilton” area. With this location, a direct connection between the hotel and the existing NPC infrastructure would be established.

- to build the hotel 250-300 meters away to the south from the present place.

In both cases, the main part of the park would stay untouched. The main sponsors –Sofia Municipality, the IFC and Company for Luxury Hotels, neglected proposed alternatives without any explanation.

Results

In 1998, after persistant protests and pressures that were put on the Sofia Municipality, it decided the following:

- to decrease a number of floors from 17 to eight (from 60 to 40 meters height);
- to decrease the area of adjoining territory by half to (2,5 acres); and
- to find another, similar area for park (about 2 acres).

Although the court case has not finished yet, the construction of the hotel started in 1999. Since then, public opinion has begun to swing against the project. Architects, landscape experts, and many others, raised their voice against the construction project.

At present, the luxury Hilton hotel, which is situated in the park, is almost completed. The construction affected the fresh airflow from the mountain and reduced the space for recreation. Even though the final decision was that hotel should have eight floors, there are 13 of them with three underground. Although promised, the Municipality did not find another equivalent area for a new park. The place that was supposed to be a park was completely destroyed and a new boulevard is to be constructed there.

This case demonstrates bad project preparation and the IFC's arrogance towards public opinion and NGOs. The IFCs do not consider the possibility that local authorities can take a biased, undemocratic approach towards certain 'pet projects'. As this case study has shown, local authorities can ignore the voice of the people they are supposed to serve. They can even ignore the law.

7.

Highway through Forests?

CAS and Transport Sector

Estonia became a member of the World Bank Group in June 1992. The first, and the only Country Assistance Strategy (CAS) for Estonia dates to September 21, 1994. The Bank's attitude and priorities were shown by suggestions to develop a foreign trade-driven infrastructure. The Bank declared that ”it will assist the Estonian government to meet the demand for the substantial public investment that will be required...to reorient transport and other infrastructure to meet the demands of the production for and trade with the West as well as the East. The Bank’s antipathy against subsidies is expressed also in the CAS: “Increased subsidies for public transport...would jeopardize the proposed transport sector project.”

Previous Transport Loans

The first World Bank's public sector loan was a rehabilitation loan of USD 28 million approved in October 1992. A part of the rehabilitation loan (approximately USD three million) was used for buying spare parts for public transport vehicles and overhauling diesel locomotives. The loan was co-financed by Japanese Export-Import Bank (JexIm) with USD 7.5 million.

So far, only one transport loan has been completed in Estonia- the highway maintenance loan of USD 12 million that was approved by the Board in May 12, 1994. The main objective of the loan was to finance routine maintenance of the roads in 1995 and 1996. A total, 3000 km of surface dressings and 200 km of surface overlays were completed, and three asphalt mixing plants were rehabilitated. The project also included a sub-section for training officials and staff who were working in private companies or as technical assistance. The Finnish Government granted an additional grant of USD two million came from Western donors, out of which 1.1 million. The project was completed in 1996 and ranked as a “highly satisfactory” in the World Bank's Implementation Completion Report.

Background - Tallinn-Tartu Highway Project

Tallinn and Tartu are the two largest Estonian cities with a distance of approximately 180 kilometers. Because of the trade between the cities, well-functioning transport infrastructure is important. The Tallinn-Tartu road is the busiest one in Estonia with average daily traffic of more than 6000 vehicles per day. In sections close to Tallinn traffic volume is up to 15000 vpd.

In the early 1980s, the Government started to upgrade the Tallinn-Tartu road, planing to expand it from two lanes to four lanes. In road sections the end of the 1980s-upgraded closer to Tallinn less than 20 kilometers of road. During the period between the fall of communism and the first years of the 1990s there was no money to continue the project.

In the late 1990s construction went slowly ahead and ten kilometers of two-lane road were built. In 1997 it was decided to speed up the project and finish the remaining construction of 150 kilometers on the Tallinn-Tartu road. The aim was to build a so-called First-class Road with two lanes in both directions. A specific Tallinn-Tartu highway lobby group was formed with strong support from the Estonian National Road Administration (ENRA). By mid-1998, a number of studies such as preliminary environmental impact assessment were conducted, but with insufficient public involvement. In February 1999 the Government decided to upgrade half of the 180-kilometre road (starting from Tallinn) from two- to four lanes and on the second half of the road (from Mäo to Tartu) to cover it with a new surface. In addition, a new bridge and bypass would be built.

Proposed World Bank Loan

The World Bank was mentioned as a possible founder of the project in December 1997, when the second Estonian transport project firstly appeared in the World Bank's Monthly Operational Summary (MOS). According to the Estonian transport ministry officials, it was not their proposal and there was no reason to list the project in MOS. However, the intensive project preparations started in 1998. The first Public Information Document (PID) about the project was released in December 1998. Since then, three steps were undertaken to proceed with the project. Firstly, the project Task Manager was replaced by the Bank in early 1999 (Cesar Queiroz replaced Anders Bonde). Secondly, Banks' Board approved the projected on March 16, 2000. Finally, preliminary negotiations about another transport loan from the World Bank began and are still going on. The new project that should start in 2003 would complete the remaining parts of the highway between Tallinn and Tartu with major realignment and environmental impact assessments (EIAs) as well.

Project Description

According to the World Bank the overall objective of the project is to improve the availability and reduce the cost of trade supporting services in order to increase the level of trading activities and the transit of goods through Estonia. According to the PID of the World Bank, the project includes the following components:

- Rehabilitation and Upgrading of Portions of the Tallinn-Tartu-Luhamaa Road. This component will include the rehabilitation of priority sections of the road and the widening of the Tartu Ring Road and construction of an Interchange.
- Improvement in Road Safety. This component would include, among other sub-components, the construction of civil works to eliminate accident black spots, installation of long life road markings for new asphalt pavements, road side delineators, changeable traffic signs, automatic speed control cameras, and the creation of campaign materials for a road safety educational campaign.
- Institutional Strengthening, Training, Office and Laboratory Equipment. This component will provide continued assistance to the Estonian National Road Administration (ENRA) for strengthening its operational capacity, including assistance for continuing the work on routine maintenance by contract, improvement of the Pavement Management System, assistance in improving financial management, and additional support for the ENRA personnel in road design and supervision for improvements in the main road network.
- Trade Facilitation. This component will include carrying out part of the action plan prepared during project preparation, including the specific actions aimed at developing an environment with:
    - laws and regulations to ensure the development of trade supporting services and infrastructure on an equal and fair basis, taking into account the EU accession process;
    - support for creation of an efficient public and private partnership based on combined resources, close and objective, and the perception of a common goal;
    - access to capital for the Estonian economy on equal terms and conditions as competitors;

- provision of quality education, training, and research on trade supporting services; and
- easy Estonian accesses to global markets and foreign access to the Estonian market. It will also include the hardware and software required implementing a pilot electronic system for providing one-stop border clearances in Estonia by the year 2003.

The total cost of the project is USD 49.5 million, including 22.65 million from the Estonian Government, 25 million as the World Bank's loan, 1.65 million from the EU, and 0.2 million from the Finnish government.

NGOs Arguments Against the Project

The World Bank second transport loan to Estonia has several sub-projects. The largest and the most controversial part of the project is the Tallinn-Tartu highway upgrade.

First of all, the project will cause environmental damage. The proposed wide highway (the total width of trace will be up to 400 meters) will virtually cut Estonia into two parts. It will cross the most valuable forested areas in Estonia that are key corridors for animal and bird migration. These forests will likely become a part of the EU network of valuable natural areas (Natura 2000). The new highway will be too wide for some species to cross, and therefore it will limit their ability to migrate. In addition, the project could endanger their ability to survive in these areas. The new highway is located right next to an important freshwater reservoir that is an important water source for the capital city of Tallinn which has 450 000 inhabitants.

Secondly, the project is not cost effective. The Government is arguing that this project is a major investment decision in a field of regional development at the end of 20th century. It would enable easier access to Tallinn from the southern and southeastern parts of Estonia creating also new jobs. However, regional development and cohesion between the Southern Estonia and the capital could be accomplished with other means and with less money.

Thirdly, there are alternatives. The current project is an example of trying to solve problems by dealing with results instead of causes. Estonian authorities argue that the current road is too narrow for increasing traffic while the proposed new infrastructure would, in itself generate more traffic. Government should seriously try to decrease people's need for mobility between Tallinn and Tartu. A need to travel from Tartu to the capital could be decreased with better telecommunications such as Internet, which enables video-conferencing instead of face-to-face meetings. It would be much cheaper to maintain the current Tallinn-Tartu two-lane road and to improve road safety. There is also a parallel road that is not used because of its bad condition, but it would be cheaper to improve the parallel road than to build a highway. According to the Estonian NGOs, no possible alternatives have been considered.

Fourthly, the Tallinn-Tartu highway is not a priority transport project in Estonia. A very good railway system is collapsing because of the lack of investments. For example, the Government recently decided to cut subsidies for passenger rail services by 50 percent in 2001. Rail is losing passengers because there is no money to keep the service quality. Rail tracks are in bad shape and trains are, therefore, rather slow. Thus it takes about 3.5 hours to get from Tallinn to Tartu by train while it takes 2.5 hours by bus. Public transport in cities is facing the same problems as rail sector- the lack of money and quality of service. There are very few bicycle paths in cities although people bicycle use is increasing. In Estonian cities, bicycles could be a very good substitute for private cars.

Finally, the argument contra the proposed project is a very poor public consultation. There has been a little meaningful consultation with the wider public throughout the project development process. The Bank correctly states in the Project Appraisal Document (dated February 23, 2000) that “massive collaboration” in project preparation was done between private and public stakeholders lead by the Ministry of Transport and Communications, namely with: “the Ministry of Finance, the Ministry of Foreign Affairs, the Ministry of Economy, the Ministry of Environment, the freight forwarders association, the Chamber of Commerce, transport companies, the Customs Administrations, and manufacturing companies.” Business associations related to the beneficiaries, including agricultural associations and other industry-related groups, are also named as key stakeholders. No surprise that NGOs had no opportunity to give theirs opinion about the project, since they were not mentioned as a part of the consultation process.

The Ministry of Transport and Communications and the Bank said that there have been enough articles about the Tallinn-Tartu highway project in the newspapers so the public should be well informed. It has happened only once that the ministry called a meeting with a few NGOs in the late stage of project preparation to “introduce the project”, obviously hoping to avoid future complains. In the Project Launch Workshop (April 28, 2000) a representative of the Ministry of Transport and Communications proudly announced that Friends of the Earth Estonia (FoE) was a part of the environmental working group of the highway project. FoE-Estonia has never heard of such working group and it had never received documents about the environmental aspects of the project.

While the Government of Estonia was still considering seven alternative routes for a new highway environmental impact assessments were carried out in mid-1979 for all possible routes. As it was stated in the study, the aim was just to give suggestions for further and more detailed environmental studies. However, the Government decided on a route that was actually a combination of several alternatives. It is almost impossible to use different EIAs that were done for several alternatives. Another EIA was done, but not surprisingly, the NGOs became aware of it only when it was completed and uploaded to the website of the institute that did the study (www.geo.ut.ee/maantee). There is indeed no link to the study from the website of the Ministry of Transport and Communications (www.tsm.ee/tsm) or Estonian National Road Agency (www.mnt.ee).

What Could the Future Bring?

It is too late to stop the project at its current stage, but the NGOs will put a pressure on both the government and the WB to minimise the environmental risks of the highway construction. At the same time, it seems that the next Tallinn-Tartu highway loan is under preparation, which could cause even greater damage to the environment.

To conclude, the Estonian transport loan has shown that the WB and the Government were not willing to include the NGOs in the project preparation process. The damage of the existing route improvements on the environment will be severe, but the new loan, which would approve major realignment through natural areas, would cause even greater damage. The Estonian NGOs will take a leading role in the consultation process of the upcoming World Bank project. The Friends of the Earth-Estonia are against further construction of the Tallinn-Tartu highway and will strongly oppose planned realignments. The aim is to stop the project.

8.

Drilling the Sea

Introduction

Chirag Early Oil Project was the first large-scaled Oil project of international financial institutions in the Caspian region. The project gives stimuli to the IFC and EBRD to be involved in ongoing process of the great Caspian game. Oil exploration in the Caspian Sea is accelerating rapidly. The Caspian region is becoming more important than the Persian Gulf.

On November 20, 1994, a consortium of oil companies signed a contract with Azerbaijan. The consortium, led by British Petroleum will invest USD eight billion in oil production during the 30-year period. The consortium consists of the following companies; Amoco Corp (17. percent), Exxon Corp (8.0 percent), McDermott International Inc, Penzoil Co (4,9 percent), Unocal Corp (10.0percent), British Companies; British Petroleum PLC (17 percent), Ramco (2.1 percent), Norway’s Statoil (8,6 percent), Itochu (3,9 percent), Turkish Petroleum (6.8 percent), Saudi Arabia’s DNKL Oil, Lukoil (ten percent), and State Oil Company of Azerbaijan (ten percent). G-7 equipment and service suppliers include; East-West Helicopters, Azerbaijan-Canada joint venture, mcDock, McShelf, Azeri-US joint ventures for supply bases, and Itochu, which has conducted seismic surveys of the shelf. In addition, Azerbaijan agreed that American Company Conoco will rehabilitate wells and develop the Guneshli field. This venture is 64.6 percent controlled by G-7 corporations.

The consortium will develop the Azeri, Chirag and Guneshli field in the Caspian Sea at a cost of USD 7.4 billion. The Consortium believes that it can extract up to four billion barrels of oil from the three wells in the Caspian Sea; Chirag, Azeri, and Gunsehli.

Early Oil Project involves commercial development of early oil from a part of the Chirag offshore oil field in the Caspian Sea. Export of oil from Sangachal will be via Northern Route Export Pipeline to Novorosisk and Western Route Export Pipeline to a new storage terminal at Supsa at the Black Sea.

Total project cost : USD 1.856 million.
Project starting year: 1996
Consession years: 25
First Oil pumping in new Pipeline: January, 1999
First Oil loaded in tankers: April, 1999

Development Banks' Involvement

The European Bank for Reconstruction and Development (EBRD) and International Financial Corporation (IFC) approved a project on February 19, 1999. The credit was to finance five of 11 shareholders of the AIOC and GPC. The EBRD's financing includes an A-loan of USD 100 million (ECU 90 million) for the account of the Bank and a B-loan of USD 100 million (ECU 90 million) for the account of participating banks.

The IFC funds five A-loans up to USD 100 million and five B-loans up to USD 100 million. The IFC's role in the project is to:

- provide long term financing, which is not currently available in Azerbaijan and Georgia;
- mobilize financing from international commercial banks; and mitigate cross-border and other political risks.

"Long-term financing, provided by the EBRD and IFC has not been previously available to the region", as the Deputy director of the EBRD's Natural Resources team Kevin Bortz said, "and the commitment of the EBRD and IFC will send a positive signal about project financing in the region".

Despite the commitments of the IFIs that the highest international standards will be used, the AIOC used the Best Available Technology Not Entailing Excessive Costs, which is far away from the Best Available Technology, commonly used in developed countries.

Project Description

The project involves commercial development of Early Oil from a part of Chirag offshore oil field in the Caspian Sea, transmission of oil via 185 km long sub sea pipeline to an onshore terminal at Sangachal, and transmission of gas via 50 km pipeline to SOCAR at Oily Rocks (an offshore island/facility near Baku). Export of oil from Sangachal will be via 12 km long new pipeline, which connects to the existing pipeline near the Russian border (Northern Route Export Pipeline). An unfinished western pipeline goes through Azerbaijan and Georgia (Western Route Export pipeline – WREP) to a new storage terminal at Supsa and an off-loading facility on the Black Sea. The Chirag platform, the sub sea pipelines, the Sangachal terminal, and the pipeline to Russia are currently operational. Remaining facilities are under construction.

The Early Oil project involves production of 100 000 to 150 000 barrels of oil per day. The project was supposed to prove the drilling potential of politically unstable region. The purpose of the pipeline construction was solely political. The governments agreed to build the pipeline, although its construction is not cost effective.

Environmental Categories

The project was screened as category A, requiring environmental impact assessments (EIAs) of the key project components, audits of existing infrastructure, disclosure of information, and public consultation. The EBRD reviewed six EIAs on the key project components such as drilling, early oil production, and export through the pipelines.

Environmental areas of concern are the following:

- soil contamination;
- surface and ground water contamination;
- damage to natural habitats;
- oil spills;
- waste management; and
- worker's health and safety.

Caspian Sea

The Caspian Sea is the largest inland water in the world. Geological history and a long-term isolation from the world's oceans resulted with unique ecosystem. The Caspian region is a habitat of various aquatic, avian and terrestrial species that are vulnerable to oil spills and discharges. This region provides habitat to 33 mammal species, 289 plant species, 256 birds, and 1248 insects. More than 90 percent of sturgeons live in this Sea. One of the endangered species is the Caspian's seal, the smallest seal in the world that usually migrates to the middle and southern part of the region, which is included in the project area.

The Sea is already affected by the oil exploration. The offshore areas are especially rich with oil. The estimations of oil reserves vary from 15 to 30 million barrels to 100 to 200 billions. The region has already been affected by the oil extraction. It was estimated that annual oil discharges reached 100 000 tones between 1986 and 1990.

Environmental concerns should not be underestimated because of economic or security interests in the region. Rapid increase in oil exploration and construction of pipelines can cause irreversible environmental damage to the Sea.

Environmental conditions of the Caspian Sea are degrading rapidly. The increased water level is damaging coastal areas, while increased oil concentration causes severe damage to the whole region.

Chirag Oil Field

The Chirag platform-1 begun to operate on November 12, 1997. The platform generates wastewater that is discharged into the Sea. However, the AIOC/EIA states that the problem of wastewater treatment will be investigated and that "water will be discharged 50 meters below the Caspian mean level to prevent damage to productive biological zone ”.

During the EIA preparation, the model of the North Sea was used. It was concluded that potential impacts on the Caspian Sea from oil spills and discharges would be lower since the Caspian had less bethnic biomass and more sparse communities. However, it is not possible to compare the North and Caspian Sea because the Caspian is enclosed water.

Oil pollution resulting from oil spills and chronic daily production discharges will have severe impacts on the endangered Caspian seals and waterfowl birds.

EIA documents state that the project will be in accordance with the World Bank standards for chronic oil and grease discharges such as those emanating from the Sangachal Terminal into sea-grass beds that provide important spawning habitat for sturgeon. These standards are outmoded, and far from the best international practices used by the US Environmental Protection Agency (US EPA). According to these standards, the average discharges are controlled on a daily and monthly basis. The US EPA's standards were used even in cases where the potential environmental risk was not so high. The highest international standards should be the EBRD's and other international financial institutions' condition in underwater pipeline construction. In addition, these standards should be applied for the Environmental Action Plan, especially for discharges during the project implementation.

The EIAs indicate that water-based muds will be used for drilling in the early stage, while synthetic muds will be used in later stages of the project. Synthetic muds are highly toxic and because of its adverse impact on the aquatic ecosystems, they were banned in the North Sea. The enclosed body of water is even more vulnerable to toxic inputs and, therefore, water-based muds should be used in all the stages. However, the AIOC EIA stated that "the current SPA requirement will allow these synthetic muds and cuttings will be discharged in the Caspian."

AIOC's responded to NGO letter on July 1998, stated that AIOC is considering a reinjection of drilling wastes into the formation under the Caspian Sea and considered either extending the discharge pipeline from Sangachal terminal at Baku well or reinjection the discharge on land.

Black Sea

The WREP and NREP are terminated on the Black Sea. The Black Sea is a large, enclosed body of water with a high concentration of hydrogen sulfite below 200 meters. Once, it was one of the most product seas, hosting sturgeon, maasbanker, bonito, turbot and trout. Due to the high pollution and fishery over the last decades, the number of species decreased significantly. Approximately 249 plant and animal species are under the threat. Since 1993, there is an ongoing Black Sea Environmental Program with the GEF and World Bank support. Since the Black Sea is one of the most polluted seas in the world, six countries in the region prepared the Black Sea Strategies Action Plan on October 31, 1996.

Northern Pipeline

The Northern Rout Export Pipeline (NREP), 1411 km long, connects Sangachal terminal with Novorosysk Port in the Black Sea. It passes close to a number of hunting areas and reserves such as the Gubustan desert. The major environmental concern is leakage in ecologically sensitive areas.

The land contamination survey was undertaken only for Azerbaijan part of the NREP. The pipeline corridor is affected by oil pollution from the abandoned Saizin onshore oil field. However, an assessment for the whole route has never been undertaken. An agreement with the AIOC states that only the clean up activities will be undertaken only if contamination will resulted from the AIOC's use of the pipeline.

One accident has already occurred on January 1997, when 1000 tonnes of oil were accidentally discharged from a corrosion hole in the northern pipeline.

Western Pipeline

On March 1996, an agreement between the Georgian International Operational Company and AIOC's representative in Georgia Pipeline Company was signed. This agreement started the Western Route Export Pipeline (WREP) project. The main objective of this project is construction of oil export pipeline from Azeri.

Initially, it was planned to use sectors of the old pipeline and build only one, 90-km long segment to connect the existing pipeline in Georgia/Azerbaijan with Supsa terminal at the Black Sea. Since the modernization project discovered that the pipeline would not be usable due to heavy corrosion, the entire stretch from Baku to Georgian border needs the replacement.

Environmental Impact Assessment

On June 1997, the AIOC released two EIA documents; the Pipeline Refurbishment and Construction from Georgia-Azerbaijan border to Supsa terminal and the Supsa terminal and offshore loading facility. Additional environmental surveys and environmental management plans were required by the Georgian Ministry of Environment.

WREP crosses five conservation units and passes nearby four protected. As the WREP crosses 27 rivers, it was required to bury the pipeline two meters under the river-bed. Another requirement was to mitigate the environmental damage caused by the construction, especially near the Gardabani reserve. Since the Supsa terminal is near the Kolkheti wetland, which is protected by the Ramsar convention, environmental management, mitigation, and monitoring programs were needed.

The Baseline Environmental Survey stated that "Kolkheti reserve is situated in one of the most sensitive areas adjacent to Paliastomi Lake, and Supsa terminal may have potential impact on unique wetlands communities and Kolkheti Forests. Therefore, it is strongly recommended to enlarge the territory of reserve.”

Cumulative effects of oil spills require appropriate response plans. Tanker accidents and spills from terminals are the main sources of the world ocean pollution. This fact clarifies the need for Transboundary Impact Assessment of the oil transportation projects under the Espoo Convention guidelines.

A "Nassia" accident, which happened in Bosporus 1994, demonstrated again the environmental risks of oil transportation. Approximately 20 000 tonnes of oil were spilled into the Sea. Another big accident with severe transboundary effects occurred on December 29, 1999.

Comments

After decision to construct entirely new pipeline was made, the project's cost jumped from USD 315 million to USD 590 million in 1998. The AIOC and SOCAR are arguing about who should pay additional costs. The SOCAR vice president Ilghem Aliyev said: "Unfortunately, Azerbaijan can not agree to pay these expenses. The western route pipeline is not needed at such a price." (Caspian Investor June/July 1998)

Public Participation

In June 1998, before the EBRD's Board meeting, NGOs sent several letters to the IFC. IFC and EBRD officials stated that public involvement should help in ensuring stronger environmental safeguards and transparency. It was also said that public participation has already improved the project and contributed to the decision to replace the western pipeline.

However, the process did not go so smoothly as described in the EIA. NGOs' letter to the EBRD pointed out the following:

- need for transparency before the project approval;
- application of EBRD's information disclosure policy;
- public participation and agency review of all Appendix 1 documents;
- need for Environmental Management Plan and Environmental Action Plan;
- re-injection of drilling wastes into the sub-sea formation;
- use of non-synthetic drilling muds during the all project stages;
- need to upgrade and re-directing proposed land-based pipeline routes; and
- assessment of cumulative greenhouse gases emissions.

The letter was partially taken into consideration and a loan approval procedure included some of NGOs' recommendations such as wider public participation, release of all Appendix 1 documents, surveys and management plans, and Oil Spill Response plans that have not been presented before.

At the same time, it was not clear whether future decisions about re-injection of wastes or pending emergency spill response plans, will be subject to public discussion or not. It is possible that the IFC and EBRD simply make the decision transparent after they make it.

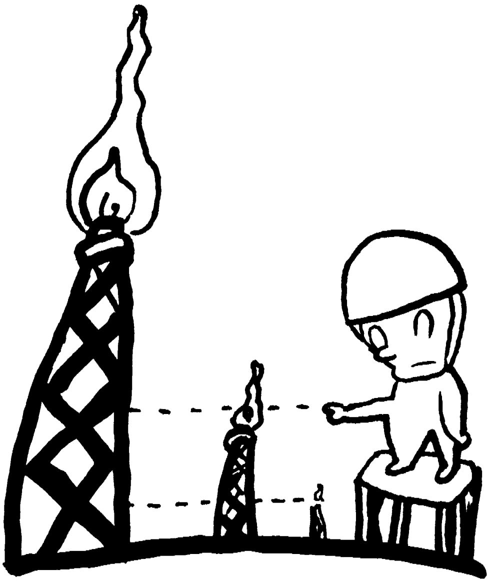
However, the EBRD and IFC do not commit for drilling water re-injection and the use of non-synthetic muds. The western pipeline was totally upgraded and rebottled, while the northern pipeline was not finished because of technical problems and accidents. Oil transportation was stopped through the northern part for several days in 1999. Water-based muds were used only in the early stages of the project.

Sponsors committed themselves to refurbish the old pipeline in Georgia. However, sponsors replaced just the important parts of the existing pipeline to increase the flow capacity. Replacement of the old pipeline was one of the requirements that were identified by the experts and NGOs during the EIA procedure. These requirements were simply neglected. In addition, sponsors did not carry out the new EIA and decommission of the old pipeline. Only after several leakages took place in the spring of 2000, mitigation measures were undertaken.

Georgian scientists have discovered several erosion sites along the western pipeline. Because of heavy rains in December 1999, the AIOC was asked to stop oil transportation from Baku to Supsa. Certain parts of the pipeline were completely uncovered and it was not possible to continue transportation.

Environmental management plan for the western pipeline was not completed as well. According to the project documentation, the EBRD required the OSRP before the approval. In spite of that, the OSRP has never been completed. The only available document was the Oil Spill Response Plan from 1999.

Cumulative impacts on the greenhouse gases emissions were never reviewed, although it was supposed to be a part of the EIA procedure. Although G-8 countries clearly stated at their Summit Communiqués in 1999 that "... we must ensure that policies and operations of the International Financial Institutions consider possible impacts on the climate change", the assessment of the Chirag Early Oil Project' effects on the climate change was not performed.



9.

Adjusting Hungary

Introduction

The World Bank does not take any responsibility for the data presented in the paper, and for the policies that would be implemented on their basis. This is a statement written on the cover of the volumes that include World Bank recommendations. It is reasonable to ask why the Bank would expect the implementation of its policies by national governments that are responsible to their voters, if the Bank itself were not willing to take responsibilities.

This paper addresses concerns about the policies of the World Bank in Hungary. Did those policies assist the transformation of the Hungarian economy and society for the benefit of the Hungarian people? To what extent did the World Bank programs function as an obstacle to development through its direct demands and intellectual influence?

The Programs of Reform and Transition

Hungary was one of the few members of the World Bank and the IMF in Central and Eastern Europe. Because of that, this paper will examine two decades of cooperation; one for the period before the collapse of communism, and the other for the period of the new Hungarian capitalism.

Crisis Management in the 1980s

Hungary became a member of the World Bank in 1982, shortly after joining the IMF. The general expectation was that membership in the World Bank would provide Hungarian economic policy with access to better development funding, foreign markets and orders, and even some guidance to the modernization of production and management.

However, 1982 was the starting year of the debt crisis, which motivated the country to join the Bretton Woods institutions along with other countries that were destabilized by the economic and financial turmoil of the 1970s, and who hoped to strengthen their economic positions. Therefore, the IMF and the World Bank were able to influence the economic policy of Hungary very significantly since the 1980s, with a greater impact since the early 1990s. The activity of the World Bank was to promote economic liberalization and deregulation, and to encourage privatization in the competitive sectors such as the public utilities and welfare institutions.

In the eight years following the accession of Hungary in 1982, the World Bank provided 20 program loans to support Hungarian economic reforms. In most cases, the loans were taken by the National Bank of Hungary with state guarantees and in two cases by the National Oil and Gas Trust. The loans provided between USD 25 and 200 million each, and covered all branches of the economy including grain- to -energy, coal, chemicals, transportation, and industrial reconstruction. These programs strengthened the role of market incentives within those sectors, and contributed to the improvement of export competitiveness. Because of Hungary's membership in the World Bank, Hungarian companies won tenders organized by the World Bank and IDA at the range of USD 160.

In 1985, Hungary joined two members of the World Bank group, the IFC and the IDA. The first action of IFC was to transform the banking system. They helped found a bank (UNICBANK) through a 15 percent participation (USD 28 million), and five years later they sold their share to a German cooperative bank that also was s founding member of

UNICBANK. In the second half of the 1980s, IFC helped establish some joint ventures.

Hungary was unable to draw loans from IDA since the goal of this organization is to assist the development efforts of the poorest countries. On the other hand, Hungary took part in filling the IDA's funds, especially in the IDA's lending activities in Africa and Asia.

By March 1988, the World Bank provided 19 loans to Hungary. Six loans involved other creditor agencies as well. 43 percent of the loans were for industry, agriculture, and 16 percent by the energy sector, and eight percent by transportation took 32 percent.

The agreement on the Industrial Structural Adjustment Loan (ISAL, 2965-HU/1988) was signed on July 1, 1988. This loan amounted to USD 200 million, with an additional 50 million provided by the Japanese EXIM bank. By signing the loan agreement, the Hungarian government committed itself to:

- improve the balance of the state budget and stop the foreign indebtedness of the country within two and a half years, i.e. by the end of 1990;
- decrease the amount of subsidies for both the producers and consumers by an additional ten percent compared to the 1988 plan;
- adopt a company act that enables transformation of the state-owned enterprises into shareholder companies, allowing the purchase of shares for individuals, and allowing individuals to found limited companies; and
- change the system of income taxation and liberalize wage regulation.

Almost all of these requirements were fulfilled by the deadline. The only exception was lowering the subsidies, which did not meet a targeted ten- percent. According to the official evaluation by the Bank, the program was successful, but needed further tightening in the reform of price subsidies. According to the Hungarian government, the experts of the World Bank greatly helped their Hungarian partners in the preparations of a coordinated program. The continuous political dialogue between the World Bank and the government was broadened by cooperation on economic policy affairs.

The cooperation was mutually beneficial. The World Bank and the IMF used the economic reforms as tools for "loosening up" the political system because deregulation and liberalization, that were showing the way towards a market economy, had inevitable affects on the social and political structures. On the other hand, these economic reforms coincided with the Hungarian strategies for diminishing the Russian influence and creating more open economic and political structures. This is why the cooperation between the Bank and the Hungarian government was justified and widely accepted in the 1980s and 1990s.

Structural Adjustment in the 1990s

After the fall of the Berlin wall, the multilateral financial agencies initiated structural and institutional reforms with much greater ambition than before. In Hungary, this endeavor materialized in two comprehensive structural adjustment loans; one in 1990 and another in 1991. The aim of these loans was liberalization, privatization and deregulation. In the early phase of the transition (1990-'92), further credit facilities supported the reform of the financial sector, the export of agriculture, and the reforms in communication, human resource management, product markets and enterprises.

The representatives of the World Bank and the National Bank of Hungary signed the first one of new comprehensive reform loans (Structural Adjustment Loan, SAL) with a government guarantee on June 21, 1990. The amount of the loan was USD 200 million provided from the Japanese EXIM bank, and one billion from the European Community. One of the loan's requirements was the amount of USD 40 million aimed for import commitments that had been made before. The main goals of the loan were:

- to begin closing the insolvent big enterprises and state farms, and to start privatization on the basis of a joint strategic program;
- to liberalize at least 60 per cent of the non-industrial imports;
- to lower the producer, investment, consumer and housing subsidies to below nine per cent of the GDP in 1990;
- to strengthen social welfare programs to handle unemployment;
- to cut costs in the pension and health care systems; and
- to introduce a system of macroeconomic and financial indicators according to the principles of the World Bank.

During the preparations and the implementation of the SAL, the relations between the Bank and Hungary became closer. Under the auspices of this agreement, for instance, a comprehensive assessment of the system of social policy, and the size and the structure of the entire state budget was carried out. In this period, privatization took place largely in line with the World Bank instructions.

Due to the rearrangements resulting from the collapse of eastern trade relations, the liberalization of foreign trade took place much faster than it had been planned. It had reached 72 percent in 1991, and the law of foreign trade was simultaneously liberalized too. By the end of 1990, almost 90 percent of consumer prices became free. In 1991, the National Price Office was abolished, and the Economic Competition Office was established instead to monitor and sanction inappropriate market behaviors.

The state construction industry was reorganized, or privatized. The housing subsidies were lowered. The comprehensive pension and health care reforms were delayed, but measures were taken to increase the eligibility period from ten years to 20 years in case of pensions. The rise of pensions was linked to the net incomes. With the objective of cost efficiency, performance related financing was introduced in health care. The subsidies on medications were lowered, and the prescription procedures were made tighter.

Assessing the early results of the SAL, both sides concluded that there would be a need for further involvement of the World Bank in the transition process. This recognition resulted in signing the second SAL on July 5, 1991. One of the main aims of the loan was to support the urgent import needs raised by the first SAL. The amount of SAL II was USD 250 million, although eventually only 175 million were drawn because the Bank blocked the last tranche - and eventually cancelled it in 1994- due to the slow progress in the reform of the public sector and the excessive deficit in the state budget. The Japanese EXIM bank amended SAL II again with an additional USD 150 million.

In addition, to the other program elements, the aim of the loan was to reduce the role of the state in the economy and to accomplish liberalization. In order to fulfil this, the government passed a new bank act imposing stricter penalties for bankruptcy and reforming the financial sector. To reduce the seize of the central state budget, they decided upon a plan that was to reduce the financing of government institutions, and privatize certain elements of applied research, education, training and culture. A part of the program was to design a budget for the year 1992 that would reduce the level of consumer, producer, investment and housing subsidies by at least two percent compared to the level of 1991. Furthermore, the price structure and price formation for gas and electricity were also changed by this agreement, in order to allow covering the costs with a reasonable profit level. The government committed itself to cooperate closely with the World Bank to prepare the reform of pensions and health care. In case of pensions, the government decided to equalize the pension age between males and females by 2000, and to increase the age for pension eligibility.

With the SAL II implementation, many more controversies between the Hungarian government and the Bank have emerged. The Bank criticized the government for the emergence of macroeconomic deficits and for the delay in the reform of health care financing. Since the end of 1992 the balance between the foreign trade and the budget has worsened, and the government was not prepared to implement austerity measures to eliminate the deficit. Because of that, the Bank cancelled the third USD 75 million tranche and made the rest conditional on a major adjustment package.

Apart from this, the Bank criticized the implementation of the program because of excessive companies' losses, the costs of the bank consolidation, and the household transfers in the GDP. It seems their experts did not take into account the fall of GDP by approximately 18 percent between 1989 and 1993. The Bank was not satisfied with the measures concerning the tax and pension systems too, while its own preparatory and instructive role was evaluated as excellent.

Before the partial failure of the SAL II, another loan agreement was signed to promote privatization. The Enterprise Reform Loan (April 1992) included three main points; privatization, transformation of state owned enterprises into shareholder companies, and implementation of liquidation procedures. The loan amounted to USD 200 million, but without the previous Japanese amendment. In addition to the transformation and privatization of state companies, the government committed itself to create a new holding company for the management of firms that would remain in state hands in the long run. The work program of this new holding was to be coordinated with the Bank.

In the second half of the 1990s, the Bank became more cautious because of the previous program failures, though it maintained its direction towards transition. The Bank's top priority remained the reform of the public sector and social security, as well as the reform in health care and education. The two major loans of the second half of the 1990s were devoted to these areas, i.e. to finance the transformation of the pension system and higher education.

IMF Activities

To get a full picture, we also have to look at the IMF activities. After the beginning of the transition, the IMF also changed its strategy and supported the World Bank financed reforms by extending facilities and authority. The Fund made stand-by, compensation and extended agreements with Hungary, and demanded the acceleration of structural adjustment, the fulfillment of import liberalization and the abolition of subsidies. The most significant loan agreement with the IMF was from 1991 (SRD 1.1 billion), which was a three year loan that had no precedent. Apart from this, the Fund provided assistance to cover the losses emerging after the Gulf crisis and the negative developments within CMEA (Comecon).

The economic developments, however, did not turn out exactly as expected by the Fund. The disintegration of the Soviet trade bloc undermined the financial situation of Hungary. Because of that, the government asked for derogation from the fulfillment of the budget criteria in 1991. However, due to the excessive deficit, the Fund suspended the tranches of the credit in 1992. In spite of this, another stand-by agreement was signed in 1993 but, since the government did not follow the agreement at all, it was unable to draw the quarterly items.

In 1993 and 1994, Hungary built up an unprecedented deficit in the current account as a result of the policies of the ruling Hungarian Democratic Forum. At that time the IMF changed its conventional attitude and was prepared to sign an agreement only after the adjustment measures were taken. These measures were taken by the Socialist-Liberal coalition, during the so-called Bokros program in 1995. Bokros included some of the policies in his 25 point's package that were the part of the World Bank recommendations but had been either ignored or attempted unsuccessfully by the previous government. Though the IMF agreed with the austerity measures, it only provided assistance after the program already succeeded. However, the government did not need the money from the IMF and the tranches were not drawn. The agreement in 1996, however, helped bringing down the spread over the market credits taken by Hungary, and also to bring the country into OECD in 1996.

Main Policy Areas

When evaluating the activities of the World Bank in Hungary, we have to analyze those measures that have always been crucial in the Bank programs, and which were also seen by the Bank as cornerstones of a successful transition to the market economy. These areas are; deregulation, liberalization, privatization, and the reform of the public sector together with welfare systems.

Deregulation and Liberalization

Apart from the main economic reforms, deregulation and liberalization were among the first reforms that took place in Hungary. The reason for this is the aim of Hungarian leadership, which started in the late 1970s, to overcome the financial crisis through market reforms. The area of market reforms was not so ideologically sensitive as privatization. The government, together with the World Bank decided to deregulate ownership of the companies when the abolition of state-owned companies was not yet on the agenda.

The breakthrough in deregulation and liberalization took place in the late 1990s, with general price liberalization and a radical reduction in subsidies. In 1987, the state started to withdraw from the direct financing of big companies. The amount of direct subsidies was reduced and the first bankruptcy law was passed. Concerning wages, however, liberalization was implemented with some delay, because the monetary policy makers saw the outflow of wages as a main threat to financial equilibrium.

The Hungarian government decided to liberalize imports in June 1988 with strong support from the IMF. The World Bank did not take part in the import liberalization program directly, but it accepted the schedule developed by the government. As a result of the import barrier abolition, the imports increased rapidly, thus affecting the domestic production. This resulted in a trade deficit in the period when the economic growth was expected (1993 and 1994).

When the process of liberalization slowed down in 1988, it was not anticipated that the collapse of the state socialist regime would result in a regional disintegration and that the domestic institutional transformation would increase the sense of uncertainty. However, the program should have been adjusted to the changing circumstances in the early 1990s, and this adjustment should have encouraged slower, rather than faster liberalization. Even if the liberalization policy, i.e. the abolition of the so-called authorization system, was to be continued, it could have been amended with the introduction of temporary customs, or a real depreciation of the Hungarian forint. In practice, a real appreciation of the Hungarian forint took place, and no temporary protection was provided for the Hungarian industries. Simultaneously with the impact of the bankruptcy law, this policy resulted in a collapse of Hungarian manufacturing and agriculture.

The World Bank also tended to criticize this accelerated and single minded liberalization policy. They thought it was a policy going far beyond the conventional shock therapies. However, the Bank came to this conclusion too late perhaps because their experts were not fully aware of the complicated authorization system that regulated foreign trade in Hungary. Thus they were unable to recommend compensatory measures that could have minimized the losses caused by the neo-liberal reforms.

Privatization

In Hungary, the governments in the period of the transition applied different privatization policies, partly because of their political character, and partly because of the changing circumstances. With social or liberal governments, financial motivations dominated the policy agenda, while social issues became more important during the dominance of the right and center parties.

The 1988 ISAL agreement between the World Bank and the government was the first one focused on the question of ownership. Individuals initiated a Company act that facilitated the transformation of state-owned enterprises into shareholder companies, and also enabled the foundation of private enterprises. The actual privatization began with selling a dozen firms of various industries to foreign owners, and also by the emergence of the so-called spontaneous privatization that soon became a synonym for theft in the Hungarian slang.

In the period after the parliamentary elections in 1990, three structural adjustment loans by the World Bank dealt with the question of privatization. They were, however, unable to anticipate the multitude of political effects influencing the actual course of privatization. Thus the recommendations of the Bank became almost irrelevant for the practice of privatization. The quantity of the latter became much more ambitious and in terms of quality it found a much greater variety of techniques. The official evaluations by the Bank declared that the Hungarian government completed that part of privatization.

Privatization came to a third phase in 1995, when the Socialist-Liberal government extended it to new areas, like public utilities and banking. In a financial sense, this privatization was successful, because it contributed to a substantial reduction of the foreign debts of Hungary. Nevertheless, the policies of this period received great criticism, because the sales contracts ignored much of the long-term consequences of privatization in terms of the prices and availability of services, as well as labor relations and environmental standards at the privatized companies.

In this period, the World Bank did not have a direct impact on shaping the privatization policies, since the financial crisis was enough to drive the government into the sale of the "family silver". The same considerations made the government continue the general laissez-faire attitude towards foreign direct investment. As a result, a dual economy was emerging in Hungary, with a dominant multinational-manufacturing sector that enjoys tax and customs breaks as opposed to the underfunded domestic owned industry. Apart from the unfairness of such a situation, it is not sustainable if we take into account the future integration of Hungary into the European Union.

The discussions about privatization reached the highest point after the sale of the electricity supply companies since they were sold without public participation. This caused the rise of consumer prices of several thousands of households without sufficient compensation. The privatization of this sector was not part of the blueprints of the first post-communist government, and not evens of the World Bank proposals. In its studies, the Bank emphasized the importance of a strong regulator, needed for a successful privatization. Nevertheless, the end of 1995 accomplished the privatization of the public utility sector. By that time, almost half of the non-competitive infrastructure fell into private hands. In January 1998, the Hungarian government winged a new PSAL agreement with the Bank to finance the public sector reform, but the implementation of this did not begin because of the change of the government soon thereafter.

Welfare Reforms

During the decade of the Hungarian transition, there were numerous discussions about the so-called public sector reforms. However, no comprehensive blueprint for performing such a reform was proposed. Perhaps this is because in the early phase of the transition the main focus was on restructuring the competitive sectors. Also, there was no political party that was prepared to make it explicit what social groups would be outright losers of the proposed or implied reform measures.

Indeed, welfare institutions and the recipients of welfare redistribution were losers of the transition. In other words, governments favored the promotion of health care, education, culture and families. In reality, all of them were captives of the economic ideology that wanted to minimize the role of the state, and thus to diminish the role of redistribution in society. All these so-called welfare areas fell victims to the resulting expenditure reduction. By 1996, the real value of state expenditures on social, health care and cultural purposes fell by a quarter.

Quite opposite to the case of privatization, the World Bank had quite definite and detailed ideas about reforming welfare. Its health policy had a very narrow focus on reducing costs, while the Bank experts also paid lip service to accessibility and quality. The same view applied to family benefits, which seemed excessive as compared to Western Europe because of the specific income structures of the state socialist system. While the text of the policy papers alluded to the reduction of poverty, and especially child poverty, the actual recipes focused primarily on the reduction of spending. This narrow-minded health and family policy was especially problematic in a period when people lost theirs jobs and other sources of income. It must be mentioned, however, that the Bank experts proposed certain aid techniques that were ignored by the Hungarian policy makers.

The cost cutting focus also was extended to the education reform proposals of the Bank. The main example for this is the USD 150 million loan for the restructuring of higher education (1998). By elaborating on the reforms of education, the Bank ignored the traditions and values of the Hungarian system, and insisted on savings even in cases where it had a direct negative impact on the quality of teaching. At the same time, the Bank did not pay attention to the real problems of the Hungarian education, such as the falling real value of funding, and the miserable low wages of teachers. As a result of structural adjustment and related austerity policies, the wages of teachers fell by 30 per cent, and the share of higher education in the GDP fell from 1.3 percent to one percent, while the OECD average is 1.6 percent.

The most significant single reform in the welfare system was pension reform, which gained international fame too. By the time the pension act was passed in 1997, the retirement age had been increased and private pension funds started to operate. The need for further reform was made explicit in the papers of the Bank and in the loan agreements too. The demand for partial privatization and for the introduction of the so-called three-pillar model appeared in 1994 only. The activity of the Bank encouraged experts and financial interest groups that were for the privatization. They all supported the maneuvers of the ministry of finance under the Socialist-Liberal coalition, which was the main agency behind the 1997 reform.

The assessment of the new pension structures suggests that advantages will mainly affect the richest groups of the society whose open and hidden influence on the parliament and the governments has been very strong. The pension reform is an example of the practice that was not forced by any objective factors but with the involvement of an external agent (the World Bank) and the change in power.

Conclusion

Over the past few years Hungary was seen as a success story among the transition countries in Central and Eastern Europe. In reality, Hungary was just another example of the Washington policy failure. In the East European transition, there were no exceptions since the general neo-liberal policy provided a straight jacket for economic and social development in the entire region. Within these conditions, individual national governments could have made better or worse choices, but even the smarter ones could not escape the main negative trends created by neo-liberal structural adjustment.

The so-called Washington consensus, which was elaborated in indebted Third World countries, was imported to Eastern Europe after the fall of the Berlin wall and showed the same outcomes. Of course, the Bretton Woods institutions are not exclusively responsible for the dire outcomes, but their responsibility is much greater than the content of the agreements made with governments. Many of the so-called local experts had been World Bank or IMF employees before, or studied similar views with scholarships at certain US universities.

The record of the Bank and fellow organizations interprets the reforms saying that in Central and Eastern Europe a multitude of unforeseen developments made the situation very complicated, thus affecting the success of these reforms. However, unfavorable circumstances could have been predicted. In the time of uncertainty, the neo-liberal experts of the World Bank and other Western agencies should have been more cautious instead of lobbying for shock therapies.

The Bank experts did not consider the local government's opinion in many cases. One of those neo-liberal experts, also a former World Bank employee, often claimed that the university professors could get a decent salary if the lazy workers were laid off. In the 1990s, however, the emergence of mass unemployment was accompanied by a dramatic decline in the real wages of university professors. The point is not that the so-called expert made a wrong forecast. The example shows that certain negative impacts may arise not from external shocks and necessarily under external pressure, but from a deliberately adapted neo-liberal framework.

Ten years after the beginning of the transition, the World Bank has become one of the few multilateral agents that were open to a critical assessment of the past. The Bank was engaged in a dialogue with non-governmental organizations, in order to counter-balance its previous secrecy and liaison with special interest groups. More open approach to a civil society, however, should only be seen as a beginning of a change. In a social oriented economic policy, which is to be designed for the 21st century, finance should serve the needs of society, without hurting the environment.

In Hungary, new economic and social policies are needed to remedy the damage that has been done during the 1990s. In addition, new policies must be prepared for the country's accession to the European Union. This integration can only be successful if the social and environmental standards are in accordance with EU standards. To achieve that, neo-liberalism, which was imposed by the IMF and the World Bank, must be rooted out from public policy.

10.

Trouble and Opportunity from the Start

Introduction

For decades now, activists have been working hard to oppose the destructive projects and policies of the World Bank[1]. There have been failures and some spectacular successes, all of which have taught activists something about how to campaign against one of the world's most powerful institutions. One such lesson is that the earlier activists get involved to try and change the Bank's misguided direction, the more likely are the chances of success. One of the earliest stages activists can get involved is during the period that the Bank plans its future operations for a particular country or, in other words, during the development of its Country Assistance Strategy. This document is intended to assist activists who wish to participate in the development of such a strategy and is based on the previous experiences of groups from the Central and East European (CEE) region.

What Is a CAS?

The World Bank prepares a `Master Plan,' or Country Assistance Strategy (CAS), for each country in which it has operations. The CAS's principal purpose is to identify which adjustment and project investments the Bank plans to finance in the medium term (usually three years). The CAS is therefore used by the Bank to:

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[1] This document is based heavily and expands on the Bread for the World Institute's, „Who Shapes Your Country's Future?: A Guide to Influencing the World Bank's Country Assistance Strategy" written by Nancy Alexander, as well as from the Bank Information Center's, „The World Bank's 'Master Plan' For Your Country: The Country Assistance Strategy." Both are excellent sources of information for anyone interested in the Bank's Country Assistance Strategy

- justify its involvement in a country based upon its assessment of financial risk and return on investment, the country's priorities, the activities of other donors and creditors, and the way that the Bank defines its comparative advantage;
- identify the analytical work and lending operations planned for the timeframe of the CAS; and
- describe the health, or quality, of the borrower's Bank-financed operations. The collection of all Bank-financed loan operations in a country is called the loan ”portfolio.”

In theory, the CAS outlines the Bank's future operations. In reality, however, this may not be the case.

In the beginning stages of the CAS development, civil society may wish to inform and influence the Bank‘s Economic and Sector Work (ESW), which serves as the analytical foundation of the CAS. The ESW includes the:

- Country Economic Memorandum: The strengths and weaknesses of the economy and of the governments' economic policies.
- Public Expenditure Review: The strengths and weaknesses of government management of the fiscal budget.
- Sector Reviews: the strengths and weaknesses of management of policies for a sector (e.g. forestry, waste, health, education, small and medium sized enterprises, energy, water management, etc.).
- Poverty Assessment: Nature, causes and extent of poverty (this could include analysis of the Roma or homeless situation, etc.).
- Private Sector Assessment: Market-friendly character of economic policies.
- National Environmental Action Plan: Major environmental problems (e.g. air pollution, biodiversity

loss etc.), government capacity to tackle them, and key actions needed for improvements.

The Bank‘s CAS influences government policies by raising or lowering a government‘s access to Bank credit based upon the government’s fulfillment of CAS ”triggers.” Each government‘s CAS contains triggers, which may require that the government achieve certain macro-fiscal targets (e.g. as outlined by an accompanying IMF program), sectoral/structural measures (e.g. privatization, trade liberalization, industry or social sector reforms, etc.), and portfolio measures (e.g. resolution of project-specific problems, reduction in the number of problem projects, etc.).

Thus, if a borrowing government performs well according to the Bank (e.g. accomplishes most trigger actions), it may be rewarded with a higher credit limit. If, on the other hand, a government performs poorly, its credit limit may be lowered.

Finally, it is important to note that in determining which projects to fund, the Bank considers three criteria: the magnitude of impact (e.g. the importance of the activity and its potential impact on economic performance and poverty reduction); the probability that the activity will be implemented successfully given the country‘s capacity and commitment; and the ”additionality of the Bank‘s contribution,” or its comparative advantage, in relation to other lending institutions.

Why Civil Society Should Participate

The Bank states that its primary goal is poverty reduction and that it is committed to socially and environmentally friendly lending. However, history has shown that Bank-supported operations often do not meet these goals and, in many cases, actually work in opposition to them. Furthermore, the findings of the Bank‘s own review of 44 CAS's shows that nearly half of Bank lending is concentrated in only a few areas- e.g. macro-fiscal management (Bank reform, restructuring of government’s fiscal policies, etc.), and infrastructure (motorways, dams, etc.). Meanwhile, other priorities were given short shrift, such as social protection, energy, social development and gender.

It is, therefore, important that civil society make its opinions known and attempts to influence choices by the government and the Bank of operations that are deserving of financial support. For example, although the Bank provides substantial finance for constructing waste incinerators, civil society may believe there are other means for addressing waste management problems. Therefore, non-governmental organizations (NGOs) with expertise in waste management may want to inform the government and the Bank of investment alternatives which can address waste management problems within the country. Likewise, the Bank may support changes to the national social insurance program, but this may not be the best approach to helping those in poverty. Therefore, those working on poverty issues would likely want to educate the Bank on such issues.

In addition, influencing the CAS process can inform the government about the priorities of civil society. The CAS contains the Bank‘s perceptions of the strengths and weaknesses of certain government policies. Civil society can exert leverage by articulating its agreement or disagreement with the Bank‘s analysis, by supporting or opposing government positions, and presenting its own independent positions.

Civil society can also highlight their concerns through their support or disapproval of the Bank‘s choice or program of sectoral or structural triggers. For instance, if education reform were selected as a trigger and civil society viewed this as a positive step, then civil society could express its support and attempt to help shape the reform process.

Furthermore, if the government consents, the Bank will release the final CAS document and if it incorporates civil society concerns, then it will help advance the objectives of civil society groups. The CAS has the potential to be a powerful tool for civil society, but only if civil society makes its voices heard in clear and powerful way that makes the Bank take notice.

Experience on the Ground: CAS Case Studies from the CEE

What follows are several case studies from the CEE region that highlight the strengths and weaknesses of the World Bank’s CAS consultations and development. There are many common concerns that can be found in all of the case studies, and yet there is also clear evidence that the Bank is inconsistent in its implementation of CAS consultations and development and thus requires clear and enforceable guidelines to be applied in all future CAS formulations.

The Country Assistance Strategy for Slovakia

In the summer of 1999, Friends of the Earth/CEE Bankwatch member group, and the Center for Environmental Public Advocacy (CEPA), received assurances from officials at the World Bank’s regional office in Budapest that the development of the Slovak CAS would be very open and transparent. With the conclusion of the public consultations in mid-March 2000, it is clear that such assurances were false.

In the early stages of the CAS development, CEPA sent the Bank a list of criteria that it considered essential to ensure an effective and transparent process for the public consultations. These criteria included 1) adequate advance notification as well as a clear framework set for the consultation process; 2) sufficient documentation publicly available at least one month in advance of the consultations, to include the draft CAS, an outline of the consultations and studies undertaken in preparation for the CAS; and 3) that the views and interests of the civil society organizations be seriously considered during the CAS development and such consideration be reflected in the final CAS document. For the most part, these criteria were ignored by the Bank's regional office in Budapest, and what little effort was made toward meeting these criteria was insufficient.

Following three postponements, the first public consultation was held in mid-February 2000, several months after the CAS development begun and less than two months before the CAS was expected to be finalized. Notification of the meeting and the informal note that served as the basis for the consultation was distributed only a few days prior to the consultation. There was no indication of how the consultation process as a whole would be conducted and relevant information, such as the significant role of an earlier World Bank country study and the fact that only two public consultations were scheduled, was made available for the first time at the meeting.

Following the introduction by Bank officials, participants were asked to give comments and ask questions. However, because the meeting was not dealing with specifics, many participants felt unclear as to what they could contribute. Furthermore, rather than seeking input for the CAS framework itself, Bank Officials scheduled consultations only at the time of implementing of the CZS.

Shortly following the release of the CAS informal note, CEPA submitted to the Bank's regional office in Budapest a list of questions, summaries and recommendations from a variety of NGOs working in various sectors relevant to World Bank activities. CEPA expected the Bank to revise the CAS informal note according to the questions and concerns raised in the submission, and to provide a formal explanation as to why some questions or concerns were not addressed in the revised draft. CEPA then expected to have the opportunity to discuss the new draft in further consultations. With the invitation for the second and final consultation, however, CEPA learned that no such draft or explanation would be made available.

Moreover, the NGO that organized the first consultation did not participate in the organizing of the second consultation. The Bank's Budapest office requested that this NGO organize the consultation in approximately one week's time, but the NGO declined saying that it needed at least two weeks to properly organize the event. The Budapest office rejected this suggestion and organized the second consultation with Bank staff. In contrast with the first consultation, no travel compensation was offered and the press apparently was not invited.

The second consultation, held one month following the first one, clearly demonstrated the poor quality of the public consultation process in relation to the Slovak CAS. In his opening statements, one Bank official admitted that the Bank had very little knowledge of the real situation in Slovakia. As the session continued, it was clear that the Bank officials only intended to focus on the implementation of the CAS, rather than the CAS framework itself. CEPA, together with other organizations present, protested that they did not have a revised draft of the informal note to discuss and that the framework of the CAS was not being addressed, despite this being the purpose of the CAS consultations. To support their position, CEPA referred to several expert reports that highlighted the poor record of the World Bank, and expressed their belief that such a poor record is the consequence of the Bank's policy, which is outlined in its CAS.

One of the studies CEPA referred to the Meltzer Commission report, which was the result of a study commissioned by the US Congress. As CEPA described the findings of this study, one Bank official interrupted and asked if the participants were really interested in ”what the Bank did in Africa.” This was an attempt to avoid criticism of the Bank itself in the consultations, despite its relevance to the purpose of the consultations. In response to the Commission report, the same Bank official surprisingly stated that it was just one report from the more than one hundred governments which are represented on its Board. Such a statement suggests that the Bank official intended to mislead a public who may not be fully aware of the specific details of the Bank's governing structure, nor the significance of a study commissioned by the US Congress, which calls for the reduction of World Bank funds and activities, including the elimination of some of its affiliated agencies.

Furthermore, CEPA is skeptical of the World Bank's firm assurances that the public will be fully consulted on the implementation of projects. In the summer of 1999, CEPA repeatedly expressed an interest in, and requested information about, the Bank's Enterprise and Financial Sector Adjustment Loan (EFSAL) for Slovakia. However, as of July 2000, CEPA has not received any reply on this matter from the Bank's Budapest office. Currently, it seems that there have already been extensive negotiations on this loan and yet CEPA has not been consulted on this project, nor has anyone else from civil society to the best of our knowledge. The CAS informal note also calls for a poverty assessment of the EFSAL, but civil society has not been informed of the nature, methodology or timeframe of the assessment.

As the second consultation was being drawn to a close, many NGOs were expressing their confusion as to the purpose of the consultations. Another NGO representative asked Bank officials present when there will be another consultation in relation to the CAS and whether the public will get to see another version of the CAS before it goes to the Slovak parliament. A Bank official, despite the admission earlier that the Bank knew very little about the real situation in Slovakia and despite the confusion at the end of the meeting, responded by saying that he saw no reason for the delay of the CAS and that he does not feel that the Bank needs to be ”audited” on the further stages of the CAS.

The public consultation in relation to the Slovak CAS was inadequate and unacceptable. It was de-legitimized in the opinion of many in Slovak civil society and there would, therefore, be no feeling of ownership of the Slovak CAS, despite the Bank's own emphasis on the importance of such a feeling.

CEPA thus sent a letter to the Bank's Board of Directors asking them to postpone the CAS until appropriate consultations were conducted. Responses from the Executive Director representing Slovakia and other Bank officials indicated that this was not going to occur. This appeared to be the end of the CAS development, but as civil society organizations learned in May, the CAS was being postponed due to a conflict between the World Bank and some within the Slovak government regarding the future role of the IMF in Slovakia. The Bank had conditioned the implementation of the CAS on the Government's accepting an IMF designed and monitored structural adjustment program. Structural adjustment programs are a common tool of the IMF in which they have countries cut government spending, re-orient the economy towards export production and free imports and foreign investment of regulations and duties, among other things.

Some within the Slovak government feared that such an agreement with the IMF would hurt the country’s standing on international capital and financial markets and were thus reluctant to accept such a proposal. Civil society organizations, on the other hand, recognized that the structural adjustment programs of the IMF have had devastating effects on the poor, the environment and small domestic businesses in the countries in which such programs are applied. In the end, however, Government officials were pressured into accepting the agreement, likely due to the fear of the possible withdrawal of Bank support and the chance of scaring away international investors and creditors, which would likely follow if the IMF were to be rejected.

The Country Assistance Strategy for Bulgaria

Bulgaria now has its third CAS prepared by the World Bank. The CAS, which covers the period 1999-2001, includes the description of the work of IBRD and IFC in Bulgaria, as well as their goals, targets, ways to reach them, and specific conditions to be fulfilled by the Bulgarian government. Now, when the CAS time period is half complete, we can assume that a lot of things that were included in the CAS, could have been done better so as to support the sustainable development of the country. Some directions of the development could be better predicted and some measures could be implemented more strictly to promote not only economic, but also social and environmentally friendly activities.

The conclusion is that some of the mistakes, delays or mis-implementation could be predicted and avoided at an earlier stage, and better decisions and implementation steps could be taken if a proper and fruitful discussion was carried out before the CAS approval and during its implementation. This discussion could involve a broad number of governmental institutions and agencies, but also a variety of NGOs, academia, local communities, trade unions, and the media. Such a discussion well structured and with a formal framework of procedures, did not take place. Instead, there were a number of meetings between the World Bank and environmental NGOs, the World Bank and trade unions, etc. All the stakeholders, however, never had the opportunity to sit around a table and discuss the proposed texts or matrix. The understanding among the NGOs was that the Bank also did not want to see practical communication between the different stakeholders on the CAS issues.

Although in the CAS' summary (p. i) it is written, "The strategy has been designed in close consultation with a broad range of stakeholders including government officials at all levels, NGOs, academia, the public, and international development partners," no one could check the input of these stakeholders because there was and still is no information available about who was consulted and what were the suggestions from different parties. There is no list of the proposals that came from the NGOs and other non-governmental institutions, nor of which proposals had been taken into account and, also if they had not been taken into account, for what reasons.

For the first time the question about public involvement of citizen organizations in the preparation of the World Bank's CAS for Bulgaria was raised during a meeting between NGOs and a Bank representative in Sofia on November 21, 1996. The CEE Bankwatch coordinator, Petko Kovatchev (CEIE), put the question up for discussion. He explained that during the years the Bulgarian government adopted many programs, some of them with the help of the World Bank, a number of projects were discussed and some of them already started, but no one, from either the government or the Bank, asked Bulgarian environmental NGOs for comments and suggestions. Moreover, whenever NGOs made their comments and proposals they were usually ignored both by the government and by the Bank. The Bank representative stated that it is usually the Government that blocked the release of draft documents for public consultations.

At the end of the discussion, the World Bank representative promised that the Bank local office will inform NGOs of its missions and that we could arrange meetings with them.

This occurred on five separate occasions. During the preparatory period (1997-1998) of the current CAS, NGO representatives met three times with people from the Bank's energy department (mainly Mr. James Moose). NGOs also met twice (October 24, 1997 and January 22, 1998) with Mr. Kenneth Lay, the World Bank Director for Bulgaria and Romania, which was organized with the help of the local World Bank office in Sofia.

The meetings were used by Mr. Lay mainly to inform NGOs verbally (without any documents) about what is the CAS (a non-binding document, but changes are possible), as well as the Bank's position on different sectoral issues. Following the first meeting, the NGOs wrote a letter to Mr. Lay addressing their concerns. In his reply, from December 15, 1997, Mr. Lay wrote: ”I’ve forwarded the correspondence to my colleagues working in the sectors concerned for their consideration and more specific follow-up.” No one from these sectors (except, again, energy sector expert, Mr. James Moose) contacted NGOs later on.

The following weaknesses marked the meetings and didn’t allow for achieving significant and positive results:

- There was no formal structure for communication or how to achieve results.
- There was no draft of the themes to be discussed; NGOs were not supplied with a draft text of the CAS. Moreover, when NGOs were provided with a part of the CAS matrix, they were told by the Bank that it is ”nonpublic” and ”not for further dissemination and discussion”.
- NGOs were not provided with the names of the World Bank representatives, who were involved in the preparation of different sectors, the CAS as a whole or how to communicate with them.
- In addition, there was no communication between NGOs and the government about the CAS and their position on concrete sectors or projects.
- Except for one attempt to coordinate activities with one of the main trade unions, there was no communication between the stakeholders, aside from the World Bank and the government.

After the second meeting with Mr. Lay, Bankwatch was provided with a segment of the proposed matrix for the CAS. The NGO was also informed, however, that, ”first, this is only a discussion draft, and not final, so that it may undergo certain changes; and, second, it is nonpublic- for the purpose of soliciting World Bank- CEE Bankwatch Network views, and not for further dissemination or discussion". This is another example of how a possible discussion between all the stakeholders was impeded.

The meetings with Mr. Moose on energy issues were also not based on any documented proposal, except for the last meeting where we received part of the proposed CAS matrix.

For the first time ever, the CAS for Bulgaria was made public. It was placed on the web page of the Bank's Sofia representative office and everyone could read or download it (though only in English). Another document that was made available to the public (both in English and in Bulgarian) was the report, "Joint World Bank- Bulgaria review of the projects." We encourage the Bank to continue with this practice and to publish also other important documents, such as sectoral analyses, review documents, Project Appraisal Documents for projects, environmental studies, etc.

There are number of weaknesses that were identified after carefully reading the Bulgarian CAS. It would have been possible to avoid at least some of them if an open and formally structured debate on the document had been carry out by the World Bank.

There are three mistakes, which resulted in these weaknesses. First, the Bank had the right analysis of the sector or problem, but the proposed actions and conditions for the government were not in favor of positive results. Second, Bank made the wrong conclusions in many cases, then led to the solutions. Finally, there were areas/sectors in which there is a need for action, but for whatever reasons, no action or support were proposed by the Bank. Some of these mistakes can be avoided in the next CAS if a broad number of interested organizations, institutions and experts are properly consulted.

Bulgarian environmental NGOs, both in letters and in verbal communication, had mentioned many of the below listed problems. Though having no document (an annex or a chapter in the CAS) describing whether our concerns had been taken into account, we could conclude that the Bank staff seriously considered very few of the proposals that the NGOs made.

- The main objective of the CAS is, ”to foster sustainable economic growth by accelerating structural reform and the rapid development of the private sector, while addressing poverty through improvements to the social safety net and other social sector programs” (p. 12). Nowhere in the CAS is it mentioned that sustainable development, in its much broader sense, is an objective for the Bank in Bulgaria. This fact narrows the focus of the Bank operations, both in direct financing and technical assistance. It also turns the Bank’s operations in the country away from the direction in which it should go.

- As one approach to meet its objectives, the Bank wrote that it must (p. 13): ”Deepen and broaden our international and domestic partnerships, in particular, with private foundations and NGOs.” As for the private foundations, perhaps the Bank had good cooperation with the Open Society (Soros) Foundation, as it is mentioned, but the communication and meetings between the Bank staff and Bulgarian NGOs couldn’t be named a ”partnership” in the preparation and revision of the CAS. The appropriate word in this case might be ”meetings”.

- Another signal that the Bank’s ”partnership” approach would be very different from a legitimate partnership is Annex B4 of the CAS. The non-lending services, which the Bank provides to Bulgaria, are listed there. Only three out of the 17 documents/activities that are included in the list were subjected to public debate. While 11 out of 15 were disseminated to the public after their completion. At this point, on the web page of the Bank's Sofia office, only three of these documents (CAS, Agriculture Sector Policy Notes and an Executive Summary of "Bulgaria: Poverty During the Transition"), plus one PAD, could be found.

- The triggers for a high-case scenario are mainly from the financial and macroeconomic sectors. Those from the agriculture sector are oriented towards the sector full liberalization. The triggers concerning social issues are only from the legislative part of the social sector. The main triggers are in connection with structural adjustment programs and there are almost no triggers for sectoral and environmental policies. Additional bad news is that in the middle case scenario, the Bank, "would not envisage support in areas such as district heating and agricultural marketing" (p. 18).

- One of the main focuses of the Bank assistance is "promoting structural reform and private sector development". Though reforms are needed, the problem is that the Bank is mainly focused on full liberalization and the liquidation or isolation of enterprises with bad economic performance (generating loses). The Bank is doing little or nothing to promote alternative jobs based on more efficiency, competitiveness and sustainability. The programs for social sector and structural adjustment lending are far from what the country primarily needs. What is missing is a comprehensive program, which would support the restructuring of the economy, including alternative job creation. The proposed approach for the support of social funds (pension fund and health-care reform), for example, is quite positive, but according to independent experts, it does not address the areas of primary importance. People need jobs which will generate more stable money flows, both to pension and health-care funds, instead of loans to these funds which should be paid back by the state budget.

- The energy sector strategy of the Bank: There were many important questions that NGOs have raised and would like to discuss with the Bank as well as with other involved parties. Since it was not possible to have such formal consultations, many problems have been left without proper solution. Among them are a lack of support for the measures in the governmental program ”Bulgaria 2001”; urgent support to tackle nuclear safety issues such as the closing down of dangerous nuclear units 1-4 in Kozloduy NPP. So far the Bank has done little or nothing in support of the rehabilitation of non-nuclear capacities and energy efficiency and conservation. Although an action plan for the restructuring of the energy sector is stipulated by the Bank, the public is not informed about the plans. The Bank does nothing to break the information curtain on energy issues that is practiced by the Bulgarian authorities. Thus, the Bank doesn’t follow its own policies on information disclosure.

- To date, the IFC has not fulfilled its goal to take a leading position in private power generation. Moreover, in the upcoming cases of possible involvement (TPPs in ”Maritza East”), IFC has also kept silent about concrete involvement and how the environmental and social issues will be incorporated into the concrete operations.

- Transport sector: The Bank declares that, ”one area where we plan to disengage once ongoing Bank-financed activities are completed is infrastructure, including railways, telecommunications and water supplies." The Bank's involvement in the Railway Rehabilitation Project is an example for such an approach, which leads towards unsustainability in the transport sector. The railway project is going on badly, although rails are more environmentally friendly than other means of transport. This project demonstrates the closing-down of destinations, the decreasing of railway traffic, the decreasing of additional works (such as the construction of wagons), etc. This is an indirect support for road transport and the construction of highways, which is a main priority for the Bulgarian government.

- In agribusiness, the main condition for Bank support is the full liberalization of the sector including export and import of goods and products, which will put local production in unfair competition against highly subsidized foreign goods. The envisaged support for agri-industrial projects by IFC is also a very debatable goal, with a lot of experts and NGOs opposing this plan.

- The indicators for reviewing the goals of the development and the implementation progress are mainly technical, financial and logistic issues. There are no indicators that could measure sustainability of the project, promotion of sustainable development on the sectoral and national level, social stability, environmental protection, or support for the local economy and employment. In addition, only Bank staff, the employees of PMUs of the projects and high level governmental officials were involved in the assessment of the Bank operations.

The Country Assistance Strategy for Poland

Consultations on the Polish CAS took place in March 1997. It was one of the first WB CAS consultations to occur, and the first in the CEE region. The consultation was conducted in the form of a half-day meeting organized by the World Bank Local Office at its headquarters in Warsaw. The invitation had been distributed approximately two weeks prior to the meeting, and contained, apart from the invitation itself, working materials for the discussion. It was not a draft of the CAS, but rather a description of issues for discussion.

At that time, because of the work of the NGO Liaison[2], the Bank already had an address list of NGOs (both environmental and social) with whom it had regular interactions. Ten representatives of environmental NGOs were invited, including from groups such as the Polish Ecological Club, the CEE Bankwatch Network and the Institute for Sustainable Development. Participants at the consultations represented different areas of the public sphere, such as environmental and social NGOs, academia and business. All the participants were divided into groups addressing topics such as the environment, social issues or business. One of the disadvantages of such a set-up was the fact that there were no interactions between the groups, who were sometimes not even aware that the consultations were conducted in parallel with different stakeholders.

The meeting allowed participants to express their main concerns related to investments, changes in the economy, environment and the role of the World Bank in Poland. There was, however, no clarity about how such concerns will be addressed by the Bank and how they will be reflected in the

[2] The position of the NGO Liaison was launched at the Warsaw WB office in the fall 1996, and the person in charged was Mr. Jacek Wojciechowicz.

CAS document. As mentioned above, because of the fact that these consultations were the first in the region, both parties seemed not to have a clear idea of how the process should look and what they could really expect from it.

The CAS was finished and approved at the very beginning of May 1997. No draft was released prior to approval and no further meetings were conducted. The final document after approval remained confidential, so there was no chance to verify how much of the NGOs' input was really addressed in it.

The situation changed in May 1997 when the Bank President, Mr. James Wolfesohn, visited Poland, just after the approval of the new CAS. President Wolfesohn also met briefly with Polish NGOs. Fourteen representatives from different organizations (environmental, social, gender and human rights) were invited for a working breakfast in Krakow. During the meeting, CEE Bankwatch demanded that the CAS be made public so that NGOs could see how their concerns were addressed. Also, they discussed access to information in a broader sense, as well as translation of documents into national languages. The President’s response was that the Bank had no problem to release the CAS document, but approval had to come also from the Polish government. NGOs asked the Bank to officially address the Polish government with this question.

One month later, an English version of the Polish CAS was officially released, followed by a Polish translation of the document shortly thereafter. It was a precedent-setting situation, as the Polish CAS was one of the first to be officially released. A short description of the process was prepared by Bankwatch and distributed by the Bank Information Center to different NGOs all over the word. The Polish precedent was used by Mozambique groups, among others, demanding more openness in the CAS consultation process and the official release of the CAS in Mozambique.

Obstacles and Shortcomings of the Process

- A lack of clarity about the process: there was lack of clarity on both sides regarding, what NGOs should and could expect from the process and how it would look. The idea of broader consultations on the CAS was new to Polish NGOs, but probably also relatively new to the Bank staff itself.

Other related problems:
- no interaction between the different groups consulted;
- no clear rules on addressing different opinions and concerns;
- the whole process was limited to one meeting only, without opportunities to comment on a draft;
- no rule existed on the release of the CAS document afterwards (it seems that the releasing of the CAS at that particular moment happened, to a large extent, because the demand was addressed directly to President Wolfensohn); and
- there was not enough capacity of the NGO’s to utilize the exercise better.

Conclusions

The experiences with the World Bank’s CAS from the CEE region highlight several issues which must be addressed if effective public consultations are to occur. Drawing from already existing documents on this topic, as well as from regional experiences, the CEE Bankwatch Network proposes the following suggestions for NGOs and for the World Bank.

Recommendations for NGOs

- Send the Bank an updated list of NGOs that might want to participate in the CAS development (if such a list exists).
- Attempt to build the capacity of local NGOs to address issues related to the World Bank and its CAS (i.e. send out documents describing what is a CAS, why it is important to participate and develop and circulate an analysis of how the previous CAS was implemented, or if not possible, circulate case studies from other countries), which will hopefully help to build a coalition of NGOs willing to participate in the CAS development.
- If possible, attempt to inform and influence the Bank's ESW during its preparation.
- Compile the recommendations of NGOs for the CAS into a written document and submit it to the Bank as early as possible in the CAS process.
- Ensure that the CAS consultations focus on the CAS framework itself, and not on the implementation of the CAS.
- Recommend to Bank staff that they read the Bank's own publication, "Civil Society Participation in World Bank Country Assistance Strategies - Lessons from Experience, FY97-98" by John D. Clark and Winona Dorschel, April, 1998.
- Monitor how the Bank conducts the public consultations and publicize the results.
- Ensure that the below listed recommendations are adhered to by the Bank.

Recommendations for the World Bank

- There should be a formal procedure for public consultation that is agreed to by all interested stakeholders.
- There should be a clear structure of the consultation process publicly announced at the very early stages of the CAS development. This should include:
    - Who will participate in the consultations;
    - How will participants be selected;
    - What will be the objectives of the consultations;
    - How will interaction between participants be facilitated and encouraged;
    - How can participants address the other's input;
    - How many meetings are planned, when and where will they occur and what will be the topics for discussion at each meeting;
    - What are the important or relevant documents to be used for the CAS development; and
    - What are the expected outputs of the consultations.

- Important and relevant documents used for the CAS development, including (but not limited to) the ESW and the draft CAS, should be made public in local languages as early in the CAS process as possible and at least one month in advance of consultations intended to address such documents.
- Civil society should have the opportunity to participate in the development of the ESW.
- Consultation meetings should be facilitated by an external professional.
- Civil society should have the opportunity to give comments directly to the World Bank teams that work on the CAS development.

- Consultations should also be extended outside the capital city.
- There should be an open round table discussion on the draft CAS prior to its submission to the Bank's Board for approval.
- All of the comments and suggestions of civil society should clearly be reflected in the final CAS (e.g. in the text, an annex or a box) along with an explanation of the reasons why certain suggestions were rejected.
- It should be mandatory that the final CAS be made public in all borrowing countries.
- The above recommendations should be formulated into a public consultation policy for the CAS, with the participation of civil society, and made legally binding, enforceable and publicly available.

It should be noted that the World Bank is the one of the world's largest and most powerful bureaucracies. Attempts by the Bank to shift blame to governments for not wanting an open and transparent process, or by making statements that effective consultations are difficult and thus require time and patience for the development of institutional capacity, should be confronted. The Bank does not hesitate to make strong demands of governments on economic matters and the speed at which it pursues projects and governmental policy changes is in sharp contrast with the time it supposedly needs to develop consultative capacities. Rather, it seems that the Bank's biggest problem in implementing effective public consultations is the priority level with which it assigns such a task.

11.

Bypass through the Environment

Project Description

The project Roads II has been discussed since 1994, after the first Project Information Document (PID) was released. The project Roads II was to continue activities initiated under the Roads I project.

The main objective of the project was to support and speed up the modernization of roads. The aim was to:

- improve the high priority National Road Network;
- assess and solve the rutting situation of the Network;
- promote the competitive capacity of domestic contractors through improvement of their technical, managerial, and financial capacity;
- improve the road safety; and
- provide assistance in operation, management, and administration of road safety and its coordination with the National Police.

The project was to cover three main areas - policy, institutions and infrastructure.

Policy

- maintain and strengthen high priority roads, including bridges, with an emphasis on winter maintenance;
- review and adjust road user charge level and distribution between different user groups in order to achieve a reasonable balance between costs and revenues;
- continue action on the road axle-load policy, initiated under the Road I project; and
- establish a leasing policy to enhance and speed up privatization of local contractors.

Institutions

- further restructuring, privatization, and development of the road contracting industry, focusing on the improvement of its managerial, financial and technical capacity, and on establishment of professional associations to enhance their competitiveness;
- improvement of the co-ordination, collaboration and operation of different transport agencies on the ongoing road safety program; and
- assistance to the vehicle inspection center networks as a part of road safety and environmental measures.

Physical infrastructure

- rehabilitation, upgrading, realignment, and resurfacing of priority roads sections and their crossings through cities;
- emergency reconstruction and upgrading of three bridges, and construction of three new major bridges;
- construction of 16 bypasses around congested cities;
- acquisition of road maintenance equipment, vehicles and materials and road safety equipment, vehicles and materials; and
- technical assistance and training for the ongoing road safety program, in the fields of management, planning, pavement and maintenance systems, protection of the environment, modern design and construction techniques, and further privatization of local consultants and contractors.

During the project preparation, in summer 1997 a big flood on the Odra River caused major damages in transport infrastructure in the western part of Poland. Therefore one of the added components of the project was post-flood reconstruction.

The project is based on 1996-2002 investment program of Polish National Roads Directorate and was going to be implemented by the Directorate in the period 1998-2002. At the beginning the project was categorized as B. Because of including of construction of new bypasses, category was changed later on into A. The project was approved in 1998 at the amount USD 300 million. The planned date of finishing the project is December 31, 2002 with a closing loan date of June 30, 2003.

Project Implementation – the Piaski Bypass

Construction of the Piaski bypass is the World Bank's third investment in Lublin Voivodship, (the first one being the bridge in Pu³awy and the second one the modernisation of Kurow-Garbow road). The aim of the investment is to build a bypass of Piaski city (Lublin Voivodship) in the course of the national roads NR.17 Warsaw - Lublin-Piaski-Zamosc-boundary of state and NR. 82 Lublin-Piaski-Che³m-Berdyszcze- boundary of state.

The project involves building a ring road section approximately 3770 km long with the investment of USD 5.52 million. The construction of the bypass has significant impact on the city of Piaski. The international road crosses the city and splits into two directions one going to Zamosc and the Ukraine border and the other to Chelm and the Belarus border. Citizens are affected by intensive transit traffic. The intensity of the main transit road is registered as 12000 vpd, which creates significant communication difficulties, extremely high noise, air pollution, and large numbers of accidents.

The suitable legislative activities were done during the preparation phase: Community of Piaski resolution about the investment in the spatial plan (1988) and Environmental Impact Assessment (1998). At present, the project is focused on its technical and geometric aspects. Starting from the beginning of 2001 the suitable grounds for the investment will be bought out from the existing owners. After permission for building is obtained, the last phase of the construction will start. According to project plans, the investment will be closed till the end of 2002.

Environmental Profile of the Investment

The planned area of investment is within the Swidnik plateau (individual NR. 343.16 according to Kondracki 1994) in the vicinity of the border of the Gie³czewska upland (individual NR. 343.17). The planned ring road, crossing the valleys of Gie³czew and Sierotka rivers would run by protected areas. With the urging of NGOs and support of the Agriculture Commission, on November 23, 1993, the community of Piaski passed resolution NR. XXXIII /184/93 from 23 XI 1993 to protect the most precious nature and landscape values of part of the Gie³czew river valley and Sierotka River, together with adjacent grounds. The Gie³czew River is an ecological corridor important for sustaining the Lublin Voivodship's ecosystems, which are part of the Ecological System of Protected Areas (ESPA). Additionally, the ecological corridor of Gie³czew River unites the areas of Krzczonowski and Nadwieprzanski Landscape Park. Splitting the corridor, thus causing harmful effects to the environment and species will cut these important ecological systems. Furthermore, it is not in accordance with the international agreements ratified by Poland (Convention on Biodiversity, Agenda 21, Bern Convention on Protection of European wild fauna and flora species and their of natural habitats, European Ecological Network EECONET). The valleys of Sierotka and Gielczew are rich with avifauna such as *Acrocephallus palustris, Acrocephallus arundinaceus, Podiceps ruficolis, Anas querquedula, Aythya ferina, Charadrius dubius,Carpodacus rhodachlamys* and numerous protected amphibians such as*:* *Bombina bombina, Bufo bufo, Hyla arborea*.

Environmental Aspects of the Investment

The biggest arguments have arisen about the valleys of Gielczew and Sierotka River because of fishpond complexes. The main concerns are the following:

- water flow in the valleys will be disturbed by the diversion of water to the fishponds. This will disrupt the existing drainage system and the peat bogs layers;
- reduction of the fish pond acreage, as well as meadows and pastures located in the valleys, which is an ecological use land and habitats of the avifauna and the amphibians;
- reduction of specific landscape values formed along the Gielczew river; and
- adverse effect on the population of Brzeziczki village, which is located in the area of the projected bypass.

The largest concerns are related to the route of the bypass that goes through the embankments of the rivers valleys (km 169+800, 170+750). This will cause irrevocable damage to various plant assemblages and to habitats of various animal species living in the valleys. These unique ecosystems and the ecological corridor of the Gielczew valley will be seriously disturbed. Additionally, tourism of the surrounding Piaski will be negatively impacted.

Public Participation

The bypass project aroused considerable public attention both opposing and supporting the investment. In 1988, the Municipality of Piaski passed a resolution approving the route of the bypass that will cross precious nature areas, and therefore damage the unique ecosystems of the Gielczew and Sierotka valleys. After the project approval a local NGO, the Ecological UNESCO Club Workshop for Biodiversity, started to promote the values of the area and called for its protection. Finally, with the support of the Ministry of Environment, the Club drafted a proposal calling for legal protection of the area. The Club's aim to protect these areas was successfully finished by the Community of Piaski resolution (1993) protecting the valleys of Gielczew and Sierotka rivers.

This resolution was a crucial point for performing the Environmental Impact Assessment (EIA) for the Piaski in 1998. Because of the natural values of both areas and the results of the EIA, the original project developed by the General Directorate of Public Roads (GDDP) was not accepted. According to the EIA findings, the GDDP decided to cancel “difficult, ecological” part of the bypass because of its high cost for the flyover construction. Although the possibility of getting funds for the flyover is very low, even half of the planned construction would bring significant relief for the most urbanised part of Piaski. This compromise is also accepted by the local society deeply involved in the process from the early stage. The inhabitants of Piaski effectively blocked the investment of the bypass in the 80’s, at the very beginning of this venture. At that time they were afraid of losing incomes from the transit trade and the damage that could be done to their arable land. However, after the rapid traffic increase, inhabitants established a Social Committee in 1995 to speed up the construction of the bypass in order to redirect the traffic from the city. Determination of the Piaski Social Committee accelerated the decision to build the bypass by putting it on the GDDP priority list.

Project Problems

Since transport projects have a great impact on the environment, several concerns have arisen:

- concerns about the PID at the beginning of the project preparation;
- concerns over the unclear status of the project category (B at the beginning);
- fears that the money can be used for highways constructions;
- anticipated problems connected with constructions of new bypasses; and
- NGOs desire to be involved in the project from the beginning to have bigger influence on it.

NGO Involvement

The Polish Ecological Club - PEC (CEE Bankwatch Network member in Poland) was involved in the project from its early stage. Special concerns were about the part of the project that included new constructions such as bypasses and bridges. The activities started with Bankwatch's Polish representative, Magda Stoczkiewicz’s visit to the World Bank Headquarters in Washington D.C in the fall 1996. The meeting with the Project Task Manager, Mr. Luis F. Revuelta, Principal Transport Engineer, when the project was at its early stage enabled further contacts and NGOs' involvement.

The next step was an invitation to the PEC for a meeting with the Bank's field mission and Polish Task Manager, Mr. Marek Rolla (Ministry of Transport/General Directorate of Roads). Besides Mr. Revuelta, other World Bank and NGO representatives joined the meeting. The aim of the meeting was to share concerns about the project, to set up the way in which NGOs should be involved and to clarify pending questions about the project. The issue of the project category was also discussed. NGOs explicitly demanded A category for the project because of the construction of new bypasses and bridges. During the meeting, NGOs demanded to put theirs comments on the proposed Terms of Reference for the EIA of planned new construction.

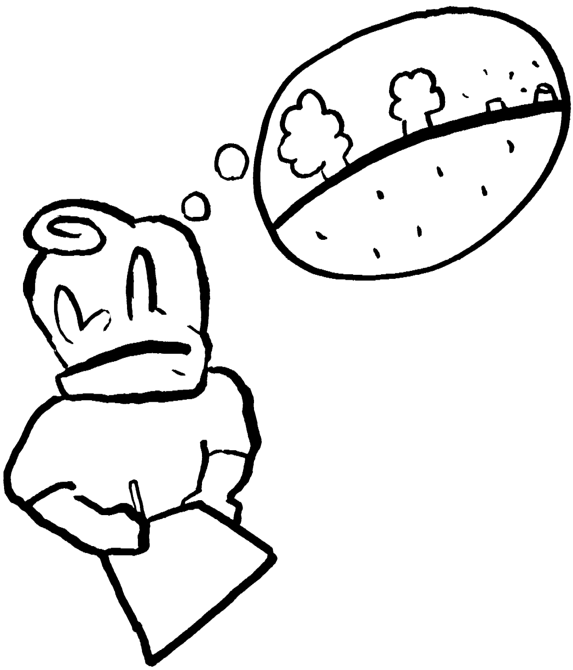
The PEC has also expressed disagreement over the PID. Shortly after the meeting, PEC prepared letters concerning the PID for Mr. Revuelta and Mr. Jean Daniel Gerber, World Bank Executive Director for Poland. This letter stated the PID contained inaccuracies that have given misleading information on the situation of transport in Poland. The PID is a working document, but as stated in the letter to Mr. Gerber: “Because the PID reflects the World Bank's approach to the country and its particular problems we believe it is crucial for the Bank to be fully informed and to have an impartial view of the situation”. The Bank forwarded the letter to the Polish Ministry of Finance and the Ministry of Transport and the PID was changed shortly after that.

Subsequently, NGOs were involved in commenting on the Terms of Reference (TOR) for the consultants. They were provided with a draft of TOR and given time (relatively short) for commenting. Their comments were prepared and sent to the Bank in written form. Furthermore, a meeting with the Bank field mission was organized to discuss that specific topic.

The recommendations started with more general comments on the legal status of the TOR. According to Polish law at that time, a full EIA was needed for highways. However, after the planning of the new constructions, NGOs demanded a full EIA. They also mentioned that EIAs for new bypasses should include traffic calming measures and construction of bike-paths along roads and streets in towns. This would decrease the growing traffic on both a bypass and in-town roads. They also demanded that clear European criteria should be used for assessing the impact on the environment of newly built bypasses.

The recommendations continued with more detailed comments related to the actual text. NGOs especially underlined a need for good public participation. In addition, Terms of References should contain detailed information about the process (number of meetings, type of the meetings, availability of information, methods used). Another strong point was that alternatives should be taken into account, including the alternative "0" (no building).

NGOs involvement has finished at that level because of the insufficient capacities and resources to continue monitoring of the project implementation in different cities. However, the Bank and NGOs cooperated from the early stages of the project. Moreover, a significant factor has been the Ministry of Transport's recognizing the importance of NGOs involvement in the project.



12.

IFC in Slovakia: What Stinks?

The case of a proposed loan from the International Finance Corporation (IFC) to the Severoslovenske Celulozky a Papierne (Northern Slovakia Pulp and Paper, or SCP) company in Ruzomberok, Slovakia, is an illustrative one. Though the loan to SCP was never realized, the case demonstrates IFC's incompetence in assessing the environmental conditions surrounding its projects, the weak practical application of IFC's information disclosure policy and the international criticism against the World Bank Group of selecting projects without adequately understanding the impact they will have on the local community. What follows are a description of the project, the problems associated with it and the action taken by citizen's groups, which is then followed by CEE Bankwatch's conclusion.

Introduction

The IFC, in early 1999, proposed a loan worth approximately USD 41 million (about half of which would be raised from among commercial bank participants in a syndicated loan) for SCP. The loan would contribute to SCP's USD 51 million modernization project. SCP, among the ten largest exporters in the Slovak Republic, which employs around 4 000 people and produces mostly uncoated woodfree paper as well as kraft and tissue papers and related products.

The main aims of the loan were the following:

- to upgrade existing operations (e.g. increase wood handling capacity, investments in a bleaching plant);
- to improve environmental control (e.g. up-grade wastewater treatment, investment in a lime kiln that would decrease certain emissions);
- to refinance existing short- and medium- term debt; and

- to provide SCP with working capital.

Approximately two thirds of IFC funds would have been used for loan restructuring while the additional one third would have been used for technological up-grades. The loan would have assisted the on-going capacity expansions and, according to IFC, would have allowed SCP to increase production capacity to approximately 200 000 tonnes of pulp annually (t.p.a.) for pulp, and over 300 000 t.p.a. for paper by the year 2000.

The project was given a category B, meaning that there would be an environmental assessment and a desk review of environmental and social information in addition to a possible site visit by someone from the Environmental Division. Under category B, the procedures of (in most cases) public consultations and an environmental impact assessment and action plan, which are present for category A projects, do not occur. Finally, the SCP plant had already switched to Elemental-Chlorine-Free bleaching and had already acquired some environmental technologies for stack emissions.

Problem

Upon subsequent review of IFC's Environmental Review Summary (ERS) associated with this project, it was discovered that a number of mistakes were made in terms of the assessment process, which might have been avoided if the project had been assigned with the Category A. There was also inadequate consideration on behalf of the IFC to reduce the foul odor emissions from the SCP plant. In fact, the foul odor was expected to worsen as a result of the increased production capacity of the plant. Furthermore, it was discovered that the SCP plant violated numerous Slovak emission laws and misleads the public, the Slovak authorities and possibly also the IFC about its emission levels.

In assessing the project, SCP and IFC did not consider the poor conditions in the Ruzomberok vicinity for the dispersion of stack emissions. They did not evaluate the climatic and geomorphologic situation, the weak winds, inversions and fogs. These are factors, which influence the dispersion of emissions into the environment and add to the level (often critically) of foul smelling substances in the air. The ERS also ignored the proximity of inhabited areas of the city and villages and did not in anyway evaluate the impact of the project (especially the increase of pulp production) on the air quality in regards to the specific conditions of Ruzomberok. It also ignores the fact that, despite the pulp factory being projected for (and therefore its capacity limited to) the production of a maximum of 200 000 t.p.a. in 1997 it had already exceeded this amount by 6 500 tonnes and in 1998 by nearly 16 000 tonnes.

Climatic Conditions of Ruzomberok and the Region

Climatic conditions of Ruzomberok and the region are substantially influenced by the geomorphology of the terrain relief. Ruzomberok is situated in the western part of the Liptov valley, which is surrounded on three sides by high mountains. In addition, there are infrequent winds of mostly low speed resulting in the high occurrence of windless weather. Reduced dispersion of emissions discharged or leaked into the air is also the result of a ground inversion layer of air. In this stable and cold air mass, the natural mixing and exchange of air is eliminated. Furthermore, the affected area is prone to the formation of fogs, which trap pollutants. Fog formation is enhanced by the proximity of the reservoir “Liptovska Mara”, especially during autumn before the water surface is frozen and large amounts of "unusable" excess heat in the form of water vapor is discharged from the technological equipment of SCP.

Under the improper dispersion conditions mentioned above, advective[1] and convective[2] exchange of the air occurs less frequently and therefore the level of harmful substances, emitted from smokestacks into the air, becomes more concentrated. Highest concentrations of pollutants in the air are the most probable when at the same time some of the following meteorological factors influencing their dispersion occur:

- duration of an anti-cyclone situation, which means the occurrence of high atmospheric pressure, which is a condition for flow-down air movements preventing the dispersion of emissions from ground layers to the higher atmosphere;
- occurrence of temperature inversion, under which stable atmospheric layers are supported, preventing any mixing and air exchange;
- occurrence of windless weather, under which there is no air exchange and therefore the density of air pollution is increasing;
- occurrence of weak air movement with an average speed of one to two m/s, blowing from the smoke stacks to inhabited areas, under which emissions can be transported to inhabited areas;
- occurrence of fogs, under which pollutants are caught and chemical reactions occur in the humid atmosphere; and
- occurrence of long-term dry and warm weather periods lasting 15 or more days, under which the washing out of

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[1] advection - horizontal movement, transfer of air masses
[2] convection - ordered transfer of the air and of the humidity of the air in the vertical direction caused by uneven heating of the ground surface

> dust and harmful substances from the air due to rainfall does not occur.

An increase of the capacity of production under these improper conditions would be possible only if there were a decrease in the current level of concentration of foul smelling substances to a level which would not bother inhabitants, and a detailed evaluation were conducted of the impacts of further increases in the capacity of production under the specific conditions of the Liptov valley. Neither of these two conditions were met under IFC's proposed loan.

The IFC's ERS was further flawed in stating that, "intensity of odor is relatively low and is comparable to Scandinavian plants of this type". Moreover, according to representatives of IFC, over the previous year SCP had made "significant progress" in emission control and the level of TRS (strong smelling substances containing reduced sulfur) is currently on the lower level of the scale typical for similar plants and comparable with Western European plants. Such proclamations were misleading and inaccurate.

The persistent existence of the strong and uncomfortable odor in Ruzomberok is not a subjective feeling of several individuals, but a generally known fact, confirmed not only by the petitions and complaints of local citizens, but also by statements made by state authorities (including authorities responsible for health protection). Moreover, SCP for a long time has not complied with the limits for odor emitting substances as outlined in a governmental provision, according to which "odor emitting substances cannot be in concentrations creating a nuisance for inhabitants."

Comparison to Scandinavian plants of this type would be possible only if there existed concrete data on the emission and emission levels of a pulp plant in Scandinavia or elsewhere in Western Europe, that has comparable production (200 000 t.p.a.) and is situated in a comparable area, in a valley with poor climate conditions for air dispersion and in the immediate vicinity of permanently inhabited areas, etc. In the immediate vicinity of the SCP pulp plant is situated at least 5 000 inhabitants. In contrast, Scandinavian plants are situated in flatlands, mostly on the shore, sufficiently distant from permanently inhabited areas.

As to the “significant progress” of SCP in the control of emissions of odor producing substances, this is simply false. Measurements of SCP’s emissions show that in 1998 there was a considerable increase of TRS emissions (comparing to 1995-97, emissions increased three to fivw times). Furthermore, by the end of 1995 there was an obvious 100-200 percent increase of average monthly values of emissions of sulfur dehydrate. This increase happened after the introduction of new technologies that were supposed to bring about a decrease in the total amount of emissions of pollutants. According to the plan for the construction of a reduced displacement heating system**,** emissions of the sulfur dioxide and methyl-mercapthane should have been significantly lower, almost to zero values. However, changes in the amounts of emissions of TRS since 1995 is directly the opposite.

The experimental operation of the reduced displacement heating system took place for three and a half years (from the end of 1995, till spring 1999), meanwhile an increase in the emissions of TRS followed. An increase of TRS emissions is acceptable only for a short period of time, but not for many years, as it was in this case.

Especially serious is the contradictory information given by SCP about the increase of the pulp production, which is the largest source of odor emitting substances? In December 1998, representatives of SCP stated for the press that in the year 2000 *they planned to increase production* of pulp to up to 230 000 tonnes annually (though only 200 000 tonns is allowed). However, in March 1999 they contradicted themselves in saying that they were *not planning an increase of pulp production* in the near future, but instead an increase of paper production. Finally, in August 1999, representatives of IFC revealed that the planned investment of IFC *"will contribute to the increase of the production"* of pulp to *200 000 tonnes*.

In March 1999, SCP stated that they had begun the permanent operation of the new technology in the recovery furnace of the pulp. This technology should have caused a significant - almost to zero values - decrease of emissions of organo-sulphur odor emitting substances. On the contrary, in June 1999, SCP used a legal opportunity (according to the existing laws in which a company could choose whether or not to comply with emission standards) not to comply with emission limits before the end of 2006. The original goal of reaching almost zero values was therefore never met.

In addition, the ERS claims that there is no significant site contamination from past SCP activities. However, SCP has in the past contaminated the soil as well as ground and stream water. Several other site contamination resulted from waste leakage, a broken sewage reservoir and a discharge of chemicals into a waste water pipeline shared with the municipality that resulted in the deaths of fish in the nearby river Vah. SCP ultimately paid a relatively large sum of money for the damages. The ERS ignored all of these incidents. Moreover, the ERS never considered a Decree of the Ministry of Environment (No. 112/1993) which declared the

Ruzomberok area as one of the twelve most devastated regions in Slovakia with a terrible health and environmental record, which is mostly the result of SCP production.

Reaction

On March 12, 1999, a small column entitled “Interest in funds” appeared in *Ruzombersky Hlas*, a local newspaper in Ruzomberok, Slovakia. The small column explained that the IFC of the World Bank Group was preparing a loan for the local SCP pulp and paper plant. It went on to say that an Environmental Review Summary (ERS) had been prepared in relation to the project and that it was now available for review at the press office in SCP and at the IFC office in Bratislava.

This column caught the attention of a few local residents who were concerned about the foul odor, which is emitted by the SCP plant. During the following days the concerned residents called the press office of SCP and asked for a copy of the ERS. The official at the press office originally agreed to fax a copy of the ERS to the residents, but later said that the ERS could only be viewed at the press office. The concerned residents, after concluding that this was not adequate, began calling the IFC office in Bratislava to request a copy of the ERS. The secretary at the IFC office said that the program director was not available, but that she had informed him of their request and that the IFC would send them a copy of the ERS. After several phone calls, the ERS still did not arrive. Thus, on April 27, the concerned residents sent a letter to IFC stating that they did not believe the ERS was a secret document despite of recent experiences, and again they requested a copy. In response, on April 30, the residents finally received a copy of the ERS with a letter from the IFC office.

Perhaps IFC's and SCP's reluctance to release the ERS reflects the poor quality of the ERS itself. As described above, a subsequent review of the ERS revealed that the document contained many inaccuracies, ignored several important factors and did not in any way address the foul odor problems affecting the Ruzomberok community. In fact, the IFC loan would have increased production at the SCP plants, which would in turn increase the foul odor emissions.

Due to these inaccuracies and misleading statements, CEE Bankwatch member group Friends of the Earth Slovakia (FoE-Sk), in coordination with the Ruzomberok residents, sent a letter to the IFC Board of Directors on October 12, 1999, asking them to postpone consideration of the loan to SCP and to re-categorize the project as category A, so as to take into account the negative environmental impacts caused by the SCP foul odor emissions. Unfortunately, the Board approved the loan anyway.

Then, two months later on December 10, Ruzomberok residents, together with FoE-Sk, met with IFC officials to discuss their concerns and complaints. During this meeting FoE-Sk outlined the possibility of taking other actions against SCP including legal actions against the company's violations of emission regulations. In response, IFC representatives stated that the IFC could at anytime refuse to provide financing for a project if the recipient of the funds is found to have violated national legislation.

Following the meeting, Ruzomberok residents and FoE-Sk sent a letter to the IFC detailing the concerns and complaints that were presented in the meeting. IFC responded requiring an explanation about the way in which the figures in the letter were calculated. The authors did not feel the need to explain such an issue because the figures were drawn from publicly available information from the regional public authorities and therefore felt that the request was an IFC's delay tactic. In addition, the authors requested IFC to provide a translated version of their letter, but the IFC refused saying that it was not their policy to provide such translations and that in any case they first wanted an explanation for the figures, further delaying the process of dialogue.

Dialogue between the IFC and the authors continued in this light until February 15, 2000, when the IFC confirmed a long existing rumor that they had agreed jointly with the SCP not to continue with the development of the approved IFC loan. For the next two months FoE-Sk tried to obtain information from IFC about the loan cancellation. Finally an IFC official stated that the issue was a matter of business confidentiality and therefore the IFC could not divulge the information.

Conclusion

The case of the IFC loan to Slovakia's SCP illustrates how the IFC is incompetent in assessing the environmental conditions surrounding its projects and how it often does not fully understand the impact of its loans on local communities. The information regarding the climatic conditions in the Liptov valley where SCP is located, as well as the emission levels of the SCP plant are easily obtained from public authorities, especially for someone conducting an environmental review. Instead of commissioning a thorough independent study on the environmental impacts of the project by assigning the project a Category status A, the IFC relied on mediocre research and analysis and on the information provided by SCP, information that it apparently did not check for accuracy. This highlight the flawed practice of the IFC to rely almost entirely on the information provided by the project sponsor. When asked during a meeting why he believed the foul odors were not of significant levels, an IFC official stated that he had visited the project site twice and smelled the air, concluding that it was not as bad as the air he had smelled in Romania or Bulgaria. As a result of such poor and highly questionable research and analysis, the IFC nearly granted a loan to a company that has regularly violated the legal limits for emissions which has contributed to the decline of the environmental integrity of the region to the detriment of the local residents.

In addition, the case illustrates the weak practical application of IFC's information disclosure policy. From the beginning till the end, civil society representatives had difficulty obtaining information from IFC (and SCP) regarding the project. Even though no IFC policies were specifically violated, civil society representatives were continually frustrated by the apparent delay tactics employed by the IFC. At the beginning, local Ruzomberok residents had trouble obtaining the ERS, first from SCP due to their requirement that it only be viewed at their offices, and then by IFC through their late response which came only after a strong letter was sent by the local residents to the IFC project director. At the end, FoE-Sk's attempt to obtain information as to the reason for IFC and SCP's decision not to pursue the project was frustrated by delay tactics, or inadequate responses to the inquiry. After two months, the IFC finally responded citing business confidentiality as the basis for not being able to provide an answer to the inquiry. Unfortunately, the concept of "business confidentiality" is often evoked in private sector projects and it is impossible to prove whether strategic information is at stake, or just the IFC's image. Despite IFC's recent improvements in its information disclosure policy, it still has much to learn in terms of practice.

13.

Wheels in the Economy?

Introduction

The World Bank provided its first loans to Hungary in 1985, when the country was faced with economic crisis. These loans were for the structural adjustment and economic restructuring. Up to present four loans were approved by the Bank, and one of these is still under implementation. The loans from 1985 and 1989 were spent on reorganization of the railway company. The Roads Project from 1993 and the Budapest Urban Transport Project from 1995, approved after the political and economic transition in 1989, were focussed on more environmentally friendly investments such as road and tram track maintenance, modernization of bus fleet and development of information and management systems.

The sector division of the projects contributed greatly to a shift towards road transport, although market development promoted this transition as well. Before the approval, projects were analyzed through several criteria. The economic analysis was to determine the broad impact of the project, but it can be interpreted in many ways highlighting different aspects of the economic impact. The financial analysis should measure the impact of the project on the financial position of the borrower. The cost-recovery refers to the percentage of revenues of the public transport or railway company or the highway authority, that is covered out of user fees.

The weight that is given to these three types of analyses differ in each of the sectors, which results in distortions of funding. The economic rate of return and the cost recovery analysis dominate in the road project assessments, while the financial analysis is a typical criteria for railway and public transport sector lending.

There is a general recognition that transport is one of the fastest growing and least predictable factors responsible for global warming. While the seriousness of future environmental problems is undisputed, the World Bank still targeted 60 percent of its transport sector lending to the road sector and only 10 percent to the rail in 1995.

This study gives a general overview of the transport sector lending to Hungary, pointing out the economic, environmental and social shortcomings of the projects. This study also suggests the ways in which the problem could be addressed. The First and the Second Transport Project will be analyzed together, looking at the modes of transport one-by-one since they are interlinked in their objectives.

First Transport Project

Loan Nr. 2557-HU, USD 30 million out of a total cost of USD 75 million
Project approval 1985
Project completion 1992

This loan provided assistance to the Hungarian State Railways (MÁV), road infrastructure (construction of the first phase of the M0 ring road around Budapest) and the trucking company Hungarocamion. According to the World Bank, "the project achieved its principal objectives, although the railway's financial performance deteriorated (due to substantial traffic losses associated with macroeconomic restructuring and decline of trade within the former CMEA)."[1]

[1] World Bank, 1992, Staff Appraisal Report on Roads Project, pp. 8

Second Transport Project

Loan Nr. 3032-HU, USD 25 mil out of a total cost of USD 95 mil
Project approval 1989
Project completion 1996
Overall weighted ERR 16%

The Second Transport Project was designed as the completion of the First Transport Project by providing follow-up assistance in the same three sectors, and it was extended by a USD 4 million support to the Budapest Transport Company (BKV).

The policy behind the projects was to:

- introduce competitive bidding into road works;
- privatize road maintenance units in part;
- introduce economic analysis into determining road expenditure programs;
- initiate a more commercial approach at railways and urban public transport.

Hungarian State Railways (MÁV)

The first loan to MÁV was mostly spent on track and rolling stock upgrading while the second one was to develop the management system, information technology and to purchase track maintenance equipment. The First Transport Project required a full cost recovery from the company, and the requirements had been increased by the Second Transport Project. The ratios seemed to be attainable up to the radical shift in the Hungarian economic and political system, when the company was confronted with a significant fall in freight rail traffic, losing its revenues compensating for subsidies to passenger transport. MÁV was not able to mitigate its financial troubles by cutting labor costs because of a strong pressure from the unions. Seeking a solution of the crisis, the second World Bank loan was used to prepare a study proposing the radical restructuring of MÁV. For future loans, the adherence to that study was a prerequisite. In consequence of the World Bank recommendations, the previously heavily subsidized company faced a gradual reduction of state subsidies and was forced to rely more and more on its own strength.

Further, the company was advised to sell off all non-economic lines to local governments, to cut wages, and to reduce workforce substantially. The World Bank's recommendations, practically aiming at the commercialization of the company were issued in the Government Decree in 1994, extended with the relief of a debt of HUF 56 billion. However, the effective debt relief was only HUF 31 billion, as MÁV had to take up a new credit of HUF 25 billion. All together, "MÁV's management was both financially and politically unable to comply with many of the World Bank recommendations for restructuring, and felt that some of the assessments about the causes of MÁV's financial troubles were incorrect."[2]

Talks between MÁV and the Bank ended in 1989 when the government, to show quick improvement, made MÁV purchase modern rolling stock which was not need. In 1995, talks were initiated again with the Bank's requirement to reduce subsidies to MÁV from 1.7 to 0.6 percent.[3]

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[2] W. Hook: Wheels..., pp. 18
[3] W. Hook: Wheels..., pp. 18

Economic and social impact

The loan did not help to overcome MÁV's financial problems. By contrast, the crisis was further deepened in several aspects. The World Bank's recommendations were based on a financial analysis, but they did not consider implicit economic and social effects of the measures. The study of the Hungarian Academy of Science revealed that deficit is not attributable to the secondary lines So the closure or selling of these lines did not balance the budget and above that, it heavily affected the populations of those areas. As access to settlements becomes more difficult, areas cut off from rail service lose their population which leads to a growing centralization of the country with a widening gap between regions.

The reduction of the subsidy required by the Bank was too high. Subsidies to the rail transport were reduced from 1.7 percent to 0.6 percent of GNP. However, to meet the level of private cars' subsidies, a reduction to 1.6 percent of GNP would have been sufficient, based on 1996 figures.

To make MÁV more viable, the management is trying to reconstruct the company by laying off personal, transferring welfare institutions (hospitals, nurseries etc.) of its budget onto the national budget and closing lines. Thus the management, although it does not strictly follow the World Bank's recommendations, is faced with strong pressures from trade unions.

Environmental impact

MÁV urgently needs funding for infrastructure maintenance. When considering subsidies and the allocation of resources, the following advantages of railways should be considered:[4]

[4] National Transport Study Hungary, 1997, pp. 53

- total toxic emissions are far below in comparison with the road transport;
- construction of one kilometer of a dual three-lane motorway costs about four times as much as the construction of one kilometer of a two-track railway;
- capacity of the railway can be increased significantly by upgrading and modernizing existing lines, while the expenses for improving road capacities are much higher. In addition, the road traffic has a more destructive impact on the environment;
- railway tracks need repairs every 20 years, while the transit motorways need upgrading every 10 to 12 years, and
- according to MÁV, even current railway tracks would be suitable for transportation of all freight.

One of the main factors in MÁV's difficulties is attributable to the rapid shift to private car traffic. By reducing subsidies to railway transport, this tendency would be enhanced, leading to a faster deterioration of the environment.

Road transport

While in other sectors the First Transport Project focussed on the rehabilitation of existing facilities. In the road sector, the priority was given to the construction the first section of the M0 Ring Road around Budapest.

The Second Transport Loan funded the second section of the M0 bypass, as well as the purchase of some equipment and the provision of management and engineering supervision.

Economic impact

Both the First and the Second Transport Project were approved without assessing its financial impact on the borrowing government. None of the Staff Appraisal Reports includes a side agreement that would assure that users of the road would bear the costs of the construction and the maintenance of the new infrastructure. This is a severe default of the projects, because the revenues were not guaranteed.

Environmental impact

The environmental damage was severe in attempt to divert transit traffic from Budapest. This includes construction of a bridge without a proper EIA, and considerable land acquisition needed for the new road.

Social impact

Although the new M0 road serves the purpose of a highway, it is not supplied with the separating safety barrier in the middle of the road.

Recommendations[5]

A comprehensive financial analysis, which includes cost and benefits of the borrower too should be carried out. Land acquisition costs should be added to the project costs, along with the loss of tax revenues from the acquired land. Environmental externalities should be included in the financial analysis only when they have a direct impact on expenditures in other sectors. The financial analysis should also include costs for local governments and the costs for road rehabilitation and maintenance.

[5] W. Hook: Wheels..., pp. 39

Government revenues rise by imposing tolls on highways' users such as gasoline taxes, vehicle registration fees and other charges. In addition, a new road generates new traffic, but this tendency reduces the use of public transport and rail, which means further deterioration of the environment.

Hungarocamion and BKV

Roads Project
Loan Nr. 3549-HU, USD 90.4 mil out of a total cost of USD 161.1 mil
Project proposal 1992
Project approval 1993
Implementation deadline 31st Dec 1996
ERR 20 %
Environmental impact rating: category B

The latest road project financed by the World Bank represents a new approach of the Bank towards investments in roads since the project financed maintenance and rehabilitation rather than construction. The principal objectives of the project were to enhance the efficiency of public expenditures on roads by supporting improvements in management, planning and programming techniques and encouraging competitive contracting for road works, to overcome the backlog of road and bridge rehabilitation work and to improve road safety.

The project covered:

- reparation of 10 routes (about 700 km) selected in accordance with their importance, the traffic level and nearby activities;
- improvement of selected bridges;

- purchase of road maintenance and road quality controlling equipment;
- Road Safety Program which includes purchase of road safety equipment, support for stricter enforcement of traffic laws and training and technical assistance and
- Institutional Development Technical Assistance (IDTA) on national and local level.

The Bank provides the loan for 15 years including a grace period of 5 years at the Bank's standard variable rate.

Economic impact

Whit this new approach the financial support to different transport sectors becomes more balanced. However, the fact that the World Bank decided to finance more environmentally friendly projects is mainly attributable to economic concerns. Under the previous loans, the Bank financed the construction of new roads. Although the country performed well in repaying debt, the Bank strongly opposed ambitious capacity expansion project plans of the Hungarian State Railways and the Municipality of Budapest (construction of a new metro line). Concerning the latter case, the Bank argued that the Municipality could not abide by providing the subsidy promised to the Budapest Transport Company and it would get into an even worse financial situation if its budget were burdened by the heavy and inestimable costs of the subway construction.

A serious problem with the project was its basis on a cost benefit analysis and not on a financial analysis, which would determine the effect on the financial status of the borrower. This means that benefits of cost reduction gained by lower fuel consumption of cars accrue to car operators, and the borrowing government suffers a loss of fuel tax, ending with a negative balance. At the same time (in 1992), 78 percent of national road expenditures were covered by road users, and the Road Project counted on a more than 80 percent cost recovery over four years.

The deficit resulting from the above calculations can only be avoided by enforcing the side agreement in which the government commits itself to maintain a system of road user taxation. This measurement is applauded.

This project implies the danger that funding projects are not in line with the Bank's policy. Namely, the World Bank's loan goes into the Road Fund, from which all road investments are financed. If the Bank provides a loan for road maintenance and rehabilitation without taking into consideration that the government is planning investments in highway construction at the same time, the Bank in fact enables the government to carry out even more unsustainable investments from the in-country funds that could have been spent on maintenance. In other words, it is difficult to tell on what are the loans really spent.[6]

The Staff Appraisal Report of the Road Project identifies the following major risks: if the government over-extended its road expenditure plans and if trucking lobby undermined increases in road user fees and taxes. Namely, this would result in a loss of revenues and risk the repayment of the loan. However, risks assumed by the government by providing guarantees to investors are not analyzed in the report.

[6] Walter Hook: Wheels out of Balance, 1996, pp. 22

Environmental impact

As highlighted before, the overall concept of road and bridge rehabilitation instead of construction is applauded from an environmental point of view. As road works are mainly strengthening with a limited widening, negative impacts are considered by the Bank as minor. A favorable environmental effect of the project is reduction of vehicle emissions and the implementation of the Road Safety Program which will decrease the number of accidents.

Concerns arise from the possibility of financing new constructions as indicated among the economic impacts. This implies new land acquisition, enhanced noise level and increase of emissions.

Budapest Urban Transport Project

Loan Nr. 8494-HU, USD 38 mil out of a total cost of USD 67.1 mil
Project proposal 1993
Project approval 1995
Implementation deadline 31st Dec 1999, extended by one more year
ERR 20%
Environmental impact rating: category B

In 1995, the World Bank approved a loan of USD 38 million to the Municipality of Budapest with the objectives of modernizing and increasing the commercial orientation of the Budapest Transport Company (BKV), decreasing subsidies to public transport, contributing to the improvement of air quality in Budapest and establishing a formal contractual relationship between BKV and the Municipality. By this loan, the Bank co-finances the development of public transport in Budapest with EBRD.

The project consists of four main components:

- Replacement of 50 buses out of a fleet of about 1750 buses, 36 percent of which are more than 8 years old, neither fuel-efficient, nor environmentally friendly. New buses will save maintenance costs and cause less air pollution.
- Renewal of 47 km of tram track, mainly on the most frequent routes, and purchase of various types of small equipment to perform the work.
- The second stage consists of the implementation of an automatic vehicle monitoring system (AVM), and provision of on-board equipment for 250 vehicles. (In the first stage, basic infrastructure of the AVM system was set up under the Second Transport Project.)
- Financing the technical assistance; information technology, finance, economics and marketing.

The loan agreement was extended with side agreements requiring the introduction of a restricted parking policy, a service and performance agreement between the Municipality and BKV, the separation of non-core activities by privatization or termination and the introduction of private provision of public transport. A further requirement was that "cost recovery rates should not be lower than 37 percent in 1995, 41 percent in 1996, 43 percent in 1997, 45 percent in 1998, 47 percent in 1999 and 50 percent in 2000"[7] .

[7] World Bank, 1995, Staff Appraisal Report on Budapest Urban Transport Project, pp. 37

Economic impact

Subsidies from the national government and the Municipality were reduced to 50 percent, which is below the level of most Western European countries. The above rate of cost recovery can be realized if revenues are raised from increased user fees, by laying off staff, closing several lines and enhancing effectiveness in fighting fare evasion. However, as ticket prices rise, the number of passengers will decline, which means that the company is forced to further increase fares in order to gain the same income, generating a fall in demand. Modernizing bus fleet and tram tracks well imply savings in operation costs, however, at the expense of a reduction in service level.

BKV got into a financially vague position in the late 1980s, when the first fare increase took place because of economic crisis. Since then, several fare increases followed, while private cars and fuel became more affordable to individuals, which resulted in fall of the public transport use. In 1991, as the City of Budapest became the owner of the Transport Company, the national government reduced finance to the BKV.

Before 1989, subsidies provided by the national government covered all passengers. After 1990, subsidies were sufficient only for compensating the preferential tariffs for pensioners, students and some other social groups. However, the regular rise in tariffs caused an estimated 5 percent loss of passengers between 1991 and 1996[8]. An aggregate decline of 30 percent in public transport trips and a 53 percent increase in car trips between 1991 and 2000 is expected[9].

[8] Walter Hook: Wheels out of Balance, 1996 pp. 14

[9] World Bank, 1995, Staff Appraisal Report on Budapest Urban Transport Project, pp. 32

The growing use of private cars is tried to be slowed down by the side agreement that requires the implementation of a new parking control scheme financed under the EBRD Urban Public Transport Rehabilitation Project loan. This measure practically reduces the subsidy to private car operators in the city center but "does not identify revenue targets for cost recovery in the road sector"[10].

Concerning the economic feasibility of the project, the Bank defines two major risks:

- BKV failure to meet the cost of recovery rate or the operating ratio targets;
- BKV or the Municipality investment in uneconomic project (this is to be avoided by regular consultation with the Bank)[11].

Environmental impact

From an environmental point of view, the project has several benefits. The impact of construction is analyzed carefully, and as a result of the tram track renewal the noise level on the routes has been reduced by 50 percent. The damage caused to buildings by vibration has also decreased.

In Budapest, 50 percent of air pollution and 90 percent of lead emission is attributable to transport, and 10 percent of the total emissions are caused by public transport. This project is expected to contribute to the reduction of carbon monoxide emissions by 20 percent, hydrocarbons and nitrogen oxide emissions by 50 percent and particulate emissions by 75 percent. The combined effect of the World Bank's and EBRD's

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[10] Walter Hook: Wheels out of Balance, 1996, pp. 15
[11] World Bank, 1995, SAR on Bp. Urban Trp Project, pp. 35

urban transport projects should reduce the overall toxic emissions by 2 percent.

A serious shortcoming of the project is its aim to decrease subsidies to public transport. This will increase car traffic, thus causing more damage to the environment. Considering the specific energy use (the cost of energy per passenger) and the specific land use, public transport again cause less damage.

Social impact

Two major social problems arise from the project. Firstly, the implementation of the project implied the lay-off of several thousands of employees. Secondly, the regular fare increases have burdened the low-income population making up the majority of the passengers.

Recommendations

Referring to the study of Walter Hook, BKV would achieve better rates of cost recovery if it gained subsidies from both the national and the municipal government for covering all the costs incurred by offering tickets to certain social groups at preferential tariffs.

BKV provides services beyond the borders of Budapest as well, but outer municipalities do not contribute to BKV's budget. It is crucial to find a solution to this problem, as the maintenance of public transport service to those suburban areas is vital due to their growing population.

If BKV intends to cover all its operating costs out of user fees and spend public subsidies on capital projects, it should consider keeping separate operating and capital budgets.

Conclusion

It is generally recognized within the World Bank that the projects in the different modes of transport sector cannot be evaluated on a consistent and comparable basis. A fixed approval process does not even exist within the same mode of transport. This approach leads to distortions in the structure of financing highlighted below.[12]

The economic rate of return should not be lower than 10 to 12 percent for all projects. However, the ERR analysis does not rely on the evaluation of public transport and rail projects, but on road projects. In these sectors, ERR measure only the costs and benefits of the capital investments without considering the impact of restructuring measures. It is usually ignored that the road sector, taking away traffic from other sectors, may burden the society with real costs by driving up operating costs per passenger in these alternative modes of transport. The above facts reveal that the ERR alone is not sufficient to determine loan viability.

A financial rate of return analysis is predominantly used in the rail and public transport sectors and weigh heavier than the ERR analysis. In the road sector, however, an FRR analysis is almost never performed, although repaired or new roads enable the reduction of fuel consumption which leads to a fall in gasoline tax revenues, thus resulting in a negative FRR, as it happened in the case of the M0 motorway. The loss of revenues should be compensated for by side agreements on tax increases. In general, the importance of the financial rate of return analysis should be enhanced in the road sector.

[12] W. Hook: Wheels…, 1996, pp. 2-9

Rail and public transport projects have a positive FRR, because fuel efficiency strengthens the financial position of the borrowing company in the long run. A balance of subsidies between different modes of transport should also be restored and maintained, and subsidies should be targeted to low-income groups within society.

Side agreements can be used as an effective tool for guaranteeing the viability of the project. For example, the government could assure that highways would not be built in the same corridor where the rail transport is promoted. The government can also cause a delay in the project implementation in a case when a loan has an unrealistic level of cost recovery such as the Budapest Urban Transport Project.

The balance of upgrading and maintenance versus new construction, the relief of the city from transit traffic is pointed out only, with no reference to the environmental damages caused by land acquisition and bridge construction. When assessing the environmental impact of rail and public transport rehabilitation projects, attention should be paid to theirs specific energy and land use requirements that are much lower in comparison with the road traffic.

The deterioration of the natural environment indirectly caused by the reduction of the relative level of subsidies to rail and public transport should not be neglected, either.

Among the social impacts, one of the most serious problem is the significant lay-off required from the rail sector in side agreements. It is also ignored in the analyses that the reduction of subsidies to rail and public transport places a heavy burden on the population, thus target groups of subsidies should be selected carefully.

Western European experience has proved that connecting less developed regions to developed ones does not help developing the poorer region but results just in the opposite - the widening of the gap between the two regions.

We believe that by introducing a practice according to which economic, financial, and other lending criteria extended by a detailed and comprehensive environmental analysis form the basis of the loan viability assessment, the World Bank would comply with its goals of poverty reduction, sustainability and economic restructuring.