CEE bankwatch network

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CEE Bankwatch input for the EBRD transport sector evaluation

Contents:

Introduction

As an economically important sector with various harmful environmental and social impacts, transport is coming under increasing scrutiny due to its rapidly rising volume and corresponding CO2 emissions increases, which are not being, and are not likely to be, sufficiently addressed by technological improvements. We are submitting comments mainly for road construction projects, as these bring with them the most visible problems regarding environmental impact, resettlement and value for money, however we also discuss other modes where we have observations to make. Most comments relate to projects financed during the period of validity of the current Transport Operations Policy, however some were also financed prior to this, but have raised issues which do not appear to have been resolved by subsequent policy changes. Additional comments relate to projects which have not yet been financed by the EBRD but which nevertheless provide important insights and lessons.

Aims of the EBRD's operations in the transport sector

Overall aims:

The EBRD's current Transport Operations Policy lays out a multitude of aims for its investments in the transport sector. Some of these are indeed reasonable, however we feel that there are some areas that have not been given sufficient attention:

Environmental, especially climate impacts of transport: In our opinion the EBRD should

have - and needs to in its forthcoming new policy - **develop objectives to prioritise financing for the most sustainable and least carbon-intensive modes of transport, limit aviation financing to safety improvements and air traffic control and decrease financing for new motorway construction**. The current policy states that environmental issues will be addressed firstly through project appraisal, and secondly through environmentally oriented investment and policy dialogue. However its concrete commitments are limited to including energy efficiency components in projects, supporting enforcement of relevant legislation, encouraging the use of cleaner vehicles, increasing the use of cleaner fuels and biofuels, and promoting environmentally appropriate transport pricing in policy dialogue. (p.43) While these are welcome, it seems unlikely that they would have had as significant an impact as decreasing financing for the most carbon-intensive modes of transport (as the construction of new roads tends to induce additional traffic[1], as, clearly, does the expansion of airport capacity).

Contradictions in environmental pricing policies: We welcome the EBRD's commitment to internalising the external costs of transport, however we still see some unresolved contradictions here. While the EBRD has been active in supporting road user fees, at least for motorways, its stance on reducing state support for rail is likely to have the effect of raising tariffs, and thus not encouraging people to use rail relative to road transport. We would encourage the bank to examine how this could be avoided.

Improving transport policy planning in transition countries: Transport planning, particularly regarding infrastructure construction, is notoriously affected by corruption and special interests in the transition countries, and the resurrection of decades-old projects, as well as less tangible but powerful factors such as the need for political prestige and a perception that public transport is passé. Transport planning will be covered later in the paper, however we believe that the EBRD could more clearly state its aims and outline how it intends to contribute in this area. It is clear that the EBRD already undertakes some policy dialogue work, however it would be useful to see what the exact aims and extent of this are.

Sub-sectoral aims:

"**Road:** The Bank will continue to support rehabilitation, upgrading and construction of new roads, where investment needs have increased in line with economic growth and a move towards greater regional integration. Sovereign transactions are expected to dominate the Bank's activity in this sector, as the economic benefits of roads are difficult to monetise.

However, the Bank will continue to support institutional development, reform of road sector financing and increased commercialisation of the sector. The Bank will also support the involvement of the private sector through PPPs, as governments seek to benefit from private sector efficiencies and increase the number of projects which can be implemented simultaneously. PPPs will not be limited to construction and operation of road infrastructure, but may also cover the provision of services to road users (catering, rest areas etc.). The Bank will support moves to more transparent road changing, addressing the costs associated with this means of transport. In particular the introduction of vignette schemes and electronic road pricing are seen as useful tools to ensure

[1] See for example: Todd Litman: Generated Traffic and Induced Travel - Implications for Transport Planning, 3 February 2009, Victoria Transport Policy Institute

that road vehicles bear an appropriate cost burden." (p.6)

The EBRD needs to lay out more clearly how it will discern which road construction projects are *really* necessary and could not be resolved in another way such as upgrading adjacent rail services, introducing tolls for transit vehicles on the existing road, undertaking improvement works on particular stretches etc. As noted below, decision-makers in transition countries are rather prone to propose the construction of new roads as their main transport development strategy and although the EBRD has procedures in place to screen out those that are not economically viable, with the need to reduce CO2 emissions paramount, the criteria for supporting road projects need to be tightened up further.

The bank is interested in promoting private sector participation as part of its mission to promote market economies. However PPPs in road construction and operation are not an inherent part of a market economy and there is no reason for the EBRD to promote them unless they are found to be consistently superior to publicly procured roads. Road construction anyway has an impact on promoting market-based economic activity, although it should be examined whether this will happen to the extent that many transition state governments expect and whether the kind of development is desirable (eg. generating freight and logistics enterprises that may result in freight moving off of railways and onto roads).

During the period since the current Transport Operational Policy was approved, the EBRD has participated in 5 PPP road projects that we are aware of:

- M6 motorway, Hungary, 2005
- M6 refinancing, Hungary, 2006
- M6-60 motorway, Hungary, 2008
- South West Corridor Road project, 2008
- R1 motorway, Slovakia, 2009

Given that only the M6 was approved more than 1.5 years ago, it may be difficult to fully evaluate the results of the projects, particularly regarding the operational phases. However, to the extent possible, **we encourage the Evaluation Department to look into whether PPP road construction projects have shown superior performance compared to publicly procured ones, whether similar results could have been achieved with publicly procured projects using turnkey contracts and whether sufficient risk was transferred to the private partner in the operational stage to justify the higher costs of private financing.** Further comments on PPP projects are below.

"**Aviation and airports** in many of the Bank's countries of operation airlines are protected under bilateral arrangements. The Bank will support transactions that prepare these airlines for eventual competition. The Bank will also continue to support investment in infrastructure to improve operating efficiency and national and regional safety. This may involve sovereign lending or corporate financing of fully commercialised public entities and airports operated by private concessionaires. Liberalisation of air traffic markets in the new EU Member States will expose the national carriers to greater competition. There may be scope for the Bank to undertake restructuring transactions in these countries to improve the competitiveness of the airlines. There may also be opportunities to support low cost carrier with either equity or debt, subject to satisfactory risk profiles." (p.6)

As mentioned above, due to aviation's high carbon intensity and the fact that it is already

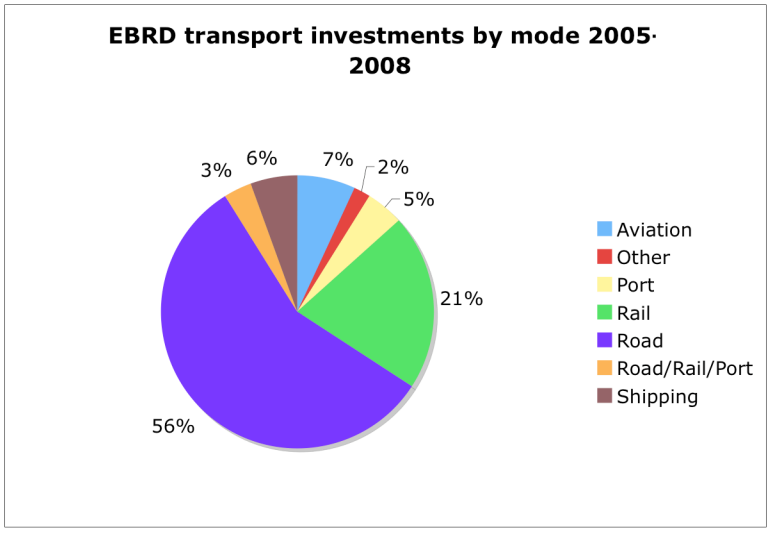
heavily subsidised through fuel tax and VAT exemptions, in our opinion the EBRD should limit aviation investments to safety improvements. **However, EBRD support for low cost carriers is particularly unacceptable, as they do exactly the opposite of providing the price signals needed for a shift to more sustainable transport.**

Railways: Railways are at varying stages of transition in the Bank's countries of operation, reflecting the political sensitivity involved in the restructuring process. The Bank will continue to support railway restructuring and commercialisation, including labour restructuring programmes. In this way the Bank can help to ensure that Railways receive the level of funding commensurate with the benefits associated with this mode of transport. There may be opportunities for private sector financing, as freight forwarders seek to fill the gaps in the market for modern freight wagons. These transactions may be asset-based. The drive to optimise the use of railway assets will provide opportunities for the Bank to finance private concessionaires operating public assets, such as railway stations. There may also be interesting equity opportunities given the expanding market.

The EBRD is very keen to restructure and commercialise rail services, however in our opinion keeping rail services **affordable** should be a key aim. This is both for social and environmental reasons: There is no point in introducing road tolls to put the different modes on a more equal footing and strengthen the use of public transport if the price of rail transport simultaneously rises and makes that mode less attractive. **The EBRD should have shown in its aims how it would balance the need for efficiency increases and service improvements with the need to keep railway pricing low enough to make the mode competitive.**

Modal split and climate impacts

According to the project list available on the EBRD's website, investments between 2005 and 2008 were, by volume, as follows:



This looks roughly similar to the graph on the EBRD's transport investments as of December 2004, shown on p.11 of the current transport policy. However we would expect that the EBRD should have moved towards greater financing of the most sustainable modes of transport since then, in line with strengthened EU policy on tackling climate change.

Clearly many countries where the EBRD operates do need investment in maintenance and upgrading of their road infrastructure, and in certain cases new roads need to be constructed, for example to avoid urban centres. **However if we are serious about tackling change we cannot keep prioritising investments into new road infrastructure, which induces new traffic and reinforces the trend away from using public transport.** Investing in roads also crowds out the investment needed to improve rail, urban public transport, cycling and pedestrian infrastructure, intermodal transport and inland waterway transport and to re-orient the economy towards reducing the need for transportation (eg. increased localisation of food economies, better communications for long-distance communications etc).

This also applies to aviation, the most carbon-intensive mode of transport. While safety improvements are most likely needed in many of the EBRD's countries of operation, in our opinion the EBRD should avoid investing in expansion of airports or airline fleets. This is particularly so considering that aviation is inexplicably subsidised through lack of tax on kerosene or VAT on international air tickets.

The M6 in Hungary was one example of a project that was undertaken due to high demand on the existing road and a poor safety record. While action was clearly needed, what would have happened if instead of building a new motorway, the railway had been improved and the existing road had been adjusted to include bypasses around settlements where necessary, a toll for transit vehicles had been implemented and investments had been made to eliminate particular accident blackspots? We will never know, but **the EBRD must increasingly ask such questions before approving projects if we are to move towards a more sustainable transport system and drastically reduce CO2 emissions from transport**.

We are disappointed that the advanced transition European countries have missed many opportunities to learn from western Europe's transport mistakes and excessive reliance on private road transport, however there are still plenty of opportunities to avoid going further down this route and reverse the trend, while we hope that the less advanced transition countries will avoid this pitfall not through being too impoverished to have a high level of usage of private vehicles but by rendering it unnecessary through effective and affordable public transport systems and intelligent economic and spatial planning policies. The EBRD needs to make a choice on how best to contribute to a sustainable transport system and to back it up with an appropriate allocation of resources.

Transition Impact Indicators

In our opinion **the EBRD needs to re-think how it weights transition to a market economy compared to environmental and social considerations in the transport sector**. Almost any transport project one can think of has some impact on increasing private sector activity and therefore on transition, but the projects which have a positive impact on the environment are much fewer. It is of particular note that very few places in the world can be said to have "got it right" as far as providing a low-carbon, user-friendly, affordable transport system in concerned, and it is therefore imperative that the transition countries do not simply follow models which are now proving so hard to change in the light of the need to reduce CO2 emissions. As transport is the fastest growing source of CO2 emissions

globally we believe that the EBRD's assessments should give greater weight to transport projects that will contribute to modal shift and significant emissions reductions.

This could be done by increasing the weight of environmental performance and environmental change assessment indicators in project assessment and evaluation or by changing the transition impact indicators to incorporate the need for a transition to a low-carbon economy as well as a market-oriented one.

There also needs to be greater clarity in the policy about where the EBRD finds competition and private sector involvement useful and where not. Concerning the current transition impact indicators on p.53-55, some criteria appear too prescriptive of private sector involvement and may prejudice the EBRD towards involving the private sector even where experience does not suggest it is particularly effective, while other criteria appear too easy to meet. Here we outline our comments on some of the transition indicators:

Early and intermediate stage of transition: Criterion No. 1: **Competition in the project sector**: Does the project increase competition in the sector? Does it promote customer orientation, innovation and greater efficiency?
Indicator 3: EBRD procurement rules and open tendering for works create competition among suppliers (e.g., road rehabilitation works)
Indicator 4: incentives for efficiency improvements through management or service contracts to private contractors (e.g., railway workshops; airport rehabilitation; urban transport services)

The criterion itself and its 4th indicator seem to bias the EBRD towards supporting any projects that involve competition and private sector involvement regardless of whether such areas have in practice proven that private sector management or service provision brings significant advantages, such as private sector operation of passenger rail transport, management of rail infrastructure, or motorway PPPs. Yet it is hard to think of almost any project complying with EBRD procurement rules that would not satisfy Indicator 3. It is therefore unclear how much this criterion is useful for the transport sector in its current form.

Early and intermediate stage of transition: Criterion No. 4: **Framework for markets**: Does the project strengthen public and private institutions that support the market? Does it support government policy formation and improvements in regulatory practises?
Indicator 1: tariff reforms as loan covenants; linked to commercialisation programme to ensure simultaneous cost reductions and tariffs increases
Indicator 2: reduction of cross-subsidisation through tariff increases and transparent public budget allocations (e.g., public service obligations transfers to railways)
Indicator 7: commercialisation and tariff reform reduces fiscal burden on the public budget, which support refocusing of government activities in the transport sector

As discussed above, **it is in our opinion necessary for the EBRD to incorporate environmentally-oriented pricing into the transition indicators relating to tariff reform and commercialisation.** It is undesirable to reduce the fiscal burden on the public budget for railways only to find that they are used less and private road transport is used more because the railway prices have increased.

Advanced stage of transition: Criterion No 2: **Market expansion**: Does the project contribute to the

integration of economic activities into the national or international economy (forward linkages)?
Indicator 1: private sector involvement to meet financing requirements

There is no inherent reason why private sector involvement in providing financing infrastructure projects (assuming this is referring to PPPs rather than simply private banks financing state projects) should be part of a market economy. Many advanced market economies have carried out only very few PPPs. This indicator should therefore not be used for the transport sector.

Advanced stage of transition: Criterion No 2: **Competition and backward linkages**: Does the project increase competition in the project sector and among suppliers?
Indicator 1: EBRD support for private service providers; review of contractual framework to balance interests of public, government and private investor (e.g., use of local contractors in transport infrastructure works). In sectors with natural monopolies (e.g. toll roads, railway infrastructure): assistance in organising "competition for the market" with private participation;

Advanced stage of transition: Criterion No 4: **Private ownership**: Does the project increase the share of goods and services provided by the private sector?
Indicator 1: private sector participation in service provision, often building on earlier EBRD involvement in the commercialisation of transport enterprises

In our opinion it is not sufficient to award points to projects simply because they include private service providers. It should be the quality of the service and value for money for the public sector that counts, not whether the service is provided by the private or public sector. It is particularly of concern in sectors with natural monopolies as in our opinion there is little evidence that involving private sector service providers in these sectors brings significant improvements and value for money over public operation. Additionally these indicators seems to push the transition countries to go further with private sector involvement than some of the advanced market economies, and we would therefore recommend their reformulation or removal.

General transition impacts: Criterion No. 6: **Demonstration effects**: Does the project create replicable practices and processes which help transfer the impact of EBRD from the project level to the sector as a whole?
- for example: the first BOT toll road in a country; the first railway privatisation etc.;
- demonstration effects are particularly strong when the Bank enters a new sub-sector and pushes the frontier of financing outwards towards increased private sector participation and commercial orientation (e.g. international airport terminals, railway operations)

In our opinion there needs to be less emphasis on demonstration effects, as innovation is only useful if it actually works well and brings clear advantages compared to other approaches. Eg. Would a project for a first BOT toll road in a country score highly in this area even if it was more expensive than a publicly procured one and if reproducing it in other projects would place a severe budget burden on the public authority?

We are aware that a review of the bank's transition impact is ongoing, and we hope that these issues will be taken into account during that process, resulting in a set of indicators that more accurately reflect the real positive and negative impacts of the EBRD's transport projects.

Projects and issues

Transport planning and prioritisation

The EBRD has already identified this area as one in which lessons need to be learnt:

> "Project selection needs to be based on a rational and robust business/investment planning process and where possible the Bank will through its project appraisal seek to complement the projects of other multilateral institutions. The Bank, in its appraisal of its projects, has due regard for the feasibility and viability of the broader context in which an individual project is developed. This is essential to maximise project returns both in financial and transition terms in the context of sound overall sector business/investment planning." (p.15, EBRD Transport Operations Policy)

However we believe that there is still more to be done. Transport planning in transition countries negatively impacted by several factors such as:

- lack of awareness of the need to switch to a low-carbon economy
- a perception that public transport is old-fashioned and untrendy
- a "predict and provide" attitude to road traffic
- the resurrection of decades-old projects
- corruption and special interests
- a preference for large, visible, prestige projects over smaller but smarter solutions
- a preference for Pan-European Network routes over routes that would better serve local people.

Corridor Vc motorway, Bosnia and Herzegovina

The Corridor Vc project - with the exception of some route variants discussed below - is widely accepted as the highest state priority for transport in Bosnia and Herzegovina (BiH), however some questions do arise as to whether other transport projects should not have been considered more important.

- Corridor Vc is based on a decades-old international corridor route, however if it had not been previously designated it is unclear whether it would have been the first choice for BiH's transport development. While the section between Sarajevo and Zenica is certainly justified, it is noticeable that the motorway does not join any of Bosnia's three largest cities (Sarajevo, Banja Luka, Tuzla) together. It connects Sarajevo to the sea, however the route goes to Ploce, situated in Croatia, not to BiH's only port at Neum. It may be that this last point is necessary for geographical reasons, however it is an issue currently causing debate in BiH.

- The cost of the motorway is extremely high. The last estimate we are aware of is around EUR 3.6 billion[2]. This raises the question of whether it is affordable for Bosnia-Herzegovina and whether it will result in a shortage of funding for other transport projects. Considering that a PPP is planned for some sections, this is particularly pertinent, as the PPP costs are likely to be fixed by the contract, leaving budget lines outside of the PPP to have to cut their costs instead.

[2] Statement by Federal Minister for transport and communcations Nail Šećkanović, 06.08.2008 http://www.cyberbulevar.com/vijesti/ekonomija/koridor-vc-kroz-bih-vise-od-tri-milijarde-eura/20080806/

Western High Speed Diameter (WHSD)
Although the EBRD is not currently involved in this project, it was clearly interested in financing it, and in our understanding may be involved again if the Russian government decides to re-start the PPP for the project again. It provides a number of lessons regarding transport planning:

- Lack of integration with local transport system: The WHSD is primarily intended for transit traffic. However it appears that it will duplicate the route taken by the St Petersburg Ring Road across the flood barrier across the Gulf of Finland. For all projects it is necessary to ensure that a coherent and publicy consulted transport plan exists, which will bring real benefits to local people.

- The EU High Level Group, chaired by Loyola de Palacio, on the extension of the major trans-European transport axes to the neighbouring countries and regions deemed the WHSD project to be one of longer-term interest. However, the project has proceeded more quickly than projects considered of "short to medium term interest" like the port of St. Petersburg, a high-speed passenger railway line from Moscow to St. Petersburg, the reconstruction of a railway section from St. Petersburg to Kotelnitch and the construction of a motorway from St. Petersburg to Moscow.

- The WHSD is a vast and complex project costing an enormous (and rising) amount to build. It is unclear why it has been prioritised over smaller and cheaper projects with clearer benefits for local people and the environment.

Port of Dubrovnik
We have not monitored this project in detail, however local people have informally expressed concerns regarding the project, which we will mention here.

Dubrovnik's main tourist attraction is its old walled town. Anyone who has visited between April and October in recent years will most likely have noticed how crowded it is, particularly near the entrance, at most times of the day, especially when groups of tourists come all at once. This raises the question of whether it is useful to expand Dubrovnik port's capacity to accommodate more and larger cruise ships, as the space in the old town is physically limited. Local people further complain that those arriving by cruise ship bring hardly any economic benefits to the city as they stay at most an hour or two in the city, sleep and eat on their cruise ship, and at most buy a postcard or two.

Clearly some income is gained from berthing fees at the port, however it is open to question whether this project has been well integrated with other local development considerations.

While the EBRD as a bank cannot resolve all these problems, there are certain steps it needs to undertake in order to ensure that the projects it finances will benefit the local people and economy, as well as the environment.

- Requiring that the projects it finances are part of a well-integrated *and publicly consulted* transport development plan on the local and national level.
- The EBRD's Environmental and Social Policy states "*In exceptional circumstances, a regional, sectoral or strategic assessment may be required."* It should be defined

what these circumstances are. We believe that where new construction is envisaged, rather than upgrading or maintenance of an existing route, a Strategic Environmental Impact Assessment must be carried out on the relevant transport plan or programme.

- Requiring a justification of why the projects put forward are to be financed before other projects from the plan (if this is not clear from the transport plan).
- Giving preference to projects in sustainable modes of transport: particularly on corridors where both rail and road are present, there is a tendency to build a large motorway and follow it with railway improvements only several years later when people have got used to using the motorway. This should be reversed.
- Avoiding the financing of construction of road sections that are primarily used by cross-border traffic, as this further increases the dominance of road freight transport over rail. Conversely the bank should step up financing for cross-border rail projects.

Selection of project locations/routes and consultation procedures

"Environmental issues need to be identified at an early phase to ensure that a project is environmentally sound and to allow appropriate mitigation measures to be put in place. Each Bank project undergoes environmental appraisal in accordance with the Bank's Environmental Policy and Procedures. The Bank will take into account, where the Bank is financing part of a wider development, the sustainability of the whole plan as appropriate in the context of the Bank's project appraisal." (p.15 EBRD Transport Operations Policy).

"Where the Bank is financing part of a wider development, the sustainability of the whole development will be appraised in the context of the Bank's project due diligence." (p.43 EBRD Transport Operational Policy).

The EBRD has made it clear that the environmental soundness of each project will be assessed as part of the project appraisal procedure, including the whole project where the EBRD is financing only some sections. However experience shows that in the 2005-2008 period some projects were still slipping through the net and being approved with inadequate public consultation or before environmental concerns had been properly addressed, or that environmental measures were not properly implemented.

Corridor Vc, Bosnia and Herzegovina

The approach to the scoping for the EIA of this project was a great improvement on anything that had happened previously in Bosnia and Herzegovina, with the project promoter contacting many of the relevant stakeholders and publishing their comments together with how they were taken into account as part of the EIA. However there are still outstanding environmental/cultural issues:

- at Blagaj, where agricultural land will be lost, the valley will be divided by the motorway, and there may be visual impacts on the tentative UNESCO World Heritage site,
- at Pocitelj where a bridge passing around 300m from a tentative World Heritage site and art colony would have severe visual impacts, and
- in the planned Prenj-Cvrsnica-Cabulja National Park, where a 6.5 km tunnel is being promoted as avoiding serious environmental impacts, however it is not clear that this will avoid significant damage to this unique area.

These issues raise the question of why the EBRD approved the Corridor Vc project before appropriate routings and/or mitigation measures had been confirmed.

Tbilisi International Airport - the shortest EIA consultation ever?

Georgian authorities and a consortium consisting of Turkish companies Tepe-Akfen-Vie and Urban, signed a contract in September 2005 transferring management rights for Tbilisi Airport to TAV-Urban for a period of 15 years. Construction of the new terminal began in January 2006.

On Friday 9 December 2005, the Georgian Ministry of the Environment announced a public consultation meeting for the EIA of the Tbilisi Airport project. According to the announcement the deadline for receiving comments on the EIA was only on Monday December 12, 2005, thus making it impossible to prepare comments properly.

During the public consultation meeting NGOs protested about this and accused the Georgian government of violating the law. According to Georgian environmental legislation the Ministry of the Environment is obliged to set a 2-week period for receiving comments on the document and to disseminate information about the public consultation meeting at least a week prior to meeting.

According to the head of the Department of Licensing and Permits of the Ministry of Environment the EIA of the project was submitted to the Ministry on 7 December, 2005 and government ordered that permission must be issued not later than 13 December. According to the Minister of the Environment the permit was issued in a hurried manner because of the high importance of the project. However Georgian law contains no provisions for accelerated procedures for issuing permits (only for certain projects to be exempted from an EIA procedure, which was not the case here).

Comments regarding the EIA study itself:
- It is quite unclear what type of works is considered in the EIA - construction of a new terminal or the reconstruction of the existing one? Nothing is mentioned about the exact name of the works in the EIA.
- In the EIA it is stated that the EIA was prepared for the operation period of the airport, but then it is quite unclear why the project investor approached the Ministry of Economic Development for construction permission.
- The economic viability of the project is not mentioned in the EIA at all.
- There is only a very general description of such important issues as safety measures in case of oil leakage, fire, technological accidents etc. that need to be described in detail.

In spite of the defiencies of the process, the EBRD's PSD states for the project that "An Environmental Impact Assessment (EIA) has been undertaken in accordance with national requirements".[3]

In the end, however, the environment had its own impacts on the airport. The new terminal was inaugurated by Azeri, Georgian and Turkish leaders on February 7, 2007, but already on February 18, 2007 the roof started to leak. On February 24, 2007 a portion of

[3] http://www.ebrd.com/projects/psd/psd2006/36385.htm

the roof was ripped off by strong winds[4]. Just after a month after the airport's official opening ceremony the rain leaked in a second time on March 9, 2007. As happened the first time, the floor was flooded and the escalator and other technical equipment in the waiting room were out of order after the heavy rain.

The EBRD's Environmental and Social Policy covers all the issues above, however we encourage the Evaluation Department to examine how environmental appraisal of projects can be reinforced to avoid such problems.

Resettlement and social mitigation measures

The safeguard standards to be followed in EBRD projects involving resettlement are clear, however as with environmental and public consultation standards, we have seen some projects failing to result in the project affected people being equally as well off after the project as before.

Resettlement of Gazela Bridge informal settlement, Belgrade, Serbia as a pre-condition for the rehabilitation of Gazela Bridge

The arrangement of this technical assistance project has been very cumbersome, as the European Investment Bank is financing the bridge rehabilitation, with the EBRD financing the approach roads, yet the EBRD has been providing technical assistance for the resettlement, with funding from the European Agency for Reconstruction and the Department for International Development. This has created difficulties in ascertaining who is responsible for what.

What is clear though, is that the resettlement has been highly unsatisfactory, to put it mildly.

- At the time of writing, two families have not been resettled at all because they did not agree with the locations offered. They are currently staying with relatives in another slum settlement.
- The other families who were "allowed" to stay in Belgrade have been resettled into shipping containers at four sites outside of the city, which have no possibilities for economic activity. At the same time the residents' former work in informal collection of waste has been made difficult or impossible because of the need to travel to Belgrade, which is not affordable.
- The other former Gazela residents who were not deemed "eligible" for resettlement in Belgrade were taken on buses to other cities in Serbia. We do not know what provisions have been made for them.
- The affected people have never seen the Resettlement Action Plan, or been consulted about it. They signed agreements for resettlement but were not given copies and people we have spoken to claim they were not even given time to read them but were rather told to take it or leave it.
- The families in the shipping containers are fully dependent on social assistance including being brought one meal a day by social services. They are becoming malnourished due to lack of income for other food.

[4] http://www.civil.ge/eng/article.php?id=14688 Wind Blows Roof off New Airport, 24.02.2007

- The physical conditions in the containers are unsatisfactory - 7-10 people per container is not uncommon, there are insufficient sanitary containers, and there is no form of heating or stoves for cooking.

While Belgrade City Council has primary responsibility for the resettlement, it is unclear why the European Investment Bank and the EBRD approved financing for the project before a satisfactory Resettlement Action Plan had been submitted to them. The EBRD Environmental Policy 2003 which governs the project states that it would follow IFC O.D. 4.30 in resettlement cases, which clearly states that "*Submission to the Bank of a time-bound resettlement plan and budget that conforms to Bank policy is a condition of initiating appraisal for projects involving resettlement, except for sector investment loans as discussed in para. 26.*" (para.30)

This is not the only time that the EBRD has approved projects before the Resettlement Action Plan had been approved. It has also done so with the Corridor Vc.

We call on the EBRD to stop approving projects before Resettlement Action Plans are approved, as it not only contravenes the bank's policy but increases the pressure on the bank to later approve something which is less than satisfactory because so much time and effort has already been put into the project.

We would also emphasise the need for the bank to do more to ensure that the project affected people are adequately consulted about the resettlement plans, particularly in cases where vulnerable groups are concerned.

Public-Private Partnerships

The current Transport Operations Policy makes much of Public-Private Partnerships and their potential contribution in transport infrastructure construction and operation:

Regional Trends: "The Bank will support well structured PPPs, which comply with the Eurostat criteria for risk transfer. These may be driven by the political need to deliver improved infrastructure faster and fiscal pressures." (p.7 Transport Operations Policy)

"Product Trends: PPPs: The Bank anticipates increasing interest in PPPs, driven by value for money, budgetary considerations and the inability of governments to deliver infrastructure improvements in line with the growth of the economy. The Bank will also support refinancing of PPPs where justified." (p.8)

"The transition goals include transparency of funding of transport infrastructure, value for money achieved through private-sector efficiencies, the developmental effect of achieving the return from improving transport infrastructure at an earlier date, that otherwise might have had to wait for the allocation of state borrowing capacity, thereby bringing forward the economic benefits of a transaction, demonstration effect of foreign direct investment in PPPs and also of the refinancing of PPPs." (p. 33)

"Wherever the PPP is implemented, the achievement of transparency through the contract between the public and private-sector can have a substantial transition impact. The Bank will support PPPs which demonstrate that they provide value for money." (p.33)

Several elements of the above statements give cause for concern:

- Eurostat criteria for risk transfer: Eurostat allows PPPs to be treated as off-balance-sheet investments if the private partner takes on the construction risk plus either the demand risk or the availability risk. However after the failure of the early Hungarian PPP motorway projects, which did transfer demand risk to the private sector, at least until the public sector had to step in and rescue the projects again, **PPP motorway projects today involve almost no risk for the private sector after construction is completed**. Either there is a toll with a guarantee by the public authority that traffic shortfalls will be compensated, or there is an availability fee, where the private company is simply paid a fixed amount by the public authority, in return for performing some not-particularly-difficult tasks such as maintenance and clearing snow off of the road.
- **Both of the first two statements seem to present moving projects off of the government balance sheet as a legitimate reason for their use**. In our opinion this is simply unacceptable deception, making the government's financial situation look better than it really is and failing to disclose commitments for future payments over the coming decades.
- Pressure to deliver infrastructure faster is indeed an issue, but as discussed above, **cheaper and more environmentally acceptable impacts may be able to be achieved with better transport planning**.
- Refinancing: Experience from the early UK PPPs brought up a number of shocking cases of massive windfalls for the private sector due to refinancing. While the issue is now better-known and there are often regulations in place to ensure that the public sector gains at least a portion of the benefits, **we encourage the Evaluation Department to examine whether the EBRD ensures that the public sector obtains a fair proportion of any refinancing gains.**
- Transparency: This word is mentioned twice in the quotes above, but it should be clear that there is transparency only between the private company and the public authority. With regard to public information and consultation about PPPs, there is very little transparency indeed. Contracts are not usually published, so it is usually unclear to the public how much the public sector will pay to the private sector over the lifetime of the contract, whether the private sector is in fact bearing any significant risks, who bears the risks if it all goes wrong, which budget the payments will come from and what the effect on other services would be in case of a future need for cost-cutting etc. **We encourage the Evaluation Department to make recommendations on how the EBRD could more effectively balance the need for public information with the need to withhold information which is truly commercially confidential.**

The problems with PPPs are nowhere more visible than in motorway construction and operation. As well as the issues surrounding all PPPs, motorways bring their own set of problems, considering the need to both raise income and provide an environmental incentive to shift to more sustainable modes of transport. If there is a toll, it provides a certain level of disincentive for using the road, in line with environmental aims (as long as the traffic does not simply use an alternative route, which in fact often happens in central and eastern Europe because for many people saving money has a greater value than saving time). However, if the motorway is being run on a concession basis, the concessionaire

needs to *encourage* traffic in order to raise income, going completely against environmental objectives. In practice it has been shown that full costs cannot generally be recovered by tolls in transition countries, so income guarantees are often given by the public sector, which also removes the incentive to encourage traffic. However this brings with it the problem mentioned above, that there is very little risk for the concessionaire during the operation period, and often a very high risk for the public sector, as traffic forecasts often turn out to be inflated.

In order to make it clearer what the public sector will have to pay, some PPPs such as the M6 in Hungary are using availability payments rather than direct tolls. However this does not solve the problem that there is very little risk for the project company during the operation phase.

This raises the question of whether it would not rather be better for the EBRD, where it considers support for road construction projects imperative, to support public sector projects carried out with fixed-term turnkey contracts, which would help to transfer the construction risk to the private sector but would avoid the expensive pretence of transferring risk to the private sector for the operational period.

Although the EBRD did not finance many transport PPPs in this period, the projects below, along with other non-EBRD financed PPPs in the region, show some of the problems encountered.

M6 motorway PPP, Hungary

The Hungarian state audit office has not been particularly impressed with the Hungarian government's PPP projects. A 2006 report on the M6 motorway states (our emphasis):

"*The M6 motorway stretch between Érd Height and Dunaújváros was constructed with the use of a PPP funding method. The State bore the cost of the preparatory measures, while the project company funded the construction by a 22-year-long "self-raised" loan for which the State made no financial commitment or guarantee.* ***No economic calculations were made prior to the decision on implementing this project with a PPP method***.

After concluding the concession contract and the underlying loan contracts (that provide the necessary funds for the "concession deal"), economy calculations were done by an external consultant, hired by the Ministry of Economy and Transport. The consultant's paper used a 10 % discount rate formerly already in use at the M5 motorway project, and the Ministry had no objection to this. Calculating with this 10% rate, the paper claimed the "governmental project option" would have a 21% drawback against a PPP method. However, it also contained the statement that the present values of the two project options (governmental versus PPP) are equal at a rate of 7,1%. ***There is no regulation on (1) the procedures, steps to be followed at projects using the PPP method, (2) on the need, requirement to apply economic calculations at such projects, (3) how to set the applicable discount rate, (4) the extent of the rate****. It is important to have an adequate discount rate since the costs emerging in the long run will have a smaller present value if a*

higher than adequate rate is used. When the paper was completed, the average return (interest rate) on the government's interest-bearing long-run resources was 7,06 %."[5]

It is of great concern that no PSC calculation was carried out before the decision to use a PPP was made, and that when it was, the decision mainly rested on the highly contentious choice of discount rate. We encourage the Evaluation Department to look into the EBRD's requirements on how decisions are taken to use PPPs in projects, and particularly the issue of discount rates, which often seem to be the only factor tipping PSC calculations in favour of PPPs.

Western High Speed Diameter, St Petersburg, Russia

Although the EBRD has not yet financed the Western High Speed Diameter, it has been involved in its development and as we understand it may be involved in the project in the future if it is again structured as a PPP. The following is a shortened version of the case study presented in Bankwatch's 2008 publication on PPPs *Never Mind the Balance Sheet*.

The 46-kilometre Western High Speed Diameter would have to cross the Gulf of Finland, with the required bridge height reaching 55 metres, and spanning an overall length of 26 kilometres. One would assume that such a complex and expensive project would have undergone an assessment of its viability before it was presented for a bidding procedure. However, when inquiring about the results of affordability analysis that would demonstrate that the predicted returns make the project fiscally affordable, Russian environmental groups learned that no such analysis has been undertaken.

Since 2006, the estimated WHSD construction costs have sky-rocketed from USD 2 billion to more than USD 9 billion. The costs may rise even higher as the prices of building materials continue to grow. Under the proposed conditions of the concession agreement, any lack of revenue from the 30-year exploitation of the road would be compensated to the company from the Saint Petersburg budget. Given that the construction cost is almost equal to Saint Petersburg's annual income in 2007, such obligations may result in serious financial problems.

According to the bidding documentation, the WHSD is expected to attract 120 000 vehicles per day by 2025, and the private operator's income is expected to be generated from direct toll payments by users. However, the traffic forecast made by the developer of the project may be too optimistic – this has already been the case with a number of toll roads in the USA and Europe. Given the inability of either the public or private sector to control the demand risk, and the high-profile failures of the direct toll approach in several cases in central and eastern Europe (for example the M5 in Hungary), it is unclear why this approach has been chosen - although an availability fee would also not impose much risk on the concessionaire during the operation period.

This threat of budget burden has been acknowledged by experts at the World Bank, which has been a consultant on the project. According to a presentation in December 2007 by William Dachs, the head of the World Bank's PPP Unit, Saint Petersburg's potential

[5] Hungarian State Audit Office: Summary of the comparative audit on the funding arrangements for motorway development projects (0645), 2006, http://www.asz.hu/ASZ/www.nsf/publications_other.html

payments under PPP guarantees are likely to amount to several billion dollars as, along with the WHSD motorway, the authorities have announced the building of the Nadzemny Express railway, the Orlovsky tunnel and the reconstruction of the Pulkovo airport. Dachs also pointed out that budgeting for uncertain payments under guarantees is already a pressing problem for Saint Petersburg. Although the WHSD and some other PPPs are now on hold they are expected to go ahead after the financial crisis lessens, and there is no sign that any lessons have been learnt.

Concession process becomes a one-horse race

After a road show held in December 2006 in the EBRD's head office in London, it was announced that more than 130 companies were interested in the WHSD concession. However, only four consortia pre-qualified in the tender to build and operate the road, with one bidder left at the last stage of the competition – the ZSD Nevsky Meridian consortium, led by the Russian multi-billionaire Oleg Deripaska. The reasons why the three other consortia did not qualify for the final stage remain unclear.

The fact that there was only one bidder in the final round of the tender process puts the city of Saint Petersburg in an extremely weak negotiating position, further increasing concerns about the value for money of the project.

Experts have listed a number of risks that could prevent companies from stepping into the project. One of the biggest problems is the lack of properly tested legal basis for PPPs in Russia. The law on concessions was passed by the Russian parliament in 2005, with amendments made in July 2008. A specific regional law on PPPs has also been approved by the Saint Petersburg regional government. Some argue the laws still contain loopholes and they are contradictory to be fully functioning documents. Due to the numerous legal issues, the bidding procedure for the WHSD took a year and a half, and during this period the cost of the road tripled. The Lawyer magazine notes that one of the major sticking points is the uncertainty over the process for disputes. The possibility of attempting to settle a dispute in the Russian courts is giving even the most robust sponsors and lenders reason to pause.

The concessionaire will also have to deal with environmental and social issues that have not received much attention from the project developer so far. In Saint Petersburg, 40,000 people have signed a petition against the toll road, saying that it is unnecessary and would destroy the local environment. More than 90 scientists from the Russian Academy of Science have publicly supported this opinion, stating that a new thorough EIA of the project must be conducted before further construction takes place.

Recommendations

Transport Operations Policy aims

The EBRD needs to:

1) develop objectives to **prioritise financing for the most sustainable and least carbon-intensive modes of transport, limit aviation financing to safety improvements and air traffic control and decrease financing for new motorway construction. No financing should be given for low-cost airlines**, which provide exactly the opposite environmental pricing signals from the ones which the EBRD says it aims to promote.

2) **avoid contradictory environmental pricing signal**s, in which road charging is introduced, but at the same time rail commercialisation renders rail services more expensive, thus providing no net incentive for traffic to shift to rail. It is necessary to balance the need for efficiency increases and service improvements with the need to keep railway pricing low enough to make the mode competitive.

3) outline how it intends to **ensure that the projects it supports are the result of coherent, rational and consultative planning processes**.

4) **lay out more clearly how it will discern which road construction projects are *really* necessary** and could not be resolved in another way such as upgrading adjacent rail services, introducing tolls for transit vehicles on the existing road, undertaking improvement works on particular stretches etc.

Transition Impact Indicators

5) re-think how the weighting of transition impact compared to environmental and social considerations in the transport sector. This could be done by increasing the weight of environmental performance and environmental change assessment indicators in project assessment and evaluation or by changing the transition impact indicators to incorporate the need for a transition to a low-carbon economy, not only a market-oriented one.

6) incorporate environmentally-oriented pricing into the transition indicators relating to tariff reform and commercialisation to avoid situations where rail reforms result in increased prices that make rail unattractive relative to road transport.

7) reformulate or avoid the usage of transition impact indicators for the transport sector which encourage private sector service provision in sub-sectors where its usefulness has not been fully proven such as rail passenger transport operation and motorway operation as part of PPPs.

Transport Planning

8) Require that the projects it finances are part of a coherent *and publicly consulted* transport development plan on the local and national level.

9) Define the circumstances in which a Strategic Environmental Impact Assessment must be carried out. For all projects where new road construction is envisaged, rather than upgrading or maintenance of an existing route, a Strategic Environmental Impact Assessment must be carried out on the relevant transport plan or programme.

10) Require a justification of why the project put forward is to be financed before other projects from the plan (if this is not clear from the transport plan).

11) Give clear preference to projects in sustainable modes of transport: particularly on corridors where both rail and road are present, there is a tendency to build a large motorway and follow it with railway improvements only several years later when people have got used to using the motorway. This should be reversed.

12) Avoiding the financing of construction of road sections that are primarily used by cross-border traffic, as this further increases the dominance of road freight transport over rail. Conversely the bank should step up financing for cross-border rail projects.

Selection of project locations/routes and consultation procedures

13) We encourage the Evaluation Department to look for ways to strengthen the bank's environmental and social assessment to ensure that all relevant issues are resolved *before* financing is approved.

Resettlement and social mitigation measures

14) Stop approving projects before satisfactory Resettlement Action Plans have been approved.

15) Step up efforts to ensure that the project-affected people are adequately consulted about resettlement plans, particularly in cases where vulnerable groups are concerned.

Public-Private Partnerships

We encourage the Evaluation Department to:

16) examine whether PPP road construction projects have shown superior performance compared to publicly procured ones, whether similar results could have been achieved with publicly procured construction projects using turnkey contracts and whether sufficient risk was transferred to the private partner in the operational stage to justify the higher costs of private financing.

17) examine whether the EBRD ensures that the public sector obtains a fair proportion of any refinancing gains.

18) make recommendations on how the EBRD could more effectively balance the need for increased public information on PPPs (total costs, risk allocations, budget burden and source of payments etc) with the need to withhold information which is truly commercially confidential.

The EBRD should:

19) be more pro-active in ensuring that an affordability assessment and PSC calculation is carried out in PPP projects and that they rely on reasonable assumptions. As a public

institution it should actively ensure that the public sector obtains value for money.

20) ensure that the long-term cumulative impacts of PPPs and other public budget commitments are quantified and analysed for their constraints on future public spending

21) ensure that public authorities release project documents such as the PSC calculation and methodology, the draft and signed versions of the contract, and information about affordability; this may entail a review of the criteria for withholding project information on the grounds of 'commercial confidentiality'.

22) ensure that the public authority has adequately shown how it will monitor and enforce performance standards; where a public authority has low capacity to undertake such work effectively, the EBRD should not finance PPP projects.

23) consider lending to the public authority rather than the private partner in order to reduce the cost of financing, so that the decision on whether to involve the private sector will not be made on the basis of the potential to rely on off-balance-sheet accounting.

24) lend only to those projects where other financing is not available on reasonable terms.

25) ensure that all project components have been included in the project, in order to avoid cost increases later.

26) set clear limits on the cost increases and specification changes that it is willing to accept during the preferred bidder stage, and be ready to walk away from a project if the public is no longer getting good value for money.

27) carry out a publicly available evaluation – with the project named – for all PPP projects, and consider doing two in order to allow the minimisation of problems that arise during the project.

28) consider lending for public-public partnership projects where public management improvements are needed, for example where well-run road companies can be twinned with ones in need of capacity building.

Annex 1: EBRD-financed transport projects 2005-2008

Country	Year	Mode	Project	Description	EUR m	State/ Private
Albania	2005	Aviation	Tirana airport privatisation project	Upgrading of facilities at the airport	31.6	Private
Albania	2005	Road	Fier-Tepelene road rehabilitation project	Upgrading and construction of the road from Fier to Tepelene	35	State
Albania	2007	Port	Durres Port	Loan to finance a ferry terminal and related infrastructure	14	State

				at the port of Durres		
Albania	2007	Road	Levan-Vlore road	Loan to upgrade the road from Levan to Vlore	22	State
Armenia	2006	Aviation	Armenia International Airport	Construction of a new passenger terminal and purchase of new terminal equipment	14.383	Private
Azerbaijan	2005	Road	Baku to Samur road	Upgrading of a 60 km section of road from Sumgait to Zarat	71.134	State
Bosnia and Herzegovina	2005	Rail	Regional railway project	Financing of track infrastructure	70	State
Bosnia and Herzegovina	2006	Aviation	Bosnia and Herzegovina Air Traffic Management System	Supply of equipment and training services to improve safety	17	State
Bosnia and Herzegovina	2007	Road	Primary road network upgrade	Upgrade and reconstruction of sections of the primary road network	75	State
Bosnia and Herzegovina	2008	Road	Corridor Vc	Loan to finance key sections of trans-European motorway	180	State
Croatia	2005	Port	Port of Dubrovnik - infrastructure modernisation project	Extension of berth area in the port of Gruz, Dubrovnik, to accommodate more and larger vessels.	26.5	State
Croatia	2006	Road	Autocesta Rijeka-Zagreb	Upgrading of a road to full motorway status	50	State
Croatia	2006	Road	Rijeka bypass	Completion of a bypass to ease traffic congestion and facilitate movement	40	State
Croatia	2007	Port	Ploce port	Finance for civil works and supply of heavy lift cranes for work to Ploce port's new bulk terminal.	11.2	State
Georgia	2006	Aviation	Tbilisi International Airport	Construction of new facilities and upgrade of existing equipment to support increasing usage	18.4	Private
Hungary	2005	Road	M6 motorway	Financing of the M6	25.3	Private

				motorway on a design-build-finance-operate basis (DBFO) under a private partnership scheme.		
Hungary	2006	Road	M6 motorway refinancing	Loan to finance construction of the M6 motorway	32	Private
Hungary	2008	Road	M6-M60 motorway	Loan for expansion of the Hungarian motorway network	75	Private
Kazakhstan	2008	Other	KTZ Transtelecom - Communication infrastructure modernisation	Loan to upgrade telecommunications infrastructure	39.1	State
Kazakhstan	2008	Road/Port/Rail	Macquarie Renaissance Infrastructure Fund	Supporting infrastructure projects in Kazakhstan, Russia and Ukraine	17.78	Private
Moldova	2005	Port	Port of Giurgiulesti - oil terminal	Recovery of debt	5.3	Private
Moldova	2007	Road	Moldova road upgrading	Loan to finance improvements to the road network and institutional strengthening	30	State
Moldova	2008	Aviation	Chisinau airport modernisation II	Loan for airport modernisation	25.5	State
Montenegro	2005	Aviation	Air traffic management modernisation and upgrade	Modernisation of the Belgrade and Podgorica air traffic control centres and corresponding infrastructure	2.68	State
Montenegro	2005	Road	Montenegro regional road rehabilitation project	Improvements to infrastructure and safety of Montenegrin roads	11.5	State
Montenegro	2007	Rail	Montenegro rail infrastructure	Supply for the upgrading of railways infrastructure	11	State
Romania	2005	Rail	CFR rail traction project	Priority investment in CFR traction energy company	22.5	State
Romania	2005	Road	Constanta bypass project	Building and maintenance of the Constanta bypass	139.76	State

				project		
Russia	2006	Aviation	Sky Express	Investment in Russia's first low-cost airline	13.1	Private
Russia	2006	Rail	JN-Wagon	Acquisition of new wagons for transport of timber and woodchips	13.4	State
Russia	2006	Shipping	Maritime Navigation Safety Project	Construction of three radio towers for location and identification of ships	4.979	State
Russia	2007	Rail	IPL	Leasing of rolling stock to private rail operators	50.3	Private
Russia	2007	Rail	TransContainer	Equity stake in Russia's largest rail container operator	133	State
Russia	2008	Rail	Freight One	Loan for rail fleet renovation	92.47	State
Russia	2008	Road/Port/Rail	Macquarie Renaissance Infrastructure Fund	Supporting infrastructure projects in Kazakhstan, Russia and Ukraine	35.567	Private
Russia	2008	Shipping	Far Eastern Shipping Company	Equity investment to develop a transportation network	77.4	Private
Russia	2008	Shipping	Globaltrans	Finance to support railway reform programme in Russia	31.879	Private
Serbia	2005	Aviation	Air traffic management modernisation and upgrade	Modernisation of the Belgrade and Podgorica air traffic control centres and corresponding infrastructure	30.8	State
Serbia	2005	Road	Belgrade to Novi Sad motorway	Upgrading a 65 km section of road from Belgrade to Novi Sad and construction of a bridge across the Danube	72	State
Serbia	2006	Rail	Serbian Railways	Purchase of freight wagons to increase efficiency	60	State
Serbia	2007	Road	Belgrade Highway and Bypass	Loan to upgrade infrastructure and reduce traffic flow problems	80	State

Tajikistan	2005	Aviation	TSA air fleet upgrade	Financing for pre-operation costs and an aviation consultant	0.71	Private
Tajikistan	2007	Road	Road maintenance development	Finance for essential maintenance work on the Tajik road network	2.8	State
Ukraine	2005	Port	Ukrrichflot	Finance for part of the acquisition costs of five new dry cargo buildings	7.4	Private
Ukraine	2005	Road	Kiev-Chop road rehabilitation	Upgrading of the M06 Kiev-Chop road and further reform of road sector administration and financing	99.19	State
Ukraine	2006	Road	Kiev-Chop road upgrade	Completion of the M06 Kiev-Chop road to European standards	199.998	State
Ukraine	2006	Shipping	Black Sea Shipping Management Company	Construction and acquisition of five cargo ships	7.1	Private
Ukraine	2007	Port	Illichivsk commercial sea port	Finance for the modernisation of the port including berth reconstruction and purchase of new equipment.	26	State
Ukraine	2007	Port	Yugreftransflot	Finance for the company's fleet expansion programme	9.2	Private