



GREENPEACE



16th March 2012

**To:
The President of the European Bank for Reconstruction and Development**

Dear President,

In January 2011, the European Bank for Reconstruction and Development (EBRD) signed a contract with the Slovenian state-owned company Termoelektrarna Šoštanj (TEŠ) for construction of a sixth block at the lignite power plant in Šoštanj, Slovenia. Out of the EUR 200 million loan assigned by the EBRD for the project „SOSTANJ Thermal Power Plant”, EUR 100 million was syndicated to five private banks. As far as we know the loan has not been disbursed yet.

Since its inception, the project has been troubled with numerous controversies including allegations of corruption, its effects on the environment and its economic feasibility. To this extent, the Slovenian parliament has refrained from providing a state guarantee necessary for the second tranche of the EIB loan.

We are writing to inform the EBRD’s highest decision-making bodies about recent developments that in our view should prompt you to drop your participation in this investment¹.

Serious suspicions of corruption and mismanagement

In February 2012, after more than two years of investigation, the State Commission for the Prevention of Corruption in Slovenia published a report documenting numerous irregularities in the TEŠ project. The report says that corruption could have influenced the awarding of the contract for a construction of the sixth block to the French company ALSTOM. Furthermore, the tender for the main technological equipment has been exempted from the requirements of Slovene procurement law and EU procurement legislation, all without legal justification.

The Commission concludes that “the project is designed and implemented in a non-transparent manner, lacks supervision and is burdened with political and lobbying influences, and as a result there has been (and still is) a high risk of corruption and conflict of interest.” The scale of the conflict of interest and political motivations behind the project are exemplified by the breach of lobbying regulations described in the report. The Commission found that the authors of the proposed Law on State

¹ The EIB has also been recently informed by the problems with the project.

Guarantee for TEŠ 6 are members of Holding Slovenske Elektrarne (HSE), the parent company of TEŠ.

Ongoing investigations

Investigations into the possible unlawful acts at TEŠ have already been opened by the National Investigations Office and by the police in the town of Celje. The Commission for the Prevention of Corruption has also called on the Slovenian Prosecutor General to establish a special group to further investigate this case. Because of the ongoing investigations, the Commission could not reveal additional details but decided to publish the report in order to protect the public interest.

The European Commission as well is currently examining the possibility of Slovenian non-compliance with EU law in connection with this EBRD-funded project. The European Commission had already registered a complaint on the possible breach of the EU Carbon Capture and Storage Directive in November 2011², and the second complaint, on the alleged non-compliance with the Procurement Directive, was submitted one month later³.

Moreover the EBRD's Office of the Chief Compliance Officer is looking into the project after being informed about irregularities and possible breaches of European and Slovene laws and ongoing investigations in connection with the project⁴. The EIB's Inspector General is also currently investigating possible unlawful activities connected to the project and the integrity of the client.

Questionable economic feasibility

One of main reason of continuous debates about the necessity of providing the project with state support in the form of loan guarantee is the question of its economic feasibility. In April 2011, a Slovene government report described a lack of proper economic analysis of the investment, especially its sensitivity to changes in the project's main variables including the price of coal, carbon emission allowances, electricity and investment costs. The government concluded, "the project, as it is set now, is highly risky. The risk of the state is to lose its property if the project goes on in such a form, as HSE will have to pay for the losses of this project."

As a result, the government asked TEŠ to prepare a new investment program that should include a detailed sensitivity analysis with all the omitted costs. The estimates in the fourth version of the investment program set the internal rate of return (IRR) at a level of 7.59 percent. However this rate does not satisfy the requirements of the April 2011 Slovene energy sector policy, which requires a minimum discount rate of 9 percent⁶. According to the analysis prepared for Bankwatch and Focus by CE Delft,⁷ the IRR in the fourth investment program is calculated wrongly and, in fact, the IRR will

² The complaint submitted by Environmental Law Service on 3 October, 2011. Registration number: CHAP(2011)3041).

³ The complaint was submitted by Focus in November 2011. Registration number: CHAP(2011)03253.

⁴ See the following letters to the Office of the Chief Compliance Officer: sent by Focus and Bankwatch on 18th July 2011; sent by Environmental Law Service on 10th January 2012 and sent by Bankwatch on 22nd February 2012.

⁵ See details about the report of the Slovenian Ministry of the Economy (in Slovene): http://www.vlada.si/si/medijsko_sredisce/sporocila_za_javnost/sporocilo_za_javnost/article/130_redna_seja_vlade_rs_16831/

⁶ Sectoral policy for the energy sector, Ministry of Economy, January 2011 (in Slovene) http://www.mg.gov.si/fileadmin/mg.gov.si/pageuploads/Energetika/Dokumenti/Sektorska_politika_Energetika_Final.pdf

⁷ A critical examination of the investment proposals for Unit 6 of the Šoštanj Power Plant, CE Delft, November 2011,

not reach 7 percent and in some cases not even 6 percent.

In this context, it is worth mentioning that another binding law in Slovenia, the “Decree on the uniform methodology for the preparation and treatment of investment documentation in the field of public finance”, requires the internal rate of return at a level of at least 7 percent⁸. The economic feasibility remains an open issue also for the new government, which decided to back the state guarantee only if the investor ensures that all the conditions are met for achieving the internal rate of return in line with the sectoral policy⁹.

TEŠ 6 is an expansion of the existing power plant, NOT a replacement

The EBRD Board Document for the project claims that “The operation is part of the Company’s overall modernisation investment programme totalling EUR 1.2 billion which focuses on the replacement of five existing low efficiency and high carbon intensity units with a new state-of-the-art coal-fired unit of 600 MW (“Unit 6”), (...). Unit 6 will utilise state of the art high energy-efficient technology and will lead to significant carbon emissions reduction of around 1.2 million tonnes CO₂ p.a. in the long run.” While the project promoter publicly claims that the sixth block will replace existing capacities at the Šoštanj power plant, the environmental permit for the project¹⁰ does not support these assertions. The environmental permit says that the manager must ensure closure of units one, two and three by the time the new sixth unit begins operations and, at the same time, ensure that unit four becomes a cold reserve that can only operate if both units five and six are stopped. When units five and six run together at full capacity, CO₂ emissions from the plant will reach 5.5 million tonnes per annum, more than all operating blocks of the plant combined, which emitted 4.78 million tonnes in 2010.

It is therefore not possible to talk about replacing existing capacities as long as the official documentation i.e. the environmental permit allows for the continued operation of unit five alongside unit six.

Gaps in the EBRD due diligence

For these reasons we believe that the quality of the EBRD's legal, environmental and economic due diligence of the project has been called into question. Controversies over the integrity of TEŠ were already widely known among the Slovene public long before July 2010, when the EBRD approved the project¹¹.

Additionally a complaint submitted by Focus, Environmental Law Service and Bankwatch on the possible breach of the EU Carbon Capture and Storage Directive and compliance with EU 2050 climate targets is being analysed by the EBRD Project Complaints Mechanism¹².

<http://bankwatch.org/sites/default/files/Sostanj-TEŠ6-economics.pdf>

⁸ Official Gazette of the Republic of Slovenia, No. 60/2006.

⁹ Announcement of the government of the Republic of Slovenia, 23 February 2012
http://www.vlada.si/fileadmin/dokumenti/si/Sporocila_za_javnost/sev103.doc

¹⁰ The environmental permit was issued by the Slovenian Environment Agency on 16 February 2011.

¹¹ The see the examples of press articles (in Slovene): TEŠ 6 pod očesom Kosove komisije, Delo, 22.01.2010; Ekološka bomba iz Šoštanja, Dnevnik, 19.12.2009.

¹² For details see the register of the EBRD's Project Complaints Mechanism
<http://www.ebrd.com/pages/project/pcm/register.shtml>.

What now for the EBRD?

We ask the EBRD Board of Directors and the Executive Committee to suspend the disbursement of the loan until all legal investigations and non-judicial proceedings are concluded.

By allowing the project to go ahead in spite of serious corruption allegations concerning the client and questions about the integrity of the EBRD's own due diligence, the EBRD risks acting against its own procedures, as well as legislation in Slovenia and the EU.

We recommend that the EBRD abandon its involvement in this project, one that contradicts long-term EU climate targets and damages the reputation of the bank.

Sincerely,

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