

RE: EBRD's potential support for electricity utilities in the Western Balkans as part of its COVID-19 response.

TO: Sir Suma Chakrabarti

EBRD President, Chair of the Board

TO: Board of Directors

European Bank for Reconstruction and Development

May 7th, 2020

Bulgaria:

Centre for Environmental Information and Education (CEIE)

Za Zemiata, For the Earth

Croatia:

Green Action

Czech Republic:

Centrum pro dopravu a energetiku (CDE)

Hnutí DUHA

Estonia:

Estonian Green Movement-FoE

Georgia:

Green Alternative

Hungary:

National Society of Conservationists - Friends of the Earth Hungary (MTVSZ)

Latvia:

Green Liberty

Lithuania:

Atgaja

Macedonia:

Eko-vest

Poland:

Polish Green Network (PGN)

Russia:

Sakhalin Environmental Watch

Serbia:

Center for Ecology and Sustainable Development (CEKOR)

Slovakia:

Friends of the Earth - Center for Environmental Public Advocacy (FoE-CEPA)

Ukraine:

Ecoaction (Екодія)

National Ecological Centre of Ukraine (NECU)
Ecoaction

CEE Bankwatch Network's mission is to prevent environmentally and socially harmful impacts of international development finance, and to promote alternative solutions and public participation.

Dear Suma,

We are writing with regard to news¹ that the EBRD is considering support for electricity utilities in the Western Balkans as part of its COVID-19 response. Given our experience in monitoring these utilities for several years we would like to raise several issues that the EBRD needs to take into consideration when making decisions and negotiating conditions for potential loans with its clients.

1) "Montenegro: EPCG has asked for a EUR 50 million short-term facility with a two-year disbursement period"

Since it became clear that the planned Pljevlja II coal power plant is not going ahead, EPCG has clearly oriented itself towards a future based on renewable energy. This is a very positive development, however several challenges remain that we believe the EBRD needs to raise with EPCG if the company is to become well-run and resilient.

- EPCG has not yet come forward with a clear date for closing the Pljevlja coal power plant and thus ensuring the decarbonisation of Montenegro's energy sector.

- In November 2019, a consortium of Dongfang (DEC International), Bemax, BB Solar and Permonte was chosen by EPCG to carry out modernisation work on the existing Pljevlja coal power plant.² To the best of our knowledge the contract has not yet been signed, as it has been delayed by Covid-19.³ This investment raises at least three issues:

- Is it economically justified? Neither EPCG nor the Montenegrin government have publicly presented any evidence to show that it is better to invest in modernisation of the existing Pljevlja coal plant, than to close the plant once its limited lifetime derogation expires (2023 at the latest).

- On the other hand, the government started working on a district heating project in Pljevlja, where the thermal power plant is supposed to serve as a heat source after its modernisation, and eventually become a cogeneration plant. The district heating project represents an excuse to keep the plant alive, making future decarbonisation of the energy

¹ <https://balkangreenenergynews.com/electricity-bill-collection-rate-drops-up-to-30-utilites-ask-for-loans/>

² <https://balkangreenenergynews.com/chinese-montenegrin-consortium-wins-bid-for-eco-reconstruction-of-tpp-pljevlja/>

³ <https://www.vijesti.me/vijesti/ekonomija/korona-pomjera-i-rekonstrukciju-termoelektrane-u-pljevljima>

sector in Montenegro much more difficult and slower, and at the same time excluding alternative, more sustainable sources of heat for the town of Pljevlja.

- Was the tender fair? The winning consortium includes BB Solar, owned by the son of President Đukanović, and Montenegrin construction company Bemax. Bemax has several times been implicated in scandals regarding tender procedures for large infrastructure projects.⁴ Following the announcement of the tender, three bids were received, with suspiciously large differences of up to EUR 43 million. Due to the difference in price, it was suspected that the tender had been rigged, and the other two bidders (German-Slovenian consortium Hamon-Rudis and Chinese group Shanghai Electric) filed complaints and requested a review of whether all the technical requirements prescribed by the tender documentation were met.⁵
- Is the planned pollution control technology fit for purpose? The Western Balkans countries have been slow to bring their coal powered power plants in line with the minimum legal pollution control requirements under the Energy Community Treaty.⁶ Yet even those who have moved ahead in installing desulphurisation equipment, namely the Kostolac B1-2 plant in Serbia and the Ugljevik plant in Bosnia and Herzegovina have hit problems. In late 2019 the Ugljevik plant started testing its long-awaited desulphurisation equipment but in February 2020 it was reported that the investment may not be functional due to faults with the recently installed dust filters, whose functionality is a precondition for desulphurisation.⁷ The issues with the Kostolac B1-2 plant are described below in the section on EPS. Although it is clearly not practical to close all of the coal plants in the Balkans immediately, and desulphurisation investments are clearly needed at some plants, both of these examples serve as a warning that the projects need better planning.
- EPCG is planning to build a new hydropower plant, Komarnica, and has recently held public consultations on the Detailed Spatial Plan for the plant. The Plan shows that rather little is known about the biodiversity in the area and it is unclear whether there are plans to carry out more detailed research on this issue. Likewise, no public information is available on the economic feasibility of the plant, especially considering Montenegro's already heavy reliance on hydropower and fluctuating rainfall patterns.

We therefore recommend the EBRD to require:

- 1) That EPCG produces a clear and timebound decarbonisation plan, and
- 2) That the company carefully analyses whether the planned Pljevlja modernisation project is economically justified.
- 3) Further, we recommend that the EBRD takes a closer look at the tender procedure for the modernisation carried out by its existing client EPCG for the Pljevlja refit to ensure that it does not expose itself to corruption risks.
- 4) That a feasibility study for the Komarnica hydropower plant be carried out if not done already and that it be made available to the public for consultation.

⁴ For example: <https://www.vijesti.me/vijesti/drustvo/mans-sumnjici-clanove-komisije-za-kontrolu-nabavki-da-su-pomogli-bemax-u>, <https://investitor.me/2018/10/17/crnogorske-firme-od-autoputa-do-sada-zaradile-404-miliona-eura-najvise-bemax/>, <https://www.aktuelno.me/crna-gora/bemax-gradio-mala-hidroelektrana-bistrica-i-od-drzavnih-para/>

⁵ <https://www.vijesti.me/vijesti/ekonomija/kako-to-da-su-dukanovic-i-partneri-jeftiniji-za-43-miliona-infografika>

⁶ <https://bankwatch.org/publication/comply-or-close-how-western-balkan-coal-plants-breach-air-pollution-laws-and-what-governments-must-do-about-it>

⁷ <https://www.capital.ba/zbog-nemara-ugrozena-investicija-od-83-miliona-evra/>

- 5) That if the Komarnica hydropower project proves feasible, that more detailed biodiversity research be carried out at the site for the purpose of the environmental impact assessment procedure.

2) “Serbia: EPS may have access to the same type of facility and is currently considering the option; the EBRD solidarity support to EPS foresees covenants related to moving to the decarbonisation of the energy sector and reinstatement of the original PPAs, as well as adherence of EBRD’s principle of disclosure of emissions and stricter rules on the financial governance of EPS”

EPS is a long-term client of the EBRD in spite of demonstrating little to no improvement in its way of operating and doing business, either in terms of becoming a market-oriented company or in improving its environmental and social compliance.

Throughout the years EPS projects have been subject to several complaints to the PCM, the latest of which was in 2018 regarding the EBRD’s 2015 corporate restructuring loan. Our [complaint](#) alleged that the EBRD’s restructuring loan to Serbia’s energy utility Elektroprivreda Srbije (EPS) had fallen short of the bank’s commitment to sustainability, rule of law and EU standards.

The PCM’s report found evidence of harm associated with EPS operations, as well as evidence of inadequate due diligence and monitoring of the EPS Restructuring project. It showed that the EBRD had done a poor job at assessing and mitigating risks and potential harm, “*which do not adequately mirror the magnitude of some of the environmental and social challenges faced by EPS, especially as they continue to be reflected in the series of PCM complaints against EBRD operations supporting EPS*”. This is especially of concern given the bank’s long experience with EPS spanning almost two decades.

In spite of the “restructuring”, the Fiscal Council of Serbia has also found in its 2019 report that “instead of taking decisive steps towards a more efficient and sustainable operation, EPS has implemented but symbolic measures for its recovery from 2015 until now. While some decisions were even harmful.”⁸

Below we outline just a few examples of EPS’ failure to adhere to legal requirements and the Serbian authorities’ failure to make sure it does so.

2.1. Serbia, through EPS, is the only country in the region currently building a new coal power plant - Kostolac B3. The ratification of the USD 608 million loan with China Exim Bank was voted on by the Serbian Parliament in January 2015 in a fast-track procedure announced to the public less than 24 hours in advance. In 2020, the project continues to accumulate legal challenges and other issues, but EPS seems determined to go ahead with it at all costs.

Since early 2014, the Ministry of Construction, Transport and Infrastructure, has issued several construction permits for parts of Kostolac B3 and associated facilities, “salami-slicing” the project into sections which would have no function on their own. At least eight construction permits had been issued for Kostolac B3, covering at least [85% of the total project](#), by September 2019.

Two construction permits for Kostolac B3, one for the chimney and one for the water treatment facility, were issued on 14 July 2017, roughly 10 weeks before the Ministry of Environmental Protection issued its 2017 EIA Decision for the plant⁹. The EIA decision is being challenged in the administrative court, but no progress has

⁸ Republic of Serbia Fiscal Council Report, summary in English, page 7:

http://fiskalnisavet.rs/doc/eng/FC_Summary_EPS_Performance_analysis_and_recommendation_for_investments_increase.pdf

⁹ Ministry of Construction, Transport and Infrastructure of the Republic of Serbia, Decision No. 353-02-00111/2017/07 permitting the construction of the chimney of the Block B3 of the Kostolac plant. Ministry of Construction, Transport and Infrastructure of the Republic of Serbia, Decision No. 351-02-00112/2017-07, permitting the construction of the water treatment facility for Block B3 of the Kostolac plant.

been registered in the last 2.5 years. On 20 November 2017, Reuters [reported](#) that the construction works on Kostolac B3 had started.

In April 2019, the construction permit for construction of the turbine, boiler and generator for Kostolac B3 was [issued](#), representing 50% of the value of the project. News items surrounding the issuing of this permit state that, by this time, the construction of the chimney and the water treatment systems were well on their way. This could also be seen in pictures posted by the Ministry of Mining and Energy on [twitter](#).

The construction of the new unit comes with an expansion of the lignite mine - Drmno - from 9 to 12 million tonnes/year. EPS never assessed the environmental impact of this expansion, and this is subject to a [complaint](#) to the Energy Community Secretariat for breaches of the Environmental Impact Assessment Directive.

EPS has made an art of avoiding the full application of environmental legislation by “salami slicing” projects, and Kostolac B3 is a stark example of this. The matter is currently subject to a [complaint](#) at the Aarhus Convention Compliance Committee.

2.2. EPS’ Kostolac B desulphurisation project has so far failed. In an apparently forward-looking manner, with regard to the 2018 deadline for compliance with the Large Combustion Plants Directive, EPS secured financing for a complete overhaul of Kostolac B1 and B2 in 2011. A USD 293 million loan was taken by the Government of Serbia on behalf of EPS from the China Exim Bank to equip the two units with flue gas desulphurisation technology and bring the plant’s SO₂ emissions into line with the LCPD.

In 2016 Kostolac B was [the largest sulphur dioxide polluter in Europe](#) and China Machinery and Engineering Corporation (CMEC) built a desulphurisation (De-SO_x) unit that was [officially opened](#) in July 2017. However, in 2018, the plant’s emissions remained almost as high as in 2016. It is not exactly clear what the problem is, but the fact that the De-Sox has yet to start operating more than two years after its official opening raises questions about the quality of the technology used.

As recent as in November 2019 at an official Environmental Taskforce meeting of the Energy Community, a representative from Elektroprivreda Srbije (EPS), Serbia’s state-owned electric utility power company responsible for the Kostolac project stated that the desulfurization unit was not working. In addition to the EPS representative’s statement, we have the note in EPS’s annual environmental report which mentions two requests for a new construction permit for the FGD installation (the actual desulfurization unit) that were rejected twice¹⁰.

It is unclear what has happened to the previous construction permit, issued in 2015 – whether it was annulled or has become invalid or if the construction specifications have changed so much that it no longer applies. The same 2018 environmental annual report by EPS confirms that the application for a **new** construction permit for the flue gas desulfurization (FGD) installation was submitted in November 2018, well over one year after the facility was publicly declared to have the construction finished. In the interim, the application for new permit was in fact rejected twice in December 2018 and January 2019, although the ground on which rejections were issued by the Serbian authority are unknown.

The only explanation we have received so far from EPS and the Serbian Ministry of Energy and Mining is that the gypsum landfill is not ready for the De-Sox to start operation. However this excuse seems unlikely considering that it requires the conversion of an already existing open-cast mine into a landfill, which the company has had at least 9 years to prepare (counting from the date the project was financed in 2011) .

A public consultation for the Environmental Impact Assessment **updated** report of the desulphurisation unit at Kostolac B at the request of EPS was [launched](#) in December 2019 - an EIA for an already constructed facility!

¹⁰ <http://www.eps.rs/eng/Documents/energyEfficiency/The%20PE%20EPS%20Environmental%20Report%202018.pdf>, page 98

2.3. EPS just signed a preliminary agreement for yet another new coal plant - Kolubara B. [News reports](#) from March 2020, mention a EUR 385 million project for a 350MW coal unit at Kolubara, and the utility expects to commission it by 2024. The contractor - most likely selected without a tender, as allowed by a Serbia-China bilateral agreement¹¹ - is Power Construction Corp. of China Ltd., which is expected to put forward a detailed plan this month.

2.4. In the Kolubara mining basin, a new lignite field is being exploited without an EIA decision. In June 2019, the Ministry of Environment of Serbia [announced](#) a public consultation procedure on the environmental impact assessment of opening a new open cast lignite mine - Field E - by EPS, the Kolubara Branch. Public consultations were held in the affected villages - Veliki Crljeni, Barosevac, Medosevac, Zeoke - but no actual EIA decision has been issued to date. Despite lacking a permit to proceed with the works, in its promotional magazine “[EPS Energy](#) Issue 52/ October” 2019 EPS openly admits that “coal digging in Field E has started”¹². Reports from the ground also indicate a re-routing of the river Pestan and a road have taken place so that the mining machinery can be moved to Field E. This display of disregard towards national laws and international treaties should no longer be tolerated.

2.5 Another issue raised by the Fiscal Council is **EPS’ high losses in distribution** (about 13%), which it states are almost double the CEE average (about 7%). The Council estimates that around EUR 1.2 billion in investments are needed to improve the distribution network and improve metering and that this would cut distribution losses by about 500-1,000 GWh per year.¹³ The EBRD therefore needs to make sure that such investments are sped up rather than delayed as a result of the crisis. Likewise, it is now ten years since the EBRD approved financing for a **smart metering project for EPS**,¹⁴ yet no results are yet publicly visible. It is high time for the bank to let the public know what is going on and speed up this investment if it is still happening.

We therefore recommend the EBRD not to support EPS, as the history of all previous loans to the company has shown that EPS has no intention of enacting serious reforms. Any kind of financial aid to an unresponsive company such as EPS is a blank cheque to continue business as usual, continue expanding coal infrastructure and cutting environmental corners while accelerating climate change and making the lives of people in affected communities a misery.

If, however, the EBRD finds that supporting a long term client in difficult times overrides the need to show clear results from reforms and step away from coal infrastructure development, **we strongly recommend that the solidarity support offered to EPS is conditioned on:**

- Cancelling all new coal capacity plans;
- Bringing its power plants in line with the Large Combustion Plants Directive that EPS has been [breaching](#) since 2018;
- Immediately stopping unauthorised mining operations in Field E and restarting the EIA permitting process.
- Immediate adoption of a corporate level decarbonisation plan, with clear targets, deadlines and milestones for portfolio diversification.
- Stepping up ambitions on cutting distribution losses and finally implementing the smart meter project.

¹¹ On 20 August 2009 the Serbian government signed a Memorandum of Understanding with the Chinese government on economic and technical co-operation in the field of infrastructure. Annex 2 to the 2009 agreement was signed on 26 August 2013. This annex includes a clause in Article 5 that (our translation): Agreements, contracts, programmes and projects carried out in accordance with Article 4 of the Agreement on the territory of the Republic of Serbia do not carry an obligation to publish a public tender for carrying out investment works and delivery of goods and services, except if it is otherwise specified in the commercial contract from paragraph 4 of this Article.”

¹² Page 8 - http://www.eps.rs/cir/SiteAssets/Pages/energija/EPS%20ENERGIJA%2052_oktobar%202019.pdf

¹³ Republic of Serbia Fiscal Council: EPS Performance Analysis and Recommendations for Investments Increase, 19 November 2019, p.5.

¹⁴ <https://www.ebrd.com/work-with-us/projects/psd/eps-metering.html>

Regarding the **reinstatement of PPAs for renewable energy producers**, a balance needs to be found between honouring contractual commitments and ensuring that the payments are proportional and do not place an excessive burden on EPS or on final consumers.

Serbia's Fiscal Council has raised concerns that EPS currently pays more to eligible producers for renewable electricity than it charges to end-users, resulting in a net loss.¹⁵ If true, this means that the fee for renewable energy for consumers needs to be increased, along with the per-unit bills for electricity consumption, which also currently do not cover the cost of generation. It will therefore be of great importance to ensure that the amount spent on renewable energy does not rise excessively, in order to ensure affordability.

Serbia took steps to ensure this by limiting the period of applicability of its regulations on feed-in tariffs, and plants which applied for incentives after 31 December 2019 have not been able to start receiving incentives.¹⁶ However, in the announcement by the Ministry of Energy and Mining on the topic, it sounded like there are plans to merely issue another Decree and prolong the current system,¹⁷ rather than ensuring that Serbia switches to an auctions and premiums system or discontinues incentives for some technologies/sizes of plant.

A switch away from feed-in tariffs would require a change in the Law on Energy, and the Government has delayed opening this process - originally until after the elections planned for April 2020 but now the timeline is even more unclear. As well as the general lack of legal clarity on the renewables incentives regime, we are also concerned about the possibility that Serbia may do what North Macedonia did: introduce auctions for wind and solar but leave feed-in tariffs in place for hydropower and potentially other technologies, thus putting them (particularly hydropower, which has no capacity cap) at an unfair advantage.¹⁸

Therefore, **we also recommend that any support for EPS be conditioned on agreement by Serbia not to reinstate any Decrees allowing new renewable energy producers to access feed-in tariffs**. The exception may be plants below a threshold of 500 kW or lower, as required by the EU's Energy and Environment State Aid Guidelines.

3) *Albania: The government has asked the EBRD to look at the financial situation of OSHEE. Support to local partner financing institutions (PFIs) is available mostly for SMEs' needs and potentially on demand for covering partly the renewable investments owned by the PFIs.*

Regarding OSHEE, it is clear that efforts have been put in to reduce distribution losses in recent years, but they still amounted to almost a quarter of all electricity (24%) by the end of 2018.¹⁹ Therefore the EBRD's efforts need to ensure that investments into loss reduction do not suffer as a result of the current crisis.

4) *"In North Macedonia, the universal supplier had to secure loans and apply for a reduction in payment of its liabilities in April"*

The North Macedonian electricity production company ESM AD has not been specifically mentioned as being under consideration for a loan, but the EBRD should remain cautious if considering loans for the company. The

¹⁵ Republic of Serbia Fiscal Council: [EPS Performance Analysis and Recommendations for Investments Increase](#), 19 November 2019, p.55
Footnote 53. Summary of the report available in English at:

http://fiskalnissavet.rs/doc/eng/FC_Summary_EPS_Performance_analysis_and_recommendation_for_investments_increase.pdf

¹⁶ <https://bankwatch.org/blog/serbia-finally-moves-to-halt-unfair-advantage-for-small-hydropower-plants>

¹⁷ "(Physical or natural) Persons who gain the status of temporary privileged producer and/or privileged producer of electricity on the basis of an application submitted after 31 December 2019 gain the right to incentives, but cannot realise it until the issuance of a new Decree."

<https://mre.gov.rs/latinica/energetska-efikasnost-obnovljivi-izvori.php>

¹⁸ See Bankwatch and Eko-svest's complaint to the Energy Community on this topic: https://bankwatch.org/press_release/north-macedonia-complaint-challenges-unfair-subsidy-advantages-for-hydropower

¹⁹ <http://oshee.al/en/losses-in-electrical-grid-dropped-below-23-96/>

Bitola coal-fired power plant is another one of the Western Balkan power plants where there have been no significant investments in pollution control equipment and it is constantly breaching the emissions limit values and emissions ceilings (in the case of sulphur dioxide the emissions are almost ten times above the ceiling).

Although the country seems to be seriously considering a coal phase-out with the latest Energy Strategy, but also with the start of the energy transformation in Oslomej, ESM AD seems reluctant to completely withdraw from coal in the foreseeable future. In a press conference on 3 March 2020²⁰, just two months after the adoption of the Strategy, the management team of ESM AD announced that they are working on a project for a new coal mine that should extend the supply of coal for the Bitola power plant for at least 15 years in addition to the existing reserves that can support its work for 10 years.

Based on this, if the EBRD is considering support for ESM AD, we believe that it should be conditioned on the alignment of its investment plans with the green scenario of the Energy Strategy by:

- Cancelling all new coal capacity plans;
- Officialising the closure of Oslomej;
- Expanding investments in the already late just transition of the Oslomej region;
- Preparing a plan for closure of the Bitola power plant in line with the Strategy and reducing operating hours in the meantime to bring it into line with the LCPD;
- Starting the development of a just transition strategy for REK Bitola in line with the timelines laid out in the Energy Strategy.

Kind regards,
Petr Hlobil
Campaigns Director

²⁰ <https://telma.com.mk/po-predupreduvanata-od-energetskata-zednitsa-rek-ke-proizveduva-struja-od-jaglen-i-vo-slednite-25-godini/>