

PUBLIC

EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

**PROJECT COMPLAINT MECHANISM
COMPLIANCE REVIEW REPORT**

**COMPLAINT: EPS KOLUBARA ENVIRONMENTAL IMPROVEMENT PROJECT
REQUEST NUMBER: 2012/04**

**COMPLAINT: EPS EMERGENCY POWER SECTOR RECONSTRUCTION LOAN,
EPS POWER II AND EPS KOLUBARA ENVIRONMENTAL IMPROVEMENT
PROJECTS
REQUEST NUMBER: 2013/03**

PUBLIC

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Abbreviations

AoI	Area of Influence
BTOR	Back to Office Report
CP	Condition Precedent
CQMS	Coal Quality Management System
EBRD	European Bank for Reconstruction and Development
EIA	Environmental Impact Assessment
EIB	European Investment Bank
ESAP	Environmental and Social Action Plan
ESIA	Environmental and Social Impact Assessment
ESIA NTS	Environmental and Social Impact Assessment Non-Technical Summary
ESP	Environmental and Social Policy
EU	European Union
GHG	Greenhouse Gases
IBRD	International Bank for Reconstruction and Development
IESE	Initial Environmental and Social Examination
IFC	International Finance Corporation
mtpa / tpa	Million Tonnes per Annum / Tonnes per Annum
NGO	Non-Governmental Organisation
NTS	Non-technical Summary
PCM	Project Complaint Mechanism
PR	Performance Requirement
SEA	Strategic Environmental Assessment
SEP	Stakeholder Engagement Plan
TOR	Terms of Reference
WBG	World Bank Group

Executive Summary

The PCM received a Complaint, on 17 August 2012, from the Ecological Society of Vreoci and the Council of Mesna Zajenica Vreoci relating to an EBRD loan to Serbia's state-owned electricity Company, Public Enterprise Elektroprivreda Srbije (EPS) for the Kolubara Environmental Improvement Project. Following an Eligibility Assessment, a Compliance Review was commissioned in September 2013. Mr Glen Armstrong was appointed by PCM to undertake an *ad hoc* appointment to carry out the Compliance Review. On 1 October 2013 a further Complaint relating to the same Project was received from Mr Zvezdan Kalmar and Ms Natasa Djereg, representatives of the Centre for Ecology and Sustainable Development (CEKOR), Serbian Coordinators for the CEE Bankwatch Network. The Compliance Review was placed on hold whilst the eligibility of the second Complaint was reviewed. Following acceptance, the Compliance Review process was recommenced in April 2014.

The PCM Compliance Review included a review of public domain project information, EBRD internal documents and documents provided by EPS and the Complainants. Meetings were held with EBRD Environmental and Social and Investment staff. Meetings were also held with the Complainant and the Project sponsor in Belgrade and Kolubara. A site visit to various locations selected by the Complainant in Vreoci was undertaken. A site visit to project facilities at Field C, Tamnava West, Barosevac and Lazarevac was also undertaken with representatives of EPS.

EPS was formed in 1991 and is wholly owned by the Serbian Government. It is organised as a holding company with 11 subsidiaries. It is a vertically integrated power company with a monopoly in generation and distribution of electricity throughout the country. It dominates lignite mining, power generation and supply and generates almost all of Serbia's electricity. Over half of the installed capacity comes from six lignite fired power stations. 75% of this lignite comes from the Kolubara Basin, situated 50km to the south of Belgrade, with annual production in the region of 30 million tonnes and reserves of over 2 billion tonnes. The mine basin is large, well over 100 square km with pit depths up to 100m and has been under development since 1896. It is bisected north/south by the Kolubara river which splits the lignite field into its western and eastern portions. Two strategic elements of transportation infrastructure reinforce this east/west separation; the state road M22 from Belgrade towards the South and the Belgrade-Bar railroad follow the course of the river north/south. EPS and the Kolubara mining basin are therefore of national significance.

EBRD has a long standing history of investment with EPS, commencing in 2001 when an Emergency Post War reconstruction loan of €100 million was agreed. A further investment in EPS Power II was made in 2003 relating to acquisition of equipment for the Tamnava West lignite field. In 2010 EBRD invested in the Electricity Metering Project and in 2011 the EPS Hydropower Projects.

The Kolubara Environmental Improvement Project (approved for funding in 2011) includes a number of components as identified by EBRD and is intended to improve the commercial and environmental performance of existing mining and generation operations and to ensure that it

is able to implement the Kolubara B (power plant) Project (and potentially the Nikola Tesla IPP). The Project components are:

1. The installation of a coal quality management system for the basin allowing EPS Kolubara to analyse the quality of lignite as it is excavated from various different fields in the basin and blend higher and lower qualities to ensure that the lignite supplied to the power plants is of a uniform quality and within the required parameters.
2. The installation of a spreader system in the Tamnava West field will allow for the separation and handling of lignite, interburden and overburden as they are mined.
3. The acquisition of a new excavator, conveyor and spreader system for the opening up of Field C in the eastern part of the basin, increasing the output of lignite of a higher calorific value for blending.
4. Consultancy support for procurement and implementation.

The Complainants make a number of allegations of non-compliance with its Environmental and Social Policy on the part of EBRD in its assessment and due diligence of the proposed financing. These overlap somewhat and were consolidated for the purposes of the Compliance Review, in particular they allege:

1. That EBRD failed to properly define the ‘area of influence’ and the scope of its due diligence appropriately for the Project.
2. That EBRD due diligence therefore excluded the village of Vreoci from its stakeholder engagement and the application of its performance requirements.
3. That EBRD did not appropriately apply the requirements of its ESP and its GHG Assessment methodology in the analysis of the Greenhouse Gas Emissions related to the Project.
4. That EBRD should have undertaken a ‘strategic assessment’ of the Kolubara basin due to its national significance and its multiple investments at MB Kolubara.

The EBRD Management Response to the Complaints asserts that the Project was appropriately appraised and structured in accordance with the Bank’s 2008 Environmental and Social Policy and that much of the Complaints’ content is due to a ‘misunderstanding of the policy wording’ on the part of the Complainant. It further contends that the strategic rationale for the Project is adequately addressed within Serbian Government documents and that the Project will not cause any harm to the village of Vreoci as it is 8km distant from the EBRD investment. EBRD believe that resettlement of Vreoci and the environmental impacts on Vreoci are caused by the open cast pits at Field D and Veliki Crljeni and by pollution from the town’s industrial zone, none of which have been funded by EBRD. EBRD also states that the GHG impact from the Project was estimated using the Bank’s established methodology which has been extensively reviewed in the public domain.

The Compliance Review Expert’s analysis (relative to the components of the Complaint set out above) has concluded that:

- EBRD inappropriately set the boundaries of the Project area of influence and its own due diligence based on the business activities being financed.
- That EBRD did not effectively consider the capacity and commitment of the Client in scoping its due diligence and conditionality associated with the Project as required by the ESP.
- That the resettlement of the village of Vreoci and impacts upon the village should have been considered by EBRD in its due diligence of the KEIP.
- EBRD did not ensure that an assessment of GHG emissions consistent with its policy and guidance was undertaken.
- That a specific strategic assessment under the ESP was not required for the Project but that because of the position of the client and its relevance to the Serbian energy sector, this single investment was in itself 'strategic' and the due diligence should have been framed to assess all of the relevant factors.

The Compliance Review Expert therefore finds:

1. That EBRD was non-compliant in its application of the ESP general requirements and the requirements of PR1, in determining the scope of its Environmental and Social due diligence on the Project.
2. That EBRD was non-compliant with the general commitments of the ESP and PR1, 3, 5 and 10 with respect to its exclusion of Vreoci from its due diligence (and application of the PR) on the Project.
3. That EBRD was non-compliant with the general requirements of its ESP and the specific requirements of PR3 with respect to the assessment of greenhouse gas emissions on the Project.
4. That whilst no new strategic assessment was necessary for Kolubara due to the existing strategic information available EBRD should have been more strategic itself in how it applied that information to its due diligence on the Project and the conditionality and requirements therefore placed upon its client reinforcing non-compliance finding 1 above.

The Compliance Review Expert has made subsequent recommendations relating to the interpretation of the EBRD ESP consistent with the shortfalls identified in this review. It has also made recommendations on how EBRD might bridge the gap between the due diligence it undertook for the Project and what the Compliance Review Expert believes should have been necessary.

The author notes the significance of two related issues in the consideration of this report. In parallel to this compliance review EBRD has been undertaking a review of its ESP which was approved in May 2014. Some of the report recommendations may have been overtaken by events through changes to the ESP. This will no doubt be addressed in any response to the report, however the author believes it is important that it makes recommendations in the context of this Compliance Review and the ESP applicable at the time of the Project. Secondly, the author also notes the significant disruption and hardship caused by recent flooding in Serbia and in the Kolubara area, causing inundation of the mines and associated

facilities and affecting local communities. It is understood that mining operations are unlikely to recommence for some time. Again the author believes it is important that its report and recommendations reflect the situation at the time of the Complaints and investigation and do not seek to second guess changes in activity or timeline which may arise as a result of the natural disaster. The author sends his best wishes to the communities involved and the employees and management of EPS for a rapid improvement in conditions.

1 Complaints received by PCM and the Compliance Review Process

A Complaint was submitted to the EBRD Project Complaint Mechanism (PCM) on 17 August 2012 on behalf of two organisations, firstly the Ecological Society Vreoci, an association formed in 1991 and secondly the 2012 Council of Mesna Zajednica, Vreoci, an elected body representing the settlement of Vreoci, part of the Lazarevac Municipality.¹ The Complaint relates to an EBRD loan to Serbia's state owned electricity company, Public Enterprise Elektropivreda Srbije (EPS) for the Kolubara Environmental Improvement Project (KEIP).² The Complaint requested both a Problem-solving Initiative and a Compliance Review of the EBRD loan for the Project. The Complaint alleges a number of non-compliances by EBRD with its Environmental and Social Policy 2008 in its appraisal of the Project.

The Complainants believe that the equipment purchases and process improvements being undertaken by EPS Kolubara as a result of the EBRD funding, constitute part of a broader programme of investment by EPS Kolubara which will expand mining activities with associated environmental and social impacts and implications for the community of Vreoci, which have not been adequately addressed by EBRD in its due diligence. In essence the Complainants allege that EBRD defined the scope of its due diligence and area of influence (AoI) too narrowly.

The PCM Eligibility Assessment Report found that the Complaint satisfied the PCM criteria for a Compliance Review but that it did not satisfy the criteria for a Problem-solving Initiative.³ On 18 September 2013 Mr Glen Armstrong was appointed by PCM to undertake an *ad hoc* Compliance Review. Initial investigations were commenced and a site visit was undertaken in the first week of October 2013.

On 1 October 2013 a further Complaint was submitted to the PCM by Mr Zvezdan Kalmar and Ms Natasa Djereg, representatives of the Centre for Ecology and Sustainable Development (CEKOR), Serbian Coordinators for the CEE Bankwatch Network.⁴ The Complaint also relates to the Kolubara Environmental Improvement Project but also invokes alleged non compliances relating to earlier EBRD loans to the same client and the cumulative impacts of these loans.^{5 6} In November 2013 PCM requested that the Compliance Review Expert should curtail investigations whilst the eligibility of this further Complaint was assessed.

¹ Complaint by 'Vreoci' Ecological Society and the Council of 'Mesna Zajednica Vreoci' to the EBRD's Project Complaint Mechanism. 17th August 2012

² BDS 11-143 EPS Kolubara Environmental Improvement Project; Serbia; 22nd June 2011

³ Project Complaint Mechanism: Eligibility Assessment Report: Complaint EPS Kolubara Environmental Improvement Project: Request Number: 2012/04

⁴ CEKOR Complaint to the EBRD Project Complaint Mechanism. 1st October 2013

⁵ EBRD Loan 17829 EPS Emergency Power Sector Reconstruction 2001

⁶ EBRD Loan 27005 EPS Power II Project. 2003

The Eligibility Assessment Report was completed in late February 2014⁷ and found that the Complaint satisfied the criteria for a Compliance Review. It was recommended that the Compliance Review processes for both related Complaints should be combined into a single process. The Compliance Review Expert was advised accordingly in April 2014 and the process recommenced.

The Compliance Review Expert notes the significance of two related issues in the consideration of this report. In parallel to this compliance investigation EBRD has approved a revised Environmental and Social Policy (ESP 2014). Some of the report recommendations may have been overtaken by events through changes to the ESP. This will no doubt be addressed in any response to the report, however the Compliance Review Expert believes it is important that it makes recommendations in the context of this Compliance Review and the ESP applicable at the time of the Project. Secondly, the Compliance Review Expert also notes the significant disruption and hardship caused by recent flooding in Serbia and in the Kolubara area, causing inundation of the mines and associated facilities and affecting local communities. The PCM Expert understands that mining operations are unlikely to recommence for some time. The PCM Expert believes it is important that this report and recommendations reflect the situation at the time of the Complaints and investigation and do not seek to second guess changes in activity or timeline which may arise as a result of the natural disaster. The Compliance Review Expert sends their best wishes to the communities involved and the employees and management of EPS for a rapid improvement in conditions.

2 EBRD and EPS: Background and Investment History

Coal was first mined in the Kolubara basin in 1896 with the Zvidar pit. In 1952, the first open pit (Field A) was started.

The current operator, the Public Enterprise Elektropivreda Srbije (EPS), was formed in 1991 and is wholly owned by the Serbian Government. In 2005 its transmission activities were spun off and it is now organised as a holding company with 11 subsidiaries one of which is MB Kolubara. It is a vertically integrated power company with a monopoly in generation and distribution of electricity throughout the country. It dominates lignite mining, power generation and supply and despite the proposed liberalisation of the Serbian power market from 2015 under the Energy Community Treaty, it is deemed likely to remain the leading electricity company in Serbia due to high barriers to entry and its low cost generation assets. EPS generates almost all of Serbia's electricity and over half of the installed capacity comes from six lignite fired power stations. 75% of this lignite comes from the Kolubara Basin. EPS and the Kolubara mining basin are of national significance.

EBRD has a long standing history of investment with EPS.

In 2001 an Emergency Post War reconstruction loan of €100million was agreed. The project aims were to finance emergency rehabilitation and upgrades to thermal and hydro-generation

⁷ Project Complaint Mechanism: Eligibility Assessment Review: Complaint: EPS Kolubara Environmental Improvement Project (No. III): Request Number: 2013/03

plants, and to rehabilitate and upgrade the transmission system.⁸ The Project summary documents issued at the time identified a number of environmental issues:

The EBRD's loan will be used for a number of rehabilitation/upgrade projects, including the overhaul of thermal and hydro-electric generation plants, the construction of new transmission sub-stations, upgrades to a transmission line and a new transmission line. Because of the variety of investments to be financed under this loan, a number of environmental issues need to be addressed. These include:

- *air emissions;*
- *waste generation and disposal (mainly ash);*
- *water usage and discharges;*
- *storage, handling and disposal of hazardous substances (e.g. oils);*
- *worker health and safety issues;*
- *downstream water management;*
- *impact on fisheries and river ecology;*
- *loss of habitat and impact on surrounding areas (new developments);*
- *visual impact (new transmission lines);*
- *public information and consultation (particularly for new developments).*

The project aims to improve the reliability and efficiency of the power system and will provide an opportunity to replace old equipment with more efficient technology, reducing losses and potential environmental impact (air emissions, oil leakages and spillages from sub-stations etc.). The project requires an Initial Environmental and Social Examination (IESE) prior to allocating a screening category (or different categories for individual components).

The loan was processed under the EBRD 1996 Environmental Policy and Procedures.⁹ Detailed environmental documentation from the project appraisal is not readily available¹⁰ however the loan agreement requires EPS to undertake an environmental audit of the project by an independent expert, in 2002 and every three years thereafter. This is consistent with the 1996 Environmental procedures.

⁸ <http://www.ebrd.com/work-with-us/projects/psd/eps-emergency-power-sector-reconstruction-loan.html>

⁹ Environmental Policy and Procedures EBRD 1996

¹⁰ Personal communication to PCM Expert from EBRD (Confidential); PCM is bound by the EBRD Public Information Policy. Some of the most significant information that has been reviewed in the course of this Compliance Review comes from internal EBRD documents or from personal communications with EBRD staff and from meetings with EBRD staff. These documents and communications are referenced within the Report such that the source of information is clear and can be cross checked efficiently as required by EBRD staff. The fact that a document is confidential is also noted so that it is clear to all readers including complainant(s) that the documents are not available for public review. Information from those documents is mostly noted in a general review and direct quotations are only used where directly applicable and deemed critical to the analysis of compliance. No individual assignation of conclusions or comments within any document is made.

In 2003 the EPS Power II Project was approved.¹¹ The financing constituted a €50million sovereign guaranteed loan co-financed by EIB. This project was given an Environmental Categorisation 'A' and included the modernisation of equipment installed at the Tamnava West lignite mine (also part of the 2011 Kolubara Environmental Improvement Project) and upgrade of the Power System Controls and internal communications. One objective being to 'increase lignite production' but with conditions attached:

The improved control and communications system is a pre-condition to Serbia's full membership in the Union for the Coordination of Transmission of Electricity (UCTE) and is key to the regional network. Further the loan will be conditioned on overall sector reform as well as those specific to the mining and transmission sectors.

€35million of the funding was allocated to the lignite mining operation. An Environmental Impact Assessment (EIA)¹² was produced for the mining component and the lignite mines using funding from the European Agency for Reconstruction. The EIA addressed the investment in Tamnava West field through provision of a bucket wheel excavator and conveyor facilitating a production increase up to 12mtpa. It identified a number of critical issues including but not limited to:

- The criticality of resettlement activities, particularly their timing, relating to a number of villages – but particularly Kalenic.
- The deterioration in the quality of services and infrastructure affecting the welfare and quality of life of inhabitants.
- The impact of pollution sources, particularly emissions, from the CB Kolubara Industrial complex.
- Risks associated with groundwater pollution due to its use for drinking water extraction.
- The overarching need for an environmental monitoring system for EPS industrial activity which was non-existent.

Once again EBRD required within the loan agreement that EPS undertake an environmental audit of the project by an independent expert in 2004 and every 3 years thereafter.

In 2010 the EPS Electricity Metering Project¹³ was approved constituting a sovereign guaranteed loan of €40 million in parallel with a similar loan of €40 million from the EIB (in total €80 million) to finance the purchase and installation of modern electricity meters and the associated infrastructure and software in the Serbian electricity distribution system. The project targeted reducing the level of electricity losses in the network over the project implementation period.

¹¹ <http://www.ebrd.com/work-with-us/projects/psd/eps-power-ii.html>

¹² European Agency for Reconstruction: Cards Framework Contract AMS/451/Lot No6: Environmental Impact of a Development Project to improve operations and production in Serbian coal mines

¹³ <http://www.ebrd.com/work-with-us/projects/psd/eps-metering.html>

This was the first EBRD investment in EPS under the 2008 ESP and the environmental and social due diligence as reported in the disclosed project documentation consisted of an Environmental Audit of the EPS assets and management capability around the Bank's Performance Requirements (PRs) and an Environmental Analysis of the proposed investment programme. Audits required by the 2001 and 2003 loans had not been commissioned by EPS and completion of the audits was made a condition precedent to disbursement of the loan. It is understood¹⁴ that EPS voluntarily decided to expand the scope of these audits to all of its subsidiaries (11 separate operating companies), that EBRD provided input to the terms of reference for these audits, but that they were not a requirement of the loan.

In 2011 the EPS Hydropower Plants project¹⁵ was approved providing financing to EPS in the form of a €45million sovereign guaranteed loan (total project cost €54million) to rehabilitate 15 existing small hydro power plants across Serbia, and to add electricity generation capability to another seven existing dams. The project objective was to extend the lifetime of the existing small hydropower plants and increase generation from renewable energy sources through increases in the capacity of the existing plants and the addition of further generation capacity to the other dams. Business activities funded included setting standards for corporate governance and business conduct (including the establishment of a new subsidiary for renewable energy) and a reduction in carbon intensity. It was anticipated that the project would act as a demonstration of the viability for other hydro projects in Serbia and facilitate technical skills transfer.

The project was categorized B under the 2008 ESP, principally because all but one of the dams had been in place for many years (the project involved rehabilitation of 15 existing small hydropower plants and creation of seven new ones by adding hydropower generation capacity to seven existing dams). One dam of the twenty-two, not owned by EPS, was completed only in 2010 and the reservoir had not yet been filled at the time of the EBRD Board approval.

The Environmental and Social Action Plan (ESAP) as well as requiring EPS to implement best practices in the project construction also required the Company to upgrade its corporate systems for managing environmental, health and safety, and social issues. The dam that had been constructed (Selova), was not owned by EPS and was regarded by EBRD as 'not part of the Project per se'. It was however defined as within the 'Area of Influence', as defined in the ESP. It was acknowledged that the owner's closing of the dam and then clearing and filling the reservoir could have potentially significant impacts in terms of resettlement and land acquisition, dam safety and associated risks to the downstream community, and biodiversity impacts from clearing forest and flooding a total of 382 hectares. As a result EPS was required to work with the dam owner to ensure that the Selova SHP project would meet the Bank's Performance Requirements 4 (community safety), 5 (resettlement and compensation), and 6 (biodiversity). Though not regarded as part of the project but part of the AoI EBRD required application of its EPS and Performance Requirements.

¹⁴ Personal communication from EBRD (Confidential)

¹⁵ <http://www.ebrd.com/work-with-us/projects/psd/eps-hydropower-plants.html>

On July 26th 2011 EBRD approved financing of the Kolubara Environmental Improvement Project to which this PCM review pertains and the details of which are discussed throughout this report.

Further commentary on the emerging significance of environmental and social governance factors within the investments and their relevance to this compliance investigation, is provided in section 6.

3 The substance of the Complaints

For the purposes of this document the two Complaints under review are referred to in the short form: Complaint 1: ES Vreoci and Complaint 2: CEKOR.

3.1 The Kolubara Mining Basin

Some description of the Kolubara mining basin is important to place the Complaint(s) in context. The basin is of major strategic importance to Serbia. It is located 50km south of Belgrade in a lowland area with an average elevation of 205metres above sea level. It generates 75% of all lignite in Serbia with annual production in the region of 30 million tonnes and reserves of over 2 billion tonnes. This lignite when combusted at the Kolubara, Nikola Tesla and Morava power plants constitutes over half of all Serbian electricity production. The land area is large, well over 100 square km. The mine basin is bisected north/south by the Kolubara River, a tributary of the River Sava, which splits the lignite field into its western and eastern portions; this is important when discussing the operation of the field. The two strategic elements of transportation infrastructure reinforce this east/west separation. The state road M22 from Belgrade towards the South and the Belgrade-Bar railroad follow the course of the river north/south. The depth of the open pits is determined by the thickness of the lignite seams which are highly variable, but generating pit depths of up to 100m.

3.2 Complaint 1: ES Vreoci

The central issue within this Complaint is the relationship between activities in Kolubara mining basin and the village of Vreoci.

3.2.1 Vreoci and mining of lignite at Kolubara

The Complaint provides significant information on the geographic, geo-spatial and socio-economic relationship between the village and the mining and related operations. These are particularly illustrated by Map 3¹⁶ and Map 4¹⁷. Vreoci is the largest settlement in the municipality of Lazarevac after the Town of Lazarevac itself. The first written record of the town dates from 1528. At the 2002 census there were 3210 residents living in 1088 households. Its economy is almost wholly dependent on mining and related activities with the

¹⁶ Map 3: Social functions in Vreoci and its Industrial Zone: Complaint 1 ES Vreoci: From Centre for Regional Research 2012

¹⁷ Map 4: Sources of Pollution and amounts of emissions in Vreoci: Complaint 1 ES Vreoci: From Centre for Regional Research 2012

only other economic activity of any significance being agriculture, also impacted by progressive mine expansion.

Exploitation of the Kolubara lignite basin has caused encroachment of mining activities and has incrementally forced Vreoci into a linear alignment along the Stepojevac-Lazarevac road, directly between the Western and Eastern elements of the field. The juxtaposition of closed and operating pits to Vreoci is important to recognise. Annex 1 of the EBRD Board Paper for the Kolubara Environmental Improvement Project¹⁸ demonstrates the relationship of the eastern and western fields and the central infrastructure spine on which Vreoci is located. However this map does not include the 'South Field' which is a technically difficult future field (due to the dip of the coal field) located very close to the railway line and therefore close to Vreoci. EBRD advises that the location of South Field was however addressed in the Board information session. The proposed location of South Field, which further encroaches onto the North/South infrastructure spine is illustrated in Map 2¹⁹ within the Complaint.

Vreoci also provides the 'industrial hub' of the basin due to its position on the north/south infrastructure spine. This hub is located south of the Vreoci settlement. It comprises numerous operations associated with mining such as extensive coal processing facilities (Kolubara Prerada), equipment manufacture and repair (Kolubara Metal) and many other service related activities. Other industrial activities are located 7km to the north of Vreoci in the settlement of Veliki Crljeni, including the Kolubara power station and Kolubara Universal.

Most significantly with respect to Vreoci it has been planned for many years that the development of South Field and the expansion of Field D, along with realignment of the Kolubara River, will require the complete resettlement of the village.

3.2.2 Components of the Complaint

The Complainant alleges non-compliance with Performance Requirements 1 (Environmental and Social Management) and 3 (Pollution Prevention and Abatement) by EBRD in its due diligence on the project. It further alleges that the actions of the EBRD Client result in non-compliances with Performance Requirements 4 (Community Health, Safety and Security), 5 (Land acquisition, Involuntary Resettlement and Economic Displacement) and 10 (Information Disclosure and Stakeholder Engagement). Particular significance is given to alleged non-compliance with PR5.

The Complaint provides a detailed commentary (from the Complainants' perspective) on the process of resettlement as applied to Vreoci by MB Kolubara and EPS. It also provides detail on the sources, locations and impacts of environmental pollution in Vreoci, some but not all of which are associated with the delayed implementation of the resettlement programme and the progressive encroachment of mining activity. Further concerns are raised about hardships

¹⁸ Annex 1; Map of the Kolubara Mining Basin: At P26 Serbia: EPS Kolubara Environmental Improvement Project

¹⁹ Map 2: Exploitation Area of Kolubara Lignite Basin: Complaint 1 ES Vreoci: From Centre for Regional Research 2012.

induced by the failure to continue investment into core public services due to the delayed resettlement programme.

It is neither appropriate nor possible for this Report to opine upon the details of the resettlement process. There are strongly held, if not entrenched positions on both sides of the issue. The EBRD role in this is discussed elsewhere in this Report. However the Compliance Review Expert recognises, without assignation of blame, that delays in the resettlement process have caused uncertainty and distress to residents of Vreoci and the propagation of unacceptable environmental conditions for the remaining residents.

With respect to PR1 (Environmental and Social Appraisal and Management) and more specifically PR 1.5, the argument set out is that the EBRD investment was part of a modernisation of EPS Kolubara mining operations, thereby directly contributing to the requirement to resettle Vreoci, and with associated direct and indirect environmental impacts on the community.

The Complainants claim the Bank failed to follow its policies by limiting the scope and area of influence of the Kolubara Environmental Improvement Project. They believe that it should be defined more broadly, beyond the footprint of Fields C and Tamnava West where the EBRD-financed equipment will be located. They claim this Category A Project is part of a larger set of current and future investments linked to EBRD's broader investment programme in MB Kolubara and the extension of the mining and power complex. They maintain the current Project and its area of influence should not be looked at in isolation but rather defined according to a wider lens that justifies delineating the area of influence more broadly. The consequences being that EBRD failed to consider the associated environmental and social impacts of the Project as it relates to the settlement of Vreoci, and thereby failed to require adequate consultation with Vreoci stakeholders.

Of these associated impacts the Complainants allege non-compliance due to the environmental degradation affecting Vreoci, the resettlement of Vreoci, and a declining quality of life punctuated by a lack of public services, as people await resettlement. The Complainant believes that EBRD has inadequately considered and appraised these risks in light of its significant investment in the Client's operations since 2001. The Complainants further believe that all of the environmental impacts should have been assessed and addressed by EBRD under Performance Requirement 3. Principally they cite the degradation of air, water and soil from the open-pit mines with the most important sources being the ash and slag dumping from the mines. In addition the industrial zone at the south edge of Vreoci where operations associated with MB Kolubara are located; contamination from the wastewater treatment plant for the industrial zone; dust from transportation of coal etc.

The Complainants also argue that the groundwater and hydrologically connected surface waters have been polluted from the open-pit fields, the industrial zone and wastewater treatment plant, and that groundwater levels in Vreoci have been lowered because of the extensive mining, harming the well-water supply in Vreoci. They argue the Project failed to address the increased need for fresh water to be imported from outside the affected area.

References in the EIAs for Field C are cited that describe potential direct and indirect harm on Vreoci to support these arguments.

A similar argument is asserted with respect to the Vreoci resettlement. They believe EBRD's assessment process inadequately considered resettlement and relocation problems in Vreoci that they believe are associated with the broader definition of the project which would have been appropriate. The Complaint also claims that the Bank promotes a climate-damaging approach to energy investments by enabling the expansion of coal-fired power plants in Serbia.

3.2.3 *Resettlement at Vreoci*

It has been clear since 2007²⁰ that Vreoci will be resettled due to the significant amount of coal underlying the settlement, the government's support of the mine's expansion and the institutional arrangements put in place by the Government and the Municipality of Lazarevac. There have allegedly been significant delays and disagreements over the quality of what has ensued. The main goals of the community members during negotiations with the Government were the resettlement of the whole community in one location in Lazarevac municipality, establishing fair compensation procedures and agreeing the process for removal of the local cemetery. The 2008 General Regulation Plan adopted by the City of Lazarevac and the EPS 'Programme Guidelines for the Relocation of the Settlement of Vreoci' were apparently both supported by the community but it is alleged that EPS did not respect the timeframe prescribed for collective resettlement or the methodology for determining fair prices for expropriation purposes, resulting in inadequate compensation. Both of these issues had allegedly been agreed over many years of discussion and negotiation. Delays in the process and detailed individual negotiations have resulted in fragmented resettlement of the community, negotiating and compensation approaches which have allegedly placed residents under duress and in some cases allegations of malpractice.

Due to delays, remaining residents are living in an uncertain environment with significant mining activity and pollution surrounding the settlement and with a lack of public services. The manner in which the cemetery was relocated has been a matter of significant contention and public unrest and allegedly in contradiction of the expressed wishes of many Vreoci residents with discrepancies in application of the agreed methodology for counting graves resulting in alleged 'forced exhumations'. All sides seem to agree on one thing; that the resettlement process has been delayed and will not be completed by 2014 as promised.

EPS set out their own perspective on the resettlement in meetings with PCM.²¹ They described the inherent tensions in resettlement programmes scheduled 5 years or more in advance and the direct agreements entered into with the Vreoci community which acknowledged the options to relocate collectively or for individual resettlement. They maintained that it remained the objective to complete the resettlement programme for Vreoci

²⁰ 2007 Resettlement Programme: Programme for setting the framework for the relocation of the settlement of Vreoci

²¹ PCM meetings with EPS and RB Kolubara, Belgrade and Kolubara, 2 October 2013 (Confidential)

by 2015 (and that this will require significant additional effort) but acknowledged also that the absence of funding and lack of capacity had caused uncertainty and delays in the process. They also explained that 30% of their budget was spent on expropriation (to demonstrate its significance to the business and priority as an issue). They also believe that changes in expectation on the part of a small proportion of the population (5-6%) who had agreed compensation levels but then chose to take the matter to court had caused problems.

Complainants believe that the EBRD definition of the Project should have included its impacts on Vreoci and that therefore it has violated provisions of Performance Requirements 3 and 10 related to resettlement and meaningful consultation, arguing that it has allowed the Client to abandon locally developed plans to exhume and relocate the cemetery. They assert linkages between this Project and EBRD's broader investment programme and effects of the mine's extension on the lives of the people of Vreoci, and the need for long-term engagement with stakeholders in Vreoci under the ESP. They argue that the Bank should look through a much wider lens in determining the requirements for stakeholder engagement, and argue this was insufficiently addressed in EBRD's appraisal process. They also claim the Project failed to include an effective community grievance mechanism, though a grievance mechanism was included in the Stakeholder Engagement Plan disclosed on the EPS and EBRD websites.

3.2.4 Complaint Key Issues for Analysis

- Was the 'area of influence' appropriately defined by EBRD in terms of the Kolubara Environmental Improvement Project.
- Were the EBRD Performance Requirements appropriately applied with respect to the Project. In particular should EBRD due diligence and performance standards including stakeholder consultation, have extended to the village of Vreoci.
- Was the EBRD Environmental and Social Policy (in its various revisions) appropriately applied through each of the multiple investments? Should the multiple investments by EBRD at Kolubara have resulted in a broader more holistic view of environmental and social impacts within the whole basin – or were the investments so discrete in their scope and impact that a focus on localised issues was justified.

3.3 Complaint 2: CEKOR

The underlying premise of the CEKOR Complaint is also based upon the EBRD approach to defining the 'area of influence' of the Project. The Complainants believe that Performance Requirement 1, and in particular 1.6, make it incumbent upon EBRD to have analysed the cumulative impacts of the development of the Kolubara basin and the whole mining/energy/industrial complex.

The Complainants draw attention to the requirement (PR 1.9) for a regional, sectoral or strategic assessment under exceptional circumstances and assert that the significance of the Kolubara complex and its impacts, plus the long term involvement of EBRD through multiple investments should have resulted in such an assessment. The complexity of ongoing field development at Kolubara and the inter-relationship of mining and energy production activities and efficiency improvements are developed within the complaint to support this view.

The Complaint then focusses on two specific themes.

3.3.1 Greenhouse Gas Emissions

The Complainants believe that the EBRD approach to the assessment of GHG emissions was defective in a number of respects. Firstly, that they failed to establish an appropriate baseline against which emissions occurring as a result of the Project could be appropriately considered. Secondly, they believe that directly related changes in energy production capacity (Kolubara B) have not been addressed (whether or not this Project would be funded by EBRD) and, thirdly, that the boundaries of the Project assessment were therefore defined too narrowly. The Complaint provides some detailed analysis in support of these assertions.

A further substantive and important point raised in support of this analysis relates to the application of the EBRD greenhouse gas guidelines.²² The Complaint asserts that there is a potential conflict between these guidelines and the EBRD ESP in the establishing the Project boundaries for the analysis of GHG emissions.

3.3.2 Social Impacts

The Complainant believes that resettlement activity undertaken in conjunction with the Tamnava West expansion (under the EPS II project 2003) was not completed according to appropriate standards and that this has undermined public confidence in the EPS process. In addition, they believe that multiple investments by EBRD have established in the public consciousness a co-responsibility on EBRD for these failures.

Specifically the Complainant believes that the complex and inter-related field expansions which have been associated with EBRD investments means that the village of Vreoci and its environs should have been included in the 'area of influence; for the Kolubara Environmental Improvement Project. The underlying analysis for this assertion discusses issues such as progressive field expansion facilitated by EBRD involvement, the cumulative effects on environmental issues such as water and air pollution and the alleged 'falsehood' of seeking to restrict the application of EBRD requirements to specific activities at Field C and Tamnava West.

The Complainant also provides significant additional material alleging non-compliances with the EBRD ESP which would be particularly relevant if, in the Complainant's view, EBRD had not sought to artificially constrain the area of influence of the Project.

3.3.3 Complaint Key Issues for Analysis

- Did EBRD appropriately apply the requirements of its ESP and its GHG Assessment methodology in the analysis of the Project.
- Was the 'area of influence' of the EBRD analysis of the Kolubara Environmental Improvement Project appropriately defined in terms of impact of this EBRD investment, and the cumulative effects of multiple EBRD investments.

²² EBRD Greenhouse Gas Assessment Methodology Version 7, 6 July 2010: EBRD Methodology for Assessment of Greenhouse Gas Emissions: Guidance for consultants working on EBRD-financed projects

- If the ‘area of influence’ should have included the village of Vreoci, would this have required EBRD to more extensively assess a range of issues ranging from resettlement standards at Vreoci to individual and cumulative environmental and social impacts on the village from MB Kolubara operations.

3.4 The Focus of the Compliance Review

The outputs from this analysis of the two Complaints relating to the Kolubara Environmental Improvement Project have been integrated to provide a consolidated focus for this compliance review. Central to the analysis is an understanding of what ‘The Project’ is as this determines the requirements placed upon EBRD under its ESP. This issue is therefore addressed first. It is then important to deal with the issues sequentially, because the ‘area of influence’ associated with ‘the Project’ determines the validity of further elements of the Complaint. The issues are therefore addressed as follows:

1. What is ‘The Project’?
2. Was the ‘area of influence’ and the scope of its due diligence appropriately defined by EBRD in terms of the Kolubara Environmental Improvement Project, having regard to the definition of the Project?
3. Based on the above - should EBRD due diligence and performance requirements including stakeholder consultation, have extended to the village of Vreoci?
4. Did EBRD appropriately apply the requirements of its ESP and its GHG Assessment methodology in the analysis of the Greenhouse Gas Emissions related to the Project?
5. Should EBRD have undertaken a ‘strategic assessment’ of the Kolubara basin due to its national significance and its multiple investments at MB Kolubara.

4 EBRD Management Responses

In their Responses^{23 24} to the Complaints, EBRD Management has asserted the following position with respect to the key issues from the Complaints, identified for analysis.

1. That the Kolubara Environmental Improvement Project was appropriately appraised and structured in accordance with the Bank’s 2008 Environmental and Social Policy. This included independent review of the Environmental Impact Assessments prepared by EPS for Field C and the Tamnava West expansion, and preparation of a gap analysis to identify additional EBRD requirements and undertaking a detailed assessment of the Project against each of the EBRD Performance Requirements.
2. That much of the Complaint(s) content is due to a ‘misunderstanding of the policy wording’ on the part of the Complainant. In particular that the elements of a Project deemed to comprise the ‘area of influence’ are not ‘subject to the performance requirements’.

²³ Management Response to a PCM Complaint on Serbia: EPS Emergency Power Sector Reconstruction Loan (17829), EPS Power II (27005) and EPS Kolubara Environmental Improvement Loan (41923).

²⁴ Serbia: EPS Kolubara Environmental Improvement (41923) PCM: Management Response.

3. That the review of the Project included appropriate analysis of strategic documents including the 2008 SEA undertaken by the Serbian Government obviating the need for any further strategic assessment. More specifically that there is no requirement for an SEA within the ESP.
4. That public consultation and most of the land acquisition and resettlement had taken place according to Serbian national requirements in advance of EBRD involvement. That all appropriate documents relevant to the EBRD investment were properly disclosed.
5. That the EBRD funded Project will not cause any harm to the village of Vreoci as it is 8km distant and will have extensive environmental management and monitoring requirements attached to it. In particular ground water levels have been historically lowered due to the extensive mining activities taking place, including Field D which lies between Field C and the village.
6. That the resettlement of Vreoci and the environmental impacts on Vreoci are caused by the open cast pits at Field D and Veliki Crljeni and by pollution from the town's industrial zone, none of which have been funded by EBRD. That EBRD has nonetheless voluntarily discussed the issues raised by the Complainants with EPS including meeting with local groups under the auspices of a local consultant. That EBRD would be prepared to engage again on a 'best efforts' basis.
7. That EBRD has consistently applied the contemporary requirements of its ESP throughout its multiple investments in EPS.
8. That the Bank has included the activities of EPS at Vreoci within its 'wider' appraisal of EPS. In addition that EPS has agreed to commission independent environmental audits of each of its subsidiary companies. This included an EHS audit of the whole of the Kolubara basin and a resulting action plan to address the issues identified, with a follow-up audit due in 2014.
9. That the GHG impact from the Project was estimated using the Bank's established methodology which has been extensively reviewed in the public domain. That EBRD is convinced that the Project will result in a net GHG emission reduction in the region of 200,000 tonnes per annum. That baseline GHG emission data is available in a range of public domain documents.
10. That broader EBRD investment strategy in Serbia is consistent with the development of renewable energy and improved energy efficiency.

A number of these assertions and the difference in position between Bank Management and the Complainant are central to the compliance review analysis and are reviewed in detail later in this Report.

5 The Compliance Review

5.1 What is ‘The Project’?

Central to this analysis is a clear understanding of what ‘the Project’ is. In the ESP the ‘Project’ is defined as the ‘business activity for which financing is sought.’²⁵

EBRD’s analysis of what the Project comprises – i.e. what ‘business activities’ are being financed is set out in its Board Paper. The Board Paper described the project as a substantial investment in EPS’ lignite basin, comprising installation of a coal management system to analyse quality of the excavated coal; installation of a spreader system in the Tamnava West field to allow for separation and handling of the mined lignite; and consultancy support for procurement and implementation. The project was said to be initiated by EPS to improve the commercial and environmental performance of its existing operations and in preparation of the Kolubara B project (and potentially the Nikola Tesla IPP).

The investment is clearly intended to provide a ‘substantial investment’ into EPS operations across the Kolubara basin, through both the acquisition of field specific equipment and the acquisition of a basin wide coal quality management system (CQMS) which will facilitate the supply of blended higher quality lignite. The CQMS is fairly basic technology and has a limited physical footprint in its own right, however this coal management component of the investment is noted to be of particular significance in terms of the benefits it will bring in supplying lignite of consistent calorific value to existing power plants (reducing shutdown periods and boiler damage) and in allowing EPS to meet contractual lignite supply commitments to the proposed Kolubara B Power Plant, which will be the first significant private sector investment into the Serbian power sector. The CQMS is also a significant financial component of the investment.

Component	Cost (€m)	%
Excavator, conveyor, spreader, and power supply for Field C	€77.2m	44%
Spreader system for Tamnava West	€19.6m	11%
Coal quality management system	€42.3m	24%
Other Costs (Consultants, Contingency, Tax)	€37.9m	21%
Total	€177.0m	

The rationale presented to the EBRD Board sets out the basis for a parallel financing with KfW, forming the ‘*most significant investment in the lignite mines.*’ The three investment components (plus the consultancy component) are described as ‘*closely integrated and inter-dependent.*’ The paper concludes that ‘*the project is crucial both for the future development of the mine, and the present and planned power plants, including the proposed Kolubara B Power plant.*’

²⁵ EBRD ESP Para C17

The transition impact of the Project is based around setting standards for business conduct (including through the adoption of environmental and social standards), the introduction of private ownership providing an essential enabling condition for Kolubara B and the development of the energy market in the application of cost reflective tariffs.

The Project is deemed supportive of key strategic objectives for the Bank in terms of its Energy Strategy²⁶ and its role within Serbia.²⁷ It is clear that the Project was seen as of some significance for EPS, Serbia and for the Bank in furthering its transition objectives within the Country and sector. The ‘business activities’ funded by the Project are quite broadly drawn in terms of process efficiencies, environmental improvement and in preparing the business for private investment in the sector and achieving contractual integrity. By EBRD’s own analysis ‘The Project’ therefore includes the specific field based investments in equipment at Field C and Tamnava West, basin wide improvements in the quality of lignite produced to improve operational efficiency and to underpin supply contracts which would facilitate future investment in and construction of power plants.

Notes from the Board briefing indicate that Directors and advisors raised a number of questions.²⁸ Directors specifically requested confirmation that the Project would not increase lignite production or power generation capacity, which was provided by Management. The issue of resettlement of Vreoci was also raised, in terms of the public consultation process, the status of negotiations and the situation regarding the cemetery. Further specific inputs from Directors clarified that there was currently no final decision on construction of Kolubara B, but that it would in any case replace obsolete and inefficient capacity. They also acknowledged that finding a satisfactory solution on social issues was challenging and that EBRD should deliberate on the limits of its responsibility and involvement in solving issues such as resettlement at Vreoci that are not ‘part of the EBRD.’

Specific questions relating to environmental and social issues were raised at the board information session.²⁹ These included issues relating to resettlement at Vreoci (asserted not to be part of the EBRD project), EPS commitment to meet prior covenants to undertake environmental audits, the methodology for calculation of reduced CO2 emissions, the relationship to the proposed Kolubara B development and the projection for future lignite production (slight increase from 2014).

Notes of the board proceedings³⁰ note that the board requested regular updates on the implementation of environmental and social action plans. EBRD Management advised that social and environmental experts would visit the region to seek to facilitate a solution to outstanding resettlement issues ‘though these were not directly related to the bank.’

²⁶ EBRD Energy Operations Policy BDS/06-093

²⁷ EBRD Strategy for the Republic of Serbia BDS/SB/07-01

²⁸ EBRD Internal e-mail July 14 2011 Board Information Session on EPS Kolubara Project 11th July (Confidential)

²⁹ Directors Advisors Questions, Board meeting 12th July 2011: Serbia: Kolubara Environmental Improvement Project (BDS11-143) (Confidential)

³⁰ Serbia: EPS Kolubara Environmental Improvement Project (BDS11-143) Minutes and Summary Record of Proceedings (Confidential)

EBRD Policy Commitments

EBRD's required approach towards 'The Project' are set out both in the specifics of the performance requirements but also in the more generic commitments of Environmental and Social Policy. For example the policy:

- Recognises that the 'transition to a market economy and sustainable development are inextricably linked'
- That '(EBRD)...expects clients to assess and manage the environmental and social issues associated with their projects so that projects meet the performance requirements'
- That the Bank will 'enhance the assessment of transition impact of proposed projects to more explicitly reflect the systemic sustainable dimension of transition and the benefits of a strategic approach in this area'
- The Bank will 'consider whether the project can be expected to contribute to the development of the host country and to broadly benefit project affected communities'

The clear intent is that EBRD sees sustainable development as intrinsic to its transition mandate, that it will be strategic in its thinking to that end and that benefits to the host country and project affected communities are important elements of its analysis.

EBRD appraisal of the Project is required to address three key elements:

- The environmental and social impacts and issues associated with the project and compliance with the Performance Requirements over a specified timeframe
- The capacity and commitment of the Client to address these impacts in accordance with the policy
- The role of third parties in achieving compliance with the policy.

It is therefore reasonable to expect that EBRD would draw upon its long history of working with EPS in assessing the second element of the appraisal and that the continuity of requirements on previous projects (particularly those processed under the 2008 ESP) and the implementation performance in previous commitments.

5.2 EBRD and EPS

The extensive history of EBRD working with EPS, based upon disclosed project documentation is set out within section 2 of this report. The 2008 ESP makes it clear (paragraph 15) that an analysis of the client's commitment and capacity to implement the performance requirements is required. It is not within the remit, nor is it the intention of this Compliance Review to express any opinion on the performance of EPS. However the role of EBRD in assessing that capacity and commitment is directly relevant.

The Kolubara Environmental Improvement Project (EPS-KEIP) Board report notes that while the Client has made progress in terms of environmental management, it has not complied with prior covenants relating to environmental action plans and environmental audits. It notes that during monitoring in 2008, the coal mines were found to have the lowest levels of environmental compliance in the EPS group. The report also notes the Bank's significant

investment in technical support to EPS in improving its performance. As far back as 2003, the EIA for the EPS II loan identified potential issues around the ongoing provision of public services to remaining residents, impacts of emissions from the industrial areas and the potential for groundwater pollution to impact domestic use. Perhaps most significantly it identified the pressing need for an environmental management system in EPS which was effectively ‘non-existent’. Notably also, the transition impact of the KEI project is partially based around setting standards for business conduct, including through the adoption of environmental and social standards.

The Board report does not mention specifically that the completion of Environmental Audits of project related facilities (to be repeated 3 yearly thereafter) was an environmental covenant going back to the original Emergency Power Reconstruction loan in 2001.³¹ The 2003 Project EPS-Power II required an environmental audit of ‘The Project’ to be undertaken every 3 years, commencing in 2004, with the Environmental Action Plan to be amended to take account of any matters arising. The Compliance Review Expert understands that these audits were substantially delayed such that their completion was made a condition precedent to disbursement of the 2010 EPS Metering Project. As previously noted, EPS determined during this period to expand the audit programme to all of its subsidiaries. Internal EBRD documentation³² indicates that these audits were undertaken in 2011 and were presented to EBRD in March 2012. At the time of the EBRD Board meeting relating to EPS-KEIP the 2010 EPS metering project had not been disbursed. EBRD Management has advised that this was unrelated to the conditions precedent related to the environmental audits and that written confirmation had been received from EPS that the audits would be carried out, prior to the KEIP Board meeting.

The Compliance Review Expert recognises that these audits³³ constitute a significant advance in the EPS approach to environmental management and were undertaken partially at the volition of, and with the significant support of EBRD.

The EBRD Management Response to the CEKOR Complaint states that...‘*in relation to the scope of appraisal (of the EPS-KEIP) EPS agreed to commission independent environmental audits of each of its subsidiary companies.*’ It goes on to note that this extensive work was presented to EBRD in 2012. This is correct in relation to the broader programme of audits agreed between EPS and EBRD, as set out above, audits of existing EBRD investments were an outstanding unfulfilled commitment going back as far as the 2001 and 2003 investments, the scope of the audits having been expanded subsequently. Also, one of the key requirements under the 2011 Hydropower Projects was for the Company corporate Environment, Health and Safety and Social Management systems and capacity to be upgraded. This project was processed in parallel with the KEIP investment.

³¹ EBRD communication following PCM request for information relating to environmental covenants (Confidential)

³² Back to Office Reports 23.09.2010, 22.2.2011, 5.3.2012, 14.9.2012 (Confidential)

³³ Environmental Audit of Locations & Facilities, Tekon & Dekonta, 2011

The Compliance Review Expert recognises that improvements in environmental and social performance require significant investments in facilities, processes and capacity and that this is highly challenging within the environment in which EPS operates. It also recognises the significant efforts made by EBRD staff to align investments with improvement in environmental performance. However past performance is a material issue in assessing client commitment and should have been a major consideration in the way that EBRD framed its due diligence and approach to the EPS-KEIP investment.

Multiple investments in EPS and associated due diligence had identified the need for improvements in overall environmental and social governance and management issues across the Kolubara basin consistent with paragraph 15 of the policy and PR1. Even though such enhancements were central to the KEI Project, EBRD focussed its due diligence and application of the PRs narrowly on mining activities at Field C and Tamnava West. At the same time EBRD was providing technical support for completion of the 2011 audits and broader company-wide EMS and OHS systems but this was not directly linked to conditionality associated with the KEIP investment.

5.3 Project Area of Influence (AoI) and the scope of due diligence

The key requirements relating to AoI are set out within the general policy statements and within Performance Requirement 1 – Environmental and Social Appraisal and Management which sets out the broader objectives and scope of the EBRD approach. The Compliance Review Expert believes that the approach to AoI must take place within an analysis of both the broader intent of the policy and the specific Performance Requirement.

The EBRD ESP requires that ‘Environmental and Social Impacts and issues will be appraised in the context of the project’s area of influence.’³⁴ PR1.6 also provides further clarity on what may be included in the area of influence. In short-form, these are:

- Assets and facilities owned by the client which are to be financed
- Supporting or enabling activities and facilities
- Associated facilities or businesses not funded by EBRD but whose viability is directly based upon the project
- Assets which are committed to EBRD as part of the security package.
- Areas and communities affected by cumulative impacts
- Areas and communities affected by unplanned by predictable developments caused by the project.

This guidance is particularly invoked by the complainant(s) in their argument that the village of Vreoci and its environs should have been included in the EBRD due diligence and application of its standards.

³⁴ EBRD ESP May 2008 PR1.6

The ESP however also states that the ‘Area of Influence does not include potential impacts that would occur without the project or independently of the project,’ thus focussing further attention on what the ‘project’ actually is.

Also of relevance in this analysis is the position set out by the Complainants that even though the 2008 ESP only applies to the Kolubara Environmental Improvement Project, that EBRD has had a history of investing into the integrated energy/mining complex and that this ‘broader investment programme’ must be taken into account.

5.3.1 EBRD approach to the AoI

EBRD has developed specific internal guidance in relation to how the ‘area of influence’ should be determined and this has been provided.³⁵ This is an internal EBRD document but critical in understanding the approach adopted to area of influence (AoI) and the EBRD Management Response to the Complaint. The following observations within the guidance are particularly pertinent:

1. The AoI should be defined as early as possible and results documented and agreed with the Client. The AoI may change during the due diligence process based on feedback.
2. The degree of appraisal can vary for each component of the AoI and the standards applied may be different for each component.
3. The ‘Project’ is expected to comply with all Performance Requirements. The PRs do not necessarily apply to other components of the AoI.
4. Components not under the direct control of the Client or where they are not yet fully defined or are speculative may be assessed on a less intensive basis commensurate with the risks.
5. Non compliances associated with components of the area of influence beyond the immediate scope of the EBRD Project are not considered to be derogations from the ESP (i.e. the failure of a project component within the AoI to meet the PR does not require EBRD to issue a specific ‘permission’ or derogation for that non-compliance to occur).

With respect to the components of the AoI relevant to this analysis:

Assets and facilities owned by the Client which are to be financed: Includes existing facilities in the case of an expansion or rehabilitation.

Supporting or enabling activities and facilities: Includes dedicated facilities associated with the Project such as wastewater treatment, waste disposal etc.

Associated facilities or businesses not funded by EBRD but whose viability is directly based upon the Project: Includes other facilities which depend exclusively on the Project and are essential for the project success. It applies to situations where from the Client’s point of view the activities are covered by the same management structure and are being considered as

³⁵ ESD: Guidance Note: Area of Influence: 15.12.08 (Internal)

separate projects simply for the purposes of financing or have been artificially divided into smaller projects.

Areas and communities affected by cumulative impacts: Includes cumulative impacts from other developments in the area where they can be forecast with a high degree of certainty. Cumulative impacts may also need to be assessed where the EBRD financed project is located in an area where the public health conditions, environmental quality standards, the absorption capacity of the natural environment or social conditions are already affected by existing activities.

Areas and communities affected by unplanned by predictable developments caused by the Project: Covers a range of induced and second order impacts which should be assessed with the client to determine what is included in the scope of the Project.

With respect to the performance requirements the guidance states that *‘other components of the area of influence should be encouraged to comply with the PRs over time, again taking into account the risks and Banks and clients leverage.’* EPS have total control over the project area and are reliant on EBRD funding and there is a history of non-compliance with project conditionality. It would therefore have been reasonable, based on its own internal guidance, to expect EBRD to apply the PRs across the broader area of influence as condition precedent to the KEIP project.

The guidance document provides a useful explanation of the approach which EBRD seeks to adopt and the logic behind it. To some degree it also explains the EBRD Management Response that the Complainants ‘misunderstand the policy wording’ with respect to AoI. The Complainant was presumably assuming that the policy wording would be interpreted in an inclusive context with the PR broadly applied to most or all components of the AoI. EBRD has developed guidance, to which the Complainant and other external stakeholders were not party, which interprets the wording quite differently. Whilst helpful in understanding the internal EBRD perspective, as it is not a formal part of the policy and has not been disclosed or subject to stakeholder review or Board approval it is not incumbent upon the Compliance Review Expert to accept this internal guidance as a reasonable interpretation of the EBRD policy requirements.

The substantive issue is whether the scope of EBRD due diligence and its definition of ‘Area of Influence’ pertaining to the Project was appropriate in the context of:

- The scope of the ‘Project’ as defined in the Board Paper
- The requirements of the ESP
- The importance placed upon environmental and social factors in project documentation
- The history of EBRD engagement with EPS and prior performance in meeting environmental and social conditionality.

5.3.2 EBRD Project Due Diligence and the AoI

The Initial Environmental and Social Examination (IESE) of the Kolubara Environmental Improvement Project took place in September 2010.³⁶ It was also used as an opportunity to monitor the Bank's ongoing investments with EPS. It describes the main components of the Project and the fact that this will enable the development of new Independent Power Projects. It observes that 6 households will require resettlement as a result of Field C implementation and that *'EPS appear to have well established resettlement procedures.....this is undertaken on a 5 year rolling basis ...done in consultation with affected people and local authorities....'* The IESE notes that environmental audits on company facilities, required as a condition precedent (CP) to prior loan agreements with EPS (the electricity metering loan), are several years overdue. The BTOR advises that the Project is a category A project (under the ESP) and that a consultant will be engaged to undertake a gap analysis on existing EIA documents and prepare an Environmental and Social Action Plan (ESAP), a Stakeholder Engagement Plan (SEP) and a Non-Technical Summary (NTS). It further notes that EPS will provide the EIAs and the benefits study for the coal management system. The BTOR does not include any discussion of the AoI of the Project. The Compliance Review Expert was advised that the AoI for the Project was determined by the consultants undertaking the review of the ESIs and was included in their terms of reference. Also that whilst a technical due diligence study was done, no specific EIA documentation for the coal management system was required.³⁷

The Terms of Reference (TOR) for the consultants undertaking the project environmental and social due diligence were provided to the Compliance Review Expert.³⁸ The TOR sets out the project components and their inter-dependency. It requires the consultant to undertake environmental and social due diligence including a gap analysis of existing documents, plus preparation of the ESAP³⁹ SEP⁴⁰ and NTS.⁴¹ A compliance table identifying the relevant performance requirements for the Project and the Client's compliance with them is also envisaged. In particular the consultant is required to:

- Confirm i) the area of influence for the project; and ii) verification of the Bank's project categorisation
- Review the EIAs for the Field C and Tamnava West open cast mines and identify any gaps with respect to the EU EIA directive and EBRD policy and PRs
- Make recommendations as to how any gaps can be addressed
- Undertake an assessment of environmental, social and labour issues, management systems and practices for aspects of the project not addressed in the EIAs

³⁶ BTOR EPS (15-16 September 2010) 23.9.10 (Confidential)

³⁷ Meeting with EBRD staff 23.5.14 (Confidential)

³⁸ Due Diligence: Environmental and Social Audit and Analysis: Terms of Reference: EPS Kolubara Environmental Improvement Project

³⁹ European Bank for Reconstruction and Development: Kolubara Environmental Upgrade Project: Environmental and Social Action Plan: ISSUE | 25 February 2011: Revised by EBRD and EPS RB Kolubara: 5 March 2012

⁴⁰ Environmental Improvement Project at Kolubara Mine Basin: Stakeholder Engagement Plan: February 2011

⁴¹ Environmental Improvement Project at Kolubara Mine Basin: Non-technical summary

- Prepare an E&S Analysis of potential environmental and social issues and benefits associated with the proposed investment components
- Identify the EBRD Performance Requirements (PRs) (1 to 6, 8 and 10) that are relevant to the Project and determine to what extent these are met
- Prepare an Environmental and Social Action Plan (ESAP) based on the findings of the above points and mitigation measures proposed; and
- Assist the Client in preparation of a Stakeholder Engagement Plan (SEP) and NTS.

A list of issues to be considered within the gap analysis is also provided. The GAP analysis was finalised in April 2011.⁴² A few issues arising from the gap analysis are specifically pertinent to this compliance review.

The Gap analysis states that the coal management system is for use in two newly developed areas – Tamnava West and Field C and that there are no additional impacts arising from its implementation other than the mining impacts at those locations. It therefore concludes that other mining activities are outside the scope of the project and that the project AoI is ‘the direct and indirect impacts of Tamnava West and Field C.’

A comprehensive lender requirements compliance matrix table is provided which provides a review of the Project (as defined) against the EBRD performance requirements. The Project is generally regarded as compliant with EBRD, EU and Serbian requirements subject to the implementation of the environmental action plans and ESAP. A small number of areas are regarded as being of ‘moderate’ risk to the Project and lender; these include the quality of stakeholder engagement and the approach to cultural property.

There are a number of further outputs from the due diligence. The ESAP developed to address the issues identified in the gap analysis was disclosed in English and Serbian by EBRD. It sets out the broader and systemic requirements to be fulfilled by EPS in meeting its commitments to EBRD. These include the need for inception reports for Field C including environmental action plans (the plan for Tamnava West was already available), implementation of the Stakeholder Engagement Plan and development of mitigation plans consistent with the EIA documents for Tamnava West⁴³ and Field C⁴⁴. The recommended mitigation and monitoring plans are set out in sections 8 and 9 of the EIAs respectively. It is noted that comprehensive monitoring plans for Kolubara as a whole have not existed in the past and that the plans for Field C and Tamnava West have been prepared to meet EU and

⁴² European Bank for Reconstruction and Development: Kolubara Environmental Improvement Project: Environmental and Social Gap analysis Report: Issue: April 2011

⁴³ Electric Power Industry of Serbia: MB Kolubara: Environmental Impact Assessment of the Project: Supplementary Mining Design, Tamnava West Field

⁴⁴ Electric Power Industry of Serbia: Environmental Impact Assessment Study for the project: ‘Coal exploitation in the open cast mine ‘field C’ for the capacity of 5 million tonnes annually, with the excavation of the East dump site Istocna Kipa

other International good practice requirements. The EIAs are prepared in the context of the Strategic Environmental Impact Assessment for the Kolubara Basin.⁴⁵

5.3.3 *The Coal Quality Management System (CQMS)*

Technical due diligence on the Kolubara Environmental Improvement Project was undertaken by KfW, the co-investors. The principal report is a comprehensive technical audit of the proposed investment, which provides the most salient technical description of the project.⁴⁶ In its description of the CQMS an immediate discrepancy occurs in what precisely the Geo-Spatial application of the system will be. The EBRD Board Report asserts basin wide benefits from the CQMS (and the need for the CQMS to enable mixing of higher calorific value lignite from the eastern portion of the mine with the lower calorific value material from the West). The Environmental and Social Due Diligence states that the system will be utilised only on Field C and Tamnava West. The technical due diligence report says that it will be utilised on the Western open pit mines, initially Tamnava West and Veliki Crljeni and in future Fields G, South Field and Radljevo. These are three different descriptions of the application of the system. These discrepancies are material in the discussion of the project AoI.

The EBRD assertion that impacts from the investment will be isolated within fields Tamnava West and Field C is not entirely credible. Field C is a natural geological continuation of Field B which is now closing and equipment will then go on to be utilised until the end of its working life (which would be beyond the lifetime of Field C). Field C also acts as a natural pre-cursor to the opening of Field E. Similarly on the western side of the basin Radljevo Field is a natural extension of Tamnava West Field. These fields will also be hydrologically connected. The point being made is that in conjunction with the CQMS the investments in mining machinery have to be seen as an investment in the efficacy of the mine basin as a whole.

The review states that the CQMS will be implemented in two versions, in parallel. Version 1 undertakes blending of lignite of mixed calorific value on a conveyor. However it is clear that the quality of lignite from Tamnava West will deteriorate in the coming years – so version 2 will enable blending from multiple sources via a blender yard. Lignite of the required calorific value is automatically directed to specific cells within a stockpile such that material of the required calorific value can be automatically achieved through use of a scraper chain, with subsequent direct transfer to train loading for transportation to the power stations. The implementation of the CQMS requires significant ‘up front’ analysis in terms of exploration/modelling, planning and production control so clarity over the fields to be utilised and when will be critical. The CQMS implementation clearly constitutes a strategic step for EPS in the overall efficiency of its operations and most significantly in achieving contractual

⁴⁵ Republic of Serbia: Agency for Spatial Planning: Electric Power Industry: Strategic Environmental Impact Assessment of the spatial plan of Kolubara Mining Basin: Report on Strategic Assessment

⁴⁶ Energy Efficiency by Sustainable Coal Quality Management: EPS/Kolubara: Audit and Analysis of Project Feasibility on EPS’ Kolubara Opencast Lignite Mine Operations

compliance and preparing its operations for the next stage in private investment in the Serbian energy sector.

5.3.4 *Compliance with respect to the AoI*

As discussed, the definition of the ‘area of influence’ as derived from the ‘project’ is central to both complaints. Once the components of the AoI are established, this then determines the application of the EBRD ESP and the performance requirements, thereby addressing other elements of the complaint.

Both complainants believe that EBRD should have addressed the broader environmental and social performance of EPS within the Kolubara basin in its due diligence. EBRD’s assertion is that broader activities undertaken by EPS at Kolubara which are unconnected to investments at Field C and Tamnava West and which are occurring regardless of those investments do not fall within the project area of influence. Furthermore EBRD states that for those elements of the project which do fall within the area of influence, it is not the case that the PR should be applied, arguing that only where specifically mentioned in the PR (4,7,8) does the AoI apply. EBRD believes that its due diligence has been undertaken in a way which is consistent with its interpretation of the ESP.

5.3.5 *Observations and Conclusions:*

1. The EBRD Board Paper makes it clear that the business activities in which EBRD is investing - ‘The Project’ - is a substantial investment in EPS’ principal lignite mining basin to improve the commercial and environmental performance of its existing mining and generation operations and secondly to ensure that it is able to implement the Kolubara B Project (and potentially the Nikola Tesla IPP). The ‘business activities’ and therefore the boundaries of the ‘Project’ includes all of these aspects. It follows a pattern of EBRD investment in EPS consistent with its transition mandate, energy strategy and country strategy. The Compliance Review Expert finds the clear focus on efficiency and environmental improvement aligned with transition to international standards and a market based energy sector entirely consistent and appropriate. However this strategic and holistic business approach is not reflected with respect to analysis of environmental and social issues. The ‘Project’ definition which encompasses the entire Kolubara basin and the ‘area of influence’, which has sought to minimise the scope of analysis required are inconsistent. As a result the scope of due diligence does not meet the aspirational or detailed requirements of the ESP.
2. The EBRD ESP specifically defines the Project area of influence broadly. This is consistent with good practice and the reasonable expectations of a multi-lateral Development Bank with a transition mandate. EBRD Management has developed internal guidance which sets out how it expects the policy requirement to be interpreted in its application to projects. Whilst this is reasonable, such guidance should be disclosed, transparent and subject to stakeholder review and input as it directly interprets the policy. As currently constituted, the Compliance Review Expert believes that it undermines the clear intent of the policy. The Compliance Review Expert accepts that some differential application of depth of due diligence and application of standards to

different components of the area of influence is justified but this should be part of the policy framework, not contained within an internal document. The guidance as written specifically appears to dissociate the broader impacts from a 'Project' funded by EBRD from EBRD responsibility to ensure application of its performance requirements. Furthermore, EBRD has sought to assert that the AoI applies only to certain PRs. PR1 sets out the overarching approach to environmental and social management and paragraph 6 is clear that it is the project's environmental and social impacts which are appraised in the context of the AoI. As all of the PRs relate to environmental and social impacts, the intent is clear – that the AoI applies across those project impacts, to suggest otherwise is inconsistent with the intent of the ESP and with good practice. As currently worded the Expert believes that it would be entirely reasonable for an external stakeholder (including a complainant) to anticipate that EBRD would apply its performance requirements to many of the components of the AoI. The Management Response to the Complainant that 'this misunderstanding of the policy wording is behind much of the Complaint' is somewhat disappointing as the Complainant would have no knowledge of the EBRD guidance which limits application of the PR to components of the AoI. The Compliance Review Expert believes that the Complainant's interpretation of the policy intent, as written, is a reasonable one.

3. The EBRD interpretation of the application of the policy and the performance requirements to the AoI, is inconsistent with the approach adopted during the due diligence on the 2011 Hydropower Investment with EPS where the Selova SHPP project was not regarded as part of the 'Project' as it was not owned by EPS but was part of the AoI and EBRD required that EPS ensure that the PRs be applied to the Project.
4. The Project is made up of several components; those relating specifically to the development of the Tamnava West lignite Field and Field C, were dealt with adequately. However the diligence failed completely to recognise the significance of the CQMS which has basin wide implications. Indeed the diligence is not clear or accurate on what fields will in fact form part of the CQMS. EBRD's own documents acknowledge the significance of this component of the Project in improving lignite quality supplied to power stations from across the basin. Indeed its implementation is a key enabling factor in the contractual provision of lignite to proposed modern power plants which will attract inward investment. The AoI and the application of the PRs should have been considered in this context.
5. The ESP requires EBRD to consider the capacity and commitment of the client. Whilst this was achieved to some degree through the EIA Gap analysis, it should have considered the client's performance from an environmental and social dimension across all of its operations at Kolubara. Both the KEIP, through its transition focus on improvements in environmental and social governance issues, and prior and concurrent investments had recognised the need to strengthen the client's systems and capacity. This had been further reflected through the requirement for environmental audits of all the EPS subsidiaries which were a CP to prior investments. Delays in implementation should

have caused EBRD to look again holistically at the E&S requirements it places on the client and the history of the client's performance over a long history of investment consistent with paragraph 15 of the ESP and PR1. At the very least, the completion of the environmental audit of Kolubara and the preparation of an action plan should have been conditions precedent to the KEIP investment. The Compliance Review Expert believes that such an approach would have been in the best interests of EPS, EBRD and all stakeholders.

6. The IESE did not discuss the Area of Influence of the Project or the components which should be addressed or the standards to be adopted for each. This is inconsistent with the internal guidance developed by EBRD and the AoI requirements of PR1. The Compliance Review Expert believes this is central to the consequent failure to address the project impacts appropriately. It is critical that the IESE addresses all elements of the project and EBRD investment history such that the due diligence can be scoped appropriately in the context of the ESP and good practice. The ESP in fact requires that this be undertaken by EBRD and agreed with the client. The Compliance Review Expert believes that the outcomes should also be disclosed in the project documentation so that the extent of due diligence and the standards being applied to components of the Project is clear to external stakeholders. This task was left to the consultants undertaking the due diligence. Resulting due diligence focussed on the impacts of equipment provision at Field C and Tamnava West. Somewhere in this process the broader significance of the project as a basin wide investment was lost. The Compliance Review Expert believes that as a result the EBRD approach to due diligence and ESP compliance was not consistent with its policies and procedures.
7. The Compliance Review Expert acknowledges that EBRD has been seeking to appropriately interpret a Policy which is poorly worded with respect to the Area of Influence of a project. The Compliance Review Expert notes that in parallel to this investigation EBRD has been reviewing its ESP and that it should be possible to correct the underlying policy weakness which has led to this situation.

The Compliance Review Expert finds EBRD non-compliant in its application of the ESP general requirements and the requirements of PR1, to its Environmental and Social due diligence of the Kolubara Environmental Improvement Project.

5.4 Stakeholder Engagement and the Village of Vreoci

5.4.1 Background

The issues associated with resettlement and the village of Vreoci have been introduced earlier in this report. The stakeholder engagement context and the response of EBRD is developed further in this section. With respect to specific impacts on the village of Vreoci, Complaint 1: ES Vreoci claims that the EBRD due diligence process related to the project and therefore the associated documentation and conditionality placed upon the Client failed to address impacts upon the village of Vreoci. As a result, it claims that EBRD failed to comply with performance requirements 1, 3 and 5. Further claims are made about the alleged failures of

EPS. Complaint 2: CEKOR alleges that EBRD artificially excluded Vreoci from the project area of influence and also that previous resettlements under the EPS II Project were not undertaken in accordance with appropriate standards. They allege that this has undermined the credibility of EPS in negotiating agreements with affected communities. The Complaints document a substantive number of issues/correspondence around the issue of resettlement at Vreoci and the specifics of the (disputed) actions taken by EPS in relocation of the village cemetery.

EBRD asserts that the resettlement of Vreoci is associated with the expansion of Field D and is not associated with the EBRD Project. Indeed, in discussions with the EBRD Board, Management consistently state that impacts on Vreoci were not associated with the EBRD investment. EBRD Management did however commit (to NGO groups and its Board) to investigate the issues and facilitate a discussion between the Company and local groups with the objective of attempting to facilitate a solution to outstanding resettlement issues. EBRD engaged a Serbian consultancy to manage this facilitation process and a meeting was held between the Company, 11 local people, EBRD staff and the consultants on 24 August 2011. A number of key locations related to complaints from the village were also visited. The consultant's report⁴⁷ documents the dissatisfaction expressed by the local residents due to alleged delays in resettlement, mismanagement of the cemetery relocation and pollution from site operations. Villagers also alleged corruption in the resettlement process. It also documents the community members' attempts to bring the situation to the attention of the Serbian Government and Courts. The report also documents the response of EPS in asserting that a majority of people resettled were happy with the process and those that were not had been able to take legal recourse and where appropriate have their compensation increased.

The resulting consultant's report makes some recommendations to EPS relating to the cemetery relocation (which was ongoing at the time and subsequently completed), specific pollution issues, and screening of Barosevac from activities at Field B. It further concluded that they could not determine whether the people attending the meeting were actually representative of the affected communities or were simply pursuing their own personal interests. Subsequent actions are unclear.

5.4.2 Stakeholder Engagement Planning

The Stakeholder Engagement Plan (SEP) provides a summary of the principles of engagement to be adopted during the project's development. It further sets out how national law would be complied with and provides an engagement framework for the key stakeholders identified. The SEP notes Serbia's commitment to EU standards and in particular the Aarhus convention (Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters) of 1998 ratified by Serbia in 2009.⁴⁸ The SEP identifies specific communities which will be resettled by the project and businesses affected. This does

⁴⁷ EPS Kolubara Environmental Improvement – Community Visit, October 2011

⁴⁸ Law on Confirmation of the Convention on Information availability, public participation in decision-making processes, and legal protection within environmental issues ('Official Gazette RS International Contracts', №.38/09)

not include the residents of Vreoci village itself other than those who would be affected along the Arondelevac-Vreoci Road. A more general stakeholder group is identified as:

General Public – one or more natural and legal persons, their associations, organisations and groups. Stakeholders – the public either affected or not affected by the project.

The methods of communication identified in the plan are wide ranging and somewhat non-specific in terms of each stakeholder group – commonly:

Method of external communication: EPS and RB Kolubara website, Kolubara and KWh magazines, public notifications, meetings with authorities, institutions and other stakeholders, Annual Environmental Report of EPS and RB Kolubara, published environmental objectives at the EPS level and via external queries from the field of product and services quality, environmental protection and health and safety. Communication to be also achieved by: media notices, notice boards, grievance forms.

The EBRD view that the residents of Vreoci were not key stakeholders with respect to the Project was confirmed in both the Management Responses to the Complaint and in meetings with the PCM Expert. EBRD staff observed that they believed that the resettlement process had generally been good, followed Serbian procedures and was systematic. They also believed that Vreoci residents had opportunity to raise concerns or issues during project preparation but that they did not.⁴⁹

An agreement was signed between the Company and the affected communities at Barosevac relating to resettlement and the provision of various community facilities over the period 2011-2015 in November 2011.⁵⁰ The resettlement and impacts at Barosevac associated with the Field C development was referred by EBRD for independent review by consultants and deemed to be consistent with EBRD Performance Requirements.

One of the underlying issues identified by the Complainant are allegations that the resettlement undertaken as part of the 2003 EPS Power II investment were sub-standard. The Compliance Review Expert has reviewed resettlement reports provided by EBRD which set out the measures to be taken to complete the resettlement to the required standard⁵¹. The report is of a high standard, recognises that delays in resettlement have occurred due to funding shortages, and makes important recommendations in terms of treatment of vulnerable people and the application of ‘soft’ initiatives to support the resettlement process. A series of indicators are also proposed against which progress can be monitored. The author of this report understands that no completion report was issued and has not been able to confirm that the resettlement had been undertaken and livelihood restoration indicators met. It can

⁴⁹ Compliance Review Expert and Bank Management Meeting (Confidential)

⁵⁰ Agreement: On implementation of the Resettlement Program of Part of Barosevac Settlement: 18th November 2011

⁵¹ EBRD: Tamnava West Coal Mine Project: Proposal for Additional Work to Complete Resettlement Plan: June 2002

therefore neither confirm nor deny the allegation. EBRD advises that the resettlement was reviewed as part of the KEIP due diligence and found to be consistent with the PRs. It is however notable that some of the same issues are prominent within the contention around the Vreoci resettlement.

5.4.3 Analysis

The central issue is whether the village of Vreoci should have been considered part of the 'Area of Influence' of the KEI project and how the PRs should be applied. EBRD decided that it should not be, based on its definition of the 'Project' it was financing.

EBRD policy requirements of relevance are contained within (i) the general commitments of its Environmental and Social Policy, (ii) the scope of policy application set out in PR1 and (iii) the specifics of resettlement practice set out in PR5. An analysis of these requirements would then determine the scope of information disclosure and stakeholder engagement required under PR10. The first two of these have been discussed in section 6.2 above and will not be repeated here except to note that:

- The Project (as set out in the EBRD Board paper) is a substantial investment in EPS/RB Kolubara to increase efficiency and support contractual integrity of future lignite sales thereby underpinning the commercial performance of the business during the transition to a more market based economy and sector.
- The CQMS is a basin wide resource to achieve those ends and is not constrained to investments at Field C and Tamnava West.
- The EBRD ESP requires it to review the capacity and commitment of the Client to meet its standards across environmental and social aspects of its operations.
- The Compliance Review Expert finds that the AoI for the Project should have been defined more broadly in terms of the application of the ESP.

As noted by the Complainants, Vreoci is situated centrally within the entire integrated complex. Transportation of materials to the transport yards from the east of the field to the proposed blending operations in the west of the field, pollution from industrial facilities to the south of the village, potential future construction of another power plant at Kolubara; all of these issues and more are directly related to life quality and impacts in Vreoci until resettlement is completed. Following through on commitments made to its board and responding to communications from representatives of Vreoci and civil society, EBRD commissioned consultants to undertake a facilitated meeting between the local community and the Client. EBRD also asserts that because the opening of lignite extraction at Field C effectively replaces Field B on an equivalent basis, that the quantity of lignite transported to the industrial complex south of Vreoci is unchanged.

Of further relevance is that, if one concludes that the village of Vreoci should have been included in the EBRD due diligence process, then environmental and other social impacts on the village should have been considered by EBRD as an integral part of its analysis of the KEIP. Whilst EBRD commissioned social consultants to assess the situation in Vreoci and supported its Client in undertaking environmental audits, it did not regard Vreoci as part of

the AoI and these activities were not therefore regarded as central to project compliance and associated conditionality.

EPS provided a substantive written update on resettlement and other issues affecting Vreoci to Compliance Review Expert following the eligibility assessment meeting in February 2013.⁵² The document reaffirms the resettlement practice and consultations and provides information on air, noise and water monitoring undertaken. It also asserts full collaboration between the Vreoci local council and RB Kolubara since the elections in December 2012.

The Complainants further state that environmental impacts on Vreoci were identified in the Field C EIA (as well as ongoing impacts from mine operations) notably from the transportation of coal from Field C into the industrial area adjacent to Vreoci and through threats to groundwater resources utilised by Vreoci through boreholes.⁵³

The EBRD Management Response states that whilst groundwater levels have been depleted that these will not be made worse by the opening of Field C as Field D which is older and deeper lies between Field C and Vreoci.

The EIA does indeed state that *'The source of this (Vreoci) water supply system is jeopardized by the opening of the open cast mine in this area'* though it is not explicit about which open cast mine it is referring to. As the EIA also notes – the *'open cast coal exploitation in the central part of the Kolubara basin physically destroys the interseam aquifer, a greater part of the alluvial aquifer and disturbs the floor aquifer regime.'* In reality, the groundwater supplies at Vreoci have and will be affected by mining operations and due to the complexities of the geology and hydrological continuity it may well be impossible to determine exactly which field is causative. That however is not the point. The community of Vreoci needs a reliable alternative supply of potable water until the resettlement programme has been successfully completed. Seeking to artificially separate the impacts from Fields C and Tamnava West does a disservice to those impacted by the cumulative effects of the basin development. Whilst EPS provides water to Vreoci, Complainants claim that it is an inadequate supply for their needs. It is not possible for the Compliance Review Expert to validate these claims or otherwise, but the approach adopted by EBRD means that the issue was not substantively addressed as part of the ESIA.

The 'without project' environmental and social scenario has not been addressed. In the absence of the EBRD investment in the new fields and in the CQMS the likely outcomes are unclear. For example, key fields within the Kolubara basin are close to exhaustion, including field B. The longer term impact of supplying lignite of variable calorific value to the existing power plants and the inability to supply new modern power production capacity would invariably change the sustainability of the lignite mining operation. Whilst this is exactly the

⁵² Answers to questions of the independent expert engaged by EBRD from the meeting held with EPS – RB Kolubara representatives on 14 February 2013 regarding the Vreoci Local Community Complaints submitted under the Project Grievance Mechanism. PD RB Kolubara 12 March 2013

⁵³ Electric Power Industry of Serbia: Belgrade: Environmental Impact Assessment Study for the Project: Coal Exploitation in the Open Cast Mine 'Field C', for the capacity of 5 MIL. Tons Annually with the Excavation of the East Dumpsite 'ISTOČNA KIPA'

scenario the EBRD investment is designed to avoid, it means that Vreoci is a stakeholder in this broader analysis.

5.4.4 Observations and conclusions

1. Vreoci sits centrally along the infrastructure spine which services the entire mining/energy industrial complex and adjacent to the industrial area. Any analysis of the impacts of MB Kolubara and the KEIP has to address the situation of Vreoci.
2. EBRD involvement has underpinned the development of the basin since 2001. Consecutive investments have identified shortfalls in environmental and social management capacity within the client organisation, which EBRD has sought to rectify on a piecemeal basis. EPS itself has recognised many of these shortcomings and is seeking to rectify them with external support. A core transition objective of the KEIP was to improve environmental and social governance.
3. The AoI for the KEI Project should have been broadened to include the Kolubara basin and the resettlement of the village of Vreoci should have been considered by EBRD in its due diligence of the KEIP. However, the Compliance Review Expert acknowledges that in general the approach taken, as driven by Serbian requirements under the approved strategic plans was systematic and intended to be based on negotiated and agreed settlements on a timely basis. EBRD first engaged with EPS with respect to resettlement in 2003 when the complexity of the process was apparent and EBRD Management commissioned additional resettlement studies. EBRD should have acknowledged that it could play a more formal strategic role (as supported by its Board) in facilitating the timely and fair completion of the Vreoci resettlement as part of the KEIP project without actually taking responsibility for resettlement undertaken to date. Its subsequent informal intervention, whilst well intentioned, has not achieved that, and may have been counter-productive in a complex process between the Client and community at the time of the Complaint. The Compliance Review Expert cannot and does not in any way assign blame for the disagreements which have ensued, but notes that EBRD missed a significant opportunity to play the honest broker to the benefit of all parties, if it had structured its diligence and engagement on the environmental and social aspects of KEIP appropriately.
4. The Compliance Review Expert also notes that EPS/MB Kolubara is in a dominant position with respect to the development of lignite resources and can resort to expropriation through eminent domain if appropriate. It also dominates employment opportunities within the affected communities and manages all relevant public services. The Compliance Review Expert does not suggest that this situation has been mismanaged; however EBRD should have recognised the potential for these relationships to place community members under duress and to have engaged appropriately.
5. It is impossible for the Compliance Review Expert to come to any robust conclusion about the veracity of Complaints relating to the Vreoci resettlement, nor should it seek to. The discussion has been highly politicised and not always constructive. However, where there is agreement, is that the resettlement should be completed according to schedule in a mutually respectful way. This resolution would in itself deal with the environmental and social impacts upon the remaining community members and allow the Company and community members to move forward. EBRD excluded itself from this

problematic dialogue by proscribing Vreoci from the application of the PRs within its determination of the AoI of the Project, EBRD should have commissioned a broader review of the social development strategy of EPS including resettlement programmes in progress across the Kolubara Basin (in parallel to the environmental audits taking place). This would have indicated where EPS needed to be supported in terms of social capacity, implementation systems (including grievance management) and any financial shortfalls causing programme delays. Inherent to such an approach the residents of Vreoci should have been directly identified as stakeholders for the purposes of engagement in the design of the Project. The Compliance Review Expert does not believe that this would have placed significant additional burdens on EBRD and would have provided constructive support to its client. Early application of a transparent grievance process may have enabled concerns over ongoing provision of public services including water supply to have been dealt with effectively and to the benefit of all parties.

6. EBRD due diligence should have more directly addressed environmental impacts on the village of Vreoci from ongoing mining activities as well as operational changes taking place as a result of the opening of Field C and the expansion of Tamnava West. The outputs from environmental audits undertaken on MB Kolubara facilities in the industrial areas and Environmental and Social Action plans developed by EPS to address them should be publicly disclosed and their implementation form part of the Company commitments to EBRD under the loan agreement.

The Compliance Review Expert finds EBRD non-compliant with the general commitments of the ESP and PR1, 3, 5 and 10 with respect to its exclusion of Vreoci from its due diligence (and application of the PR) on the KEIP.

5.5 Greenhouse Gases

5.5.1 *The Complaint and the Management Response*

The Complainant argues that for a number of reasons, the analysis of the Projects' cumulative GHG emissions was too limited in scope and not consistent with EBRD Policy. This is based upon planned increased lignite production, the inter-relationship of the investment with potential contractual commitments to the planned Kolubara B power plant and the planned closure of Kolubara units 1-5.

Taking these three major factors into account, we conclude that the EBRD has set the boundaries of the project inappropriately narrowly to capture the project's direct and easily foreseeable impacts on GHG emissions.

The Complainant further sets out the reasons why they believe a broader analysis should have been undertaken based on the EBRD ESP, particularly PR 1.6.

We see PR1.6 on the project's area of influence as giving the clearest guidance on what elements should be included in the greenhouse gas assessment for the project. Both a baseline and a post-project estimate are needed in order to measure the project's impact, and considering that the EBRD has carried out three projects connected to the Kolubara mining complex, a true cumulative impact assessment would look at the impact of these altogether and would have taken as its baseline

what would have happened without all three of the projects. However given the practical difficulties associated with this (data on lignite combustion before 2003 for example is not precise) and the complications of assessing projects which span 2-3 different EBRD policy periods, we conservatively maintain here that at least for the 2011 Environmental Improvement Project a greenhouse assessment should have taken place which would have included all the elements in PR 1.6.

The Complaint further proposes that there are links between the Project and EBRD funding of increased thermal generation capacity through the construction of the Kolubara B Power Station.

The EBRD Management Response asserts that the analysis undertaken by EBRD is consistent with its Policy.

The GHG impact of the project was estimated using the Bank's established methodology. The methodology has been extensively peer reviewed and is in the public domain. This methodology aims to estimate the impact of the Bank's investment by comparing the pre-investment situation with expected emissions once the project is complete and operational. In this case, the Project will undoubtedly lead to a reduction in emissions through more efficient combustion at the power plants. The introduction of new mining equipment will also lead to more efficient operations and further GHG saving versus the existing equipment, but these benefits are relatively minor and their exclusion from the assessment adds to the conservativeness of the calculations.

The net GHG reductions were estimated by EBRD's technical experts at 200,000 tonnes per year.

The Response also advises that no increased coal production is anticipated as a result of the Project and production will simply substitute for existing operations as they close down. It also states that the Bank is not currently considering the Kolubara B Project and that the Complainant's data, based on Serbian energy strategy documents, is out of date and no new thermal capacity is imminent. EBRD has further asserted to the Compliance Review Expert that it does not believe that the GHG assessment requirements under PR3 were triggered for this Project.

Whilst EBRD may indeed not be considering investment at Kolubara B, it is clear from prior analysis that the intent of the EPS-KEIP was to assist EPS in its preparation for private investment into the power sector through fulfilment of supply contracts relating to the quality of lignite. It is also clear that without EBRD funding there would be a progressive reduction in production and the viability of existing fields would be jeopardised due to the need for improved lignite quality and consistency.

5.5.2 EPS: Greenhouse Gases and the 'Project'

EPS is 100% state owned and is responsible for mining, generation, transmission and distribution to property. It is a vertically integrated company and has control over all

elements of the power generation cycle. This is an important factor in determining an appropriate approach towards GHG analysis and disclosure.

In 2010, EPS produced a total of 37.2 million tonnes of lignite in opencast mines located in the Kolubara and Kostolac basins. The lignite from Kolubara was used to generate 46.2% of the total electricity produced by EPS, whilst the lignite mined at Kostolac fuelled 14.4% of EPS power generation. The ratio of excavated overburden to lignite was 2.19:1 cubic metres per tonne in the Kolubara mining basin and 4:1 cubic metres per tonne in Kostolac.

As at 2013⁵⁴ the company has an installed capacity of 8,359 MW of which 5,171 MW (62%) is lignite fired thermal plants. The most recent EBRD carbon emission factor of 792 g CO₂/kWh for Serbian electricity is dated 2009.

The EIB published more comprehensive data in 2014.⁵⁵ All values are g CO₂/kWh.

Country	Country Grid Factor	High Voltage Grid +2%	Medium Voltage Grid +4%	Low Voltage Grid +7%	Operating Margin
Kosovo	1,314	1,341	1,369	1,413	1,345
Bosnia and Herzegovina	892	910	929	959	1457
Serbia	804	820	838	865	1106
Czech Republic	636	649	662	683	1058
Romania	496	506	517	533	958
Belarus	486	496	506	522	487
Montenegro	481	491	501	518	1331
Slovenia	352	359	366	378	976
Hungary	339	346	354	365	682
Croatia	304	310	317	327	656
Slovak Republic	217	222	226	234	814
OECD Europe	360	367	375	387	704
Non-OECD Europe	470	480	490	506	724

The carbon intensity of grid electricity in Serbia is high – even for the region - and this has an impact on the carbon footprint of all industrial, business and domestic users of electricity in the country. For example – if powered from the Serbian grid a Nissan Leaf electric vehicle would have CO₂ emissions equivalent to 130 g/km; higher than many similar diesel or petrol cars.

The use of lignite as a primary fuel source for over 60% of the generating capacity is the main reason why the Serbian grid carbon intensity is so high with emissions from the lignite stations equivalent to over 1,200g CO₂/kWh. Lignite has a comparatively low energy density and often contains high levels of moisture. It is, however, low in methane (a potent

⁵⁴ Euro Coal - Serbia: <http://www.euracoal.com/pages/layout1sp.php?idpage=78>

⁵⁵ EIB Project Carbon Footprint Methodologies, Version 10.1, April 2014: http://www.eib.org/attachments/strategies/eib_project_carbon_footprint_methodologies_en.pdf

greenhouse gas) when compared with deep coal and only negligible amounts of methane are produced in its extraction.

5.5.3 EBRD GHG Analysis

The following benefits were quantified in the 2011 EBRD Board Report

Benefit	Where	Quantified Saving
Savings in coal currently dumped with the overburden (which can then burn following spontaneous combustion).	Mine	500,000 m ³ per annum
Reduction in use of heavy fuel oil at power plant due to poor lignite quality control and improved efficiency of power plant operation.	Power Plant	200,000 tonnes CO ₂ per annum
Reduction in sulphur dioxide emissions	Power Plant	6,600 tonnes per annum
Energy Savings	Power Plant	310 GWh per annum
Improved Thermal Efficiency	Power Plant	1-2% per annum

No data has been presented regarding the impact of the Project on the carbon intensity of the electricity generated by the power stations as measured in g CO₂/kWh. At a national level this is the value that has the greatest significance as it impacts on all consumer carbon footprints.

The Compliance Review Expert requested a copy of the analysis undertaken by technical experts for the claimed reduction of 200,000 tonnes CO₂ per annum arising from improved burn efficiency and reduced use of heavy oil. The following was provided:⁵⁶

The expected resource efficiency improvements and related CO₂ emissions reductions will be realised in the boilers of the power plants that use the lignite produced from the mine. At the moment, the mine supplies the power plants without the necessary coal preparation operations, especially in relation to uniform chemical analysis, characteristics and heating values. Consequently, there are many and wide variations in the lignite quality burned in the boilers and the result is continuous load fluctuations, lower efficiency and extensive need of fuel oil for co-firing in order to maintain uninterrupted operation. The installation of the coal management system will allow the mine to better treat (milling, screening and storing) the lignite on site and mix the various qualities in order to deliver lignite of uniform quality to the power plants. The system will be able to produce 17 million tons of uniform quality lignite per year, which correspond to power generation of around 11,400 GWh, with an assumed 32% thermal efficiency. The expected efficiency improvements at the boilers of the power plants is estimated at 1-2%, so the expected lignite savings for the same production is 1.5% x 17 million = 255,000 ton lignite per year. The corresponding CO₂ savings for this type of lignite is around 195,000 ton CO₂ per year. Additional savings will be realised due to reduced needs of fuel oil co-firing. At

⁵⁶ Management response following the Compliance Review Expert's request for information (Confidential)

the moment the power plants use around 44,000 ton fuel oil for co-firing and it is expected that with the improved operation due to the uniform quality lignite this amount will be reduced by at least 15%, i.e. by 6,500 ton fuel oil corresponding to around 20,000 ton CO₂. So the total CO₂ savings for the same power generation is at least 215,000 ton CO₂ per year.

This is tabulated by the Compliance Review Expert:

Factor	Value
Annual uniform quality lignite production	17 million tonnes
Energy Content of Serbian lignite	Units MJ/kg – Not Stated
Production at 32% thermal efficiency	11,400 GWh per annum
Expected efficiency improvements	1-2%
Estimated carbon reduction (1.5% Efficiency)	195,000 tonnes CO₂ per annum
44,000 ton fuel oil reduced by at least 15%	6,500 tonnes fuel oil per annum
Carbon intensity of Fuel Oil	Units kg CO ₂ /tonne
Estimated carbon reduction (Fuel Oil)	20,000 tonnes CO₂ per annum
Total Saving	215,000 tonnes CO₂ per annum

The exact details of the calculation have not been provided, in particular the factor used for the energy content of the ‘improved’ lignite, the carbon intensity of the fuel oil and the derivation of the 32% thermal efficiency factor for the power station are not supported although the EPS 2010 Report⁵⁷ does suggest a 1.5% improvement.

No data was offered to support power plant energy savings of 310 GWh/annum (and associated carbon dioxide emissions) or the reduction in sulphur dioxide emissions (an indirect greenhouse gas). The EPS 2010 Report identifies an increase of 10% in auxiliary energy consumption due to poor quality lignite but quantifies this as 32.2 GWh or one tenth the amount reported to the EBRD.

The Gap analysis prepared for EBRD by consultants advises that:

The generation and release of greenhouse gases associated with the proposed activities is not considered in either of the environmental impact assessments (Field C or Tamnava West).

That there is:

no reference to the EBRD recommended methodology.

Also that:

An assessment of the CO₂ emission associated with the project has been undertaken but the calculations were used emission factors available from the US EPA, Business Association of Motor Vehicle Manufacturers in Serbia and the carbon trust. The

⁵⁷ Quantification of Impacts, EPS, June 2010

Assessment reports an estimated saving of 723,410 tonnes CO₂ per annum (This figure was later superseded by EBRD's own analysis). It is understood that the EBRD methodology is not mandatory. The assessment appears to meet PR reporting requirements.

5.5.4 Energy Consumption in the Mining Operation

The 2011 Environmental Audit covers the Kolubara mining basin. Electrical energy consumption data for the main mining equipment (bucket wheel excavators, spreaders and conveyors) was estimated as 400,000,000 kWh (400 GWh) with a power factor of only 0.75 giving an overall equivalent power demand of over 530 GWh. A power factor of 0.75 is poor; in OECD countries a commercial power user with a power factor below 0.90-0.95 would normally be financially penalised by the electricity supplier. At a national grid intensity of 804 g CO₂/kWh the 530 GWh consumption is equivalent to 426,000 tonnes of carbon dioxide. If the intensity of the lignite power station is used (1,200 g CO₂/kWh) then the carbon dioxide emissions increase to 636,000 tonnes.

No comment is made regarding the impact of the new technology on the power factor and no objective is set to raise the power factor to a minimum acceptable level; in the mining sector this would be over 0.80 and ideally significantly higher.

5.5.5 EBRD Policy Requirements regarding GHGs and their application at Kolubara

The Complaint and the EBRD response focus on two fundamental requirements of EBRD Policy as they relate to GHGs. Firstly, the requirement to clearly define the project area of influence under PR 1.6 and secondly, specific GHG assessment, reporting and reduction requirements under PR 3.

The definition of area of influence (or project boundary as it is termed in PR3.18) is central to the Complaint, which argues that under 1.6 i-v it was incumbent upon EBRD to assess the GHG emissions (and the broader impacts) from the whole of the Kolubara basin. The arguments are complex but founded upon the principle that as an integrated energy complex seeking broader efficiency through investment and with a long potential operational life, it was inappropriate to base the analysis on the limited impacts delineated by investments at Fields C and Tamnava West. It is also based upon the long relationship between EBRD and EPS through the multiple investments that have taken place.

EBRD assert that the area of influence of the Project – as set out within PR 1.6 vi do not include potential impacts which would occur without the project or independently of the project. They regard the boundaries of the Project as specific to the investments at Field C and Tamnava West.

There are several requirements placed upon the client relating to GHG emissions under PR 3. Firstly the acquisition of enough data to undertake a baseline (pre-investment) and an estimate of post investment emissions. Notably this should include

direct emissions from the facilities owned or controlled within the physical project boundary, together with those...on which the project is dependent, including indirect emissions associated with offsite production of power used by the project....

Guidance on the definition of project boundary should also be sought from the Bank.

In addition the client is required to promote the reduction of project-related GHG emissions and to assess financially feasible and cost-effective options to reduce carbon intensity.

EBRD issues guidance with respect to the assessment of GHG emissions (as referred to in the quote from the gap analysis above).²²

The complainant believes that the project boundary was set too narrowly and did not establish an appropriate baseline against which future changes in GHG emissions could be measured. EBRD Management argue that their guidance on this issue has been extensively peer reviewed and that the consequent analysis undertaken by its technical experts indicating a GHG reduction of 200,000 tpa CO₂ equivalent, (which it believes to be an under estimate) is consistent with its guidance.

The key questions to be assessed for the purposes of this compliance review with respect to Greenhouse Gas assessment are therefore:

- Was the AoI or ‘project boundary’ for the purposes of GHG assessment consistent with EBRD Policy and guidance?
- Was the assessment of GHG emissions undertaken consistent with the ESP and EBRD technical guidance and good practice? Is the estimate of emission reductions within that assessment technically robust?
- Was the Project consistent with the policy requirements to promote the reduction of GHG emissions and reduction in carbon intensity?

5.5.6 GHGs and the Area of Influence or the ‘Project Boundary’

The issue of the Project ‘area of influence’ has been substantively discussed earlier. It is not the intent to repeat that analysis here but a number of key points are pertinent.

The ‘Project’ does not simply relate to investments in Field C and Tamnava West. The investment in the CQMS facilitates efficiency improvements more broadly across the Kolubara basin and in preparing EPS to supply higher quality lignite to future power plants which will attract private investment. This is reflected in the EBRD Board paper but not in the environmental and social due diligence AoI.

The approach taken by EBRD in assessing GHG reductions based on efficiency savings at the power plant is in fact more consistent with a broader definition of the AoI or the Project Boundary. The estimate of GHG reductions provided is based upon the integrated efficiency improvements which will occur due to all elements of the Project (ie including the CQMS). This would seem to indicate that EBRD defined the Project AoI differently for the GHG emissions assessment and for other environmental and social elements of the Project, though this is not described in any of the project documentation.

EBRD has made a number of investments in EPS across more than 10 years, all of which have some bearing on operating efficiencies and therefore GHG emissions (Power II, metering, investments in renewables etc). The strategic nature of its relationship and investment profile with EPS and the monopoly position that EPS holds within the Serbian

Electricity generation sector would support a holistic view of the GHG baseline and emissions trends based upon the Kolubara Basin, which would prove valuable in future strategy development.

In 2013 the estimated output of Field B (which will be replaced by Field C apparently at the same rate of production according to the EBRD Board Report) was 3.0 million tonnes per annum while the output of Tamnava West is estimated as 12 million tonnes⁵⁸. Together they account for around 50% of planned output of the Kolubara Basin for the foreseeable future. The actual percentage depends on the total production. In 2008 it was estimated to rise to between 30 million tonnes and 32.5 million tonnes by 2013 but according to the EBRD Management Response to the CEKOR complaint production has not been increased as new power generating capacity has not been built. In any case, the argument that EBRD can limit its environmental and social appraisal to the two fields is flawed based on the fact that they represent 50% of total mine basin production.

As EBRD notes in its guidance:

EBRD investments invariably improve the efficiency of production even where increased production outweighs this, leading to an increase in overall emissions. To demonstrate this benefit, GHG emissions per unit of product output should be calculated for the project and baseline cases, in addition to the absolute GHG emissions.

If EBRD had assessed GHG emissions across the whole of the electricity production operation against a dynamic baseline it would have allowed it to measure the impact of its involvement on carbon intensity within the Serbian Electricity Sector – the equivalent of calculating GHG emissions per unit of product output.

5.5.7 GHG Emissions Assessment and EBRD Guidance

The statement in the gap analysis undertaken on behalf of EBRD that the assessment of GHG emissions in accordance with EBRD methodology is understood to be ‘voluntary’ is difficult to understand. Whilst the EBRD technical assessment documents are called ‘guidance’, the ESP is very clear that the client will procure and report the data for a baseline assessment and will assess options to reduce its energy intensity and promote GHG reductions. This does not infer a voluntary approach.

EBRD guidance on GHG assessment sets out the parameters for its analysis:

In keeping with the Bank’s transition mandate, the assessment has sought to estimate the change in GHG emissions (Δ GHG) brought about by investments. This is the difference between the emissions following the implementation of the project investment and the emissions that would have occurred in its absence. Estimation of the post-investment emissions is relatively straightforward and amenable to routine monitoring during the project lifetime. In contrast, definition and estimation of the baseline or reference emissions, reflecting the emissions that would have occurred in

⁵⁸ Strategic Environmental Assessment of the Spatial Plan of Kolubara Mining Area, 2008

the absence of the investment, are not well defined. The concept of baseline or reference emissions may be interpreted in a variety of ways. Baseline or reference emissions are not amenable to measurement. They must be based on a set of assumptions, which may range from the very simple to the highly complex.

There is generally no 'right answer.' EBRD has generally followed a simple approach, but depending on the extent of information available and the extent to which future developments can be predicted, an attempt is made to provide the best estimate possible of the GHG impact of the project.

The EBRD analysis for EPS-KEIP, attributes a decrease in GHG emissions of approximately 200,000 tpa CO₂ equivalent to the project. However, the Compliance Review Expert believes this to be simplistic and inconsistent with the EBRD methodology which further states:

An attempt is made to provide the best estimate possible of the GHG impact of the project....

Some projects, particularly those involving high emissions may have a sufficiently large impact on their sector to generate consequences well beyond the project boundary.... In these situations it may be appropriate to replace a static baseline (pre-project emissions with a dynamic reference (without project) scenario over the project lifetime.

The Compliance Review Expert does not agree with the EBRD assertion that PR3 does not apply. Using the threshold criteria in PR3, or the broader interpretation of impacts under the project AoI, GHG's should have been more substantively assessed. Using any reasonable interpretation of the EBRD Policy and guidance - considering previous discussion of the project Area of Influence, there is no doubt - because EPS is vertically integrated - that the whole operation from mining the lignite through to its consumption in the power stations should be covered by the scope of the GHG baseline assessment. The assessment for the mining operation is mandatory; improvements in the equipment at the mine itself falls into the EBRD medium to high category (100 Kt to 1 Mt CO₂e per annum) but the vertical integration with a large fossil fuelled power generating plant puts the overall emissions in the high category. As a high category project it should be considered for a dynamic reference scenario. On the basis of the EBRD 2010 guidance and its reasonable interpretation this project requires a full baseline assessment for the whole Kolubara site and the generation plant. It is also the case that the lignite mined at Kolubara accounts for over 45% of total Serbian electricity supply and there is a very strong case to be made that the impacts beyond the project warrant the determination of a dynamic baseline carbon footprint.

The EBRD guidance document provides limited specific guidance on the precise scope of emissions which should be considered. These are most effectively set out in the international GHG reporting protocols.⁵⁹

⁵⁹ <http://www.ghgprotocol.org/calculation-tools/faq>

The Greenhouse Gas Protocol (GHG Protocol)⁶⁰ is the most widely used international accounting tool for government and businesses in the quantification and management of greenhouse gas emissions. It was developed by the World Resources Institute (WRI) and the World Business Council for Sustainable Development (WBCSD) and serves as the foundation for nearly every GHG standard and program in the world, indeed it is referenced and prominent within the EBRD guidance. It also offers developing countries an internationally accepted management tool to help their businesses to compete in the global marketplace and their governments to make informed decisions about climate change.

Based on this protocol, the baseline should include all the Scope 1 (All direct GHG emissions – defined as emissions from sources that are owned or controlled by the reporting entity) and Scope 2 emissions (Indirect GHG emissions from consumption of purchased electricity, heat or steam - Indirect GHG emissions are emissions that are a consequence of the activities of the reporting entity, but occur at sources owned or controlled by another entity, e.g. In this case – electricity) as well as selected Scope 3 emissions (Other indirect emissions, such as the extraction and production of purchased materials and fuels, transport-related activities in vehicles not owned or controlled by the reporting entity, electricity-related activities (e.g. T&D losses) not covered in Scope 2, but not downstream emissions from the use of the electricity generated.

The GHG assessment of the Kolubara Investment as evidenced to this review does not meet a reasonable interpretation of the EBRD policy or guidance or good international practice. No attempt has been made to develop a dynamic baseline and consider the impact of not investing in the site or investing in alternative technologies.

5.5.8 Robustness of the EBRD Assessment of GHG emission reductions

The EBRD GHG assessment for the project has been set out in detail in preceding sections. It is based upon GHG reductions at the power plant based upon a 1.5% efficiency improvement through improved lignite quality and reduced use of fuel oil.

The Compliance Review Expert has sought to broadly validate this assertion based on the available technical data without undertaking a forensic analysis, and to review other components of the GHG impact to gain an overall view of the veracity and robustness of the assessment. Based on the sources available it is not possible to replicate fully the basis of the 1.5% efficiency improvement at the power stations, however neither has the Compliance Review Expert any particular reason to contest the number. EPS reports suggest a 2% reduction for each 1000 kJ/kg reduction in the fuel; other reports have used 1.5% and 1.2%. There are also significant variances in the reported reduced volume of lignite from 66kt to 250kt. As far as the Compliance Review Expert can ascertain however the projected reduction in GHGs was not disclosed in accordance with the EBRD policy and guidance.

There are numerous other GHG impacts which have not been considered (many of them positive) in the analysis even though data was available from EPS. For example the EPS⁵⁷

⁶⁰ <http://www.ghgprotocol.org/about-ghgp>

analysis of the impact of the new mining and grading equipment does identify the direct carbon emission impact arising from the installation of the new equipment.

- Energy saved by ECS in Field C (mainly reduced use of diesel): 324 t CO₂/annum.
- Energy associated with mining coal then dumped (mainly electricity): 1,855 t CO₂/annum.

The calculations to support these claims have been provided but have not been checked as part of this report. These savings were not included in the EBRD analysis or reported to the EBRD Board.

The same EPS analysis goes on to identify the impacts on the Nikola Tesla (NT) power plant. It identifies some significant potential reductions in energy use and therefore carbon emissions:

- 500 extra train journeys are undertaken due to poor quality lignite.
- Additional milling requiring 32.2 GWh of electricity (38,750 tCO₂)
- 22,000 tonnes of oil used to offset poor quality lignite
- Increased consumption of 66,300 tonnes of lignite (1.5%)
- 1,200 tonnes of ‘masout’ used for restarts
- Increase in the transportation of fuel ash – no estimate of additional journeys.

Unfortunately there is no documented calculation of the carbon emission associated with these major impacts or of some others which were not identified by EPS. For example: the reduction from fewer overburden fires (500,000 cubic metres of lignite is diverted from the waste stream).

Overall the EPS document estimates the savings in lignite as 66,300 tonnes/annum while the EBRD report suggests 250,000 tonnes of lignite giving an overall carbon reduction of 200,000 tonnes. It is not appropriate for the Compliance Review Expert to assess the accuracy of these analyses in further detail, but notes the absence of any detailed assessment of GHG emission reductions against an established baseline by EBRD.

5.5.9 Policy commitments to GHG and Carbon Intensity Reduction

The underlying objectives of the Project in terms of operational efficiency are generally consistent with EBRD sector and Country policy commitments. They provide another reason why it is in the interests of the client, EBRD and Serbia that a broad definition of the ‘Project’ and the AoI is used. A coherent view of GHG impacts across such a strategic integrated facility as Kolubara would enable direct assessment of impacts on national carbon intensity in electricity generation. As such the Project represents a significant opportunity missed rather than a policy non-compliance on these specific issues. It does however raise the question whether the circumstances of the project are so exceptional as to warrant a sectoral or strategic assessment under PR1 and that is addressed elsewhere in this Report.

5.5.10 Future Policy and GHG Guidance

The Compliance Review Expert recognises that these requirements were reviewed as part of the ESP revision in 2014. The Compliance Review Expert notes that the 2008 EBRD policy leaves the assessor with some latitude to interpret the scope of the baseline. This can result in significant variation between projects and recommends expansion of the EBRD good practice documentation. Case Studies and Examples would help improve the guidance.⁶¹

There is a wider issue in relation to the appropriate baseline: ‘as is’, ‘with the investment’, ‘without the investment’, ‘if the investment went elsewhere’. Although there is no clear international guidance on this it is increasingly clear that this needs to be considered, especially in relation to fossil fuel extraction and power station projects.

In the case of this project the original investment has been linked to the construction of two new power stations. These are not now being funded by EBRD but the scale of the investment locks EPS into a number of scenarios:

- extended life of the existing old and inefficient power stations
- build new power stations without investment bank funding (EIB, WB, IFC and EBRD have all withdrawn from fossil fuel power station funding)
- abandon the equipment before the end of its operational life.

No consideration appears to have been given to the life of the equipment which has a bearing on the embedded carbon in the project. While embedded carbon would normally be small in comparison to carbon arising from operation this may not be so if the equipment has a short operational life. A very good analysis of the issues surrounding the assessment of investment in fossil fuels is to be found in the 2013 Stockholm Environment Institute discussion Brief⁶² on new fossil fuel infrastructure. This is addressed further in the section on strategic assessment.

5.5.11 Observations and Conclusions

1. Emissions from the new mining equipment provided by the project triggered a GHG assessment under PR3. It is unclear what the definition of AoI or ‘Project Boundary’ with respect to GHGs was or whether the same definition was used for all elements of the project (for example with respect to other environmental or social impacts). The EBRD analysis is based on assertions about the impact on combustion efficiency at the power stations. Some detailed information on GHG reductions associated with the mining equipment was provided by EPS but it was incomplete and was not utilised in the EBRD calculations. The GAP analysis identified that the GHG assessment undertaken as part of the EIAs was not consistent with EBRD guidance. The AoI based on the project as defined in the EBRD Board paper should have been more broadly drawn as described above and the requirement invoked for development of a dynamic baseline.

⁶¹ European Commission Framework Programme 7 Cooperation Thematic Area Environment 6.4 Earth Observation and assessment tools for sustainable development: Best Practice for Reducing the Carbon Footprint of the Mining Industry. October 2011

⁶² Assessing the GHG Emissions Impact of New Fossil Fuel Infrastructure, SEI, 2013

2. EBRD holds multiple investments in EPS, all with impacts on the GHG emissions profile of the group. EPS is synonymous with the mining and power industry in Serbia and fundamental to the underlying carbon intensity of energy generation in Serbia. It would have been consistent with the EBRD transition mandate and its Country and Energy strategies to require a GHG assessment across the Kolubara basin and associated energy production against which future investment and improvements in operational efficiency could be measured. It would have also provided the kind of strategic assessment (as requested by the complainant) which would have exposed the issues around investments in renewables, carbon 'lock in' and carbon intensity more transparently.
3. Based on the lack of clarity around the AoI the absence of an adequate GHG assessment was missed in the gap analysis and therefore excluded from the ESAP. This is inconsistent with PR3. As far as Compliance Review Expert is aware the EBRD calculation of GHG reductions was not made public until complaints were received. As a result the information on GHG emissions and trends in the public domain is extremely limited which is inconsistent with good practice and EBRD commitments on transparency. As far as Compliance Review Expert is aware no ongoing commitment has been placed upon EPS to report GHG emissions.
4. The GHG assessment undertaken on the 'project' is piecemeal, unsubstantiated in terms of supporting information (the values presented to the EBRD Board have not been evidenced and are in some cases not supported by the EPS study) and inconsistent with EBRD guidance and international good practice.

The Compliance Review Expert finds EBRD non-compliant with the general requirements of its ESP and the specific requirements of PR3 with respect to the assessment of greenhouse gas emissions on the Kolubara Environmental Improvement Project.

5.6 Strategic Assessment

The Complainants use a number of issues to argue that EBRD should have undertaken a strategic assessment in relation to the KEIP project. These include the significance of Kolubara within the Serbian Energy Sector, the complexity of the industrial complex, the multiple financings of various aspects of the operation by EBRD and the phenomenon of 'locked in' carbon due to the investment.

The ESP asserts that 'In exceptional circumstances a regional, sectoral or strategic assessment may be required.' The EBRD Management Response states:

Management notes that the current ESP does not place any obligation on EBRD or its clients to undertake strategic assessments. Strategic (environmental) assessments are undertaken of policies plans or programmes and are therefore a tool for national or regional authorities. The Bank may through its policy dialogue with such authorities, support preparation of strategic assessments where they support the environmental or social appraisal of the Bank's projects, especially when there is significant concern for the potential cumulative impact of a number of similar projects in the same geographic area.

By any reasonable interpretation of the ESP there is an obligation upon EBRD to consider whether there are any 'exceptional circumstances' relating to the project. The response

suggests that one such circumstance might be the potential for cumulative impacts in the same geographic area, which is certainly the case at Kolubara. Other potentially exceptional circumstances might be the dominance of EPS and Kolubara in the Serbian energy sector and the long term role that EBRD has taken in supporting the expansion of the lignite mining operations in Serbia against a backdrop of increasing international concern with respect to coal fired power production (especially lignite) and the progressive withdrawal of major financial institutions from the funding of coal fired power production. The inherent difficulty for Serbia in attracting international investment into its energy sector could be an indicator of that dynamic.

EBRD did consider a number of strategic studies in its due diligence and the Compliance Review Expert agrees that where such studies exist they can fulfil the policy requirement. The strategic environmental assessment of the Kolubara basin and EBRD's own energy and Serbia Country strategies provide much of the basis for the strategic involvement.

The Bank's recent updated strategy for Serbia⁶³ focuses on the significant transition gaps in the energy sector, the need to focus on energy efficiency and renewable energy and the need to achieve alignment with EU standards as part of the accession process. The Bank's new Energy Strategy⁶⁴ emphasises the importance of energy efficiency and demand side management and in particular cleaner production and the low carbon transition as it seeks to help countries switch away from coal powered production. Whilst Compliance Review Expert recognises these issues were less prominent in earlier strategies, the direction of travel has been clear. Even amongst similar transition economies Serbia is less well developed and retains high carbon intensity in power production.

EBRD should take a considered view on the adequacy of the strategic basis for a project on a case by case basis and consider whether sectoral, regional or strategic analysis is required to address information gaps which might guide the structure of the project. In the case of the KEIP a number of factors are relevant.

- The EBRD Client is dominant within the Serbian national energy sector which is highly carbon intensive. Further investment essentially locks the client in to lignite based power production for the foreseeable future.
- The Client is a major GHG emitter with limited baseline information and without a history of information disclosure.
- EBRD has a long history of engagement with the client and has sought to align its clients operations over time with EU environmental standards through independent audits of its operations; this has only been partially successful and has been substantially delayed.

Whilst the Compliance Review Expert does not believe that these factors alone would necessarily justify a new sectoral or strategic analysis when significant data was available from other sources, they should have been a material influence on how EBRD approached its

⁶³ Document of the European Bank for Reconstruction and Development Strategy for Serbia: 8 April 2014

⁶⁴ European Bank for Reconstruction and Development: Energy Sector Strategy: 10 December 2013

due diligence on the project and defined the AoI and application of the ESP and PRs. Because of the position of the client and its relevance to the Serbian energy sector, this single investment was in itself ‘strategic’ and the due diligence should have been framed to assess all of the relevant factors consistent with existing and emerging EBRD Sector and Country strategies. It is in this sense that EBRD should have been more strategic.

The Compliance Review Expert does not agree with the assertion that there is no obligation upon EBRD or its client in the ESP to undertake strategic assessments when there is clearly an implicit obligation to address whether the exceptional circumstances exist whereby one would be necessary. However, Compliance Review Expert does not find that a strategic assessment was necessary for Kolubara due to the existing strategic information available.

The Compliance Review Expert does find that EBRD should have been more strategic itself in how it applied that information to its due diligence on the project and the conditionality and requirements therefore placed upon its client. Rather than seek to take a strategic view of the environmental and social implications of the investment in the interests of the client, the Country and affected communities, EBRD constrained its analysis of the impacts. This was inconsistent with the EBRD transition and general objectives for the Project and the general commitments within its ESP. Whilst outside the direct commitments of the ESP the transition objectives for this Project included improvements in Environmental and Social Governance. EBRD failed to draw upon lessons from its successful history of investment into the sector in Serbia with the same client and to robustly pursue improvements in E&S Governance and transparency consistent with that policy.

6 Conclusions, Findings and Recommendations

Observations and conclusions relating to the individual components of this Compliance Review are set out in detail within Section 6. A summary of conclusions is provided here along with the findings.

6.1 Summary of Conclusions

1. The EBRD Board Paper makes it clear that the business activities in which EBRD is investing - ‘The Project’ - is a substantial investment in the Kolubara lignite mining basin to improve the commercial and environmental performance of its existing mining and generation operations and secondly to ensure that it is able to implement the Kolubara B project (and potentially the Nikola Tesla IPP). Transition impacts of the project include anticipated enhancements to environmental and social governance in EPS. The ‘business activities’ and therefore the boundaries of the ‘Project’ includes all of these aspects. This strategic and holistic business approach is not reflected in the environmental and social due diligence issues, which reduced the scope of analysis required, and does not meet the aspirational or detailed requirements of the ESP. In particular the diligence failed to recognise the significance of the CQMS which has basin wide implications. The Kolubara basin should have been identified as the project area of influence and standards applied as appropriate to the components of that area of influence. The due diligence was therefore inconsistent with the general policy requirements relating to Area of Influence and PR1.

2. The EBRD guidance used internally in how to apply the ESP and PRs to the project AoI is not transparent and as currently constituted, undermines the intent of the policy. Any differential application of depth of due diligence and application of standards to different components of the area of influence should be part of the policy framework, not contained within an internal document. The Compliance Review Expert acknowledges that EBRD has been seeking to appropriately apply the Policy wording which is open to alternative interpretations with respect to the Area of Influence of a project.
3. The EBRD interpretation of the application of the policy and the performance requirements to the AoI, is inconsistent across the KEIP and Selova SHP Investments.
4. EBRD did not effectively consider the capacity and commitment of the client in scoping its due diligence and conditionality associated with the project as required by the ESP. In particular it did not look holistically at the E&S requirements it places on the Client and the history of the Client's performance over a long history of investment. EBRD involvement has underpinned the development of the complex since 2001 and consecutive investments have identified shortfalls in environmental and social management capacity within the client organisation. A core transition objective of the KEIP was to improve environmental and social governance. EBRD should have adopted this holistic approach within its E&S due diligence.
5. The IESE and early stages in EBRD due diligence were ineffective in establishing an appropriate Area of Influence for the Project Area or the components which should be addressed or the standards to be adopted for each. As a result the EBRD approach to due diligence and ESP compliance was inadequate.
6. Vreoci sits centrally along the infrastructure spine which services the entire mining/energy industrial complex and adjacent to the industrial area. Any analysis of the impacts of MB Kolubara has to address the situation of Vreoci. Residents of Vreoci should have been identified as stakeholders within the SEP and engaged as appropriate consistent with PR10. Environmental impacts are being addressed within the 2011 audit report undertaken by the Company with EBRD support, however such audits were CP to the 2010 investment and not delivered. Failure to then address the pollution issues from EPS facilities affecting Vreoci as a core conditionality of the KEIP project is inconsistent with PR3.
7. The resettlement of the village of Vreoci should have been considered by EBRD in its due diligence of the KEIP. Though substantively complete under Serbian requirements EBRD should have acknowledged that it could play a more formal strategic role in facilitating the timely and fair completion of the resettlement and have provided support in the validation of outcomes in accordance with Serbian law and good international practice. This could have offset the dominant position of EPS/MB Kolubara and obviated claims of mismanagement, and duress. EBRD should have commissioned a broader review of the social development strategy of EPS including resettlement programmes and their consistency with PR5, in progress across the Kolubara Basin (in parallel to the environmental audits taking place). This would have indicated where EPS needed to be

supported in terms of social capacity, implementation systems (including grievance management) and any financial shortfalls causing programme delays.

8. EBRD seems to have adopted a different definition for AoI or ‘Project Boundary’ with respect to assessment of GHG emissions than for other environmental or social impacts. The EBRD analysis is based on assertions about the impact on combustion efficiency at the power stations, thereby addressing a basin-wide approach to AoI.
9. EBRD holds multiple investments in EPS, all with impacts on the GHG emissions profile of the group. EPS is synonymous with the mining and power industry in Serbia and fundamental to the underlying carbon intensity of energy generation in Serbia. It would have been consistent with the EBRD transition mandate and its Country and Energy strategies to require a GHG assessment across the Kolubara basin and associated energy production against which future investment and improvements in operational efficiency could be measured. As far as the Compliance Review Expert is aware the EBRD calculation of GHG reductions was not made public until Complaints were received, even though requirements on the Client under PR3 were triggered. As a result the information on GHG emissions and trends in the public domain is extremely limited which is inconsistent with good practice and EBRD commitments on transparency. As far as the Compliance Review Expert is aware no ongoing commitment has been placed upon EPS to report GHG emissions. The GHG assessment undertaken on the ‘Project’ is piecemeal, unsubstantiated in terms of supporting information (the values presented to the EBRD Board have not been evidenced and are in some cases not supported by the EPS study) and inconsistent with EBRD guidance and international good practice. It is therefore inconsistent with the general requirements of the ESP relating to GHGs and the specific requirements of PR3.
10. The Compliance Review Expert does not agree with the EBRD Management Response that there is no obligation upon EBRD or its Client in the ESP to undertake strategic assessments. There is clearly an implicit obligation to address whether ‘exceptional circumstances’ exist whereby a strategic assessment would be necessary. The key question being what would constitute exceptional circumstances and should EBRD respond when such circumstances exist. However in the context of KEIP one should not have been necessary. Because of the position of the Client and its relevance to the Serbian energy sector, this single investment was in itself ‘strategic’ and the due diligence should have been framed to assess all of the relevant factors consistent with existing and emerging EBRD Sector and Country strategies. It is in this sense that EBRD could have been more strategic.

6.2 Findings

The summary of findings below is linked to the specific elements of the Compliance Review drawn from the Complaints received by PCM as set out in section 4.

1. Was the ‘area of influence’ and the scope of its due diligence appropriately defined by EBRD in terms of the Kolubara Environmental Improvement Project, having regard to the definition of the Project?

The Compliance Review Expert finds EBRD non-compliant in its application of the ESP general requirements and the requirements of PR1, to the scope of its Environmental and Social due diligence of the Kolubara Environmental Improvement Project.

2. Based on the above - should EBRD due diligence and performance requirements, including stakeholder consultation, have extended to the village of Vreoci?

The Compliance Review Expert finds EBRD non-compliant with the general commitments of the ESP and PR1, 3, 5 and 10 with respect to its exclusion of Vreoci from its due diligence (and application of the PR) on the Kolubara Environmental Improvement Project.

3. Did EBRD appropriately apply the requirements of its ESP and its GHG Assessment methodology in the analysis of the Greenhouse Gas Emissions related to the Project?

The Compliance Review Expert finds EBRD non-compliant with the general requirements of its ESP and the specific requirements of PR3 with respect to the assessment of greenhouse gas emissions on the Kolubara Environmental Improvement Project.

4. Should EBRD have undertaken a 'strategic assessment' of the Kolubara basin due to its national significance and its multiple investments at MB Kolubara.

The Compliance Review Expert does not find that a new strategic assessment was necessary for Kolubara due to the existing strategic information available. The Compliance Review Expert does find that EBRD should have been more strategic itself in how it applied that information to its due diligence on the Project and the conditionality and requirements therefore placed upon its client.

The Compliance Review Expert further finds that rather than seek to take a strategic view of the environmental and social implications of the investment in the interests of the Client, the Country and affected communities, EBRD sought to constrain its analysis of the impacts. EBRD failed to draw upon lessons from its successful history of investment into the sector in Serbia with the same Client and to robustly pursue improvements in E&S Governance and transparency. This was inconsistent with the EBRD transition objectives for the Project and with the intent of the ESP to '*enhance its assessment....of projects to more explicitly reflect the systemic sustainable development dimension of transition and the benefits of a strategic approach in this area.*'

6.3 Recommendations

Based on the Compliance Review Expert's findings, recommendations are framed around two key areas:

- Clarifications to EBRD Environmental and Social Policy and underlying guidance and procedures.

- How to address the ‘strategic gap’ between the approach adopted by EBRD in its due diligence on KEIP and what should have been undertaken in the opinion of the Compliance Review Expert.
1. The EBRD Environmental and Social Policy implementation guidance requires significant clarification. Based upon this Compliance Review the following issues require substantive explanation and guidance.
 - The process of due diligence to be undertaken by EBRD where it has been involved in multiple investments in a single client should be clarified, including how non-compliances with prior environmental or social commitments will be dealt with. A specific procedure to review environmental and social management practices within the client organisation across all of its activities and to include necessary improvements within the project ESAP should be developed. Particular guidance should be developed for situations where the client occupies a dominant position within a sector or region and where its approach and practices have broader socio-economic or environmental impacts. EBRD should be required to consider such broader impacts in its analysis of the required due diligence and AoI.
 - The definition of project area of influence (AoI) and the applicability of the ESP, International Standards and the PRs to the AoI should be clarified. Because of the importance of stakeholders understanding how the requirements and standards of the project are applied, this clarification should be publicly disclosed. EBRD current practice is inconsistent and opaque. Any guidance utilised by EBRD in defining the AoI and application of standards to the AoI should be publicly disclosed and subject to stakeholder engagement and form part of the board agreed policy.
 - The definition of AoI and the scope and scale of E&S due diligence to be undertaken and which has been agreed between EBRD and the Client as part of the IESE or in other due diligence activities should be publicly disclosed.
 - Policy guidance should be expanded and formalised with respect to the circumstances under which sectoral, regional or strategic studies are required to support the diligence on a project and provide clarity over who is responsible for such analysis and the role that EBRD will play in its absence.
 - Policy guidance on the scope and scale of required GHG emissions analysis should be substantively improved in line with current good practice, combined with expanded disclosure requirements. The EBRD GHG emissions assessment ‘guidance’ should be updated in line with current good practice and made mandatory for all EBRD investments.
 2. EBRD should commission a review with EPS of future environmental, social and energy investment strategy for the Kolubara basin. This should address:
 - EBRD priorities based upon its revised energy strategy and Serbia Country strategy, GHG Emissions baseline and future emissions projections based upon projected

future mining, transportation and power plant developments. To include assessment and disclosure of information and objectives relating to effects on Serbian Carbon intensity.

- Analysis of cumulative environmental and social impacts based upon future strategic development of the basin.
- Upgrading of the EPS Environmental and Social Governance capacity and management systems implementation.
- Updates to the action plan relating to implementation of environmental audit findings.
- Review of environmental and social conditions affecting the mining communities within the basin including Vreoci and action plans relating to the management of public services and timely completion of the resettlement process.

Outputs from this work should be publicly disclosed and consulted upon and an appropriate action plan developed.