

**ISSUES OF NON-COMPLIANCE WITH THE WORLD BANK'S
*CRITERIA FOR SCREENING COAL PROJECTS UNDER THE
STRATEGIC FRAMEWORK FOR DEVELOPMENT AND CLIMATE
CHANGE***

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Introduction

As the World Bank’s Independent Evaluations Group has concluded, the Bank’s resources “are best spent in helping clients find domestically preferable alternatives to coal power, such as through increased energy efficiency. Coal support should be a last resort when lower cost and concessionally-financed alternatives have been exhausted and when there is a compelling case WBG support would reduce poverty or emissions.”¹

Towards this end, the *Strategic Framework for Development and Climate Change (SFDCC)* sets out specific conditions that must be met before the World Bank can provide support for new coal power projects.² Under the *SFDCC*, the World Bank must determine that:

- (i) there is a demonstrated developmental impact of the project including improving overall energy security, reducing power shortage or access for the poor;
- (ii) assistance is being provided to identify and prepare low-carbon projects;
- (iii) optimization of energy sources by considering the possibility of meeting the country’s needs through energy efficiency (both supply and demand) and conservation;
- (iv) after full consideration of viable alternatives to the least-cost (including environmental externalities) options and when the additional financing from donors for their incremental cost is not available;
- (v) coal projects will be designed to use the best appropriate available technology to allow for high efficiency and therefore lower GHG emissions intensity; and
- (vi) an approach to incorporate environmental externalities in project analysis will be developed.

To promote consistency and rigor in the application of these requirements, the Bank has issued *Operational Guidance for World Bank Group Staff: Criteria for Screening Coal Projects under the Strategic Framework for Development and Climate Change (Operational Guidance)*.³ The *Operational Guidance* sets out specific “monitoring indicators” that staff must use to determine whether the *SFDCC* criteria have been met. It also provides that for each proposed project, the Bank will engage an “External Panel of Experts” to independently evaluate the quality of compliance with the screening criteria.⁴

In the case of the proposed Kosovo Power Project, the Expert Panel delivered its report to the Bank in January, 2012.⁵ With limited “reservations” and “modifications” the Expert Panel found that the project complies with the six *SFDCC* criteria. However, the Expert Panel failed to

¹ IEG, 2010. *Climate Change and the World Bank Group: Phase II The Challenge of Low-Carbon Development*, at ix.

² World Bank, 2008. *Development and Climate Change: A Strategic Framework for the World Bank Group*.

³ World Bank, 2010. *Operational Guidance for World Bank Group Staff: Criteria for Screening Coal Projects under the Strategic Framework for Development and Climate Change*.

⁴ *Operational Guidance*, at 4.

⁵ Beér, Mielczarski and Taylor, (2010). *Kosovo: Kosovo Power Project Report of the SFDCC External Expert Panel to the World Bank*.

adequately address several important areas of non-compliance with the *SFDCC* criteria. Specifically, the Kosovo Power Project does not meet the *SFDCC* criteria with respect to:

1. Criterion 1: Development impact;
2. Criterion 2: Assistance for low-carbon alternatives;
3. Criterion 3: Assessment of efficiency options; and
4. Criteria 4 and 6: Assessment of externalized costs and potential support for incremental costs.

In light of these shortcomings, the Kosovo Power Project cannot be said to be in compliance with the *SFDCC* criteria.

1. The Project does not meet the requirements of Criterion 1, because the Bank has not adequately demonstrated a developmental impact in terms of increasing energy access for the poor.

The *Operational Guidance* requires that a proposed coal-fired power plant demonstrate development impact by (a) increased access to electricity; and/or (b) improved system reliability.

The *Expert Panel Report* found that the project complied with the energy access criterion because the new plant would make up for the loss of capacity from the closure of the Kosovo A plant, and would help reduce the country's supply/demand gap.

Energy access, however, is a question of more than just supply/demand balance. It also encompasses issues of price, income, and affordability for vulnerable groups. Accordingly, the *Expert Panel Report* should have also addressed whether the proposed project will be able to deliver adequate energy services at affordable rates.

In fact, significant tariff increases will be needed to finance the simultaneous development of a new mine, renovation of Kosovo B plant and the construction of the proposed new 600 MW plant. Indeed, because this investment will create more baseload capacity than Kosovo needs, at least some of these units will operate at substantially less than full load. As a result, it is feasible that tariffs up to four times higher than current rates would be needed to service the total new investments.⁶ Yet, the *Background Paper* significantly underestimates the tariff increases that will be required in the near term, and the *Background Paper* and *Expert Panel Report* fail to examine the impacts of these increases on the Kosovo economy and quality of life of ratepayers. In addition, the project will privatize the existing power plant "Kosova B", thus creating a *de facto* generation monopoly. This will in turn hit hard the consumers with increases in electricity tariffs. This plant is profitable on its own and does not require to be privatized in order to be revitalized.

⁶ Buckheit, 2012. *Reevaluating Kosovo's Least Cost Electricity Option Preliminary Evaluation of the World Bank's December, 2011 "Background Paper, Development and Evaluation of Power Supply Options for Kosovo"*, available at

http://action.sierraclub.org/site/DocServer/Reevaluating_Kosovo_s_Least_Cost_Options_for_Electricity.pdf?docID=8861

2. The Project does not meet the requirements of Criterion 2, because insufficient assistance is being provided to identify and prepare specific low-carbon projects for development.

The *Operational Guidance* sets out specific actions the World Bank must take to assist in identifying and preparing low-carbon projects. These requirements vary depending on the current state of the host country's low-carbon planning and investment. The *Operational Guidance* distinguishes between three scenarios.

- (1) Where studies, policies and/or national strategies for promoting renewable energy, energy efficiency and other low-carbon interventions are not available, the Bank must provide technical assistance to help prepare them;
- (2) Where such studies have already been prepared, the Bank must provide technical assistance to help develop and design a pipeline of bankable projects and other lower carbon interventions. If other donors are also supporting the preparation of bankable projects in the host country, the Bank's work must be additional to these efforts; and
- (3) Where studies and projects design and/or national strategies for promoting renewable energy, energy efficiency and other low-carbon interventions have already been prepared, the Bank must either (a) support the financing of bankable projects and/or implementation of policy recommendations as part of the project; and/or (b) ensure that access to finance for these projects is available from other sources. If the defined pipeline of projects or policy implementation action plan allows for the engagement of several donors, the Bank's financing must be incremental to the efforts of others.⁷

The Expert Panel found that the Project complied with this criterion, based on the fact that (a) several studies of renewable energy alternatives have been conducted; (b) grant assistance is being provided for studies on wind potential, carbon capture and storage, and solar power and water heating; (c) an investment credit is proposed to be provided by the Bank for further work on energy efficiency improvements and renewables; and (d) the Government of Kosovo has instituted a feed-in tariff for small scale hydro and wind.⁸

However, the fact that a number of studies have been conducted or are planned, and a limited set of policies have been adopted, is not sufficient to satisfy the requirements of the *Operational Guidance*. Rather, the *Operational Guidance* makes clear that the Bank must take affirmative steps to develop and fund bankable projects and policy initiatives, above and beyond what others are supporting. The Expert Panel did not discuss any commitment on the part of the Bank to provide assistance to develop and support any specific projects or policy initiatives.

For example, although it referred to the Bank's support for the update of the feasibility study of Zhur, it did not address whether the Bank will actually fund the project. Moreover, private

⁷ *Operational Guidance*, at 6-7.

⁸ *Expert Panel Report*, at 10.

investors in Kosovo have already developed a significant pipeline of renewable energy projects. Although investors have sought licenses for over 200 MW of hydro and wind from the Kosovan Energy Regulatory Office, these requests have not been processed in a timely fashion.⁹ Under the third scenario of the *Operational Guidance*, the Bank should evaluate these projects, and ensure that the bankable projects receive financing, either from the Bank or other sources, before moving forward with the current project.

Moreover, the Expert Panel assumes that the criterion does not require it to review the quality or comprehensiveness of the studies that have been undertaken. Rather, it assumes that the fact that they exist is sufficient. Therefore, the Expert Panel simply lists the studies that have been conducted, without offering any independent assessment of their rigor. This approach would appear to violate the spirit and intent of this criterion. It seems evident that the criterion is intended to ensure project decision-making is made on the basis of a rigorous and comprehensive assessment of renewable energy and energy efficiency alternatives. Studies that are done poorly or are not considered in decision-making should not suffice. Accordingly, the Expert Panels treatment of these studies is inadequate.

3. The Project does not meet the requirements of Criterion 3, because the Bank has not fully evaluated the possibility of meeting the country's needs through energy efficiency (both supply and demand) and conservation.

The *Operational Guidance* specifies actions that the Bank must take in two different scenarios:

- (1) Where energy efficiency studies have already been prepared, the Bank must (a) quantify the reduced energy consumption that would allow the country to avoid/delay the planned increase in power generating capacity from the national or sub-national baseline value; and (b) define the policies and regulations necessary for the above interventions to be made effective, including for pricing strategies (increased cost recovery from tariffs and enhanced collections, targeting of energy subsidies or other methods, including minimum efficiency standards).¹⁰
- (2) Where energy efficiency studies have not been conducted, the Bank must support their preparation and implementation, and assess the potential savings generated from both supply-side reduction of losses in generation and/or transmission and distribution and demand-side management programs to reduce electricity consumption that would allow to avoid/delay the proposed power generating capacity additions.¹¹

The Expert Panel found that the project mostly complied with this criterion. It noted the “considerable efforts” of the Government of Kosovo to improve the efficiency of both supply and demand. It found that on the supply side, “the new project would result in considerable improvements in the efficiency of electricity generation and consume significantly less fuel per unit of electricity produced than the present plants...” On the demand side, the Expert Panel

⁹ These needless delays have raised suspicions that they are intended to keep the “need” for a new coal plant alive in the public debate.

¹⁰ *Operational Guidance*, at 8.

¹¹ *Operational Guidance*, at 8.

found “there are a number of projects and actions that have been implemented in Kosovo, ranging from awareness raising to improving the energy efficiency of many public buildings.”

However, the Expert Panel also expressed reservations, based on the need for increased effort to reduce energy demand and the technical and commercial losses related to electricity supply. Overall, it found that “while energy efficiency measures are unlikely to alter the need for new power generating capacity, they should be important elements of Kosovo’s energy strategy.”

The Expert Panel’s treatment of this issue is wholly inadequate. The *Operational Guidance* places the burden of proof on the Bank to quantify the efficiency opportunities that are available, and to demonstrate that they are not sufficient to avoid or delay the proposed generation expansion, before going forward with the project.¹² Here, there is no evidence in the Report that the Bank has fully quantified the potential energy savings from supply- and demand-side energy efficiency initiatives.

Rather than point out this shortcoming, however, the Expert Panel treats this issue in conclusory fashion, offering its (apparently unsubstantiated) view that “energy efficiency measures are unlikely to alter the need for new power generating capacity.”¹³ In fact, Kosovo’s energy system is highly inefficient. On the supply-side, for example, over 37 percent of overall generated and imported electricity is lost. Over 20 percent of this loss is a commercial loss (mainly theft). The overall losses of electricity equal or exceed the overall production of Kosova A. Kosovan energy company (KEK) has continuously failed to tackle this problem due to the lack of institutional support, mainly that of courts and police. With support, this problem is readily solvable, and would have enormous impact.

Moreover, the Expert Panel inexplicably treats the new plant itself as a supply-side efficiency initiative. This contradicts the clear objective of this criterion, to assess efficiency alternatives to the proposed project that could enable Kosovo to “to avoid/delay the planned increase in power generating capacity.”¹⁴

Due to these shortcomings, the Expert Panel should not have found even partial compliance with this requirement.

¹² *Operational Guidance*, at 8.

¹³ *Expert Panel Report*, at 10.

¹⁴ *Operational Guidance*, at 8. Treating the project itself as an efficiency improvement over Kosova A is also inconsistent with the base case analysis used by the Expert Panel in Criterion 1. In the Criteria 1 analysis, the Expert Panel assumes that Kosova A will be retired, and that the project will make up for its lost supply and thus expand energy access to the poor. Here, the Expert Panel assumes that Kosova A will continue to be operated, and therefore that the proposed project represents an efficiency improvement over the base case.

4. The Project does not meet the requirements of Criteria 4 and 6, because the Bank has not fully accounted for the Project's environmental externalities, and because the Bank has failed to consider how any incremental costs of low-carbon alternatives could be covered by additional financing from other sources.

Criterion 4 of the *Operational Guidance* requires the Bank to conduct a “least-cost analysis” that (a) quantifies environmental externalities; (b) demonstrates that the project is least cost after full consideration of alternatives and after factoring in environmental externalities costs; (c) assesses incremental costs of alternative options (with and without environmental externalities); and (d) evaluates switching prices between the proposed project and alternative low-carbon options [expressed in US\$/ton CO₂]. In addition, Criterion 6 requires that a methodology be developed for assessment of net local (SO_x, NO_x and PM) and GHG emissions at the project level, and that such methodologies inform the analysis of alternatives and least cost options under Criterion 4.

Moreover, where low-carbon alternatives carry an incremental cost over the proposed project, Criterion 4 requires the Bank to (a) identify and evaluate external funding sources to meet the incremental financial cost gap between the proposed project and a lower carbon alternative, and (b) explain the steps it has taken to access such sources, including carbon market, GEF, CTFs, and bilateral donors.

The Bank has met neither the requirement to fully assess and compare the internal and externalized costs of the proposed project and low-carbon alternatives, nor the requirement to identify potential sources of incremental financing for low-carbon alternatives, where the proposed project is determined to be the least-cost alternative.

First, the Bank has not fully explored all potential alternatives. As noted above, the Bank has not fully explored the opportunities to improve efficiency, and the Expert Panel conceded that neither wind nor natural gas alternatives have been fully analyzed.¹⁵

Second, there are compelling reasons to doubt that the proposed project is in fact the least-cost alternative. The Expert Panel cites the World Bank *Background Paper* of December 2011 as the basis for this conclusion, but analyses by the Renewable and Appropriate Energy Laboratory at the University of California Berkeley, and the Kosovar Institute for Development Policy and Sierra Club contradict that conclusion.¹⁶ These studies found that the proposed project will be extremely costly and will necessitate a sharp increase in tariffs, and that a mixture of efficiency and renewable alternatives can provide a lower cost alternative. The Bank should re-evaluate the assumptions and methodology of the December 2011 in light of these studies before concluding that the proposed project is indeed the low cost alternative.

¹⁵ *Expert Panel Report*, at 11.

¹⁶ Daniel M. Kammen, M. Mozafari and D. Prull, 2012. *Sustainable Energy Options for Kosovo An analysis of resource availability and cost*. Available at, <http://rael.berkeley.edu/energyforkosovo>; Buckheit, 2012. Reevaluating Kosovo’s Least Cost Electricity Option Preliminary Evaluation of the World Bank’s December, 2011 “Background Paper, Development and Evaluation of Power Supply Options for Kosovo”, available at http://action.sierraclub.org/site/DocServer/Reevaluating_Kosovo_s_Least_Cost_Options_for_Electricity.pdf?docID=8861

Third, the Bank has failed to adequately internalize all relevant environmental costs. Thus, the *Expert Panel Report* fails explain how the Bank has assessed, quantified and internalized the impacts of the rehabilitated Kosovo B and the new Kosovo C power plant on competing uses and environmental values in the “severely stressed”¹⁷ Iber-Lepence water system.¹⁸

The Bank has also failed to internalize the costs of the mine complex. The *Operational Guidance* is clear that the impacts of upstream activities such as coal mining and processing must be internalized if they are “developed for the purposes of supplying fuel feed stock for specified coal-based power generation facilities....”¹⁹ Although the proposed new mine complex clearly meets this standard, neither the *Expert Panel Report* nor the *Background Paper* quantifies or internalizes the substantial costs associated with the mine’s development and operations, including those caused by expansion of mining operations, resettlement, impacts on local agriculture, road upgrades and maintenance, mine reclamation, and ash dump costs (associated with mining and Kosovo C).

Fourth, even assuming that the proposed project is the least-cost option including externalities, the Bank must still “identify and evaluate external funding sources to meet the incremental financial cost gap between the proposed project and a lower carbon alternative.” It is entirely insufficient to simply conclude that there is a cost gap; the Bank must also determine that the cost gap cannot be filled by other sources. However, the *Expert Panel Report* provides no discussion of whether the Bank has undertaken this analysis, or reached out to other potential funders. The requirements of this criterion have not been met until alternatives for incremental cost financing such as the CDM, the GEF, the CTF, and other multilateral and bilateral donors have been explored and exhausted.

Conclusion

In light of the shortcomings identified above, it is evident that the Bank has not satisfied the letter or the spirit of the *SFDCC* criteria. In short, it has not met its burden of showing that no lower cost or concessionally-financed alternatives are available, or that Bank support for this project is the best way to expand energy access and meet the pressing energy needs of Kosovo. That being the case, it would not be appropriate for the Bank to provide support for this project.

¹⁷ Currently, the water exploitation index (WEI) is assessed at 50% for an average year. Severe water stress can occur where the WEI exceeds 40%.

¹⁸ The World Bank-utilized water supply study appears to have underestimated competing demands for requirements for potable water, hydropower, and irrigation. COWI, 2008. *Water supply from the Iber-Lepenc hydro system for the proposed Kosovo C power plant*.

¹⁹ *Operational Guidance*, at 3.