About this Report

This Report, which covers EBRD activities in 2005, focuses on the Bank’s impact on the people and the environment in the countries where we operate. It also describes how we operate internally.

Part 1 of the Report focuses on the EBRD’s overall approach to financing projects – which is where our greatest contribution to sustainability lies. Part 2 is a special focus on energy, covering the development of the EBRD’s new Energy Policy and the Bank’s activities across the energy sector. Part 3 looks at issues of transparency and accountability while Part 4 covers the Bank’s own internal performance. Information about the Bank’s project approval process and other operational issues are detailed in the annex to this Report.

About the EBRD

The European Bank for Reconstruction and Development invests in the businesses and financial institutions that form the core of strong market economies in 27 countries from central Europe to central Asia. Our capital is provided by 60 governments and two intergovernmental institutions.

The EBRD invests in virtually every kind of enterprise and financial institution, mainly in the form of loans and equity. Investments are designed to advance the transition to market economies, to set the highest standards of corporate governance and to promote environmentally sound and sustainable development. We seek to finance only those projects that will benefit from EBRD involvement and which cannot be funded on equivalent terms by the private sector.

The EBRD’s Environmental Policy is the umbrella for much of the Bank’s mission to work in a socially and environmentally responsible way. In support of our investment activities, the EBRD conducts policy dialogue with governments to develop the rule of law and democracy. For more information about the Bank, please see our web site at www.ebrd.com.
2 President’s foreword

Energy is needed to sustain any society, but energy itself needs to be sustainable. Across the EBRD region, there are four countries that are well-endowed with energy sources and the others are dependent on imports.

But all the countries, without exception, inherited the decidedly unsustainable approaches to energy that prevailed in planned economies where light, heat and power were treated as virtually free goods.

For the EBRD – and this report – a focus in 2005 was energy. The starting point is enhancing energy efficiency. Saving energy that would otherwise be wasted is equivalent to adding to energy supply as well as reducing pollution and preserving resources. And there is vast scope for efficiency gains in a region that is seven times more energy intensive than Western Europe and produces 30 times more greenhouse gas per unit of gross domestic product.

For several years, the Bank has encouraged efficiency by auditing proposed industrial investments to determine whether the project – from steel mill to sawmill or glass manufacturing – could benefit from investment in energy-saving measures. In many cases, in many sectors, the Bank has provided additional capital to invest in making the energy use more efficient, often with complementary funding from donors.

And the EBRD is expanding its investments in district heating, energy savings companies, credit lines to banks for enterprises or residences to upgrade their energy efficiency, and funds dedicated to renewable energy or efficiency investments. This kind of financing is at the heart of the new Energy Policy that was drafted and reviewed by the public in 2005-06.

A country such as Bulgaria is emblematic of the region’s energy problems and the solutions. Bulgaria has few energy sources beyond abundant, relatively cheap but highly-polluting lignite coal. To a large extent, it relied on energy from Soviet-era nuclear installations that were so unsafe that much of that nuclear capacity has been shut down.

To improve the acid rain problem from what was once Europe’s most polluting coal-fired power plant, the EBRD led with financing to meet EU standards. To compensate for some of the loss of nuclear supply, funding was provided by the international community, and the EBRD established credit lines with Bulgarian banks so that they could make loans to businesses for energy-saving measures and to householders to retrofit their homes.
It is heartening to visit a baker in Sofia who used the loan to cut energy costs by 85 per cent, or the developer of a ski resort that made similar savings converting to thermal heating. Their motivation was to become more competitive in a country that will soon join the European Union. But the result is a more sustainable energy prospect for Bulgaria and a cleaner, safer environment too.

Certainly, traditional forms of energy are still very much part of the EBRD agenda. The Bank will continue to reconstruct and upgrade generation and hydro plants, make electricity transmission and distribution safer and more efficient, and work on rational, sustainable pricing structures for public utilities.

Oil and gas pipelines to carry resources that are much in demand in the region and beyond must integrate high environmental standards and reflect full consultation with people affected. In 2005 the EBRD endorsed the Extractive Industries Transparency Initiative to underline its support for fair revenue management and transparency in petroleum projects. Intensive effort to make oil and gas projects beneficial to the community and reflect the views of all affected communities have become an EBRD benchmark.

The new reality is that there is increasing understanding of – and growing world pressure to address – the dual issues of climate change and energy security. In 2005 the European Union and the G-8 summit both called for concerted international action to promote sustainable energy, with a clear role for international financial institutions in supporting clean energy and energy efficiency. The EBRD is playing a leading role, introducing carbon trading initiatives related to the Kyoto Protocol, a joint multilateral Carbon Credit Fund established along with the European Investment Bank, and a climate change initiative for 2006. If launching such initiatives was a focus for 2005, sustainable energy will remain a priority for 2006 and the coming years.

Jean Lemierre
President
4 Where we operate

The EBRD operates in 27 countries from central Europe to central Asia.

1 Albania
2 Armenia
3 Azerbaijan
4 Belarus
5 Bosnia and Herzegovina
6 Bulgaria
7 Croatia
8 Czech Republic
9 Estonia
10 Former Yugoslav Republic of Macedonia
11 Georgia
12 Hungary
13 Kazakhstan
14 Kyrgyz Republic
15 Latvia
16 Lithuania
17 Moldova
18 Poland
19 Romania
20 Russia
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22 Slovak Republic
23 Slovenia
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26 Ukraine
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Early transition countries
2 Armenia 3 Azerbaijan 11 Georgia
14 Kyrgyz Republic 17 Moldova 24 Tajikistan
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EU member countries
8 Czech Republic 9 Estonia 12 Hungary 15 Latvia
16 Lithuania 18 Poland 22 Slovak Republic
23 Slovenia
2005 highlights

Environmental investments

The EBRD invested €346 million in energy efficiency, municipal infrastructure and clean-up operations in 2005, representing 8 per cent of the Bank’s total investment for the year. This generated additional environmental investment of €552 million from the EBRD’s clients.

The Bank provided a further €369 million for the environmental aspects of projects in other sectors, such as manufacturing, heavy industry and agribusiness. This generated additional environmental investment of €269 million from EBRD clients.

Consultation

The Bank consulted widely with governments, industry, non-governmental organisations (NGOs), research institutes and think-tanks on its draft Energy Policy in 2005.

We also liaised extensively with NGOs and local communities on projects with complex environmental considerations, such as a proposed EBRD investment on Sakhalin Island.

Environmental and social monitoring

EBRD staff made environmental and social monitoring visits to 26 projects in 14 countries in 2005. Four of these visits focused specifically on social monitoring.

In 2005 the Bank appointed its first social development expert, whose role is to work with the Bank’s clients to address potentially negative social impacts and to identify opportunities to increase community benefits.
The EBRD invested €255 million in 2005 to promote the growth of small businesses, which are vital for the creation of jobs and for a country’s long-term growth.

EBRD financing is provided through over 1,000 local banks that on-lend EBRD financing and their own funds to small businesses. In 2005 some 480,000 loans totalling €2.5 billion were provided.

Projects with high social benefits

Helping the poorest countries

In 2005 the EBRD invested €250 million in 61 projects across the seven poorest countries where the Bank operates – the early transition countries.

Investment was almost three times higher than 2004 levels. Supported by donor funding, the Bank’s investment is helping to boost business growth and to alleviate poverty.

Working with donors

The Bank makes full use of donor funding to support initiatives in health and safety, pollution reduction and the growth of small businesses. Notable projects in 2005 included:

- an electrical safety awareness campaign in Moldova to educate children and their parents on the dangers of stealing electricity from power lines and substations
- completion of the St Petersburg Southwest Waste Water Treatment Plant to improve living conditions for 50 million people
- a loan in local currency and training for a Kazakh microfinance organisation, which is now able to make small loans to local businesses.

Helping the poorest countries

Projects with high social benefits

Working with donors
Investing responsibly

In 2005 the EBRD invested a record €4.3 billion in 151 projects across the 27 countries where the Bank operates (from central Europe to central Asia). We expanded our investments in energy efficiency and operations to clean up polluted land and rivers and conducted more environmental and social monitoring visits. In particular, we increased our investment in smaller projects, in keeping with the needs of the less developed countries.
Every EBRD project aims to help our countries of operations move towards a future that is sustainable. By optimising the environmental and social benefits of EBRD-financed projects, we can help to achieve positive change.

The Bank’s commitment to sustainable development covers both the environmental and social impact of EBRD-financed projects, including health and safety, labour and community issues. Our activities reflect good practice among international financial institutions (IFIs) and in both the public and private sector. The EBRD seeks to improve the investment climate of the countries where we operate and to finance projects that will help to build sustainable market economies and to alleviate poverty, particularly in the early transition countries (ETCs) – the poorest countries in the EBRD’s region.

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The EBRD has independent mechanisms in place to verify that the Bank’s operational policies, procedures and other requirements are being met by EBRD staff. The key departments within the Bank to evaluate performance against the Bank’s mandate and to provide additional checks and balances are the Internal Audit Department, Risk Management, the Evaluation Department and the Chief Compliance Office.

Environmental Policy
The EBRD’s Environmental Policy underpins the Bank’s commitment to sustainability in all our activities. It commits the Bank to:

• fully integrating environmental and social considerations into the project cycle and ensuring that each project considered for financing undergoes environmental and social appraisal
• promoting environmental investments across a variety of sectors to achieve resource efficiency, cleaner production processes, biodiversity and best practice in environmental management
• financing projects with clear environmental objectives, such as better water and waste-water management, energy efficiency and renewable energy
• working in partnership with other institutions to address regional and global environmental issues.

The social dimension within the EBRD’s Environmental Policy establishes minimum performance standards in line with good international practice and in compliance with the relevant International Finance Corporation (IFC) Safeguard Policies. The standards are applied for issues such as the involuntary resettlement of people and the protection of indigenous
people and cultural heritage in areas affected by Bank-financed projects.

The Bank also requires that all projects meet the applicable provisions of the International Labour Organization (ILO) conventions relating to child labour, forced labour and discrimination as well as all applicable national laws and standards on employment.

At the end of 2005 the Bank started planning its three-yearly review of the Environmental Policy, which it will carry out in 2006.

Promoting democracy and market economies

The EBRD is committed to promoting democracy and market economies throughout our countries of operations in line with Article 1 of the Bank’s Founding Agreement. The Bank supports economic and democratic reform through investment and regular dialogue with governments. In 2005 the EBRD worked with national and local authorities to develop sound legal frameworks, to improve corporate governance and to encourage progress in democratic reform.

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Country strategies

The EBRD’s country strategies provide an overview of the needs and priorities in each country where we operate. They also provide a basis for dialogue with the government, relevant authorities and local communities about the Bank’s activities.

In keeping with its mandate to promote economic and democratic reform, the EBRD reviews country strategies every two years. Each new country strategy approved by the Bank includes an assessment of the country’s compliance with Article 1 and with internationally recognised civil and political human rights. The strategy also covers issues such as poverty and social exclusion as well as environmental conditions, legislative progress and the impact of EBRD projects.

Before preparing a new country strategy, the Bank monitors and analyses political and legal developments and visits the country (including project sites) to gather information. Our aim is to make a fair and balanced assessment of whether the country is fulfilling the principles of the EBRD’s mandate. In developing a new strategy, the Bank considers the country’s stage of transition and the economic and political framework of the country.

In the more developed countries, the emphasis is mostly on supporting transition to fully developed market economies. In the less developed countries, priorities might be to strengthen the regulatory and legal framework for private investments, to support diversification of the economy and to increase the number and range of EBRD projects.
12 Investing responsibly

In the poorest countries where the EBRD operates, the emphasis is mostly on increasing the availability of finance for the private sector (for small businesses in particular), strengthening the banking sector and improving vital infrastructure, such as water distribution and transport. In these countries, the Bank is able to make use of methods of financing under the EBRD’s ETC Initiative (see pages 32-34).

New country strategies in 2005
The EBRD published 12 new country strategies in 2005 covering Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Hungary, Latvia, Moldova, Romania, Tajikistan, Ukraine and Uzbekistan.

In adopting a new strategy for Uzbekistan in July 2005, the EBRD expressed concern that the country’s progress towards implementing Article 1 of the Bank’s Founding Agreement continued to be slow and characterised by setbacks. A particular cause of concern for the Bank was the state’s indiscriminate use of force against civilians in Andijan in April 2005. Because of these concerns and the country’s poor prospects for political liberalisation, the EBRD has restricted its investments since July 2005 to private sector activities. However, existing public sector commitments will still be implemented.

The lack of progress in democratic and economic reform in Belarus and Turkmenistan has led the EBRD to severely limit its activities in these countries as well. The Bank is financing only private sector activities while continuing to seek ways of improving the investment climate and supporting reform efforts.

All EBRD country strategies are published on the Bank’s web site in English and in local languages (see page 63).

Measuring the EBRD’s sustainability footprint
One of the challenges for the EBRD is to find key performance indicators to measure how the Bank implements its Environmental Policy commitments and to assess the environmental and social impact of the projects we finance.

The Bank is developing performance indicators that it can use to measure environmental and social change “on the ground” as a result of our investments. One of the most important portfolio indicators already in use is the amount of greenhouse gases (GHG) associated with our projects (see pages 45-46).

Key performance indicators

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Other indicators under consideration include the number of people newly connected to clean water and sewerage systems, and common environmental performance data, such as water use and air emissions. In 2005 we designed a new reporting and monitoring system for project data (which will be rolled out in 2006). It will allow us to keep track of the environmental and social performance of EBRD-financed projects and to produce data on the performance of our project portfolio.

Appraising and monitoring EBRD-financed projects

The EBRD’s Environment Department is responsible for ensuring that the Bank takes account of environmental and social issues in all EBRD-financed projects. The department identifies projects with specific environmental aims, conducts project appraisal and monitoring (including site visits, audits and reporting) and provides advice and training to Bank staff on environmental, health and safety and social issues.

Before investing in any project, the Bank undertakes an environmental appraisal to identify any action that the client needs to take to comply with the EBRD’s Environmental Policy. These requirements become binding when the project is signed. Environmental expenditure by clients is in addition to the EBRD’s environmental investment (see page 22).

The Bank undertakes an environmental appraisal to identify any action that the client needs to take to comply with the EBRD’s Environmental Policy.

For the most environmentally sensitive projects, the Bank undertakes extensive public consultation. We also monitor projects throughout their lifetime. In 2005 we published information about 181 projects under consideration for EBRD financing.

Focus on integrity

Integrity and money-laundering issues are an integral part of project appraisal. The Bank makes every effort to ensure that EBRD financing is used for its intended purpose.

The Chief Compliance Office (CCO) has overall responsibility for integrity issues, both project-related and within the Bank. The CCO provides advice on the suitability of prospective Bank clients, and investigates allegations of fraud, corruption and misconduct. The office was strengthened in 2005.

Working towards a unified approach

In 2005 the EBRD reviewed its procedures for investigating allegations of fraud, corruption and collusive or coercive practices in procurement operations funded with EBRD finance. As a result, the Bank increased its cooperation within the Multilateral Development Bank Investigators Forum. This brings together the investigative units of the EBRD, the African Development Bank, the Asian Development Bank, the Inter American Development Bank and the World Bank. This collaboration will lead to a unified approach to the definition and investigation of fraud and corruption across these five international financial institutions.

Ethical behaviour and integrity

The EBRD follows specially defined procedures to review the shareholders, corporate governance and procurement processes of a client company before approving financing for a project. We also review the client’s audited financial statements based on best practice. We pay particular attention to identifying the ultimate beneficiaries of any company seeking to receive EBRD finance.
Investing responsibly

Integrity investigations involve identifying whether there is any suspicious or unethical behaviour by the client, its management or shareholders. We carry out a legal check to evaluate a client’s status, assets and liabilities.

In 2005 the EBRD delivered a training programme designed to remind all staff members of their ethical obligations as employees of an intergovernmental organisation. We also continued to review the Bank’s Code of Conduct. The Bank’s Board of Governors is expected to adopt revised codes in 2006, covering the behaviour expected of the Board of Directors and EBRD staff.

Corruption
The EBRD works closely with our countries of operations to promote institutional reforms that tackle the problem of corruption. In 2005 the Bank started work on an anti-corruption report that sets out what the Bank is doing to combat corruption, such as money laundering and terrorist financing. The report will be published by the Bank’s Chief Compliance Office later in 2006 and will be produced annually.

The EBRD works closely with our countries of operations to promote institutional reforms that tackle the problem of corruption.

Combating money laundering is a key to improving the investment climate. In 2005 the Bank launched a training programme aimed at local financial institutions to raise awareness of best practice. Pilot training courses were delivered to banks and regulators in Bosnia and Herzegovina, FYR Macedonia and Central Asia.

Building on these pilot courses, the EBRD conducted fact-finding visits to 16 countries to find out more about anti-money-laundering issues. These visits allowed the Bank to develop a training programme with the support of the European Union and the Swiss State Secretariat for Economic Affairs.

A series of training workshops targeted at staff from financial institutions and relevant regulators was completed by the end of the year. The workshops covered money-laundering risks and best practice for addressing this issue. Over 200 bankers from institutions in ten countries have so far been trained on the programme.

Portfolio monitoring
Attentive monitoring of the EBRD’s growing portfolio is a key part of the Bank’s business activities. As we continue to develop new business and to expand into more challenging areas, the Bank needs to ensure that high standards are maintained in our portfolio of existing projects and that key objectives – in the areas of environment, governance and procurement, for example – are always met.
A new Business Group Director for Portfolio Monitoring was appointed in 2005 to work with the Bank’s business groups. The director supports departments in monitoring portfolio risks and provides assistance in tackling potential problems.

**Environmental and social monitoring**

Every EBRD-financed project is monitored to ensure that the client implements the environmental and social standards included in the project’s legal agreements. Monitoring includes assessing the effectiveness of measures taken to reduce any negative environmental or social impact. Monitoring stops when the loan has been repaid or when the Bank divests its equity share in a company or if the project is cancelled.

The Environment Department allocates an environmental risk rating for monitoring purposes to all EBRD-financed projects under implementation. High-risk projects are monitored more intensively and more often than those with a lower risk. All projects are reviewed by the Environment Department at least once a year.

**Monitoring visits**

At the end of 2005, 754 EBRD projects were under implementation. Of these, 54 were rated as having a high environmental risk, of which 11 were subject to monitoring visits in 2005. EBRD staff made monitoring visits to 26 projects in 14 countries (including audits by Bank staff and independent experts). Four of these missions focused specifically on social monitoring, including visits to Azerbaijan and Georgia in relation to the Bank’s ongoing involvement in the Baku-Tbilisi-Ceyhan pipeline project (see page 16).

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**Environmental categories in 2005**

Each EBRD-financed project receives two environmental classifications:

- **The first** indicates the type of analysis needed to assess the expected future environmental/social impact of the project. Category A indicates projects with the highest potential impact. Financial intermediaries are not included and are classified simply as FI. Of the projects signed by the EBRD in 2005:
  - 2 per cent were classifed as category A (requiring an environmental impact assessment)
  - 22 per cent were classifed as category B (requiring an environmental analysis)
  - 7 per cent were classifed as category C (requiring comprehensive due diligence but neither of the above)
  - 64 per cent were classifed FI.

- **The second classification** indicates whether an environmental/social audit is needed to assess the environmental performance of an existing facility. Of the projects signed in 2005:
  - 22 per cent were classifed as 1 (requiring an environmental audit as part of the due diligence process)
  - The balance were classifed as 0 (not requiring an audit).
Monitoring the BTC oil pipeline

The EBRD's €106 million investment in the Baku-Tbilisi-Ceyhan (BTC) oil pipeline was signed in February 2004. The Bank’s continuing involvement includes environmental and social monitoring visits to assess compliance and progress. Experts from the EBRD's Environment Department make regular and extensive visits to monitor compliance with EBRD policy and international standards (set out in the legal agreements) and to ensure that commitments made by the client to mitigate environmental and social impacts are being met.

As well as aiming to promote long-term economic development in Georgia and Azerbaijan, the EBRD aims to ensure that the BTC project will benefit local communities in the long term. As a result, the Bank increased its monitoring visits in 2005 to check on social issues, such as resettlement compensation, resolution of grievances and implementation of community development programmes.

The EBRD undertook four monitoring trips in 2005. During these trips, the Bank met with the Georgian Ministry of Environment to discuss the BTC Oil Spill Plan and with the Ministry of Economy and Finance. The Bank discussed the resettlement of Dgvari village and our potential role in assisting the government to develop and monitor the resettlement process. A comprehensive Resettlement Action Plan was prepared to address the land acquisition impact of the BTC project. The plan includes a Vulnerable Peoples Initiative, which aims to assist those less able to restore their livelihood through existing compensation mechanisms. The initiative has assisted approximately 4,000 people (including pensioners and the disabled) in Georgia.

Land compensation has been especially challenging in Georgia because of the complexities of the country's land registration system. Although some 97 per cent of land parcels have now been compensated for, more time will be needed to unravel the contentious remaining cases. Compensation payments are also in progress in Azerbaijan.

BP and its partners in the BTC consortium and the South Caucasus gas pipeline project (SCP) consortium have already channelled some €21 million to community investment programmes in Azerbaijan, Georgia and Turkey. These range from the renovation of school buildings to the establishment of irrigation systems and from local micro-finance to sewerage systems.

A Regional Development Initiative (RDI) has been developed by BP, the main project sponsor, and its partners to create long-term benefits and sustainable economic development. Part of the initiative will be co-financed by and implemented with EBRD assistance. The EBRD component will foster private sector growth through a broad range of grassroots initiatives, such as loans and grant funding for micro businesses, training programmes and infrastructure.

BP has committed an initial €5 million for the first phase of the EBRD/RDI partnership, and will endeavour to solicit additional commitments from its partners with the aim of raising a total of €21 million for the joint facility.
In 2005 the EBRD increased its emphasis on assessing social issues and integrating social appraisal into the overall appraisal process. A new position for a social development expert was funded by the UK government and filled in February 2005. The expert works with the Bank’s clients to tackle potentially negative social impact and to identify opportunities to increase community benefits. On more complex projects, this involves field visits and a high level of monitoring (see pages 14-15).

A new position for a social development expert was funded by the UK government and filled in February 2005.

Projects in the oil and gas, mining, heavy industry and infrastructure sectors are likely to have a significant social impact. The social development expert is supported by international labour rights consultants who are retained to advise the Bank on the implementation of the labour aspects of the EBRD’s Environmental Policy.

The appraisal of all projects includes highlighting relevant social issues and identifying action needed. When issues are identified, the first aim is to ensure that the standards within the EBRD’s Environmental Policy are met. Beyond this, the Bank encourages clients to take proactive measures to identify ways that a project could improve the livelihood and quality of life of affected communities. Such measures are often agreed in the form of a community development programme to complement the main investment.

The standards in the Bank’s Environmental Policy require that indigenous people must not only be compensated for any hardship experienced as a result of a project but must also benefit from a project.

Regarding a potential EBRD investment on Sakhalin Island (see pages 66-67), the Bank’s staff worked with the client (Sakhalin Energy) to draw up an Indigenous Peoples’ Development Plan. This is now under way and being implemented according to best international practice. The client is working in partnership with the indigenous people and has agreed to give some €250,000 to finance improvements, irrespective of whether the EBRD decides to go ahead with the investment.

Community development programmes

Engaging with the community and ensuring that local communities benefit from projects is increasingly seen as a form of good corporate citizenship. It is particularly important when a company is developing new facilities or processes and/or large natural resources. Community development programmes are designed to benefit all sections of a community equally (the old, young, women, minorities and vulnerable groups), ensuring that decisions are not made by one dominant section. Communities are asked to choose what is most important to them – for example, health, education, culture, improved access to infrastructure.

Addressing core labour standards

When addressing labour standards in a prospective project, the EBRD considers three of the International Labour Organization (ILO) core principles: no forced labour, no harmful child labour and no discrimination in the workplace. The Bank’s Environment Department provides guidance and support to bankers and clients on these issues.

The Bank collects key information to identify issues relating to the core labour standards referred to in the EBRD’s Environmental Policy. Clients are expected to comply with national labour laws and regulations as well as the standards incorporated in the policy.
Improving labour relations at a hypermarket chain

Following EBRD investment in a hypermarket chain with outlets across central Europe, it was alleged that the company was not complying with labour laws. Specifically, this related to long working hours and the non-payment of overtime.

After an inspection by the National Labour Inspectorate (NLI), the EBRD engaged an independent expert on labour rights, who carried out a project monitoring visit with Bank staff in June 2005. The EBRD also held meetings with the NLI and trade unions.

Following discussion of the issues, the company agreed to improve labour relations within the company and undertook to:

• implement a new procedure to record working hours throughout the company
• ensure that overtime is paid at agreed rates
• train market managers in people management
• ensure that recruitment agencies that supply labour comply with national labour laws
• report annually to the EBRD on the implementation of labour and HR procedures.

The company is required to observe national labour laws and standards as well as the requirements of the Conventions of the International Labour Organization relating to the employment of children and young people, discrimination at work and forced labour.

A subsequent report from the NLI reported significantly improved compliance with national labour laws within the company’s operations. The EBRD continues to monitor labour issues in the project as part of its standard project monitoring.

Labour standards appraisal and monitoring
EBRD screening identifies specific risks that need to be addressed by the client to comply with core labour standards. If the Bank identifies a particular risk, it assesses the extent of the risk and asks the client to confirm what action is being taken to address this. Undertakings by clients commonly include:

• a commitment to review and improve the company’s human resources policies
• agreement to non-discriminatory recruitment policies
• assessment of contractors’ compliance with labour standards.

Project monitoring may sometimes indicate problems of compliance with labour standards that are endemic in the sector or country and that are beyond the scope of the client to correct. Where this occurs, the EBRD seeks to work with other agencies, such as the ILO, to improve labour rights in the sector or country with the help of donor funding.

Labour training workshops
The EBRD ran a series of training workshops on labour issues in 2005. These were attended by a total of 125 banking staff at the EBRD’s Headquarters. Staff at the Bank’s Resident Office in Kiev have also benefited from the workshop. Training is to be extended to other regional offices later in 2006.

The aim of the training was to build understanding of labour issues and how they are integrated into the Bank’s project cycle. The workshops helped to clarify how the Bank’s Environmental Policy is implemented. For example, if a privatisation project results in workforce cuts, the policy addresses how the cuts should be made to ensure that they are undertaken in
a justifiable manner based on national law and collective agreements and with no discrimination.

**Independently evaluating EBRD activities**

The Evaluation Department (EvD) evaluates selected EBRD projects. EvD operates separately from banking operations and in 2005 began reporting directly to the Bank’s Board of Directors to strengthen its independence.

EvD evaluates all aspects of EBRD-financed activities, including consultant assignments funded through donor funding. The evaluation considers the impact of EBRD projects on the transition process and the project’s environmental performance, which includes health and safety, labour and other social issues. Assessments are made against the objectives established for each EBRD project, the requirements of the Bank’s Environmental Policy and the relevant country and sector strategies. The evaluation considers, for example, the environmental change between the start and finish of the project.

**The evaluation considers the impact of EBRD projects on the transition process and the project’s environmental performance.**

Projects are assessed usually one to two years after final disbursement. From 1996 to 2005, EvD assessed 469 operations. Of these, 54 per cent achieved a transition impact rating of “good” or “excellent” and a further 23 per cent were assessed as “satisfactory”. In 2005, 85 per cent of the Bank’s evaluated projects had an “excellent-satisfactory” impact on the transition process. Since 1993, EvD has evaluated over 450 grant-funded consultant assignments. These assignments were donor funded and have involved over €130 million of funding from 28 countries and 29 multilateral funds under the Bank’s Technical Cooperation Funds Programme.

**Projects evaluated in 2005**

Of the 53 projects evaluated in 2005, the environmental performance of the client and the Bank was rated “excellent” in 15 per cent of cases, “good” in 43 per cent, “satisfactory” in 28 per cent and “marginal” in 13 per cent. No projects were rated “unsatisfactory” or “highly unsatisfactory”.

Assessing environmental change, the differences in 27 per cent of projects were rated “substantial” or “outstanding”. Some differences were found in 56 per cent, and no difference was found in 17 per cent. No projects recorded a “negative” change in 2005.
Examples of Evaluation Department special studies in 2005

Mongolia Cooperation Fund

The acceptance process for Mongolia to become a new EBRD country of operations moved closer to completion in 2005. To help the country prepare for future EBRD investment, the Bank has used funding from the Mongolia Cooperation Fund (MCF). This has supported private sector activity and improvements to the investment climate. The fund receives donor contributions from Japan, Luxembourg, the Netherlands and Taipei China.

Between 2001 and 2004, the Fund committed €6.3 million to 11 assignments aimed at improving managerial capacity and supporting programmes with high social benefits. They included:

- TurnAround Management (TAM) advisers in 22 companies
- a management team at Mongolia’s national airline
- micro credit advisers within a major Mongolian bank
- training for nearly 300 bank managers and staff
- studies into the privatisation of the power and telecommunications sectors, the implementation of legal reforms, and the development of infrastructure and natural resources.

Evd rated five of the seven completed assignments as “successful”. Three of the four still under way are also expected to achieve successful ratings. Overall, the 11 projects are expected to achieve positive results, with seven (representing 86 per cent of the Fund’s total commitments) achieving the key investment objectives set by the EBRD and the MCF.

Changes to project conditions

A commitment to sustainability includes acting responsibly and transparently. As far as EBRD financing is concerned, this means following the correct procedures if the Bank agrees to make any changes to a project during implementation. Changes may include agreeing to waive a covenant in a loan agreement or amending the project’s terms and conditions. All changes must be approved internally before a client is notified. Major changes must be approved by the Bank’s Board of Directors.

A commitment to sustainability includes acting responsibly and transparently.

In 2005, EvD evaluated the impact of waivers, amendments and consents on project objectives. The study analysed 557 such changes across 60 projects approved between 1 September 2000 and 31 August 2001 which had received a minimum Bank investment of €10 million. Around one-third were public sector projects and two-thirds in the private sector.
The study concluded that the volume and frequency of changes was in line with the levels experienced in commercial banks, that the Bank’s processing of changes is in line with best practice and that the Bank’s documentation and project conditions were not excessive or unrealistic.

Investing for sustainable development

A key way to view the impact of the EBRD’s activities is through the projects we finance. In 2005 the EBRD invested across a wide range of sectors and made its highest-ever level of investment. The EBRD invested €4.3 billion: €2.5 billion in early and intermediate transition countries, €1.1 billion in Russia and €0.7 billion in advanced transition countries.

Over one-third of the EBRD’s business volume was devoted to financial institutions to support local enterprises while one-fifth supported infrastructure developments, including municipal and public transport projects. The Bank’s focus on the poorest countries led us to finance many smaller projects aimed at helping the least well-off.

The Bank’s focus on the poorest countries led us to finance many smaller projects aimed at helping the least well-off.

### EBRD investments 2004-05

<table>
<thead>
<tr>
<th>Sector</th>
<th>2005 (€ million)</th>
<th>2004 (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Financial institutions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank equity</td>
<td>94.6</td>
<td>197.3</td>
</tr>
<tr>
<td>Bank lending</td>
<td>796.7</td>
<td>858.9</td>
</tr>
<tr>
<td>Equity funds</td>
<td>284.4</td>
<td>185.5</td>
</tr>
<tr>
<td>Non-bank financial institutions</td>
<td>196.1</td>
<td>173.9</td>
</tr>
<tr>
<td>Small business finance</td>
<td>55.7</td>
<td>71.8</td>
</tr>
<tr>
<td><strong>Energy</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy efficiency</td>
<td>16.0</td>
<td>60.8</td>
</tr>
<tr>
<td>Natural resources</td>
<td>196.2</td>
<td>439.6</td>
</tr>
<tr>
<td>Power and energy</td>
<td>528.4</td>
<td>271.6</td>
</tr>
<tr>
<td><strong>Infrastructure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Municipal infrastructure</td>
<td>290.0</td>
<td>96.2</td>
</tr>
<tr>
<td>Transport</td>
<td>668.0</td>
<td>405.5</td>
</tr>
<tr>
<td><strong>Manufacturing</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agribusiness</td>
<td>480.7</td>
<td>409.1</td>
</tr>
<tr>
<td>Property and tourism</td>
<td>163.5</td>
<td>210.3</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>123.0</td>
<td>262.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4,277.5</td>
<td>4,133.0</td>
</tr>
</tbody>
</table>

1 A total of €190 million of bank lending was devoted to small and medium-sized businesses in 2005.

2 Small business finance comprises investments in microfinance banks and microfinance programmes, such as the Russia Small Business Fund and the US/EBRD SME Finance Facility.

3 Energy efficiency only refers to investments with specialised energy efficiency firms, such as energy service companies. The energy efficiency components within all EBRD projects signed in 2005 totalled €205 million compared with €201 million in 2004.
Investing responsibly

Environmental expenditure
In 2005 the EBRD invested €346 million in energy efficiency, municipal infrastructure and clean-up operations, representing 8 per cent of the Bank’s total investment for the year. This generated additional environmental investment of €552 million from EBRD clients.

The Bank provided a further €369 million for the environmental aspects of projects in other sectors, such as manufacturing, heavy industry and agribusiness. This generated additional environmental investment of €269 million.

Environmental expenditure 2004-05

<table>
<thead>
<tr>
<th>EBRD investment in 2005 (€ million)</th>
<th>Environmental financing mobilised from EBRD clients in 2005 (€ million)</th>
<th>EBRD investment in 2004 (€ million)</th>
<th>Environmental financing mobilised from EBRD clients in 2004 (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental projects involving municipal infrastructure, energy efficiency and clean-up operations</td>
<td>346</td>
<td>552</td>
<td>377</td>
</tr>
<tr>
<td>Environmental improvements in other sectors, such as manufacturing, heavy industry and agribusiness</td>
<td>369</td>
<td>269</td>
<td>71</td>
</tr>
</tbody>
</table>

Breakdown of total environmental expenditure in non-environmental sectors 2004-05

<table>
<thead>
<tr>
<th></th>
<th>2005 (€ million)</th>
<th>2004 (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air emissions/greenhouse gas reduction</td>
<td>15.90</td>
<td>13.1</td>
</tr>
<tr>
<td>Energy efficiency</td>
<td>189.00</td>
<td>74.6</td>
</tr>
<tr>
<td>Waste-water management</td>
<td>88.50</td>
<td>38.2</td>
</tr>
<tr>
<td>Solid waste management</td>
<td>65.60</td>
<td>25.0</td>
</tr>
<tr>
<td>Health and safety</td>
<td>9.10</td>
<td>46.7</td>
</tr>
<tr>
<td>Environmental Management System</td>
<td>8.10</td>
<td>10.8</td>
</tr>
<tr>
<td>Clean-up of contaminated soil and groundwater</td>
<td>4.20</td>
<td>0.4</td>
</tr>
<tr>
<td>Training</td>
<td>3.60</td>
<td>2.6</td>
</tr>
<tr>
<td>Labour and social</td>
<td>0.05</td>
<td>Not collected</td>
</tr>
<tr>
<td>Other</td>
<td>253.80</td>
<td>33.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>638.00</strong></td>
<td><strong>244.8</strong></td>
</tr>
</tbody>
</table>
Investing responsibly

Municipal and environmental infrastructure

In 2005 the EBRD invested €290 million (up from €96 million in 2004) in 13 municipal infrastructure projects across ten countries. This increase in funding reflects the urgent need for investment in district heating, urban transport and water services across the Bank’s countries of operations.

EBRD investment in this sector has helped to improve the quality of life for tens of thousands of people who have benefited from better public transport, greater access to clean drinking water and more reliable heating services. Raising standards also achieves environmental improvements. Investment in public transport, for example, achieves lower emission levels, better fuel efficiency, better air quality, less noise pollution and reduces usage of heavily polluting cars.

A key aspect of the EBRD’s activity is to promote greater private sector involvement. The Bank actively promotes decentralisation as a means of improving the quality, cost and environmental efficiency of local infrastructure and services.

Municipal infrastructure projects signed by the EBRD in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Sub-sector</th>
<th>Project description</th>
<th>EBRD finance (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>District heating</td>
<td>Upgrading of municipal district heating distribution network in Iasi</td>
<td>13.0</td>
</tr>
<tr>
<td>Russia</td>
<td>District heating and waste water</td>
<td>Upgrading and improvement of water and waste-water assets as well as district heating infrastructure in Surgut</td>
<td>8.8</td>
</tr>
<tr>
<td>Georgia</td>
<td>Urban transport</td>
<td>Finance for buses, spare parts and workshop equipment in Tbilisi</td>
<td>3.1</td>
</tr>
<tr>
<td>Poland</td>
<td>Urban transport</td>
<td>Improvements in public transport, including better regulation and opening up to private sector competition, in Krakow</td>
<td>19.4</td>
</tr>
<tr>
<td>Regional</td>
<td>Urban transport</td>
<td>Expansion of Veolia’s public transport services in central and eastern Europe</td>
<td>n/a</td>
</tr>
<tr>
<td>Romania</td>
<td>Urban transport</td>
<td>Three projects for modernisation of infrastructure and rolling stock of public transport in Arad, Brasov and Sibiu</td>
<td>n/a</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Waste water</td>
<td>Upgrading and improvement of water and waste-water infrastructure in Burgas</td>
<td>50.0</td>
</tr>
<tr>
<td>Croatia</td>
<td>Waste water</td>
<td>Upgrading of sewerage system and water supply network, and construction of a waste-water treatment plant near Karlovac</td>
<td>11.0</td>
</tr>
<tr>
<td>Poland</td>
<td>Waste water</td>
<td>Improvements in the water and sewerage system in Bydgoszcz</td>
<td>41.5</td>
</tr>
<tr>
<td>Poland</td>
<td>Waste water</td>
<td>Modernisation and improvement of the sewerage network in Gliwice</td>
<td>15.0</td>
</tr>
<tr>
<td>Romania</td>
<td>Waste water</td>
<td>Creation of special-purpose municipal enterprises to invest in the upgrading of water and waste-water treatment assets in Cluj Salaj</td>
<td>7.2</td>
</tr>
<tr>
<td>Russia</td>
<td>Waste water</td>
<td>Construction of sludge incinerator to provide environmentally sustainable solution to sludge disposal near St Petersburg</td>
<td>20.0</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Waste water</td>
<td>Modernisation of municipal water treatment works and distribution networks</td>
<td>20.0</td>
</tr>
</tbody>
</table>
Public transport

The EBRD invested around €70 million in five public transport projects across three countries in 2005 and undertook one regional project covering many countries. The EBRD’s equity investment in Veolia Transport (formerly known as Connex) is helping the company to improve bus services across its operations in central and south-eastern Europe. The initial focus is on Croatia, the Czech Republic, Poland, the Slovak Republic and Slovenia.

In Georgia the EBRD loaned €3 million to the municipality of Tbilisi to improve local transport through the acquisition of new and second-hand buses. The Bank’s loan will also help to finance repair facilities and to develop a regulatory framework that will improve the quality of services provided by private minibus operators.

The EBRD’s loan to the city of Tbilisi is the first to be provided to a municipality in an early transition country without a state guarantee. This means that state funding is freed up for investment elsewhere. Modernising the bus fleet will decrease traffic congestion, increase traffic safety and improve air quality in the city.

EBRD investment in Sibiu in Romania – selected as the Cultural Capital of Europe for 2007 – will help the city to modernise key aspects of its infrastructure and to introduce commercial practices to its public transport system. The Bank’s loan will help to improve roads and to finance lighting for the city’s historic buildings, for the benefit of tourists and residents alike. This loan builds on the Bank’s previous investments in the city’s water company.

Water services

The EBRD invested €120 million in eight water projects across six countries in 2005. Most of this investment was in waste-water treatment plants and sewerage networks.

Obsolete infrastructure in many of the Bank’s countries of operations is a cause for environmental and health concerns. The EBRD’s investments are used to modernise plants, pumping stations and networks and to reduce river and lake pollution. Financing has also been provided to install water metering to provide incentives for more careful use of water.

The EBRD’s investments are used to modernise plants, pumping stations and networks and to reduce river and lake pollution.

A milestone project in 2005 was the completion of the St Petersburg Southwest Waste Water Treatment Plant (inaugurated by the Presidents of Russia and Finland and the Prime Minister of Sweden). Of the plant’s total cost of €138 million, the EBRD has lent €20 million which has been earmarked to fund construction work. The project will cut the levels of untreated sewage entering the Baltic Sea, helping to improve living conditions for the 50 million people around its shores. The Bank has also lent €20 million to build a similar plant at the northern edge of St Petersburg and to finalise construction work in the city of Surgut.

In Bydgoszcz, one of Poland’s second-tier cities, the EBRD agreed in 2005 to purchase €42 million of revenue bonds issued by the city’s water company – the first project of its kind in central Europe. The transaction will enable the city and the municipal water company to complete an investment programme that will raise water services and quality to EU standards. It will also act as an example of how other infrastructure projects could be financed by the capital markets.
Brasov's public transport company currently provides over 55 million journeys a year (the city’s population is 285,000), reflecting the city’s busy urban network and its popularity as a holiday destination (with excellent skiing opportunities in the nearby Carpathian Mountains).

To help the city deal with this vast number of journeys, the EBRD is providing a €10 million loan to the local transport operator. To alleviate any strain on public funding, the EBRD is lending without a municipal guarantee. This is the Bank’s first such municipal loan in Romania. A further loan of €10 million to the city of Brasov will be used for road improvements in the historic old town.

The city’s public transport network will be transformed. The old and inefficient tramline will be closed, cutting maintenance costs. Large trolley buses will be used only outside the historic centre and will be replaced by new “midi” buses, which are better suited to the narrow streets. The new buses will require less maintenance while the road improvements will ensure that the new fleet has a longer working life.

The new, lighter vehicles will be more fuel efficient than heavy trams and trolley buses. Locals and visitors will benefit from reduced road congestion and an improvement in air quality. The new buses will all meet EU emissions standards, helping Romania to prepare for EU membership. Better public transport and roads will also boost Brasov’s economic development and tourism revenue.
Investing responsibly

Transport infrastructure
An efficient transport sector is crucial for the development of market economies in the EBRD’s countries of operations. The Bank significantly increased its investment in transport infrastructure in 2005, investing €668 million (up from €406 million in 2004) in 14 projects in nine countries.

In Romania an EBRD loan of €144 million (provided in local Romanian lei) is being used to support the construction of a north-south by-pass for the town of Constanta and other major road projects (see page 27).

In Albania the EBRD is lending €21 million to Tirana Airport Partners (TAP), a German-led consortium, to support a €50 million refurbishment project. The new airport will be one of the most modern infrastructures in the country, serving a million passengers a year. TAP will create over 2,000 jobs in and around the airport in the first few years of operation and a further 5,000 jobs over the next two decades.

A new Transport Policy
The EBRD approved a new Transport Policy in April 2005. The policy re-affirms the key role of an efficient transport sector in the operation of regional markets. The Bank will continue to cooperate with the European Union on the development of trans-European networks and on the implementation of regional initiatives.

The EBRD will also continue to cooperate with other IFIs, such as the European Investment Bank, the International Monetary Fund, the World Bank and regional development banks.

Transport projects signed in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Sub-sector</th>
<th>Description</th>
<th>EBRD finance (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>Roads</td>
<td>Upgrading and construction of the road from Fier to Tepelene</td>
<td>35.0</td>
</tr>
<tr>
<td>Albania</td>
<td>Air travel</td>
<td>Upgrading of facilities at Tirana Airport</td>
<td>21.0</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>Roads</td>
<td>Upgrading of a 60 km section of road from Sumgait to Zarat</td>
<td>84.5</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>Railways</td>
<td>Financing of track infrastructure</td>
<td>70.0</td>
</tr>
<tr>
<td>Croatia</td>
<td>Ports</td>
<td>Extension of berth area in the port of Gruz, Dubrovnik, to accommodate larger vessels</td>
<td>26.5</td>
</tr>
<tr>
<td>Hungary</td>
<td>Roads</td>
<td>Financing of the M6 motorway on a design-build-finance operate basis under a public-private partnership scheme</td>
<td>32.0</td>
</tr>
<tr>
<td>Romania</td>
<td>Railways</td>
<td>Priority investment in a rail traction project</td>
<td>22.5</td>
</tr>
<tr>
<td>Romania</td>
<td>Roads</td>
<td>Building and maintenance of the Constanta bypass</td>
<td>144.2</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Roads</td>
<td>Upgrading of a 65 km section of road from Belgrade to Novi Sad and construction of a bridge across the Danube</td>
<td>72.0</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Air travel</td>
<td>Modernisation of the Belgrade and Podgorica air traffic control centres and corresponding infrastructure</td>
<td>33.5</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Roads</td>
<td>Improvements to infrastructure and safety of Montenegrin roads</td>
<td>11.5</td>
</tr>
<tr>
<td>Tajikistan</td>
<td>Air travel</td>
<td>Upgrading of the TSA air fleet</td>
<td>4.2</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Roads</td>
<td>Upgrading of the M06 Kiev-Chop road</td>
<td>100.0</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Shipping</td>
<td>Finance for acquisition costs of five new dry cargo buildings</td>
<td>11.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>667.9</strong></td>
</tr>
</tbody>
</table>
Institutional and regulatory development will continue to be one of the principal areas of activity.

The new policy commits the EBRD to incorporate a wide range of environmental measures, such as enhanced energy efficiency, waste minimisation/recycling and cleaner technologies, in its transport projects to ensure they support sustainable development.

The EBRD helps its clients in this sector to develop energy efficiency solutions and administers donor funding which is available to help companies carry out energy audits and to develop energy-saving programmes. The Bank encourages projects that promote the use of cleaner vehicles and cleaner fuels, including biofuels.

Members of the Environmental Advisory Council (ENVC) assisted the Bank in developing the new Transport Policy (see page 68). The full policy and a summary of the public consultation are published on the Bank’s web site.

**Supporting a sustainable financial sector**

The EBRD places great emphasis on supporting financial institutions (FIs), such as banks, leasing companies and private equity funds, in recognition of the vital role that they play in assisting local enterprises. The Bank uses a variety of financing mechanisms, such as equity investments, loans and guarantees. In 2005 over one-third of the EBRD’s total investment was devoted to FIs.

By supporting FIs, the EBRD is helping to increase the level of financing that is available to small and micro businesses. The Bank requires all financial intermediaries to undertake environmental risk management as an integral part of their lending and investment operations.

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**Constanța by-pass**

An EBRD loan provided in November 2005 is funding a major by-pass for Constanța, the reconstruction of ten bridges (crossing the Danube and Black Sea Channel) and repairs to Romania’s road network, which was damaged by severe floods in 2005.

In March 2005, at the EBRD’s request, a public meeting was held in Constanța to identify issues to be addressed in the project’s Environmental Impact Assessment (EIA). Over 100 representatives attended the meeting, including many NGOs. EBRD staff also visited a number of NGOs working on environmental issues in the Constanța region to seek their opinion on the potential impact of the Bank’s project and how any adverse effects could be minimised.

A second public meeting took place in July 2005 in Constanța and was again attended by a wide cross-section of the local community. Although concerns were raised about the effects of the construction, there was overwhelming support for the by-pass and the positive impact it will have on reducing traffic problems in the centre of Constanța. In particular, traffic destined for the port will be rerouted from the town centre. The by-pass will also provide a convenient route for tourist traffic from Bucharest and the north of Romania to the popular seaside resorts south of Constanța.

The issues raised at the meetings will be taken into account in the preparation of the project and included in the Environmental Management Plan. The client has agreed to provide regular disclosure of information on the project and its environmental impact via their web site, annual environmental reports and press releases. A public information programme will also be launched and every community along the proposed route will be visited.
Investing responsibly

Specific requirements include:

• adopting environmental due diligence procedures satisfactory to the Bank
• annual environmental reporting to the EBRD
• adhering to the Bank’s FI Environmental Exclusion and Referral list
• requiring clients to comply at a minimum with the host country’s health, safety, labour and environmental regulations and standards
• appointing a member of management with overall responsibility for environmental matters.

Environmental training programme
Conducting effective environmental risk management is a challenge for many FIs, particularly in countries with weaker environmental law enforcement and lower levels of general environmental awareness. The EBRD has established a major environmental training programme for FIs across the Bank’s countries of operations. It provides training to individual FIs and also includes workshop sessions where groups of similar FIs can be trained together.

The EBRD has established a major environmental training programme for financial institutions across the Bank’s countries of operations.

The training involves working with an FI’s management and staff to embed environmental risk management procedures into their existing credit appraisal and decision-making procedures, training credit staff to perform environmental due diligence, monitoring and reporting, and providing materials to support the implementation of the procedures. The training uses case studies to focus on health, safety, environmental and social risks.

Since the programme started in 1995, it has provided environmental training to 193 FIs. Donor support has been essential for the programme. To date, the European Community has been the main contributor, with total funding of €5.6 million committed.

In 2005 environmental due diligence training workshops were undertaken with four financial intermediaries in Bulgaria, Poland and the Slovak Republic, supported by EU funds. In addition, the EBRD carried out a one-day environmental training workshop for financial intermediaries in Serbia and Montenegro.

Electronic manual
The EBRD’s electronic manual Environmental Risk Management for Financial Institutions contains all of the Bank’s FI environmental procedures, guidance materials and other practical tools. It assists FIs with the implementation of an environmental management system in line with good practice and EBRD requirements. In 2005 the EBRD published the manual on the Bank’s web site. Czech, Latvian, Lithuanian, Polish, Romanian and Russian versions will be published on the web site later in 2006.

Environmental monitoring visits
In 2005 the EBRD made monitoring visits to financial intermediaries and their clients in Poland, Romania and the Slovak Republic. The FIs visited were found to comply with the Bank’s environmental requirements.

Collaborating with the UNEP FI
The United Nations Environment Programme Finance Initiative (UNEP FI) was launched in 1991 to advance the consideration of environmental issues by financial markets. There are roughly 230 signatories to its “Statement on Environment and Sustainable Development”. In January 2005 the EBRD was the first multilateral financial institution to sign the statement. The Bank is also assisting partner FIs to become signatories.
The EBRD is currently chair of the Central and Eastern European Task Force (CEETF) within UNEP FI. In 2005 CEETF organised awareness-raising conferences in Warsaw and Zagreb. The conferences attracted senior-level representatives from the financial sector, academia, consultancies and NGOs to learn more about the opportunities of sustainable finance.

Presentations were given on environmental liabilities following EU accession, the importance of environmental issues in privatisation transactions, best practices in sustainable finance and environmental issues affecting company ratings. Similar events are scheduled for Greece, Lithuania and Russia in 2006.

**Promoting small business growth**

Small businesses are vital for the development of a vibrant market economy. Entrepreneurship creates new jobs and provides the basis for a country’s long-term growth. The EBRD has long supported this sector as an essential way of fulfilling the Bank’s mandate.

In 2005 the EBRD invested €255 million in small business finance, including investments in microfinance banks and microfinance programmes. In particular, we expanded our support for rural businesses that find it difficult to get loans from other sources.

**Supporting micro businesses in Kazakhstan**

Only 2 per cent of people in Kazakhstan have access to microfinance. However, the donor-supported Kazakhstan Small Business Programme is gradually helping to increase this percentage by bridging the gap between Kazakh financial institutions and entrepreneurs. In 2005 the EBRD provided two new streams of financing.

An EBRD loan of €4.2 million was extended to Alliance Bank (the fifth-largest in Kazakhstan) to help it provide smaller loans and develop a fast and flexible lending strategy. The bank now offers an “express micro loan” of up to €4,200, which can be quickly disbursed with no need for fixed assets as collateral.

A €1.7 million loan was provided by the EBRD to the Kazakh Loan Fund (KLF), a microfinance organisation that makes small loans of up to €850 to its clients. KLF was originally set up with USAID financing but has now developed sufficiently to receive a loan at market rates from the EBRD. This was provided in local currency, the Kazakh tenge. This is a watershed in Kazakh financial history and vital for organisations such as KLF, which are only allowed to make micro loans in local currency.
30 Investing responsibly

Donor funding
The EBRD uses donor funding to train staff in local banks and to develop more efficient legal and regulatory frameworks for small business finance. The donor-supported Micro and Small Business Programme operates in 19 of the EBRD’s countries of operations. It provides financing through over 1,000 branches of 54 financial institutions. These support small businesses through a combination of EBRD finance and their own funds. In 2005 some 480,000 loans totalling €2.5 billion were disbursed.

The EBRD uses donor funding to train staff in local banks and to develop more efficient legal and regulatory frameworks for small business finance.

The EU/EBRD Preparatory Action Programme was set up in 2005 to boost lending to micro and small businesses in the eight new EU member states. The first project was signed with Istrobanka in the Slovak Republic to provide financing to local businesses with an average portfolio size of less than €25,000.

The United States is the largest supporter of the EBRD’s microfinance programmes, providing €71 million in donor funding for projects in 15 countries. The US/EBRD SME Finance Facility promotes private sector growth and economic development in south-eastern Europe and in Armenia, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Tajikistan and Ukraine.

The EBRD’s largest individual programme is the Russia Small Business Fund, which has provided €2.2 billion in loans to Russian micro and small enterprises (MSEs). The RSBF is supported by a variety of donors.

The EU/EBRD SME Finance Facility operates in 11 countries in central Europe, channeling finance through local banks, leasing companies and equity funds. In 2005 the EBRD increased the funding available through this facility to €1.1 billion, including at least €50 million earmarked for farmers and small businesses in rural areas.

Impact of EBRD investment
To investigate the link between EBRD investment, economic growth and poverty alleviation, the EBRD’s Office of the Chief Economist (together with the University of Michigan) surveyed 1,272 micro, small and medium-sized enterprises (MSMEs) in 2005 in four of the EBRD’s countries of operations – Bulgaria, Georgia, Russia (Nizhny Novgorod region) and Ukraine. Two-thirds had received finance in 2002 from local banks and other financial institutions (through which the EBRD channels credit targeted at small businesses). The other third was a control group of businesses active in 2002.

Initial analysis showed that, compared with the control group, the EBRD-backed firms had better survival rates, were 60 per cent more profitable, had lower labour costs because their staff were 30 per cent more productive and created 5 per cent more jobs. The EBRD-financed businesses were also more likely to get renewed financing (mostly from their local EBRD-backed bank rather than from elsewhere in the financial sector).

A second, related study by the EBRD’s Office of the Chief Economist showed that through its engagement with local banks, the Bank has helped to improve the overall efficiency of banking systems, reduced customers’ banking fees and fostered greater competition between banks.

Targeted programmes
The EBRD uses a range of donor-supported programmes to support small businesses. These include the TurnAround Management (TAM) and Business Advisory Service (BAS) Programmes and the Trade Facilitation Programme.
TAM and BAS programmes in 2005

<table>
<thead>
<tr>
<th>TAM programmes</th>
<th>BAS programmes</th>
</tr>
</thead>
<tbody>
<tr>
<td>102 new projects started in 16 countries</td>
<td>987 new projects started in 14 countries</td>
</tr>
<tr>
<td>Operates in 27 countries</td>
<td>Operates in 15 countries</td>
</tr>
</tbody>
</table>

TAM and BAS are complementary programmes, which help enterprises to increase productivity and improve sales. With the assistance of business leaders from economically developed countries, TAM helps companies to develop technical and management skills and to increase turnover. BAS utilises the expertise of local consultants to help companies improve their competitiveness and to develop their strategic planning.

The EBRD’s Trade Facilitation Programme (TFP) uses donor funding to support cross-border trade. The TFP provides guarantees to help businesses grow through export and import trade. It also provides loans to banks for on-lending to local exporters and importers. Most transactions support small businesses: more than half are for under €100,000 and many would not be possible without the programme.

Activities under the Trade Facilitation Programme

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Participating local banks</td>
<td>100</td>
<td>88</td>
</tr>
<tr>
<td>Trade guarantees</td>
<td>1,024</td>
<td>1,089</td>
</tr>
<tr>
<td>Total value of business transactions guaranteed (€ million)</td>
<td>549</td>
<td>500</td>
</tr>
</tbody>
</table>

The EBRD has developed two forms of financing to help companies in countries where local banks are not available to act as intermediaries. The Direct Investment Facility (DIF) makes equity investments (ranging from €0.4 million to €2 million) in private sector companies. The Direct Lending Facility (DLF) provides loans (ranging from €0.5 million to €4 million) directly to medium-sized enterprises.

Securing employment for people with disabilities in Hungary

In a challenging project completed in September 2005, TAM helped to strengthen a Hungarian company so that it could compete successfully in a difficult business environment.

Relabor was set up in 1989 by two doctors in the town of Esztergrom as a scheme to reintegrate people with disabilities into the community. It started with seven people cultivating mushrooms and other food products. By 2002 when TAM started working with the company, it had become an organisation of 800 employees nationwide, with 80 per cent of the workforce having some form of disability.

Relabor’s activities ranged from packaging small items, such as screws, nuts and bolts, to wood-working, assembling electrical and mechanical components, and gardening services for the cities of Esztergom and Dorog. TAM advisers identified that, despite government support in the form of wage subsidies, the company needed to become market-oriented rather than product-oriented. When the Hungarian government tripled minimum wages, Relabor was in danger of no longer being competitive.

Working with Relabor’s management, the TAM team developed and introduced a five-year strategy that took account of competitive pressure. The TAM team’s main goal was to re-orient management focus towards customer demands. During the course of the programme, Relabor’s managers established a marketing division within the organisation. Turning to export markets was also a priority and the employment of a marketing manager familiar with international markets was an important step.

During the project, Relabor hired around 300 more people with disabilities. The company has contracts with international companies such as Ikea, Opel, Sanyo, Samsung and Haribo, and holds an ISO-9001 quality certification in woodworking, electronics, assembling, gardening and cleaning. With partners in Austria and Germany, turnover has increased from €3.8 million to €5.5 million.
Both schemes also provide advice on professional management practices, transparency and good corporate governance.

**Supporting the early transition countries**

The early transition countries (ETCs) are a group of seven countries in Central Asia, Western CIS and the Caucasus, comprising Armenia, Azerbaijan, Georgia, the Kyrgyz Republic, Moldova, Tajikistan and Uzbekistan. They are some of the poorest countries where the EBRD operates and the ones in most need of the EBRD’s local experience and relationships with potential co-investors.

The ETCs are some of the poorest countries where the EBRD operates and the ones in most need of the EBRD’s local experience and relationships with potential co-investors.

The Bank’s aim in these countries is to improve the investment climate, build sustainable market economies and alleviate poverty. Many of the people lifted out of poverty are the working poor. The EBRD helps them by developing the private business sector, which in turn creates more jobs, better job security and higher wages.

### Early Transition Countries Initiative

The Bank’s Early Transition Countries Initiative was launched in 2004 and is showing good results. By the end of 2005, EBRD investment in the ETCs had almost tripled compared with 2004 levels. Co-financing with the private sector increased in Azerbaijan and Ukraine, and was provided for the first time in Georgia.

**EBRD investment in the early transition countries**

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>EBRD investment</td>
<td>249.0</td>
<td>93.0</td>
</tr>
<tr>
<td>Donor funding</td>
<td>18.0</td>
<td>12.7</td>
</tr>
<tr>
<td>Projects signed</td>
<td>61</td>
<td>32</td>
</tr>
</tbody>
</table>

* Oil and gas projects are excluded because the size of these investments varies significantly from year to year.

The ETC Initiative extends the Bank’s reach and impact in the poorest countries where we operate. It aims to boost business growth in the private sector by using a streamlined approach to finance a greater number of projects (many of them small) and to mobilise additional investment. The projects financed by the Initiative also support infrastructure improvements and economic and legal reform. Its success rests on the Bank’s readiness to take on a higher level of risk in ETC projects (respecting sound banking principles) and increased support from the donor community.
Contributors to the ETC Fund (launched in November 2004) include Canada, Finland, Ireland, Japan, Luxembourg, the Netherlands, Norway, Spain, Sweden, Switzerland, Taiwan, China and the United Kingdom. The largest contributors are Japan, the Netherlands and the United Kingdom.

Donor-funded commitments to the seven ETCs increased by 40 per cent in 2005. About half was provided through the ETC Fund, which approved financing of around €16 million to fund 46 technical cooperation projects. These include microfinance programmes, small municipal infrastructure projects and environmental initiatives, including helping companies and governments to fund energy efficiency and renewable energy projects.

**Investment in the ETCs in 2005**
In 2005 the EBRD invested €249 million in 61 projects across all seven ETCs.

### Projects signed in the early transition countries in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Number of projects</th>
<th>Project sectors and descriptions</th>
<th>Total EBRD financing (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>11</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>16.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Natural resources: Working capital investment in a gold mining project</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Power and energy: Investment in a small hydropower project</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Manufacturing: Investment in a plastics manufacturer and a pharmaceutical company</td>
<td></td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>12</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>113.4</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Transport: Sumgait-Zarat road upgrade project</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Property and tourism: Office development in Baku</td>
<td></td>
</tr>
<tr>
<td>Georgia</td>
<td>13</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>44.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Municipal and environmental infrastructure: Investment in Tbilisi public transport network</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Agribusiness: Loans and equity investments in agribusiness projects</td>
<td></td>
</tr>
<tr>
<td>Kyrgyz Republic</td>
<td>8</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>13.6</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Agribusiness: Working capital facility for cotton company</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Property and tourism: Expansion of Raduga tourist resort</td>
<td></td>
</tr>
<tr>
<td>Moldova</td>
<td>8</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>15.7</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Agribusiness: Loan and equity investments for agribusiness projects</td>
<td></td>
</tr>
<tr>
<td>Tajikistan</td>
<td>5</td>
<td>Financial institutions: Credit lines and equity investments through local banks</td>
<td>9.6</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Transport: Loan financing for air fleet upgrade</td>
<td></td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>4</td>
<td>Manufacturing: Investment in a textile plant</td>
<td>35.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Agribusiness: Investment in agribusiness projects</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Telecommunications: Equity investment in Unitel</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>61</strong></td>
<td><strong>Investing responsibly</strong></td>
<td><strong>248.8</strong></td>
</tr>
</tbody>
</table>

* Excluding oil and gas projects.
Micro and small businesses in the ETCs

One of the main ways that the EBRD reaches small businesses in the ETCs is through the donor-supported Micro and Small Business Programme. The United States is its largest supporter through the US/EBRD SME Finance Facility. By the end of 2005, the facility had provided over 134,000 loans totalling almost €500 million to the ETCs. The average loan size was under €3,200, ensuring that even very small businesses can benefit from the scheme.

TAM and BAS programmes (see page 31) in the ETCs are funded through donor contributions and managed by the EBRD. There are BAS offices in six ETCs and new offices were opened in Moldova and the Kyrgyz Republic in 2005. Both programmes continued to assist enterprises in rural areas in 2005. In the Caucasus a new cross-border programme and a “women in business” initiative were started. In Central Asia, projects on environmental issues and tourism were started.

Remittances from workers living abroad

The money that migrants send to their families is believed to have a major impact on building assets in their native countries. Little is known about their specific impact in the ETCs because the money mainly enters through unofficial means, carried in by migrants on home visits or wired via grassroots money transfer companies.

Following on from a conference sponsored by Switzerland in 2005, the ETC Fund approved finance for a study on remittances sent by migrant workers back to their homes in three ETCs. It is expected to help local banks to develop new remittance-based financial products that will contribute to economic growth.

New framework for on-lending through NGOs

Micro and small businesses usually lack assets that they can offer as collateral and so have difficulty in getting loans from mainstream lenders. This is particularly so in the ETCs.

To address this, the EBRD provided financing in 2005 for on-lending through institutions other than banks, such as non-governmental organisations (NGOs). These organisations have a wider remit to lend to people who lack collateral and who cannot obtain finance from elsewhere. Four new partners received funds: Imon in Tajikistan, Finac and Bai Tushum in the Kyrgyz Republic and the Rural Finance Corporation in Moldova.

Supporting legal reform

The EBRD used donor funding in 2005 to support legal reform programmes in three of the Bank’s ETCs. The funding is helping to create a regulated commercial sector, which will help entrepreneurs gain access to finance and start businesses, which in turn will help the economy to grow. In Georgia, reform of loan transactions – using assets as security – will protect both borrowers and lenders. In the Kyrgyz Republic a programme is funding training for judges who deal with commercial matters, a local judicial training centre and a new law library for judges. In Moldova, much-needed reform of the leasing law is giving small enterprises easier access to finance for major equipment purchases.

Working in partnership

The EBRD works in partnership with a variety of international bodies to tackle environmental challenges, such as nuclear safety, pollution of international water resources, and biodiversity conservation. We also support the implementation of global and regional agreements related to the environment and sustainable development.

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**Espoo Convention**

The Espoo Convention (Convention on Environmental Impact Assessment in a Transboundary Context) establishes a framework for assessing the environmental impact of projects across borders. Member countries (33 to date plus the European Union) consult on all major projects under consideration that are likely to have a significant adverse environmental impact across borders.

In 2005 the EBRD initiated discussions with the United Nations Economic Commission for Europe (UNECE) and the Black Sea Commission to assist the states that border the Black Sea in developing guidelines for implementing the principles of the Espoo Convention. The United Nations Environment Programme and UNECE are turning the existing regional guidelines concerning the Caspian region into a binding protocol.

Two key projects in 2005 had the potential for transboundary impacts:

- **Northern Dimension Environmental Partnership (NDEP) activities in north-west Russia**: The EBRD held public meetings in Moscow, Murmansk and Severodvinsk and invited representatives of Finland, Norway and Sweden to participate in the review of a strategic environmental assessment for the decommissioning of nuclear submarines (see page 37).

- **Sakhalin II Phase 2**: The EBRD held a series of public meetings, including a meeting in Sapporo (Hokkaido), to hear the views of all those affected by this complex project (see page 67), which includes the construction of a large liquefied natural gas terminal and loading facility near the Japanese Island of Hokkaido. To fulfil a requirement to consult with Japanese stakeholders, the client has translated relevant studies and reports on transboundary issues into Japanese and held numerous meetings with Japanese environmental groups, local fishermen and members of the public.

**Global Environment Facility**

The Global Environment Facility (GEF) is an independent financial organisation that provides grants to developing countries for projects that benefit the global environment and promote sustainable livelihoods in local communities.

The EBRD and GEF are currently co-funding an Environmental Credit Facility in Slovenia to reduce pollution entering the Slovenian part of the Danube River Basin. In 2005 the EBRD disbursed approximately €22 million to four local banks for on-lending to local businesses and small municipalities that invest in pollution-reduction projects.
Grant funding from GEF is also channelled through the multi-donor Business Advisory Services Programme (see pages 30-31). Grants pay for consultancy and expert advice – for example, to tackle water pollution and to help local businesses prepare an investment proposal. Additional GEF funds prepare the way for borrowers to undertake these projects.

By the end of 2005, over 35 projects had received funding. In total, credit lines of €43 million have been extended to local participating banks. Loans are being provided via four banks: Bank Austria Creditanstalt, Nova Ljubljanska Banka, Probanka and Volksbank-Ljudska Banka.

**Promoting biodiversity**

Preserving and protecting biodiversity is an essential part of managing the environmental impact of EBRD projects. All EBRD projects are expected to include measures to safeguard and, where possible, enhance natural habitats and biodiversity. In addition, the Bank is committed to supporting investments that specifically promote biodiversity.

**Activities in 2005**

The EBRD has worked with the European Centre for Nature Conservation (ECNC) for a number of years to consider biodiversity concerns in the Bank’s countries of operations. In 2005 the EBRD participated alongside ECNC and other organisations, such as the European Investment Bank (EIB) and Rabobank, in the framework of the Pan-European Biological and Landscape Diversity Strategy. This considers financing mechanisms for supporting biodiversity and the possible establishment of a European Biodiversity Finance Facility.

A European Task Force on Banking, Business and Biodiversity was established in 2005 and met a number of times at the Bank’s headquarters in London. The task force includes Deutsche Bank, the ECNC, the EIB, the International Finance Corporation and Rabobank. The task force and the Bank are considering how to structure a donor-funded biodiversity finance facility.

The EBRD is working with Flora and Fauna International (FFI) on a biodiversity project that is being funded by the Dutch DOEN Foundation. FFI has been working in Hungary and Poland to develop projects that will have a positive impact on biodiversity. The Bank is acting as an adviser and is providing access to finance through the EBRD’s Small Business Programme and to advisory services through the TurnAround Management Programme (see pages 30-31).

The FFI project aims to identify over 5,000 small businesses working with biological resources. Investment in these companies would assist the sustainable management of biodiversity and improve the commercial performance of these firms.
Investing responsibly 37

Northern Dimension Environmental Partnership

The Northern Dimension Environmental Partnership (NDEP) mobilises investment to tackle longstanding environmental problems in north-west Russia. These include water supply, waste-water treatment, energy efficiency and nuclear safety. NDEP consists of the Russian government, the donor community and international financial institutions (IFIs), including the EBRD.

The Northern Dimension Environmental Partnership mobilises investment to tackle longstanding environmental problems in north-west Russia.

The NDEP Steering Group identifies priority projects and puts together financing packages, consisting of grants from the NDEP Support Fund, IFI loans, bilateral funding and contributions from local sources. The EBRD has chaired the Group since July 2005. NDEP implemented its first project in 2005 – the completion of the St Petersburg Southwest Waste Water Treatment Plant (see page 24).

NDEP Support Fund

The NDEP Support Fund is managed by the EBRD and supervised by an Assembly of Contributors. At the end of 2005, contributions to the Fund amounted to €224 million, of which €148 million was earmarked for nuclear safety.

In 2005 new funding was pledged by the European Community, Denmark, Finland, Norway, Russia and Sweden. The Assembly of Contributors has approved NDEP co-financing of €57 million for ten environmental projects, with a total project value of over €1 billion.

NDEP nuclear “window”

The nuclear “window” of the NDEP Support Fund was set up to address the nuclear legacy of the former Soviet nuclear fleet in north-west Russia and entered the implementation phase in 2005. The Assembly approved funding of €19 million for five high-priority projects. They include a radiation monitoring and emergency response system in the Murmansk region and safe storage and unloading of spent nuclear fuel from submarines in Gremikha.

The Assembly also approved the second phase of the Strategic Master Plan. This provides an overview of all requirements related to spent nuclear fuel, radioactive waste and the environmental upgrading of coastal bases.

United Nations Environment Programme Finance Initiative

The United Nations Environment Programme Finance Initiative (UNEP FI) was launched in 1991 to encourage financial markets to actively consider environmental issues. In January 2005 the EBRD became the first multilateral financial institution to sign UNEP FI’s “Statement on Environment and Sustainable Development” (see page 28).

Coordinating nuclear safety improvements

The EBRD manages six nuclear safety funds on behalf of 28 donor countries and the European Community: the Nuclear Safety Account (NSA), the Chernobyl Shelter Fund (CSF), three international decommissioning support funds (IDSFs) for Bulgaria (Kozloduy), Lithuania (Ignalina) and the Slovak Republic (Bohunice) and the nuclear “window” of NDEP (see above). Donors have so far contributed around €2 billion to these funds.
Early NSA-financed projects focused on the most pressing safety deficiencies in old Soviet-designed nuclear power plants. These short-term measures helped to ensure the safest possible operation of these plants until conditions were in place to close them. Most experts agreed that these plants could not be upgraded to acceptable safety levels at a reasonable cost.

The NSA and the three IDSFs also finance projects that assist with the decommissioning of closed plants. It is this assistance that helped to achieve the closure of Chernobyl 3 in 2000, Kozloduy 1 and 2 in 2002 and Ignalina 1 in 2004. By 2009, the remaining five first-generation Soviet-designed reactors in the enlarged EU will have been closed.

**Reforming the energy sector**

As well as helping to decommission old reactors, the IDSFs help to compensate for lost capacity and to modernise the energy sectors of the countries concerned. The potential for increases in energy efficiency in some of these countries is enormous. This is why the Kozloduy IDSF is contributing to an EBRD-financed energy efficiency credit line that allows local banks to on-lend to small energy efficiency projects.

The Kozloduy Fund contributes to energy efficiency measures in public and residential buildings as well as to the upgrading of district heating systems. Projects in Bulgaria will realise savings equivalent to 300 MW. Similar projects are envisaged for the Slovak Republic.

Lithuania will need to compensate for the loss of about 80 per cent of its electricity production once the Ignalina power plant is closed. The Ignalina IDSF is providing €90 million to co-finance the environmental upgrade of a thermal power plant. Once completed, this plant will provide most of Lithuania’s electricity.

**Progress in 2005**

The Chernobyl Shelter Fund (CSF) is funding the Shelter Implementation Plan to convert the destroyed Chernobyl unit into an environmentally safe state. In 2005 all infrastructure and preparatory projects were completed. The complicated stabilisation measures to reduce the risk of collapse for the existing shelter are on schedule. The tender process for the new safe confinement, which will enclose the unit and provide safe working conditions for future work, resulted in two bids by international consortia.

The Chernobyl Shelter Fund is funding the Shelter Implementation Plan to convert the destroyed Chernobyl unit into an environmentally safe state.

Donors to the NSA approved a contract amendment that will ensure the completion of a liquid radioactive waste treatment facility in Chernobyl. Major IDSF projects launched in 2005 included the environmental upgrade of a thermal power plant and the construction of a storage facility for solid radioactive waste in Lithuania.

**Project Preparation Committee**

The Project Preparation Committee (PPC) is primarily a networking mechanism to assist donors and IFIs in the preparation and financing of environmental projects. The PPC is based at the EBRD’s headquarters in London.

**Activities in 2005**

Four PPC officers (based in Belgrade, London and St Petersburg) helped to prepare and develop 16 investment projects at the EBRD in 2005. These mostly related to water supply and sanitation, waste management, energy efficiency and renewable energy.
A new web site was launched for PPC members (www.ppcenvironment.org). It is published in English and Russian and includes a database of grant finance sources. New publications developed in 2005 were:

- **Good Practice in Project Preparation:** guidance notes on good practice in project preparation for water and waste-water investment
- **A Model Public Services Agreement for the Water Sector:** for public water utilities
- **How to Promote Municipal Infrastructure Projects:** guidance on how to prepare a project concept document for discussion with potential financiers.

In November 2005 the Third Joint Meeting of the Task Force for the Implementation of the Environmental Action Plan (EAP) and the PPC took place in Yerevan, Armenia. The PPC session discussed opportunities and constraints for mobilising finance.

The PPC also organised a workshop on the Clean Development Mechanism (a financial instrument under the Kyoto Protocol) aimed at helping client companies understand the benefits of investing in emission reduction projects.

### Harnessing donor funding for environmental activities

In 2005 donors provided €16 million to support environmental activities connected with EBRD-financed projects and donor-supported programmes managed by the EBRD.

Nearly half of EBRD investment is supported in some way by donor funding. This is used to finance consultants who help to prepare the way for EBRD projects and provide specialist advice and training – for example, in lending procedures for small business clients.

For more information, see the EBRD Donor Report 2006 on the Bank's web site (www.ebrd.com/pubs).

#### Donor funding for environmental activities in 2005

<table>
<thead>
<tr>
<th>Sector</th>
<th>TC funds (€ million)</th>
<th>Source of funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Municipal and environmental infrastructure</td>
<td>8.0</td>
<td>Austria, Canada, Denmark, European Union, ETC Fund, Finland, France, Italy, Luxembourg, Netherlands, Northern Dimension Environmental Partnership, Norway, Spain, Sweden, United Kingdom, Switzerland</td>
</tr>
<tr>
<td>Energy</td>
<td>2.8</td>
<td>Austria, Canada, Central European Initiative, Denmark, ETC Fund, European Union, Italy, Japan, Netherlands, Norway, Switzerland</td>
</tr>
<tr>
<td>Finance</td>
<td>0.7</td>
<td>Canada, European Union</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1.2</td>
<td>Central European Initiative, European Union, Finland</td>
</tr>
<tr>
<td>Project Preparation Committee</td>
<td>1.1</td>
<td>Italy, Netherlands, United Kingdom</td>
</tr>
<tr>
<td>Training</td>
<td>0.2</td>
<td>ETC Fund, United Kingdom</td>
</tr>
<tr>
<td>Transport</td>
<td>1.7</td>
<td>Austria, Central European Initiative, European Union, Germany, Italy, Sweden</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>15.7</strong></td>
<td></td>
</tr>
</tbody>
</table>
The energy sector plays a vital part in the transition to sustainable market economies. Economic growth and modern living depend on reliable, cost-effective energy supplies. More than any other single issue, energy holds the key to future economic development in the Bank’s countries of operations.
By the end of 2005, oil and gas prices were far higher than forecast just a few years earlier. At the same time, energy needs are projected to rise by 60-80 per cent over the next 20 years. This intensifies the impact of energy on economic, social and environmental sustainability for the EBRD’s countries of operations.

Of the 27 countries in the EBRD’s region, only four produce oil and gas (Azerbaijan, Kazakhstan, Russia and Turkmenistan). The others depend on oil and gas imports as well as nuclear, hydro and coal as their main (and often problematic) sources of energy. Sustained higher world energy prices may offer significant growth opportunities for countries rich in hydrocarbon resources although questions of sustainable development and transparent revenue management also need to be addressed.

Sustained higher world energy prices may offer significant growth opportunities for countries rich in hydrocarbon resources.

For the energy consumers, higher prices may change the economics of energy use and offer greater incentives to increase the security of supply. This can be done by diversifying sources of energy, reducing energy waste, increasing renewable energy and cooperating with neighbours on cross-border energy issues.

Whether they are endowed with fossil fuels or not, the EBRD’s countries of operations are highly inefficient in their energy use and are heavily polluting. Compared with western Europe, they use up to seven times more energy and emit up to 30 times more greenhouse gases to produce each unit of gross domestic product. This may be partly due to the cold climate and a reliance on heavy industry but this high level of usage threatens energy security and economic development. It also leads to disproportionate levels of greenhouse gases and subsequent global warming.

For these reasons, energy efficiency is the cornerstone of the EBRD’s 2006 Energy Policy. The aim of the policy is to help the Bank’s countries of operations achieve secure, affordable and efficient energy supplies. This is fundamental to the emergence of open market-based economies and sustainable development.

Progress towards a new energy policy

Progress was made in 2005-06 on updating the EBRD’s Energy Policy. We consulted widely and put a timetable in place for adoption of the new policy by mid-2006.

Action on energy

To underline the importance of energy efficiency, the Bank’s draft Energy Policy proposes a formal target for EBRD investment in energy efficiency and renewable energy projects. The target is to lend or invest a total of €1 billion in such projects between 2006 and 2010, compared with €674 million in the previous five years.

The EBRD will also continue its support for regulatory reform and private sector participation in energy investment, the modernisation of power systems and reductions in transmission losses.

Corporate responsibility is another important focus, including transparency and the sound management of state revenues from natural resource development. The policy also addresses the environmental and social impact of energy activities.
The EBRD will continue to manage nuclear safety grant funds, as requested by the donors. The draft policy proposes one modification to the Bank’s existing energy policy regarding the financing of nuclear facilities. The proposal is that the Bank may provide financing to an operating facility for nuclear safety improvements or for the safe and secure management of radioactive waste and spent nuclear fuel without a direct link to the closure of high-risk reactors.

This modified approach would allow the Bank to address the continuing pressing concern with safety at nuclear power plants in the EBRD’s region. For more information on the Bank’s nuclear safety activities, see page 37.

**Summary of key points in the draft Energy Policy**

The new policy will mandate the EBRD to:

- increase its investment in energy efficiency as a means of improving competitiveness and energy security and of reducing future needs for energy investment
- address climate change and environmental concerns
- promote renewable energy technologies to help our countries of operations reduce their dependence on external supply
- raise the standards of corporate governance in the energy sector and promote a transparent approach to revenue management.

**Consultation exercise on the new Energy Policy**

At the start of 2005 the Bank held open forums in London, Sofia and Moscow to consult with non-governmental organisations (NGOs), research institutes and think-tanks. We also consulted widely with governments and within industry. Based on the consultation feedback, the Bank has refined its approach to the energy sector.

The EBRD is considering all recommendations from the consultation process. A final 45-day consultation period started in March 2006 (ending on 19 April 2006). After final modification, the policy will be submitted to the EBRD’s Board of Directors for approval. Publication of the final policy on the EBRD’s web site is expected in mid-2006. Summaries of all discussions are also available on the web site.

The draft Energy Policy has benefitted from the work of the EBRD’s independent Evaluation Department as well as two recently commissioned background papers from leading independent experts in power and energy and natural resources.

The Environmental Advisory Council (ENVAC, see page 68) assisted the Bank in preparing a discussion paper to kick off the consultation process. The draft policy was discussed at the Bank’s meeting with ENVAC in April 2005. ENVAC recommended a stronger focus on energy efficiency and suggested that the way to convince countries of the importance of energy efficiency would be to calculate the costs of not addressing this issue.
Energy initiatives in 2005

Sustainable energy initiative
The EBRD has developed a sustainable energy initiative to complement the EU Green Paper on Energy Efficiency. This is in response to the 2005 G8 meeting at Gleneagles, where there was a call for international financial institutions (IFIs) to develop new ways of supporting clean energy and energy efficiency as part of the wider campaign on global warming. The initiative will also help new EU member states and candidate countries to meet the EU renewable electricity targets. This initiative was announced at the Bank’s Annual Meeting in May 2006.

Carbon trading
Carbon credits help countries meet emission reduction targets under the Kyoto Protocol and other related agreements. They also give private companies an incentive to invest in climate-friendly projects, such as renewable energy.

Carbon credits give private companies an incentive to invest in climate-friendly projects, such as renewable energy.

The EBRD’s countries of operations have the potential to become large-scale suppliers of carbon credits. The EBRD acts as an intermediary, buying carbon credits on behalf of EBRD member states.

The Bank established its first carbon fund in October 2003, buying carbon credits on behalf of the Netherlands government from Bank-funded projects, under a trading mechanism created by the Kyoto Protocol. The fund supports energy efficiency, renewable energy, fuel switching and waste processing projects. Credits are generated when a project achieves a reduction in greenhouse gas emissions.

In 2005 the fund prepared a number of emission reduction projects for potential EBRD investment, particularly in Bulgaria, Romania and Ukraine. Ukraine also adopted procedures to become a seller of carbon credits (as a result of an initiative between the EBRD and the World Bank).

Supporting the Kyoto Protocol
The Kyoto Protocol commits the EU and 35 industrialised countries to reduce their greenhouse gas (GHG) emissions below levels specified for each of them in the Protocol. Between 2008 and 2012 this should amount to reductions of at least 5 per cent below 1990 levels overall. This includes 13 of the EBRD’s countries of operations (the eight EU countries plus Bulgaria, Croatia, Romania, Russia and Ukraine). A further eight EBRD countries signed the Protocol but do not have an emissions cap; most of the remaining EBRD countries of operations are working towards ratification.

The Protocol has created a market in which companies and governments that invest in projects to reduce GHG emissions can sell the ensuing carbon credits. Under the Joint...
Implementation (JI) trading mechanism, an industrialised country can invest in emission reduction projects in another industrialised country and apply the carbon credits received for those projects towards meeting its own carbon emission reduction goal.

The EBRD supports implementation of the Kyoto Protocol by funding emission reduction projects and by promoting the trading of carbon credits.

**Multilateral Carbon Credit Fund**

In 2005-06 the EBRD worked with the European Investment Bank (EIB) to set up a Multilateral Carbon Credit Fund (MCCF). It will be open to the EBRD’s member states and private companies. The fund will facilitate the sale of carbon credits resulting from projects in the EBRD’s countries of operations financed by the EBRD and/or the EIB. Typical projects will include industrial energy efficiency and renewable energy.

In 2005 the EBRD worked with the European Investment Bank to set up a Multilateral Carbon Credit Fund.

The preparing, negotiating, signing and monitoring of carbon credit transactions will be outsourced to private companies (“carbon managers”) that are expert in the carbon trading market. Selection of companies will be by a competitive process based on the EBRD’s Procurement Policies and Rules. The Fund is expected to become operational later in 2006.

**Greenhouse gases**

The EBRD conducts an annual review of the projects in which the Bank has made a direct investment for their potential to generate significant increases or savings in greenhouse gas (GHG) emissions.

We screen out the projects that lie in inherently “low-emission” sectors or that are not energy-intensive in character. For all other projects, the Bank makes an assessment of current and future levels of GHG emissions (before and after investment). We also include any significant process-related GHG emissions that occur in addition to those relating to energy use. The emissions are calculated for the project as a whole rather than for the Bank’s actual involvement.

**Basis of the assessment**

Many industrial projects involve modernising existing facilities. This may increase output capacity and produce consequently a rise in GHG emissions. Choosing the appropriate pre-investment baseline for measuring emissions is not always easy for projects in countries that have undergone huge political and economic upheavals. Uncertainty in the starting point inevitably means uncertainty in the change in emissions attributed to some projects.

Improvements to processes and in energy efficiency built into these projects lead to more efficient production and a more certain reduction in GHG emissions for each unit of output. Expanded production may displace less efficient production elsewhere, resulting in overall savings in emissions even when site emissions rise. Detailed baseline and forward projection studies are needed to quantify and verify the legitimacy of such indirect savings for GHG accounting purposes. These studies would normally only be undertaken for projects seeking to benefit from the Kyoto mechanisms (carbon trading etc.) so these potential savings cannot generally be included in the GHG assessment.

Many more projects now focus on energy efficiency improvement and result in overall reductions in GHG emissions, even when capacity rises. If the EBRD is financing the construction of new facilities, the Bank aims to ensure that greenhouse gas emissions are in line with current best practice.
Project analysis in 2005

In 2005 the EBRD signed 151 new projects. Of these, 24 (including sub-projects) were assessed as having potential for significant GHG emissions or emission savings. Analysis showed 20 as significant: this means pre- or post-investment emissions above 20 kilo tonnes a year (> 20 kt/y). These projects were in power and energy (eight), manufacturing (11) and transport (one).

Breakdown of the 20 projects assessed as having significant levels of emissions in 2005

<table>
<thead>
<tr>
<th>Number of projects</th>
<th>Impact</th>
<th>Reason for change in emissions</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>&gt; 0.6</td>
<td>Energy efficiency improvements in existing facilities for steel manufacturing and processing, aluminium processing, district heating, electricity transmission and distribution and aircraft fleet, giving absolute emission reductions</td>
</tr>
<tr>
<td>2</td>
<td>0.06</td>
<td>Expansion and/or modernisation of existing facilities for copper rolling and paper mill activities, giving higher absolute emissions but lower emissions per unit output in all projects</td>
</tr>
<tr>
<td>8</td>
<td>6.2</td>
<td>New or replacement facilities for manufacture of electricity, cement wood products, textiles and for industrial air separation</td>
</tr>
</tbody>
</table>

Annual assessment

The direct investments signed by the EBRD in 2005 are estimated to lead to a net increase in GHG emissions of 5.6 Mtpa. The dominant contribution is the 5.3 Mtpa emission increase associated with the new Maritza East I power station. This new plant will compensate for further closures of nuclear capacity, required as a condition of Bulgaria’s planned accession to the EU. The dominance of one or two projects in the annual assessments can generate significant variability in the net change in emissions from one year to the next. However, comparison with the 2004 assessment shows a broadly similar pattern continuing.

EBRD projects with significant GHG emissions

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Projects with significant emissions</td>
<td>20</td>
<td>27</td>
</tr>
<tr>
<td>Before-investment emissions (Mt CO(_2) pa)</td>
<td>15.6</td>
<td>19.6</td>
</tr>
<tr>
<td>After-investment emissions  (Mt CO(_2) pa)</td>
<td>21.2</td>
<td>23.6</td>
</tr>
<tr>
<td>Project net impact (Mt CO(_2) pa)</td>
<td>5.6</td>
<td>4.0</td>
</tr>
</tbody>
</table>

Investing in the energy sector

In 2005 the EBRD invested €741 million in the energy sector (comprising energy efficiency, natural resources, and power and energy projects), representing around 17 per cent of the Bank’s total investments during the year.

Energy efficiency

Energy efficiency is central to sustainability. Tackling the legacy of energy-intensive, poor-quality infrastructure has been one of the most difficult challenges of the transition process. The EBRD invests in modernising production systems, power and heat generation, transmission and distribution, and on improving the use of energy, especially in industry.
Projects with energy efficiency components
The EBRD’s dedicated energy efficiency team works with clients to identify opportunities and assists with project implementation. At the start of project appraisal, the Bank screens all projects for a potential energy efficiency component and gives every project a rating based on its potential for saving energy.

At the start of project appraisal, the Bank screens all projects for a potential energy efficiency component and gives every project a rating based on its potential for saving energy.

The Bank usually arranges a detailed energy audit for the most energy-intensive projects. Audits are funded by donors (currently, Austria, the Central European Initiative, the EU and Greece) and are provided at no cost to the client. The aim is to engage and focus the attention of senior management on energy efficiency – often for the first time and usually with positive results. In 2005 the Bank’s energy efficiency team carried out nine on-site surveys, including eight projects that involved energy audits by consultants.

To improve the effectiveness of its energy efficiency lending, the Bank is developing ways of benchmarking the energy efficiency performance of all EBRD clients. This will allow energy efficiency opportunities to be determined more efficiently than is possible at the moment (using only energy audits). It is hoped that this programme will be implemented later in 2006.

EBRD investments
Many of the EBRD’s energy efficiency investments are in projects where energy efficiency is not the sole objective but forms a significant component of the project. The energy efficiency components of EBRD investments signed in 2005 amounted to €205 million (excluding energy-saving investments in power generation and transmission).

These investments were spread across 23 projects. They included two investments in district heating systems (totalling €16 million) and a wide range of energy-saving activities in the industrial sector (totalling €102 million). The Bank also channelled €30 million through Bulgarian banks to finance energy efficiency projects in people’s homes (see page 51) and provided its first credit line to a Russian Bank (Spurt Bank) for the sole purpose of financing energy efficiency activities.

In the industrial sector, the EBRD invested €15 million (out of a total EBRD investment of €25 million) to finance energy efficiency improvements in Mittal Steel in Bosnia and Herzegovina. The finance is being used to modernise an old steel plant in the town of Zenica. The annual energy savings of 1.4 million gigajoules are roughly equal to the energy used by 70,000 homes. The reduction in carbon dioxide emissions by 200,000 tonnes is equal to that produced by 90,000 homes.
Tackling energy efficiency in Ukraine

Ukraine imports 70 per cent of its gas supply, mainly from Russia and Turkmenistan. Low awareness of energy waste coupled with the legacy of Soviet-era energy systems have contributed to Ukraine using over three times the amount of energy used in western Europe for each unit of gross domestic product. The dispute over gas prices between Kiev and Moscow at the start of 2006 highlighted the importance of this gas supply and the urgent need for energy efficiency in Ukraine.

Although cost-cutting investments can pay for themselves within a few years, it is still not easy to convince companies of the need for energy efficiency. Many companies do not know how to calculate the true cost of the energy that they use and are not aware of the impact on the company’s accounts.

To raise awareness of the need for energy efficiency, the EBRD collaborated with the EU and Ukraine to establish in 1998 the Ukrainian Energy Service Company (UkrESCO). Similar to other ESCOs that the EBRD has established, UkrESCO helps companies to understand where energy is wasted and to finance energy efficiency improvements. UkrESCO also helps to reduce carbon dioxide and other greenhouse gases (GHG) emitted in energy production.

Energy-saving projects initiated by UkrESCO include installing new boilers and pelleting machines (to convert grain into food pellets) at Ukraine’s biggest chicken feed factory. The new equipment has cut steam use from four to three tonnes an hour (and increased the volume and quality of the pellets produced).

The improvements in energy use have saved the company €2.5 million since 2003 and the new machines paid for themselves within 18 months.

In 2005 the EBRD provided a second, government-backed loan in preparation for the privatisation of UkrESCO in the near future. Privately owned ESCOs have already started up in competition with UkrESCO. One such firm, Energy Alliance, has received EBRD investment.
Financing energy efficiency through third parties
The EBRD finances energy efficiency through a number of mechanisms. These include:

**Energy service companies (ESCOs)** – specialist companies that invest in energy efficiency in the public and private sectors. They operate in many of the Bank’s countries of operations. In 2005 the EBRD made a second loan to UkrESCO.

**Energy efficiency credit lines** – EBRD funding is provided through local banks to finance smaller projects. An example is the Bulgarian Energy Efficiency and Renewable Energy Credit Line, which is supported by grants from the EBRD-managed Kozloduy IDSF (see page 50). In 2005 a second credit line was set up to support residential energy efficiency projects.

**Equity funds** – the funds provide equity for energy efficiency and renewable energy projects. An example is the Dexia-FondElec Energy Efficiency and Emission Reduction Fund, which invests in projects across a range of sectors, including district heating, public lighting and industry.

### EBRD projects with energy efficiency components signed in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Client</th>
<th>Sector</th>
<th>Project description</th>
<th>EBRD finance (€ million)</th>
<th>Energy efficiency component (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>Bazenc</td>
<td>Renewable energy</td>
<td>Small hydro power project</td>
<td>1.1</td>
<td>1.1</td>
</tr>
<tr>
<td>Armenia</td>
<td>DENO Gold</td>
<td>Natural resources</td>
<td>Working capital financing of a gold mining operation</td>
<td>3.8</td>
<td>0.1</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>Mittal Steel</td>
<td>Manufacturing</td>
<td>Implementation of crucial energy efficiency measures in newly reopened steel-making factory</td>
<td>25.0</td>
<td>15.0</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Distrigaz Sud</td>
<td>Power and energy</td>
<td>Modernisation of gas distribution system</td>
<td>31.0</td>
<td>18.2</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>North-eastern Bulgaria electricity distribution companies</td>
<td>Power and energy</td>
<td>Modernisation of electricity distribution network</td>
<td>16.8</td>
<td>16.8</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Residential energy efficiency credit line</td>
<td>Financial institutions</td>
<td>Credit line targeting energy efficiency improvements in households</td>
<td>30.1</td>
<td>30.1</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Svilosa</td>
<td>Manufacturing</td>
<td>Energy efficiency investments to enable the pulp mill to meet EU environmental standards</td>
<td>18.0</td>
<td>13.9</td>
</tr>
<tr>
<td>FYR Macedonia</td>
<td>Mittal Steel</td>
<td>Manufacturing</td>
<td>Investment in steel processing to improve energy efficiency</td>
<td>25.0</td>
<td>1.7</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>Central Asia Cement</td>
<td>Manufacturing</td>
<td>Expansion and modernisation of the Karaganda cement plant</td>
<td>16.9</td>
<td>16.9</td>
</tr>
<tr>
<td>Poland</td>
<td>Dalkia</td>
<td>Energy efficiency</td>
<td>Further investment in a district heating and co-generation facility for energy efficiency improvements</td>
<td>7.5</td>
<td>7.5</td>
</tr>
<tr>
<td>Regional</td>
<td>Lesaffre</td>
<td>Agribusiness</td>
<td>Financing to improve energy efficiency in yeast production in subsidiaries of Lesaffre</td>
<td>22.2</td>
<td>1.9</td>
</tr>
</tbody>
</table>
50 Special focus on energy

<table>
<thead>
<tr>
<th>Country</th>
<th>Sector/Project Description</th>
<th>Value (€ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>CFR Electrifi care Infrastructure Upgrade of electric traction power supply equipment</td>
<td>22.5 5.1</td>
</tr>
<tr>
<td>Romania</td>
<td>Egger Manufacturing Construction and start-up of a new particleboard production plant</td>
<td>61.0 2.0</td>
</tr>
<tr>
<td>Romania</td>
<td>Iasi district heating Municipal and environmental infrastructure Modernisation of the city district heating system</td>
<td>13.0 13.0</td>
</tr>
<tr>
<td>Romania</td>
<td>Stirom Agribusiness Modernisation and energy efficiency investments in glass manufacturer</td>
<td>10.0 7.1</td>
</tr>
<tr>
<td>Russia</td>
<td>Air Liquide Manufacturing Construction of on-site air separation facility to improve air quality</td>
<td>36.0 30.9</td>
</tr>
<tr>
<td>Russia</td>
<td>Botnia – SVIR Manufacturing Construction and start-up of a new sawmill</td>
<td>22.5 1.0</td>
</tr>
<tr>
<td>Russia</td>
<td>OAO Samara Metallurgical Plant Manufacturing Environmental and energy efficiency improvements alongside general modernisation programme</td>
<td>25.4 4.1</td>
</tr>
<tr>
<td>Russia</td>
<td>Pfeiderer Manufacturing Construction of a chipboard production facility</td>
<td>32.0 1.2</td>
</tr>
<tr>
<td>Russia</td>
<td>Spurt Bank Financial institutions Credit line targeting energy efficiency improvements in households</td>
<td>8.1 8.1</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Sevojn rolling mill Manufacturing Fuel switch, provision of new equipment and modernisation of existing machinery</td>
<td>14.0 1.0</td>
</tr>
<tr>
<td>Slovak Republic</td>
<td>Kronospan Manufacturing Expansion of existing MDF manufacturing capacity</td>
<td>14.5 0.4</td>
</tr>
<tr>
<td>Ukraine</td>
<td>UkrESCO II Energy efficiency Further investment in state-owned energy service company established in 1998 by the EBRD</td>
<td>8.2 8.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>464.6 205.4</strong></td>
</tr>
</tbody>
</table>

Kozloduy International Decommissioning Support Fund
The donor-funded Kozloduy International Decommissioning Support Fund (KIDSF) was set up to finance the closure of four nuclear units at the Kozloduy Nuclear Plant that were considered unsafe by the international community (see page 37). To compensate for the loss of electricity generating capacity, almost half of the fund has been dedicated to strengthening Bulgaria’s energy sector.

Energy efficiency is a key area of support for the KIDSF. The main focus is on financing smaller projects through innovative financing mechanisms. The fund provides grants to prepare the way for future projects and gives incentive payments to participating banks and borrowers. This has been a key factor in the success of the Fund. Cutting energy costs in Bulgaria is helping the country to improve its competitiveness and to reduce the environmental impact of its economic growth.

Bulgarian Energy Efficiency and Renewable Energy Credit Line
The Bulgarian Energy Efficiency and Renewable Energy Credit Line was established in March 2004 with EBRD financing of €50 million and a €10 million grant from the KIDSF to promote
energy efficiency and renewable energy projects in private sector businesses across Bulgaria. Loans are currently disbursed through six local banks.

By the end of 2005, loans totalling €20 million had supported 36 projects (€12.5 million for 20 renewable energy projects and €7.5 million for 16 energy efficiency projects). These have led to emission reductions of 263,000 tons of CO₂ a year – the equivalent output of over 40,000 UK households in one year. The benefit from the increase in capacity (through renewable energy projects) and the energy saving (through energy efficiency projects) is the equivalent of a 90-megawatt electricity power station (see www.beerecl.com).

**Residential Energy Efficiency Credit Line**

The Residential Energy Efficiency Credit Line was launched in mid-2005 with a €10 million grant from the KIDSF and €50 million from the EBRD. By the end of 2005, credit lines totalling €30 million had been extended to four Bulgarian banks. This financing has been used to provide almost 400 loans totalling €500,000 to households for the installation of gas boilers, stoves, heat pumps, energy-efficient windows and other measures.

As an incentive for rapid implementation, borrowers benefit from a grant on completion of the work. Over 200 projects were completed and eligible for a project completion payment by the end of 2005 (see www.reecl.com).

### Saving energy in the home in Sofia

Apartment blocks built in the communist era were poorly constructed, with little insulation to keep heat in and cold out. Saving energy was not a concern because heating was supplied by centralised municipal systems and funded almost entirely by the state. But times have changed and consumers now have to pay their own utility bills.

To ease the burden, homeowners in Sofia can now apply for small home improvement loans via a residential credit line funded by the EBRD and the donor-funded Kozloduy International Decommissioning Support Fund. The loans pay for new windows, insulation panels, heat pumps, solar water heaters and new fuel-efficient boilers. Once the home improvements are done and independently checked, each home-owner gets a grant of up to 20 per cent of their project costs.

The availability of the loans is raising awareness of the need to reduce energy waste. Around 30,000 households across Bulgaria are expected to benefit from the programme. The average loan size is between €1,000 and €1,500. It is also boosting Sofia’s window-framing businesses: sales are expected to rise by about 22 per cent a year in 2006.

The credit line also finances households to switch to renewable fuels, including wood waste and wood pellets (abundant in well-forested Bulgaria), cherry pits from a local jam company and sunflower seed shells from a vegetable oil manufacturer.

EBRD funds are loaned at market rates via four Bulgarian banks: United Bulgarian Bank (UBB), Raiffeisenbank (Bulgaria), Postbank and DSK Bank.
Natural resources
The EBRD’s countries of operations have large energy resources, particularly in oil and gas but also in coal. Russia alone accounts for over a quarter of global gas reserves. The concentration of resources in a few countries raises concerns about energy dependence among energy-importing countries and about the scope for corruption in resource-rich countries.

The Bank continues to support sound management in the natural resources sector, helping to ensure that best international standards and practices in environmental and social issues, transparency and revenue management are followed. This includes applying the principles of the Extractive Industry Transparency Initiative in countries where these have been endorsed.

The EBRD invested €196 million in six natural resources projects in 2005. These included a €59 million investment to finance the completion of a gas pipeline in Azerbaijan and Georgia and €93 million for the first stage of an offshore gas development in Azerbaijan.

Natural resources projects signed by the EBRD in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Client</th>
<th>Project description</th>
<th>EBRD finance (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>DENO</td>
<td>Gold mining project</td>
<td>3.8</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>Lukoil Overseas</td>
<td>Development of the offshore Shah Deniz gas and gas condensate field</td>
<td>93.0</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Chelopech Mining</td>
<td>Environmental improvements, refurbishment, modernisation and expansion of the Chelopech gold and copper mine and processing plant</td>
<td>8.5</td>
</tr>
<tr>
<td>Regional</td>
<td>Lukoil Overseas</td>
<td>Completion of the pipeline in Azerbaijan and Georgia</td>
<td>59.2</td>
</tr>
<tr>
<td>Russia</td>
<td>High River Gold</td>
<td>Equity stake in a gold mining company</td>
<td>10.7</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Galnaftogaz</td>
<td>Partial funding for the reconstruction, construction and acquisition of petrol stations</td>
<td>21.1</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>196.3</td>
</tr>
</tbody>
</table>
**Power and energy**

Reliable power supplies are critical to improving living conditions, especially for those who live in freezing temperatures for several months of the year. This was highlighted by the blackout that hit Moscow and the surrounding region in May 2005 and the disruption in power supply in Georgia at the start of the 2006 winter.

EBRD investments in the power and energy sector are used to modernise heat and power plants, increase capacity, reduce losses and increase the quality and reliability of supply. The Bank invested €528 million in nine projects in 2005.

In Russia, financing for two projects was provided in local currency, avoiding exchange risk to the local economy. The EBRD lent the rouble equivalent of €147 million to Russia’s electricity transmission monopoly, the Federal Grid Company, and €85 million to Mosenergo, Russia’s largest electricity generating company.

Both projects are financing the modernisation of infrastructure as part of the EBRD’s support for the wide-ranging reform of the power sector (launched by the Russian government in 2001). The investment in the Federal Grid Company will improve the flow of electricity to central Russia and the Caucasus. Financing for Mosenergo will help the company to modernise its existing plants and to reduce emissions, leading to a more reliable electricity supply for the residents of Moscow and less air pollution.

### Power and energy projects signed by the EBRD in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Client</th>
<th>Project description</th>
<th>EBRD finance (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>Bazenc</td>
<td>Investment in small hydropower project under the Bank’s Direct Lending Facility</td>
<td>1.1</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Maritza East I Power Company</td>
<td>Construction of a lignite-fired power plant</td>
<td>114.0</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>North-eastern Bulgaria electricity distribution companies</td>
<td>Support for the privatisation of two electricity distribution companies</td>
<td>16.8</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>KEGOC</td>
<td>Development of YukGres-Shu power transmission infrastructure</td>
<td>44.6</td>
</tr>
<tr>
<td>Poland</td>
<td>Patnow II</td>
<td>Construction of a new unit at Patnow Adamow Konin, a group of three lignite-fired power plants</td>
<td>62.8</td>
</tr>
<tr>
<td>Romania</td>
<td>Distrigaz Sud</td>
<td>Support for the privatisation of a gas distribution company</td>
<td>31.0</td>
</tr>
<tr>
<td>Russia</td>
<td>Mosenergo</td>
<td>Loan to generation company</td>
<td>85.3</td>
</tr>
<tr>
<td>Russia</td>
<td>Federal Grid Company</td>
<td>Rouble financing for modernisation of the company’s infrastructure</td>
<td>147.1</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Odessa high-voltage grid</td>
<td>Loan to upgrade high-voltage grid</td>
<td>25.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>528.5</strong></td>
</tr>
</tbody>
</table>
Renewable energy

Renewable energy offers important benefits in terms of ensuring a diverse supply of energy and reducing adverse environmental impact. Most of the countries in the EBRD’s region are heavily dependent on imported gas. Diversifying energy supplies to reduce dependence on imports is now a top priority in these countries.

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The EBRD’s region is rich in renewable energy resources, such as biomass, wind and hydro. In 2003 the Bank commissioned an extensive survey of renewable energy potential in each of its countries. As part of the programme (supported by the United States Agency for International Development), a dedicated web site has been established at www.ebrdrenewables.com. It includes up-to-date information and news on renewable energy developments throughout the EBRD’s region.

Hydro power, wind energy and biomass offer significant scope for reducing pollution and dependence on other sources of energy. In spite of this potential, renewable energy currently contributes a comparatively small amount to power generation in the EBRD’s countries of operations. Hydro is currently a significant source of power in Albania, Romania and Russia but elsewhere the contribution from renewables is modest or non-existent.

An important factor in this relatively low uptake has been the lack of supporting regulatory frameworks to provide the necessary levels of revenue for renewable energy, which often cannot compete directly with conventional power – particularly when the full market price is not being charged for primary energy supplies. With the accession of eight of the Bank’s countries of operations into the European Union, this is now changing.

Adoption of the EU directive on generation of electricity from renewable energy sources has led to the introduction of regulatory support frameworks. This, in turn, has led to major renewable energy projects in the EBRD’s region being developed. The EBRD is actively engaged in these new markets and will develop our involvement as the new EU members adopt their

<table>
<thead>
<tr>
<th>Project</th>
<th>Country</th>
<th>Loan (€ million)</th>
<th>Project cost (€ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drin River cascade upgrade</td>
<td>Albania</td>
<td>1.4</td>
<td>34.2</td>
</tr>
<tr>
<td>Albania power sector reconstruction</td>
<td>Albania</td>
<td>30.0</td>
<td>63.2</td>
</tr>
<tr>
<td>Yenikend renewable energy</td>
<td>Azerbaijan</td>
<td>42.7</td>
<td>60.3</td>
</tr>
<tr>
<td>Mingechaur power</td>
<td>Azerbaijan</td>
<td>17.4</td>
<td>38.8</td>
</tr>
<tr>
<td>Enguri hydro power plant</td>
<td>Georgia</td>
<td>31.1</td>
<td>119.7</td>
</tr>
<tr>
<td>Daugava hydro schemes upgrade</td>
<td>Latvia</td>
<td>18.8</td>
<td>56.8</td>
</tr>
<tr>
<td>Mutnovsky independent geothermal power plant</td>
<td>Russia</td>
<td>80.2</td>
<td>120.6</td>
</tr>
<tr>
<td>Drava River hydro power</td>
<td>Slovenia</td>
<td>65.1</td>
<td>107.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>286.7</strong></td>
<td><strong>600.8</strong></td>
</tr>
</tbody>
</table>
Harnessing renewable energy in the Bulgarian ski region

Heating is one of a hotel’s biggest costs, especially one that specialises in winter sports. At the new Orphey Hotel in the Bulgarian ski resort of Bansko, a 100-cubic metre man-made reservoir five metres below ground collects warm water from underground sources and cold water from melting snow running down nearby mountains. Heat created by a change in water pressure is used to warm the hotel’s rooms, showers, jacuzzis and pool.

The renewable energy source has had a big impact on the hotel’s monthly heating bill: the cost is just 7,500 lev (€3,800) – 75 per cent less than the 31,000 lev (€16,000) that Mr and Mrs Gigova, the hotel owners, estimate it would have cost to heat it using oil.

There is a constant, reliable source of fuel to heat all 70 rooms and a hot pool that stands at a steady 33 degrees, something no other hotel in the ski region can boast. The hotel emits little carbon dioxide, one of the gases responsible for global warming.

To finance the project, the Gigovas turned to United Bulgaria Bank (UBB), which had provided an earlier loan for hotel construction. They were delighted to discover that the project qualified for a grant, in the form of a 20 per cent loan rebate, to be provided on completion of their project.

The Gigovas are one of many UBB clients in Bulgaria benefiting from this money-back grant scheme. They qualify under a fund set up in 2005 by the EBRD and the multi-donor Kozloduy International Decommissioning Support Fund, which helps compensate for Bulgaria’s loss of electricity from the closure of four units at the Kozloduy nuclear plant (see page 50).

The grant finance is an important catalyst in promoting energy efficiency and renewables, acting as an incentive for entrepreneurs to undertake such projects.
own regulatory frameworks. The Bank will also work with other countries to encourage them to develop renewable energy.

By the end of 2005 the Bank had financed 28 renewable energy projects totalling €299 million (see table). This includes 20 projects financed indirectly via the Bulgarian Energy Efficiency and Renewable Energy Credit Line (see page 51).

**Renewable energy projects financed through the Bulgarian Energy Efficiency and Renewable Energy Credit Line**

<table>
<thead>
<tr>
<th>Project name</th>
<th>Loan (€ thousand)</th>
<th>Project cost (€ thousand)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tamrash hydro power plan</td>
<td>1,329</td>
<td>2,147</td>
</tr>
<tr>
<td>Treshena hydro power plant</td>
<td>258</td>
<td>316</td>
</tr>
<tr>
<td>Daisy Technology geothermal</td>
<td>485</td>
<td>539</td>
</tr>
<tr>
<td>Lesitchevo hydro power plant</td>
<td>380</td>
<td>884</td>
</tr>
<tr>
<td>TAS hydro power plant</td>
<td>330</td>
<td>435</td>
</tr>
<tr>
<td>Katunci hydro power plant</td>
<td>750</td>
<td>1,200</td>
</tr>
<tr>
<td>Wiwa Agrotex biomass project</td>
<td>350</td>
<td>409</td>
</tr>
<tr>
<td>Erato Holding biomass project</td>
<td>368</td>
<td>412</td>
</tr>
<tr>
<td>Sily-D wind park project</td>
<td>170</td>
<td>188</td>
</tr>
<tr>
<td>Nik Building wind park project</td>
<td>150</td>
<td>188</td>
</tr>
<tr>
<td>Lesitchevo hydro power plant 2</td>
<td>280</td>
<td>700</td>
</tr>
<tr>
<td>Argos wind power plant</td>
<td>600</td>
<td>771</td>
</tr>
<tr>
<td>Loziata hydro power plant</td>
<td>1,500</td>
<td>1,800</td>
</tr>
<tr>
<td>Efekt 3 geothermal project</td>
<td>680</td>
<td>700</td>
</tr>
<tr>
<td>Byala Mesta hydro power plant</td>
<td>1,000</td>
<td>1,250</td>
</tr>
<tr>
<td>Cherna Mesta hydro power plant</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td>Vita 02 biomass project</td>
<td>80</td>
<td>100</td>
</tr>
<tr>
<td>PFS biomass project</td>
<td>2,000</td>
<td>7,500</td>
</tr>
<tr>
<td>Energy Company Prometheus biomass project</td>
<td>380</td>
<td>500</td>
</tr>
<tr>
<td>Eton geothermal project</td>
<td>458</td>
<td>573</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>12,548</strong></td>
<td><strong>21,612</strong></td>
</tr>
</tbody>
</table>

**Taking corrective action**

As part of the assessment whether projects are eligible under the Bulgarian Energy Efficiency and Renewable Energy Credit Line, all proposed projects are subject to an environmental due diligence and feasibility study conducted by independent consultants. In addition to assessing the project’s projected energy performance, the consultant verifies that projects are in compliance with Bulgarian environmental regulations.

All proposed projects are subject to an environmental due diligence and feasibility study conducted by independent consultants.

In the case of mini-hydro projects, the EBRD has found that additional safeguards are needed to ensure that the projects comply with good international practice and the EBRD’s Environmental Policy. During a monitoring mission carried out in July 2005, prompted by NGO concerns, the EBRD’s environmental staff found that one small hydro project financed under the credit line was leading to environmental degradation of the related river system, despite being in full compliance with Bulgarian environmental legislation.

The EBRD responded quickly to the findings of the monitoring mission and required the borrower to put additional safeguards in place. All future mini hydro projects financed under the credit line have to meet additional environmental eligibility criteria, based on good international practice. A local environmental impact expert, also funded by the KIDSF, has been hired to assess compliance with these eligibility criteria as part of the project approval process. While these safeguards were being agreed with the participating banks, financing for hydro projects was put on hold.
Affordability of energy

Reform of public utilities includes removing heavy subsidies and introducing tariff structures that reflect the true costs of energy generation and distribution. Charging true costs helps energy companies to finance the large-scale investment needed for energy efficiency investments and improvements in the reliability of energy supply. Since tariff reform has the biggest impact on those who find it hardest to pay high energy bills, measures need to be taken to protect the economically vulnerable.

Reform of public utilities includes removing heavy subsidies and introducing tariff structures that reflect the true costs of energy generation and distribution.

Taking account of the ability to pay

Even with currently low prices, many low-income households find it hard to pay their utility bills in full and on time. For example, in Croatia, FYR Macedonia, Georgia and the Slovak Republic, the poorest 10 per cent of households currently spend more than 10 per cent of their income on electric power alone. Expenditure of 10 per cent or more of the household budget for electricity is often considered to be the point beyond which affordability becomes a problem. The issue of affordability is particularly acute in the seven poorest countries where the Bank operates – the early transition countries.

Affordability of utility services for the poorest 10 per cent of the population in the early transition countries

(Percentage of household expenditure devoted to electricity)

<table>
<thead>
<tr>
<th>Country</th>
<th>2003</th>
<th>2007 (projected)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>6.1</td>
<td>8.5</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>2.4</td>
<td>2.7</td>
</tr>
<tr>
<td>Georgia</td>
<td>14.1</td>
<td>15.5</td>
</tr>
<tr>
<td>Kyrgyz Republic</td>
<td>2.8</td>
<td>5.9</td>
</tr>
<tr>
<td>Moldova</td>
<td>4.9</td>
<td>5.1</td>
</tr>
<tr>
<td>Tajikistan</td>
<td>2.5</td>
<td>8.9</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>4.6</td>
<td>9.0</td>
</tr>
</tbody>
</table>

Notes: Data for Armenia and the Kyrgyz Republic refer to 2002. Data for Georgia and Uzbekistan relate to household income as opposed to expenditure. The 2007 estimate is based on a scenario where power tariffs reach cost-recovery level by this date.

Considering the effects of tariff reform

In many countries where the EBRD operates, electricity and district heating tariffs are still unsustainably low and the payment record is patchy. Dilapidated infrastructure can only be improved once underfunded energy industries are put on a sound financial footing and tariffs are adjusted to be more reflective of actual costs.
Safety campaign aims to reduce death toll in Moldova

Death from electrocution is 100 times higher in Moldova than in the UK – caused mainly by poor people trying to steal electricity through illegal hook-ups to power lines and substations. Children accounted for 20 out of 47 accidents and 8 out of 33 deaths in the Moldovan power sector in 2004: injured or killed while stealing coils of metal worth €1.5-€2.5. Poverty is the root cause, particularly in rural areas where villagers get by on half the national income of €85 a month (if they have a cash income at all).

To tackle the issue, the EBRD joined forces with the Moldovan government and the Canadian International Development Agency to establish a safety awareness campaign and to educate the public to keep away from electrical facilities. The Moldovan Working Group on Electrical Safety was formed in 2003 to bring together all relevant Moldovan ministries and agencies and the public and private electricity distribution companies. The EBRD was its first chair.

The campaign reaches children through their teachers, and parents through their children. An Electrical Safety Awareness Week focused on schoolchildren was launched in November 2005 with a hugely successful poster contest. A teacher training programme and colourful, easy-to-understand safety posters were developed by consultants funded by the Canadian government via the EBRD.

The project directly trained teachers from 60 schools but over 300 schools sent in entries for the safety poster contest. “That’s half the schools in the country, which means the first batch of teachers went beyond their own schools to tell others about it. We ended up with 2,500 poster entries, a fantastic result,” commented an EBRD banker who worked with the consultants. The Working Group on Electrical Safety is already planning its 2006 electricity safety week.

Moldova’s electrical distribution network is partly privatised. Union Fenosa, which has received EBRD financing of €25 million, focuses its maintenance and upgrading programme on those areas where accidents happen most often.
A Working Paper published by the EBRD in 2005 looked at the impact of tariff reform on the economically vulnerable who are hardest hit by higher tariffs. Given current conditions, there appears to be no “quick fix”. Affordability problems caused by higher, market-oriented tariffs are likely to get worse before they get better. In most cases, tariff increases will be steeper than the rate of income growth and will only level off once cost recovery has been reached.

The paper discusses various models to mitigate the effects of tariff reform, including block tariffs, targeted assistance programmes and end-user efficiency programmes. Although there are a number of constraints for implementing these solutions, they point to an urgent need to improve social safety provisions rather than postpone tariff reform. The paper is published on the Bank’s web site at www.ebrd.com/pubs/econo/wp0092.htm.

There is an urgent need to improve social provisions rather than postpone tariff reform.

Measures to reduce the social impact of higher tariffs

During the project appraisal process, the EBRD uses a standard affordability analysis to assess the probable impact of tariff changes. Following this, the Bank seeks to incorporate measures into the project structure to alleviate the impact on low-income households, where necessary.

Some of the measures available are outlined below.

**Block or lifeline tariffs:** a minimum amount of energy is provided at a low price or free and consumption beyond this threshold is charged at full cost. However, household consumption has to be metered and, at least in the case of district heating meters, may be difficult to install.

**Targeted assistance programmes:** vulnerable consumer groups in some of the poorest countries are eligible for means-tested cash payments or direct income transfers to cover a minimum level of electricity consumption. Some programmes operate only in winter when fuel bills are highest. However, these programmes require effective management, administration, monitoring and funding and are difficult to maintain.

The type of measure used depends on the effectiveness of a country’s institutions. Countries with high poverty levels and poor targeting systems might be better off with lifeline tariffs while countries with a lower level of poverty may benefit from direct income transfers.
Promoting transparency and accountability

The EBRD is committed to transparency and accountability in all of the Bank’s activities and has policies and mechanisms to ensure that we operate responsibly.
Public Information Policy

The EBRD’s Public Information Policy (PIP) underscores the Bank’s commitment to enhance the transparency of all our operations. It ensures that we act responsibly and that we consider the views of others in the shaping of our policies and actions.

The Bank continues to be guided by the underlying principle that, whenever possible, information concerning the Bank’s operations will be made available to the public unless there is a compelling reason for confidentiality.

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The annual report on the Bank’s implementation of the PIP found that the EBRD had fulfilled all of its commitments. At the end of 2005 the Bank started its three-yearly review of the policy, which it completed in 2006.

Making information accessible

The EBRD translates policy documents and country strategies into the local languages of the Bank’s countries of operations to widen opportunities for public consultation. By the end of 2005 the Bank’s Environmental Policy was available in 13 languages (Bosnian, Croatian, Czech, English, Estonian, Lithuanian, Moldovan, Polish, Romanian, Russian, Serbian, Slovak and Slovenian). All of these are available via the Bank’s web site.

The Guidelines and Rules of Procedure for the Independent Recourse Mechanism are available in English, Russian and Slovenian (see page 69); they are also being translated into other languages.

A total of 20 country strategies have been translated into local languages, with work in progress on the remaining seven new strategies.

Engaging in dialogue

The EBRD consults regularly and widely with the people and organisations that are affected by the projects that the Bank finances. We also invite comments on all new Bank policies and country strategies from all interested parties, including central and local government and businesses.

This consultation is a critical part of the EBRD’s decision-making process. Complex projects that have the highest potential environmental impact (“Category A”) include a public consultation period. Depending on the public/private status of the project and its complexity, the consultation period ranges from 60 days to up to 120 days and is an opportunity for anyone to voice concerns.

All views received during public consultation help the Bank to make a full assessment of a project. At the end of this period the EBRD analyses the comments before making any investment decision.

In our general consultation we include:

• local communities
• local and international non-governmental organisations (NGOs)
• international financial institutions (IFIs)
• businesses
• local authorities
• environmental bodies and multilateral organisations, such as the Project Preparation Committee, the Northern Dimension Environmental Partnership and the Global Environment Facility (see pages 35 and 37).
Public consultation on the EBRD’s Energy Policy
Development of the EBRD’s draft Energy Policy involved widespread consultation in 2005, starting with public consultation workshops in January 2005. The Bank held open forums in London, Moscow and Sofia with NGOs, research institutes and think-tank organisations. The Bank also consulted widely with governments and within industry and took their comments into account in refining the policy. Summaries of the discussions are on the Bank’s web site (www.ebrd.com). For further information about the draft Energy Policy, see Part 2 of this Report.

Inviting comments on new country strategies
EBRD country strategies outline the Bank’s approach for each of the countries where we operate. The Bank reviews each strategy every two years and invites public comment during the review process. A summary of the comments, along with the Bank’s responses, is posted on our web site once the revised strategy is approved. In 2005 we published new country strategies for 12 countries: Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Hungary, Latvia, Moldova, Romania, Tajikistan, Ukraine and Uzbekistan (see page 11).

NGO relations
The EBRD engages in regular dialogue with NGOs regarding Bank projects and policies. Dialogue between the EBRD, NGOs and local communities is facilitated by the Bank’s Outreach Unit.

The EBRD has developed an NGO area on the Bank’s web site, which includes a “What’s new” section and “Useful advice for NGOs”. An NGO newsletter is published four times a year, in English and Russian, and this is also posted on the web site.

Each year at the EBRD Annual Meeting, NGOs have their own programme of discussions, consultations and meetings. NGOs regularly attend meetings with the EBRD Board and provide briefings to Board members ahead of a Board visit to one of the Bank’s countries of operations.

Public consultation on the Sava River crossing
Consultation with the local community was a key element of an important transport project in Belgrade (Serbia), which was approved by the EBRD in 2005. The EBRD requested two public meetings to ensure that all issues concerning a new crossing for the River Sava were being addressed in the project’s Environmental Impact Assessment (EIA).

Belgrade has only two road bridges connecting the older part of Belgrade (900,000 inhabitants) with New Belgrade and Zemun (400,000 inhabitants). Traffic congestion, noise and air pollution caused by the lack of crossings are some of the city’s most pressing problems.

The EBRD-financed project supports the construction of a new bridge that would significantly reduce traffic congestion between the two parts of the city. However, the bridge would cross the Ada Ciganlija island, the biggest recreational area in central Belgrade. With a combination of forest and open meadows, the “Ada” is one of the most popular spots for the 1.6 million residents of Belgrade.

A wide range of NGOs attended the public meetings. Following the consultation, changes were made to the project – notably moving the location of the bridge from the centre to the tip of the island. The meetings confirmed strong support for the project but some concerns were raised about the protection of natural resources, cultural and historical monuments, the effects on flora and fauna, and the impact on recreation on the island.

Assurances were given that all the issues raised by the EIA and the consultation process would be taken into account in the preparation of the project and included in the Environmental Management and Monitoring Plan.
Promoting transparency and accountability

NGO programme at the 2005 Annual Meeting

Around 110 people from 80 international and local organisations in 30 countries attended the Bank’s NGO programme at the 2005 Annual Meeting in Belgrade. Their concerns ranged from the environment and development issues to biodiversity and human rights.

The NGO programme included consultation meetings on the Bank’s policies and evaluation activities. The NGOs met with the Bank’s President, Board of Directors and other key staff. A meeting was also organised for business associations and chambers of commerce to present the Bank’s small business finance, TurnAround Management and Business Advisory Services Programmes (see page 31).

The main topics discussed were the Bank’s draft Energy Policy, the forthcoming review of the Public Information Policy, Sakhalin Island (see page 67), corruption, human rights and the EBRD’s new strategy for Uzbekistan (see page 12). Other topics for discussion included the privatisation of KAP Aluminium in Montenegro, property and human rights in Serbia, the Baku-Tbilisi-Ceyhan pipeline and progress under the new government in Ukraine.

Disclosing information on EBRD projects

For projects that might receive EBRD financing, the Bank publishes a Project Summary Document (PSD) to give interested parties an opportunity to comment on the project. This discloses the main aim of the project, its financial details and a summary of the environmental aspects. For private sector projects, PSDs are posted (subject to certain exceptions) on the Bank’s web site at least 30 days before consideration by the Bank’s Board of Directors. For public sector projects, this is extended to 60 days.

Publication of PSDs may be delayed in certain circumstances. These include:

- legitimate sponsor or client concerns about confidentiality
- concern about the likelihood of substantial changes or rejection at the Board’s final review stage of a project proposal, which might embarrass the sponsor and prejudice alternative sources of funding
- concern about financial market sensitivity if capital transactions are involved.

In 2005 the EBRD published PSDs for 181 projects under consideration for financing.

Environmental Impact Assessments

Environmental Impact Assessments (EIAs) are required for the most environmentally sensitive projects financed by the EBRD (see page 15). These are classified as “Category A”. The client must release the EIA for public comment in the Bank’s headquarters and in the relevant Resident Office in our countries of operations. The period of disclosure varies from project to project. The minimum set by our Environmental Policy is 60 days prior to Board discussion but the period could be twice that long depending on the public/private status of the project and its complexity. For public sector projects, the minimum disclosure period is 120 days. During the public consultation period, interested parties from locally affected people to the wider interested public – can raise any problems that they have identified. Clients are required to provide information on how these comments will be taken into account.

EIAs in 2005

Eleven projects were classified as “Category A” in 2005. Full EIA documentation for all 11 was made available by the client in the relevant local languages. Nine of the 11 projects had full documentation available electronically on the client’s web site in the local language. Two projects did not have web site disclosure:
Promoting transparency and accountability

- **M6 motorway in Hungary:** Since local farmers and villagers had limited access to the internet, the EIA was made available in village halls along the motorway route so that people affected by the project could review the documents in hard copy.

- **Belgrade-Nov  Sad motorway in Serbia and Montenegro:** The client did not have a website when the EIA was published. It has subsequently developed a website. A request has been made to post the EIA during the construction period.

For all 11 projects, executive summaries (in English) were posted on the EBRD’s website. Links were provided to a local website and local language information where possible. Eight of the 11 projects progressed to Board review during 2005. Seven of the projects met the public disclosure requirements about the release of information. However, there was a delay in posting information on the Bank’s website for one project (Belchatow II – see table) and one project (Odessa grid – see page 66) did not comply with the 120-day disclosure requirement.

### Environmental Impact Assessments released in 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Project name</th>
<th>Sector</th>
<th>EIA made available in HQ/Resident Office</th>
<th>Date of Board</th>
<th>Days available before Board</th>
<th>Language</th>
<th>Electronic availability/language</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>Fier-Tepelené road upgrading</td>
<td>State</td>
<td>2 July 2004</td>
<td>17 May 2005</td>
<td>320 days</td>
<td>Albanian</td>
<td>Web site in Albanian, English</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Maritza East 1 Power Co.</td>
<td>Private</td>
<td>31 March 2005</td>
<td>26 July 2005</td>
<td>118 days</td>
<td>Bulgarian</td>
<td>Web site in Bulgarian, English</td>
</tr>
<tr>
<td>Hungary</td>
<td>M6 motorway</td>
<td>Private</td>
<td>4 March 2005</td>
<td>17 May 2005</td>
<td>74 days</td>
<td>Hungarian</td>
<td>Hard copy only – Hungarian, English</td>
</tr>
<tr>
<td>Poland</td>
<td>Belchatow II</td>
<td>State</td>
<td>2 August 2005 (Board received); 5 August 2005 (web site)</td>
<td>29 November 2005</td>
<td>120 days (117 days on web site)</td>
<td>Polish</td>
<td>Web site in Polish, English</td>
</tr>
<tr>
<td>Romania</td>
<td>Constanța by-pass</td>
<td>State</td>
<td>1 July 2005</td>
<td>15 November 2005</td>
<td>138 days</td>
<td>Romanian</td>
<td>Web site in Romanian, English</td>
</tr>
<tr>
<td>Russia</td>
<td>Sakhalin II Phase 2</td>
<td>Private</td>
<td>20 December 2005</td>
<td>–</td>
<td>–</td>
<td>Russian, parts in Japanese</td>
<td>Web site Russian, English; some information in Japanese</td>
</tr>
<tr>
<td>Russia</td>
<td>Berezitovy gold project</td>
<td>Private</td>
<td>19 December 2005</td>
<td>–</td>
<td>–</td>
<td>Russian</td>
<td>Web site in Russian</td>
</tr>
<tr>
<td>Russia</td>
<td>Trans Siberian gold</td>
<td>Private</td>
<td>1 July 2005</td>
<td>–</td>
<td>–</td>
<td>Russian</td>
<td>Web site in Russian, English</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Sava river crossing</td>
<td>State</td>
<td>19 July 2005</td>
<td>29 November 2005</td>
<td>134 days</td>
<td>Serbian</td>
<td>Web site in Serbian, English</td>
</tr>
<tr>
<td>Serbia and Montenegro</td>
<td>Belgrade-Nov  Sad motorway</td>
<td>State</td>
<td>20 February 2004</td>
<td>19 April 2005</td>
<td>424 days</td>
<td>Serbian</td>
<td>Hard copy only – Serbian</td>
</tr>
<tr>
<td>Ukraine</td>
<td>Odessa high voltage grid upgrade</td>
<td>State</td>
<td>9 August 2005 (Board received); 17 August 2005 (web site)</td>
<td>29 November 2005</td>
<td>112 days (105 days on web site)</td>
<td>Ukrainian</td>
<td>Web site in Ukrainian</td>
</tr>
</tbody>
</table>

Note: ‘–’ denotes projects which were not discussed by the Board in 2005.
• Odessa high voltage grid upgrade: The client released the draft EIA to the public in Ukraine and posted it on the company’s web site on 29 July 2005. Public meetings on the draft EIA were held in September 2005 in the four districts affected by the transmission line. The electronic version of the executive summary was circulated on 9 August and was posted on the Bank’s web site on 17 August. The Board therefore had the executive summary for 113 days, and the EBRD web site posted the notification 105 days before the Board meeting. The Board of Directors was notified of the timing discrepancy and was reassured that public consultation in the region had been fully compliant with the Environmental Policy.

After completion of the public consultation process, the EBRD’s Board of Directors decides whether to approve EBRD financing of a project. This is partly based on its assessment of the findings of the consultation with the local community, NGOs and other interested parties.

Sakhalin Island: consultation

During 2005 the EBRD prepared for a decision on whether to provide finance for Phase 2 of an offshore development – the world’s largest oil and gas project – on Sakhalin Island in the Russian Far East.

A specific area on the Bank’s web site (www.ebrd.com/sakhalin) provides information on all aspects of the EBRD’s potential involvement in the project. An email address is available to receive the public’s comments: sakhalinfeedback@ebrd.com

About the project

The Sakhalin Energy Investment Company is held by Shell (55 per cent) and the Japanese corporations Mitsui and Mitsubishi (25 per cent and 20 per cent respectively).

Sakhalin Energy’s €17 billion project involves the construction of a pipeline and three oil platforms. It will bring reserves from the north of Sakhalin Island to a new Liquefied Natural Gas (LNG) facility, which is being built in the south of the island. The gas will be exported to consumers in the Far East, including Japan and South Korea, and the United States.

Phase 1 of the project – offshore development – began in 1996 and has been producing oil since 1999. It was financed by the EBRD, the Overseas Private Investment Corporation and the Japan Bank for International Cooperation; each institution loaned €98 million.

Phase 2 extends the project, adding offshore facilities and pipelines that carry oil and gas to Sakhalin Island and pipelines that cross the island to an oil terminal and Russia’s first plant to produce liquefied natural gas. After Phase 2 is completed, gas and oil from the fields will be available to the market all year round.

Public consultation

Throughout the year there were many meetings, discussions and exchanges of correspondence, including discussions at the Bank’s Annual Meeting and meetings in October 2005 between the EBRD’s President and a number of NGOs. These included the World Wildlife Fund (WWF), Sakhalin Environment Watch, Pacific Environment and CEE Bankwatch. The project’s environmental and social issues are described on page 67.

After assessing information on all issues, the EBRD decided on 14 December 2005 to proceed to the public consultation phase before making a decision on whether to recommend that the Bank should finance Phase 2. Sakhalin Energy released project information into the public domain for a period of 120 days to allow public consultation to take place. On 20 December 2005 the EBRD published the executive summary of Sakhalin Energy’s Environmental Impact Assessment along with a list of venues where full documentation is available.

During the 120-day consultation period, public meetings were undertaken with communities on the island and with interested parties in London, Moscow and Sapporo, Japan. Translation into English and Russian was provided for the meetings in Russia, and into English and Japanese for the Sapporo meeting. To ensure full transparency, the transcripts of the meetings and the independent facilitator’s report have been disclosed to the public on the Bank’s web site. The EBRD is also in dialogue with national and international NGOs.
Considering the environmental and social impact

This complex project involves considerable environmental and social issues. Environmental concerns have focused on the effects of the development on the area's whales, salmon and birds. Social concerns have focused on how Sakhalin islanders – and Russia – will benefit from the revenue from the project, the proposed development plan for indigenous peoples and the establishment of a mechanism for compensating people affected by the project.

Environmental impact

The oil and gas development is close to the summer feeding grounds of the Western Gray Whale, a critically endangered species. As a result of concerns raised about the welfare of the whales, Sakhalin Energy rerouted the marine pipeline connecting the platforms to the oil processing facility in order to avoid the whales' feeding areas. The company is working with the world’s leading scientists under the auspices of the International Union of Nature Conservation. It has agreed to set up the Western Gray Whale advisory panel consisting of these experts and has agreed to abide by all reasonable recommendations that it makes to protect the species.

Sakhalin Island also has extremely important spawning grounds for a variety of salmon species. The onshore gas and oil pipelines cross 1,084 rivers, generating sediment from river crossing construction activities. The EBRD has been working with Sakhalin Energy to understand and minimise the potential impact for the salmon spawning grounds. The company has developed a river crossing strategy, which sets out commitments to ensure that there will be no net loss of salmon spawning habitats. It has also established an extensive monitoring system to assess the impact of each river crossing and to ensure proper construction techniques.

Together with the Russian authorities, Sakhalin Energy has assessed and categorised the environmental and commercial importance of each watercourse and has adapted the crossing method according to the respective importance of each river. Supervision and monitoring will take place for those crossings where there is a significant potentially adverse environmental impact. Implementation of the new river crossings strategy is being monitored by the company, independent monitors and the EBRD. The monitoring must show that implementation of the new strategy has been successful for the EBRD to be able to consider making an investment. Monitoring has continued beyond the end of the 120-day public consultation period.

Sakhalin Energy has also developed conservation measures for the Steller’s sea eagle. Measures include rerouting the pipeline to avoid critical nests and avoiding site clearance activities during sensitive bird nesting seasons.

Social impact

Local businesses are able to provide services to the fledgling oil and gas industry on the island. The project has created 17,000 jobs, mainly in construction activities. A total of €4.7 billion worth of contracts have already been awarded to Russian companies by Sakhalin Energy.

Sakhalin Energy has invested €85 million in the Sakhalin Development Plan for infrastructure upgrades, improvements to the power supply and investments in health and education. Under EBRD supervision, the company has worked with indigenous peoples in the north of the island to develop a programme that will help to preserve cultural heritage and traditional ways of life on the island.

Sakhalin Energy has also established a procedure for managing complaints and grievances arising from the performance of the project. The purpose of the procedure is to ensure that complaints are addressed in an effective and timely manner and that appropriate corrective action is identified and implemented to provide for a satisfactory conclusion to both parties.
68 Promoting transparency and accountability

Following the conclusion of the consultation on 28 April 2006 the EBRD is assessing the findings and plans to make a decision later this year. If it decides to proceed, the EBRD would need to agree an appropriate environmental and social management plan with the client.

Listening to expert advice

The Environmental Advisory Council (ENVAC) is an independent body of environmental specialists that advises the Bank on managing environmental protection and natural resources, policy development and project activities. ENVAC members come from NGOs, the private sector, academia and policy-based institutions.

ENVAC met in April and September 2005 at the Bank’s headquarters in London. Topics discussed at the April meeting included the EBRD’s Transport Policy, development of the new Energy Policy and the tourism sector. The main topics discussed at the September meeting were the EBRD’s draft Energy Policy and the application of the Bank’s Environmental Policy to the investment practices of the Bank’s capital and retirement funds.

Several members of ENVAC participated in the EBRD’s regional workshops on the new Energy Policy. ENVAC provided significant input to assist the Bank in developing the draft policy (see page 27). ENVAC members encouraged the Bank to focus more on energy efficiency – while encouraging the development of renewable energy – and include more detail on how the Bank intends to achieve its goals and implement specific policies. On affordability, ENVAC was in favour of raising tariffs to cost recovery levels in all sectors as long as measures were put in place to help people who cannot afford essential services.

ENVAC members also assisted in the preparation of the EBRD’s first Sustainability Report published in 2005. Reports of meetings with ENVAC are now available on the Bank’s web site at www.ebrd.com.

Current ENVAC members
Professor Urkhan Alakbarov (Azerbaijan): former Vice President of the Azerbaijan National Academy of Sciences
Dr Andrzej Kassenberg (Poland): President of the Institute for Sustainable Development
Professor Jacqueline McGlade (Canada and United Kingdom): Executive Director of the European Environment Agency
Professor Dr Andjelka Mihajlov (Serbia and Montenegro): formerly Serbian Minister for the Protection of Natural Resources and Environment
Professor Nicholas Robinson (United States): holder of the Gilbert and Sarah Kerlin Distinguished Chair in Environmental Law, Pace University School of Law
Dr Roustam Sagitov (Russia): Associate Professor at St Petersburg State University, Director of the Baltic Fund for Nature and Vice President of St Petersburg Naturalists Society
Mr Marko Slokar (Slovenia): President of the Environmental Fund of the Republic of Slovenia Management Board and Vice Chairman of the European Environmental Agency Management Board
Mr Achim Steiner (Germany): Executive Director of the United Nations Environment Programme (as of 15 June 2006)
Dr Jan-Olaf Willums (Norway): Chairman of Inspire
Mr Sven Hansen, Sir Crispin Tickell and Dr Nicholas Grishin retired as ENVAC members in 2005.

Handling complaints

The EBRD’s management can receive comments and complaints via any of its departments and resident offices. Often the Outreach and NGO Relations Unit will be the first point of contact for NGOs. It is able to assist by identifying and contacting the appropriate department or staff member to provide a response.
In addition, the EBRD established in July 2004 an Independent Recourse Mechanism (IRM). This is a formal and independent process for receiving complaints from local groups that claim to be adversely affected by an EBRD-financed project. The IRM, which was established to strengthen the EBRD’s accountability and the transparency of its decision making, is administered by the Chief Compliance Officer (CCO), who is independent of the EBRD’s banking operations.

When a complaint is registered by the CCO, it is assessed to determine its eligibility for a Compliance Review and whether it should be further processed towards a problem-solving initiative. Under a Compliance Review, the appointed IRM Expert assesses whether the EBRD has complied with its Environmental Policy and the provisions of the Public Information Policy. A problem-solving initiative might also be considered to restore an effective dialogue between the parties without apportioning fault or blame. This might include independent fact-finding, mediation, conciliation, dialogue facilitation, investigation or reporting.


**Complaints assessed in 2005**

IRM rules define who may make a complaint and what an affected group may make a complaint about. In 2005 the IRM received a total of four complaints. Two were registered as eligible complaints and further assessed. Two were deemed ineligible and rejected for registration because:

- the complaint referred to a matter outside the scope of the IRM
- the group making the complaint was not an affected group as defined by IRM rules.

The two eligible complaints concerned a potential EBRD investment on Sakhalin Island (see page 27) and the Bank’s 2004 investment in the Baku-Tbilisi-Ceyhan (BTC) pipeline (see page 16). For further details, see the register of complaints on the Bank’s web site (www.ebrd.com/about/irm/register).

**Sakhalin Island II, phase 2**

The affected group consists of individuals and local enterprises involved in fishing and fish processing. It alleges that construction vessels travelling to and from the gas plant and the construction of terminals restrict safe access of fishermen to their nets, causing damage to the nets and reducing the quality and quantity of fish caught in Aniva Bay.

The CCO and the appointed independent expert assessed the complaint and concluded that it did not warrant a compliance review because there was no evidence to suggest that the EBRD had contravened its Environmental Policy or Public Information Policy. Following the EBRD’s decision at the end of 2005 to declare the project fit for the purpose of consultation, the CCO is examining the feasibility of a problem-solving initiative.

Other complaints and comments regarding the project have been received by the Bank. These will be considered and responded to as part of the consultation process.

**BTC pipeline**

The complaint was received from a group of residents of Gyakh Kesemenli village in the Akstafa district of Azerbaijan. The residents allege that trucks involved in the construction of the pipeline have caused vibration damage to their property.

The CCO and the appointed independent expert assessed the complaint and concluded that there was no evidence to warrant a compliance review. The complaint was processed towards a problem-solving initiative but after further review the CCO concluded that it would be unlikely to have a positive outcome and should not be initiated. The President of the EBRD accepted the recommendation, which finalised the processing of the complaint.
Managing our internal environment

The EBRD has headquarters in London and local offices in the 27 countries where the Bank operates. In 2005 the Bank’s London-recruited staff totalled 969 people (compared with 965 in 2004) while locally hired staff in the Bank’s Resident Offices totalled 234 (compared with 237 in 2004).
Managing our internal environment

The EBRD has a responsibility to treat all staff fairly, to provide them with a safe place to work and to manage the environmental impact of our buildings and operations.

Managing our internal environment involves how we manage the environmental impact of physical resources and materials, such as our approach to energy efficiency, waste management and recycling. It also involves how we manage our human resources, such as ensuring that our staff work safely and have opportunities for continuous learning and development.

Managing our internal environment involves how we manage the environmental impact of physical resources, such as our approach to energy efficiency, and how we manage our human resources.

Working responsibly

Refurbishment of EBRD headquarters

After extensive planning and preparation, the EBRD began major engineering and refurbishment works to its London headquarters in September 2005. The works are essential to replace or upgrade ageing equipment and building systems, to meet current UK building regulations and best practice, to address health and safety issues and staff needs and to achieve energy savings and higher environmental standards.

The work involves replacing the current lighting and lighting control system as well as the building energy management system, which regulates ventilation, heating and air conditioning.

The fire detection system and its operating system will be upgraded and smoke detectors and call points replaced. Based on best practice in major financial institutions, the current single uninterruptible power supply (UPS) unit will be replaced with two UPS units in parallel, which will increase the protection of the Bank’s systems during a power failure.

The lifts will be replaced in a separate phase of the project. The new lifts will be fully compliant with the UK’s Disability Discrimination Act and result in lower maintenance costs and power consumption.

Throughout the project, the goal is to ensure that construction and refurbishment activities proceed with minimal disruption to staff and to the work of the Bank. The refurbishment is expected to be complete by mid-2007.

Setting renewable energy targets

In 2005 the EBRD’s management considered a study by the Bank’s energy consultants on the availability and cost implications of purchasing a percentage of the Bank’s energy requirements from renewable sources. A decision was taken to source at least 10 per cent of the Bank’s electricity needs from renewables for the supply contract, starting in October 2005. The Bank’s policy is to renew its supply contract yearly so that it can respond to market fluctuations. The 10 per cent target for renewables will be reviewed and may be increased if the cost is reasonable.

A decision was taken to source at least 10 per cent of the Bank’s electricity needs from renewables.
Managing our internal environment

Energy and Environment Management Working Group

Arising from discussions about sourcing energy from renewable sources, the EBRD’s management formed a multi-departmental working group to consider a range of energy and environment related issues. These include increasing the Bank’s internal energy efficiency, increasing recycling and reducing the environmental impact from the Bank’s international travel.

The group will also review how the EBRD might manage the environmental impact of its purchasing decisions by formally including environmental considerations in purchasing decisions. The working group is made up of members from the Administration Department, Environment Department, Communications Department and Staff Council. It will meet regularly and report to the Bank’s Executive Committee.

Managing sub-contractors

The EBRD outsources its cleaning and catering contracts. Both contractors have environmental policies, which include waste minimisation, energy efficiency, safe handling of chemicals and responsible sourcing of supplies. The catering contractor uses organic produce where possible and will not knowingly use ingredients containing genetically modified organisms (GMOs). Both the catering and cleaning contractors are equal opportunities employers.

In 2005 the EBRD reduced the amount of paper that we use by distributing information electronically on our internal computer network and external web site.

Paper usage

The paper used in the EBRD is sourced from sustainably managed forests. It is produced without using chlorine bleach by mills that conform to the ISO 14001 environmental management systems standard.

In 2005 the EBRD reduced the amount of paper that we use by distributing information electronically on our internal computer network (intranet) and our external web site (www.ebrd.com).

<table>
<thead>
<tr>
<th>Year</th>
<th>Tonnage</th>
<th>Million sheets</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>96</td>
<td>20.2</td>
</tr>
<tr>
<td>2002</td>
<td>90</td>
<td>18.9</td>
</tr>
<tr>
<td>2003</td>
<td>88</td>
<td>17.6</td>
</tr>
<tr>
<td>2004</td>
<td>89</td>
<td>18.2</td>
</tr>
<tr>
<td>2005</td>
<td>78.3</td>
<td>16.5</td>
</tr>
</tbody>
</table>

Recycling

The EBRD recycles used paper, light bulbs, printer and toner cartridges and glass. We use certified companies that follow the required environmental standards to dispose of obsolete IT equipment, such as computers and copy machines.

The Bank increased paper recycling by 5 tonnes in 2005, representing a rise of 21 per cent. This may be related to the office refurbishment – as people moved out of the office space to make way for the builders, out-of-date paperwork was cleared.

Glass recycling doubled in 2005. The Bank’s London headquarters includes sub-let areas and it is possible that increased glass usage by tenants contributed to this increase rather than improved efforts to recycle glass.

Toner recycling also doubled in 2005. This too is linked to the office refurbishment – as staff cleared offices for moving, they were careful to recycle old toners.
74 Managing our internal environment

**Materials recycled**
Glass and paper (tonnes)

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Glass</td>
<td>25</td>
<td>56</td>
</tr>
<tr>
<td>Paper</td>
<td>23</td>
<td>28</td>
</tr>
</tbody>
</table>

**Refrigerants**
The EBRD’s refrigerants comply with EU regulations. We employ a refrigerant recovery unit to retrieve and re-use refrigerant gas. We dispose of redundant refrigerators using licensed contractors.

**Business travel**
The EBRD’s main use of energy (apart from heating and cooling our buildings) is from travel, which is associated with carbon dioxide emissions. Business travel by air and rail is essential for our staff to carry out the Bank’s business effectively. We use video-conferencing to reduce the need to travel where possible.

The Bank encourages staff at our London headquarters to reduce car use by providing interest-free loans for season tickets for public transport. We also provide secure storage space for people who cycle to work.

**Energy and water consumption**
An independent study on energy and water usage within the Bank in 2005 concluded that:

- energy use was reduced by 4.6 per cent, saving the emission of 352 tonnes of carbon dioxide (at the power station) plus sulphur dioxide, nitrogen oxide and dust emissions (particulates)
- gas use increased by 9.6 per cent – the increase may be related to cold weather or increased activity in the kitchens
- water use increased by 7.8 per cent, with consumption up to 223.4 cubic metres a day – this is due in part to the ongoing refurbishment of the building.

To increase monitoring and management, there are plans to increase energy and water metering within the headquarters building. Metering will allow for more accurate identification of areas of high use and where energy efficiency gains could be made.

**Business travel**

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air travel (million kilometres)</td>
<td>23.7</td>
<td>28.1</td>
</tr>
<tr>
<td>Rail travel (kilometres)</td>
<td>294,200</td>
<td>308,896</td>
</tr>
<tr>
<td>CO₂ from business travel (kilo tonnes (approx.))</td>
<td>4.03</td>
<td>4.4</td>
</tr>
</tbody>
</table>

**Materials recycled**
Printer and toner cartridges (units)

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>420</td>
<td>900</td>
</tr>
</tbody>
</table>

**Energy and water consumption**

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electricity consumption (GigaWatt hours)</td>
<td>19.48</td>
<td>20.43</td>
</tr>
<tr>
<td>Gas consumption (GigaWatt hours)</td>
<td>3.254</td>
<td>2.969</td>
</tr>
<tr>
<td>Water consumption (cubic metres)</td>
<td>84,461</td>
<td>79,215</td>
</tr>
<tr>
<td>London headquarters office gross floor area (metres squared)</td>
<td>42,500</td>
<td>42,500</td>
</tr>
</tbody>
</table>

Note: Part of the EBRD’s London headquarters building is sub-let. These figures include our tenants’ consumption.
Managing our internal environment

Developing our human resources

Diversity
The EBRD recruits staff without gender, racial or religious bias. We recruit from a variety of backgrounds in our member countries to achieve a multinational and diverse workforce. At the end of 2005, a total of 54 nationalities were represented in the Bank’s workforce. Women represented 55 per cent of the total workforce, of whom 38 per cent were at professional or senior management levels at the Bank’s headquarters.

We encourage our staff to pursue opportunities within a variety of departments at Headquarters and in our local offices to experience new working environments and expand their skills. By promoting mobility within the workplace, the Bank builds greater flexibility in the workforce to meet evolving business needs.

Staff numbers

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>London headquarters</td>
<td>969</td>
<td>965</td>
</tr>
<tr>
<td>Regional offices (27 countries of operations)</td>
<td>234</td>
<td>237</td>
</tr>
<tr>
<td>Ratio of male to female professional staff</td>
<td>1.63 to 1 (approx.)</td>
<td>1.62 to 1 (approx.)</td>
</tr>
</tbody>
</table>

Staff welfare

Work-life balance
The EBRD’s work-life balance programme offers opportunities to staff to tailor how they work to their personal needs. It includes home-office working, flexible working hours, part-time working, job sharing, and parental, study and unpaid holiday arrangements.

Learning and development
Learning and development is important to individual performance and personal growth and to the success of the Bank. Mobility, formal training and on-the-job development are at the heart of the many opportunities that the Bank offers to staff to expand their competencies.

In 2005 the EBRD continued with its management development programme. Over one-third of the Bank’s managers have attended a course on the programme, which is tailored for each management level within the Bank.

Another training objective in 2005 was to raise staff awareness of the Bank’s retirement plans, which were amended last year. More than half of EBRD staff attended retirement seminars at the Bank’s London headquarters and in our regional offices.

Overall, a total of 3,657 days of training were undertaken in 2005, including integrity training. In 2006 the focus on management skills will continue with the pilot of a new executive development programme.

2005 training days

- IT: 14%
- Technical skills: 16%
- Banking skills: 8%
- Introductory programmes: 16%
- Managerial skills: 16%
- Business and personal skills: 38%
- Health and safety: 1%

EBRD Sustainability Report 2005
Managing our internal environment

Working safely
The EBRD’s health and safety policy covers staff working at our London headquarters and our Resident Offices. The Bank reviewed its health and safety programmes in 2005. Improvements were introduced to medical, insurance and retirement plans, and to travel safety arrangements for pregnant staff who travel on Bank business.

Two new online training courses were developed, covering first aid training (as a follow-up to classroom teaching) and fire evacuation procedures. These courses were delivered early in 2006, building on the successful implementation of earlier courses covering computer use and basic travel security. The Bank also began work on a new programme to improve health and safety advice to the large network of consultants who work for the Bank.

Travel safety
In undertaking the business of the EBRD, staff are required to travel extensively between our London headquarters and operating countries, and for business meetings anywhere in the world. In 2005 the Bank introduced a series of travel safety lectures to remind staff of the need to take care when travelling. This programme is continuing in 2006.

Crisis response procedures
The EBRD reviewed crisis procedures in response to the terrorist bomb attacks in London in July 2005. As a result, the Bank strengthened its crisis management procedures for major incidents, introducing an improved roll-call system to locate staff and a new enquiry line for close relatives to call.

The Bank strengthened its crisis management procedures for major incidents and introduced a new enquiry line for close relatives.

Bird flu
The EBRD developed a contingency plan covering the possible effects of a bird flu pandemic and established a working group to keep the issue under review.

No-smoking policy
In 2005 the Bank decided to end the practice of allowing smoking in specified areas. Smoking is no longer allowed in any Bank offices. The non-smoking policy came into effect at the start of 2006 (giving smokers time to adjust). A series of courses was offered in London to help staff who wanted to stop smoking.

Integrity and whistle-blowing
The EBRD’s Chief Compliance Office has overall responsibility for all matters to do with preserving integrity, including within the Bank. Recognising that whistleblowing is an important way of ensuring good governance, the Bank published a Whistleblower Protection Statement on its web site in 2005. Publication is designed to encourage employees to disclose information that may not otherwise be discovered.

The statement confirms the EBRD’s commitment to maintaining a working environment that protects employees who report suspected misconduct. This is defined as an “intentional or negligent failure” by an employee to observe the rules of conduct or standards of behaviour prescribed by the EBRD.

An employee who reports suspected misconduct and discloses information to the CCO in good faith will be protected by the EBRD from “pressure, retaliation or reprisal” in connection with this cooperation.

Staff representation
The EBRD’s Staff Council promotes the rights, interests and welfare of staff. The Bank’s management works with the Council on all issues relating to the welfare of the Bank’s employees, such as working safely and retirement arrangements and benefits.
Representatives on the Staff Council are elected by fellow staff and represent various professional and support levels within the Bank and the Resident Offices. In 2005 the Council provided input on the refurbishment of the Bank’s London headquarters, the new non-smoking policy and revised pensions arrangements.

Retirement arrangements and benefits
In 2005 the EBRD improved its staff retirement plans. These are overseen by the EBRD’s Retirement Plan Committee, which retains specialist advisers selected from industry leaders to administer the plans, to provide investment advice and to ensure prudent and responsible management of the plans’ funds. As with the Bank’s Treasury operations, there are currently no specific social or environmental investment criteria. However, the Bank will investigate options for including a sustainability investment option as part of the Bank’s Money Purchase Plan in 2006.

Grievance and appeals
The EBRD is an international organisation with a number of privileges and immunities. In employment disputes, this includes immunity from the jurisdiction of the employment tribunals and courts of the member states of the Bank. To give employees a substitute independent process in which to air their employment-related concerns, the Bank has implemented a three-stage grievance resolution system through its Grievance and Appeals Procedures.

The final stage of appeal is to the EBRD Administrative Tribunal, which constitutes a “quasi-judicial” forum for review of the administrative decision that forms the basis of an employee’s grievance. The President of the Administrative Tribunal must be a person of high competence in the legal field from outside the Bank.

In 2005 the EBRD improved its staff retirement plans, which are administered by specialist advisers.

Dispute resolution
Ombudsman
The EBRD has appointed an independent Ombudsman whose main role is to provide an advisory service for all staff on personnel-related issues. The service is completely confidential and can include advice for staff members on how to resolve issues as well as intervention to help all parties reach a satisfactory agreement.

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- HR2: Consideration of human rights as part of investment and procurement decisions
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- HR6: Policy and procedures on preventing child labour
- HR7: Policy on preventing forced labour

**Additional guidelines**

- HR8: Employee training on human rights policies
- HR12: Policy to address needs of indigenous people

**Society**

**Core guidelines**

- SO1: Policy to manage impact on people affected by activities
- SO2: Policy to manage bribery and corruption
- SO3: Policy for managing political lobbying

**Product Responsibility**

**Core guidelines**

- PR1: Policy for preserving customer health and safety
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- PR3: Policy for customer privacy

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**Social Performance Indicators Corporate Social Responsibility (CSR) Management**

- CSR1: Description of social elements of CSR policy
- CSR2: CSR responsibilities within organisation
- CSR3: Number of CSR audits
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- INT1: Social responsibility aspects of HR policy
- INT2: Staff turnover and job creation
- INT3: Employee satisfaction
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- INT7: Employee profile per hierarchy level

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- SUP1: Screening of major suppliers
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- RB1: Retail banking policy
- RB2: Lending profile
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- See note 2

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- F1: Environmental policies applied to core business lines
- F2: Procedures for assessing and screening environmental risks
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**KEY**

- BC: Back cover
- AR: Annual Report
- TR: Transition Report
- SR04: Sustainability Report 2004

**Note 1**

- Not applicable to Banks generally

**Note 2**

- Not applicable because the EBRD is an International Financial Institution
- Not currently covered by the Bank’s reports

**EBRD Sustainability Report 2005**
80 Annex: organisation and procedures

This annex gives additional information about responsibilities, organisation and procedures within the EBRD.

Responsibility for sustainability management

The Environmental Policy and other EBRD policies, country strategies and the Bank’s budget are approved by the EBRD’s Board of Directors.

All projects submitted for approval to the EBRD’s Board of Directors include a summary of the environmental and social issues associated with the project and how these will be addressed to ensure that the objectives of the Environmental Policy are achieved.

Responsibility for implementing the Bank’s mandate lies with the Executive Committee. It comprises: the President; the Chief Economist; the First Vice President, Banking; the General Counsel; the Secretary General; the Vice President, Finance; the Vice President, Human Resources and Administration; and the Vice President, Risk Management. Prime responsibility for environmental matters lies with the Risk Management Vice Presidency and its Environment Department.

The Vice President, Human Resources and Administration, is primarily responsible for health and safety aspects relating to Bank staff, human resources management and the management of the Bank’s premises and transport. Senior management within the Banking Vice Presidency ensure that environmental issues are taken into consideration in project preparation and implementation and in the preparation of country strategies and sector policies.

Project approval

All potential EBRD projects are reviewed by the Bank’s Operations Committee, which is chaired by the First Vice President, Banking. The Committee comprises: the Vice President and Director of Risk Management; the Vice President, Finance; the General Counsel; the Chief Economist; and a Business Group Director from Banking.

The Operations Committee approval process is normally based on a Concept Review and a Final Review before a project is submitted to the Board of Directors for approval. After a project has been approved and signed by the EBRD Board, with financing fully or partially disbursed, the Committee remains involved by approving material changes to the project.

Project derogations

A derogation is when the EBRD’s Board of Directors decides that it is prepared to waive a condition of the Bank’s Environmental Policy. If in any project going before the Board there are areas where full compliance with our policy has not been reached, it will be flagged to our Board before their decision-making session as a potential derogation from our policy. The Board considers derogations from our environmental policy as extremely serious and the intention is that all projects should comply fully.

Environmental and social monitoring mechanisms

The environmental performance of all active projects in the Bank’s portfolio is monitored in the following ways:

• weekly review of projects by the Portfolio Review Committee, which meets up to four times a year
• review of annual environmental reports submitted to the Bank by project sponsors
• periodic third-party audits of projects in environmentally sensitive sectors
• project visits by EBRD staff.

Harmonising standards

In our general consultation with stakeholders we include international financial institutions (IFIs) and environmental bodies. To help develop a consistent approach to environmental issues among IFIs we participate in the Multilateral Financial Institutions Environmental Working Group and the Development Financing Institutions Social Issues Working Group. Part of this relationship is the harmonising of standards and approach. We are also in regular dialogue with the UN Environment Programme’s Financial Institutions Initiative that promotes sustainability in the financial community.

Financial reporting

Treasury Risk Management is responsible for identifying, controlling and managing risks incurred by Treasury.

The EBRD has adopted the “Internal Control – Integrated Framework” to certify internal controls over external financial reporting. The framework was issued by the Committee of Sponsoring Organisations of the Treadway Commission (COSO), has been adopted by other international financial institutions and represents the broadest international best practice.

COSO & Operational Risk Management is responsible for coordinating and developing operational risk Bank wide (reporting to Risk Management). It also manages the Bank’s certification process over internal controls on financial reporting (reporting to Finance).

Capital market investments

The EBRD’s Treasury department undertakes capital market investments for the Bank. Environmental or social criteria are not explicit investment parameters but form part of the investment decision. The average rating of the portfolio is Aa/ A or better: over 75 per cent of the investment exposures are to regulated financial industries with the remainder largely invested in AAA/Aaa assets.

Treasury’s credit parameters allow investment in sovereign and sovereign-guaranteed paper with a minimum rating of A-/A3. In accordance with these parameters, limits have been established for 22 countries, all of which are members of the Financial Action Task Force (FATF), an intergovernmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing.

Retirement Plan Committee for EBRD staff

The EBRD’s Retirement Plan Committee oversees the retirement arrangements and benefits for EBRD staff. It is made up of: two elected staff members; the President; the Vice President, Finance; the Secretary General; the Vice President, Human Resources and Administration; the General Counsel; and two representatives of the Board of Directors.
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Working towards a sustainable future

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