

## **Environmental Advisory Council of the European Bank (ENVAC)**

**Meeting in London, 28 September 2005**

### **Meeting Summary**

The Environmental Advisory Council of the European Bank for Reconstruction and Development (EBRD or “the Bank”) met in London on 28 September 2005. The morning sessions were chaired by Vice-President Fabrizio Saccomanni and the afternoon session was chaired by President Jean Lemierre. Representatives of the EBRD Board of Directors for the constituencies of Canada, the Czech Republic/Hungary/Slovakia/Croatia, the EC France, Italy, Japan, Spain, the UK, and the USA, observed the meeting. Representatives of EBRD management and the Executive Committee of the Bank also observed the meeting and the ENVAC members’ summary during the final session. The ENVAC meeting focused primarily on the draft Energy Policy, which is currently under revision. This document comprises a concise summary of the ENVAC meeting, from the notes of the Secretariat, and has been commented on by ENVAC members to ensure it reflects the discussion. It should be noted that ENVAC is a body of individual members, and the summary does not mean to imply that all members had a uniform opinion of an issue raised.

	<b>Topic</b>	<b>Background Documents</b>
	<b>Introduction and Welcome of New Members</b>	<ul style="list-style-type: none"><li>• Brief biographies</li></ul>
<b>1.</b>	<b>EBRD Investments of Capital and Retirement Funds</b>	None.
<b>2.</b>	<b>EBRD Draft Energy Policy</b>	<ul style="list-style-type: none"><li>• Draft Energy Policy (Aug. 05)</li><li>• Written comments from ENVAC members received prior to the meeting.</li><li>• Background paper provided by IUCN.</li></ul>
<b>3.</b>	<b>Summary of ENVAC Comments</b>	

### **Introduction**

Fabrizio Saccomanni, Vice President of Risk Management, opened the meeting and welcomed the Council. As in the previous meeting, the format of the ENVAC meeting was a number of sessions, with the President chairing the afternoon session, and culminating in a summary by ENVAC members of the key issues and comments made in the meeting on each topic.

Mr Saccomanni welcomed the five new members of the Council and introduced them.

- Professor Jacqueline McGlade (Canada/United Kingdom), Executive Director of the European Environment Agency;
- Professor Dr Andjelka Mihajlov (Serbia and Montenegro), former Serbian Minister for the Protection of Natural Resources and the Environment;
- Professor Nicholas A Robinson (United States), Pace University School of Law, working on environmental law issues in the Bank’s region for over 30 years;

- Dr Roustam Sagitov (Russia), Director of the Baltic Fund for Nature (BFN) in St Petersburg; and
- Mr Marko Slokar (Slovenia), President of the Management Board of the Environmental Fund of the Republic of Slovenia.

## **Session One: EBRD Investments of Capital and Retirement Funds**

### Bank Staff:

Axel van Nederveen, EBRD Treasurer

Steven Kaempfer, Vice-President Finance, Acting First Vice-President

At the previous ENVAC meeting (4 April 2005), ENVAC members requested that the next meeting of the Council include the topic of EBRD investments of capital and retirement funds. Given that the EBRD Environmental Mandate states that EBRD will “promote in the full range of its activities environmentally sound and sustainable development,” they wanted to know how the Bank’s commitment to environment and sustainable development were taken into account in 1) the investment of funds that have not yet been allocated to projects and 2) the retirement plan funds of the Bank’s employees.

The EBRD Treasurer, Axel van Nederveen gave an introductory presentation on function of the Treasury Department and the governance the Bank works under. The Financial Policies and Treasury Risk Management Authority and Guidelines were outlined, as well as the Bank’s Liquidity Policy. The Treasurer explained the extensive system of independent checks and balances that apply to Treasury Operations.

With regard to investments, the Bank’s Treasury Function is designed to manage risk so that the necessary funding and liquidity support for the Bank’s overall activities are consistent with the Bank’s objectives and earn an appropriate return on capital, reserves, and borrowed funds. A conservative approach is held, by investing in assets in developed markets at the upper end of the investment grade, resulting in a treasury portfolio with a high credit rating, primarily in banks, residential mortgages in selected countries, commercial bank properties and other low risk investments. At any time, investment funds are in the range of €10 billion.

Approximately 55% of the investment banks are signatories of the Global Compact (<http://www.unglobalcompact.org>) or the Equator Principles (<http://www.equator-principles.com>). There is an assumption that these signatories to the Global Compact or Equator Principles will be in line with international standards for environment and social issues.

With regard to staff retirement plans, the funds are relatively small. The Final Salary Plan is only invested by the EBRD. The Money Purchase Plan provides investment by both the Bank and Staff, and staff select an appropriate mix of money market, equity, or bonds in which they wish their funds to be invested. Equity investments are in index funds only. There is no sub-selection of companies or choices beyond a number of country or regional selections (e.g., UK equities, European equities).

### **ENVAC Comments**

ENVAC members welcomed the summary and asked for clarifications as to what extent the Bank’s environmental mandate was taken into account in the investments. They questioned why no exclusion criteria was used in decision making with regard to index

funds and asked how the EBRD reviewed the investment banks who had signed the Global Compact or Equator Principles to see their implementation record.

Several ENVAC members suggested that the Treasury Department engage a (SRI) Social Responsibility expert to review the portfolio and assist in the risk evaluation process. They highlighted that Standard & Poors and others are including non-credit criteria to their risk rating to give a more holistic view. Another example was given of a study Societe Generale is doing on extra-banking criteria, which will soon be completed.

The Bank was encouraged to look at the Norwegian Petroleum Fund and other funds, where special committees set strict guidelines on the investments to exclude certain types of companies from the portfolio, such as defence and tobacco companies. There is also an opportunity to proactively invest in cleaner technologies, such as wind farms.

One ENVAC member pointed out that Bank staff should be made aware of how their retirement funds are being invested and the principles that the investments meet and any restrictions.

### **Response from Staff**

The Treasurer emphasized the risk of the Bank's region of operations and that it was necessary to have very strict risk management guidelines to limit the Bank's exposure to additional risk. He explained that the Bank's Treasury funds were not active investments in companies, but only invested in index funds. The Bank has not looked at engaging SRI consultants; however the investments are made in heavily regulated industries. ENVAC was advised that the Treasury Department needs to limit risk and maximise the financial strength of the Bank, and that while SRI principles are acknowledged to be part of the modern world, these issues may not be completely compatible with the remit of the Treasury Department.

For the time being, for the sake of efficiency, the selections for retirement funds were limited; however if there was a groundswell of demand from staff for additional choices taking SRI characteristics into account, the Bank would need to look at this. Treasury highlighted recent training programmes for Bank staff on retirement funds, which did not go into this level of detail; however, only a few questions were raised by staff on the categories of index funds and criteria for investment.

### **Response from ENVAC**

ENVAC members cautioned about reliance on heavily regulated industries, citing the vast difference between companies in high risk sectors. They also stated the willingness of some banks to sign the Equator Principles without adequate resources for implementation, and the need for the Bank to review their annual sustainability reports to see if their commitments were being implemented. They stated that even a small investment in SRI would be seen as a big step forward, without compromising on principles. The minimal level of assurance would be a negative screening for sectors such as tobacco and defence.

ENVAC members asked for this topic to be back on the agenda in 6 to 12 months to review steps taken. In the first instance, ENVAC members agreed to write a discussion paper on issues and to provide examples of funds and institutions which had taken positive steps in the area of SRI commitments, while protecting the risk profile of the institution.

## **Session Two: EBRD Draft Energy Policy**

### Bank Staff:

Peter Reiniger, Energy Business Group Director

Tony Marsh, Director, Power & Energy

Vince Novak, Director, Nuclear Safety

Jacquelin Ligot, Director, Energy Efficiency

Bert van der Toorn, Deputy Director, Natural Resources

Peter Hobson, Senior Banker, Energy Efficiency

Louis Borgo, Senior Banker, Power & Energy Team

At the April 2005 ENVAC meeting, members requested that they be able to comment on a draft of the Energy Policy prior to it being released for public review. They were sent an early draft of the Energy Policy during summer 2005. A number of the members provided detailed written comments, which were circulated to all members, and to the Bank staff working on the Policy revision.

Peter Reiniger, the EBRD Energy Business Group Director, gave a brief presentation on some of the main themes driving the Policy revision, such as the evolving best international practice, issues of climate change, transparency, and the World Bank Extractive Industries Review. In addition, the EBRD wanted to make a more comprehensive policy, combining Energy, Energy Efficiency, Nuclear Safety and Natural Resources. Two studies were commissioned by external experts.

Existing elements were strengthened, such as the need for regional cooperation between smaller countries, an increased focus on CIS countries and SEE where the need is the greatest, to prioritise the private sector, to finance the sovereign sector where it will encourage commercialisation of state companies, and to increase the use of equity to attract greater private sector interest.

The new initiatives are the emphasis on sustainability and governance, targets for renewables, and energy efficiency, and in the extractive industries, to require project sponsors to adhere to the Extractive Industries Transparency Initiative, enhance environmental performance, and to provide benefits to local stakeholders, such as Small and Medium-sized Enterprises and municipal services. In the nuclear sector, the draft policy looks at nuclear safety and waste disposal, with no concurrent links to closure of existing power plants.

The Energy Efficiency Team gave a brief presentation on their work on Energy Efficiency in the region, including a description of due diligence on the Bank's portfolio to look for energy efficiency opportunities, and to provide grant-funded energy efficiency audits, as well as develop projects to provide finance for energy efficiency through financial intermediaries (energy service companies—ESCOs).

The Bank noted the four main areas of written ENVAC comments related to demand-side management, energy efficiency and renewables, capacity-building of legal and institutional frameworks in the region, and evaluating externalities in project economic analyses.

Peter Reiniger concluded that the draft Energy Policy is a work in progress and that the Bank needs to be responsive to shifting priorities. ENVAC comments and comments from the Board of Directors' Policy Committee will be taken into account in a revised draft, which will be put on the Bank's website ([www.ebrd.com](http://www.ebrd.com)) for 45 day public review, in accordance with the requirements in the EBRD Public Information Policy.

The results of the public consultation will be reported to the Board of Directors with the final version of the Policy for their consideration and approval.

The President put forward the key questions of global warming, the price of oil (which to some countries will have more of an impact than debt relief), and the amount of activity in energy efficiency projects. The largest political issue was said to be how to encourage countries in the Bank's region of operations to move energy efficiency to a high priority. Right now, while donors are interested in initiatives, and the Bank is interested in projects, it can still be extremely difficult to convince countries that are below Kyoto levels that they need to take any action to reduce energy waste. The Bank should look for opportunities to work more closely with the EU and others on capacity-building.

### **ENVAC Comments**

ENVAC members congratulated the Bank on the progress from the old Energy and Natural Resources policies, and considered them to be a significant step forward.

They thought it was a good start, but generally thought the draft read too much like a report, and not like an operational policy. The draft needed strengthening in implementation and evaluation guidelines. As an operational policy, it should clearly show how it will be implemented and evaluated. They recommended it be very concise and contain a mission statement, strategic goals and principles, and operational guidelines, and move all of the information about projects to annexes. It should send a clear message from the Bank, show how to calculate costs of energy, and incorporate the issues of job creation and sustainable competitiveness, which are currently missing. ENVAC members wanted to see a stronger link between the Environmental Policy and the Energy Policy. The members welcomed the increased attention to energy efficiency and renewable energy, and suggested that the document reflect more of the Bank's work in energy efficiency, in particular.

One ENVAC member thought the draft policy seemed to be more qualitative in nature, and suggested staff look at ways to make it more quantitative. The Bank was also encouraged to show new initiatives in the policy, including new types of projects, approaches, and objectives that would clearly delineate EBRD's role in energy in the region. It should show an innovative Bank, which has bold new ideas.

The Bank was encouraged to strengthen the links between energy and biodiversity impacts, which can be significant, and are not adequately addressed in the current draft.

The Bank was told that the area of Energy Efficiency was central to its activities and the opportunities in the region, particularly in industrial energy efficiency, needed to be more clear throughout the document. A number of ENVAC members thought that the Bank has had an important impact in energy efficiency, particularly the inclusion of this as a criterion in project appraisal, and that this proactive approach is not yet reflected in the paper. ENVAC members generally thought that Energy Efficiency should be one of the primary principles of the Energy Policy, not just a sub-section. The concern was that even the work the Bank is currently doing in evaluating each project for energy efficiency potential, is not currently conveyed in the draft. The energy efficiency (EE) and demand-side management (DSM) tools that the Bank builds into the projects will be value-added, even after the Bank has left the project. ENVAC members thought that there were few areas that EBRD can influence more than energy efficiency in the region—and the role of EBRD in this area needs to focus strongly in the policy.

ENVAC members raised the issue of affordability of energy in the region and its affect on the public, and in particular on the general public. The way consumers are affected should be factored into the evaluation. It was unclear, in practical terms, how the Bank would factor in externalities, and since the Energy Policy was an operational policy, this should be more clear.

- How will the Bank's benchmarking fit with EU schemes, such as the Eco-Management and Audit Scheme (EMAS)?
- How best available techniques (BAT) would be determined?
- What is the biggest risk to implementation of the Energy Policy?
- Why is climate change the only global issue mentioned in the draft policy?
- The need for country and regional-specific strategic environmental assessments on energy should be recognised.
- How will the issue of environmental contamination during privatisation be incorporated into energy projects, which are known for legacy issues?

More information was requested on how the Bank intends to influence policy and undertake capacity-building in the region. Capacity building and policy dialogue on renewables, was seen to be very important by some members, and examples, such as Germany and Spain were used to illustrate possible approaches.

The EBRD Sustainability Report was mentioned with reference to internal energy consumption, and that the milage of Bank travel, energy use, paper use, and other indicators seemed to be going in the wrong direction, and that the Bank should be looking at energy efficiency in its own operations. Examples were given in other organisations where a fee is charged to offset travel impacts, and this should be considered by management when authorising travel.

A number of editorial comments and suggested reorganisation comments were also made.

### **Response from Staff**

The President remarked that the draft Policy was long, but contained a balance of issues. He agreed that it needed to convey a clearer message on the Bank's commitment to Energy Efficiency. He talked about the importance and sensitivity of energy issues to the political dynamics of the region of the Bank's operations, and agreed that the Bank needed to collaborate with ENVAC members on some of the ideas raised in the discussion, where their expertise would be helpful.

Bank staff agreed that there needed to be a clear statement in the Policy that energy efficiency and demand side management were as important as supply side initiatives.

The Bank stated that the biggest risk to implementation of the Energy Policy was likely to be affordability and tariff reform, establishing the appropriate regulatory framework. Analytically, dealing with externalities is extremely challenging. While it has been done academically, the Bank looks at setting the economic standard at the same level as the cost of meeting the international standards—and that these costs are taken into account in the project assessment. This is a pragmatic approach, and the Bank uses international environmental and safety standards as its benchmark. There is, however, a big loophole in that CO<sub>2</sub> is not regulated. Increasingly the Bank is able to look at the carbon market for projects; however, this is applicable only to particular projects, not horizontally across projects.

The Bank summarised its additionality in energy projects as legal conditionality, the international standard of EBRD's Environmental Policy and Procedures, the transparency of the process, including public consultation before decision-making, and strict requirements on governance, as well as initiatives, such as the Extractive Industry Transparency Initiatives. It also can take on additional risk with equity investments, which are increasingly important in the energy sector. The Bank also has the capacity to accompany major projects with clustering activities, such as regional development.

The Bank noted that with regard to its own energy use and transport impacts, that the shift in Bank operations to countries further east, along with greater need for hands-on capacity building would likely require more trips, rather than less.

Bank management reminded ENVAC that there were differing views from the Bank's shareholders about the role of the Bank in energy in the region, and that these would need to be at the Board meeting on the Energy Policy.

The President agreed that the draft Energy Policy needed to convey a clearer message on the Bank's commitment to energy efficiency. He agreed to continue discussions with ENVAC members on relevant topics, such as identifying the "cost of inaction" if countries do not increase their energy efficiency. He also expressed his concerns about the availability of technical cooperation funds to accomplish many of the necessary initiatives and wanted to continue discussions on this topic as well.

## **Response from ENVAC**

One ENVAC member stated that the best way to convince countries of the importance of energy efficiency would be to do calculations and model the implications of not addressing the issue. The Bank should put credible numbers on the table and show what the cost is of not addressing the issues—Calculate the cost of inaction. Policy instruments and elections get triggered by certain thresholds, and if impacts are seen to be high enough, they trigger action. The big issues of demography, climate change, and urbanisation needs to be factored into the equations. The demographic trend toward populations leaving rural areas and moving toward urban areas was seen to stress energy needs, and to also add to unemployment problems in urban areas. A clear message needs to be sent that unless we go for a low carbon energy supply, by 2020, there will be brown-outs in the region. Energy efficiency can mean, not only long term sustainability, but is also job-intensive when compared to most supply side energy projects. Jobs, money, and a safe and reliable energy supply are all good motivators for politicians. Energy efficiency needs to be presented as modernisation, as progress, as jobs. The Bank should look at examples in other countries that might help the Bank's region to become more efficient and less dependent such as Iceland, where communities are working on developing their geothermal energy sources to become less energy-dependent.

The Bank was cautioned not to look at projects one by one, or incrementally, it could find itself in an unsustainable pattern. The Bank was also warned that impacts of one project could negate the benefits of another, or affect another area, such as biodiversity. The EBRD should take a long-term view.

The Bank was urged to look at rural energy needs, to strengthen the text on biomass, and to include more on opportunities for public-private partnerships. The management were encouraged to add more staff with specific capacity in different renewables, and to look at the staffing of the various departments.

One ENVAC member suggested that the Bank look at the new Chinese law on renewables, which had simple principles that might have some value for the Bank's region, as none of the Bank's countries of operation have addressed the energy problems in legislation.

ENVAC members thought that the calculation of externalities used by the Bank was too simplistic, and that while it might calculate environmental upgrades, it would not look at health impacts or other issues that are linked to energy uses. Several ENVAC members urged the Bank to look at the use of subsidies, which were considered to be non-sustainable, and not just in the energy area, but agribusiness, transport, and other sectors that rely on energy. As long as subsidies are being used in the traditional fuel areas, there would be little chance for renewables and energy efficiency projects to flourish.

It was noted that the difference between countries in the region is very significant, and that the Bank should have its principles in the Energy Policy, and then apply them in regional or country studies, perhaps within the Country Strategies.

Two ENVAC members wanted a clear commitment from the Bank that it would only do nuclear safety projects and decommissioning projects, and that it would not consider any projects involving the creation of new nuclear power capacity.