

Corporate Environmental & Social Due Diligence

EPS Restructuring Project, Serbia

Draft Non-Technical Summary

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ERM GmbH
Environmental
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Environmental and Social Assessment
EPS RESTRUCTURING, SERBIA



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Non-Technical Summary

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Neu-Isenburg, 24 July 2015

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1 INTRODUCTION

1.1 PURPOSE OF THE ASSESSMENT

ERM was contracted by the European Bank for Reconstruction and Development (“EBRD” or the “Bank”) to conduct a corporate environmental and social assessment of the Serbian company, Public Enterprise Elektroprivreda Srbije (EPS). EPS is a state-owned electric utility power company in Serbia which is engaged in lignite mining, thermal power plants, hydropower projects and power distribution. *Figure 1* gives an overview of EPS’s current operations in Serbia.

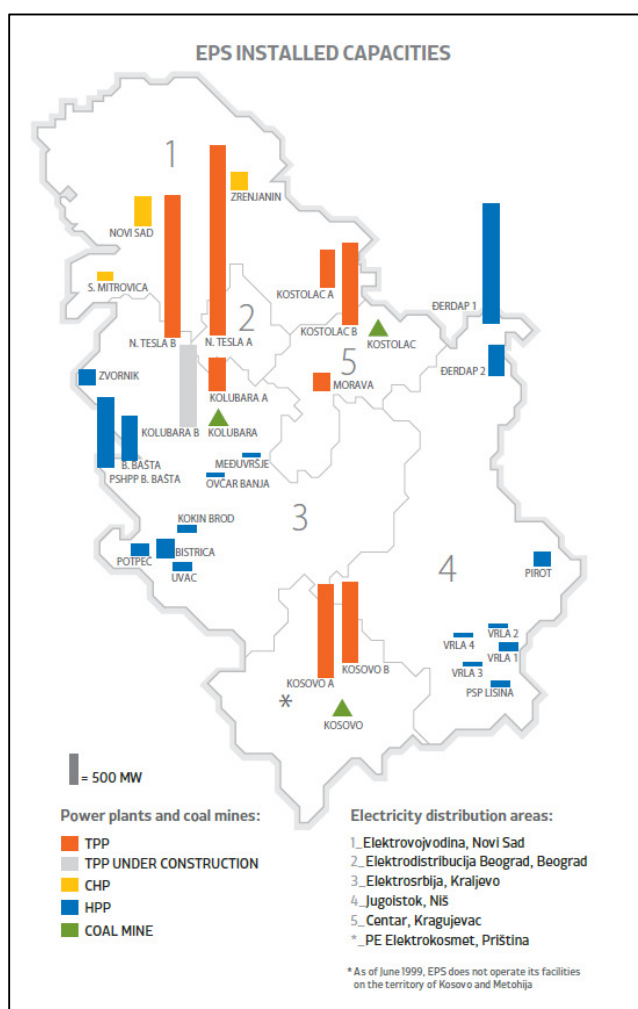


Figure 1 Overview of EPS operations (Source: EPS Technical Report 2014)

EBRD is considering providing up to EUR 200 million in sovereign guaranteed loans to EPS. The EBRD investment will be conditional upon an

agreed plan for the restructuring of EPS (the “EPS Restructuring Project”). This reform package sets clear milestone for restructuring and reorganization for the purpose of clear legal, organizational and financial division between activities that are of general interest and market energy activities, as well as the change of legal form into joint-stock company, in order to ensure full compliance of Serbian energy sector with EU directives

The Project is categorised “B” in accordance with EBRD Environmental and Social Policy (2014). Due to the general corporate finance nature of the proposed project and the EPS’s multi-site operations, a corporate Environmental and Social Assessment (ESA) of the EPS’s current environmental and social management systems, operations and assets/facilities was conducted by ERM with the local partner ENVICO d.o.o.

As part of the ESA, a review of key documents and a site visit to the EPS Headquarters and two EPS subsidiaries was conducted between June 1 and 3, 2015 to understand the currently implemented management system and the planned restructuring as well as environmental and social risks associated with EPS activities, especially the Kolubara mine and the thermal power plant Kostolac B. Interviews with site management, Non-Governmental Organizations (*CEKOR – Centre for Ecology and Sustainable Development*, and *Serbian Centre for Ecology*) and local population were conducted (June 1 – 3, June 18 and July 15, 2015).

Based on the results of the corporate ESA, ERM prepared an EPS Corporate Environment and Social Due Diligence (ESDD) Report, Environmental and Social Action Plan (ESAP), and a Stakeholder Engagement Plan (SEP). This Non-Technical Summary (NTS) summarizes the main findings of the corporate ESA and describes next steps and crucial actions to improve EPS’ environmental, social and Health & Safety performance in the scope of the EPS Restructuring Project.

1.2

BACKGROUND EPS RESTRUCTURING PROJECT

The EPS Restructuring Project is currently on-going. The 13 subsidiary companies will be merged as of July 1, 2015, to form three new companies (NewCo’s), including (i) a company comprising the headquarters and all

production sites, (ii) a distribution company, and (iii) a supplier company for energy¹.

NewCo's	Activities
(i) Headquarters & Production Company	<p>Installed generation capacity of approx. 8 GW, of which 55% is coal-fired, 40% hydropower and 5% fuel and gas-fired combined heat and power generation:</p> <ul style="list-style-type: none"> • Hydro power plants (Djerdap, Drinsko-Limske, Vlasinske); • Thermal power plants - coal, heating oil, natural gas (Nikola Tesla, Kolubara, Morava, Kostolac); • Combined heat and power plants (CHP - Novi Sad, Zrenjanin, Sremska Mitrovica); and • Small hydropower plants. <p>Operation of two open pit lignite basins, Kolubara and Kostolac, which produce approx. 38 Mio tonnes per annum (79% at Kolubara and 21% at Kostolac). Kolubara is located approx. 60 km south of Belgrade) and Kostolac is located approx. 90 km southeast of Belgrade.</p>
(ii) Distribution Company	Distribution of electricity
(iii) Supplier Company	Supply of electricity to the end consumers and public supply.

Since 2001, EBRD has made five investments with EPS and its various subsidiaries to upgrade thermal and hydro generation, improve mining efficiency and introduce smart meters. The company faces a number of environmental and social challenges, including those associated with aging and inefficient thermal power plants, future applicable compliance requirements from European regulations and the management of an on-going land acquisition and resettlement programme at the Kolubara mine.

EPS activities, and EBRD's association with them, have been subject to criticism from local and international civil society organisations. One reason for those issues is considered the EPS structure and weaknesses in the corporate environmental and social management systems (ESMS). The ESMS is currently decentralised – each of the currently existing 13 subsidiaries is running its own management system, with minor support from a small

¹At the moment of preparing ERM report, the organization of three new companies was not finally agreed. It is understood by ERM that after the merger there will be three separate new companies with several sites. ERM assumed that, there would be corporate functions with responsibilities for all three NewCo's. ERM therefore refers in this Non-Technical Summary to Corporate, NewCo or Site Level as applicable.

environmental, health & safety (EHS) department on corporate level. EPS subsidiaries have implemented integrated management systems for Quality, Environmental and Health & Safety (QEHS) issues in line with ISO 9001, ISO 14001, and OSHAS 18001. Each site has nominated a number of employees responsible for environmental issues (between approximately 1-20 employees per site) and health & safety issues (approximately 10-50 employees per site).

The EHS department on corporate level comprised a total of 14 employees including two health & safety experts. In addition to the EHS department there are 9 employees responsible on corporate level for the ESMS and review of the integrated management systems at the several sites.

2 *ESA FINDINGS*

The ESDD Report identifies gaps between EPS' ESMS and EBRD's performance requirements. Based on the ESDD Report the ESAP defines actions to be implemented in the EPS Restructuring Project to improve performance related to environmental, social and Health & Safety, including a suitable QEHS management system. The Corporate SEP includes stakeholder engagement activities and describes the internal and external grievance procedure. A summary of these reports with main findings, defined corrective actions and expected impacts from the EPS Restructuring Project on the ecological and social environment is given below.

2.1 *SUMMARY OF ESDD REPORT AND ESAP*

The EPS Restructuring Project itself is considered to only have limited direct impacts on environmental and social aspects. However, there are a number of indirect impacts to be expected from the restructuring process which are outlined below together with the actions defined in the ESAP.

Management System

To improve the environmental, social, Health & Safety management of EPS an integrated QEHS management system at corporate, NewCo and site level will be implemented. EPS will ensure that adequate and robust structures are established, resources are provided and clear responsibilities are defined for future management of environmental and social issues relevant for the production and administrative activities of EPS. EHS departments both at NewCo level and at corporate level, with sufficient employee capacities and clearly defined responsibilities and reporting lines will be established. A management team has already been formed for the implementation of the

QEHS management system. The team is currently collecting information from the sites and is compiling a management handbook on corporate level with related procedures, which should be established on NewCo level by November 2015. The capacity of this management system team appears to be adequate. If required, additional management system managers from site level may be added to the team to manage the development and implementation at all levels. EPS expects that a transmission period of three to five years will be required to get all site specific management systems that are currently in use transferred to one integrated system at corporate and NewCo level.

Labour and Working Conditions

Details regarding potential changes of employment rates, conditions and contracts, as well as regarding any need for retrenchment measures are not yet clear, as the merger of the existing subsidiary companies to form the three NewCo's started recently, on July 1, 2015. It is assumed by EPS management that it will take at least 12 months to evaluate the need for retrenchment. Based on this evaluation, EPS will (if required) develop a retrenchment program together with the worker unions and the authorities in line with the legal requirements.

In general the working conditions at EPS will be improved by implementing a list of corrective measures including human resources policy, procedures for contractor management, an internal grievance procedure and ensuring freedom for workers unions.

Health and Safety

EPS has recently contracted building material manufacturing company *Lafarge* to provide external H&S training to reduce the accident rates. The first step started in early 2015 with top management training to raise H&S awareness. Subsequently, training of trainers will be performed at operational and management level. The overall focus of the training is to increase awareness regarding relevant H&S issues at the several sites and to establish an overall pro-active management of H&S issues to prevent future serious accidents at the sites.

The public health institute and other authorized institutions perform ambient air monitoring in the proximity of mining sites and power plants, as public health issues are the responsibility of the government. EPS does not get formal feedback from ambient air monitoring campaigns so far but will ask for this in the future to apply corrective actions if required.

Environment/ Resource Efficiency

The new QEHS management system aims at managing the environmental impacts from the EPS activities. Special consideration in this regard will be given to the mining sites and the power plants. EPS will ensure that the EU BREF requirements¹ will be met in the future and air emissions from the power plants are reduced. Responsible persons will be defined, resources allocated and databases implemented to manage environmental topics more efficiently, such as waste management, wastewater management, emission control and saving resources. Also procedures for management of biodiversity aspects and living natural resources will be implemented to protect flora and fauna from impacts through EPS activities.

Social

Interviews were performed as part of this ESA with residents and NGO's in the vicinity of the Kolubara open cast mine, including people who have been subject to resettlement requirements. The results of the interviews showed that in some cases the process of expropriation is lacking comprehensive transparency. In addition, it appeared that interviewees were mainly not familiar with existing grievance procedures, and were often not satisfied with the expropriation and compensation process, and it was partly claimed that there is no credible dialog established between EPS, local communities and affected residents.

EPS will evaluate their procedures for the communication with communities and affected residents and their existing grievance procedures in order to improve the existing procedures to a more transparent and pro-active program for community relations. This program will be staffed with specialists trained in communication and experienced in such activities. Designated experts for the management of grievances on site, NewCo and corporate level will be established for a more transparent, reproducible and credible response to all complaints.

As part of the EPS Restructuring Project a Corporate SEP and site specific SEPs will be implemented to improve the communication with the general public, affected people and NGO's. This will include an EPS internal and

¹ BREF: Best Available Techniques Reference. BREFs are drawn up for defined activities and describing, in particular, applied techniques, present emissions and consumption levels, techniques considered for the determination of best available techniques for energy intense projects.

external grievance procedure. Also a Resettlement Framework will be prepared at corporate level to lay down procedures for any EPS resettlement activity aligned with the EBRD requirements and international best practice. Site-specific resettlement action plans will address the local circumstances and implementation will be monitored to apply corrective actions if required. Besides, EPS plans that the corporate real estate manager is responsible for the management of resettlement issues and to support the managers on site level regarding all related issues.

2.2 *SUMMARY OF SEP*

The Corporate SEP aims at ensuring that a timely, consistent, comprehensive, coordinated and culturally appropriate approach is taken to consultation and project disclosure for all EPS activities. It is intended to demonstrate the commitment of EPS to an 'international best practice' approach to engagement in line with Serbian requirements and EBRD's 2014 Environmental and Social Policy including the 10 Performance Requirements (PR).

The Corporate SEP is the framework document, which will be amended and updated as required. It will be supported by site specific SEPs that may be required by the implementation of new EPS projects or the extension of existing ones with the goal of having a fit-for-purpose approach for the local circumstances. The SEP describes the Serbian and EBRD requirements for stakeholder engagement, identifies stakeholder groups to be considered and provides a stakeholder engagement program with detailed activities. Also a grievance procedure for EPS employees and project affected people is described that will be implemented at corporate- and site level (including grievance forms). Finally the Corporate SEP includes responsibilities and reporting and monitoring requirements.

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