

The Inspection Panel

Overview

Inspection Panel Investigation Report South Africa – Eskom Investment Support Project (EISP)

Prepared by World Bank Inspection Panel

The following is an Overview of the Request for Inspection on the Eskom Investment Support Project (EISP) and the Panel’s Investigation Report which was discussed by the World Bank Board of Directors on May 22, 2012.

The Request and Investigation scope

On April 6, 2010, the Inspection Panel received a Request for Inspection from community members living in the impact area of the 4,800 MW Medupi power plant, which is a core component of the Bank-financed EISP. The South African parastatal agency Eskom Holdings Limited is the Borrower and the Government of South Africa is the Guarantor of the loan.

The Request contained 15 claims alleging potential harm as a consequence of the Project and related issues of Bank policy compliance. The potential harms alleged were mostly local in nature, but some related to national or wider impacts. As per its mandate, the Inspection Panel assessed all claims, and concluded that 11 of these claims warranted an investigation of the Bank’s compliance with its relevant policies. A key feature of the Panel’s investigation was the application of the policy *Piloting the Use of Borrower Systems to Address Environmental and Social Safeguard Issues in Bank-Supported Projects – OP 4.00* (or “Use of Country Systems”). This was the first Panel investigation related to this policy, posing methodological challenges with assessing compliance at both a ‘system’ and ‘project’ level, as provided for in OP 4.00.

The Project context

The need for electricity generation in South Africa is urgent and of paramount importance to development in the country. The Panel recognizes that the Project’s development objective is to support South Africa in enhancing its power supply and energy security. The US\$ 3.75 billion Project is the largest loan made by the Bank to date, and includes the 4,800 MW Medupi coal-fired power plant at Lephalale and associated infrastructure. It thus carries with it considerable reputational risks for the Bank in the event of non-compliance with its operational policies, and related harm.

The construction of the Medupi plant had already commenced when the Bank was approached for financing consideration. The design and environmental impact assessment (EIA) of the plant had already been completed. The Bank had to review the consistency of the EIA and related documents with its policies and request additions or corrections, where warranted, before submitting the loan for Board approval.

The Panel findings

The Panel findings on compliance and harm were reached with the assistance of six international and local experts in relevant fields. As required by the Resolution, each finding has a basis in Bank operational policies applicable to this Project.

At the *system level*, i.e. the Bank Management's assessment of the country's legal and institutional framework, the Panel found that:

Overall, Management's view that the South African system is equivalent and acceptable, supporting the application of the "Use of Country Systems" policy, is well founded. However, the Panel identified three shortcomings in the Bank's assessment (the Safeguard Diagnostic Review) and related gaps that were linked to risk and impact management and oversight.

Firstly, Bank policy requires that appropriate studies are undertaken proportional to, amongst others, cumulative impacts; the latter issue was a major concern of the Requesters. At the time that the Medupi EIA was prepared there was not an equivalent requirement in South African law and the project's EIA did not reflect these important impacts. Secondly, the Panel found that there was an inadequate assessment by Management of capacity at provincial and local authority levels. Although the national level of government is responsible for decision making on the project and for enforcement of conditions of environmental authorization, the sub-national authorities play a crucial role in managing air quality and water services, and in oversight and compliance monitoring, enforcing environmental (including water) laws. Thirdly, Bank policy calls for the use of an independent advisory panel of international experts in the preparation and implementation of projects that are highly risky or involve serious environmental and/or social concerns. There is no such requirement in South African law.

At the *project level*, the Panel found lack of compliance with provisions of Bank policy with respect to three main issues of potential harm:

Water supply to the plant and related impacts: Operation of the power plant, including the technology for removal of sulphur dioxide from emissions (flue gas desulphurization - FGD), will place an additional strain on water resources in an area that is already suffering from water scarcity. The Panel is of the view that although Management recognized the risk of water availability to the plant, it did not fully consider the impacts and risks of water supply alternatives to other local water users. The Panel's understanding from the project documentation is that the operation of FGD is dependent on the completion of Phase 2 of the Mokolo-Crocodile Water Augmentation Project (MCWAP). The apparent postponement of Phase 2 of MCWAP adds considerable risks to the successful outcome of the Project in terms of air quality and health issues. Bank Management has not provided adequate information on alternative sources of water for the plant and the environmental and social implications of their use, other than stating that Phase 1 of MCWAP (with possible augmentation from groundwater and municipal wastewater) will be sufficient for these purposes.

Air pollution: Emissions from the Medupi plant pose a health risk to local communities, adding to existing background levels of air pollutants from the existing Matimba power plant and other sources. The Panel commended Management for insisting on incorporating FGD in the plant

design, but noted that complete installation of FGD was only planned for three years after full operation of the power plant, and that the choice of ‘wet’ FGD technology significantly increases the water requirements of the plant. Delays or interruptions in water supply may further extend the interval without emissions reduction.

Public services and infrastructure: The influx of people related to the project and the associated expansion of the coal mine places additional strain on public services and infrastructure in the local municipality. By its own recognition, this municipality is poorly equipped in terms of financial and human resources to accommodate the increasing needs. The Panel noted that the EIA identified this as an issue involving risks of high significance, but found that Management had not adequately assessed the identification and implementation of commensurate mitigation measures.

Bank Management response and looking forward

The Panel wishes to emphasize that the purpose of the Panel process is to address the concerns raised by requesters when validated in relation both to alleged harms and compliance with Bank policy. A Panel investigation may also provide important lessons for the Bank in terms of policy application. Hence, the intended outcomes of the Panel process, in terms of actions moving forward, are (i) identification and implementation of appropriate actions in terms of redress when harm has been caused, (ii) identification and implementation of actions to improve the project and strengthen implementation to manage risks of potential harm, and/or (iii) identification of actions in response to lessons emerging from the Panel’s analysis of compliance.

Bank policy requires project supervision for pilot projects applying the “Use of Country Systems” which, according to OP/BP 13.05, involves identification of key risks to project sustainability and the recommendation of appropriate risk management strategies and actions to the borrower. In this case, the investigation validated three areas of significant environmental and social risks and potential harm at the local and project level linked to Bank’s policy compliance, namely regarding water resources, air quality and public health, and local public services and infrastructure. The risks and harms regarding water resources are inextricably linked to those of air quality and health. The investigation also provides lessons with respect to application of the policy on “Use of Country systems” in terms of system and project level assessments.

In this respect, and in response to the Panel’s findings, the Panel acknowledges Management’s preparation of a Supplemental Note to the Management Report and Recommendation, its commitment to extended supervision of the Project until 2022, and further elaboration of the scope of its supervision.

The Panel notes that many of the potentially significant impacts may only materialize during the operational phase of the project; operation of the first unit is planned to start in 2013. In light of the potential significance of harms, should the risks materialize, the Panel notes that Bank policy (BP13.05) calls for a supervision plan within a clear results framework to enable timely intervention where necessary to resolve problems. Moreover, the Panel notes that the “Use of Country Systems” policy emphasizes capacity building and human resource development beyond individual project settings as a key objective of this policy.

The Panel concurs with Management that it is proper and appropriate to rely on South Africa's comprehensive systems as the core means to address these issues going forward. In addition, the Panel appreciates that the outcome of the Project relies heavily on a good working partnership between the Bank and Eskom as well as the country's national and sub-national authorities. The Panel also appreciates the commitment to foster transparency and broad stakeholder participation during the supervision period, and hopes that Management continues to include the Requesters and other locally affected persons in their consultations.

For the complete Inspection Panel Investigation Report, World Bank Management Report and Recommendation in Response to the Inspection Panel Report and World Bank Supplemental Note to the Management Report and Recommendation, please visit the Inspection Panel website: <http://www.inspectionpanel.org/>

The African Development Bank's Independent Review Mechanism (IRM) received a complaint about AfDB's financing of the Medupi Power Project. The complaint raised issues similar to those raised in the Request sent to the Inspection Panel. The AfDB IRM's compliance review report is not yet publicly available. For more information, please visit the AfDB IRM website at: <http://www.afdb.org/en/about-us/structure/independent-review-mechanism/>