

# POWER SECTOR AT CROSSROADS: THE NEW POWERPLANT – AN OLD IDEA?

MAY, 2019





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# “KOSOVA E RE” POWER PLANT AND TARIFFS

ALBAN HASHANI, VISAR VOKRRI

**T**he process of reforms in the energy sector in Kosovo, in particular the process of building of “Kosova e Re” power plant, for which the Government of Kosovo has signed a contract at the end of 2017, has been met with polarizing opinions in favor and against it. Because this sector is of vital importance to the quality of life of Kosovo citizens, the way of contracting and the results of this important process attracted greater attention.

This process, which started in 2005, underwent major changes for more than a decade up to the current formulation which can be found in the contract signed by the Government of Kosovo. During this time, in addition to delays, significant costs have been incurred for technical assistance in designing and keeping up the process. These costs, apparently, have failed to justify themselves. The entire process has been going on in an environment lacking overall basic social consensus. While attracting the interests



**KOSOVO GOVERNMENT FAILED TO COMMUNICATE PROPERLY AND CONVINC AN IMPORTANT PART OF THE AUDIENCE ABOUT THE BENEFITS OF BUILDING ‘KOSOVA E RE’ POWER PLANT AND ABOUT THE RATIONALE OF CHOOSING SUCH A SCENARIO.**



of right investors for such an investment process is important, the Government must make clear that other audiences are equally, if not more important. These audiences first of all include citizens who in the last instance are also public service customers. They should be totally aware of the benefits and the costs of such a process. From this perspective, the Government of Kosovo has failed to communicate properly and convince an important part of this audience about the benefits of this process and the rationale of choosing such a scenario. Such communication and consensus can only be achieved through a comprehensive dialogue which is anchored in a strong legal and institutional framework that provides transparency and accountability. In this concrete case, as argued in many research reports, there has been a significant lack of such a discussion that would attract wide social support. Moreover, the process was characterized by a considerable lack of transparency followed by a limited access to data. The creation of a communication platform is a prerequisite for the success of such a process, especially in energy sector which has more complex features compared to other sectors. Moreover, due to high-

er impact that this sector has on the economy and the well-being of citizens, it is necessary to create mechanisms of control and balance between the Government and the Assembly, which in this case have been very limited.

While it is evident that conditions for sustainability of electricity supply must be created, this cannot be done without carefully analyzing the issue of cost-affordability, directly by the government and the consumer. Tariff impact assessments vary ranging from above 50 percent (according to preliminary assessment of Energy Regulatory Office) to those that are close to twice the current price (according to assessments of various non-governmental organizations). Accurate assessment cannot be done without finalizing the financial report of the agreement and without knowing the terms of financing through a loan that “Contour Global”. will receive from Overseas Private Investment Corporation, known as OPIC, However, even the most conservative assessments show that the rise in energy prices after the start of operation of “Kosova e Re” power plant raise the alarm regarding consumer affordability.



**TARIFF IMPACT ASSESSMENTS VARY RANGING FROM ABOVE 50 PERCENT (ACCORDING TO PRELIMINARY ASSESSMENT OF ENERGY REGULATORY OFFICE) TO THOSE THAT ARE CLOSE TO TWICE THE CURRENT PRICE (ACCORDING TO ASSESSMENTS OF VARIOUS NON-GOVERNMENTAL ORGANIZATIONS).**

According to Kosovo Agency of Statistics data, households in Kosovo spend about one fifth of their household income to cover electricity costs. The sensitivity to higher energy prices is higher among low-income households, for which the share of energy paid represents a larger share of household spending. The over 50 per cent of rise of energy price (according to more conservative assessments) is considered to have around 5 per cent of households fall below the poverty threshold. Alternatively, Kosovo Government should increase the number of households as part of social assistance scheme that would cover their energy spending. Currently there are over 26 thousand households that are part of this scheme and the budget cost reaches 4.5 million euros per year covered by citizens' taxes. The government's main incentive for subsidies is the intention to keep low electricity prices for the final consumer in order to avoid potential economic, social or political problems. Thus, citizens may not be facing higher electricity prices directly in bills, but they will indirectly be affected by taxes that will be used by Kosovo Government to cover the difference between the agreed price and market price.

Power supply continues to be a problem for enterprises, especially for production companies. Therefore, the creation of conditions for regular supply is essential to maintain and increase the competitive position of enterprises in Kosovo. However, higher prices as per current projections may lead to lower competitiveness as electricity is the main input for most production companies. Moreover, in circumstances with inter-subsidies between the industry and the household still in place, the cost of energy disproportionately increases for enterprises. According to assessments, current energy prices for industrial customers should be reduced by almost one-tenth in order to eliminate inter-subsidies. Under such conditions, businesses may lower their competitive position as the high price of electricity cannot turn into price increase of products they produce and sell. This is because consumers are susceptible to rising product prices and can find other alternatives from among the imported products given the current trade arrangements of Kosovo.



**“ THE OVER 50 PER CENT OF INCREASE ENERGY PRICE (ACCORDING TO MORE CONSERVATIVE ASSESSMENTS) IS CONSIDERED TO HAVE AROUND 5 PER CENT OF HOUSEHOLDS FALL BELOW THE POVERTY THRESHOLD.**

The real cost of construction of “Kosova e Re” power plant is not only limited to high, potentially unaffordable, price of electricity. Direct budget implications of the construction of ‘Kosova e Re’ power plant are significant. With this contract, Kosovo Government disproportionately takes over many obligations that violate market rules and the path of European integration.

It is clear that Kosovo Government has no easy way out of this commitment. This is because the withdrawal from the contract and its cancellation are followed by financial costs. However, in the context of this discussion, this cost may be lower than the cost assumed by the Government of Kosovo, and consequently the citizens, if it continues with this scenario. Withdrawal from the contract could create a new momentum for more comprehensive dialogue on the future of energy sector in Kosovo.



**“ HIGHER PRICES UNDER CURRENT PROJECTIONS MAY LEAD TO LOWER BUSINESS COMPETITIVENESS AS ELECTRICITY IS THE MAIN INPUT FOR MOST PRODUCTION COMPANIES.**

**“ WITH THIS CONTRACT, KOSOVO GOVERNMENT DISPROPORTIONATELY TAKES OVER MANY OBLIGATIONS THAT VIOLATE MARKET RULES AND THE PATH OF EUROPEAN INTEGRATION.**

# “KOSOVA E RE” POWER PLANT AND THE ENVIRONMENT

LUAN SHLLAKU

**I**t is obvious that coal / lignite-based operations are highly polluting. This will also be the case with Kosova e Re Power Plant (TCKR). Not everyone agrees with this fact: environmental NGOs and environmental experts constantly argue that the construction scenario of TCKR in Obiliq is a strong attack on environmental quality in a wide area around the power plant; Government officials,

who are not letting go off of this scenario for 15 years, attempt to argue that after the TKCR's construction, the environmental situation will improve. Above the interests of the parties in Kosovo are those of imposed by the European Union which, whether we like it or not, will have to be decisive in the development of this sector - if we want to be part of Europe one day. The development of a clean, efficient



**“ OVER 800 INHABITANTS LIVE IN ONE SQUARE KILOMETER OF THE SPACE THAT HAS A DIAMETER OF 30 KM, WITH POWER PLANTS AT ITS CENTER. THIS SHOULD BE THE MAIN ARGUMENT TO PROVE THAT THE CONSTRUCTION IN OBILIQ IS A VERY BAD OPTION.**

and a safe concept of energy supply, promotion of clean energy generation opportunities, better management of mining resources - these are the most important investments of the European Union in this sector.

## Arguments brought by environmental experts:

### Problems coming directly from power generation in TKCR plants:

**a** The burning of fossil fuels, such as lignite, will necessarily be abusive vis-a-vis virtually all environmental values. Lignite as fuel is far from the quality compared to some non-renewable fuels. Its low calorific value [The calorific value of lignite in Kosovo is averagely 7.1 MJ/kg.] requires burning a large amount of energy to generate the projected energy. The more we burn lignite, the more we pollute the surrounding air, water and soil.

**b** The content of lignite is very unsuitable for the environment: the high level of moisture, the presence of sulphate and its chemical composition that is rich in heavy metals and other potential pollutants cause many headaches to the designers of exploitation, processing and combustion technologies which, despite having managed to eliminate the high emission levels, are still far from building a power plant without significant impact on the quality of the environment.

**c** Many of those who work with power plants, when speaking about the pollution that comes from them, unfairly refer only to flues – respectively gases and particles emitted by them, as the only cause of pollution. The truth is that PPs emit much more pollution than their flues and have far more emission points of pollutants. If we look at the entire technological cycle (simplified) of a PP, we will see that each part of this cycle emits pollution: (1) lignite extraction in surface mining, (2) lignite transport at landfills, (3) combustion of lignite (combustion products go to the flue), (4) ash transport at ash landfills, and (5) ash deposited in active landfills. Each of the aforementioned activities emits pollutants in the air, water and soil.



**THE TRUTH IS THAT PPS EMIT MUCH MORE POLLUTION THAN THEIR FLUES AND HAVE FAR MORE EMISSION POINTS OF POLLUTANTS.**

**Problems related to the location of TKCR:**

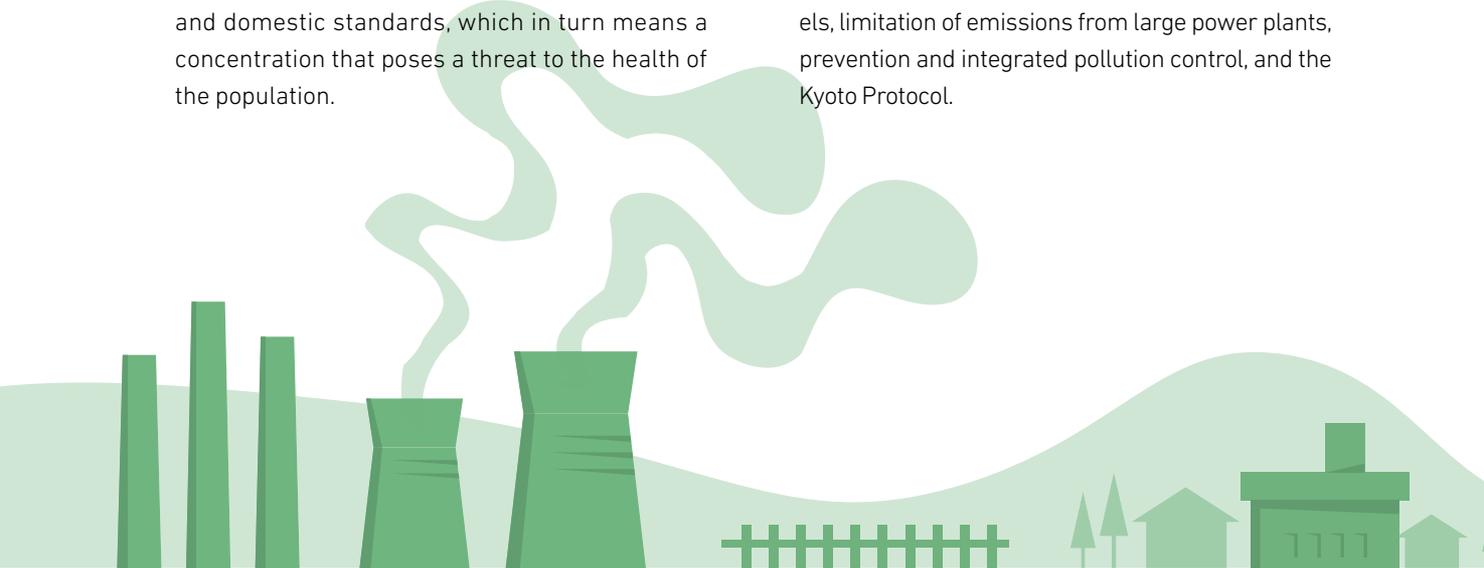
**a** TKCR will be only 4-5 kilometers from Prishtina. When winds blow in the direction of Prishtina, pollutants emitted by flues or even active ash landfills can easily pollute the air in the capital city and its surroundings.

**b** Pollutants emitted by TCKR will add to pollutants coming from other sources, such as TC Kosova A and Kosova B, dense traffic and home heating – especially during winter. This means that no matter how little a single pollutant of TCRR can emit, for example, nitrogen oxides, that can be the “straw that broke the camels’ back” – the amount of pollutant that adds to what is present in the air because it has come from other PPs and thus exceeds the concentration allowed according to EU and domestic standards, which in turn means a concentration that poses a threat to the health of the population.

**c** The selected location will also bring a significant problem: all polluting operations of the TCKR will be directed towards a very dense population living in its area of impact. Every polluting episode – and we have many of those throughout a year, especially during winter – has negative impact on the health of a large number of citizens living in the area.

**Problems arising from non-compliance with European energy and environment legislation and policies**

**a** The EU insists that each country respect the European acquis which stipulates the quality of the living environment. This, among other things, includes studies on strategic and social impact of environmental impact, reduction of sulphate contents in fuels, limitation of emissions from large power plants, prevention and integrated pollution control, and the Kyoto Protocol.



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**b** Specifically, they are told that the whole region emits a large amount of greenhouse gases due to excessive use of lignite. Member States are required to sign the Kyoto Protocol.

**c** Special EU directive (80/2001) obliges member states and those who adhere to use the best technologies of the time to avoid pollution, and this applies both to existing PPs and to those that are being constructed. This directive also sets out measures that avoid the chances of industrial waste production.

**d** Citizens' participation in decision-making before the construction of large facilities that are seen as potentially polluting is regulated by several Directives and Conventions; and this is considered as a very important decision-making moment for new investments in this regard. The decisive moment in this Directive, which is not respected by our decision-makers, is that: (1) citizens should be clearly informed about government plans to invest in large energy facilities; (2) citizens should be informed about these plans before any decision is made; and

(3) when all development options are still open, including the option "not to be built at all". Citizens' opinion should be taken into account and mechanisms should be provided so that this opinion is given in the best democratic circumstances.

**e** European Parliament has set emission limitations for each pollutant emitted by power plants bigger than 50 MW. This Directive sets out the limit values for sulphate dioxide, nitrogen oxides, particles and heavy metals emitted by plants which operate with non-renewable fuels (of fossil origin). Also, this Directive, which includes 10 annexes, defines combustion technologies and emission limits separately for each one.

**f** Among many laws which set out the quality of the environment, a special place occupy those which relate to the regulation of climate change. EU stipulates that greenhouse gas emissions should be reduced by 20% by 2020. In general terms, the emission level of these gases should be brought to that of 2008-2010.



**WHEN WESTERN BALKANS COUNTRIES SIGNED CONTRACTS WITH THE EU, THEY WERE INFORMED THAT THE QUALITY OF THE ENVIRONMENT IN THESE COUNTRIES IS LARGELY AFFECTED BY THEIR ENERGY OPERATIONS.**

## The arguments of Kosovo decision-makers

Strongly convinced of the need to build a PP where existing PPs have been working for 5 decades, Kosovo decision-makers (central governments) have been struggling for two decades to build TCKR in Obiliq near the existing PPs. This great change was not the result of analyses that they carried out in the meantime and learned something new, but rather the result of dictates of major international agencies, which changed their approach after global pressure to minimize coal-fired power plants. We can freely say that the insistence on the construction of lignite-based in Obiliq comes from the interest of our governments and international partners (World Bank, USAID, EU) to build this PP despite the objections of citizens, environmental NGOs and any opposition political party. What are the arguments that the governments which, helped by some agencies interested in this investment, provide to prove that the quality of the environment will not deteriorate - on the contrary - will improve by the construction of the TCKR. They say:

**a** Kosovo by all means must use its mining assets - this is a comparative advantage that must be utilized. This way, we will become significant energy producer in the region. Failure to build new PPs jeopardizes the country's economic development.

**b** A modern plant will be built with almost no pollution whatsoever. Moreover, most of similar power plants we have visited in the region, have no flue at all!

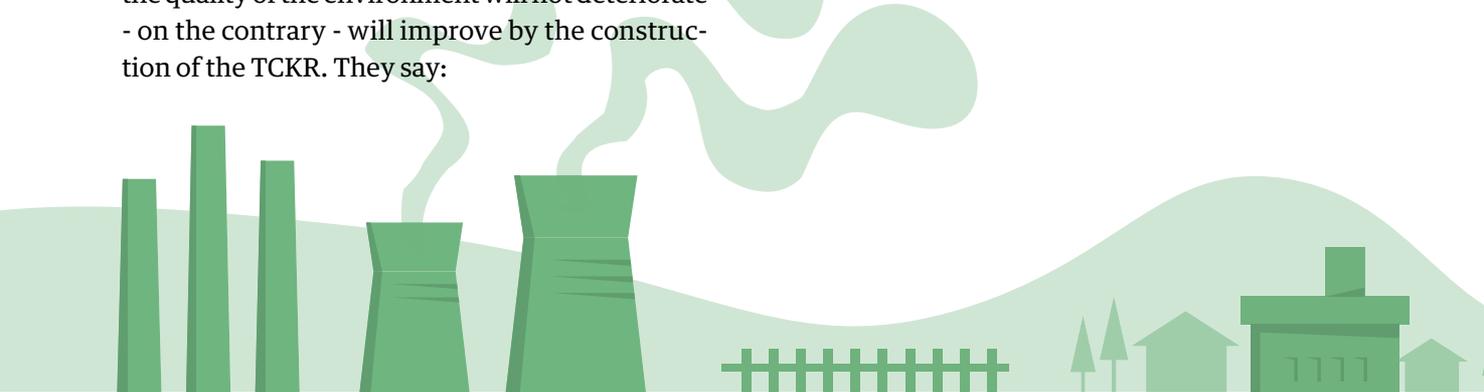
**c** With the construction of TCKR power plant the overall situation will not deteriorate but will improve significantly.

**d** The emitted pollutants will be filtered to the maximum and their impact will be almost zero.

**e** Newer technologies to increase the efficiency of TCKR and reduce the emitted pollutants will be applied.



**GOVERNMENTS CHANGED BUT THERE WAS LITTLE DIFFERENCE IN THEIR APPROACH: WHAT MAKES ONE DIFFERENT FROM THE OTHER IS ONLY THE INSTALLED POWER OF THE PP WHICH WAS REDUCED FROM 2100 MW TO 500 MW, LIKE IN THE CURRENT ONE.**



## The most relevant challenges for Kosovo's energy development

The energy sector, especially that of electricity generation, should be further developed. It is a complex sector that has found post-war Kosovo quite unprepared to design future development patterns. However, even two decades later and with a decisive state administration which did not lack the determination to develop this sector, we are still in the pre-war situation. New generation capacities were not built and, moreover, no modern development concept was built to advance Kosovo energy production. From the outset, decision-makers chose to build PPs, where two existing PPs already operate, and quite close to the capital. This was the easiest possible decision to make: very simple; you open an international bid and choose and sign a contract with the winning company. What our decision-makers did not think was that they intended to build a large PP, initially 2100 megawatts, over our lignite potential, generating many environmental as well as economic problems and creating many developmental

knots with other sectors such as hydro-economy, agriculture, inducing undesirable demographic movements and affecting the public health of the population. All these aspects that were not taken into account by our decision-makers and some of international agencies could not have been neglected by global organizations which were globally targeted as supporters of abusive developments on health and the environment, such as the World Bank. They withdrew their support without which Kosovo governments could not construct.

After the first failure, Kosovo governments continued their efforts to build something in Obiliq, although now they were less ambitious - they wanted PPs with 1000 megawatts and later agreed on 500. But in the meantime, the international market, the rules imposed by EU and other international environmental conventions, have made it increasingly difficult to build PPs based on fossil fuel.

At this point of time we are facing many development challenges of this sector. But whatever

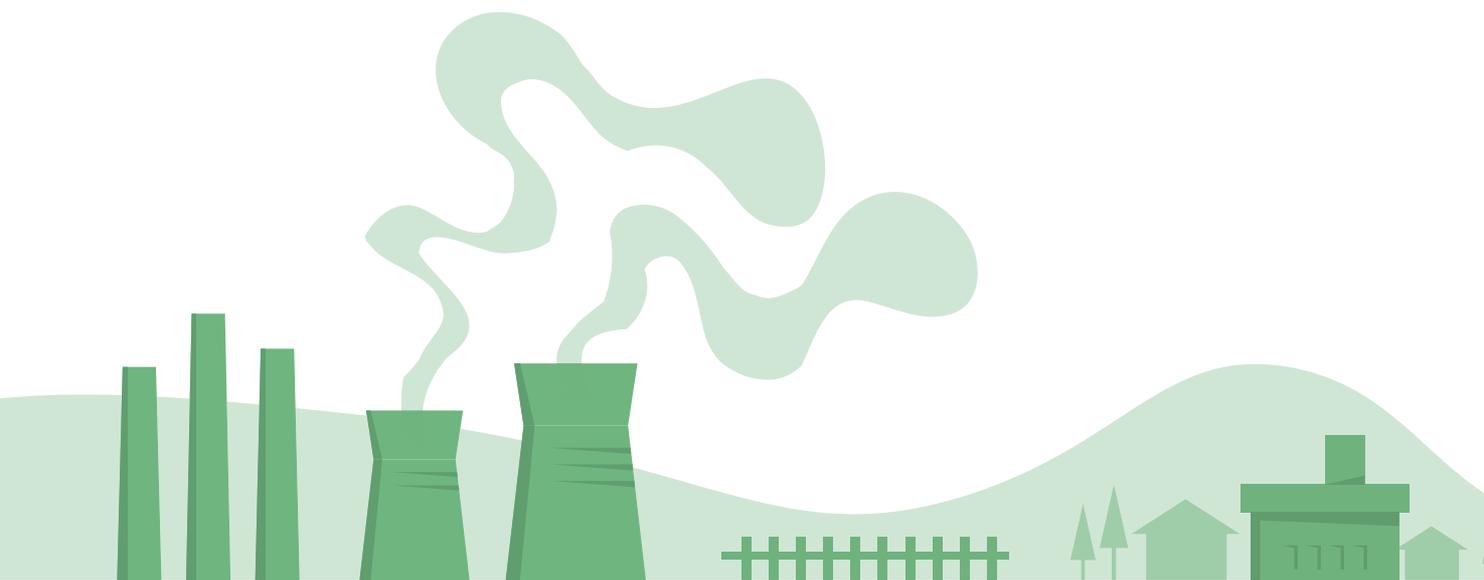


**MOVE AWAY AS MUCH AS POSSIBLE (DOWN TO ZERO) FROM THE EXPLOITATION OF LIGNITE AS FUEL FOR THE CONSTRUCTION OF NEW PPS.**

scenario we chose for its development, we should make sure we are in full compliance with: (1) EU environmental standards; (2) Basic rules of functioning of free energy market, imposed by Energy Community Treaty; (3) Treaties that set out the rules of conduct in respect to climate change and (4) Basic standards for the harmonization of economic and social development of Kosovo by providing integral action among different sectors.

**The most relevant challenges to harmonize energy development with environmental quality would be:**

**a** Kosovo has a lot of constructive space to bring alternative, renewable resources, such as wind, sun, water, geothermal energy in the focus of future developments. At present, existing power plants can represent a sufficient energy “load” as primary energy to guarantee the well-being of the sector. Depending on the amount and speed of energy generation from these alternative resources, the sector development strategy needs to be built.



**THIS STRATEGY WOULD FOLLOW THE PRINCIPLE: “ALTERNATIVE RESOURCES TO THE MAXIMUM, THEN WE WILL SEE IF WE NEED A SMALL PP, NOT NECESSARILY BASED ON LIGNITE.”**

**b** In the event of construction of a lignite PP, we should get as far as possible from the existing PP (Obiliq) and examine the possibilities of building small generating blocks in the Dukagjin plain, which is the second largest resource of lignite in Kosovo. In this site, we would avoid the phenomenon of added pollution from other nearby sources such as existing PPs, traffic, house heating and similar, and we would be closer to the necessary water resources.

**c** It can be co-owned by introducing the existing Kosova B, which can divide a generating block that would produce the electricity for the Albanian market as a priority. So, the modalities can be various, but the benefits for both sides would be enormous. Among other things, Kosovo can thus fulfill the condition of energy generation from renewable resources, which is set by the EU deriving from 20-20-20 energy policies.

**d** Consolidation of alternative energy generation market, increased level of energy efficiency application, stabilization of energy market based on EU rules would directly lead to minimization of negative impact of this sector on the quality of the environment and the health of citizens.



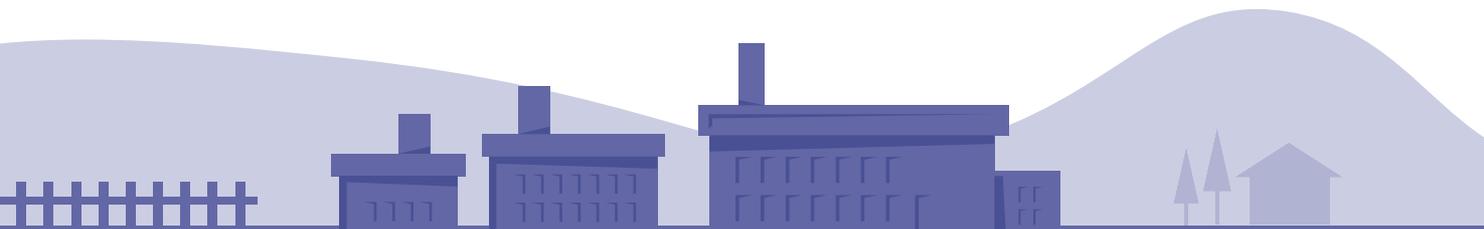
**“ WE SHOULD HAVE THE COURAGE TO THINK BEYOND NARROW NATIONAL INTERESTS: TO BUILD A HYDROPOWER PLANT IN ALBANIA OVER THE MANY WATER RESOURCES THAT ARE STILL UNUSED. THIS HYDROPOWER PLANT OF CCA. 500 MW CAN BE BUILT WITH DIFFERENT SCENARIOS, IN COOPERATION WITH THE ALBANIAN AUTHORITIES. ”**

# “KOSOVA E RE” POWER PLANT AND STATE AID



**T**he issue that has raised great concern regarding the construction project of “Kosova e Re” power plant is that of competition and state aid. The latter is defined as the aid states give to a company by using public resources, which damage or threat-

ens competition. There is sufficient evidence to show that the construction of ‘Kosova e Re’ in the current arrangement constitutes state aid defined under the EU directives, but also by Kosovo legislation.



“ ACCORDING TO PRELIMINARY ASSESSMENT, THE ENERGY PURCHASE AGREEMENT, THROUGH THE NEW GOVERNMENT-CREATED COMPANY (NKEC), BY CONTOUR GLOBAL CLEARLY CONSTITUTES STATE AID, AND THE SAME RESTRICTS COMPETITION.

“ THE CONSTRUCTION OF “KOSOVA E RE,” WITH ITS CURRENT ARRANGEMENT, WILL EFFECTIVELY SHUT DOWN THE ENERGY MARKET IN KOSOVO, AT LEAST AS LONG AS THE CONTRACT IS IN FORCE, I.E. FOR THE NEXT 20 YEARS.

The primary argument of the Government of Kosovo to support such a project is that the attraction of investors in the energy generation project is impossible without providing stimulating support. This support in the case of Kosovo, among other things, comes as a warranty for the market for a period of twenty years, including an investment loan. Such support effectively means closing the market and restricting competition.

European Union ensures that member states do not take steps which are contrary to the provisions of the legislation on state aid. In this context, European Commission has the right to assess whether a specific measure constitutes state aid or not. Although Kosovo is not yet an EU member, since 2015 it is a signatory of the Stabilization and Association Agreement as a contractual agreement for its road towards the European Union. As part of this agreement, state aid is generally prohibited. Moreover, through the adoption of new legislation in the field of energy in 2016 Kosovo has complete-

ly transposed the third package of Energy Community legislation. This legislation explicitly requires the market to be open to competition. As a signatory party of the treaty for the establishment of energy community, and as a signatory party of the Stabilization and Association Agreement, Kosovo is bound to be in line with the applicable legal framework. Kosovo has already adopted the law on state aid and the law on protection of competitiveness. Kosovo has signed the contract for the construction of the “Kosova e Re” power plant without obtaining approval from the state aid department, as envisaged by domestic legislation. Although state aid, in limited contexts, may be allowed, Kosovo Government did not provide evidence that the current arrangement could be classified as state aid.

According to a preliminary assessment by the energy community secretariat, the energy purchase agreement through a government-created company (NKEC), by Contour Global clearly constitutes



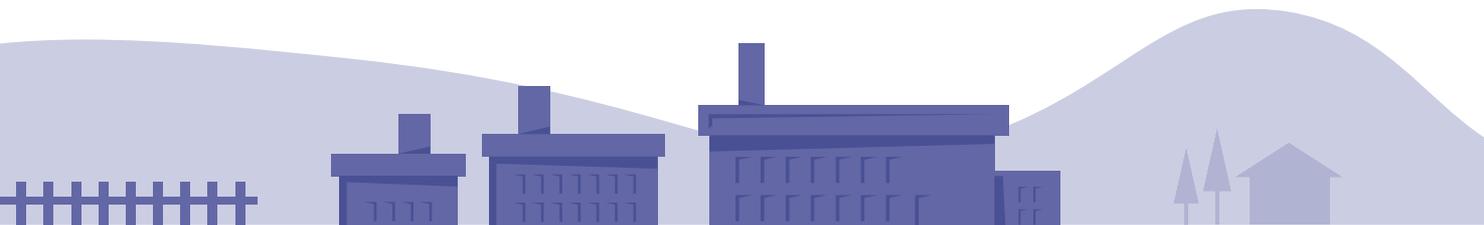
**“ KOSOVO GOVERNMENT HAS TO GUARANTEE THE LOAN FOR FINANCING THE CONSTRUCTION OF “KOSOVA E RE,” WHICH IS TREATED AS A PUBLIC DEBT. THIS MEANS THAT WITH SUCH A TREND, AND UNDER THE ASSUMPTION OF CURRENT LEGAL CONSTRAINTS, THE POSSIBILITY OF GETTING NEW LOANS WOULD BE LIMITED FROM 2023 AND ESPECIALLY FROM 2025.**

state aid and the latter limits competition. This is because such an arrangement puts Contour Global in a more favorable position compared to other generating operators in Kosovo. Under current market conditions, NKEC may not be able to sell the energy at the purchased price and such a difference should be subsidized by the state or the cost should be distributed/passed to the customer.

Under the contract, NKEC is also obliged to pay other system charges and network access fees normally paid by the generation company itself. Also, Contour Global is exempted from paying VAT and customs while the transfer of land carried out as compensation for the payment which is far from reflecting the market price. The construction of “Kosova e Re,” with its current arrangement, will effectively shut down the energy market in Kosovo, at least as long as the contract is in force, i.e. for the next 20 years. The duration of this energy purchase contract is nearly twice as long as the duration of current incentive schemes for alternative sources. Current contractual conditions iso-

late Contour Global against market influences and systemic risk is carried by the Government. This puts Contour Global company in a better position compared to all other operators.

Under the current arrangement, Contour Global has to get the loan for financing the construction of “Kosova e Re.” The guarantee of this loan is given by the Government of Kosovo. However, loan guarantees, as well as the loan itself, are treated equally under the law on public finances and it should be ratified by a qualified majority in the Assembly of Kosovo. Overall, the Republic of Kosovo has a low public debt burden which, according to data for the third quarter of 2018, now reaches over 1 billion euros or close to 17% of country’s GDP. However, this requires increased attention of the Government and other actors regarding Kosovo’s absorption capacity to transform this debt into economic growth and social welfare, respectively when it comes to medium and long-term implications of these movements on macro-economic and fiscal stability.



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A loan guarantee for Contour Global would result in a significant reconfiguration of some macro-fiscal parameters. In this way, the guarantees issued by the Government, respectively the Republic of Kosovo, which by the end of 2017 amounted to 44 million euros would be added to about 350 million guarantees for Contour Global (MED Minister assessment). With this guarantee, under the conditions set by fiscal rule, respectively the Law on Public Debt according to the presented projections, by 2021 total debt participation would be about 28% in GDP, an overall debt of about 2,3 billion euros, compared to about 1 billion as it is now. This means that with such a trend, and under the assumption of current legal limitations, the possibility of getting new debts would be limited from 2023 and especially from 2025 onwards. This issue should be addressed now since it can have serious fiscal implications and also when it comes to keeping the necessary pace of new borrowing needs or guarantees for new development projects in infrastructure and other fields.

If Kosovo continues with this arrangement, it may face a lawsuit by other competitive companies for violating the law on state aid. Also, Kosovo can seriously undermine its position in the European integration process since, in that case, it would fail to comply with the directives deriving from the Stabilization and Association Agreement. Moreover, if it continues with this arrangement, Kosovo risks the right to vote at the highest level of representation in the Energy Community Treaty.







