



<Executive Summary>

**Fair Finance Guide the 11th Report on Case Study
Indonesian Coal-fired Power Exposed to Corruption**

Cirebon coal-fired power project: problems on environment, human rights, and corruption, and banks' non-compliance with international norms



(Photo by WALHI West Java - Friend of Earth Indonesia, October, 2016)

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Executive Summary

Cirebon coal-fired power project is implemented by an independent power producer (IPP) to provide electricity to Jawa-Bari grid, Indonesia. Private and public sectors in Japan, Korea and Indonesia are the main actors to promote the project. Three Japanese private banks (Mizuho Bank, Ltd., Sumitomo Mitsui Banking Corporation (SMBC), and the Bank of Tokyo-Mitsubishi UFJ, Ltd.), in cooperation with Japan Bank for International Corporation (JBIC), the Export-Import Bank of Korea (KEXIM) and ING bank in the Netherlands, have been providing co-financing for both Unit 1 (660 megawatt (MW)) that has been already operational and Unit 2 (1,000 MW).

Since 2007 when the construction of the Unit 1 was started, the local residents living around the project site have protested concerning negative impacts of the project on their livelihoods and health. The local residents also oppose the Unit 2 plant that is currently under construction. They filed an administrative lawsuit demanding the revoke of the environment permit in December 2016, for their livelihoods, such as small-scale fisheries and salt-making farms have already been greatly affected by negative effects of the construction and operation of Unit 1. As the result of the lawsuit, a decision was made to win the residents in April 2017; that led the banks, even who had just signed the loan agreement on the Unit 2 project one day before the verdict, to refrain from disbursing the loan.

However, even after that, the project company still continued the land preparation work and proceeded to the full-scale construction based on the new environment permit (issued in July 2017 without letting the local residents know). In November 2017, the banks also decided to make an initial loan disbursement for the Unit 2 project. The construction work of Unit 2 has got about 61% completed as of September 2019.

Meanwhile, issues on environmental, social and governance (ESG) regarding the Unit 2 project remain piled up, including bribery allegations which have been raised since 2019. The banks have not complied with international norms including the Equator Principles (EPs) (compliant with the International Finance Corporation's Performance Standards (IFC PSs)), the United Nations Global Compact (UNGC), and the OECD Guidelines for Multinational Enterprises (OECD Guidelines) although they are supposed to.

(1) Impacts on various livelihoods and lack of appropriate compensation and measures to restore livelihoods

— 11 items of non-compliance with EPs & IFC PSs/ 2 principles of non-compliance with UNGC/ 1 item of non-compliance with OECD guidelines

The coastal ecosystem was destroyed because of the construction and operation of Unit 1. Small-scale fishermen, who have caught fish around the shoal without using a boat, are suffering from a decrease in the fish catch and forced to have a harder life than before. Also, the salt-making farmers around the power

plant had to remove some black dust from the salt they produced although the cause could not be identified as coal dust or fly ash. The product quality of salt has been getting lower, and the farmers experienced a decrease in their income. Although the project company gives support for their livelihoods, for example, providing fishing net as a part of corporate social responsibility (CSR); however, that cannot be an effective solution since the number of fish is decreasing. As the result, none of effective measures to improve or restore the living standards of affected residents have been taken.

The local residents have been worried that the construction and operation of Unit 2, which is larger in scale than Unit 1, would exacerbate the impact on their livelihoods. In fact, small-scale fishermen have already started suffering from adverse effects of the construction of the Unit 2's port and jetty facility. However, an appropriate impact assessment on livelihoods has not been made based on the environmental impact assessment (EIA), and effective measures to enable the local residents, who are engaging in small-scale fisheries, salt production, etc., to improve or at least restore their living standards have not been developed or implemented either. It is also pointed out that it is necessary to restore a healthy coastal ecosystem for fishing activities rather than implementing CSR program.

(2) Concerns about health effects of dust etc., and lack of use of the best available technology (BAT) in pollution control

— 2 items of non-compliance with EPs & IFC PSs/ 3 principles of non-compliance with UNGC/ 2 items of non-compliance with OECD guidelines

The local residents around the project site of Unit 1 point out that fly ash is coming from the chimney of the power plant to individual houses and elementary schools depending on the wind direction. According to the EIA regarding the Unit 2 project, it was acute upper respiratory tract infection (ISPA) that had the highest prevalence in the local residents of the survey area in the past three years (2012-2014). The residents are concerned that the construction and operation of Unit 2, the larger one than Unit 1, would increase the risk of respiratory diseases such as ISPA.

The air pollution prevention technology, i.e. BAT is not introduced in Unit 1, even though it has been available for several decades at coal-fired power plants built in Japan, and will not be used in Unit 2 either. The project company insists on its use of "clean coal technology"; however, Indonesia's standards are loose, and the governance doesn't work well – that allow the project company to push an export of pollution using a double standard in reality.

(3) Inadequate environmental impact assessment (EIA) and lack of adequate and sufficient public participation in its development process

— 19 items of non-compliance with EPs & IFC PSs/ 2 principles of non-compliance with UNGC/ 2 items of non-compliance with OECD guidelines

As for the EIA regarding the Unit 2 project (March 2016), it has been pointed out that the impact of land expropriation, the cumulative impact, the impact on livelihoods etc. have not been properly evaluated. The appropriateness of public participation and information disclosure in the process of developing the EIA was also questioned. Only selected people were invited to the consultations. Knowing about the consultations, small-scale fishermen, who hadn't been invited actually, participated in the consultations and expressed their concerns and opposition to the Unit 2 project; however, their voices were not incorporated into the EIA.

Furthermore, there was no prior consultation with the local residents on the EIA Addendum developed in July 2017 and on the new environmental permit issued on July 17, 2017.

(4) Environmental administrative lawsuit and illegality of the Unit 2 project
— 2 items of non-compliance with EPs & IFC PSs/ 1 item of non-compliance with OECD guidelines

In December 2016, six of the local residents filed a lawsuit against the West Java provincial government for illegally issuing an environmental permit (May 2016) for the Unit 2 project, and requested the cancellation of the environmental permit. In consequence, the district court decision on April 19, 2017 declared the environmental permit void for violating the Cirebon spatial plan. The banks that had entered into a loan agreement on April 18 without waiting for the district court decision of the next day, had to refrain from disbursing the loan for the Unit 2 project.

After that, the project company continued the construction of the Unit 2 based on the new environmental permit issued in July 2017. The banks also made an initial loan disbursement in November 2017, despite knowing that another lawsuit on the new permit would be filed.

On the other hand, the procedures regarding the issuance of the new environmental permit were carried out in a very non-transparent manner without letting the local residents know. On December 4, 2017, the local residents and NGOs re-initiated an administrative lawsuit to revoke the new environmental permit issued by the West Java provincial government. Although the district court, the high court, and the Supreme Court dismissed the plaintiffs' appeal in 2018, the local residents and NGOs requested a verdict review on the dismissal decision of the Supreme Court on August 6, 2019; therefore, the new environment permit is still subject to be against the law.

(5) Human rights violations against local residents who raise voices in opposition to the project
— 2 items of non-compliance with EPs & IFC PSs/ 2 principles of non-compliance

with UNGC/ 3 items of non-compliance with OECD guidelines

Human rights violations have been a concern for the local residents who have raised voices in opposition to the project, especially for plaintiffs in lawsuits. Between April 19, 2017 when the local residents won the lawsuit and December 4, 2017 when the administrative lawsuit to demand the cancellation of the new environmental permit was filed again, the original six plaintiffs got threatened from the project company, and thereby gave up filing a lawsuit as plaintiff again. In addition, the plaintiff for the second lawsuit has testified that he was being monitored by some entities. There have also been reports of overt threatening and surveillance by the police against the local residents who are demonstrating opposition to and taking action against the project.

This sort of series of threats and surveillance acts are a serious violation of human rights, bringing about anxiety and fear among other residents and preventing them from appropriate participation in the decision-making process of the project.

(6) Bribery case and corruption risks

— 2 items of non-compliance with EPs & IFC PSs/ 1 principle of non-compliance with UNGC/ 1 item of non-compliance with OECD guidelines

Since April 2019, allegations of bribery have been raised: a Korean company, Hyundai Engineering and Construction Co., Ltd. (HDEC), which is an EPC contractor for Unit 2, had provided a large amount of illegal money to the former Cirebon Regent. The Indonesian Corruption Eradication Commission (KPK) already announced the former Cirebon Regent as a suspect of money laundering, including bribery related to the Unit 2 project. And then, KPK has also identified Herry Jung, a former General Manager of HDEC, as a suspect of bribery related to the permission for the Unit 2 project. Currently, two former senior managements of the project company, including a former president director are prohibited to travel abroad.

While the future process of KPK's prosecutions and building cases is drawing more attention, it is a fact that should be already be taken seriously at this stage, that the project operators' and EPC contractor's involvement in alleged bribery and the way of doing it are clearly stated in details in the verdict document (May 2019) of another bribery case that the former Cirebon Regent was convicted, and that indeed the former Cirebon Regent and the former management of EPC contractor have been identified as suspects and the former senior management of the project company is under travel ban. In addition, the alleged bribery related to the Unit 2 project got questions at the national parliamentary audit of the Korean Parliament, and the senior executive of HDEC made an answer implying the flow of money related to land disputes.

(7) Impacts on climate change and going against the international trend of

divestment from coal

— 5 items of non-compliance with EPs & IFC PSs/ 3 principles of non-compliance with UNGC

Globally, since the adoption of the Paris Agreement in 2015, the sense of crisis about climate change has continued to rise. It has become an international common recognition that none of the construction of new coal-fired power plants should be allowed. Taking into account their impacts on climate change, major Western private banks have issued a policy of not lending to coal-related projects one after another, and the trend of divestment is surely expanding beyond the West.

On the other hand, the Japanese government has been the subject of international criticism because it has decided to provide public assistances through JBIC, etc., for eight new coal-fired power plant plans overseas even after the adoption of the Paris Agreement. Japanese private companies and banks have announced a new policy on financing for coal-fired power plants since 2018. However, its content follows the policy of the Japanese government with exception rules. Under the new policy, for example, banks will provide financing for coal plant if the recipient country asks for, and will adopt the OECD rule, which allows a so-called high efficient technology such as ultra-supercritical pressure – that is, it has not caught up with the global trend aiming at decarbonization.

Regarding the Cirebon Unit 2 project, in 2017, Credit Agricole, a major French bank decided to exit from the lender before the conclusion of the loan agreement because of its own policy change on climate change. Yet, the construction of Unit 2 is still in process without serious discussion by looking at climate change.

As discussed above, the banks should not have signed a loan agreement because the compliance with the EPs, UNGC, and OECD guidelines was not ensured as of April 18, 2017. The banks ought to carry out an appropriate due diligence prior to making any further loan disbursement, that is, it is necessary to carefully examine every issue on Unit 2 and contents of international norms to comply with.

The full report is available only in Japanese at: <https://fairfinance.jp/>

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