

ENERGY PROJECTS AND CORRUPTION IN GEORGIA



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Contents

Introduction	2
1. Peri – Company Profile	2
1.1 Peri Ltd	2
1.2 Companies, in which Peri Ltd owns shares	3
1.3 Companies affiliated to Peri Ltd	5
1.4 Peri Ltd and funding of the ruling political party	6
2. Hydro energy projects related to Peri Ltd	6
2.1 Kazbegi HPP on River Brolistskali (Khdistskali)	6
2.1.1 Terms of project implementation, licenses and permits	7
2.1.2 Purchase of generated electricity	8
2.1.3 Bank guarantee to ensure that the obligations are fulfilled	8
2.1.4 Penalties on Non-fulfillment of Obligations	11
2.1.5 Resolution 107 of the Government of Georgia dated April 18, 2008 and HPP planned on Khdistskali.....	11
2.1.6 Refusal by the competent authorities to issue a permit and subsequent amendments to privatization conditions and memorandum of understanding	12
2.1.7 Illegal construction of road in Brolistskali (Khdistskali) Gorge and inaction by public agencies	16
2.2 Dariali HPP on River Tergi	17
2.2.1 Increase of HPP capacity from 50 to 109 MW and respective doubtful circumstances	17
2.2.2 Project-related violations in the decision making process	18
2.2.3 The Parliament of Georgia – participant in a wrongdoing.....	19
2.2.4 Illegal construction and inaction by public agencies (Dariali and Larsi HPPs)	19
2.2.5 Court proceedings and newly detected wrongdoings	20
2.2.6 Appeal to the prosecutor’s office	21
2.3 Khadori-2 HPP project on River Alazani	22
List of boxes	
Box 1. Extracts from the letter by Lasha Iordanishvili and Lela Ioseliani dated May 29, 2012	6
Box 2. Extracts from the letter sent by Chairman of Kazbegi Municipality Sakrebulo dated May 29, 2012.....	7
Box 3. Extracts from the report dated October 2, 2010 prepared by Vakhtang Kikvadze, the head of Energy Department of the Ministry of Energy	12
Box 4. Short overview of public criticism voiced against HPP project planned on the River Brolistskali	13
Box 5. Extracts from the letter #2403 sent by Director of Kazbegi HPP Ltd, Giorgi Gogava to Minister of Energy and National Resources of Georgia on April 3, 2013.....	13
Box 6. Extracts from the report #4098 dated September 2, 2010 submitted to Energy Minister Alexander Khetaguri by Head of the Energy Department of the Ministry of Energy, Vakhtang Kikvadze	17
Box 7. Extracts from the report #334 dated February 3, 2011 submitted to Energy Minister Alexander Khetaguri by Head of the Energy Department of the Ministry of Energy, Vakhtang Kikvadze	17
Box 8. Extracts from application #2698 and motivation letter submitted by Ioseb Mchedlishvili, the director of Peri Ltd, to Deputy Minister of Environmental Protection and Natural Resources, Gocha Mamatsashvili on June 11, 2009	22

Introduction

One of the declared goals of the Georgian state policy is to ensure energy independence. To achieve this goal, the country is striving for maximum utilization of the existing energy potential; hydro energy is in the focus of attention. The new Georgian government, which came to power as a result of the 2012 parliamentary elections, like its predecessor, is carrying out an intensive campaign to attract investments to hydro energy projects. According to the data of the Georgian Energy Ministry, presently up to 30 hydro energy projects are being implemented in the country (construction of a part of hydropower plants has already been launched, while the other part is at the stage of planning); over 20 memorandums of understanding and/or agreements have been signed between the Georgian Government and Georgian or foreign companies (consortiums) on the projects of construction, operation and ownership of small, medium and large hydro power plants (hereinafter – HPP(s)).

Corruption can be detected in energy sector by different forms and at different levels. It may cover both petty corruption, for example, when paying electricity bills by citizens, or in case of elite corruption, when, for example, special conditions are created for this or that company in exchange of a particular benefit (for example, financing political campaign or simply making certain persons rich). The opportunities for elite corruption are especially high, when the legislation is weak, when the process of signing agreements between public agencies and companies, as well as the process of issuing licenses and permits by competent authorities is closed for the public, or when law enforcement and monitoring is weak. Unfortunately, exactly these conditions are presently observed in Georgia.

In the present publication, we tried to highlight those conditions, which create a fruitful ground for the development of corruption in energy sector. For this purpose, we have selected one company and energy projects related to it. After example of this company, we tried to demonstrate how institutional weakness and bias, as well as lack of transparency can promote corruption.

Thus, in the first chapter of the present publication, readers will get acquainted with the company Peri as well as the companies and individuals affiliated to it; the second chapter discusses some hydro power projects and the special conditions in which these projects are being developed.

1. Peri – Company Profile

1.1 Peri Ltd¹

The company Peri² is a limited liability company that was founded in 1991. In August 1996, by the moment of its registration in business registry, Peri had 11 founders. All the founders, except one, owned a small share in the company (1-5%); the greatest share – 64% - was owned by **Ioseb Mchedlishvili**; the same person served as CEO of the company. The first changes in the founders' shares were made in 1998. In 1998-2007 four shareholders gave up their shares in favor of Ioseb Mchedlishvili. In 2012-2013, the latter received the shares from five more shareholders. Thus, as of today, the greatest share in the company – 96% - is owned by Ioseb Mchedlishvili, while a 4% share is owned by **Kakhaber Shevardnadze**. Mchedlishvili presently holds the position of the company's chief executive officer. The company also has the director (chief manager). This position has been held by **Merab Iordanishvili** since 2005.

According to the information posted on the company's website³, *“main activities of Peri Ltd are focused on the range of construction and installation works for engineering projects throughout Georgia, including area with complex terrain conditions. Our services comprise construction of roads, hydro-technical structures, tunnels, office and accommodation buildings, etc. Also, we have experience in implementing all phases of the hydropower construction projects, including design, construction, procurement and operation”*.

In 1996 the company's authorized capital was USD 1 000; in 2004 it increased up to GEL 400 000 and in 2005 – decreased to GEL 2 000. According to the Registry of Entrepreneur and Non-entrepreneur (non-commercial) Legal Entities (hereinafter - Registry) (the company's identification code: 211352187), as of October 29, 2013, the company is a debtor to TBC Bank. It has pledged a tunnel boring machine, the company's 30% share in Energy Ltd (a 70% share of the second owner of Energy Ltd, Mevlud Bliadze has also been pledged), as well as existing and future non-material property of Energy Ltd (see next subchapter “Energy” Ltd). Peri has also concluded leasing agreements on movable property with TBC Bank (2011, 2012).

In May 2012, Peri company became the winner in one of the nominations of Mercury Business Awards 2012 – it was recognized as Business of the Year; the President of Georgia personally handed over the award to the company⁴.

¹ Identification code in the Registry of Entrepreneur and Non-entrepreneur (non-commercial) Legal Entities: 211352187

² The company's website: <http://peri.ge/>

³ <http://www.peri.ge/index1.php?menuid=2&lang=1>

⁴ According to the information posted on the website of the Ministry of Economy and Sustainable Development, Mercury is a joint initiative of the Ministry of Economy and Sustainable Development, Georgian National Investment Agency and Georgian Chamber of Commerce. According to the Ministry, “the aim of the event is to promote and popularize Georgian businesses. Its aim is to develop new initiatives, innovative ideas and expand the area of activities on the example of previous successes. Moreover, the aim of the award is to introduce emerging small and medium businesses to the society. Receiving “Mercury” would serve them as a great stimulus. It is remarkable that the national award gained great popularity and trust among leading companies in just a year from its foundation and became one the most prestigious contests in Georgia. “Mercury” became an exemplary prize for successful businesses. The first Mercury 2012 – National Business Award was held in 2011. <http://economy.ge/en/media/news/quotmercury-2012quot->

According to the information posted on the company's website, "the company began introduction of the ISO 9001:2000 Quality Management System International Standard from early 2007 that completed in September 2007 with Peri Ltd. certification and the company was granted ISO 9001:2008 International Quality Certificate". "During its activities the company gives preference to introduction of modern technologies and putting them in practice. The company pays special attention to the issues of quality assurance and occupational safety⁵".

1.2 Companies, in which Peri Ltd owns shares

- **Energy Ltd⁶**

The company was founded in September 2010. A share of **Peri Ltd** in the company (CEO Merab Iordanishvili) is 30%; the remaining 70% is owned by **Mevlud Bliadze**. Gaioz Ugrelidze is the director of the company. The company is registered (legal address) at the area owned by Peri Ltd (owner and director **Lasha Iordanishvili**).

At the moment of its foundation the company's authorized capital was GEL 2 000. As already mentioned above, the company has pledged the shares of both owners (Peri Ltd 30% and Mevlud Bliadze's 70% shares) at TBC Bank, as well as existing and future non-material property. According to the pledge agreement posted on the website of the Registry⁷, "all and any equipment of Larsi HPP to be purchased by Energy Ltd in future and/or to be handed over to it in future, including derivation pipeline and aggregate, also any movable and non-material property to be purchased in future, any movable property and/or material property, the right to ownership on which will be granted after signing this agreement, including all the equipment of 19 MW Larsi HPP, derivation pipelines and aggregates have been pledged at USD 30 million.

As it turns out from the registry, the company has concluded an agreement with Bank Republic in 2011 on deposit insurance liability. The subject of the agreement is a mortgagor's redemption right from the deposited sum at USD 1 200 000.

Presently, Energy Ltd is building a 19-megawatt **Larsi HPP** in the Dariali Gorge of Kazbegi municipality. The project is being implemented under the memorandum of understanding on construction, operation and ownership signed between the Government of Georgia, Electric System Commercial Operator (ESCO) and Energy Ltd on May 17, 2011.

In July 2012 Energy Ltd concluded a memorandum of understanding with the Government of Georgia on construction, operation and ownership of another HPP. This is a 5MW **Shilda HPP** in Kvareli municipality, on the River Chelti⁸. According to the project documents, initially the project was implemented by JSC GGEDC⁹ – a company established by Georgian Oil and Gas Corporation (with 100% ownership of the corporation), while HPP design and construction was carried out by Peri Ltd¹⁰. Based on the memorandum, Energy Ltd continued the project implementation launched by JSC GGEDC in July 2012. In September 2012, by presidential decree, certain land plots, Saguramo-Tsiteli Khidi 972-meter trunk gas pipeline as well as Chelti riverbed lands (for a term of 99 years) were handed over to Energy Ltd for project needs. Shilda HPP was put in operation in September 2012¹¹.

- **JSC Dariali Energy¹²**

Dariali Energy Ltd was founded in December 2010. It had two founding partners: U.S.-registered **Robbins Company¹³** – with a 30% share and **Peri Ltd** – with a 70% share. Dariali Energy Ltd, as well as Energy Ltd was registered (legal address) at the area owned by Peri Ltd (owner and director Lasha Iordanishvili). **Lasha Iordanishvili** was appointed the director of the company.

The company was established to build, develop and operate **Dariali HPP** on the River Tergi in Kazbegi municipality. To develop Dariali HPP project, on May 19, 2011 the Government of Georgia, Dariali Energy Ltd, Energotrans Ltd and Electric System Commercial Operator signed an agreement on building, operation and ownership of 109 MW Dariali HPP¹⁴.

In September 2011 the company decided to reorganize itself into a joint stock company. By that period, the company's capital amounted to USD 100 000, which later increased up to USD 33 333 333. 30% of shares were still owned by Peri Ltd, while 30% - by Robbins Company. In September 2011 the company's shares were redistributed - a new shareholder appeared in the person of **JSC**

⁵ It should be noted that a month after being recognized as Business of the Year, in June 2012, according to media reports, an accident occurred in Ganmukhuri, where the company Peri was carrying out construction works. A worker died as a result of the accident that happened during installation of Anaklia-Ganmukhuri central water system. According to the source, the workers connect the accident with accelerated works (TV 9 "Accident", 28.06.12: http://www.youtube.com/watch?v=BBg_xsleLks). We have no information about the results of the investigation.

⁶ Identification code in the Registry: 401950037

⁷ Pledge agreement #12312353214; #12312353436; #12312353330; creditor TBC Bank; mortgagor Energy Ltd, Peri Ltd, Mevlud Bliadze; July 19, 2012

⁸ Memorandum of understanding concluded between the Government of Georgia, Electric System Commercial Operator (ESCO) and Energy Ltd on July 13, 2012; apparent volume of investment USD 5 500 000.

⁹ Georgian Green Energy Development Company (GGEDC) underwent reorganization in September 2012; it merged with JSC Georgian Energy Development Fund (in 2010 – director Archil Mamatelashvili; in 2013 – director Giorgi Bezhuashvili).

¹⁰ <http://www.gogc.ge/ge/page/mdinare-celtze-hidroeleqtrosadguris-proeqtireba-mseneblobas-sps-quotferiquot-ganaxorcieles>

¹¹ Energy Minister Kakha Kaladze and CEO of the company Peri, Lasha Iordanishvili opened Shilda HPP. http://energyplatform.ge/show_news.php?id_news=47

¹² Identification code in the Registry: 401953061

¹³ See the company's website <http://www.therobbinscompany.com/>

¹⁴ As of October 31, 2013, the agreement was amended three times: firstly – on November 18, 2011; secondly – on February 13, 2012 and thirdly – on August 24, 2012. As a result of the second amendment, the HPP capacity was reduced by 1 megawatt (to 108 MW capacity).

Georgian Energy Development Fund (GEDF), which purchased 30% of the company's shares at USD 10 million. As a result, a share of the company Peri in the capital decreased to 40%, while Robbins Company retained the same share – 30%. In October 2011, Zurab Alavidze replaced Lasha Iordanishvili on the post of the director¹⁵.

As already mentioned above, the company is implementing the project on construction of Dariali HPP in Kazbegi municipality. In August 2013 JSC Dariali Energy said that because of financial problems, project development faced a threat and project completion might be postponed for an indefinite period. In a letter sent to Georgian Energy Minister Kakha Kaladze¹⁶ on August 14, 2013, the company offered the minister the following solution:

“Bank financing is needed to complete the project over which the company has been in talks with Georgian and international financial institutions. As a precondition for granting a loan, the banks demand the company to attract additional capital worth USD 20 million. JSC Dariali Energy raised relevant resources – Energy Ltd is ready to transfer USD 10 million to the company's capital as well as to allocate additional USD 10 million to the company in a form of shareholder loan with interest rate at 10% per annum. In exchange, Energy Ltd demands to have an option of buying the shares owned by Georgian Energy Development Fund (hereinafter GEDF) at USD 15 million after putting the HPP in operation. At this moment, JSC Dariali Energy has no other option to raise additional USD 20 million.”

By its letter, JSC Dariali Energy demands consent for GEDF to sign the document envisaging the increase in the capital of JSC Dariali Energy and getting a loan¹⁷. On October 1, 2013 the Government of Georgia met the above mentioned requirement – a governmental decree was issued, which approved the draft agreement on placement of shares and shareholders¹⁸.

- **Eastern Energy Corporation Ltd¹⁹**

Eastern Energy Corporation was founded in 1999 with the participation of three partners: Sichuan Electric Power Import and Export Corporation – 54%; corporation Hainan S.I.T Enterprise – 39% and Peri Ltd – 7%. The company was focused on development and implementation of **Khadori HPP** project. Eventually, Hainan S.I.T Enterprise gave up its share in the company and finally, since 2004 the shares have been distributed as follows: 93% is owned by **Sichuan Electric Power Import and Export Corporation (China)** and 7% - by **Peri Ltd**.

At the moment of its foundation, the company's authorized capital was USD 54 980, while in 2004 it exceeded USD 5.5 million. The Chinese company deposited money to increase the authorized capital, while Peri Ltd handed over to the company a mini HPP located near Khadori HPP. According to the information posted on the website of the Registry, as of October 2013, the company's shareholders have a dispute at Tbilisi City Court. Because of this dispute, the court ruled to impose a lien on the share (93%) of Sichuan Electric Power Import and Export Corporation. On October 1, 2013 the parties to the dispute agreed that Peri Ltd will withdraw its lawsuit and demand removal of a lien, while the Chinese party will purchase a 7% share of Peri Ltd at USD 1 900 000 until December 31. After meeting these requirements, the Chinese company pledges to give Peri Ltd the right to transmit electricity generated by Khadori 2 HPP through its own power transmission line for a term of 10 years and at a preferential rate of USD 50 thousand.

- **Kazbegi HPP Ltd²⁰**

Peri Ltd purchased Kazbegi HPP Ltd owned by Kazbegi municipality at GEL 200 000 through direct selling in August 2011²¹. By the moment of privatization, Kazbegi HPP Ltd owned a small 0.38-megawatt HPP – Kazbegi HPP located on the River Brolistskali (Khdistskali) in Kazbegi Municipality. Shortly after purchasing the company, in April 2012, Peri Ltd sold its 100% share to individual persons – **Lasha Iordanishvili** (66.67%) and **Lela Ioseliani** (33.33%). It should be noted that according to share purchase agreement, payment of the cost of 33.33% share was imposed not on Lela Ioseliani, who was defined as buyer in the agreement, but on **Ioseb Mchedlishvili** – co-owner of Peri Ltd (see above)²² and this latter agreed to fulfill this obligation. The company has replaced its directors for already three times: from the moment of privatization till August 24, 2012, the director of the company was **Giorgi Pitshelauri**; he was later replaced by **Irakli Shengelia**; in June 2013 this latter was replaced by **Giorgi Gogua**.

The key privatization condition was to increase the capacity of a HPP owned by Kazbegi HPP Ltd up to 2.5MW; however, later this condition was changed and the company was instructed to build a new, at least 5MW **Kazbegi HPP** on the same river.

As of October 21, 2013, according to the Registry, tax lien has been imposed on the shares of the both owners (on the entire property, except of several immovable items).

¹⁵ Since 2005 Zurab Alavidze held the position of Deputy Director General of VTB Bank; in 2009-2010 he was Deputy Economy Minister.

¹⁶ Letter #5374 sent by Dariali Energy to Georgian Energy Minister Kakha Kaladze on August 14, 2013

¹⁷ Letters from one of the Austrian banks as well as on loan conditions from the Bank of Georgia are attached to the letter. The Bank of Georgia notes in its letter that it demands the company to increase its authorized capital by USD 20 million as a precondition for issuing a USD 61 million loan.

¹⁸ Decree #1415 of the Government of Georgia dated October 1, 2013 on the agreement to be signed between PERI Ltd, Robbins Company, Georgian Energy Development Fund, Energy Ltd and JSC Dariali Energy.

¹⁹ Identification code in the Registry: 211390387

²⁰ Identification code in the Registry: 241495422

²¹ On the basis of presidential decree #15/08/07 dated August 15, 2011 and purchase agreement signed with Kazbegi municipality on August 16, 2011

²² See the share purchase agreement dated April 11, 2012 between PERI Ltd (represented by its director, Merab Iordanishvili), Lela Ioseliani and Lasha Iordanishvili

1.3 Companies affiliated to Peri Ltd

- **Landsvirkjun Power**

Landsvirkjun Power is a state-owned company based in Iceland²³, which has apparently been operating in Georgia since 2010. According to the information posted on the company's website²⁴, in 2010 Landsvirkjun Power signed a contract with the United Nations Development Programme (UNDP) in Georgia for provision of consulting services for the UNDP/Global Energy Fund Project: Georgia - Promoting the Use of Renewable Energy Resources for Local Energy Supply. According to the same report, the work was publicly tendered in January and Landsvirkjun Power in cooperation with the Icelandic consulting firm VERKIS and some Georgian partners was the successful bidder. USD 1 million contract involved rehabilitation of 3 hydroelectric power plants in Georgia, ranging in size from 2.0-6,5 MW, and development of pre-feasibility studies for 4 additional small hydroelectric projects. According to the information posted on the company's website in November 2011²⁵, one of three HPPs designed for rehabilitation was **Khadori-2 HPP** (see subchapter 2.3). Apparently, the agreement between Peri Ltd and the company Landsvirkjun Power was concluded within the framework of this project.

Cooperation between Peri Ltd and the company Landsvirkjun Power continued within the framework of other projects too. According to another information (dated July 20, 2011) posted on the company's website²⁶, Landsvirkjun Power and Verkis signed a contract with **Dariali Energy Ltd** on the feasibility study, tender design and preparation of tender documents and detail design of the 109 MW Dariali hydroelectric project. The company also notes that Landsvirkjun Power and Verkis have additionally concluded a sub-consultancy agreement with the local engineering company, **Peri Ltd**. Geological explorations will be executed by **Geoengineering Ltd.** and topographical survey and mapping by **Geographic Ltd.**, both of Tbilisi.

The cooperation between Icelandic companies and Georgian companies continued within the framework of another project: construction of **20 and 25 MW HPPs on the River Machakhela**. According to the information posted on the website of Landsvirkjun Power²⁷, Landsvirkjun Power and Verkis Consulting Engineers signed an engineering consultancy agreement with the Georgian company **Machakhela HPP-1 LLC**. According to contracts Landsvirkjun Power and Verkis are to conduct site investigations, prepare a feasibility study, followed by initial project design, preparation of tender documents for construction work and detail design of civil works. Like in case of Dariali HPP project, the company notes that Landsvirkjun Power also concluded sub-consultancy agreements with **Peri Ltd**, **Geoengineering** and **Geographic**.

- **Scientific-research firm Gamma**

Scientific-research firm Gamma is a consultancy providing different services including carrying out environmental impact assessments for various projects. Gamma Consulting, as it is referred to frequently, is the author of environmental impact assessment (EIA) of **Dariali HPP** project. Gamma Consulting has also prepared a revised version of EIA report on **Kazbegi HPP** project planned by Kazbegi HPP Ltd on the River Brolitskali (Khdistskali) (after the initial EIA report submitted by the company was rejected by the Ministry of Environmental Protection). According to media reports, cooperation between Gamma Consulting and Peri Ltd was established in frames of **Poti Municipal Water Supply Project**²⁸.

- **Tbiltskalgeo**

As of July 20, 2000, Tbiltskalgeo was a legal entity of public law²⁹. The company's current legal status is unclear. Upon the contract with Energy Ltd, Tbiltskalgeo carried out environmental impact assessment of **Larsi HPP** project; the same organization has prepared the initial version of EIA report on **Kazbegi HPP** project planned by Kazbegi HPP Ltd on the River Brolistskali (Khdistskali) (this version was rejected by the Ministry of Environmental Protection – it did not issue a positive conclusion of ecological expertise).

- **Energo-Aragvi Ltd**

The majority of HPPs are being developed in Mtskheta-Mtianeti region by Peri Ltd and the companies affiliated to it. The only exception is an 8-megawatt **Aragvi HPP** project on the River Tergi, implemented by Energo-Aragvi Ltd. However, according to media reports, **Peri Ltd** is involved in this project too. In this particular case, it is carrying out construction works upon the instructions of Energo-Aragvi Ltd³⁰.

²³ The company's website <http://www.landsvirkjun.com/company>

²⁴ See: <http://www.lvpower.com/News/Article/landsvirkjunpowersignsacontractwithundpingeorgia/>

²⁵ UNDP Georgia extends contract with Landsvirkjun Power, 8.11.2011, <http://www.lvpower.is/about/news/nr/163>

²⁶ Landsvirkjun Power and Verkis sign a contract on design of a 109 MW hydropower project in the Republic of Georgia, 20 July 2011, <http://www.landsvirkjun.com/company/mediacentre/news/news-read/1442->

²⁷ Landsvirkjun Power and Verkis sign an engineering consultancy agreement with Machakhela HPP 1 LLC, 17 August 2012, <http://www.landsvirkjun.com/company/mediacentre/news/news-read/1632->

²⁸ Akhali Gazeti; Maia Metskhvarishvili, 08.09.2009 "27 Millions in Troubled Waters" http://regions.ge/8&newsid=1873&year=2009&position=news_main

²⁹ Order #43 by the Minister of Urbanization and Construction of Georgia dated July 20, 2000 "On a legal entity of public law Tbiltskalgeo" https://matsne.gov.ge/index.php?option=com_idmssearch&view=docView&id=51244#

³⁰ Sakinformi; HPP Construction Launched on the River Aragvi; August 2, 2012; http://saqinform.ge/index.php?option=com_content&view=article&id=11072:2012-08-02-08-54-35&catid=99:actual1&Itemid=419#axzz2jrxq4508

1.4 Peri Ltd and funding of the ruling political party

During the 2010 local elections Georgian legislation did not ban making donations by companies in favor of political parties. It should be noted that during those elections **Peri Ltd** was among the companies having donated money to the United National Movement. On February 19, 2010 the company donated GEL 50 000 to the ruling party³¹.

During the 2012 parliamentary elections, Georgian legislation already banned political parties to receive any donations from the companies. Individual persons were allowed to donate maximum GEL 60 000 per year. According to the data on political party donations³², among the UNM donators there were persons associated with Peri Ltd and the companies affiliated to it, including **Zurab Alavidze**, director of JSC Dariali Energy – he donated GEL 35 000 to the ruling party on July 30, 2012; **Lasha Iordanishvili**, former director of JSC Dariali Energy, co-owner of Kazbegi HPP Ltd – he donated GEL 40 000 to the ruling party on July 10, 2012; on the same day **Ioseb Mchedlishvili**, owner of a 96% share in Peri Ltd, donated maximum amount, GEL 60 thousand to the United National Movement.

2. Hydro energy projects related to Peri Ltd

2.1 Kazbegi HPP on River Brolistskali (Khdistskali)

On the basis of presidential decree #15/08/07 dated August 15, 2011³³ and purchase agreement concluded with Kazbegi Municipality on August 16 2011, Peri Ltd purchased 100% share of Kazbegi HPP Ltd owned by Kazbegi municipality at GEL 200 000 through direct selling. By the moment of privatization, Kazbegi HPP Ltd owned a small 0.38-megawatt HPP – Kazbegi HPP located on the River Brolistskali (Khdistskali) in Kazbegi Municipality³⁴.

Under privatization conditions set by presidential order (as well as by the agreement), the company undertook:

- To pay a privatization sum within a month after signing the purchase agreement;
- To increase the capacity of HPP owned by Kazbegi HPP Ltd up to 2.5MW within 25 months and put it in operation;
- To transfer within 25 months those land plots to Kazbegi municipality out of the lands owned by Kazbegi HPP Ltd, which did not represent a necessary area for HPP operation.

Besides the above mentioned, the privatization agreement set the following conditions:

- The company should confirm its obligation on HPP capacity increasing and putting it in operation by an audit conclusion (the agreement lists 11 organizations out of which the company can select one);
- Due to failure by the company to increase HPP capacity within the established timeframes and to put it in operation, a GEL 500 penalty will be imposed on the company, from the day of violation, per each overdue day;
- Similar sanctions are envisaged for violation of the agreement on transfer of land plots;
- To meet the requirement of paying a penalty in case of failure to increase HPP capacity and put it in operation, the company provided an unconditional bank guarantee (valid during the term of the agreement and the term of validity of the agreement is also specified there – 24 months after signing the agreement).

Almost eight months after buying Kazbegi HPP Ltd, on April 11, 2012, Peri Ltd sold its 100% share to individual persons – Lasha Iordanishvili (66.67%) and Lela Ioseliani (33.33%).

In about a month and a half after selling the share, on May 29, 2012, the owners of Kazbegi HPP Ltd applied to Chairman of Kazbegi Municipality Sakrebulo Gocha Malania and demanded changes to the agreement³⁵. They explained the necessity and nature of changes only in two sentences (see box 1):

Box 1. Extracts from the letter by Lasha Iordanishvili and Lela Ioseliani dated May 29, 2012

“After we purchased Kazbegi HPP Ltd and respectively undertook the fulfillment of all obligations under the agreement signed between Peri Ltd and you, we learnt that River Brolistskali, on which Kazbegi HPP is located, has more hydro potential than 2.5MW.

Hence, we request you to change the privatization condition in order to build a new 5-6MW HPP instead of planned 2.5MW power plant. All other conditions will remain unchanged”.

³¹ See: <http://liberali.ge/mg-100-000-kombiteki-100-000-tbili-sakhli-100-000-sasursato-kombinati-100-000-mit-ana-100-000-lari>

³² See the website of the United National Movement: <http://unm.ge/index.php?m=137>

³³ Presidential decree #15/08/07 dated August 15, 2011 on privatization of 100% share of Kazbegi HPP owned by Kazbegi municipality through direct selling to Peri Ltd.

³⁴ Electric System Commercial Operator (ESCO) website: http://www.esco.ge/index.php?article_id=18&clang=0

³⁵ Letter #133 sent by Lasha Iordanishvili and Lela Ioseliani to Gocha Malania on May 29, 2012.

These two sentences proved enough for the Chairman of Sakrebulo to apply to Minister of Economy and Sustainable Development, Vera Kobalia on the same day, May 29 2012, without any further discussions or requesting additional information, and to offer changes to the relevant presidential decree, in line with the requirements of Kazbegi HPP Ltd. Below there is an extract, where Gocha Malania offers the Minister the text of amendments to be made to the presidential decree (see box 2).

As it seems, these two sentences proved enough for the Ministry of Economy and Sustainable Development to make a decision and five days later, an amendment³⁶ was made to presidential decree #15/08/07 dated August 15, 2011 – privatization condition was amended in line with the requirements of the owners of Kazbegi HPP Ltd: instead of increasing the capacity of already privatized HPP, the company was demanded to build and put in operation no less than 5-megawatt HPP on the River Brolistskali (the term of fulfillment of obligations remained unchanged – 24 months).

Box 2. Extracts from the letter sent by Chairman of Kazbegi Municipality Sakrebulo dated May 29, 2012

“Kazbegi municipality has received a joint letter from Lasha Iordanishvili and Lela Ioseliani dated May 28, 2012, where they raise the issue of making amendments to the above mentioned agreement. In particular, since the River Brolistskali, on which Kazbegi HPP is located, has more potential than 2.5MW, it is expedient to change the condition indicated in subparagraph “b”, paragraph 2 of the presidential decree and amend the formulation “to increase the capacity of HPP owned by Kazbegi HPP Ltd up to 2.5MW within a term of 24 months after signing the relevant agreement” by the following wording: “To build and put in operation a HPP with the capacity of no less than 5MW within 24 months after signing the relevant agreement.”

After amending the presidential decree, the process of amendments moved to Kazbegi and just a day after amending the decree, on June 5, 2012, relevant amendment was made to the purchase agreement between Kazbegi municipality and Peri Ltd in 2011³⁷. It should be noted that while the entire process was launched by sending a brief letter by the owners of Kazbegi HPP Ltd to the Chairman of Kazbegi Municipality Sakrebulo, in the agreement signed on June 5, 2012, the parties note when substantiating the need for changes, that they guided themselves by the presidential decree.

Hence, without any substantiation and calculation of any positive or negative consequences and in order to satisfy the desire of the owners of Kazbegi HPP Ltd, various governmental structures made a decision within a week about construction of a new, at least 5-megawatt HPP on the River Brolistskali.

When making similar decisions (construction of new HPPs is meant), current legislation envisages conclusion of a memorandum of understanding between the Government of Georgia and an investor³⁸. Thus, in this particular case, a month after the above mentioned processes, on July 13, 2012 a memorandum of understanding was signed between the Government of Georgia, Electric System Commercial Operator (ESCO) and Kazbegi HPP Ltd.

Below we discuss some important conditions set by the memorandum of understanding, privatization agreement and presidential decree; this report also provides a brief overview of how the company was meeting its commitments and how the relevant agencies were reacting.

2.1.1 Terms of project implementation, licenses and permits

The memorandum of understanding, along with the capacity (no less than 5 megawatts) defined the location of a new HPP (1570 – 1300m point) and timeframes for the beginning and completion of construction (October 10, 2012 – August 16, 2013).

The company was given about 10 months to build a HPP, while only three months were defined by the parties (government and company) to obtain necessary permits for launching the construction. At the same time, under the memorandum, the Government of Georgia committed itself to assist the company as much as possible in project implementation in terms of obtaining relevant permits and licenses (paragraph 3.5 of the memorandum).

Setting the timeframes for launching the construction and promising to assist in obtaining permits and licenses creates a conflict of interests to both the Government of Georgia and its subordinate agencies that are in charge of issuing licenses and permits. Setting such conditions by the memorandum is nothing but emphasizing again that the decision on HPP construction has already been made and the state agencies simply need to implement it through issuing licenses and permits (the possibility of refusal to issue licenses and permits is not even discussed).

³⁶ Presidential decree #04/06/02 dated June 4, 2012 on privatization of 100% share of Kazbegi HPP owned by Kazbegi municipality through direct selling to Peri Ltd.

³⁷ Agreement dated June 5, 2012 on making amendments to the purchase agreement dated August 16, 2011 between Kazbegi municipality and Peri Ltd.

³⁸ The only statutory act establishing special regulations with regard to MoUs with the Georgian government on construction of power stations and giving explanation to “memorandum” is Resolution of the Government of Georgia # 107 of 18 April 2008 on Approval of the national programme “Renewable energy 2008” – regulation for construction of new renewable energy sources in Georgia. Although resolution #107 does not apply to all memorandums and agreements on construction of power plants (the resolution sets certain exceptions), most of the already signed memorandums reiterate the conditions of model MoU defined by the resolution (however, there are some, which set quite different conditions). For additional information, please view “Memorandums of Understanding and Agreements Concluded for Implementation of Energy Projects in Georgia. Legal Analysis” (December, 2012). The publication is available at www.greenalt.org

2.1.2 Purchase of generated electricity

“To ensure power supply in the country,” according to paragraph 3.3 of the memorandum, the company shall be obliged during 10 years after putting the HPP into operation, annually, during three months (November, December, January) to sell entire electricity generated by HPP to Georgian energy system for domestic consumption.

In addition, the subsequent paragraph (3.4) of the memorandum sets additional conditions – under this paragraph, the company shall be obliged, during 10 years after putting the HPP into operation, to sell entire electricity generated by HPP to ESCO. The memorandum also defines electricity price (from October through March – 6.5 cents; from April through September – 5 cents) and sanction (paragraph 3.4.1) in case if the company does not sell electricity to ESCO (the company shall be obliged to pay USD 0.1 per kilowatt of electricity that has been generated (or has not been generated through the fault of the company) and has not been sold to ESCO.

It is absurd but fact that paragraph 3.4.2 of the memorandum completely releases the company from these obligations (except of an obligation related to compulsory sale of electricity during three winter months). According to paragraph 3.4.2, the company has the right, through submitting a written notification to the government and ESCO, to refuse fulfillment of its obligation and not to assume any responsibility for it. With the exception of a three-month period, the company is free in selecting electricity buyer “both on local and foreign markets” (paragraph 3.4.3).

An obligation, which can be rejected anytime, without any substantiation, and non-fulfillment of which does not entail any sanctions, cannot naturally be discussed as an obligation.

It should be noted that similar pseudo-obligation is envisaged by the memorandum of understanding signed with Energy Ltd (30% of the company’s shares are owned by Peri Ltd) on **Larsi HPP** project – this “obligation” appeared in the memorandum as a result of amendments made on July 13, 2012; as well as by the memorandum of understanding signed with Energy Ltd on **Shilda HPP** project on the same day, July 13, 2012.

2.1.3 Bank guarantee to ensure that the obligations are fulfilled

The memorandum of understanding does not envisage an obligation for submitting bank guarantee to fulfill the obligations defined by the memorandum. However, submitting bank guarantee is envisaged by the purchase agreement on current small HPP existing on the River Brolistskali; as already mentioned above, the purchase agreement envisages submission of a USD 200 thousand unconditional bank guarantee. Since the obligation for increasing the HPP capacity was replaced in the purchase agreement by the obligation for building and putting into operation a new 5MW HPP, we can suppose that the construction of a new HPP is provided on the River Brolistskali just with the USD 200 thousand bank guarantee (naturally, this bank guarantee cannot apply to other obligations envisaged by the memorandum).

When discussing the issue of submitting bank guarantee, it is important to briefly review the practice used in this sphere as well as legal requirements. In 2012, Green Alternative provided legal analysis of 15 memorandums of understanding concluded between the Government of Georgia and different companies in 2007-2011 on construction and operation of power plants³⁹. Out of these 15 memorandums of understanding, seven envisage submitting of a bank guarantee and eight do not⁴⁰. The table below provide information about 15 memorandums of understanding: second column of the table gives the name of a company with whom a memorandum had been concluded and the date of concluding this memorandum; the third column provides the subject of memorandums – power plants and their capacities (as defined by the memorandums); the fourth column provides apparent amount of investment as defined by the memorandums; the last column provides the amount of bank guarantees defined by the memorandums and their percentage ratio to apparent amount of investment⁴¹.

³⁹ Memorandums of Understanding and Agreements Concluded for Implementation of Energy Projects in Georgia. Legal Analysis” (December, 2012). www.greenalt.org

⁴⁰ An obligation for submitting bank guarantee was imposed in one of the mentioned eight memorandums later (see table below).

⁴¹ Out of the memorandums listed in the table below, only the first indicates exact percentage ratio of bank guarantee to apparent amount of investment.

Table 1. Some memorandums of understanding concluded between the Government of Georgia and the companies on power plants in 2007-2011.

#	Company and date of signing a memorandum of understanding	Power plant and installed capacity (MW)	Apparent amount of investment	Bank guarantee amount and percentage ratio to apparent amount of investment
1	Adjara Energy 2007 Ltd (February 28, 2008)	Kintrisha HPP (7.50) Kobuleti I HPP (13.30) Kobuleti II HPP (14.30) Kirnati HPP (14.40) Khelvachauri HPP (22.40) Chorokhi I-II HPPs (48.00)	USD 167 860 000	USD 5 035 800 3 %
2	Bakhvi Hidro Power Ltd (May 14, 2009)	Bakhvi III HPP (6)	USD 9 700 000	USD 1 020 000 Approximately 10 %
3	JSC Caucasus Energy and Infrastructure (November 24, 2008)	Mtkvari HPP (28)	USD 50 000 000	USD 4 760 000 ოდ Approximately 9%
4	Energo Aragvi Ltd (2007; exact date is unknown)	HPP cascade in the Tetri Aragvi river gorge, in the north from the village of Zemo Mleti (8)	Not ascertained ⁴²	Not requested ²
5	Georgian Investment Group Energy Ltd (September 15, 2009)	Khobi HPP-2 (25) Khobi HPP-3 (11)	USD 64 000 000	Not requested
6	Nurol Energy Production and Marketing Inc., Korea Electric Power Corporation, SK Engineering and Construction Co., Ltd (December 8, 2009)	Khoneti HPP (100) Namakhvani HPP (250) Tvishi HPP (100)	USD 1 000 000 000	Not requested
7	Rusmetal Ltd (July 27, 2009)	Lukhuni 1 (10.8) Lukhuni 2 (12) Lukhuni 3 (7.5)	From USD 39 000 000 to USD 51 000 000	Not requested
8	Zoti Hydro Ltd (May 28, 2009)	Zoti HPP (36) Kvirila HPP (5.20)	From USD 78 000 000 to USD 92 000 000	Not requested
9	Georgian Railway Construction Ltd (June 11, 2010)	Nenskra HPP	Not ascertained	Not requested
10	Kolin Construction, Tourism, Industry and Trading Co, Inc (November 10, 2010)	Nobulevi HPP (25.70) Tskhimra HPP (32.00) Erjia HPP (27.00) Lechakha HPP (21)	USD 150 000 000	By preconstruction period – USD 2 000 000 Approximately 1% By construction period USD 10 000 000 Approximately 7% The possibility of submitting additional bank guarantee is envisaged, but it should not exceed total of USD 20 million, approximately 13%
11	UNAL INSAAT VE TICARET AS (December 28, 2010)	Khunevi HPP (11.00)	USD 19 780 000	USD 1 921 000 Approximately 10%

⁴² Ascertained in four years after signing the memorandum, on September 15, 2011 (amendments were made to the memorandum). Apparent investment amount was set at USD 8 million.

⁴³ Under the amendments made to the memorandum on September 15, 2011, the company was instructed to submit a 1 million bank guarantee amounting to 12.5% of apparent investment amount.

#	Company and date of signing a memorandum of understanding	Power plant and installed capacity (MW)	Apparent amount of investment	Bank guarantee amount and percentage ratio to apparent amount of investment
12	JSC Energo-Pro Georgia (February 15, 2011)	Alpana HPP (71) Sadmeli HPP (97)	USD 305 000 000	Not requested
13	Optimum Enerji Uretim A.S. (February 19, 2011)	Arakali HPP (11) Abuli HPP (20) Akhalkalaki HPP (15)	USD 90 000 000	USD 9 080 000 Approximately 10%
14	Energy Ltd (May 17, 2011)	Larsi HPP (20.00)	USD 20 000 000	3 400 000 Approximately 17%
15	Wind Energy Investment (May 23, 2011)	Wind power plant in the area adjacent to Paravani Lake (50)	USD 70 000 000	Not requested

As seen from the above table, the amount of government-requested bank guarantees is ranging from 3% to 17%; in some cases the companies are not at all requested to submit bank guarantees to ensure the fulfillment of their obligations. In case of Kazbegi HPP Ltd, an apparent amount of investment is USD 3 million (under the memorandum of understanding), while the amount of requested bank guarantee is USD 200 thousand (under the purchase agreement) that is about 7% of the apparent amount of investment.

The analysis of memorandums does not show any pattern that would have justified the correctness of the amount of bank guarantees demanded from various companies and refusal to demand submitting bank guarantees at all. The issue of “selective” demand of bank guarantees should become a subject of investigation by law enforcement agencies. Furthermore, in case of the memorandums listed in the above table (like in case of Kazbegi HPP), only those liabilities are secured by bank guarantees, which the companies have undertaken with respect to construction and operation of HPPs, while no bank guarantees are provided for those liabilities, which are related to the sale of electricity generated during operation of HPPs for Georgia’s internal needs, during a three-month period.

As far as the legislation is concerned, the method of defining a bank guarantee and the rule of its submission upon signing a memorandum of understanding on construction, operation and ownership of HPPs is defined by the national programme “Renewable energy 2008” – regulation for construction of new renewable energy sources in Georgia” approved by Resolution of the Government of Georgia #107 of 18 April 2008⁴⁴. According to this regulation, “to ensure that the HPP is built and put into operation in due terms,” the company has to submit a bank guarantee worth USD 170 thousand or EUR 120 thousand per megawatt, according to the installed capacity of a HPP. It should be noted that this and other rules set by the regulation do not apply to all HPPs; a number of exceptions (under paragraphs 23, 23² and 24 – mostly on the basis of plant capacity) and the possibility of making amendments to a draft model memorandum are also envisaged (paragraph 6).

The above mentioned regulation is imperfect, including in terms of information availability and transparency of decision-making process; moreover, it contains a number of controversial norms. Despite it, **if the Georgian government/Ministry of Energy had applied the rules set by the regulation to the HPP planned on the River Khdistskali⁴⁵, the amount of a bank guarantee to be submitted by Kazbegi HPP Ltd would have been much higher than it has now. In this case, instead of USD 200 thousand, the company would have been requested to submit a USD 850 thousand bank guarantee.**

Another circumstance is also quite interesting with respect to bank guarantees: the regulation approved by Resolution #107 of the Government of Georgia dated April 18, 2008 envisages a possibility of gradual reduction of a bank guarantee submitted by a company. It should be noted that this possibility has been used three times with respect to **Energy Ltd** (the company’s 30% share is owned by Peri Ltd), which is building a 19MW **Larsi HPP** in Dariali Gorge. In particular, the company’s USD 3 400 000 bank guarantee was first reduced on May 11, 2012 to USD 2 034 600; secondly – on December 21, 2012, to USD 1 430 000 and thirdly – on May 2, 2013, to USD 575 000⁴⁶.

⁴⁴ On August 21, 2013 the Government of Georgia approved by its decree #2013 “The rule of expression of interests on technical-economic study of the construction, construction, ownership and operation of HPPs in Georgia.” This new rule does not apply to the memorandums of understanding concluded before the new rule entered into force.

⁴⁵ This is envisaged by paragraph 23¹ and its subparagraph “a” of the regulation, according to which if a person plans to study the expedience of construction of such HPP, which is not included in the list of potential sources of renewable energy, he is obliged to notify the Georgian Government and the Ministry of Energy about it in writing. In addition, if the capacity of this HPP does not exceed 100MW, the Government of Georgia is authorized to include it in the list of potential sources of renewable energy.

⁴⁶ See the memorandum of understanding concluded on Larsi HPP and its amendments <http://www.energy.gov.ge/4421>

2.1.4 Penalties on Non-fulfillment of Obligations

We believe that one more issue concerning the fulfillment of obligations defined by the memorandum of understanding on construction, operation and ownership of HPPs should become a subject of investigation by relevant bodies.

As already mentioned above, practice of requesting bank guarantees is varying from project to project; in addition, the practice of using selective approach towards various companies is quite clear. As it seems, the Ministry of Energy/the Government of Georgia had a selective approach towards using the issue of penalties for non-fulfillment of obligations. In particular, no fines have been imposed for non-fulfillment of obligations in any of the cases described in the above table, with the exception of two memorandums signed with Kolin Construction, Tourism, Industry and Trading Co, Inc (2010, total of 105MW) and Optimum Enerji Uretim A.S. (2011, 11MW). Under these memorandums, the companies are obliged to pay quite strict fines (if we give due consideration to the fact that other companies do not have to pay any fines at all) for the non-fulfillment of obligations on obtaining of permits, launching and completion of construction, putting HPP in operation. For example, the two companies have to pay USD 1000 per overdue day from the 1st to 30th day; USD 2 000 – from the 31st to 60th day and so on. After the 150th overdue day, the fine increases up to USD 45 thousand per overdue day.

As far as Kazbegi HPP Ltd is concerned, in this case the issue of imposing penalties for non-fulfillment of obligations is regulated not by the memorandum of understanding but by the purchase agreement (amount of bank guarantee, as already mentioned above). Under this agreement, the company is obliged to pay only GEL 500 for non-fulfillment of construction and operation obligations per overdue day. In addition, the company has to pay the same amount under the same scheme in case if it violates the second obligation defined by the agreement on transferring land areas to Kazbegi municipality.

2.1.5 Resolution 107 of the Government of Georgia dated April 18, 2008 and HPP planned on Khdistskali

Another important circumstance should be noted concerning the issue of applying the regulation approved by Resolution #107 of April 18, 2008 to the HPP planned on the River Khdistskali.

Paragraph 3 of the regulation approved by the Government's resolution 107 obliges the Ministry of Energy to ascertain "the list of potential sources of renewable energy." By including the HPP in the list, the state declares that it is interested in attracting investment, under the conditions set by the regulation, for the construction and operation of this HPP. Paragraph 3 also defines that the list may periodically undergo certain changes – the Ministry of Energy can revise it; however, the regulation says nothing about which particular circumstances can serve as the ground for changing the list.

The practice of making amendments to the list looks as follows: over 40 amendments have been made to the list since the day of approval of the regulation; as a rule, the amendments have the following nature – the capacity of HPP/HPPs (apparent capacity) is changed; a new HPP/HPPs are added to the list or already existing HPP/HPPs are removed from the list; there were multiple cases, when HPPs were included in the list, then removed and later re-introduced in the list. The list is changed by orders of the Energy Minister, while the orders are usually based on the reports from the ministry's staff explaining the necessity for making certain changes to the list.

Upon its request, Green Alternative received from the Ministry of Energy the copies of amendments made to the list until now as well as the copies of reports explaining these amendments. As it turned out, in 2010 the construction of a HPP with apparent 9.3MW installed capacity on the River Khdistskali was added to the list of planned HPPs; however, later the HPP was removed from the list. The details of this fact are given below:

By order #10 of the Minister of Energy dated February 17, 2010, several HPPs to be built in Kazbegi municipality were added to the list, including a HPP planned on the River Khdistskali with the following characteristics: installed capacity – 9.3MW; average annual electricity generation – 41.14m kWh. This ministerial order was issued on the basis of a report prepared by Head of the Energy Department of the Ministry of Energy, Vakhtang Kikvadze on February 15, 2010. The report reads that Gross Energy Ltd⁴⁷ studied the issue and ascertained the possibilities of construction of new potential HPPs, including the possibility of construction of HPP with the above mentioned characteristics on the River Khdistskali. Just on the basis of this study, the author of the report recommends the Minister to add the HPP to the list.

Eight months after the HPP planned on the River Khdistskali was added to the list, the minister issued a new order (#54 dated October 12, 2010) under which the HPP was removed from the list. The report prepared by the Head of Energy Department of the Energy Ministry on October 2, 2010 explains the need for removal of HPP from the list by the following reasons:

⁴⁷ The company Gross Energy, with the financial support of U.S. Agency for International Development (USAID/Winrock International) was involved in identification of potential HPPs and preparation of investment proposals. In addition, on the basis of investment proposals, the company created a mathematical model of company rankings as well as a database of perspective hydropower facilities of the Ministry of Energy of Georgia. See the company's website <http://www.gegroup.org/index.php?m=780>

“...The Ministry of Environmental Protection and Natural Resources and its agencies were constantly expressing concerns about the location of potential HPPs, particularly about intercrossing between potential HPPs and protected areas, nature reserves, national parks, mineral waters, various deposits that hampered us from approving the coordinates and obstructed our relations with investors.

To discuss this issue and settle the problems as much as possible... several consultations were held with the Ministry of Environmental Protection, the National Environmental Agency and the Agency of Protected Areas.

In the process of consultations, upon our request Gross Energy Ltd revised a number of problematic HPPs posted on the website of the Energy Ministry; schemes were corrected as much possible and certain problems related to a number of HPPs were removed. Out of the corrected HPPs, some underwent changes in their schemes without changing their capacity; others underwent changes in the key technical-economic parameters and respectively, it triggered changes in their capacities; it became necessary to remove from as well as to add several HPPs to the list... Below we present a list of those HPPs that underwent various changes...

3. The following HPPs need to be removed or added to the list:

...

- To be removed: Khdistskali – 9.3MW HPP, as its construction is planned on the territories of Kazbegi National Park and planned protected areas.”

Thus, according to the above extracts, the HPP planned on the River Khdistskali was removed from the list of potential renewable energy sources already in 2010 because of its conjunction with the existing and planned protected areas.

The above mentioned circumstances raise two important issues, which, in our opinion, should become a subject of intra-agency investigation or probably be investigated by law enforcement agencies. In particular:

1. If the construction of HPP on Khdistskali was not considered expedient in 2010 because of its conjunction with the existing and planned areas, what has changed in 2012? What was the reason for satisfying unconditionally the demand of the owners of Kazbegi HPP Ltd about changing the privatization conditions, without any environmental assessments (concerning the construction of a new HPP, instead of increasing the existing capacity)? Why were not consultations held with the Ministry of Environmental Protection in 2012, as it happened in 2010⁴⁸?
2. Why was not the planned HPP included in the list of potential renewable energy sources and respectively, why did not the rule defined by the Georgian Government’s Resolution #107 apply to the company after the owners of Kazbegi HPP Ltd expressed their interest to construct a new HPP on Khdistskali (both the legislation and existing practice enabled to do so)?

2.1.6 Refusal by the competent authorities to issue a permit and subsequent amendments to privatization conditions and memorandum of understanding

The privatization agreement and the memorandum of understanding define the conditions of investment project, as well as apparent capacity of a new facility (no less than a 5MW capacity HPP). To implement the project, the company has to obtain necessary permits from competent authorities. In order to build a new HPP on the River Khdistskali, the company should prepare all necessary documents envisaged by law and carry out environmental impact assessment of the planned HPP project (to prepare EIA report). Finally, based on these documents, the company should obtain construction permit from the Kazbegi Municipality Sakrebulo as well as a positive conclusion of ecological expertise from the Ministry of Environment and Natural Resources Protection of Georgia⁴⁹.

In late 2012 and early 2013 Kazbegi HPP Ltd tried to obtain construction permit and respectively, a conclusion of ecological expertise, but in vain. The company submitted a very poor quality environmental impact assessment report (actually prepared within two weeks) for obtaining the necessary permit documents. This circumstance (the report did not meet legal requirements), as well as serious public criticism and protest voiced against the project (see box 4 below) prompted competent authorities to reject the project implementation: owing to the reasons provided in conclusion #11 of ecological expertise dated March 18, 2013, the Ministry of Environmental Protection did not issue a positive conclusion of ecological expertise concerning the EIA report on construction and operation of 6MW HPP on the River Brolistskali by Kazbegi HPP Ltd⁵⁰. On March 21, 2013 the Chairman of Kazbegi

⁴⁸ As known, in 2010 the Ministry of Environmental Protection developed a draft law on natural monuments, under which Khde Gorge, along with other objects, was expected to be granted a status of natural monument. Reportedly, during the inter-agency discussion of the draft law, the Ministry of Energy spared no efforts to reduce the list of about 100 potential natural monuments to 14. Along with other objects, Khde Gorge was also removed from the list of potential natural monuments.

⁴⁹ According to current legal framework (established along with the enforcement of the Law on Licenses and Permits in 2005), the Ministry of Environment and Natural Resources Protection issues an environmental impact permit on the basis of a conclusion of ecological expertise in case if a company does not need a construction permit to launch its activities (for example, in case of reconstruction of the existing facility, changing its capacity, its technical re-equipment, etc.). If construction permit is needed to launch the activities (for example, construction and operation of a new facility), then the Ministry of Environment and Natural Resources Protection issues only a conclusion of ecological expertise, which is a component of construction permit and becomes its condition (in this case, a conclusion of ecological expertise is practically its permit document, which is “integrated” into another permit document – construction permit).

⁵⁰ Conclusion #11 of ecological expertise dated March 18, 2013 issued by the Ministry of Environment Protection on construction and exploitation of HPP (6MW Kazbegi HPP) on the River Brolistskali.

Municipality Sakrebulo did not issue construction permit (second stage of issuing construction permit)⁵¹.

Box 4. Short overview of public criticism voiced against HPP project planned on the River Brolistskali

The project on construction of 6MW capacity HPP on the River Brolistskali met fierce criticism from the society, including environmental non-governmental organizations, geology and hydrology experts, alpinists, part of local population and simply, interested citizens; public protest was mostly focused on three issues described below:

1. **Project design:** According to the design offered by Kazbegi HPP Ltd, the project envisaged redirecting 90% of the river into a pressure pipeline and remaining 10% of average annual sanitary flow. The project's EIA report did not contain any hydrological data; neither did it study and substantiate what particular impact it might have and whether 10% of average annual flow would be enough for the river ecosystem, generally, and particularly, for fauna, including fish, dependent on the River Brolistskali.
2. **Project implementation in Khda Gorge:** Khda Gorge, the project-affected area, is a habitat for lots of rare and endangered species, which are protected by national and international laws. In addition, as far back as the Soviet period, Khda Gorge was granted a status of natural monument and was included in Georgia's Red Book. In 2006, over 180 Caucasian experts recognized the gorge as a part of Priority Conservation Area of the Caucasian ecoregion. The government also planned to adopt a law on creation and management of natural monuments, where the status of natural monument should have been granted to Khda Gorge again. The EIA report submitted by Kazbegi HPP Ltd did not assess adequately the scales and quality of project impacts on the landscape and habitats in Khda Gorge, as well as the project impact on the Kazbegi National Park and the perspectives of its expansion.
3. **Project need and potential social-economic benefits:** EIA report did not provide any assessments or substantiation of the necessity for project implementation, as well as any goals or alternatives to achieve these goals. Neither did the report analyze social-economic factors, including the project impacts on tourist-recreation potential of Khda Gorge; no economic analysis had been conducted that would have ascertained a potential harm caused to tourism and recreation sector.

Naturally, the company could not have started project implementation without obtaining the relevant right (construction permit and conclusion of ecological expertise). Under the presidential decree, it would have led to violation of the terms defined by privatization agreement and memorandum of understanding: under the memorandum of understanding, the construction should have been launched on October 10, 2012 and completed (according to the same document as well as under the presidential decree and purchase agreement) on August 16, 2013. Thus, shortly after receiving negative answers from competent authorities, Kazbegi HPP Ltd started to lobby for making changes to all the above mentioned documents.

On April 3, 2013, Kazbegi HPP Ltd sent two, actually similar letters to the Minister of Energy and Natural Resources⁵². In one letter the company requests changing of the privatization condition (set by the presidential decree and privatization agreement concluded with Kazbegi Municipality), and in the other – changing of the conditions set by the memorandum of understanding concerning the terms of completion of construction and putting HPP into operation. In particular, the company requests to postpone the fulfillment of its obligation for a year – until August 16, 2014. It is quite interesting in the both letters how the company justifies the need for postponing its obligation and how public agencies respond to the company's request.

In the both letters, the company explains that it has done huge work and defrayed huge expenses to meet legal requirements, but the competent authorities did not issue necessary permit documents. The company accuses the competent authorities – Kazbegi Municipality Sakrebulo and the Ministry of Environmental Protection – for violating the decision making deadlines. In addition, the company justifies its failure to meet the deadlines by the circumstances that the conclusion of ecological expertise issued by the Ministry of Environmental Protection contains such remarks, which the Ministry had not voiced earlier, at the stage of public discussions. Thus, the company notes: *"Giving due consideration to the position of the Ministry of Environmental Protection, it became necessary to prepare a new EIA report taking into consideration all the remarks expressed in the conclusion of ecological expertise issued by the Ministry of Environmental Protection in order to obtain a permit on construction of Kazbegi HPP. However, this requires much time (the entire procedure needs several months)".* Thus, based on the above mentioned circumstances (and taking into consideration the technological processes of construction – because of seasonal works), the company asserts that it is impossible to fulfill its obligations duly by reasons beyond its control and demands to postpone the deadline for completing the construction by one year. In the end of one of the letters, Director of Kazbegi HPP Ltd, Giorgi Gogava reminds the Ministry of Energy and Natural Resources that the government is obliged to assist a company in obtaining permits and licenses (see box 5 below).

Box 5. Extracts from the letter #2403 sent by Director of Kazbegi HPP Ltd, Giorgi Gogava to Minister of Energy and National Resources of Georgia on April 3, 2013

"It should be noted that pursuant to paragraph 3.5 of the memorandum, the government, under the rules set by Georgian legislation, should do its best within its competence to support the company in project implementation that may be connected to obtaining relevant permits and licenses."

⁵¹ Order #59 of the Chairman of Kazbegi Municipality Sakrebulo dated March 21, 2013 on rejecting the agreement with Kazbegi HPP Ltd on architectural project, construction and technological scheme at the second stage of issuing a permit on construction of 6MW Kazbegi HPP on the River Brolistskali (Khdistskali) in Kazbegi Municipality.

⁵² One letter (#2404) is undersigned by the company owners, Lasha Iordanishvili and Lela Ioseliani (the second addressee of this letter is the Ministry of Economy and Sustainable Development), while the second letter (#2403) is undersigned by Giorgi Gogava, the director of the company.

Shortly after the two letters were sent by Kazbegi HPP Ltd, relevant agencies (Ministry of Energy and Natural Resources⁵³, Chairman of Kazbegi Municipality Sakrebulo⁵⁴, National Agency of State Property Management and Ministry of Economy and Sustainable Development⁵⁵) satisfied the company's request without any explanations and remarks and postponed the obligation concerning HPP construction and operation till August 16, 2014: In April-May 2013, relevant acts were issued by the Government of Georgia⁵⁶ and the President of Georgia⁵⁷ (the amendments were made to the memorandum and presidential decree) and a bit later (in June 2013) the amendment was made to the privatization agreement too⁵⁸.

As mentioned above, the company explained its failure to fulfill its obligations by the reasons beyond its control. It should be noted that none of public agencies even tried to clarify whether the reasons for delay were really beyond the company's control. This, first of all, demonstrates unprofessional approach towards the issue and irrelevant approach towards the Ministry of Environmental Protection. While issuing relevant acts, in explanatory notes public agencies almost blindly repeat the reasons provided by the company, by this justifying the need for adopting these acts. Below there is a short overview of the reasons provided by Kazbegi HPP Ltd and those circumstances, which were not studied by public agencies.

The company's argument 1: The company carried out huge work and defrayed huge expenses to meet legal requirements, but competent authorities still did not issue necessary permit documents.

Probably the company had really done huge work and defrayed huge expenses, but it does not mean that this effort was efficient. It would be quite enough for public agencies to view one of the major documents related to the project – an introduction of EIA report – to make sure of inexpediency of the company's argument.

It appears from the introduction of EIA report that the scientific research institute Tbiltskalgeo, commissioned by Kazbegi HPP Ltd to carry out EIA study and prepare EIA report, conducted EIA study and prepared relevant report in a period between October 10, 2012 and November 1, 2012⁵⁹, i.e. within 21 days – in the best case and 15 days in the worst case (excluding weekends). And it happens when at least six months are needed to assess the environmental impact of similar HPPs⁶⁰.

It is absolutely unrealistic to carry out EIA study in such a short period of time and it definitely had been reflected on the quality of the report. The EIA report unveiled for public discussion on November 1, 2012 and the EIA report submitted for ecological expertise to the Ministry of Environmental Protection on February 5, 2013 actually do not differ from each other. It means that the company did not carry out additional studies and did not revise the report through taking into consideration all the remarks received during the stage of public discussions (see box 4 above). It submitted the same poor quality EIA report as during public discussions to obtain a permit. Therefore, no surprise that the conclusion of ecological expertise issued by the Ministry of Environmental Protection (dated March 18, 2013) lists 31 remarks (and numerous inaccuracies) concerning the fundamental issues of EIA report.

Thus, the company did not meet the requirements of Georgian legislation; it did not carry out those necessary studies, which would have enabled the Ministry of Environmental Protection to take an informed decision on the project. If the Ministry of Environmental Protection had issued a positive conclusion on the basis of poor quality and faulty EIA report, then the Ministry itself would have violated the requirements of law. Based on the decision of the Ministry of Environmental Protection and substantiation of the local administration of Kazbegi Municipality⁶¹, the Kazbegi Municipality decided to reject the proposed HPP project.

⁵³ Letter #03/1925 dated April 15, 2013; the same ministry was the author and initiator of draft decree #339 of the Government of Georgia dated April 25, 2013.

⁵⁴ Letter #34 dated April 15, 2013 sent by the Chairman of Kazbegi Municipality Sakrebulo to Deputy Minister of Energy and Natural Resources, Ilia Eloshvili. In the letter, the Chairman of Sakrebulo expresses readiness on behalf of Kazbegi Municipality to amend the privatization agreement and to postpone the fulfillment of obligation by the company till August 16, 2014. It should be noted that the Chairman of Sakrebulo sent this letter to the Deputy Minister of Energy and Natural Resources in response to the Deputy Minister's letter #03/1921 sent on the same day – 15.04. 2013. Furthermore, the chairman's letter was registered at the Ministry of Energy and Natural Resources on April 15, 2013.

⁵⁵ The first agency was the author of draft decree 379 of the Government of Georgia dated April 26, 2013; the second agency was its initiator.

⁵⁶ 1) Decree #339 of the Government of Georgia dated April 25, 2013 on making amendments to the memorandum of understanding concluded between the Government of Georgia, Electric System Commercial Operator and Kazbegi HPP Ltd on July 13, 2012; 2) Decree of the President #15/08/07 dated August 15, 2011 on making amendments to decree #379 of the Government of Georgia dated April 26, 2013 on privatization of 100% share of Kazbegi HPP owned by Kazbegi municipality through direct selling to Peri Ltd.

⁵⁷ Decree of the President #07/05/02 dated May 7, 2013 on making amendments to decree of the President #15/08/07 dated August 15, 2011 on privatization of 100% share of Kazbegi HPP owned by Kazbegi municipality through direct selling to Peri Ltd.

⁵⁸ The agreement dated June 18, 2013 on making amendments to the purchase agreement concluded between a self-governing unit, Kazbegi Municipality, and Peri Ltd on August 16, 2011.

⁵⁹ The introduction of the project's EIA report reads that under the agreement signed between the scientific research institute Tbiltskalgeo and Kazbegi HPP Ltd on October 10, 2012, the latter commissioned Tbiltskalgeo to carry out EIA study and prepare a report. Kazbegi HPP Ltd published an announcement about the availability of EIA report for public discussion in newspaper 24 Hours on November 1, 2012. Thus, it appears that the EIA report was prepared in a period between October 10 and November 1.

⁶⁰ Professor Michael McClain, UNESCO-IHE, Institute for Water Education Environmental flow assessment induction workshop October 2, 2013, Tbilisi, Georgia

⁶¹ Letter #265 of March 20, 2013 sent by the acting governor of Kazbegi Municipality; enclosed with this letter is a conclusion of the Service for Supervision on Spatial Arrangement, Architecture and Construction Activity of Kazbegi Municipality "On rejecting the agreement on architectural project, construction and technological scheme with Kazbegi HPP Ltd at the second stage of issuing a permit on construction of a 6MW capacity HPP on the River Broilistskali (Khdistskali) in Kazbegi Municipality".

The company's argument 2: Competent authorities made decisions on refusing permit issuance through violation of deadlines.

This argument is not true. Green Alternative applied to the Ministry of Environmental Protection and local administration of Kazbegi Municipality to specify the details related to the terms of decision making process. As it turned out, the both agencies made decisions within the established timeframes. Below there is a short description of decision making procedures:

Kazbegi HPP Ltd applied to Kazbegi Municipality Sakrebulo for making a second stage decision on issuing a construction permit (agreement on architectural project) on January 25, 2013. According to legislation, Kazbegi Municipality Sakrebulo had no more than 20 days to make a decision; the Ministry of Environmental Protection had the same terms to conduct ecological expertise and take a decision on issuing or rejecting a positive conclusion. Because of huge public interest towards the project, the Ministry of Environmental Protection (with observance of established terms) applied to the local administration of Kazbegi Municipality with a request to increase the term of administrative proceedings for three more months – this right was granted to it by the Law of Georgia on Licenses and Permits. On February 14, 2013, the 20th day of administrative proceeding, the Kazbegi Municipality satisfied the Ministry's request and made a decision on increasing the term of administrative proceeding for three more months⁶². The applicant, Kazbegi HPP Ltd was also notified about it. Finally, competent authorities made a decision (rejecting the project) much earlier than a three-month term expired (the Ministry of Environmental Protection – on March 18, 2013 and the Chairman of Kazbegi Municipality Sakrebulo – on March 21, 2013).

The company claims that the decision should have been made within a 20-day term allocated for administrative proceeding and not on February 14, but no later than February 14. Even if we admit that the competent authorities made a decision with violation, the company had two solutions, though it used none of them: 1. under law, if a competent authority fails to adopt a decision, a decision is automatically considered adopted in favor of an applicant (for example, a permit will be considered issued). If competent authorities had really violated the terms, Kazbegi HPP Ltd could have considered a positive conclusion of ecological expertise issued and architectural project agreed (second stage of issuing construction permit). This is how the company acted during the first stage of issuing construction permit, when Kazbegi Municipality violated the terms established by law – the company deemed the decision adopted⁶³ and moved to the second stage of obtaining a construction permit. 2. Kazbegi HPP Ltd could have appealed against 'illegal decision' in court; it had one month for it.

While the company accuses the competent authorities of making decisions through violation of terms, none of "broker" agencies (Ministry of Energy and Natural Resources, Ministry of Economy and Sustainable Development) tried to investigate whether or not the delay in fulfillment of obligations was the company's fault. To clarify it, the "broker" agencies simply had to read the memorandum of understanding and the project's EIA report.

According to the memorandum of understanding, the company should have launched construction on October 10, 2012, i.e. the company should have had a detailed design of HPP by that time; it should have conducted EIA study and obtained permit documents (construction permit and conclusion of ecological expertise). As it turned out, the company had not done any of the above mentioned works on October 10, 2012, to say nothing about obtaining permit documents. This becomes absolutely clear from the introduction of EIA report, which notes that the EIA study was conducted by scientific research institute Tbiltskalgeo under the agreement concluded between Tbiltskalgeo and Kazbegi HPP Ltd on October 10, 2012. Thus, it appears that Kazbegi HPP Ltd started conducting necessary research for obtaining a permit on the day, when under the memorandum, construction works should have started.

The company's argument 3: a conclusion of ecological expertise (refusal to project implementation) contains such remarks, which the Ministry of Environmental Protection had not made earlier, at the stage of public discussions.

This argument is absolutely inadequate to current situation. According to legislation, project initiator has to publish EIA report for public discussion and to organize public meetings before the launch of administrative proceeding. At this stage, through consultations with the society, the project initiator can receive remarks from the society and detect those problematic issues, which should be studied during EIA study. Under the law, the Ministry of Environmental Protection is not obliged to give remarks to the project initiator at this stage; however, the Ministry shows goodwill and in the period of public consultations it discusses EIA report and gives its remarks to the company. It has the only goal – to ensure that during formal administrative proceedings the project initiator (when it applies to competent authorities for obtaining a permit) submits better EIA report (if, of course, the company is willing to improve the report). Thus, the Ministry of Environmental Protection has no obligation to provide any remarks during the stage of public discussions.

The above mentioned proves that non-fulfillment of obligations by the company is not caused by the reasons, which are beyond the company's control. Because of non-fulfillment of obligations (the company had already violated the obligation related to the term of beginning the construction), the Government of Georgia, in line with the conditions set by the memorandum of understanding, could have terminated the memorandum and demanded the company to return the property transferred by the state for project

⁶² Order 32 of the Chairman of Kazbegi Municipality Sakrebulo dated February 14, 2013 on prolongation of the term of administrative proceeding on the second stage of issuing a permit for the construction of a 6 MW capacity Kazbegi HPP on the River Khdistskali (Brolistskali) in Kazbegi Municipality.

⁶³ During the first stage of issuing construction permit (approval of conditions for using land area for construction purposes), Kazbegi HPP Ltd considered the first stage decision automatically adopted (approved), because the Chairman of Kazbegi Municipality Sakrebulo made a decision on extending the administrative proceeding for a term of three months with violation of the terms defined by law (letter 2403 of April 3, 2013 sent by Kazbegi HPP Ltd to the Minister of Energy and Natural Resources).

purposes (paragraphs 5.2 and 5.3 of the memorandum). As it seems, the Government of Georgia/"broker" state agencies did not consider necessary to study the above mentioned circumstances or probably they studied them, but did not react appropriately and instead, satisfied the company's requirements without any objection – they postponed the term of fulfillment of obligations till August 16, 2014.

2.1.7 Illegal construction of road in Brolistskali (Khdistskali) Gorge and inaction by public agencies

On December 26, 2012 Green Alternative applied to the Minister of Environment Protection and asked to investigate the issue of legality of the road under construction in the River Brolistskali Gorge. Citing local population, Green Alternative supposed that Kazbegi HPP Ltd was building the road for the construction of a new HPP on the River Khdistskali. Since the company had not obtained necessary permit documents (construction permit, conclusion of ecological expertise) for the project implementation by then, the organization demanded to study the legality of road construction and to react appropriately in case of detecting any wrongdoing.

In response, the Ministry of Environmental Protection notified Green Alternative on January 23, 2013 that the Ministry's Inspection Department studied "actual state of road construction" on the ground and revealed that "no construction process was underway in the process of inspection." Thus, although the road actually was under construction, the Ministry of Environmental Protection did not or could not detect a wrongdoing only because it failed to witness the construction process during inspection.

With the above mentioned letter, the Ministry of Environmental Protection also informed Green Alternative that the organization's notification about possible illegal construction was sent to local administration of Kazbegi Municipality for further reaction. Thus, on March 6, 2013 Green Alternative applied to the local administration of Kazbegi Municipality and demanded access to investigation results and public information kept at the municipality concerning road construction. In response (March 11, 2013), the organization received only the copies of documents kept at the municipality, according to which:

On August 29, 2011 the company Peri applied to Chairman of Kazbegi Municipality Sakrebulo Gocha Malania and requested a permit to rehabilitate "a tractor road on the ground". The company explains this request in the following way: it reminds the Chairman of Sakrebulo about a privatization condition, according to which the company should increase the capacity of the existing privatized HPP up to 2.5MW. The company explains that stemming from this condition, it needed to rehabilitate the existing tractor road, "which would subsequently be used in the process of construction of headwork for a new HPP." It should be noted that the company explains the necessity for road rehabilitation by the need for construction of a new HPP and this happens when an obligation on construction of a new HPP appeared in the privatization agreement only on June 5, 2012 (almost after a year), to say nothing about the fact that the company (Kazbegi HPP Ltd) has not obtained any permit documents so far to build a new HPP.

More interesting is how the Kazbegi Municipality reacted on the company's request. Based on the documents provided by the company, on September 21, 2011 the Municipality issued a permit on road construction, though not for the needs of either HPP already existing on Khdistskali or planned HPP (as the company requested), but for the needs of absolutely another HPP – 109MW capacity Dariali HPP, which was under construction in Dariali Gorge⁶⁴.

It is beyond any doubts that the above mentioned represents a violation and should be investigated by law enforcement agencies.

⁶⁴ Order 177 of the Chairman of Kazbegi Municipality Sakrebulo dated September 21, 2011 concerning the agreement on project documents provided for the construction of road in Dariali Gorge of Kazbegi Municipality and issuing a construction permit; construction permit #23 issued by the Kazbegi Municipality Sakrebulo on September 21, 2011.

2.2 Dariali HPP on River Tergi

The Dariali HPP project envisages the construction of derivation type HPP with 109MW installed capacity on River Tergi in Dariali Gorge of Kazbegi Municipality, near the Georgian-Russian border. The HPP will join the grid by 110kw line, which connects Georgian and Russian grids. As already mentioned in the first chapter, the project is implemented by the company Dariali Energy. The project is implemented under the agreement signed between the Government of Georgia and Dariali Energy on May 19, 2011⁶⁵.

The project was subject to huge public criticism because of its design⁶⁶. The subchapters below review those violations, which accompanied the project planning and implementation.

2.2.1 Increase of HPP capacity from 50 to 109 MW and respective doubtful circumstances

As already mentioned when describing the case of HPP planned on Khdistskali, by Order #46 of the Minister of Energy dated April 23, 2008⁶⁷, a list of potential renewable energy sources has been approved. The list constantly undergoes certain changes – new HPPs are either added or removed from the list, or else their capacities are changed. Below we will focus on the amendments made to the list with respect to Dariali HPP.

According to the list approved on April 23, 2008, Dariali HPP will have installed capacity of 50 megawatts. By Order 10 of the Minister of Energy dated February 17, 2010, the apparent installed capacity of Dariali HPP increased up to 93 megawatts; this amendment was justified by “optimization of the scheme of river hydropower potential.” In a couple of months (on October 12, 2010) the installed capacity of Dariali HPP was increased up to 99.9 megawatts. This amendment was based on the report by the Head of Energy Department of the Ministry dated September 2, 2010, which notes the following (see box 6):

Box 6. Extracts from the report #4098 dated September 2, 2010 submitted to Energy Minister Alexander Khetaguri by Head of the Energy Department of the Ministry of Energy, Vakhtang Kikvadze

“The Ministry of Environmental Protection and Natural Resources and its agencies were constantly expressing concerns about the location of potential HPPs, particularly about intercrossing between potential HPPs and protected areas, nature reserves, national parks, mineral waters, various deposits that hampered us from approving the coordinates and obstructed our relations with investors...

Upon our request, Gross Energy Ltd revised a number of problematic HPPs posted on the website of the Energy Ministry; schemes were corrected as much possible and certain problems related to a number of HPPs were removed. Out of the corrected HPPs, some underwent changes in their schemes without changing their capacity; others underwent changes in the key technical-economic parameters and respectively, it triggered changes in their capacities...

Dariali – a part of the tunnel was passing through the territory of Kazbegi National Park and a part of HPP was crossing solid materials license facility; the scheme was changed and the capacity increased from 93MW to 99.9MW.”

A couple of months later, on February 3, 2011, the Head of the Energy Department again applied to the Energy Minister. This time he substantiates the necessity of removing Dariali HPP from the list and notes the following (see box 7):

Box 7. Extracts from the report #334 dated February 3, 2011 submitted to Energy Minister Alexander Khetaguri by Head of the Energy Department of the Ministry of Energy, Vakhtang Kikvadze

“The Ministry of Environmental Protection and Natural Resources and its agencies made remarks about the location of potential HPPs, particularly about intercrossing between potential HPPs and various protected areas, nature reserves, national parks, mineral water deposits and various engineering facilities and communications. Although the remarks were partially taken into consideration and the schemes and parameters of hydro power plans were changed, still there are certain objections on approving X, Y coordinates as well as in our relations with investors. Hence, in order to use the hydro potential of River Tergi basin as much as possible and to take all geological conditions into consideration, as well as to settle the above mentioned problems and further specify HPP schemes and parameters, we deem it expedient to remove the HPPs of Dariali Gorge from the list of potential HPPs approved by you, including Tergi, Dariali, Amali HPP, Chkheri HPP, Juta HPP, Snostskali, Kobi HPP, Truso HPP and Tsdo HPP.”

Despite it, Decree #549 of the Government of Georgia was issued on March 11, 2011, which approved the application submitted by Dariali Energy on the construction of Dariali HPP. Under the same decree, the Ministry of Energy was instructed to submit a draft memorandum of understanding within three months. On May 19, 2011 the Government of Georgia (Minister of Energy and Natural Resources signed it on behalf of the government), Dariali Energy Ltd, Energo Trans Ltd and Electric System Commercial Operator signed an agreement on the implementation of Dariali HPP project⁶⁸. According to this agreement, **installed capacity of Dariali HPP has been increased up to 109MW**. Let us focus on two important circumstances here:

⁶⁵ See the agreement and the amendments to it at the website of the Ministry of Energy <http://www.energy.gov.ge/4421>

⁶⁶ See Green Alternative, July 2012 “How Tergi River is Being Killed – Fact sheet about the Dariali HPP project”; available at www.greenalt.org

⁶⁷ Issued on the basis of the Georgian Government’s resolution 18.04.08 N107

⁶⁸ According to the information provided by the Ministry of Energy and Natural Resources (17.05.2012), the agreement has been prepared only in English and its Georgian copy is not available at the Ministry.

1. The agreement does not contain a clause emphasizing that the project area should not cover Kazbegi National Park, although Minister of Energy and Natural Resources, Alexander Khetaguri has been informed numerously about intercrossing of the territories of planned Dariali HPP and Kazbegi National Park. Despite it, the minister exceeded his powers and signed the agreement, envisaging illegal construction of HPP within the protected area.
2. Why was the capacity of planned HPP increased from 50 to 109 megawatts? In the interview with Green Alternative, energy specialists express serious doubts whether it is possible to generate 109 megawatts on River Tergi. It is difficult to discuss this issue with available information, but the question remains open, especially as there have been no data about hydrological monitoring on River Tergi since 1985. It should also be noted that in the interview with Liberali magazine, Director of Dariali Energy Zurab Alavidze said that the capacity was increased up to 109MW just upon the request from the Ministry of Energy; the company itself wanted to build a 70-megawatt HPP.

The fact is certain that the increase of capacity has yielded the following two results: (1) Dariali Energy was not demanded to submit a bank guarantee to ensure the fulfillment of contractual obligations. According to the legislation of that period, in case of construction of up to 100MW HPP, a company was obliged to submit a bank guarantee – USD 170 000 per megawatt. Thus, in case of 50MW, Dariali Energy would have to submit a bank guarantee at USD 8 500 000; 70MW – USD 11 900 000; 99.9MW – USD 16 983 000. If the planned capacity of HPP exceeded 100MW, the company would not be demanded to submit any bank guarantee. In addition, although the agreement envisages certain sanctions for violation of the terms of fulfillment of obligations by the company (maximum amount of fines is limited by USD 600 000), this obligation is not secured by bank guarantee or other security. (2) Twice and more increase of the capacity has significantly increased the project's impact on biodiversity.

2.2.2 Project-related violations in the decision-making process

On November 17, 2011, Dariali Energy Ltd submitted Environmental and Social Impact Assessment (ESIA) report on the project of Dariali HPP construction and operation to obtain a conclusion of ecological expertise necessary for project implementation. The process of making a decision on issuing a conclusion passed with significant violations; the conclusion was issued with violation of environmental legislation and procedural norms on public participation. Below there is a short description of these violations.

HPP Construction on Protected Area

The ESIA report submitted by Dariali Energy for ecological expertise clearly indicated that “according to HPP working draft design, diversion pipeline, sedimentation basin and entrance portal of diversion pipeline will be located in Kazbegi National Park traditional usage territory. Area of the mentioned communications and access roads will be 2.64 hectare.”

Since Georgian legislation prohibits the construction of a HPP on the territory of a protected area, particularly national parks⁶⁹, Dariali Energy was actually demanding a permit on committing a violation. Despite the above mentioned, instead of disapproving the project, the Ministry of Environmental Protection roughly violated the law and issued a positive conclusion of ecological expertise on the Dariali HPP project.

Violation of decision making procedures on issuing a conclusion of ecological expertise

On September 21, 2011 Green Alternative applied to the Ministry of Environmental Protection with a request to involve the organization in administrative proceedings on issuing a conclusion of ecological expertise concerning the Dariali HPP construction and operation project. The organization was requesting to have access to the copy of ESIA report upon its submission by the company to the Ministry as well as to be notified about the terms of launching administrative proceedings. In response, Green Alternative was assured that the Ministry would involve the organization in administrative proceedings⁷⁰.

Despite this promise, the Ministry made a decision on issuing a positive conclusion of ecological expertise on Dariali HPP project without involving Green Alternative in the decision making process; by this, the Ministry violated a number of requirements of Georgian legislation.

On November 28, 2011 Green Alternative received a letter from the Ministry of Environmental Protection dated November 18, 2011 (10 days after its sending), by which the organization was notified that the EIA report on 110MW Dariali HPP was submitted to the Ministry of Environmental Protection for obtaining a conclusion of ecological expertise. The Ministry did not provide a copy of the report, but indicated a website where the report was posted. Moreover, the Ministry notified Green Alternative about the date of launching an administrative proceeding (November 17, 2011), but did not indicate the date of its completion. On the same day of receiving the above mentioned notification, Green Alternative familiarized itself with the EIA report posted at www.aarhus.ge. The information about the terms of administrative proceedings was also indicated at the website. According to this source, administrative proceedings should have been held from November 17, 2011 till December 2, 2011.

⁶⁹ Article 5 and paragraph 4 of article 20 of the Law of Georgia on the System of Protected Areas

⁷⁰ Letter #132 of September 27, 2011 sent by Head of Public Relations Department of the Ministry of Environment Protection, Ekaterine Bendeliani to Association Green Alternative.

Despite a great volume of the document and limited terms, Green Alternative prepared its remarks and comments on the report practically in two days and submitted them to the Ministry of Environmental Protection on December 1, 2011 (on the last day of announced term of completion of administrative proceeding) with a request to take the organization's remarks into consideration in the decision making process. As it appeared later, the Ministry of Environmental Protection made a decision on issuing a positive conclusion on November 28, 2011 – before the announced date (December 2) and particularly on the day, when Green Alternative received a notification on launching administrative proceedings and availability of the report. Thus, the Ministry of Environmental Protection violated Georgian legislation, including a number of requirements of the Aarhus Convention on ensuring public participation in the process of making environmental decisions.

2.2.3 The Parliament of Georgia – participant in a wrongdoing

“To rectify” an obvious wrongdoing committed by the Ministry of Environmental Protection by allowing the construction of Dariali HPP on the protected area, the Parliament of Georgia amended the law later thus becoming a participant in the wrongdoing. The situation has developed as follows:

In February 2012 information was posted on the website of the Parliament's NGO Liaison Office, according to which the Government submitted a bill on making amendments to the Law of Georgia on the Status of Protected Areas to the Parliament of Georgia. According to the bill, the area of Kazbegi National Park was planned to be reduced by 8.7737 hectares. According to the explanatory note of the bill, its adoption became necessary for promotion of implementation of hydro power project on the territory adjacent to Kazbegi National Park;” while its goal was “to remove a status of a protected area from those areas allocated for HPPs under construction, which fall under the territory of Kazbegi National Park.”

As a result of analyzing the bill it was ascertained that it contradicted a number of requirements defined by Georgian legislation; in particular, 1) territorial reduction of a protected area (national park) is possible only in special cases defined by law; HPP construction does not belong to this category. Thus, it was illegal to reduce the territory of national park with the purpose of promoting the implementation of hydropower project; 2) Georgian legislation clearly defines the agency (Ministry of Environmental Protection of Georgia), which is authorized to submit a proposal to the Parliament of Georgia on territorial reduction of protected area. It was obvious from the explanatory note of the bill that the author was the Ministry of Energy and Natural Resources, rather than the Ministry of Environmental Protection. Thus, in this case too, it was quite obvious that legal requirements were violated; 3) it was clear from the explanatory note that the requirements of the Georgian Law on the System of Protected Areas as well the Aarhus Convention were violated when developing the bill – the society was not given an opportunity to participate in the process of developing the bill.

Besides the above mentioned, the bill envisages the removal of the status of a protected area from 8.7737 ha included in Kazbegi National Park for HPP needs, whereas in the EIA report on Dariali HPP approved by the Ministry of Environmental Protection, this area was much less (2.64 ha). Thus, it was unclear what calculations were made in the bill and what was the purpose of offering the removal of a status from the remaining 6.1337 ha.

Green Alternative notified the Parliament of Georgia, including the Parliament Speaker, Vice Speakers, chairmen and deputy chairmen of parliamentary committees and factions, about the above mentioned circumstances at the stage of discussing the bill by the legislative body. The organization was demanding the Parliament to suspend the discussion as well as to probe into illegal actions committed by the Ministry of Environmental Protection and take relevant measures.

Unfortunately, none of these persons reacted on the organization's appeal and did not suspend the process. On March 13, 2012 the Parliament adopted an amendment under which the area was removed from Kazbegi National Park. Moreover, without any substantiation, the Parliament, instead of 2.64 ha needed for the construction of Dariali HPP, removed the area of 20.3633 ha from the Kazbegi National Park – much more than envisaged by the bill initially (8.7737 ha).

After the law was adopted, Green Alternative again applied to the parliamentary committee for environment protection and natural resources to substantiate the adopted amendments and to study illegal actions committed by the Ministry of Environmental Protection, but the committee did not respond to the request.

2.2.4 Illegal construction and inaction by public agencies (Dariali and Larsi HPPs)

On September 2011 the Mtskheta-Mtianeti Information Center published information about launching the implementation of Dariali HPP project. The Director General of Dariali Energy confirmed that the construction has really been launched, according to the Information Center. Since the company had not obtained necessary permit documents to launch the construction, referring to this information by the Information Center, Green Alternative applied to the Ministry of Environmental Protection⁷¹ and demanded to investigate the legality of works ongoing on the project territory as well as to take relevant measures in case of detecting any wrongdoings. In response, Green Alternative was assured that it would receive information about the legality of ongoing works

⁷¹ Letter #04/06-38 sent by Green Alternative to Minister of Environment Protection Goga Khachidze on September 15, 2011.

after the planned inspection⁷². Almost a month and a half after the promise was given, Green Alternative applied to the Ministry of Environmental Protection again and requested information about the response measures. The Ministry answered that by that period Dariali Energy had already obtained a conclusion of ecological expertise necessary for the project implementation. Thus, the Ministry of Environmental Protection did not react on the notification about the fact of wrongdoing; moreover, it rapidly issued a permit document (conclusion of ecological expertise) thus trying to return illegal construction to legal frameworks.

Besides the Ministry of Environmental Protection, Green Alternative also notified the Ministry of Energy and Natural Resources about illegal construction (because one of its departments was in charge of monitoring environmental issues) and asked the latter

to investigate the legality of ongoing construction⁷³. A month after notification, the organization received an answer, according to which the letter has been sent to the relevant regional unit (Agency of Natural Resources) of the Ministry for the purpose of taking relevant measures. A month after this response, like in case of the Ministry of Environmental Protection, Green Alternative requested information about the implemented measures. Finally, two months after initial notification, the organization received an answer from First Deputy Minister of Energy and Natural Resources, Mariam Valishvili⁷⁴. It appeared that like the Ministry of Environmental Protection, this agency did not react on the notification either. The latter told the applicant, that the company had already obtained all necessary permit documents.

Both the Ministry of Environmental Protection and the Ministry of Energy and Natural Resources were obliged to suspend illegal construction and react in line with the requirements of the Code of Administrative Offences and/or the Criminal Code of Georgia. However, they both contributed to illegal activities carried out by Dariali Energy.

Like Dariali HPP, the construction of **Larsi HPP** also started illegally, before permit documents (conclusion of ecological expertise, construction permit) were obtained by Energy Ltd. Like in case of Dariali HPP, in October 2011 Green Alternative applied to the both ministries – the Ministry of Environmental Protection and the Ministry of Energy and Natural Resources – with a request to study the legality of works ongoing on the Larsi HPP project area. The both ministries sent so called “intermediate” response and ultimately, the issue was forgotten at all.

2.2.5 Court proceedings and newly detected wrongdoings

As already mentioned above, the Ministry of Environmental Protection did not let Green Alternative participate in the process of making a decision on issuing a conclusion of ecological expertise concerning the Dariali HPP project. By this the Ministry violated the requirements of the General Administrative Code of Georgia and the Aarhus Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matters. Thus, on January 30, 2012 Green Alternative filed a lawsuit in Tbilisi City Court and demanded cancelation of that order by the minister, which approved the decision adopted through violation.

In addition, it turned out in February 2012 that by the above mentioned order the Ministry of Environmental Protection issued a conclusion of ecological expertise on the project, which envisaged the use of the area existing within the Kazbegi National Park for HPP construction. Thus, on March 1, 2013 Green Alternative filed a revised lawsuit to the court as well as additional demand to scrutinize the compliance of the order with the Law of Georgia on the System of Protected Areas, the Law of Georgia on Environmental Protection and the Law of Georgia on the Red List and Red Book of Georgia.

The court of the first instance (May 31, 2012), as well the Court of Appeals (December 19, 2012) rejected Green Alternative’s lawsuit, while the Supreme Court found Green Alternative’s lawsuit inadmissible (April 18, 2013)⁷⁵.

It should be noted that one important circumstance was revealed during court proceedings, which complemented the list of wrongdoings committed by public agencies in favor of Dariali Energy and its project, Dariali HPP. In particular:

On December 6, 2012 Nikoloz Chakhnania, former head of the Department of Ecological Expertise and Inspection of the Ministry of Environmental Protection, who was questioned during the hearing related to the discussion of Green Alternative’s appeal at the Court of Appeals, submitted Decree #2247 of the Government of Georgia dated November 18, 2011 on allocation of 87737 sq/m of land area on the territory of Kazbegi National Park for the construction of Dariali HPP. It should be noted that the decree had not been published officially and although the trial had been underway for already a year, neither the Ministry of Environmental Protection, nor Dariali Energy submitted this document during the trial.

Nikoloz Chakhnania explained that because of illegality (he meant the construction of HPP on the protected area), he did not plan to launch administrative proceedings on the EIA report provided by the company; however, he changed his mind after the company handed over to him the above mentioned governmental decree of November 18, 2011. It should also be noted that the decree

⁷² Letter #133 of September 27, 2011 sent by Head of Public Relations Department of the Ministry of Environmental Protection, Ekaterine Bendeliani.

⁷³ Letter #04/06-38 of September 15, 2011 sent by Green Alternative to Levan Mkheidze, the first deputy head of the Agency of Natural Resources under the Ministry of Energy and Natural Resources

⁷⁴ Letter #02/5447 of December 16 sent by First Deputy Minister of Energy and Natural Resources Marian Valishvili to Green Alternative

⁷⁵ Green Alternative’s lawsuit, as well as court rulings and complete materials of court proceedings, including protocols of interrogation of witnesses are available at Green Alternative’s website: www.greenalt.org

(which was not published even after a year) appeared in the hands of the company in a printed form on the very day of its adoption by the government.

As far as the content of the decree is concerned, guiding itself by paragraph 1 of article 27² of the rule approved by Decree 242 of the Government of Georgia dated August 20, 2010 “On Approval of the Rules of Forest Use”, the government by its decree, before obtaining a construction permit by the company, allocated 87737 sq/m of land area necessary for the construction of Dariali HPP on the territory of Kazbegi National Park for special purpose usage. It means that by adopting the decree, besides the fact that then Prime Minister Nika Gilauri exceeded his official powers (because it is the Parliament’s competence to solve this issue), he adopted an absolutely illegal decision, because allocation of the national park area for special purpose usage is inadmissible.

After Chakhnokia provided the governmental decree during the hearing, Dariali Energy submitted the agreement on forest usage for special purposes concluded with the Agency of Protected Areas on the basis of the above mentioned governmental decree.

Green Alternative requested the government’s chancellery to provide documents related to the adoption of governmental decree #2247 of November 18, 2011; these documents confirmed that the Ministry of Environmental Protection applied to the Government with an initiative (without any substantiation) to grant illegal powers to Dariali Energy. Georgian Prime Minister Nika Gilauri was aware about the problems of incompliance of the decree with the law through the conclusion issued by the Legal Department of the Georgian Government.

As it seems, nobody from the Ministry of Environmental Protection dared to sign an obvious violation – construction of a HPP on a protected area. Thus, the superior agency – Government/Prime Minister undertook this task. Apprehending that such solution was not legally correct, on initiative of the Ministry of Energy, on March 13, 2012 the Parliament of Georgia adopted a law on making amendments to the Law of Georgia on the Status of Protected Areas. Because of the above listed violations, the decree was kept secret (it was neither published officially, nor had the parties submitted it to the court hearing). By unveiling it during the hearing Nikoloz Chakhnokia tried to disclaim his own responsibility for issuing a conclusion through violation of the law.

2.2.6 Appeal to the prosecutor’s office

Since certain signs of criminal offences were detected in the case of Dariali HPP, in November 2012 (and then in December – with additional circumstances) Green Alternative applied to Chief Prosecutor Archil Kbilashvili. The organization demanded the prosecutor’s office to investigate the wrongdoings related to Dariali HPP construction project. After filing a lawsuit in prosecutor’s office, Green Alternative’s representative was summoned for a long questioning. Unfortunately, no progress has been observed since then.

2.3 Khadori-2 HPP project on River Alazani

The hydropower project planned on River Khdistskali was not the first case, when the companies affiliated with Peri Ltd (or the latter itself) demanded competent authorities to issue permits based on poor quality research. Khadori 2 HPP project is a clear example for it.

On April 29, 2009 Peri Ltd submitted an EIA report⁷⁶ to the Ministry of Environmental Protection on Khadori-2 HPP reconstruction and construction project to obtain an environmental impact permit. The project envisaged the construction and reconstruction of a 1.8 MW HPP on the River Alazani in Pankisi Gorge of Akhmeta district. As a result, the installed capacity of HPP would have increased up to 5.4MW.

According to EIA report, a 24-megawatt HPP – Khadori HPP was already functioning in the vicinity of the planned project. According to another document⁷⁷ submitted by Peri Ltd to the Ministry of Environmental Protection in 2009, the purpose of a 1.8-megawatt Khadori 2 HPP was to supply the construction of a 24-megawatt Khadori HPP with electricity. According to the company, Khadori 2 HPP ceased operation in 2004 because of certain damages caused by flooding; since then the company had been working on the HPP construction-reconstruction project, trying to attract investments.

The EIA report submitted by the company to the Ministry had such poor quality that the company's request for obtaining an environmental impact permit was rejected on May 22, 2009⁷⁸. According to the conclusion of ecological expertise⁷⁹, the EIA report was not prepared in line with legal requirements. In addition, according to expert assessments, the report contained numerous inaccuracies, technical and other errors. Thus, the commission of experts ruled that it was inadmissible to issue a positive conclusion of ecological expertise and a permit for the planned activities.

Logically, following the Ministry's refusal to issue a permit, the company should have conducted additional research; it should have revised and improved the EIA report and submitted it again for obtaining a permit, but Peri Ltd acted otherwise: about three weeks after getting a refusal (on June 11, 2009), it again applied to the Ministry of Environmental Protection and demanded to exempt it from environmental impact assessment of the project.

It should be noted that Georgian legislation envisages the possibility of exempting from EIA if "because of common state interests it is necessary to begin the activity and to take a decision duly" (Law of Georgia on Environmental Impact Permit). The law does not explain what this provision mean or what particular conditions should exist to prove the existence of common state interests. This

important shortcoming of the law has not been improved so far that enables the Ministry of Environmental Protection and other interested companies, such as Peri Ltd, to bypass legal requirements and do not carry out environmental impact assessment of planned projects. The company Peri Ltd used this opportunity after receiving a rejection letter.

In his application and motivation letter submitted to the Ministry of Environmental Protection, the director of Peri Ltd substantiates the necessity for exempting the company from EIA as follows (see box 8):

Box 8. Extracts from application #2698 and motivation letter submitted by Ioseb Mchedlishvili, the director of Peri Ltd, to Deputy Minister of Environmental Protection and Natural Resources, Gocha Mamatsashvili on June 11, 2009

"Peri Ltd is carrying out different types of construction works. It has a huge experience in the construction of HPPs...."

"In 2001 Peri Ltd obtained an environmental impact permit for the construction of Khadori HPP, which also covers the construction area of Khadori 2. The work over the above mentioned project has been underway since 2005 in order to attract investors.

July 15 is defined as the date for launching the construction. Postponement of this date will lead to the beginning of the construction by next spring that will cause violation of the agreement with foreign investors. Hence, the issue of project implementation will be questioned. It should also be noted that on February 11, 2009 the company received a letter of support from the Ministry of Energy of Georgia as well as assessment of project report from Landsvirkjun Power (LVP). This latter has implemented numerous important projects worldwide".

⁷⁶ Peri Ltd commissioned Ecolservice Ltd to conduct EIA study and prepare a report. It should be noted that EIA reports prepared by a consultancy Ecolservice are generally characterized by poor quality.

⁷⁷ Letter #2698 of June 11, 2009 sent by Director of Peri Ltd, Ioseb Mchedlishvili to Deputy Ministry of Environment Protection and Natural Resources, Gocha Mamatsashvili

⁷⁸ Order #292 of May 22, 2009 of the Minister of Environment Protection and Natural Resources on refusal to issue an environmental impact permit to Peri Ltd

⁷⁹ The Service of Licenses and Permits of the Ministry of Environment Protection and Natural Resources; conclusion of ecological expertise #55, May 19, 2009

A week after Peri Ltd submitted an application, a special council gathered at the Ministry of Environmental Protection, which discussed the documents provided by Peri Ltd again; according to the protocol adopted by the council on June 17, 2009, the members of the council again highlighted a number of important issues, which were touched superficially in the documents, but this time the council took quite a different decision – the council ruled that the company should be exempted from submitting EIA report.

A couple of days after the council's decision, on June 23, 2009, the government (Prime Minister Nika Gilauri) issued decree #460 on exempting from providing an environmental impact assessment report concerning the construction of Khadori 2 HPP on the River Alazani. The decree repeats word for word the above mentioned explanations given in Ioseb Mchedlishvili's letter adding:

“Common state interests require launching of the activity immediately”.



Association Green Alternative is a non-governmental, non-profit organization founded in 2000. The mission of Green Alternative is to protect the environment, biological and cultural heritage of Georgia through promoting economically sound and socially acceptable alternatives, establishing the principles of environmental and social justice and upholding public access to information and decision-making processes.

We organize our work around six thematic and five cross-cutting areas. Thematic priority areas include: energy – extractive industry – climate change; transport sector and environment; privatization and environment; biodiversity conservation; waste management; water management. Cross-cutting priority areas include: environmental governance; public access to information, decision-making and justice; instruments for environmental management and sustainable development; European Neighbourhood Policy, monitoring of the lending of the international financial institutions and international financial flow in Georgia.

Green Alternative cooperates with non-governmental organizations both inside and outside Georgia. In 2001 Green Alternative, along with other local and international non-governmental organizations, founded a network of observers devoted to monitoring of development of a poverty reduction strategy in Georgia. Since 2002 Green Alternative has been monitoring implementation of the Baku-Tbilisi-Ceyhan oil pipeline project, its compliance with the policies and guidelines of the international financial institutions, the project's impacts on the local population and the environment. Since 2005 the organization has been a member of the Monitoring Coalition of the ENP (European Neighbourhood Policy) Action Plan. In 2006 Green Alternative founded an independent forest monitoring network. Since establishment Green Alternative is a member of CEE Bankwatch Network - one of the strongest networks of environmental NGOs in Central and Eastern Europe. Green Alternative closely cooperates with various international and national organizations and networks working on environmental, social and human rights issues; Green Alternative is a member of the Coalition Transparent Foreign Aid to Georgia founded in 2008. In 2010 Georgian Green Network was established on the initiative of Green Alternative. This is informal association of civil society organizations and experts dedicated to protecting environment, promoting sustainable development and fostering principles of environmental and social justice in Georgia.

In 2004 Green Alternative received the Goldman Environmental Prize as the recognition of organization's incredible work for environmental protection, social justice and equity.

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