

ENVIRONMENTAL SUMMARY

BR-0346

Project: Political Risk Guarantee for *VBC Energia S.A.*
Country: Brazil
Sponsors: *VBC Energia S.A.*
Department: Private Sector Department

I. INTRODUCTION

- 1.1 The operation relates to projects for which the entire financing, both debt and equity will be provided by the private sector. IDB will provide a guarantee for currency convertibility and transferability ("CCT") for US\$100 million of a US\$200 million four year loan (the "Loan") to be provided to *VBC Energia S.A.* ("VBC") by a syndicate of foreign commercial banks. Multilateral Investment Guarantee Agency ("MIGA") will provide CCT cover for the other US\$100 million. The Loan will comprise two tranches each of US\$100 million. IDB will provide CCT cover for one tranche ("the IDB Tranche") and MIGA will provide cover for the other tranche ("the MIGA Tranche").

II. PROJECT DESCRIPTION

- 2.1 The IDB Tranche will form part of the financing for projects for the expansion of the electricity distribution networks of two affiliated companies of VBC, namely: *Companhia Paulista de Força e Luz* ("CPFL") and *Rio Grande Energia* ("RGE"). CPFL and RGE are the energy distribution companies of the states of São Paulo and Rio Grande do Sul, respectively. The CPFL and RGE projects involve a three-year investment program involving an estimated total of Rs580 million (approximately US\$302 million). These projects will result in a significant expansion of the distribution networks of CPFL and RGE.
- 2.2 CPFL will invest a total of Rs452 million to expand and modernize its energy transmission and distribution network. Investments in new distribution lines and upgrading of existing ones will involve expenditures on aluminum towers, high-voltage lines and other materials. Other capital expenditures relate to the construction of new substations for which new investments in meters, transformers, software, hardware, training and civil works will be necessary. The proposed investments will enable CPFL to increase the number of consumers by an average of 3.6 percent per year over the next 4 years. Currently, CPFL serves 2.6 million consumers. In 2003 the company expects to be providing electricity for 3 million consumers.
- 2.3 RGE will invest a total of Rs128 million for the construction of new distribution lines and substations, as well as investments to improve the system's reliability: automation of substations, provision of substation capacitors, mobile transformers, distribution network capacitors and improvement of feeders and of secondary circuits. RGE's program is expected to result in 2.6 million low-income families in 70 municipalities being connected to power supply.

- 2.4 The 30-year concession agreements held by the companies – agreements #13/97 for RGE and #14/97 for CPFL, respectively – contain broad language requiring the new private sector concessionaires to perform services of an appropriate quality. The concession terms were designed to allow flexibility in the way improvements to service coverage and quality are provided, rather than establishing specific performance benchmarks for the concessionaires, for example specific service quality or coverage targets or specific investment requirements.
- 2.5 CPFL's emphasis following the award of the concession was in improving customer service. Starting in 1999, CPFL's focus has been in achieving a higher electric system performance level. This is the purpose of CPFL's current proposed program. RGE has already increased its overall installed capacity since privatization by 23 percent. In 1998, RGE invested US\$53 million equivalent in infrastructure, an amount three times that invested in the previous five years (under state ownership). Of these investments US\$25 million were primarily to increase the number and capacity of transmission lines (over 100 km have been added to the current system) and sub-stations (10 sub-stations where refurbished to increase capacity, five new sub-stations were constructed and three new sub-stations have begun construction) in order to avoid blackouts.

III. PROJECT COMPANIES

- 3.1 CPFL is the fourth-largest energy distributor in Brazil, attending to 2.5 million consumers, being 86 percent residential, 2.0 percent industrial, 8.1 percent commercial and 3.9 percent other segments. The energy distributed by CPFL is made possible by a distribution network totaling some 64,000 km plus 6,000 km of transmission lines covering a geographical area of 90,440 km². CPFL also carries on a limited amount of electricity generation.
- 3.2 RGE is responsible for power distribution in the north and northeast regions of the State of Rio Grande do Sul, an area of approximately 90,718 km² and with 900,000 customers. RGE has 59,402 km of low voltage distribution lines and 1,611 km of 138 kV transmission lines. RGE also has a limited generation capacity representing less than one percent of the electricity that it distributes.

IV. ENVIRONMENTAL AND SOCIAL ASPECTS

- 4.1 From an environmental standpoint, the project consists of two components involving investments in two separate, existing electricity distribution systems, one in the northern part of the State of São Paulo (CPFL), and the other in the Northern part of the State of Rio Grande do Sul (RGE).
- 4.2 The CPFL investments involve the construction of several substations and the installation of the associated distribution lines, all of which are of short distance (i.e. less than 5 km). In addition, one short (approximately 4 km) 138 kV transmission line will be installed. All of the substations and distribution lines will be located near the perimeter of urban areas. Given the project characteristics and proposed site locations, no significant environmental or social impacts are anticipated. The new facilities will not require involuntary resettlement or significant loss of livelihoods and there is no significant adverse impact on natural habitat. No potentially environmentally or socially sensitive projects were identified

in the proposed projects. The state of Sao Paulo environmental authorities has reviewed the environmental assessments for various projects (i.e., those for which designs have been finalized). Based on these assessments, the authorities have concluded that the projects do not present significant environmental impacts or risks and have issued the applicable licenses/authorizations. The state environmental authorities appear to have sufficient institutional capacity to properly evaluate proposed new projects and to perform the subsequent monitoring and enforcement.

- 4.3 RGE plans similar types of investments. New substations will be constructed with associated short distance transmission lines. In addition, 9 short (i.e., all less than 10 km and one of 19 km) 69 kV or 138 kV transmission lines will be installed. All of the substations and distribution lines will be located near the perimeter of urban areas. Given the project characteristics and proposed site locations, no significant environmental or social impacts are anticipated. The new facilities will not require involuntary resettlement or significant loss of livelihoods and there is no significant adverse impact on natural habitat. No potentially environmentally or socially sensitive projects were identified in the proposed projects. The State of Rio Grande do Sul environmental authorities have reviewed the environmental assessments for various projects (i.e., those for which designs have been finalized). Based on these assessments, the authorities have concluded that all projects, except one, do not present significant environmental impacts or risks and have issued the applicable licenses/authorizations. For one project, the Porto Colombia – Caicara Transmission Line, the state environmental authorities requested the preparation of a more complete environmental assessment (i.e., RIMA). The RIMA has been prepared and submitted and it appears there are no significant impacts or issues. The state environmental authorities appear to have sufficient institutional capacity to properly evaluate proposed new projects and to perform the subsequent monitoring and enforcement.
- 4.4 While CPFL does not have a formulized Environmental Management System (EMS), the company has implemented various components of an EMS and is presently performing an EMS evaluation (e.g., gap analysis). The company has an environmental department with staff and designated responsibilities. The company has written internal norms and guidelines. The company has demonstrated that they have sufficient resources to ensure all necessary environmental permits and authorizations are obtained for all new projects. In terms of health and safety, the company has implemented a very effective health and safety management system, including designated staff, written procedures, training, internal evaluations (audits, reviews, etc.), and reporting.
- 4.5 RGE environmental responsibilities are handled by the engineering department, and are very effective in performing the necessary tasks to obtain the environmental permits and authorizations required for new projects. The company has some written internal norms and guidelines. Related to health and safety, RGE has implemented a complete health and safety management system and anticipates obtaining certification (i.e., BS 8800) by July 2000.
- 4.6 Both companies are presently in compliance with the applicable environmental, health and safety Brazilian regulatory requirements and neither company has had any significant regulatory non-compliance within the last three years.