

*MOL Alternative  
Sustainability  
Report*



2008

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# INTRODUCTION •

*The first in a new series issued by the National Society of Conservationists (NSC), this publication is intended to be an alternative 2008 annual report of Hungary's largest corporation, Hungarian Oil and Gas (MOL). Subsequent alternative annual reports are planned to be published to ensure that green considerations are incorporated as much as possible into MOL's activities, including during its planning and implementing of projects.*

*NSC urges priority for long-term, sustainable development solutions not only in rhetoric or various committees but also in practical action. Perspectives and views from NGOs including NSC – who have been consistent proponents of sustainable development – should also be taken into account. Enforcing principles of long-term sustainable development is in the interest of all, a basic prerequisite for maintaining a healthy human habitat in Hungary and also a key to the survival of mankind and preserving the health of earth's ecosystems.*

This study is divided into three main parts. The first chapter - '**THE WAY WE SEE IT**' - quotes information from MOL's website, annual reports and communications, summarising this information without altering the structure of presentation used by the company.

Part two, '**THE WAY WE READ IT**', contains information gathered from print and internet media and other sources deemed important, to judge the normal operation of the company from the green perspective.

'**THE WAY WE THINK**' discusses and evaluates the information from preceding chapters, providing insights and analyses of certain issues and concludes with a set of recommendations to MOL. NSC hopes that MOL genuinely takes on board these recommendations, such that the rhetoric enshrined in the company's popular ad slogans - "MOL's success become Hungary's success" with "unlimited dynamism" – become a reality in the company's operations.

A final section provides an outlook on INA's operations, written by a Bankwatch associate living in Croatia. INA is the Croatian Oil Company, huge part owned by MOL which leads to a significant influence of the company everyday operations.

# I. THE WAY WE SEE IT

1.

## General facts and figures

### An overview of MOL

Magyar Olaj- és Gázipari Nyrt. (MOL) Group is one of Central Eastern Europe's leading integrated oil and gas companies with a variety of activities including:

- exploring and producing crude oil and natural gas; refining, transporting, storing and distributing petroleum products at both retail and wholesale levels;
- transmission of natural gas, production and sales of olefins and polymers; and producing electricity and thermal energy from gas and renewable resources.

MOL group also includes one of Hungary's leading chemical companies TVK, Slovak oil company Slovnaft and the Austrian retail and wholesale company, Roth. MOL also has strategic partnerships with Hungarian Horizon Energy, a subsidiary of the US-based Aspect Energy and with Croatia's INA, in which MOL holds a controlling interest with 44 per cent of its shares.

In Europe, MOL group is present in Italy, Slovakia and Croatia, operating a network of over 1000 filling stations in ten countries of the region. Its Exploration and Production Division focuses on the Middle East, Central Asia and North Africa and has recorded several significant discoveries in Hungary, Russia and Pakistan in recent years.

In 2008, MOL embarked on a new business, joining forces with Czech Energy Company to gain a footing in the power generation market. MOL Group shares are listed on the Budapest, Luxembourg and Warsaw Stock Exchanges and its depositary receipts traded on the US Pink Sheet and London's International Order Book.

Since 2001, MOL's Chairman and Chief Executive Officer is Zsolt Hernádi, former manager at K&H Bank and Savings Cooperatives Bank.

### Key figures (2008):

Sales revenue (bn HUF):	<b>3.535</b>
Market capitalization (bn USD):	<b>5</b>
Number of employees:	<b>17.339</b>
Number of filling stations:	<b>1.076</b>
Total crude oil production (kt):	<b>1.924</b>
Total refinery throughput (kt):	<b>18.141</b>
Total natural gas production (net dry, mcm):	<b>2.533</b>
Total crude oil product sales (kt):	<b>17.735</b>
Total petrochemical product sales (kt):	<b>1.358</b>

## *“MOL’s core values*

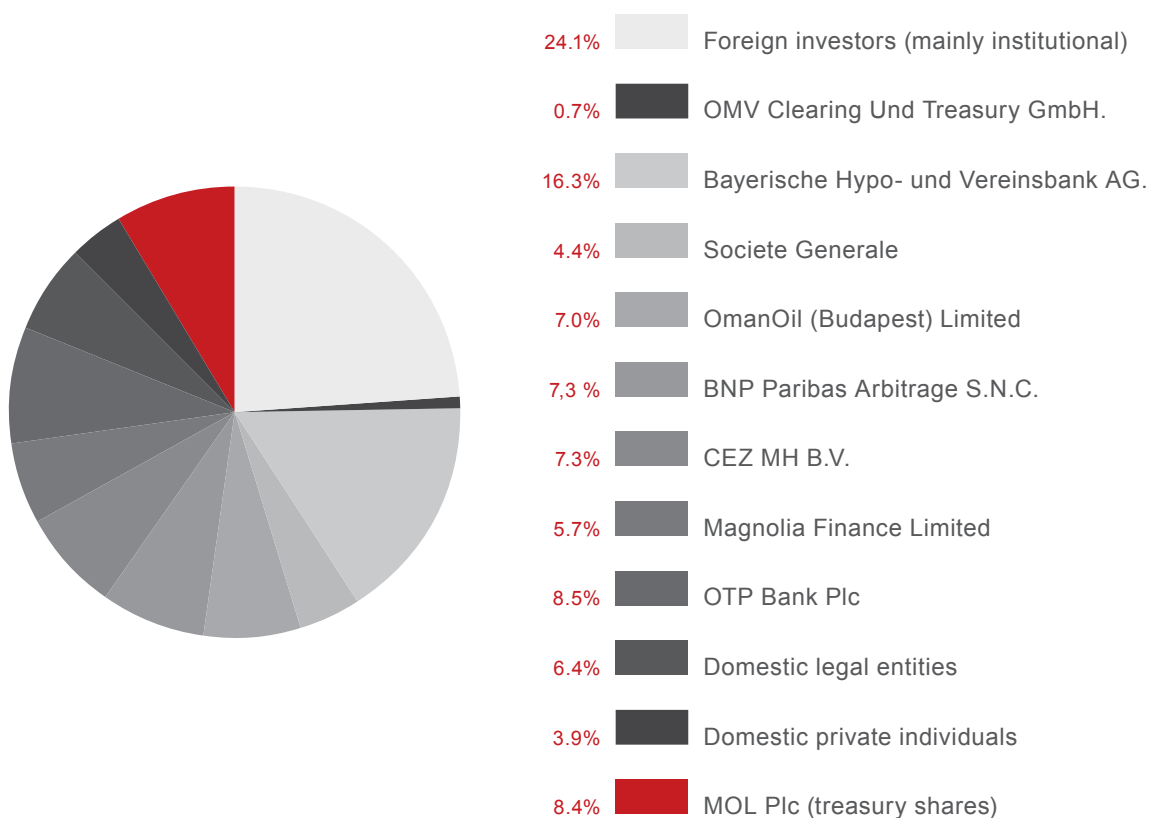
- Drive for value-creating growth
- Pace setter and improvement agent
- Hard work and continuous self-improvement
- Team player and partner
- Quality and company of choice
- Health, safety, environmental and social commitment”

## *Vision*

“Our ambition is to become the most respected multinational integrated oil company in Central Europe with an at least 10-billion-dollar market capitalization and operations linking several seas.”

## *Ownership structure*

*(as of 31 December 2008)*



Key financial data	HUF Mn		USD Mn	
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### Net sales revenue

	2007	2008	2007	2008
Exploration and production	334.806	428.780	1.822	2.496
Refining and marketing	2.290.414	3.145.641	12.461	18.310
Gas & power	90.694	199.124	493	1.159
Petrochemicals	497.616	470.457	2.707	2.738
Corporate and other	102.163	148.703	556	866
<b>Total</b>	<b>3.315.693</b>	<b>4.392.705</b>	<b>18.039</b>	<b>25.569</b>

### Net external sales revenue

Exploration and production	178.804	237.306	973	1.381
Refining and marketing	1.932.290	2.768.537	10.513	16.115
Gas & power	78.244	145.726	426	848
Petrochemicals	398.181	366.090	2.166	2.131
Corporate and other	6.432	17.349	35	101
<b>Total</b>	<b>2.593.951</b>	<b>3.535.008</b>	<b>14.113</b>	<b>20.576</b>

### Operating profit

Exploration and production	78.864	191.018	429	1.112
Refining and marketing	171.935	72.450	935	422
Gas & power	38.743	38.661	211	225
Petrochemicals	40.892	-7.589	222	-44
Corporate and other	26.446	-37.697	144	-220
Intersegment transfers	-1.375	-57.619	-7	-335
<b>Total</b>	<b>355.505</b>	<b>199.224</b>	<b>1.934</b>	<b>1.160</b>

Sources:

[http://www.mol.hu/hu/a\\_molrol/tarsasagunkrol/tarsasagunkrol\\_roviden/](http://www.mol.hu/hu/a_molrol/tarsasagunkrol/tarsasagunkrol_roviden/)

[http://www.mol.hu/hu/a\\_molrol/tarsasagunkrol/mukodesunk/](http://www.mol.hu/hu/a_molrol/tarsasagunkrol/mukodesunk/)

[http://www.mol.hu/hu/a\\_molrol/tarsasagunkrol/vallalatiranyitas/jovokepunk\\_ertekeink/jovokepunk/](http://www.mol.hu/hu/a_molrol/tarsasagunkrol/vallalatiranyitas/jovokepunk_ertekeink/jovokepunk/)

### Operating profit excluding special items

Exploration and production	80.554	125.699	438	732
Refining and marketing	171.935	67.821	935	395
Gas & power	38.743	40.764	211	237
Petrochemicals	40.892	-7.589	222	-44
Corporate and other	-31.329	-38.334	-170	-224
Intersegment transfers	-1.375	5.597	7	33
<b>Total</b>	<b>299.420</b>	<b>193.958</b>	<b>1.629</b>	<b>1.129</b>

[http://www.mol.hu/hu/a\\_molrol/tarsasagunkrol/vallalatiranyitas/jovokepunk\\_ertekeink/](http://www.mol.hu/hu/a_molrol/tarsasagunkrol/vallalatiranyitas/jovokepunk_ertekeink/)

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## MOL and the environment

### Code of Ethics

MOL's first Code of Ethics was developed in 1992 and has since been periodically updated. It contains norms to which all employees and member companies are equally required to comply. The code covers not only environmental protection but also health, safety and quality issues. In 2006, an Ethics Council was established to investigate any non-compliance with the code and prepare risk assessments. The current, fourteen-page code states the following on the environment:

*"In line with our commitment to sustainable development, we have adopted a systematic approach to health, safety, security and environmental management in order to achieve continuous improvement in performance. We are committed to reducing health, safety and environmental risk, in relation to our activities, by creating safe working conditions and by continuously improving our environmental management performance. Focus on quality is a fundamental requirement in our activities. We facilitate programmes for the protection of the environment in the regions in which we operate. We observe all technological and ecological guidelines in force, in all our activities, and promote the acceptance of more demanding standards designed to minimise the risk of adverse effects on the environment resulting from such activities. The MOL Group is committed to providing all employees – and those of other companies working on our premises – with a safe and secure work environment, where no-one is subject to unnecessary risk. We recognise that safe operations depend not only on technically sound plant and equipment, but also on competent people and an active HSE culture."*

### HSE policy

A new MOL Health, Safety and Environment (HSE) policy was introduced in 2005 to improve HSE performance. This policy applies to all business units and MOL-controlled subsidiaries and is the basis on which to develop their own HSE objectives, strategies, goals and programmes.

In drafting the policy, efforts were made to comply with the EU's Major Industrial Accidents Directive within the **SEVESO PROJECT**, to help mitigate risk and reduce the consequences of accidents. The **SAFE WORKPLACES PROJECT** develops MOL manager and employee attitudes and skills in relation to safety issues.

Under the umbrella of the HSE policy, MOL has initiated subsequent policies such as the Waste Management Policy and the Road Safety Policy. Within the framework of a new regulatory system, MOL has introduced the new HSE group guidelines "Health, Safety and Environment Management System" to focus on the responsibilities and accountabilities of line management with regards to turning its HSE policy and thematic policies (Road Safety Policy) into practice.

Based on various guideline elements, specific processes have been identified and described in the so-called Global Operative Regulations (GOR), summarising the key processes, methods and division of responsibilities that present MOL Group-level expectations towards the individual member companies.

These GOR descriptions include, in addition to traditional HSE areas (e.g. waste management, fire protection, etc.) new regulatory areas like Product Stewardship, or Process Safety Management. This is also the first document to define requirements for the three basic pillars of sustainable development, providing new rules for the main corporate processes in order to secure compliance with the relevant criteria.

## *Sustainable development*

In 2006, MOL set up their own Sustainable Development Framework aimed at adopting international best practices and requirements, and, as a long-term objective, developing sustainable operations within the company. This new framework provides MOL with an effective monitoring system and a robust planning and decision making-process, based on the principle that SD should be an integral part of MOL's day-to-day operations and prevailing business strategies. There is, therefore, no such concept as a "sustainability strategy" or "sustainability budget" since every business strategy and budget should embrace sustainable development.

Under the new system, the company's current practices are reviewed on an annual basis against international best practice, benchmark documents and international conventions to identify existing and missing elements. The framework ensures the efficient achievement of MOL's clearly stated strategic objectives and specific goals.

The most senior SD governance body is the Sustainable Development Committee of the Board of Directors, which has two non-executive members and is chaired by MOL Group's CEO, Mosonyi György. The Committee ensures the highest commitment and representation of sustainability issues, in both internal and external MOL Group relations, helping strengthen MOL's market position and long-term performance in this strategic area and supervising action for sustainable development.

The implementation of SD objectives is coordinated by the so-called Sustainable Development Panel, made up of MOL Business and Functional Unit representatives. Panel members are responsible for ensuring the integration of the sustainability approach into day-to-day business operations and coordinating the unit-level SD action plan.

## *Social impact on communities*

Prior to commencing any major projects and planned interventions, MOL conducts assessments of projected impacts on local communities and implements safeguards to minimise any negative



impacts, and the well-being of all stakeholders is considered by MOL to be of critical importance.

“We study and analyse the possible intended and unintended social consequences of our developments during the planning phase so any changes required can be incorporated and considered in due time. The primary purpose of our assessments is to bring about a more sustainable and equitable biophysical and human environment.

Success depends on our capacity to adapt best practices and make the most of local opportunities and synergies by incorporating and addressing stakeholders' views throughout the project lifecycle. During stakeholder engagement process we inform stakeholders about the proposed project and its probable effects, collect their input, views and concerns and take account of this information in decision-making. Beyond identifying and mitigating adverse impacts we consider positive reimbursements from the projects. This means not only creating job opportunities but supporting various local initiatives. Successfully answering local challenges further underpins MOL's ability to adhere to sustainability principles.”

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### *Compensation and relocation/ resettlement*

“Using third-party properties is a particularly sensitive issue, since several parts of society may be affected. Under the official system, the competent authorities determine conditions of land use and compensation. However we only use compensation as a last resort ensuring that impacts are not borne disproportionately, other means such as relocation/resettlement are treated as a special case.

In impact mitigation and management phases we consider it to be essential that all local lay residents who may be affected by a project are kept sufficiently informed about it, as a means of reassurance. One way is to establish a public forum with the local inhabitants, even if not stipulated in law, where features of the development and its direct impact is presented to and discussed with all parties concerned to ensure appropriate co-operation after construction has commenced.

The management plan comprises actions, responsibilities and timing of mitigation and enhancement actions and monitoring of impacts and actions. Mitigation measures are built into the selected alternative. As part of the project organisation there is an allocated officer who is responsible for feedback, general information and relevant communication. The allocated officer is continuously available during the course of the whole project and provides information to stakeholders on issues related to land-use and the project status.”

### *Strategic SD initiatives (2005 to 2010)*

1. Strengthen good governance and risk management
2. Focus on future portfolio steering

3. Focus on internal and external customer relations
4. Enhance trust and credibility among stakeholders
5. Reduce our environmental footprint

*“The protection of the environment has become one of the most impassioned issues of the 21st century. As a direct result, the MOL Group urgently needs to identify all those areas where it can make a difference and take measures to reduce the environmental footprint of its production facilities and products. Emissions reduction, water and waste management and the protection of natural resources are some of the areas where we can and where we must act each year in line with international best practices to satisfy the energy demands of society whilst minimising our environmental footprint. For instance, in 2002, the MOL Group introduced the use of the ‘carbon thinking’ approach in as early as the planning stage of every project to reduce our environmental impacts. In addition, an efficient greenhouse gas strategy was also developed to curb carbon dioxide emissions.”*

6. Manage opportunities, risks & liabilities in the value chain
7. Capitalize on human resources

## *MOL’s environmental activities*

**IMPROVING ENERGY EFFICIENCY:** more efficient systems with reduced operational losses have been implemented, existing systems renewed or replaced (e.g. boiler replacement, heating system modernisation, increased efficiency of water cooling).

**RENEWABLE ENERGY:** driven partially by the need to comply with external regulations, a survey has been started to assess the potential of renewable energy for use in production.

- Biogas production – a feasibility study has been prepared.
- Wind energy utilisation – a feasibility study has been prepared.
- Solar energy utilisation – a project plan has been prepared and is being implemented (A ‘Solar Wall’ of 240 cells and an overall surface area of 240 sqm has been set up at a MOL filling station by Motorway M1. The heat and electricity converted from solar energy is used to contribute to providing lighting and hot water supply for the station building. The system is capable of generating an annual total of around 14,000 kWh of electricity.

**WATER MANAGEMENT:** new projects and improvements have helped reduce water use and wastewater discharge.

**BIODIVERSITY** is a key responsibility of sustainable development. MOL pays particular attention to operations within nature conservation areas, seeking engagement of specialists and associations and planning processes based on studies and assessments.

### **EMISSIONS, EFFLUENTS AND WASTE**

- Waste management - while the number one priority is the reduction of hazardous waste generated, close attention is paid to waste resulting from maintenance, construction activities or unexpected events. In 2008, the Comprehensive Waste Management Project was launched with a view to revising MOL’s waste management processes to reduce costs, improve

Sources:

[http://www.mol.hu/hu/a\\_molrol/sd/a\\_vallalatcsoporthiranyitasa/etikai\\_kodex/](http://www.mol.hu/hu/a_molrol/sd/a_vallalatcsoporthiranyitasa/etikai_kodex/)

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[http://www.mol.hu/hu/a\\_molrol/sd/kozeppontban\\_az\\_ember/hatasvizsgalat\\_beruhazasok\\_helyi\\_kozossegekre\\_gyakorolt\\_hatasarol/](http://www.mol.hu/hu/a_molrol/sd/kozeppontban_az_ember/hatasvizsgalat_beruhazasok_helyi_kozossegekre_gyakorolt_hatasarol/)

process efficiency and optimise waste management.

- Preventing spills - malfunctions that may occur during the transport of crude oil and petroleum products via pipelines pose the most serious risk of contamination of soil and groundwater. Possible causes vary, but MOL uses regular aerial and ground monitoring of pipelines, continuous pressure control and a capable troubleshooting system for prevention.
- Air emissions - environmental projects continue to bring about a decrease in air emissions.
- Remediation - increasingly efficient planning processes allow remediation funds to be reduced continually. In 2008, MOL spent HUF 2.2 billion on remediation.

**LEGAL COMPLIANCE:** legally required environmental impact assessments (for nature conservation and agricultural land protection) are made during the project preparation phase and results considered before the project launch.

## Reports

Every year, MOL issues an **ANNUAL REPORT** and a **SUSTAINABLE DEVELOPMENT REPORT**, based on HSE and SD policies. The 2007 SD Report sets the following environmental targets for 2008:

- Increase energy efficiency
- Each Business Unit to create a leading waste management indicator
- Reduce MOL Group environmental liabilities as at the end of 2007 by HUF 6.0 billion
- Reduce carbon dioxide emissions by 1% as a direct result of GHG reduction initiatives
- Reduce Group-level fresh water intake by 10% until 2009
- Replace oil heating with gas heating at filling stations
- Increase the number of hazardous waste disposal facilities at filling stations

3.

## Social responsibility

In line with the Corporate Social Responsibility (CSR) policy, MOL has launched various initiatives such as Culture & Sciences, Sports, Education & Children, the New Europe Foundation and Environment & Health, the latter including the following programmes:

- Green Light for Our Environment – run in collaboration with and under professional supervision by Ökotárs Foundation, this funding programme has been open for applications every year since 2005. Proposals are selected in two stages to create, improve or rehabilitate public green areas of at least 1500 sqm.

Since its launch, the programme has provided HUF 77 million of funding to 113 towns and villages in Hungary, Romania and Slovakia. In 2008, a total of 90 online proposals were received for the HUF 13 million of funding offered, out of which 36 (applying for over HUF 35 million) were eventually shortlisted. The funds made available under the programme are continuously increased,

reaching 13 million by 2008 from 2.5 million in first year.

- A Dash of Care Foundation – an ongoing programme for diabetes and diabetics
- Ongoing support for water rescue services in Hungary
- Ongoing support the Hungarian Red Cross
- Ongoing support the Maltese Charity Service
- Tree to the Tatras – remediation of the 2004 storm damage in the Czech Republic and Slovakia by planting 500,000 trees and providing aid worth a total of HUF 147 million
- Mátrakeresztes – programme for the mitigation of 2005 flood damage
- Sri Lanka and Pakistan: efficient rescue team, deployable within days (Sri Lanka 2005, Pakistan 2005)

Sources:

[http://www.mol.hu/hu/a\\_molrol/tarsadalmi\\_szerepvallalas/](http://www.mol.hu/hu/a_molrol/tarsadalmi_szerepvallalas/)

<http://zoldovezet.okotars.hu/>

4.

## *Activities outside Europe*

### *Exploration and Production*

#### **PAKISTAN** (MOL Pakistan Oil and Gas Company BV)

- Tal block – in 2008, a development project was implemented with two production wells drilled and a new field discovered. At the same time, the Makori-2 well was abandoned.
- Karak block – 40 per cent ownership interest acquired
- Margala and Margala north blocks

#### **RUSSIA**

- Zapadno-Malobalik (ZMB) – with seven new wells drilled in 2008, MOL and Russneft now own 222 wells, 50 per cent each.
- Bajtugan (Bai Tex) – a 3D seismic survey was completed in 2008. Eight new wells were drilled, increasing production by 17 per cent from 2007. There was some land remediation in 2008 as well.
- Matjushkinskaya field – three new wells were put on stream, increasing production by 144 per cent. Two wells were drilled, one resulting in significant discoveries, the other requiring further testing. Petrol-powered generators were replaced with gas-powered ones to reduce pollution and the quantities of gas flared to the atmosphere.
- Surgut-7 field – first exploration well drilled

#### **CAMEROON**

- 40 per cent of ownership interest in Ngosso block was acquired from Tullow Cameroon Limited, under approval by the government of Cameroon.

#### **OMAN**

- 25 per cent of interest in an Oman block was sold and used by MOL to acquire 40 per cent of the Karak block

#### **INDIA**

- Under an earlier agreement with Oil and Natural Gas Corporation Limited, MOL acquired 35 per cent ownership interest in Block HF-ONN-2001/1

#### **YEMEN**

- Owned 100 per cent by MOL, Mol Yemen is currently engaged in exploration operations

## IRAQ

- Kalegran Ltd, a subsidiary of MOL, carried out exploration operations in partnership with Gulf Keystone in the Kurdistan Region. Following a successful exploration campaign (with two billion barrels of resources being estimated) and with the Kurdish Regional Government's support, a company called Weatherford Drilling International was commissioned to drill oil wells.
- Gulf Keystone is a British off-shore company, operating primarily in Algeria and Iraq and with interests in Bermuda. Weatherford Drilling International is one of the world's largest oil and gas rig suppliers, present in over 100 countries worldwide.

## KAZAKHSTAN

- Under an agreement with OOC, MOL gained access to a potential production site in Kazakhstan in exchange for eight per cent of its shares sold to OOC (for USD one billion). Exploration had shown that sufficient quantities and quality of oil and gas are available in the area, but further tests are required to assess economic viability.

Sources:

[http://www.mol.hu/hu/a\\_molrol/befektetoknek/jelentesek/eves\\_jelentes/](http://www.mol.hu/hu/a_molrol/befektetoknek/jelentesek/eves_jelentes/)

In addition, INA has exploration and production interests in Croatia, Angola, Namibia, Egypt, Iran and Syria.

5.

## *Internal developments*

- With a view to covering primarily its own power demand in a more energy efficient manner, MOL set up a joint venture with Czech Energy Company to fully supply the power needs of MOL's own refineries and sell the balance on the electricity market.
- Partnering with an Icelandic and an Australian company, MOL established a joint venture for the utilisation of geothermal energy and later went on to acquire the Icelandic partner's shares in the venture. The company's activities include research, construction of geothermal power plants, direct utilisation of thermal steam and marketing of geothermal energy.
- In 2008, a Trading Platform was established to allow MOL to manage energy issues uniformly. To increase income from carbon dioxide emissions trading, MOL intends to decrease its carbon dioxide emissions.
- 2008 saw the Gas Business Unit engaged in operations to convert Hungary's depleting gas reservoirs into storages. It is a matter of course that MOL, a 16.66 per cent owner of Nabucco, takes a very active part in the construction of the Nabucco gas pipeline. In addition, a 108-km-long gas pipeline is being planned to run from Romania to Hungary, expected to be put in operation during 2009.

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## *II. THE WAY WE READ IT*

1.

### *The attempted takeover by OMV*

Formerly a ten per cent owner in MOL, Austrian OMV purchased another block of shares in 2007, subsequently announcing its intention to acquire majority ownership of MOL and thus to gain a controlling stake. OMV representatives claimed that the merger would create a market player strong enough to compete with Russian oil companies, which was in the best interest of shareholders as well.

MOL management was not receptive to the idea and made every effort to stop OMV achieving its goal. MOL managers thought that the deal would not create added value and would even restrict competition by merging the region's oil industry facilities and capacities into a single corporation. The attempt eventually failed, with OMV giving up its takeover plan by autumn. But before that happened, a number of remarkable events had taken place.

The underlying conflict is rooted in a structural difference between the two companies. While OMV relies on exploration and production, MOL focuses on processing. The Austrian company yields a huge profit as long as crude oil and gas stay high, but may get into trouble when this trend ends. MOL is more efficient even in this respect, its production costs per barrel being only a quarter of that incurred by OMV.

OMV's solid earnings are primarily due to an increase in profits from its Romanian operations, while OMV-owned Petrom shows rather low efficiency. 80 per cent of OMV's profits derive from exploration and production - 60 per cent of which comes from the Romania - meaning that roughly half of all profits are tied to the Romanian market. Some analysts say there is an ongoing exploitation of Romania. The Romanian government has probably realised that action should be taken and is reported to be considering doubling the royalty to generate an additional USD 200 million income for the national budget.

MOL began buying back its own shares to reduce the number of shares on the market before OMV made a formal proposal. At the same time, companies on friendly terms with MOL's management also purchased additional shares to restrict OMV's room to manoeuvre towards a takeover.

There are several issues here. Firstly, it should be noted that MOL carried out the buyback in a hurry, purchasing shares at a price above that which analysts thought they were actually worth. Secondly, Hungarian law does not allow any company to own over ten per cent of its own shares. MOL has much more but has lent the portion above the 10 per cent limit to its strategic partner – without informing the stock exchange of the fact. Analysts estimate the percentage of treasury shares to be 40 per cent, added to which are those owned by companies supporting MOL's management. It is also a problem that

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the management used MOL's resources to strengthen their position.

Mention should be made of the rather curious deal between MOL and OOC (Oman Oil Company) involving MOL selling to OOC eight per cent worth of shares lent to MFB (Hungarian Bank for Development) in exchange of cash and interests in some unspecified international assets. What is most dubious about the deal is the fact that the shares were sent by MOL to the buyer without the purchase price having been paid, and then the buyer never paid the price and eventually sent the shares back to MOL. It is estimated that MOL lost as much as HUF 33 billion on the deal. Nevertheless, OMV's manoeuvring space was further restricted.

Simultaneous with stock market developments, the Parliament of Hungary elaborated and adopted 'Lex MOL' (following suit with Germany's 'Lex VW') aimed at reducing the chances for businesses to acquire interests in strategic energy and water companies. The bill received unanimous cross-party support, which otherwise happens rarely. While some analysts argue that this measure was unnecessary because MOL would have been able to protect itself without it, others go as far as to claim that the new law actually serves to protect shareholders' investment and the company's management.

Such legislation may give rise to serious issues, resulting in a loss of freedom in trading of shares of 'strategic companies' at the stock exchange, maintaining the possibility of political intervention, etc. Of course, both OMV and the EU vehemently protested against the new law, which, however, remained in force with some amendments, and OMV's room to manoeuvre was curbed further.

After the purchase of shares was announced, the European Commission started an investigation into what effect a merger would have on competition and came to the conclusion that (as MOL claimed) competition would be compromised, so such a transaction should be subject to certain conditions.

At MOL's General Meeting in April, OMV representatives did not stand a chance to get their voice heard, although they raised several issues (e.g. the offer for the shares was well above the market price and the price MOL was selling shares at, so rejection amounted to a decision against shareholders' interest). OMV challenged the General Meeting's decisions on the grounds that the issue of voting rights from lent shares had not been properly dealt with.

MOL showed interest in acquiring INA (Croatia), with which it had closer ties than OMV, but its defensive actions against OMV's takeover bid had exhausted its reserves. So the acquisition of INA could only be through an exchange of shares, a type of deal that was good for the government of Croatia and was not bad for MOL either, allowing MOL to reduce the number of its treasury shares by passing them on to a strategic partner.

MOL even counter-attacked OMV by purchasing an Austrian network of filling stations and rebranding it to MOL.

At that time, there was a fierce advertising battle in the media between MOL and OMV, with quite considerable amounts of money spent in the process.



2.

Sources:

## *Robin Hood tax*

On 10 November 2008, the district heating competition bill passed Parliament with 190 votes for and 184 against and no abstentions, establishing the so-called Robin Hood Tax - an eight per cent surtax imposed on large energy supply and trade companies. Revenues from the Robin Hood tax would only be used to support the use and modernisation of district heating systems. The new law will enter into force on 1 January 2009 and expires on 1 January 2011.

The new tax will be payable by hydrocarbon (oil and gas) producers, producers of petroleum products, as well as wholesalers and retailers of excisable petroleum products, exemptions including energy sector services offered at government-fixed prices.

The new tax was strongly opposed by the Hungarian Petroleum Association (whose membership includes MOL) as an excessive burden on companies in the energy sector. Along with the Association, MOL too criticised the new tax, describing it as a 50 per cent corporate tax increase and being destructive of the market and investment propensity.

Some analyses show that such companies should not have any difficulties paying the new tax from their huge profit windfalls. Others believe that this is the price to pay for Lex MOL. Anyhow, with the law enacted, the company's slogan 'MOL's success is Hungary's success' will become reality for a while.

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3.

## *The world economic crisis*

No study about 2008 will let the world economic downturn pass unmentioned. The bankruptcy of Lehman Brothers on 15 September 2008 is widely considered to have marked the beginning of the crisis, early signs of which were seen back in 2007 with the realisation that existing practices and approaches can no longer be applied.

MOL has not been left unaffected by the downturn either. The company's statements show that earlier on they were optimistic that the crisis would be soon over and MOL might even benefit from it. As the crisis continued to deepen, profits and other figures increasingly worsened. The loss of value of the Hungarian currency and the extremely weak performance of the Budapest Stock Exchange only added to MOL's already unhappy situation.

According to MOL's CEO, the economic crisis may actually do good to the company, forcing MOL to cut expenses and implement any long-delayed cost cutting projects. Cost cuts will affect employees in the form of lost jobs, as well as increased workload and efficiency.

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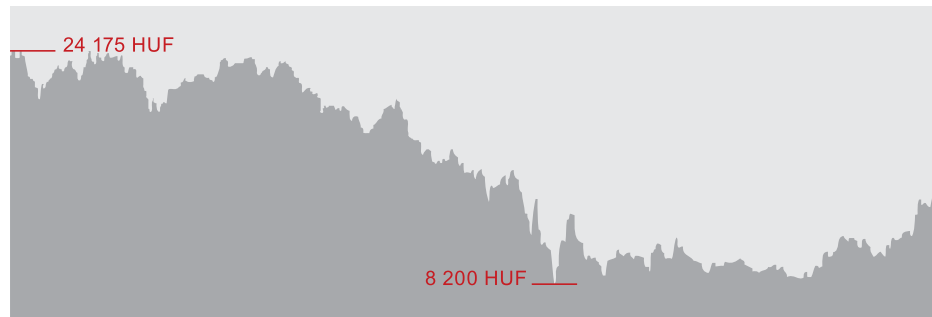
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The value of MOL shares  
throughout 2008



15

4.

## *The paraffin wax cartel*

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According to the New York Times, the most important items of evidence concerning the paraffin wax cartel (involving Sasol, Repsol, Tudapetrol, Hanson&Rosenthal, ENI, RWE, MOL, Total, ExxonMobil and Shell) operating between 1992 and 2005 were found at MOL's premises. The European Commission imposed a total of 675 million euros in fines (23.7 million euros of which on MOL), an amount that is relatively minor compared to what the companies involved may have to pay out in damages to claimants. Only Shell received full immunity from fines for being the first to come forward with information about the cartel.

A high number of actions for damages is expected to be instituted beyond the cartelling period as paraffin wax is used for the manufacturing of a wide variety of products, like candles, grease-proof paper, paper cups and plates, cheese wax, chemicals, tyres and car parts. MOL has emphatically pointed out that they have put in place new regulations to prevent any such issue occurring in the future. Anyhow, this affair will keep teams of lawyers busy dealing with damages actions, giving a hard time to former cartel members for some time to come.

The fact that the cartel's existence was eventually revealed probably has to do with cartel members keeping an eye on each other and the energy war being increasingly aggravated.

5.

## *The Pilis gas line*

According to spokeswoman for MOL subsidiary FGSZ Földgázszállító Zrt Edina Lakatos, future gas supply needs in southeast Budapest and Százhalombatta warrant a 55-km-transmission pipeline (DN 800 PN 63) to be built from Pilisvörösvár to Százhalombatta. In addition to supplying increasing needs in the region, the new line will contribute to the provision of gas and power supply in Budapest and environs, where gas supply would otherwise be insufficient after 2010.

The spokeswoman says the construction of the new gas transmission line will necessarily disturb the harmony of nature on a temporary

basis, but FGSZ has substantial and stringent requirements for nature conservation, which are strictly adhered to during project implementation. Acting in its capacity as technical supervisor, FGSZ took utmost care in preparing the project to ensure that all statutory obligations were fulfilled by both FGSZ and its subcontractors. There is a valid construction permit in place for the gas pipeline construction works, after completion of which land remediation will take place as an integral part of the project.

16

The problem does not lie in the fact that a MOL-owned company is laying, but in routing it through the Pilis forests. Some say local residents were given no official information whatsoever about the project, not even from the local media. The original route was planned across an illegal waste dump on a private area behind Pilisvörösvár-Szabadságliget. Some tried in vain to prevent the rubbish along the route being buried and to arrange for it to be removed from the area instead. The solution MOL eventually decided in favour of was to fell trees to clear the way for the new line.

This raises the question of whether the contractor really confines planning work to reviewing some maps in a secluded office somewhere, without ever visiting the actual site. Moreover, the rerouting to avoid the rubbish dump was executed curiously fast. It is also not known how MOL is going to will guarantee to prevent further damage to the environment in the affected areas.

Here are some photos of the project:



The pink stick indicates the original track (first row, right) / The original and the new track (third row, right) / 2005, 2008 (fourth row)

## MAYOR'S STATEMENT

*(on the gas pipeline project)*

Over the past week, MOL's gas pipeline, planned to run through the Pilis to Százhalombatta, has become a widely-discussed topic on the Internet and in the broadcast media. Please be informed that the Municipality of Pilisvörösvár is not involved in the pipeline project, either as an owner or operator or licensing authority.

That said, the Municipality passed multiple resolutions last spring with a view to protecting the environment and safeguarding the interests of property owners affected by the pipeline. The Municipality protested against the project, made re-routing suggestions and even hired a lawyer to find out what action could be taken to prevent the construction of the pipeline.

Unfortunately, little was achieved. The construction permit was issued by the Budapest Mining Inspectorate which was responsible for obtaining approvals from various authorities, including the Environmental Inspectorate. As one of such authorities, the Municipality of Pilisvörösvár could only have minor influence on the line routing.

As some MOL people said at the time, "Even if we had wanted to run the pipeline right through the town hall, all you could do would have been to ask us not to do so".

As a municipality, we have done everything in our power regarding this issue. We have exchanged multiple letters with MOL, hired a lawyer to assess alternative courses of action for the municipality, convened a forum and arranged legal advice for all property owners and even contacted The Clean Air Action Group, a major environmental NGO, on the issue.

All we achieved was to receive threats from MOL to sue the municipality for HUF 100 million in damages for 'playing for time' in an administration matter. The Municipality's lawyer considered the threat to be taken seriously. His written opinion reads "...if a claim is submitted for damages caused in an administration matter (which requires a separate procedure to substantiate the claim by proving the occurrence of the damage and the culpable and unlawful nature of the tortfeasor's conduct, as well as a clear cause-effect relationship between the two), the Municipality may be found liable."

In summary, despite not being an owner or operator of the area concerned, the Municipality has made very effort to mitigate the pipeline project's impact on natural and economic resources.

*Dated in Pilisvörösvár on 14th February 2008*

*István Gromon*

*Mayor*

It is particularly curious that then Minister of Economy and Transport's response to opposition MP Dénes Gulyás' question about the gas line is nearly identical with the communication issued by FGSZ spokeswoman Edina Lakatos.

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*“For various reasons (obstacles in the form of mines, railway, villages, etc.), the line is bound to run through forested areas. In the planning phase, special care was taken to find a route with the least impact on natural assets. The line is therefore mainly routed through uncharacteristic pine forests and non-indigenous locust forests of a low silvicultural quality and limited ecological value...” (Csaba Kákósy, Minister of Economy and Transport)*

*“For various reasons (obstacles in the form of mines, railway, villages, etc.), the line is bound to run through forested areas. In the planning phase, we closely collaborated with the authorities, local forest management organisation Pilisi Parkerdő Zrt and specialist consultants from the Duna-Ipoly National Park to find the least painful solution from the nature assets point of view. The line is therefore mainly routed through uncharacteristic pine forests and non-indigenous locust forests of a low silvicultural quality and limited ecological value...” (Lakatos Edina, Spokeswoman for FGSZ)*

A univocal opinion is also fostered by the opening in 2009 of a forest walkway that belongs to the village of Piliscsaba and was built by MOL as part of remediation operations under the pipeline project. This ‘success story’ was communicated jointly by Piliscsaba’s municipal council members, local NGOs and MOL.

6.

## Medgyesbodzás – Gábortelep

(25-02-2008)

Behind the Kiss Ernő farm just off a small village near Mezőkovácsháza, an oil well that had been shut down for years was reopened after a padlock was forcibly removed. The unknown perpetrators must have been frightened by the sight of crude oil gushing out of the tap and quickly abandoned the scene. Gas, too, escaped from the well and subsequently evaporated. MOL used lorries to remove contaminated soil from the area.

Remediation cost nearly HUF 30 million. MOL is planning to put the well on stream again this year, someone having apparently anticipated it. The incident was notified to MOL by locals. Although neither signs nor tapes were placed to warn people off, MOL’s representatives on site instructed both the deputy mayor and journalists to leave the area on grounds of safety. However, according to disaster relief professionals, there was no fire or explosion hazard on the site.

7.

## Friendship oil pipeline

(14-10-2008)

Under pressure of 45 bar, crude oil spurted out of the Friendship oil pipeline as high as ten metres at kilometre 44 of Motorway M0 between

[http://www.indavideo.hu/video/Lovellt\\_a\\_koolaj\\_Ecsernel](http://www.indavideo.hu/video/Lovellt_a_koolaj_Ecsernel) (video)



Vecsés and Ecser. A continued supply of oil from the line subsequently created a considerably large oil pond.

Sources:

Remediation work could only be started after the affected section of the pipeline was isolated. Oil was pumped out of the pond and oil-soaked soil replaced. MOL's completing the isolation would not stop the discharge of oil from pipeline, as it was going to take quite a long time for the line section to be emptied on a sloping ground. Fire fighters tried to contain the spill using sand, while engineers continued to work on isolating the damaged pipeline section.

According to the County Disaster Relief Authority, several hundreds of thousands of litres of oil spilled have caused a major environmental pollution.

Some photos about the pollution:



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8.

## *MOL abroad*

### *Hungarian Oil Company to be sued over environmental pollution in Yemen (2007)*

The Hadramout local council has decided to take legal action against Hungarian oil company MOL for polluting the area of Al-Dhaliha district, located 270 kilometres west of Mukalla. The local council decided to bring the issue to court after numerous reports from area residents.

<http://www.arabenvironment.net/archive/2007/3/182906.html>

In a meeting in Mukalla last week, the council pointed fingers at MOL for causing environmental hazards that detrimentally affected citizens. It also promised to call for international environmental organisations to determine the oil firms' compliance in terms of environmental safety.

The council did not allude to the incidence of pollution in the area, whether it's high or low and how many were affected by the pollution. According to one source, MOL began drilling an exploratory well for oil in 2001, but the chemical waste resulting from the drilling was left uncovered at the site. Residents of the village did not realise the hazards until an unidentified disease soon began spreading among those residing around the waste.

Some of the infected people needed medication and even travelled

to Jordan for treatment, where Jordanian doctors concluded that a highly-poisonous material was likely to have caused their diseases. The company has turned down locals' demands for reimbursement of related expenses.

In the meantime, the number of cancer patients increased in the area and even stomach cancer cropped up, cases of which had never until then occurred due to local eating habits. Some international committees examined the composition of the leftover materials and reported that they were free of any toxic substances. However, according to some sources, some committee members disagreed with the official report.

The waste remains in the same location until now, and when it rains, the water washes part of it into nearby valleys, which poses a threat to animals and people. What aggravated the situation was the company allowing its workers to sell used and probably contaminated barrels to residents to use as containers for storing water and seeds.

The largest non-partisan newspaper in Hadramout, Al-Muharer, published a report in May 2006 about the hazardous waste, quoting Obead Salim Balahrak as saying, "We were happy when the oil company came to drill in our village. We thought our water shortage problem would come to an end and our sons would find jobs in the firm, but nothing of the sort happened. They drilled for oil near our houses and we even helped them. We sent a message to the official in Hadramout to solve the water shortage and compensate us for our land".

Although Hadramout Deputy Governor Awadh Hatem ordered MOL to supply the houses with pure drinking water, his orders went up in smoke. After finishing drilling the well, the company poured the waste over a mountain range, violating all environmental regulations and refusing to comply despite being directly instructed by the authorities to do so.

Salim Bamasad, a cancer sufferer, says, "I am exhausted by the treatment expenses. I suffer from blood carcinoma. I have heard that the government may pay some \$10,000 in compensation, but I need \$35,000 for the treatment, which I can't afford. I have no choice but to await death".

Omer Balahrak lost a son. "While I was with him at a Sana'a hospital, a doctor asked me if there was any oil drilling near where we lived. She said this was a crime and carelessness regarding people's lives and that we should sue the company".

According to information obtained by Yemen Times, the Hadramout governor sent a letter in June 2002 to the management of MOL, informing them of what had happened. Minister of Oil Rasheed Baraba sent a letter to the Hadramout governor telling him that the ministry would bear the expenses of treating two of the cancer patients – in 2005, three years after residents first reported the incident.

Former Hadramout Secretary-General also addressed the manager of the Ministry of Oil office in Hadramout, telling them that there was a spread of disease among locals, probably caused by the waste in the area. The Ministry of Oil established a department for environmental

oversight by a decree in 2006, but when Yemen Times contacted the department, they were referred to the local authority.

9.

## E85

22

A Budapest filling station is expected to start selling E85 bioethanol in 2009, says a Hungarian representative of a car maker that produces vehicles that can run on bioethanol. E85 is a fuel blend of 85 per cent biologically produced ethanol and 15 per cent 95-octane petrol. The environmentally benign fuel will come from a Swedish supplier, whose sponsorship allows the new product to be 30 per cent cheaper than 95-octane petrol. The Swedish exporter plans to ship an initial 10 000 litres of E85 to Hungary and then go on to supply more subject to demand.

Both Saab and Ford have started selling E85-capable cars at prices three to five per cent higher than those with conventional engines. Sales have so far been scarce, but hopes are high that there will be an increase.

E85 may be filled into conventional cars 'at one's own risk', but it is not good for the engine. Experience shows that conventional engines can tolerate a bioethanol content of up to five to ten per cent without failure. Involved in coordinating setting up Hungary's first bioethanol filling stations, Saab announced in late summer 2007 that green petrol was going to be available in Hungary. Since early 2008, legislation has made this type of fuel a competitive choice by exempting bioethanol from excise tax.

The opening of E85 filling stations is delayed because oil companies have expressly prohibited their franchise operators from selling E85 and the registration and financial licensing procedures for independent filling stations is more time consuming.

Sources:

Bioethanol has a lower energy density than petrol, therefore 'green cars' consume 20 to 30 per cent more than conventional ones. On the other hand, it boosts engine performance. For instance, a two-litre 150 horsepower engine can produce 185 horsepower when run on bioethanol. Since 2008, all petrol sold in Hungary has contained two per cent bioethanol, blended by MOL into petrol as an octane boosting additive.

In Germany, the first E85 filling stations were opened last year, numbering 50 by today. Sweden has 628 E85 stations, looking to increase the number to 800 by 2008. E85 petrol stations have been opened in France over the past few weeks and, according to the French government's plans, the end of the year will see the number reach 500.

<http://www.e85kft.hu/>

<http://www.origo.hu/auto/20071003-mar-negy-bioethanolkut-mukodik-itthon-egy-tobb-ceg-knal.html>

<http://index.hu/gazdasag/magyar/bio080811/>

[http://www.paszti.hu/portal/index.php?option=com\\_content&view=article&id=54:e85-bioethanol-mindenkinek&catid=1:friss-hirek&Itemid=50](http://www.paszti.hu/portal/index.php?option=com_content&view=article&id=54:e85-bioethanol-mindenkinek&catid=1:friss-hirek&Itemid=50)

<http://www.zoldtech.hu/cikkek/20070814-E85-bioethanol>

[http://www.zoldtech.hu/cikkek/20060828e85/index\\_html](http://www.zoldtech.hu/cikkek/20060828e85/index_html)



## Biodiesel

Following an investment of 40 million euros, the Komárom facility of Rossi Biofuels, a company owned by Austrian Roth Group and MOL, has commenced biodiesel production with an annual output of 150 000 tonnes. The primary feedstock used is rapeseed. The plant was started just in time, as ordinary diesel sold at filling stations in Hungary must contain a minimum of 4.4 per cent fuel of vegetable origin to come under a lower excise tax band from 1st January.

The opening of the new production facility was timed to coincide with the introduction of this new requirement, as purchase of biodiesel from a plant owned 25 per cent by MOL would apparently be at a more competitive price than from external sources. As reported earlier, MOL awarded contracts to multiple biodiesel suppliers after a tendering process in 2006, which means purchase from external sources still remains a possibility. MOL's domestic biodiesel needs are 200 000 tonnes, 120 000 of which will come from Komárom.

The related permit issued by the Competition Authority shows that Rossi Beteiligungs GmbH, which owns 75 per cent of Rossi Biofuels, Komárom is a member of a group run by Austrian businessman Rudolf Roth, from whom MOL purchased 20 filling stations and 52 automatic diesel pumps in the area of Graz and Linz back in 2004.

Sources:

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<http://index.hu/gazdasag/magyar/bio060728/>

[http://www.mol.hu/hu/a\\_molrol/beszallitoi\\_kozpont/biodizel\\_tender/](http://www.mol.hu/hu/a_molrol/beszallitoi_kozpont/biodizel_tender/)

[http://hvg.hu/gazdasag/20070129\\_mol\\_biodizel.aspx](http://hvg.hu/gazdasag/20070129_mol_biodizel.aspx)

<http://www.nol.hu/archivum/archiv-391978>

<http://www.mfor.hu/cikkek/28830.html>

[http://www.greenfo.hu/hirek/hirek\\_item.php?hir=15796](http://www.greenfo.hu/hirek/hirek_item.php?hir=15796)

<http://www.zoldtech.hu/cikkek/20080130-Komarom-Mol-biodizel-uzem>

<http://www.privatbankar.hu/html/cikk/friss.php?hir=35430>

<http://www.okoline.hu/hireink.php>

With the partially MOL-owned plant in Komárom put in operation, there will be an increased demand for rapeseed in Hungary, which in turn is good news for many, including Vice Chairman of MOL's Board of Directors (and Chairman of OTP Bank) Sándor Csányi, who has recently acquired controlling interest in one of Hungary's largest rapeseed producer, Bóly Zrt.

According to the Central Statistical Office of Hungary, last year saw an increase in oilseed rape production, partly generated by EU-supported biodiesel production. There is no direct link between Bóly and Rossi, as the rapeseed received from producers is processed by a third company to create a product the biodiesel producer can use, and there may be further middlemen in between all these parties. However, a producer may only be eligible for major grants if there is a direct trade link between the rape farmer and the biodiesel plant. Both Rossi and Bóly have refused to comment on this issue.

As the primary wholesale trader of fuel in Hungary, MOL has been complied with all Hungarian biofuel standards imposed in accordance with European legislation over the past years, sometimes even surpassing statutory requirements. However, there have recently been dissenting voices heard from EU officials claiming that the production of biofuel additives causes more emissions than biofuels themselves can save and the resulting increase in food prices only adds to the problems.

### III. THE WAY WE THINK

1.

#### *MOL and the Environment*

(I/2)

*"The MOL Group is committed to sustainable development. We recognise the need to create shared values. We also regard SD as a benefactor to society and a provider of great value to our business as well." • (MOL Annual Report 2008)*

As far as sustainable development is concerned, we believe MOL takes the wrong approach, covering the company's financial sustainability and the importance of staff training under the same chapter. This approach is based on the 1987 Brundtland Report, the underlying concept of which many experts say has become obsolete by today.

Instead, a new direction should be taken to replace the old three-pillar approach (society, economy and the environment) by the new inclusion sustainable development should be reconceptualised more as a series of concentric circles with economy - the smallest unit, in the middle, the society and encompassed by the environment. Unfortunately the continued growth of the economy, coupled with unthinking and careless conduct by some players, poses an increasing threat to the both society and the environment.

NSC disagrees with this statement in MOL's Annual Report, as sustainable development should not be a provider of value to business but rather an obligation that cannot be evaded. Neither is sustainable development a mere benefactor to society but more like the only course that can and must be followed.

That may well be why it is regarded that the Sustainability Report as a very nicely presented document, but with a great deal of confused statements that do not reflect the company's commitment to the environment.

Derived from MOL's initial approach is the perception of environmental and social issues as a key to long-term business success, and climate change as a factor affecting earning capacity. We believe that this approach should be revised urgently to give environmental and climate protection priority over business success and profitability in an effort to ensure the survival of mankind and the earth's biosphere.

In this light, the Annual Report considers the prevention of environmental damage important only insofar as it safeguards MOL's business reputation, and not regard it as an obligation to be fulfilled without external imposition.

The **STRATEGIC AND FINANCIAL TARGETS** for the Period 2006-2010 fail to cover environmental protection, sustainable development,

protection of local heritage or social responsibility, which any such geographically diverse oil company as MOL should in fact take into account. The document deals with growth, efficiency, financial flexibility, development of the retail network and transit revenues, which we think are quite well-justified objectives, but should not be the sole strategic focus.

The MOL website offers a playful tool to calculate how much carbon dioxide emission one's lifestyle generates (if one can answer all the questions). The hitch is that the application refers to the result of the calculation as the quantity of carbon dioxide one burns. Of course, carbon dioxide is not burnt, but emitted here.

*„The MOL Group paid HUF 92.23 million in HSE related fines in 2008, out of which the most significant was that imposed on the two refineries (Duna and Tisza) in Hungary, for air pollution issues. These amounts were imposed for excessive emissions from the FCC and Claus Units during 2007. During 2008, these units were upgraded / renewed, therefore no similar fines will arise for the year 2008.” • (MOL Annual Report 2008)*

Regrettably, this statement also testifies to the above-mentioned approach issue. We believe that fines should not be the driving force behind the need to curb air pollution, but rather a commitment towards society and the environment. As MOL keeps advertising such a commitment, we should like to see MOL implementing their principles in actual practice. On the other hand, it seems to prove that environmental penalties do achieve the purpose they are designed for, forcing companies to invest in measures to reduce environmental pollution.

*“The Gas & Power Division was formed in 2008 in order to provide reliable, environmentally friendly and efficient natural gas and energy supply within the MOL Group and for external market participants...” • (MOL Annual Report 2008)*

We are, of course, very happy to see MOL set up that division and particularly that their objectives include ensuring an environmentally friendly and efficient natural gas supply. However, the Annual Report does not give any clue as to whether this issue has been dealt with before or is something of a new initiative. That said, the question arises how the use of natural gas can be referred to as environmental in an age when the link between fossil fuels and climate change is beyond doubt.

Environmental data in the Annual Report are extremely scarce. Quantities of non-hazardous waste, the volume of spills, water consumption, hazardous air pollutants and many other details are first recorded in 2008. It is difficult to accept the fact this area has received so little attention. We very much look forward to the 2009 Report and a noticeable decrease in waste quantities.

Comparable data include carbon dioxide emissions from MOL Group facilities under the European Emissions Trading Scheme. 2008's 6.42 Mt seems to be a considerable increase from 4.09 in 2007 and is the 1 per cent decrease targeted by MOL. As the company explains, it is caused by the commissioning of a steam boiler in Duna Refinery, the inclusion of additional installations in the scheme for the second trading period, as well as new acquisitions.

It begs the question what exactly MOL means by '*carbon thinking*' approach it adheres to. A more detailed explanation would have been welcome both on the website and in the Annual Report.

A review of annual activities shows no evidence of implementation of the guidelines under "*Social impact on communities*" and "*Compensation and relocation/resettlement*". The most controversial issues are related to the Piliscsaba gas pipeline project, where adherence to MOL's principles is uncertain.

The guidelines state that stakeholder views are always incorporated in final project plans. Yet this is contradicted by the mayor of Pilisvörösvár's statement quoting MOL tell them "*Even if we had wanted to run the pipeline right through the town hall, all you could do would have been to ask us not to do so*". A lack of effort to reach agreement is evidenced by the fact that, according to the mayor, MOL threatened to sue the municipality. In our opinion, abuse of a dominant position is characteristic of large corporations, and clearly inconsistent with MOL's policy. It is highly problematic that support for local initiatives is mentioned in this case as a potentially positive outcome of the project, since the results appear more as buying public acceptance.

Last but not least, here is an interesting fact about the Annual Report. The complete Report consists of 263 pages, of which 12 are devoted to the environmental chapter with 5 taken up by pictures and 3 pages of the remaining 7 used to describe strategic objectives. MOL has set out 7 strategic objectives, only one of which is related to environmental protection. It follows from the above that just a little more than 4 pages of the 263-page Annual Report are dedicate to the environment. In terms of proportion, it means 1.5 per cent. We believe MOL should pay more attention to this area.

2.

## *Social Responsibility*

(I/3.)

Compared to other major Hungarian companies, MOL is considerably active when it comes to corporate social responsibility. The Green Light for Our Environment programme, run in collaboration with the Ökotárs Foundation, is described above. The programme is very welcome; yet, we think that the funds spent on advertising it (and MOL at the same time) should be reallocated to the programme proper to increase funds to be awarded.

Yet this programme is the only environmental one of MOL's nine CSR programmes (not all of them for 2008), despite the environment being what MOL causes the greatest harm to by its everyday activities. It would therefore be reasonable to concentrate more on supporting this area, of course, while keeping a focus on greening core activities.

## *Activities outside Europe*

(I/4.)

It is notable that MOL uses standards that surpass local environmental requirements abroad, particularly in developing countries where such advanced regulations are not in place. There are particular cases that do give pause for alarm.

27

The **YEMENI** case requires further investigation into specifically for what MOL is culpable, in spite of its assertions that the project was performed “with the greatest care for the environment” and production having never commenced after unsuccessful exploratory drilling activities.

As far as MOL’s foreign partners are concerned, the situation is hardly better. In **INDIA**, Oil and Natural Gas Corporation Limited (ONGC) is involved in multiple environmental pollution cases and has since 1994 been continually criticised by green organisations, local residents and the military for causing air, water, soil and noise pollution. A significant proportion of such pollution does not occur under normal operating conditions, but is due to outdated processes or negligence.

That was the case with the Nagaland State incident, where residents and the local authority had ONGC’s facilities shut down because of the company’s continued failure to limit pollution and implement promised upgrades. For the latter, it is, however, not only the oil company that should be held responsible, but also the local government, as only a small portion of royalties production companies pay is channelled back to areas affected most by production activities. It is sad that

ONGC’s terminating production helped neither reduce the level of contamination, nor launch local development projects. In fact, the extent of contamination only aggravated with time, as aging equipment was posing an increased, serious hazard. There are now plans to restart production, while locals remain resolute in opposing ONGC’s proposition until existing contamination is remediated and long-promised upgrades are put in place.

Since 2004 in Iraq, the Kurdish Regional Government has signed agreements with over 20 oil companies, including MOL. While these agreements should be open and transparent, the Regional Government refuses to disclose these to third parties. While most of the agreements are for exploration, in two instances the contracting parties have already started production. At the same time, Iraq’s oil minister considers the agreements invalid but is unable to stop the Kurdish Regional Government from making such agreements.

Though the above cases may be regarded as isolated incidents, but it should be noted that corruption, living difficulties and technological backwardness are all very present in these regions and affect oil companies’ activities. Therefore, we believe that oil companies should not engage in production activities in developing countries, unless

supported by local residents. If any such project does take place, it is essential that local communities benefit through improvements in living conditions, otherwise tensions that cannot be resolved to mutual satisfaction are bound to emerge.

4.

## *Development opportunities*

(I/5., II/9.)

### *Energy from water resources and terrestrial heat*

Heat through the earth's crust increases by one degree centigrade for every 33 metres of depth. In the Carpathian Basin the same figure is reached after 22 meters and between 13 to 25 meters in central Hungary between the Duna and Tisza Rivers. Hungary's underground water reserves contain 4.7 million petajoules of energy, of which around 260 petajoules, or over one-fifth of Hungary's annual energy needs, could be used in compliance with relevant regulations. Yet currently only three petajoules is in use.

Geothermal energy can only be exploited if the highly salinated natural groundwater is not discharged into surface water bodies, as damage to aquatic flora and fauna will occur. This was the case with pollution to the Lapincs river caused by the Fürstenfeld geothermal power plant. The resulting year-long intergovernmental dispute will be resolved - rather surprisingly - with the federal state of Styria converting the facility into a biomass fired plant, although the geothermal facility was originally built using EU funds.

Since 2004, any new geothermal power station in Hungary may only be operated with water being reinjected into the ground, as otherwise the strict environmental limits cannot be complied with.

Geothermal energy is a risky business in Hungary, because there is no uniform 'hot sea' under the country. Geothermal energy requires expansive exploration to locate sufficient geothermal resources and determine where to drill production and reinjection wells. During hydrocarbon explorations, many hot water-bearing formations have been accidentally encountered.

MOL lost massive investments near the village of Iklód when it was discovered that the 120-degree hot steam was mixed with oil in a deep aquifer and thus could not be used in the projected power station. The extra energy needed for possible oil removal would have adversely impacted the project's financial return.

MOL is not the only company seeking to implement geothermal heating systems, yet it is well-positioned financially. One such company, Pannergy, lacks sufficient resources and therefore is interested to obtain loans from the European Bank for Reconstruction

and Development and European Investment Bank, and grants from the EU to assemble enough funds for their projects. As its competitor, MOL intends to use geothermal energy for electric power generation, for which the more common low-temperature resources are not suitable.

We hope that MOL will increasingly focus its attention on geothermal energy, Pannergy will succeed in entering the market, which would not only increase the proportion of green energy generated, but also compel MOL to be more active in this area. It should, of course, be remembered that, as in every aspect of life, moderation is very important to allow 'refilling' and regeneration.

Sources:

[https://www.mke.org.hu/index.php?option=com\\_content&task=view&id=152&Itemid=98](https://www.mke.org.hu/index.php?option=com_content&task=view&id=152&Itemid=98)

<http://zoldtech.hu/cikkek/20080422-gamma-valerolakton?h=1>

## *Gamma-Valerolactone*

Gamma-Valerolactone (GVL) is a low-molecular substance, naturally occurs in fruits, and can be used as liquid biofuel. A research team lead by Tamás István Horváth at ELTE University, Budapest published their findings in the academic journal Green Chemistry. The publication was even reported by the Royal Society of Chemistry's website.

## *E85*

Some might say that the E85 is a promising option to reduce oil consumption, domestic fuel distributors hinder the spread of E85 pumps. MOL's purpose can not be anything else than to ensure that fossil fuels remain dominant. MOL argues that the very low number of vehicles that could reliably run on E85 does not warrant a serious focus on this "special segment".

We are of the opinion that biofuels are not a suitable replacement for fossil fuels, as their production involves its own set of problems (increasing land use, loss of biodiversity, conservation of water resources, food price rises, issues of food supply) that are just as difficult to tackle as those caused by the use of fossil fuels. Consequently, NSC is against the widespread and extensive use of biofuels. We believe that the reduction of the use of fossil fuels combined with an enhanced energy efficiency and energy savings measures and a gradual shift to an increased use of renewable energy, may be the key to a sustainable economy.

Sources:

<http://www.agrotrend.hu/cgi-bin/agrotrend/index.cgi?view=ck&tid=415&nID=18508&nyelv=>

5.

## *Economic events and challenges*

(II/1., II/2., II/3.)

Considering OMV's attempted takeover, the introduction of the Robin Hood tax and the global economic downturn, MOL's 2007 dividend announcement was anticipated with curiosity. As reported at the Budapest Stock Exchange's website, MOL was going to pay a dividend of HUF 883.36 per share, giving a total payout of HUF 85 billion.



In the light of this, fears aired earlier over the Robin Hood tax are hardly substantiated. 2008 data show that MOL's pre-tax profit of HUF 158 billion (well below 2007's HUF 344.3 billion) would be subject to a Robin Hood tax of 12.64 billion, in addition to a 16 per cent corporate tax of HUF 25.28 billion. As a result, the amount of dividend per share would be reduced by HUF 131 to 752, (based on 2008 data).

Of course, the company's management and shareholders would not be happy to pay the surtax of 8 per cent; yet we think it is not a considerable amount compared to the 85 billion paid out as dividend. We are of the opinion that under the current circumstances, when the livelihood of hundreds of thousands of people in Hungary is put at risk amidst the global economic crisis, it is only right that the individual taxpayer is not left alone to bear the brunt of the downturn and the owner-investors making billions of extra profit should also contribute a portion of their profits to society to mitigate the impact of the crisis.

## *Nabucco and South Stream gas pipes*

Increasing support for the project and developments regarding its implementation have given rise to growing concern. The political leadership of Turkmenistan, which would be the main source of supply, is controversial. Civil liberties virtually do not exist and the country is run by an incestuous political elite. All that is known about the recoverable quantities of gas in Turkmenistan's reservoirs is that it is plenty. It is probable that local communities will not benefit from the money flowing into the country as a result. An indeed, they may not even know a lot about the gas pipeline being planned.

Hungary's involvement in the project is difficult to justify. MOL and Exxon Mobil have discovered a large gas field near Makó in southern Hungary that could be put on stream by 2012 and has reserves enough to supply Hungary's needs for the next 50 to 100 years (which also makes it difficult to understand why MOL and Gazprom managers are in consultation about the details of a gas storage facility to be built in Hungary if the South Stream project goes ahead). This remains true independent of serious doubts about the actual quantity and recoverability of such gas. One thing is sure, Nabucco will help enhance energy supplies and energy security for Hungary. NSC believes that participation in the Nabucco project is needed primarily to generate transit revenues.

Considering the adverse impacts of construction works and ever-increasing project cost estimates, it may not be worth the trouble – not to mention the fact that spending the same amount of money on the energy efficiency upgrade of buildings, as well as on further research into, development and use of renewable energy would represent a much more progressive approach. Incidentally, the quantities of oil, gas and coal consumed in a year are the product of 500 years of photosynthesis, that is, indirect solar energy.

We believe that the events and developments dealt with in this chapter give sufficient reason for the management to take a not so keen focus off the environment.

Sources:

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6.

## *The Pilis gas line*

(II/5.)

The municipalities of both Piliscsaba and Pilisvörösvár are in disagreement about this issue. In our opinion, negative impacts on the environment are hardly remedied by a forest walkway being built over the pipeline one and a half years later. We think that a company should not only proclaim a commitment to the environment, but also follow up on it, which does not at all seem to be the case with the Pilis gas pipeline. It appears that MOL failed to adhere to its own policies and principles during the project. Despite all the positive statements in project specifications and summaries, this project remains the most problematic issue for MOL in 2008 – a fact evidenced by the tone of related ‘articles’ quoted in the previous chapter.

7.

## *Medgyesbodzás – Gábortelep*

(II/6.)

We find it rather difficult to understand why wells are not guarded by security staff or fitted with safe shut-off devices that can only be opened with special tools. We believe that MOL’s leaving a shut-down well unattended makes it responsible for the incident. Much more care should be taken in this regard.

## IV. AN OUTLOOK ON INA

### *MOL in Croatia: let's not learn from INA*

Industrija Nafta d.d. (INA), Croatia's main oil company, is the largest company in the country for oil and gas exploration and production, oil refining and the distribution of gas and petroleum products. It has onshore and offshore oil and gas exploration facilities within Croatia and other licence interests in Angola, Egypt, Syria and Namibia. It also has refineries located at Rijeka (Urinj) and Sisak, and lubricants plants in Rijeka (Mlaka) and Zagreb, as well as a chain of some 415 retail outlets and terminals throughout Croatia and neighbouring countries.<sup>1</sup>

INA was founded on 1 January 1964. In 1990, it became a state-owned company and in 1993 a joint stock company. The first stage of privatisation, when MOL Company became INA's strategic partner by purchasing 25 per cent plus one share, was completed in 2003. INA is now owned 47.155 per cent by MOL, 44.836 per cent by the Croatian government and 8.009 per cent by institutional and private investors.<sup>3</sup>

<sup>1</sup> INA webpage: <http://www.ina.hr/default.aspx?id=272>

<sup>2</sup> INA webpage: <http://www.ina.hr/default.aspx?id=267>

<sup>3</sup> INA webpage: <http://www.ina.hr/default.aspx?id=565>

### *INA's corporate social responsibility framework*

INA, like most other oil companies, has in recent years put considerable effort into improving its environmental image. It belongs to numerous national and international initiatives such as the Corporate Social Responsibility Association and the Environmental Protection Association of the Croatian Chamber of Economy (CCE), and the UN Global Compact. The INA Code of Business Conduct and Ethics came into effect at the beginning of 2007, with guidelines corresponding to the principles of the Global Compact on relations toward work, coworkers, business partners, healthcare, safety, environmental protection, respect for the law and custom, guidelines against conflicts of interest, and control mechanisms.

One of the most visible ways in which INA has sought to improve its image within Croatia is through advertisements. These have attracted considerable criticism from Croatian civil society organisations (see below), which feel that INA's claims do not match reality.

### *Environmental issues*

INA's most serious environmental impact in Croatia results from its direct and indirect climate impact and its oil refineries in Sisak and Rijeka. Further impacts come from oil spills in its exploration and production division.

## Climate Impact

INA has stated on its advertising billboards that 83 per cent of Croatia's total energy comes from oil and gas. In an era where climate change is one of the greatest challenges facing humanity, it is doubtful whether this is something to be proud of.



"83.1 per cent of Croatia's total energy comes from oil and gas" says INA's advertisement. "What makes a wise person ashamed makes a fool proud", was the response from an anonymous group calling itself Sexy Guerillas Against Climate Change .

While INA is not the sole actor that could bring about a large-scale increase in energy efficiency and the use of renewable energy, as the main oil company in Croatia it has an extremely important role to play. It is generally acknowledged that the era of cheap oil is slowly coming to an end, even if there is little agreement about the speed at which it is happening. Every company needs to be prepared for this, orienting its research and development and new investments towards non-fossil energy sources and increasing energy efficiency.

While increasing shortages of oil may initially enable high profits to be made (barring government price capping), a failure to be prepared for a transition to renewable sources of energy presents a large risk for the company. Yet INA does not appear to have shown how it intends to make its transition to renewable sources of energy and needs to map out a strategy for this. The only clear move it has made is the planned introduction of biofuels into the Sisak refinery, which is necessary to comply with the EU targets for the use of biofuel in transport. Moreover it is unclear how INA intends to ensure that the crops it uses are from sustainable sources that will not compete with food crop cultivation.

INA's operations also generate a significant quantity of direct greenhouse gas emissions. In 2007 <sup>4</sup> these were as follows:

<sup>4</sup> 2008 figures not yet available at the time of writing.

Rijeka Refinery - Urinj	886 715 tonnes
Sisak Refinery	701 335 tonnes
Rijeka Refinery - Mlaka	124 833 tonnes
Exploration & Production Division	870 855 tonnes
Retail Network Management Sector	52 tonnes
<b>Total</b>	<b>2 583 790 tonnes</b>



On International Day of Action Against Climate Change, 7 December 2007, Green Action/Friends of the Earth Croatia activists protested against INA's greenwashing and lack of action to tackle climate change.

## Oil refineries

<sup>5</sup> See eg. INA Glasnik, 2 December 2008, <http://www.ina.hr/default.aspx?id=1055>

The city of Sisak is widely regarded as Croatia's environmental hotspot. As well as INA's oil refinery the city also hosts a thermal power plant and a pesticide factory, which contribute to the very poor local air quality. INA is fond of pointing out that it is not the only polluter in Sisak<sup>5</sup>, however the figures from the air quality monitoring station point to its culpability.

Organisational unit	SO <sub>2</sub> emissions (tonnes)	NO <sub>2</sub> emissions (tonnes)	CO emissions (tonnes)	Particulates (tonnes)
Rijeka refinery - Urinj	7 841,97	1 376,28	178,77	77,78
Sisak refinery	7 256,69	1 632,73	168,71	100,25
Rijeka refinery - Mlaka	1 206,91	293,58	82,30	13,09
Exploration and production	17,53	1 608,96	519,89	0
Retail Network Development Sector	0,015	0,21413	0,150542	0,0591
<b>Total</b>	<b>16 322,10</b>	<b>4 911,55</b>	<b>949,67</b>	<b>191,12</b>

Source:

INA Sustainability Report 2007

Az olajfinomítás mindig is környezetszennyező tevékenység marad, a Oil refining will always create pollution. The questions are whether a) moves are being made to significantly reduce the use of oil as a fuel overall, in favour of cleaner sources, and b) INA is doing all it can to reduce the pollution to a minimum and to rehabilitate areas previously affected by pollution.

As discussed above, it does not appear that INA is making efforts to move towards renewable energy sources beyond what is necessary to meet EU targets on biofuels.

On the question of whether INA is doing all it can to reduce pollution to a minimum, the answer is mixed.

In Sisak, the company has started an investment programme and in 2007 the Claus Desulphurization Plant and the storm water section of the wastewater treatment plant started test operations. A pollution monitoring station at Galdovo started regular operations in 2008, however not before INA had paid a fine of HRK 30 000 in 2007 for missing the deadline the government had imposed.

As part of the 2008 activities on the Sisak refinery modernization project, the Hydrodesulphurization Plant for FCC gasoline was completed and started a test run. The reconstruction of the central chimney was also completed.

The desulphurization plants have had a positive impact on levels of sulphur dioxide, which in 2008 with one exception stayed within the limit value of 350 µg/m<sup>3</sup>.<sup>6</sup> However there are still problems with high levels of hydrogen sulphide.

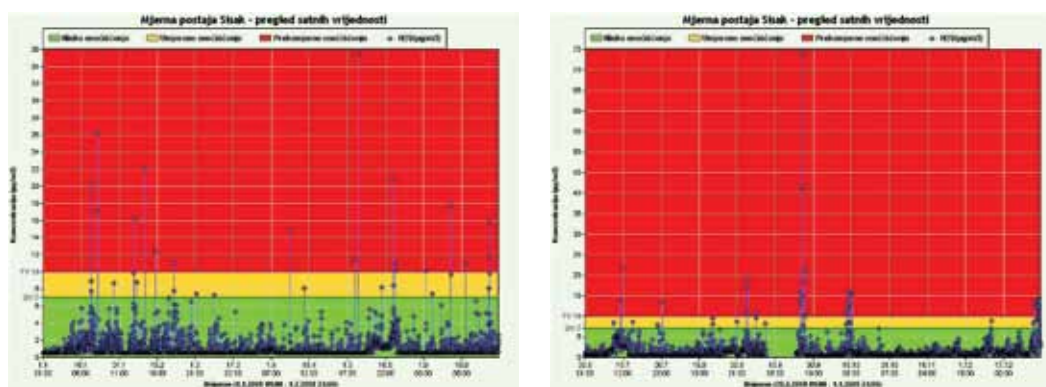
<sup>6</sup> IMeasurements from Sisak monitoring station, supplied by Sisak Ecological Action.

According to local residents' group Sisak Ecological Action the high levels of hydrogen sulphide are a result of the Sisak refinery's antiquated coking plant. This is due to be replaced in 2011-12. Residents have expressed their dissatisfaction that the improvements

that will help INA financially, such as the desulphurization plant necessary to make Euro 5 standard fuel, have been prioritised over the replacement of the coking plant, which residents see as the most important investment for improving the local environment.

In 2007, concentrations of COD, BOD5, phenols, total nitrogen, phosphorous, copper, and total organic carbon exceeded the maximum allowed concentrations set in the Water Management Permit of the Rijeka Refinery - Urinj Plant. The refinery was ordered to align its operation with the provisions of the water management permit and to pay the costs of sampling and analysis. On April 3, 2007 the refinery was fined for non-compliance with HRK 46 070.00 to be paid to the account of the Kostrena municipality.<sup>7</sup> In 2008 The Rijeka Refinery - Urinj site commenced biological treatment of wastewater and renovated 6.000 metres of sewage pipelines. The Rijeka Refinery (Mlaka site) stopped production of base oils, bitumen, fuel oils and paraffin in October 2008, which according to INA's Annual Report 2008 resulted in considerable improvements in air quality.<sup>8</sup>

In 2008, there were 13 unforeseen events with considerable environmental impacts,<sup>9</sup> three less than in 2007. The most frequent causes were leaking pipelines due to obsolescence and corrosion and the breakdown of processing units and product spills.



## False solutions

Instead of a clear focus on energy efficiency and truly renewable energy, INA's statements on using cleaner fuels and reducing emissions tend to centre on using more natural gas, biofuels and carbon sequestration.<sup>10</sup>

While the use of gas is indeed less polluting and climate-damaging than oil and coal, it is nevertheless a finite source of energy which may play an interim role during a transition to truly renewable fuels but should not form the main plank of any investment strategy.

As outlined above, while the EU has a target of using 10 per cent biofuels in transport by 2020, there are significant problems with the production of first generation biofuels. The vast amount of land needed for their production often results in competition with food crops, and they have been associated with the destruction of tropical forests (e.g. for palm oil production or forest clearance

<sup>7</sup> INA Sustainability Report 2007

<sup>8</sup> INA Annual Report 2008

<sup>9</sup> INA Annual Report 2008

<sup>10</sup> See for example INA's Sustainability Report 2007



for soy plantations). It is not surprising that INA is planning to use biofuels in its production considering that EU policy promotes this, however the company should not promote this as clean energy unless second generation biofuels with a low environmental impact become a commercial reality.

Carbon sequestration (often known as Carbon Capture and Storage or CCS) involves injecting carbon dioxide deep into the ground and thus reducing greenhouse gas emissions into the atmosphere. It has recently gained increasing support from governments and companies looking for ways to reduce carbon dioxide emissions without significantly decreasing the use of fossil fuels, while critics point out that it is quite unproven and essentially presents a technological fix that serves to delay the inevitable need to move towards a low-carbon economy. In addition, it is frequently overlooked that carbon capture and storage itself requires significant amounts of energy to carry out, requiring a 10-40 per cent increase in the energy to be produced<sup>11</sup>, and that it sometimes also serves to increase recovery from oil fields by increasing the pressure, which rather defeats the emissions reduction aims of the technology.

INA is actively engaged in developing carbon sequestration, though at least it is more straightforward about its intentions than many other proponents of the technology:

*"In 2006, INA's Exploration & Production Division launched a project for boosting oil recovery from the Ivanic and Zutica fields in Croatia by carbon dioxide injection, which is planned to be realized by 2009. Apart from the direct economic benefits of recovering additional volumes of crude oil, this also involves an indirect environmental benefit of safe carbon disposal, and thus reduced emissions. The EOR project plans to use the carbon dioxide produced at the Molve Gas Plant which is currently being released into the atmosphere.....an optimum amount of 430 000 t carbon dioxide is to be injected annually, which in 2009 would result in savings on carbon dioxide emission fees of HRK 1 791 113 to 5 872 500."*

It is understandable that INA would wish to boost its oil recovery through this method, however it cannot at this stage be seen as an aid to reducing emissions and should not be promoted as such when its primary aim is to recover more oil. INA needs to concentrate on proven means of emissions reduction through moving to low-carbon renewable energy sources and increasing its energy efficiency.

## Greenwashing

In view of INA's poor record in moving towards low-carbon renewable energy and its slow progress in improving its environmental performance in Sisak, it is well known in Croatia as a major polluter. The company has therefore attracted a barrage of criticism for some of its advertising campaigns, particularly one that featured a series of animals and birds in their habitats, with the slogan "Ucimo od prirode", which can be interpreted as either "Let's learn from nature" or "We're learning from nature". Green Action/Friends of the Earth Croatia, concerned by the lack of correspondence between INA's claims and the on-the-ground reality, responded with its own series of 'subverts'.

<sup>11</sup> Bert Metz, IPCC special report on carbon dioxide capture and storage, WMO/UNEP, 2005, p.25



Oil spill: Let's not learn from INA

## *Conclusion*

MOL/INA needs to develop a strategy for transition to a low-carbon renewable economy and take practical steps to implement it as soon as possible. While pilot projects will certainly be needed, the company should take care to avoid tokenism and should ensure that the strategy is comprehensive enough to address the scale of the issues involved. INA must not rely on either unproven technologies such as CCS or those which are technologically proven but have unacceptable environmental impacts, such as many first generation biofuels.

INA also needs to continue the improvements at its Sisak and Rijeka refineries as soon as humanly possible in order to improve the quality of life of local inhabitants, including those improvements which do not necessarily bring any commercial advantage but have a significant effect on pollution reduction.





*“Even if we had wanted to run the pipeline right through the town hall, all you could do would have been to ask us not to do so.”*

*“The MOL Group is committed to sustainable development. We recognise the need to create shared values. We also regard SD as a benefactor to society and a provider of great value to our business as well.”*

*“The Gas & Power Division was formed in 2008 in order to provide reliable, environmentally friendly and efficient natural gas and energy supply within the MOL Group and for external market participants...”*

*“Beyond identifying and mitigating adverse impacts we consider positive reimbursements from the projects. This means not only creating job opportunities but supporting various local initiatives.”*



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