



CENTER FOR **I**NTERNATIONAL **E**NVIRONMENTAL **L**AW

**COMMENTS TO THE IFC
BAKU-TBLISI-CEYHAN PIPELINE PROJECT**

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**CIEL COMMENTS TO THE IFC
BAKU-TBLISI-CEYHAN PIPELINE PROJECT**

I. INTRODUCTION

Purpose Of These Comments

The Center for International Environmental Law (CIEL), based in Washington DC, is particularly concerned with the legal, environmental, and social ramifications of the proposed Baku-Tblisi-Ceyhan Pipeline Project (BTC Project). CIEL provides a full range of environmental legal services in both international and comparative law, including a major focus on the sustainable development impacts of trade and investment. CIEL seeks to ensure that international environmental and human rights rules are developed and applied effectively without negative interference from international trade and investment rules and practices, and that foreign investments and international financial institutions that fund these investments adequately consider the environmental and social impacts of their projects.

The purpose of these comments is twofold. First, we highlight our concerns about the potential adverse environmental and social impacts of the project, focusing primarily on impacts in Turkey. Second, we demonstrate how the BTC Project raises larger issues relating to how the IFC implements its mandate to provide social and economic benefits in order to alleviate poverty.

Methodology and Sources of Information

CIEL has prepared these comments based on its analysis of existing sources of information available in the public domain. CIEL also conducted field research in Turkey during May 2003 to gather first-hand information on the BTC Project. Details of the research methodology employed in field research may be found in Appendix 2.

Contents/Organization of Comments

These comments elaborate on several key concerns that CIEL has identified, namely the Project's impacts on the rule of law and climate change, as well as deficiencies on consultation and compensation. An Appendix also offers an overview of the regional context, particularly in its political and economic dimensions.

II. DESCRIPTION OF PROJECT

Background Information

The BTC Project is proposed by an international consortium of companies known as BTC Co.¹ The project aims to carry Caspian crude oil from the Azeri-Chirag-Guneshli (ACG) fields in the Caspian Sea to a Turkish port on the Mediterranean Sea for delivery to world markets. The approximately 1760 km (1056 miles) long pipeline will run from Baku, Azerbaijan, through Tblisi, Georgia, and will end at the deep water port of Ceyhan, on the Mediterranean bay of Yumurtalik, in Southern Turkey. The pipeline will run underground along the entire route, except for surface pump stations. Project documents indicate that the pipeline has a life expectancy of 40 years, and may be extended for another 20 years,² while the pump stations have a life expectancy of 30 years.

On November 2000, the Main Export Pipeline (MEP) participants issued the Notice to Proceed for the commencement of the Project activities. The construction of the Project began in June 2002 in Turkey. The project is expected to be completed by 2005.

The Project is estimated to cost approximately US\$3.3billion. The BTC Pipeline system is expected to deliver US\$21 million worth of fuel everyday, nearly US\$8billion a year (50 million tones of oil per year). Initially, several oil companies, including BP, were strongly opposed to the project, believing it would be too costly and uneconomical for the planned oil volumes from Azerbaijan.³ The economic soundness of the project is still in question, as further explained in Appendix II.

Legal and Fiscal Regimes Governing Project

The legal and fiscal regimes of the Project are defined within the framework of an Intergovernmental Agreement (IGA) between Georgia, Azerbaijan and Turkey, and the Host Government Agreements (HGA) signed between the Consortium and the individual governments in September 1999 and October 2000 respectively. The Agreements were ratified by Azerbaijan in May 26, 2000; by Georgia in May 29, 2000, and by Turkey in June 22, 2000. By the second week of December 2002, the three governments involved had approved the Environmental and Social Impact Assessments. On May 16, 2003, the three countries issued a *Joint Statement*, intending to clarify applicable project standards, and recently on September 23, 2003 BTC Co. unilaterally signed the *Human Rights Undertaking*, addressing the conflicts between the HGAs and international human rights treaties.

Financing

Although the construction of the Pipeline has already started, financing is still being arranged. The Consortium hopes to fund 70% of the project from public funds via the International Financial Corporation (IFC), the European Bank of Reconstruction and Development (EBRD), export credit agencies (ECA) from Europe (such as the UK's Export Credit Guarantee Department and the UK Department for International Development), the USA (such as OPIC and the ExIm Bank), and Japan. The consortium will cover the remaining 30% of the cost.

¹ The Consortium is also referred to as Main Export Pipeline Participants (MEP) and is led by British Petroleum. Other project participants include: Azerbaijan State Oil Company (SOCAR), Unocal, Statoil, Turkish Petroleum (TPAO), Agip, TotalFinaElf, Itochu, Phillips, Inpex ve Hess. For further information, see www.btc.com.tr.

² Turkey-BTC HGA, Article 3.1.

³ BP cited doubts that sufficient oil had been found to justify these high costs. However, following further research, and negotiations and incentives offered by the host governments, BP decided to participate in the construction of this pipeline and became the leading company of the international consortium.

III. CRITICAL ISSUES/PROBLEMS

We believe the BTC Project raises a multitude of important concerns, many of which have been identified and analyzed by other NGOs and stakeholders. We focus, however, on the following three issues, which are central to CIEL's concerns.

The BTC Project Compromises the Rule of Law

Introduction

The set of agreements and other instruments applicable to the BTC Project (hereinafter referred to as the BTC legal regime) is extraordinary in the degree to which it favors the private investors in this project, and it has caused much concern among civil society organizations and international legal scholars. The BTC Project legal regime is an example of a trend in investment liberalization and protection that undermines democratic structures of governance and the rule of law. These investment agreements favor international corporations at the expense of developing countries and their citizens. Furthermore, they curtail legislative, executive, and judicial powers of local governments; undermine their abilities to protect health, the environment, worker safety, and other public values; and compromise the legal system's ability to ensure compensation for environmental damage, among other problems. Investment agreements typically are negotiated and implemented without adequate public input; and disputes about them almost invariably are settled via arbitral procedures that are not open to the public. Unfortunately, the BTC legal regime epitomizes all of these problems.

This analysis explores the public interest implications of the BTC legal regime, focusing on the abdication of law, the impacts of the economic stabilization provisions on the host-states' regulatory space, the inadequacy of liability standards, the secrecy surrounding dispute settlement, the lack of transparency during negotiations, and BTC's lack of measurable contributions to local development.

Abdication of Law – Contemporary Capitulations

The complex BTC legal regime has as its basis the Inter-Governmental Agreement (IGA) entered into by the Governments of the Republics of Azerbaijan, Georgia, and Turkey. The IGA is elaborated in, and reinforced by, the three separate agreements between the private investors and each of the host-governments (HGAs). For the purposes of this analysis, the most important aspect of the IGA and HGAs are the facts that they:

1. Remove the investors from the reach of the domestic laws of each of the countries;
2. Hold the investors harmless with respect to any future changes in laws ("economic stabilization");
3. Institute instead vague, confusing, incomplete, and difficult-to-prove contractual obligations; and,
4. Remove disputes about the HGAs, including regarding compliance with the contracts' health, safety, environmental, and human rights provisions, from each nation's courts, favoring instead ad hoc arbitration tribunals conducted in Geneva under English law.

Quite apart from the specific substantive inadequacies of this approach, discussed below, these provisions of the Project Agreements compromise the principle of equality under the law, one of the fundamental elements of the rule of law, and undercut the court systems in each of the countries, the effective functioning of which is also essential to the rule of law.

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IGA's article II(2) provides that its attached appendices, the HGAs, are an integral part of the BTC legal regime. HGAs are contracts between the respective governments and the BTC Co. that govern the relationship between the BTC Co. and the host governments, and set out specific procedures and requirements to be followed during the project's construction, operation, and decommissioning. As an integral part of the IGA, HGAs are thus incorporated into the legal system of each country, prevailing over domestic law, except the Constitution, during the life of the project (40-60 years). This abdication of domestic law is all the more problematic because it trades away available legal remedies, including criminal sanctions and administrative fines, leaving only contractual remedies subject to contract law and statute of limitations.

IGA's article IV defines the BTC Project's applicable technical, safety, and environmental standards. According to this provision, the Project shall be governed,

“[...] in accordance with international standards and practices within the Petroleum pipeline industry (which shall in no event be less stringent than those generally applied within member states of the European Union) and the requirements as set forth in the relevant HGA, which shall apply notwithstanding any standards and practices set forth in the domestic law of the respective State.”

The HGA elaborates on this provision further in its Article 13, which states that the applicable health, environmental, and safety (HSE) standards and practices for the BTC Project shall be set forth in Appendix 5 containing the Code of Practice. This Code of Practice provides that project operators shall “comply with good international Petroleum industry standards and practice generally observed by the international community with respect to Petroleum pipeline projects comparable to the Project”.⁴ This code further provides that any project operator “shall have the right to take any action that, in the opinion of the Person so acting, a reasonably prudent operator would take under the circumstances”.⁵ Moreover, the Code of Practice contains many different standards with respect to industry behavior, thus creating a bewildering array of uncertainties, as the following examples illustrate:

- In conducting all activities involved in the construction, reconstruction, capacity expansion, relocation, repair, replacement, decommissioning, dismantling, removal, use or operation of the Facilities (the “Pipeline Activities”) the MEP Participants *shall use Best Endeavors* to minimize potential disturbances to the environment... (paragraph 3.1, p. 3).
- ...[I]n no event shall the Project be subject to any such standards to the extent they are different from or more stringent than the *standards and practices generally prevailing in the international Petroleum pipeline industry for comparable projects*” (paragraph 3.3, p. 3).
- “MEP Participants or any Operating Company shall...*comply with good international Petroleum industry standards and practice generally observed by the international community with respect to Petroleum pipeline projects comparable to the Project*” (paragraph 2.1, p. 2).
- “...in accordance with generally accepted practices and standards” (paragraph 2.2, p. 2).
- “...in accordance with the standards and practices generally prevailing in the international Petroleum pipeline industry” (paragraph 3.10, p. 6).
- “...employing the best practicable environmental option” (paragraph 3.10, p. 7).
- “...the standards relevant to the international community with respect to Petroleum pipeline projects comparable to the Project shall apply” (paragraph 0, p. 1).
- “In conducting the Project Activities the MEP Participants shall use Best Endeavors...” (paragraph 4.1, p. 10).

⁴ HGA, Appendix V, Code of Practice, 2.1.(i).

⁵ *Id.*, 2.1.(iii).

The HGA thus refers to a set of industry standards and practices, not to the standards and laws applied by EU Member countries. Further, these industry standards would not apply if the project operator decides that the circumstances warrant a different practice, in which case this decision prevails over all other domestic and international standards.⁶ Furthermore, in case of conflict between industry standards and domestic or international standards, the former prevail, as follows from the HGAs' preambular paragraph 10 (using the HGA with Turkey as an example):

...[T]he intergovernmental Agreement shall become effective as law of the Republic of Turkey and (with respect to the subject matter thereof) prevailing over all other Turkish Law (other than the Constitution) and the terms of such agreement shall be the binding obligation of the Republic of Turkey under international law;

From a historical perspective, the BTC Agreements resemble capitulation arrangements of the XVIIIth-XIXth Centuries between the Ottoman Empire and Western States. "Capitulation" means giving privileges to foreigners in disadvantage of a country's citizens. The roots of capitulations in the Ottoman Empire go back to the commercial agreement signed between the Ottoman Sultan, Suleyman the Magnificent, and the King of France, Francis in 1536. According to that agreement, Ottoman and French merchants were bound only by their home laws in the conduct of commercial activities. This meant that a French merchant could conduct commercial activities in the Ottoman Territories, bound only by French law. Furthermore, French ships were allowed to trade in Ottoman harbors freely. Later on, particularly during the 18th and 19th centuries, these agreements were extended to other European countries without giving equal rights to Ottoman citizens.

Through capitulations, external European powers were able to intervene into the domestic politics of the Ottomans, while exempt from local laws and regulations. Moreover, all Ottoman ports and trade were capitalized, thus controlled by foreign powers. Capitulations were considered one of the major reasons for the collapse of the Ottoman Empire and have left bitter memories in the Turkish collective consciousness. The Republic of Turkey officially terminated capitulation policies with the Lausanne Agreement signed on July 24, 1923.

Economic Stabilization Clause

Stabilization clauses can take several forms and differ in scope, but all generally aim at protecting the private parties to a contract from application of legislation or administrative measures subsequent to the conclusion of the contract. Earlier models sought to incorporate and freeze the host country's municipal law into the contract,⁷ while current practice prefers to transfer the increased financial burden associated to more stringent standards from the investor to the government, i.e. right to compensation. Economic stabilization clauses such as those in the HGAs thus stand in direct confrontation with the sovereignty of the government to regulate for the public interest, with the polluter-pays principle as the cornerstone of environmental policy, and with the progressive implementation of a human right to a healthy environment.

BTC's stabilization clauses require compensation if newly introduced legal requirements negatively affect the value of the project. The HGAs articulation of this Economic Equilibrium

⁶ More on the gaps apparent in the definition of the applicable health, safety, and environmental standards in the economic stabilization clause, including the deficiencies of the *Joint Statement* and the *Human Rights Undertaking*.

⁷ For example, the BP-Lybia stabilization clause that was later the object of arbitration, *BP Exploration Co. (Libya) Ltd. v. Libyan Arab Republic*, 53 I.L.R. 297 (1979), (Award of Aug. 1, 1974). The focus of earlier stabilization clauses was to prevent nationalization or expropriatory effects of changing tax regimes.

formula rests on two provisions: (a) the Government's covenant to restore the economic equilibrium of the project if affected by a "Change in Law"⁸ and (b) compensation owed to the investors in case of interference with the economic equilibrium of the Project.⁹ The first pillar is composed of Paragraphs 7.2 (vi) and (xi), which provide that,

7.2 "The Government hereby covenants and agrees (on its behalf and acting on behalf of and committing the State Authorities) that throughout the term of this Agreement:

...

vi. "if any domestic or international agreement or treaty; any legislation, promulgation, enactment, decree, accession or allowance; any other form of commitment, policy or pronouncement or permission, has the effect of impairing, conflicting or interfering with the implementation of the Project, or limiting, abridging or adversely affecting the value of the Project or any of the rights, privileges, exemptions, waivers, indemnifications or protections granted or arising under this Agreement or any other Project Agreement it shall be deemed a Change in Law under Article 7.2(xi).

...

xi. "The State Authorities shall take all actions available to them to restore the Economic Equilibrium established under the Project Agreements if and to the extent the Economic Equilibrium is disrupted or negatively affected, directly or indirectly, as a result of any change (whether the change is specific to the Project or of general application) in Turkish Law (including any Turkish Laws regarding Taxes, health, safety and the environment) occurring after the later of (1) the Effective Date or (2) the date that the Government has fulfilled its obligations under Section 7.1 or 7.2(i), as applicable, including changes resulting from the amendment, repeal, withdrawal, termination or expiration of Turkish Law, the enactment, promulgation or issuance of Turkish Law, the interpretation or application of Turkish Law (whether by the courts, the executive or legislative authorities, or administrative or regulatory bodies), the decisions, policies or other similar actions of judicial bodies, tribunals and courts, the State Authorities, jurisdictional alterations, and the failure or refusal of judicial bodies, tribunals and courts, and/or the State Authorities to take action, exercise authority or enforce Turkish Law (a "**Change in Law**"). [...]"

The *Change in Law* concept introduced in the economic stabilization provisions clearly affects the ability of the host-State to regulate in the public interest, as any such regulations having an impact on the expected profits of the project would give rise to an obligation to pay compensation. Further, the stabilization clauses affect not only the legislative powers of the host-states, but also bind their administrative acts, judicial decisions, and other authoritative acts; that is, the State apparatus as a whole is placed at the service of the investors instead of its citizens. Finally, the stabilization clause even constrains the ability of the host-states to implement international treaties and otherwise to perform their international obligations, and thus impairs the progressive implementation and development of, *inter alia*, international human rights and environmental law.

The second provision that supports the articulation of BTC's economic equilibrium formula is the right granted to the investors to claim compensation for losses in cases of changes in laws. As provided in Article 10.1 of the Turkish HGA:

"the Government shall provide monetary compensation as provided in Article 10 for any Loss or Damage which is caused or arises from: . . .(iii) any failure by the State Authorities, whether as a result of action or inaction, to maintain Economic Equilibrium as provided in Section 7.2(xi);"

BTC's economic equilibrium provisions directly impact both on the government's regulatory space and on its abilities to perform its international duties in safeguarding, *inter alia*, the health and

⁸ Turkey-BTC HGA, Paragraphs 7.2 (vi) and (xi).

⁹ Turkey-BTC HGA, Paragraph 10.1

safety of the population, equality under the law and judicial remedies, and the right to a healthy environment. The economic stabilization provisions even affect the applicability of international standards, as follows from the HGA Appendix V on Code of Practice on Environmental, Health, and Safety,

“If any regional or intergovernmental authority having jurisdiction enacts or promulgates environmental standards relating to areas where Pipeline Activities occur, the MEP Participants and the Government will confer respecting the possible impact thereof on the Project, but *in no event* shall the Project be subject to any such standards to the extent they are different from or more stringent than the standards and practices generally prevailing in the international Petroleum pipeline industry for comparable projects.”¹⁰

Furthermore, Appendix D of the Turkish section of the EIA states clearly that Turkish Laws and regulations and applicable international standards (including those regarding environment, public health and security) will be applicable as long as they are not inconsistent with the IGA and HGA (which adopt the petroleum industry standards in comparable projects). Such clauses clearly abrogate the Government’s legislative and executive powers, with serious consequences on its ability to govern.

The *Joint Statement* and the *Human Rights Undertaking* have seemingly attempted to address these flaws after the fact. However, these documents are narrowly drafted and do not resolve the deficiencies apparent in the HGAs.

The *Joint Statement* confirms the IGA’s provision that environmental standards and practices will not fall below European Union (EU) standards, including as they evolve.¹¹ The countries’ commitment to apply standards no less stringent than those applied in the EU is problematic because these industry standards (not EU standards) are vague, confusing, and inapplicable in cases where operators so decide. The issue is further compounded if a country finds that it needs to apply health, safety, and environmental (HSE) standards that are *more* stringent than those generally applicable in the EU, in order to adequately protect its environment or the health and safety of its population. In such case, the domestic standards would conflict with the applicable project standards, and any attempt by the host-State to apply its more stringent standards would make it liable to compensation for loss under the economic stabilization provisions.

The *Human Rights Undertaking* seemingly deals with this problem in paragraph 2(a) by committing BTC not to advance interpretations of Section 2.8 of the IGA that are inconsistent with governmental actions required under human rights and labor treaties. Careful reading of this document reveals that the flaws apparent in the HGAs detailed above remain outstanding. First, paragraph 2(a) only refers to interpretations of Section 2.8 of the IGA and not to the broader BTC legal regime. Further, paragraph 2(a) deals with the host government’s ability to regulate HSE under domestic law, in accordance with relevant standards. That is, a country that enacts HSE standards more stringent than applicable or relevant project standards is not covered by this Undertaking. Further, according to this same paragraph, to qualify for protection, a country’s regulation must satisfy a number of cumulative requirements, including that it is:

- reasonably required by international labor and human rights treaties (not international environmental treaties or customary law)
- required by the public interest
- in accordance with its domestic law
- provided that such domestic law is no more stringent than applicable project standards

¹⁰ HGA, Appendix V, paragraph. 3.3. (emphasis added).

¹¹ Joint Statement by Azerbaijan, Georgia, and Turkey, May 16, 2003, para. 7.

The requirements specified above significantly reduce the scope of BTC's undertaking. More problematic however, is the fact that BTC acquires the power to determine whether governmental actions are *reasonably required* by human rights treaties, whether they are required by the *public interest*, and even whether regulations are consistent with domestic laws. In a democracy bound by the rule of law, determinations of this sort belong to the domestic judiciary – not to ad hoc arbitral panels not subject to appeal and closed to the view and participation of the public -- and, subsidiarily, to international supervisory bodies, such as those created by the European Convention of Human Rights.

The *Human Rights Undertaking* also seems to commit BTC in paragraph 2(d) not to seek compensation for actions required under human rights, labor, and HSE treaties.¹² Again this undertaking is applicable only to governmental actions or inactions *reasonably required* to fulfill international HSE obligations. This narrow protection for environmental regulations is not applicable under the plain terms of para. 2(d) in cases where an international environmental agreement allows, but does not require, Parties to adopt more stringent measures, a feature present in a large number of international environmental treaties that Turkey is a party to, including:

- Article 2:11 of the *Montreal Protocol on Substances that Deplete the Ozone Layer*
- Article 5 of the *Protocol concerning Mediterranean Specially Protected Areas*
- Article 4:1 of the *Ramsar Convention on Wetlands of International Importance Especially as Wildfowl Habitat*
- Article 12 of the *Bern Convention on the Protection of Europe's Wildlife and Living Environment*
- Article XIV:1 of the *Convention on International Trade in Endangered Species of Wild Flora and Fauna*
- Article 4.11 of the *Basel Convention on Transboundary Movements of Hazardous Wastes and Their Disposal*

Thus, in cases where a country enacts HSE standards authorized but not required by these environmental conventions that are more strict than applicable project standards, that country would be subject to claims for loss of profits. On this point, BTC has stated that it is unlikely to file a arbitration claim against a government for its economic loss associated to more stringent standards in the absence of evidence that Government action seeks to change the commercial terms of the Project.¹³ That is, BTC retains the right to seek compensation in case a country decides to regulate for the protection of its environment, but may discretionally waive its right. In other words, the problems associated to the economic stabilization provisions in the HGAs remain outstanding, in spite of BTC's *Human Rights Undertaking*.

The case of Yumurtalik bay, which literally means the “hatching area”, is a clear example of the practical implications of the HGA's flaws. CIEL's team interviewed university professors at Cukurova University who confirmed that no carrying capacity studies of the bay had been undertaken, even in the knowledge of the expected increase in tanker traffic. This important deficiency is amplified by the fact that the EIA for Turkey does not include MARPOL's 1978 Protocol or MARPOL's other Amendments as applicable project standards.¹⁴ It may well be that once these studies are undertaken, the protection of the bay's ecosystem, and particularly the protection of the highly endangered migratory (*Caretta caretta*) turtles that nest next to the bay, will require environmental standards more stringent than those generally applicable in the EU.

Even the consolidated version of the Treaty Establishing the European Community adopted in 2002 recognizes that EU standards may not be sufficient or adequate, and provides that Member

¹² BTC Co., deed done 22 September 2003, Human Rights Undertaking, para. 2(d).

¹³ BTC Citizen's Guide, pg. 25.

¹⁴ That is, BTC's promise of subjecting the Project to the 'highest international standards' is contradicted by actual practice in this case.

States shall not be prevented from maintaining or introducing more stringent protective measures.¹⁵ That is, BTC's *Citizen's Guide* reference to EU standards as a floor¹⁶ should rather refer to them as a ceiling, a barrier to public interest environmental regulation that countries may not overcome without exposing themselves to liability.

Liability Standards

Although BTC claims to apply the "highest international standards",¹⁷ a more careful examination of liability standards reveals that an action for damages would need to overcome undefined (and arguably undefinable) standards of caution. Article 11(2) of the HGA provides that MEP Participants shall be liable to a third party for loss suffered as a result of MEP's breach of the standards of conduct set forth in the Project's Agreements. These relevant standards of conduct are found in HGA's Appendix V, the *Code of Conduct*, which provides in turn that, in conducting all activities involved in the BTC project, MEP Participants shall use "Best Endeavours" to minimize potential disturbances to the environment and property. The term "Best Endeavours" is defined in the HGA Appendix 1, Certain Definitions, as,

"Best Endeavours means the taking by the relevant Person of all lawful, reasonable steps in such Person's power which a prudent and determined man acting in his own interest and anxious to achieve what is required would have taken under the circumstances."

As defined, Best Endeavours embodies a negligence standard for liability. Problems of evidence associated to such a liability standard of *culpa* or negligence are compounded by the inherent indeterminacy of the concept. The concept of strict liability has been crafted to overcome these difficulties and to establish an ample margin of environmental safety. If the HGAs had introduced strict liability as the relevant standard, BTC would be obliged to restore and compensate for environmental damages in any event, except ones caused by *force majeure*. That is, affected persons and communities would be protected without having to enter into long (and costly) discussions on whether BTC operators failed to exercise due caution. In most cases, given that relevant evidence rests with BTC operators, proof of such negligence will be extremely difficult. That is, if BTC were serious in its commitment to high environmental standards, it would have agreed to introduce strict liability standards to the HGAs.

Non-Transparent Private Arbitration

Any dispute arising under the HGA, or in any way connected to the HGA, between the host-State on the one hand and one or more of the MEP Participants on the other hand may be submitted to arbitration at the MEP Participant's choice. Although an international arbitration clause is not unusual in investment agreements of this nature, Article 18 of the HGA's governing dispute resolution and applicable law does not provide for an open and transparent dispute settlement mechanism.

Particular issues compounding the lack of transparency in arbitration under the HGA include the lack of disclosure of the arbitration documents to the public and the secrecy in the conduct of arbitration hearings. That is, despite the public interest nature of the issues under adjudication in the arbitration, the public does not have access to the Parties' arguments and the hearings take place behind closed doors. The lack of transparency is further aggravated by the lack

¹⁵ Official Journal of the European Communities, 24.12.2002, C 325/109, consolidated versions of the Treaty establishing the European Community, incorporating the amendments made by the Treaty of Nice, article 176.

¹⁶ BTC Citizen's Guide, pg. 19.

¹⁷ BTC Co, Citizen's Guide to the BTC Project Agreements: Environmental, Social, and Human Rights Standards, at pg 5.

of participation of affected communities as parties to the arbitration, unlike other MEP participants who do enjoy this right.¹⁸ Finally, the HGA does not provide opportunity for civil society organizations to present their views as *amicus curiae* as a matter of right.

Historical precedents reveal the democracy deficits of the arbitration practices envisaged in the BTC legal regime. Early in the XXth century, a dispute involving Ottoman water-works concessions in Jerusalem became the object of dispute between a Greek investor and the United Kingdom. This investment dispute was heard by the Permanent Court of International Justice in open hearings, only after domestic recourse had been exhausted, and its Judgment was based on international law.¹⁹ In contrast, disputes connected to the BTC Project would be heard in closed arbitration chambers in Geneva²⁰ by a private tribunal applying the substantive law of England.²¹

Arbitration under the Turkish HGA rules would be governed by ICSID rules, (which do not explicitly ensure a transparent arbitration) unless the dispute “related to the property and real rights upon the real estates”.²² In such case, given the Turkish reservation to ICSID jurisdiction, the arbitration would be conducted under the Rules of Arbitration of the International Chamber of Commerce (ICC), which suffer from even more severe transparency deficits.

In sum, despite that the disputes submitted to arbitration may involve issues of relevance to the public at large, including the application of health, safety, and environmental standards, the public does not enjoy the right to attend arbitration hearings, to access documents presented in the arbitration, and to participate as Parties or as *amicus curiae*. These transparency deficits further highlight BTC’s lack of real commitment to high standards of transparency and participation.²³

Lack of Transparency and Public Participation during the Negotiation of the BTC Legal Regime

Although the BTC Project Agreements are now available to the public at the project’s website, there was no public discussion about their impacts prior to, during, or after they were signed. CIEL’s interviews with NGOs, government representatives, legal scholars, media, villagers, and others reveal that there has been neither public discussion nor consultation in regards to the Project Agreements. These agreements, which severely undermine the capacity of the government to conduct its legislative, executive, and judicial powers, should have been open to public discussion before they were finalized. The fact that these agreements were negotiated in secret and were disclosed only after they were ratified highlights the project’s lack of consultation with civil society and substantive flaws.

Public Interest Implications

BTC Co. is currently seeking funding from International Financial Institutions (IFIs) such as IFC, EBRD, and various Export Credit Agencies (ECAs). In light of the mandate and policies of IFIs and ECAs, a *sine qua non* for public funding is the project’s demonstrable contribution to poverty reduction and local development. Accordingly the BTC Project should be designed to deliver

¹⁸ HGA, Article 18(1).

¹⁹ *The Mavrommatis Palestine Concessions*, PCIJ, Series A, No.2, 1924.

²⁰ Arbitration would take place in Geneva, Switzerland, unless otherwise agreed in writing. Further, HGA Article 18(6) requires that any arbitration take place in a country that has ratified or acceded to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

²¹ HGA, Article 18.12.

²² Turkish Reservation under Article 25(4) on the ICSID’s Jurisdiction.

²³ Good practices in transparency in arbitration can be found in the investment chapters of the recently concluded Bilateral Free Trade Agreements between the United States and Chile, and between the United States and Singapore.

measurable benefits to local communities and to operate in the public interest. However, Article II(8) of the IGA reads:

“Each State hereby represents and warrants that (I) the MEP Project shall not involve provisions of services to the public at large in its Territory for purposes of satisfying the general or common needs of the populace, (II) the MEP Project is not intended or required to operate in the service of the public benefit or interest in its Territory, and (III) as such, no applicable Project Agreement shall be characterized or treated, in whole or in part, as a concession contract or a special administrative contract granting a concession.”²⁴

BTC argues that this clause was introduced into the IGA to distinguish BTC from public utilities, such as power plants.²⁵ In light of the *TOPCO* Case and Arbitrator Dupuy’s analysis of special administrative contracts,²⁶ it would rather appear that BTC has a clear interest in avoiding any discussion on whether the HGAs constitute special administrative agreements or concessions because, if such were the case, an arbitral tribunal could find that the government, for the public interest, retains its sovereignty to affect the terms of the concession.

In any case, the IGAs language is clear: “the MEP Project is not intended or required to operate in the service of the public benefit or interest”. To overcome this difficulty, BTC would need to furnish overwhelming evidence on how this project operates in the public interest and contributes to local development and poverty eradication. That is, general dollar figures of country income or ideological positions on the automatic contributions of foreign direct investment to development are not sufficient. In this regard, CIEL’s field research found that BTC representatives, had not discussed development issues with directly affected villagers or with other indirectly affected stakeholders. Interviews revealed that local needs, including primarily hospitals, schools, and employment, were not addressed by the BTC Project.

BTC Project Fails to Consider, Fully, Implications for Climate Change

Global Warming is an international environmental issue of utmost importance, and it is critical that the IFC take global warming fully into consideration in deciding which projects it will fund. The world community has taken steps to control the emission of greenhouse gases (GHGs) to the atmosphere in the UN Framework Convention on Climate Change (UNFCCC) and several other instruments.²⁷ The IFC has stated that it supports the development of projects that will reduce GHGs under the UNFCCC.

Given the profound threat global warming poses to the Earth’s climate, the determination of the world community to address that threat, and the IFC’s own commitment to support such efforts, it is vital that the full impact that projects will have on the climate be fully assessed before a decision is made to proceed with financing. We note that the Environmental Impact Statement (EIS) prepared for the Turkish section of the BTC Pipeline project addresses only the GHG emissions from the terminal and pumping stations. It does not address the implications for the climate of

²⁴ Inter Governmental Agreement Among the Azerbaijan Republic, Georgia, and the Republic of Turkey Relating to the Transportation of Petroleum Via the Territories of the Azerbaijan Republic, Georgia and the Republic of Turkey Through the Baku - Tblisi - Ceyhan Main Export Pipeline” November 18, 1999 Istanbul Turkey. Article II (8).

²⁵ BTC Co, Citizen’s Guide to the BTC Project Agreements: Environmental, Social, and Human Rights Standards, at pgs. 25-6.

²⁶ *Texaco Overseas Petroleum Co. & California Asiatic Oil Co. (TOPCO) v. Libyan Arab Republic*, 53 I.L.R. 389 (1979), Award of Jan. 19, 1977.

²⁷ Although Turkey is not yet a party, the UNFCCC has been ratified by most of the countries of the world.

bringing additional oil onto the market, which is bound to have an effect on prices and result in increased GHG emissions. This climate impact should be assessed before a decision is made to fund this project.²⁸ Lacking such information, as it does, we consider the EIS to be deficient.

We also note that due diligence requires an assessment of the risk that climate change could pose to the financial viability of the BTC project. We are aware that many companies have begun to assess their own operations with an eye to preparing for a future in which GHG emissions and fossil fuel consumption may be tightly constrained by international environmental disciplines, including the UNFCCC. If oil consumption drops due to a world-wide shift away from fossil fuels and toward renewable energy and increased energy efficiency, projects such as the BTC Pipeline may cease to be profitable.

The BTC Project Violates IFC Requirements and Raises Mandate Issues

Facts we collected during our field research corroborate the findings of other NGOs²⁹ that the IFC has violated several IFC policies and procedures, particularly those related to compensation and consultation. Additionally, our research and analyses raise serious concerns about the extent to which the IFC has mechanisms in place to ensure that this project will achieve positive poverty alleviation benefits. More specifically, we found the following:

- BTC project sponsors failed to compensate affected people adequately as required by the OD 4.30 Involuntary Resettlement.
- BTC project sponsors failed to consult adequately with affected people as required by OP/BP 4.01 Environmental Assessment and OD 4.30 Involuntary Resettlement.
- Failure of the World Bank to address key issues raised by the BTC Project may undermine its ability to achieve its mandate.

Compensation

Although the BTC Project does not require any physical involuntary settlement, the construction of the pipeline, the pumping stations, camps, supply and staging areas, and access roads require acquisition of approximately 3,105 hectares of land either permanently or temporarily,³⁰ causing economic dislocation of about 30,000 people.³¹ Private and public landowners, and public and private land users, will be adversely affected in this process. According to the IFC *Handbook for Preparing a Resettlement Action Plan*,³² in addition to physical resettlement, ‘involuntary resettlement’ also involves economic displacement “that interrupts or eliminates people’s access to productive assets without physically relocating the people themselves.” Because development projects that displace people involuntarily usually give rise to severe economic, social and environmental problems, IFC guidelines—and in particular World Bank Operational Directive 4.30 (OD 4.30—

²⁸ In a recent decision of the 8th Circuit U.S. Court of Appeals, the U.S. court held that increased access to coal supplies, facilitated by the permitting of a new rail line, would likely contribute to increased emissions of pollutants, including pollutants related to increased global warming. As such, the failure to address these emission issues in the environmental impact assessment prepared for the project violated the National Environmental Policy Act. See *Mid States Coalition for Progress v. Surface Transportation Board*, Oct. 2, 2003, 8th Circuit Ct. of Appeals.

²⁹ See comments submitted by Bankwatch and others.

³⁰ RAP Turkey, November 2002. 1-6.

³¹ *Ibid.* 1-7

³² IFC *Handbook for Preparing a Resettlement Action Plan*, 2002

require such projects to meet certain conditions in order to receive funding.³³ These requirements involve, *inter alia*, developing a Resettlement Action Plan (RAP) that should ensure, among other things, community participation and planning, land, housing, infrastructure and other compensation for the adversely affected people, as well as plans for environmental protection and management.³⁴ As such, BTC Co., which has stated that it will apply relevant World Bank policies,³⁵ has developed a Resettlement Action Plan (RAP) that it claims is in conformance with the HGAs.³⁶

The RAP states that land acquisition will be undertaken through negotiation with affected landowners, users and occupiers.³⁷ Similarly, Turkish Expropriation Law, which BTC Co. has committed itself to, states that “the administration [BOTAS] shall assign one or more than one reconciliation commission... for the purpose of executing and completing the purchasing works through bargaining over the estimated cost and through barter... the bargaining negotiations shall be held on a date designated by the commission.”³⁸

Specifically, the RAP indicates that the Project will seek to ensure that all affected parties are compensated and assisted in restoring their livelihoods, and it commits BTC Co. to:

- Minimizing Project land use, reclaiming land after construction, and reinstating the land, with minimum restrictions following construction, for use by the original landowners and users;
- Designing the routing to avoid any physical resettlement and to minimize expropriation both permanently and temporarily;
- Determining compensation values based on extensive data collection and market analysis, and providing compensation as required by Turkish legislation before pipeline construction begins;
- Establishing a process of consultation with the affected populations and with local public and civic organizations to maximize understanding of (i) Turkish legislation and (ii) applicable World Bank Group policies on resettlement and (iii) implementation arrangements for resettlement, expropriation and compensation;
- Incorporating where possible, preferences voiced during the consultations with local populations and government agencies, Non-Governmental Organizations (NGOs) and other stakeholders; and
- Establishing a RAP Fund, administered by BTC Co. to ensure fair compensation to those groups denied compensation by the Turkish Expropriation Law.³⁹

³³ World Bank Operational Directive 4.30 on Involuntary Resettlement at www.worldbank.org p.1

³⁴ For a full list, see OD 4.30

³⁵ The World Bank has stated that it will apply World Bank Operational Directive OD 4.30, as well as the IFC guidelines on public consultation, IFC’s *Good Practice Manual*, and the IFC publication *Handbook for Preparing a Resettlement Action Plan*³⁵ during the life of the project.

³⁶ See HGA Article 7.2 (vii) (5) “...pay such compensation to Persons in the Territory as may be required by Turkish Law to authorise the State Authorities to grant to and vest in each of the MEP Participants the rights obtained in accordance with...; (7) “ensure that the Rights to Land including, in particular, the rights obtained in accordance with the foregoing clause (4), and all necessary documents related thereto, are properly and timely registered or recorded in favor of each of and specifically naming the MEP Participants as property rights holders in respect of the Permanent Land and owners of the Facilities in accordance with Turkish Law in order to satisfy any applicable requirements of Turkish Law and to provide public notice of the rights of each of the MEP Participants to the Rights to Land including, in particular, the rights obtained in accordance with the foregoing clause (4)” and also Lump-sum Turnkey Agreement Appendix A, Section 8.42

³⁷ RAP summary overview, November 2002.p. 17

³⁸ Turkish Expropriation Law Article 8 cited in *Campagna per la Riforma della Banca Mondiale et.al.* FFM, May 2003 p. 50.

³⁹ *ibid.*

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Furthermore, the BTC Co. states in its RAP that it will create efficient mechanisms for monitoring compliance within the guidelines of OD 4.30 and Turkish law, and will allocate sufficient monetary resources to cover the costs of mitigation and monitoring. BTC Co. also adds that implementation arrangements will be undertaken in a participatory manner, in consultation with the affected communities and, where appropriate, in accordance with the preferences people have expressed during the course of the socio-economic survey.⁴⁰

CIEL interviewed various stakeholders during its field research in Turkey, in order to assess the compensation process undertaken by the Project sponsor. The issues of compensation were evaluated against the laws, regulations, and guidelines stated in the RAP. Despite significant improvements recorded since August 2002,⁴¹ major shortcomings were detected by CIEL. These included:

- Not all affected communities are being compensated;
- Insufficient information was provided on which economic losses were going to be compensated;
- Prices were not negotiated but imposed; and
- Prices were considered to be under their market prices.

Fishermen in Yumurtalik

Interviews with fishermen in the village of Yumurtalik indicate that they believe they are not being adequately compensated for their losses. In the region near Yumurtalik, two miles of the Mediterranean Sea will be closed to fishing, causing loss of income for local fishermen. Various sections of the bay have already been closed as a result of construction of a thermo-electric plant. The BTC Pipeline will narrow the range of fishable waters even further, potentially harming the income-earning opportunities of the fishermen. Furthermore, construction of the marine terminal will contribute to the pollution in the bay—a body of water that is already polluted from trawlers, tanker traffic industrial waste, and 11 other industrial plants currently surrounding the bay.

The fishermen stated that the size of their catch has declined radically over the last decade and that the BTC will make the situation significantly worse. The Yumurtalik fishermen say that they use the two-mile area that will be closed to fishing – and that it will become even more important to them as pollution increases in other parts of the bay. BTC Co. and BOTAS told field research interviewers that only the fishermen from Golovasi, which is a fishing town near Yumurtalik, will be negatively effected as a result of the two-mile restriction and that they will compensate only the fishermen from this village. However, BTC Co. officials were not clear about how this research was conducted, how it was determined whether the fishermen were going to be negatively impacted by the closing of the area, nor how the economic losses would be calculated.

Villagers of Ulas Region

The villagers of Ulas, Kurtlu Kaya and Yesil Yurt believe they were being compensated for land use and agricultural loss within the 28 meters of the pipeline corridor. According to them, BTC is not compensating those within 28 meters. These villagers were not informed about the compensation of non-land related issues. For example, they were not informed about how the construction dust and noise would affect their bees, and how they would be compensated for their losses. They were also not informed about whether they would be compensated if their animals were killed or injured as a

⁴⁰ *ibid.*

⁴¹ see also Campagna per la Riforma della Banca Mondiale et.al. FFM report, p.47.

result of the pipeline construction or operation. Neither were they informed about the grievance procedures or how to claim their losses.

Furthermore, the villagers of Ulas, Kurtlu Kaya and Yesil Yurt stated that, in violation of the RAP and Turkish Expropriation Law, the compensation was not negotiated, but rather imposed upon them.

Finally, the villagers of Ulas, Kurtlu Kaya and Yesil Yurt, complained that, in violation of the RAP requirement that BTC Co. “pay fair compensation based on market value, full replacement cost or loss of income, as the case may be,” the compensation offered was below the market place value, and it was not clear how the compensation was evaluated or by whom. Most people interviewed thought the amount was unfair. Thus, the majority of the villagers were unsatisfied with the compensation process. The team was also told that, because some villagers were upset with the compensation amount they were paid, they went to the Turkish courts to challenge it. At the time of our interviews, the courts had not decided on a ruling.

BOTAS and BTC Co. Response

During our interview with BOTAS and BTC Co, we raised the issue of compensation and communicated the complaints of the villagers. In response, BTC Co. and BOTAS stated that all those who were affected by the project would be compensated. They added that BTC Co. is compensating ‘even’ those who do not hold legal rights, but have been using the land. Furthermore, BTC argued that they will even resolve title problems among family members by taking the cases to the court and paying for the costs themselves. Finally, according to the BTC Co. RAP, in addition to those who have a legal right to compensation, the users of private land and public land will also have their rights recognized, be provided for and compensated for assets and crops.⁴²

Although many villagers expressed relief that the land is going to be restored after construction is completed, and were satisfied to have already received their compensation (particularly those who would not have received compensation under Turkish law), questions related to under-compensation and failure to negotiate compensation remained.

Communication Concerns Related to Compensation

Finally, the team generally observed that communications between BTC. Co. and the villagers are not adequate; information flow between the villagers and BTC Co and BOTAS is insufficient and information to interested parties is not always communicated clearly and in an easily understood language. Moreover, mechanisms through which affected communities can contact BOTAS and BTC Co. representatives to raise questions and communicate their concerns are virtually non-existent. These communication issues urgently need to be addressed.

Consultation/Transparency/ Public Participation

The process of consultation is one of the main funding requirements of international financial organizations and export credit agencies. For instance, the World Bank Environmental Assessment Policy OP/BP 4.01, and Involuntary Resettlement Policy, OD 4.30, as well as IFC manual “Doing Better Business Through Effective Public Consultation and Disclosure: A Good Practice Manual” require that all potentially affected parties, both at national and local levels, are

⁴² RAP 1-8

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consulted.⁴³ The IFC also requires that consultation be an on-going process to be carried out during the construction and operation phases of a project. Specifically, the IFC manual states that the sponsor should ensure that the information regarding the project is meaningful and easily accessible; that all stakeholders have early access to information about the project, the information provided can be understood easily, the locations for consultation are easily accessible for all those who want to attend, and that minority groups are consulted.

In its Public Consultation and Disclosure Plan (PCDP),⁴⁴ BTC Co. states that the consultation process will conform to Turkish regulation and requirements of IFC, EBRD, European Commission and other relevant international conventions.

Furthermore Appendix 5 of the HGA, Article 3.9 (iii) states that the EIA shall be subject to public review and comment in accordance with the following procedures:

(a) Affected public and non-governmental organizations will be notified about the nature of the operation of the Facilities during the development of the EIA through dissemination of information to these organizations through meetings and exhibitions.

(b) Following the completion of the EIA, the public will be provided with information on the environmental aspects of the Project to enable it to comment with respect thereto. To facilitate this process the EIA and an executive summary (in the Turkish language) will be made available in a public place for review and comments; additionally an information copy of the executive summary shall be submitted simultaneously to the Government.

(c) A maximum of sixty (60) days will be allowed for public comments, which will be provided to the Government by the MEP Participants within thirty (30) days after the expiration of said sixty (60) day period. Demonstration that the MEP Participants have reasonably addressed public concerns (through modification of the EIA, if necessary) will be included in a final executive summary that will be submitted to the Government.

The PCDP, additionally, states that the Project will identify key stakeholders and ensure that there are adequate mechanisms for stakeholder feedback and information sharing; provide an outline for consultation at the local, national and international levels during the planning, construction, operation and decommissioning stages of the pipeline; ensure issues raised by stakeholders are addressed in the EIA report as well as in project decision-making and design processes, and outline a grievance mechanism for local stakeholders.

In order to evaluate the compliance with IFC requirements of the consultation process undertaken by BTC Co., CIEL visited and interviewed various stakeholders. These stakeholders were identified from the list provided by BTC Co. in the EIA. We asked these stakeholders whether they thought the consultation process had been satisfactory. Based on these interviews, we evaluated the consultation process against the aims stated in the PCDP, procedures outlined in the HGA and the guidelines of the international financial institutions—specifically IFC guidelines—and we concluded that although there were some positive developments within the Turkish contexts, overall, the process still had major shortcomings. Some of these include:

- Not all affected communities were consulted;
- Not all stakeholders were informed in a timely manner;

⁴³ See <http://wbln0018.worldbank.org/institu...FBA60518525672C007D0974?OpenDocument> and www.ifc.org

⁴⁴ EIA Turkey, Appendix A1, June 1 at www.caspiandevlopmentandexport.com

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- Affected communities were not informed about the negative impacts and risks of the project;
- Consultation process was not easily accessible to all affected communities; and
- BTC Co. and BOTAS were not accessible by all stakeholders who wanted to raise concerns.

Views of Affected Communities

Villagers we interviewed were more critical of the consultation process than most NGOs. The Muhtar (village leader) of Ulas, for example, stated that the consultation process was insufficient, despite the fact that BTC Co. and BOTAS had distributed booklets to villagers. Indeed, the village leader of Ulas had a booklet on his desk when we visited him. The Muhtar added, however, that they have always been visited by “subcontractors” of BOTAS or BTC Co., and never directly by representatives from BOTAS or BTC Co.. Questions raised by villagers usually were not answered, since all those who came to the region responded to the questions by stating that they were “just subcontractors” or were doing research “like us.” A villager from the village of Kurtlu Kaya stated that there had been problems with information flow regarding the Project, and that some village leaders were not informing people who were going to be affected. This villager recommended that BTC Co. make sure that information reaches those who are going to be affected. Due to this inadequate dissemination of information, many questions remain in the minds of the villagers. Most of these questions related to the potential damages that could negatively impact the health and safety of the villagers and their livelihoods.

The villagers of Ulas were informed that they were not going to be able to use the land (which is 18 meters wide) during the construction phase. They would be able resume their agricultural activities over the land once the construction was complete and the soil restored. The BTC. Co. also informed the villagers that they reserve the right to enter these lands for maintenance and problem shooting whenever they think it is necessary. However, they were not informed sufficiently how their economic losses will be evaluated and compensated.

The fishermen in Yumurtalik also argued that they had not been visited, nor consulted, despite the fact that the BTC Project will directly affect them. The villagers stated that although they heard there were meetings in Ceyhan (a town approximately 30 km away), many of the fishermen were not able to attend these meetings because transportation was rather difficult. Thus, they argued that these meetings were not easily accessible.

During our interviews, it became clear that the issues of local development and access to benefits were not discussed with the villagers. Both villagers stated that BOTAS did not discuss development issues with them. The villagers stated that the region is in urgent need of a primary school and a hospital, and that they would benefit significantly from creation of more permanent job opportunities in the region, if the BTC were to contribute to the development and alleviation of poverty in the region.

The villagers of Ulas claimed that instead of contributing to local development and poverty reduction, the construction of the pipeline was actively causing damage—especially to roads. They complained that a company delivering pipes to the construction site damaged the roads when the Mayor of Ulas asked BOTAS to rebuild the roads BOTAS did not respond. The Mayor, according to the villagers, decided to fund the road with village funds and will not allow BOTAS trucks to use the road unless they pay at least half the cost of reconstruction. The villagers noted that, because the trucks are not allowed to go through the village, they use the grazing lands of animals

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and cause significant damage to the villagers, whose main income comes from animal husbandry. BOTAS has denied using the road and contributing to damage, but the issue remains outstanding.⁴⁵

Another issue that was raised by the villagers of Ulas was unemployment. Villagers of Ulas, Kurtlu Kaya and Yesil Yurt stated that unemployment was the biggest problem in the region. They said that they had applied for employment during the BTC Project (although they are aware that this is a very short-term solution and will benefit only a few people), but that they have not yet heard anything from BOTAS. The villagers of Ulas and its neighboring communities are still not clear how the BTC pipeline and the third Pump Station will contribute to the long-term employment in the region. They also complained that they were told they would receive animals, but that this had not yet taken place.

Furthermore, neither the villagers of Ulas nor the fishermen in Yumurtalik that we interviewed were informed about the potential environmental, health and safety risks of the BTC Project, nor were they informed about the potential effects of dust and noise. Furthermore, the villagers complained that they had not been informed about how the damages to their animals, farms, etc. would be compensated. They were also not informed about where the tested waters will be discharged. The villagers were particularly concerned about what to do or how to act if there were to be an oil spill or other accident that could cause harm to the villagers, to their crops, animals or to the environment. Furthermore, they were not sufficiently informed about what economic losses would be included for compensation. The villagers who have bees, for example, were not informed about whether or not they would be compensated for their losses.

Based on these findings, CIEL concludes that, although significant positive measures have been taken by BTC Co. and BOTAS, the consultation process still has major shortcomings.⁴⁶ The

⁴⁵CIEL communicated these complaints to a journalist from the Turkish newspaper *Zaman*⁴⁵, and the story appeared in the newspaper immediately before our interview with BOTAS and BTC Co. According to the article in *Zaman* Newspaper, the Mayor of Ulas, Mr. Ismail Kocak, stated that he dosed down the roads to the BTC construction site because the company Limak Bayindir caused damage worth 82 billion Turkish Lira (approximately US\$57,000) by carrying high tonnage pipes to the site. The Mayor also stated that he attempted to contact the BTC Co. Directorate twice but to no avail, forcing the municipality to repair the road from its own budget. Due to this situation, the Mayor will not allow the trucks to use the road unless they agree to cover at least half of the cost.⁴⁵

BTC Co. denied the claims. They argued that the construction had not started in Ulas, therefore it was impossible for BOTAS to have caused the damage, but that it could be related to a previous project.⁴⁵ They emphasized that their contractors 'have to' repair the damages they cause. They added that BOTAS will reinstate even the previous impacts done by other companies and that the US\$9 million reserved for community development will cover these costs. During our interview with BTC Co., they promised to learn the details and send us information on this issue. Following their promise, BTC Co. representatives called us immediately, stating that the damage could not have been caused by a BTC subcontractor, as the construction in Ulas had not started yet. In relation to this issue, BTC Co. also wrote CIEL the following:

"Pipes of BTC Project's LOT C section are coming from Iskenderun and Ceyhan Railway and they are being transported to the Kösreli Stockyard which is on Highway E5. None of PLL's (Construction Contractor in Lot C) and BOTAS's heavy loaded vehicles/trucks have passed through or are passing now through Ulas and it is not expected that they will pass through Ulas until the end of this year. The BTC Project's requirement is to reinstate or compensate the damages to infrastructure along the pipeline route. Therefore, Project will ensure all complaints regarding BTC project are recorded and necessary actions are taken against the complaints."⁴⁵

⁴⁶ CIEL also concluded that no consultation has taken place regarding the IGA and HGA, which establishes the legal regime of the project. Because these agreements undermine legislative and implementation powers of the Turkish state, CIEL considers a serious lack. This issue is dealt under the "Legal Aspect of the Project" section of this report.

international financial institutions and export credit agencies should ensure that these shortcomings are eliminated before the Project receives any public funding.

IFC Mandate Issues

The BTC Project raises several issues related to how the World Bank works to ensure that projects it funds will achieve, or at least advance, its mandate to alleviate poverty and promote social and economic development. Specifically, it raises concerns about the extent to which the World Bank has developed and implemented a rigorous “development screen” or criteria by which it evaluates a proposed project to ensure that financial and other benefits will accrue to local populations to alleviate poverty. In the context of the BTC Project, for example, the failure of the World Bank to address, adequately, issues related to regional economic relationships and regional stability, national corruption and governance, and impacts of the HGAs, could threaten the financial benefits and/or the abilities of affected people to benefit from the project.

For example, we believe the IFC’s failure to adequately address issues described earlier—including, for example, those related to HGA provisions that impose project override costs on Turkish citizens, those related to the uncertain legal status of the Caspian Sea, and those related to regional stability—may threaten financial benefits for people in Turkey in particular.

Even assuming that financial benefits materialize, the IFC’s failure to address national governance issues, and, in particular, the potential for corruption, raises doubts that affected people will enjoy these benefits. As noted in a recent report developed by the Turkish Parliament’s special Anti-Corruption Commission, banking sector corruption is responsible for \$54 million in national economic losses and energy sector corruption for \$40 billion.⁴⁷ As noted by the President of Turkey, poverty and corruption are Turkey’s most pressing problems and corruption must be addressed to achieve sustainable growth.⁴⁸ Clearly, the failure of IFC to address these issues fully will impact the extent to which poverty alleviation is achieved.

Finally, IFC’s failure to consider and address possible constraints the HGAs may impose on the countries’ abilities to manage and protect their natural resources during the life of the project also raises concerns about benefits that will accrue to the impoverished. Natural resources are of critical importance to poverty alleviation efforts. If the abilities of Turkey, Georgia, and Azerbaijan to respond to existing international environmental obligations—or to respond to environmental concerns that are not evident currently but could be in the next 40 years—are constrained by the HGAs, the IFC will have failed to achieve its mandate.

⁴⁷ See Turkish Press Review July 1, 2003

<http://www.byegm.gov.tr/YAYINLARIMIZ/CHR/ING2003/07/03x07x01.HTM#%204>

⁴⁸ See Turkish Press Review, May 5, 2003

APPENDIX I: THE ECONOMIC AND POLITICAL CONTEXT OF THE BTC PIPELINE PROJECT

This section will provide a description of factors, including economics, actors, and politics influencing implementation of the BTC project in the region and, in particular, Turkey. Our research and analyses focused on issues of concern to Turkey since most of the pipeline will be located in Turkey and since it will terminate at a Turkish port on the Mediterranean.

- **Economic Context**

Potential Reserves of Gas and Oil Provided by Caspian Region

The Caspian Sea, which is surrounded by Russia, Iran, and the Republics of Kazakhstan, Turkmenistan, and Azerbaijan, is recognized as an important resource to world energy markets. Over 700 miles long, its waters cover vast reserves of undeveloped gas and oil, including six separate identified hydrocarbon basins. The majority of these basins are undeveloped, and much of the Sea and surrounding areas remain unexplored. The Caspian region contains 10 billion barrels of *proven* oil reserves (defined as oil deposits whose existence is considered 90% probable).⁴⁹ Moreover, there are strong indicators that the region's *possible* oil reserves (defined as 50% probable), mostly in Azerbaijan, could yield another 233 billion barrels of oil.⁵⁰ In addition to oil, the *proven* natural gas reserves in the Caspian region are estimated at approximately 170 Tcf. ⁵¹ *Possible* natural gas reserves in the Caspian region are even larger, estimated to yield another 293 trillion cubic feet (Tcf) of natural gas.⁵²

Significance of Oil and Gas for Region

The world demand for crude oil is expected to rise 30% by the year 2010.⁵³ As the world energy demand escalates, these rich oil and gas reservoirs of the Caspian region will continue to attract a growing number of investors. Under prevailing (unsustainable) patterns of energy production and consumption, the development of the Caspian reserves is increasingly viewed as an important step toward satisfying the future energy needs of the world.

Transportation of Caspian oil to world markets is a central issue for many countries in the Caspian region. The Republics of Azerbaijan, Turkmenistan, and Kazakhstan have been developing their natural gas and oil reserves since their independence in 1991. During the last decade, Azerbaijan and Kazakhstan in particular have received large amounts of foreign investment in their natural gas and oil sectors. Azerbaijan holds 18.5% of the region's total oil reserves, and is in the process of developing these reserves. Azerbaijan is constructing a pipeline to Georgia on the Black Sea (Baku-Supsa Pipeline) and, in response to pressure from Russia, restoring a portion of the Baku-Novorossisk Pipeline—on the condition that it will bypass Chechnya. Azerbaijan's most significant and well-publicized attempt to develop these reserves, however, is the Baku-Tblisi-Ceyhan (BTC) pipeline.

Economic Significance of Project for Turkey

⁴⁹ Energy Information Administration "Caspian Sea Region" at <http://www.eia.doe.gov/emeu/cabs/caspian.html> <http://www.eia.doe.gov/emeu/cabs/caspian.html>

⁵⁰ Ibid.

⁵¹ Ibid.

⁵² Ibid. The same source notes that Turkmenistan (101 Tcf) and Kazakhstan (65 Tcf) are among the top 20 countries in the world in terms of proven natural gas reserves.

⁵³ <http://members.tripod.com/~KELSAGHIR/Home/index>

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The Republic of Turkey supports the view forwarded by BP that the Project will enable crude oil to be transported from the Caspian Sea to world markets more economically and with less environmental hazard than if it were to be transported by a combination of pipelines and tankers via the Turkish Straits.

According to the Turkish Foreign Affairs (MFA) and the BTC Co., the Project will provide the following economic benefits to Turkey:

- The Turkish section of the BTC – 1070 km long - will be constructed by the nationalized Turkish company, BOTAS, under a US\$1.4 billion Lump-sum Turnkey Agreement. This agreement effectively constitutes a direct investment to Turkey of US\$1.4 billion in foreign capital.⁵⁴
- Following the implementation of the operational phase, Turkey will gain yearly revenues amounting to US\$200 million—an amount that will increase to US\$290 million dollars in 2022 from transportation fees.⁵⁵
- The construction phase will create about 5,000 short-term and long-term employment opportunities in Turkey. BTC Co. argues that the Project will create 350 additional long-term employment positions during the first 40 years of its operation (this number includes all three of the host countries).⁵⁶

The MFA also stresses that, in addition to these economic benefits, the Community Investment Program (CIP), which has a budget of US\$9 million for Turkey, will promote sustainable social and economic development for the settlements along the BTC pipeline that will be affected by the project. Furthermore, the same sources argue that the project will provide opportunities for capacity-building and transfer of technological expertise to Turkish companies taking part in the construction of the pipeline.

Despite these projected benefits, a closer look into the Project suggests that these economic benefits ultimately may not be as significant or positive as they are projected to be. BP Co. estimates that the Project will cost \$US 2.95 billion. The International Finance Corporation, however, estimates that the Project will cost around \$US 3.6 billion.⁵⁷ The Turkish section of the pipeline could vastly exceed projected costs of construction. BOTAS currently expects to cover costs for under \$US1.4 billion, but it has been suggested that the “the contract is under-priced by some \$US600 million.”⁵⁸ According to a Government Guarantee letter signed by the Under Secretariat of Treasury of the Republic of Turkey with the Main Export Pipeline (MEP) participants, the government of Turkey will cover any costs that exceed the amount stated in the Lump-sum Turnkey Agreement.

The experience of other BP-led projects in the region suggests a high probability of the BTC Pipeline exceeding its estimated costs of construction; three out of four have gone or are going over-budget. In this case, the Turkish government would have to cover the additional costs itself. Such an event could place an enormous financial burden on the Turkish Government—a government that is still struggling to re-stabilize its economy after the financial crisis of March 2000.

Significance of the BTC Project for Turkey's Energy Needs

⁵⁴ www.mfa.gov.tr/grupa/an/BTC2.htm

⁵⁵ Ibid.

⁵⁶ Resettlement Action Plan (RAP) Turkey, Summary Overview.

⁵⁷ Mansley, Mark, *The Baku-Tblisi-Ceyhan Pipeline and BP: A Financial Analysis. Building Tomorrow's Crisis?* (Platform, London: May 2003). p. 10.

⁵⁸ Ibid.

Supporters of the BTC Project continue to point out the project's potential importance in satisfying Turkey's future energy needs. The Turkish economy has been expanding, and the country's energy demand continues to increase. In 2002, the Turkish Energy Minister at the time, Zeki Cakan, stated that Turkey is likely to experience a major energy shortage by 2006.⁵⁹ According to one energy expert, Turkey produces 3 million tons (mt) of oil per year, which satisfies only 13% of its oil consumption needs, and which would require Turkey to import 49mt by 2010.⁶⁰ According to the Turkish Energy Ministry, Turkey is planning to procure 20mt of this amount from Russia and the Caspian region. Turkey could consume at least 15mt of this amount from Azerbaijani and possibly Kazakh oil transported via the BTC Pipeline Project connecting Baku with the Yumurtalik port of Ceyhan.⁶¹

Turkey is currently competing with Russia and Iran to ensure that Caspian oil is transported across its territory. Without this source of oil, Turkey will be politically and economically dependent on Russia to satisfy its energy needs. Constructing a significant portion of the Pipeline in Turkish territory would ensure Turkey's position as a powerful actor in regional politics and development. Within this political context, the BTC is seen as a project closely linked to the broader "interests of the Turkish State."

Despite strong backing from the Turkish government, some economists question the Project's economic soundness. According to one such analysis, BTC looks marginal on financial return.⁶² The revenue generated by the pipeline will depend on the tariff charges per barrel, which are estimated to be between \$US2.58 and \$US3.30.⁶³ This analysis argues that without a substantial amount of oil from Kazakh reserves⁶⁴, the estimated financial returns of the Project will be as low as 5.42%.⁶⁵ If this becomes the case, it will be necessary to increase the per barrel shipment cost to approximately \$3.2/barrel, and, even then, the return would increase only up to 8.76%.

An additional challenge to successful implementation is a lack of agreement with Kazakhstan. Currently, there is no agreement on whether the Kazakh oil will be transported through the BTC Pipeline. Representatives of BP declared that "Kazakh crude oil will not be necessary because there would be enough Azeri oil to fill a[sic] Baku-Ceyhan Pipeline."⁶⁶ One analyst argues that BP's optimism is linked to its Shah Deniz Gas project, which is planned to run parallel to the BTC pipeline from Baku to Erzurum in Turkey, a strategy designed to reduce costs.⁶⁷ However, it is difficult to determine how much Turkey's need for gas is actually going to increase; Turkey may have already committed itself to more gas than it needs, with the controversial Blue Stream Project.⁶⁸

⁵⁹ Ibid. p.80

⁶⁰ Ibid. p.79

⁶¹ Ibid.

⁶² Mansley, Mark, The Baku-Tblisi-Ceyhan Pipeline and BP: A Financial Analysis. Building Tomorrow's Crisis? (Platform, London: May 2003). pp. 4 and 12.

⁶³ Ibid.. 11

⁶⁴ With the Kazakh oil this amount goes up to 10.94%, which is still lower than the return that BP typically expects. Ibid. p.12

⁶⁵ Ibid.

⁶⁶ Micheal Lelyveld, "Caspian: Russian Opposition to Baku-Ceyhan Pipeline" Radio Free Europe/Radio Liberty Report, Boston, March 6, 2001 cited in Winrow, Gareth. "Pivotal State or Energy Supplicant? Domestic Structure, External Actors, and Turkish Policy in the Causasus" in Middle East Journal Vol. 57, No. 1 Winter 2003 (pp.76-92); 88

⁶⁷ Winrow. p.88

⁶⁸ The Blue Stream Project: Turkey signed an Agreement with Gasprom, a Russian gas company, in which it commits itself to "buy or pay." According to this agreement Turkey has to pay a certain amount even if it does not receive the gas. This agreement caused significant uproar in Turkey. Recently negotiations were held between the parties to resolve this issue. However, the negotiations have failed and Turkey has decided to take the case to Arbitration during the last days of June 2003.

Significance of Project for Turkey's Strategic Importance

Despite the uncertainties involved, many in the NGO community in Turkey as well as state officials recognize that BTC is part of a bigger project that will carry Caspian oil from other countries like Kazakhstan to world markets in the future. These NGOs and the MFA point out that, when that occurs, the amount of oil transported will increase from 50 million barrels to 150 million barrels. Transportation of this massive amount of oil through the BTC Pipeline rather than across the Turkish Straits will prevent increases in tanker traffic in the already over crowded Straits. Lower levels of tanker traffic would contribute to the security of Bosphorus and Istanbul and to the protection of the environment—both main concerns of the MFA and NGOs located in Istanbul. Moreover, transportation of Kazakh oil via Turkey will establish Turkey as an important energy bridge in the region. Therefore, to many, BTC is seen as a step, rather than an end in itself, and as progress toward enhancing the strategic importance of Turkey in the region. For these individuals, the significance of this project for Turkey lies more in the political and strategic advantages it promises the country and less in its potential economic benefits.⁶⁹

Actors and Stakeholders

The Array of Actors

Such an important and political project naturally involves diverse actors and complex relations between and among these actors. Within Turkey, these actors include the Turkish Army, the Prime Minister and his office, the President and his office, Turkish Ministry of Foreign Affairs, the Parliament, the Ministry of Energy, the Treasury, Ministry of Finance, Ministry of Environment, State Planning Organization, BOTAS, Turkish Petroleum Corporation (TPAO), business associations, NGOs, and the Russian lobby—which mainly consists of Turkish construction companies that have invested in the Russian market significantly. All of these actors have different interests and their own agendas regarding the Project, and each stakeholder attempts to influence the political and economical agenda of Turkey toward facilitating their own objectives.

The Turkish Army and MFA

The Army and the MFA, both of which are suspicious of Russian and Iranian ambitions, are strong supporters of the BTC Project. The MFA, the Ministry of Environment, and various NGOs (especially those located in Istanbul) have a particularly strong interest in avoiding tanker traffic in the overcrowded Bosphorus. A major accident would cause an environmental disaster, affecting the Black Sea and the Marmara Sea, and potentially costing the lives of many people in Istanbul.

Russia and Iran

The Russian Government, a major actor in this Project, actively opposes the BTC pipeline, favoring instead that Caspian oil be transported directly to Russian ports. Carrying Caspian oil to world markets from Russian terminals would be less costly and more economically viable, as the distances are much shorter, and as there are already pipelines constructed (such as the Baku-Novorossiyyak Pipeline). This situation would give Russia a monopoly over the Caspian gas and oil resources, and have significant economic and political ramifications for other nations of the Caspian region. Groups such as the Russian military and foreign ministry actively promote the integration of

⁶⁹ This view is supported by Turkish NGOs, and government officials in particular. During the field-trip conducted by CIEL various Turkish citizens, NGOs, scholars, and government officials referred to BTC as a critical political issue rather than an economical one.

the South Caucasus and Central Asia into a single common space—a move which would place Russia in a position to dominate regional politics and potentially use its monopoly over the Pipeline as a policy tool to thwart Caspian energy development.⁷⁰ With these interests in mind, Russia has been a strong opponent of the BTC Pipeline, encouraging the use of existing Russian pipelines and routes. The Russian lobby in Turkey, which consists mainly of Turkish construction companies that have invested heavily in the Russian market, has strong interests in keeping its relations with Russia on positive grounds, and supports the Russian position.⁷¹ Iran, like Russia, would like to see the Caspian oil transported to world markets via routes that go through Iranian territory. Such a situation would contribute to Iran's strategic importance and leverage in the region.

The United States

In addition to Russia and Iran, the major and most influential external actor is the United States. The US Government recognizes Turkey's regional importance and strongly supports the BTC Project. The United States has considerable interest in the Caspian region, as it could potentially contribute towards greater security in oil supply. Toward this end, the United States supports the principle of multiple pipeline export routes, with the aim of avoiding a Russian monopoly over oil supply. However the United States opposes the idea of any export routes that go through Iran, a position based on the *Iran-Libya Sanctions Act* (ILSA).⁷² Turkey, which has traditionally been a loyal ally of the United States, is one of the most stable and dependable states in the region. Therefore, in support of the Project, the US granted BOTAS US\$823,000 for technical assistance through its Trade and Development Agency (TDA) and allowed BOTAS to access U.S. technical, financial, environmental, and legal expertise for negotiations of the BTC Main Export Pipeline and Trans-Caspian Gas in October 1998.⁷³

In addition to TDA, OPIC and EX-IM Banks of the United States play a crucial role in making financing available, in mitigating risks to investors, and in placing the weight of the U.S. government behind the realization of the BTC Project.⁷⁴ Towards that end, TDA, OPIC and EX-IM Bank have also opened the Caspian Finance Center in Turkey's capital, Ankara.⁷⁵

- **Political**

The turbulent political climate of the region makes it difficult and extremely risky to invest in Caspian oil and gas resources. Unstable political situations within each of the countries, as well as corruption within the energy sector in Turkey, further complicate the energy policy-making process. Moreover, within the context of the BTC Project, these instabilities threaten efforts to provide long-

⁷⁰ Sheila N. Heslin "Key Constraints to Caspian Pipeline Development: Status, Significance and Outlook" Caspian Library at www.treemedia.com/cfrlibrary/library/pipelines/heslin.html p.3

⁷¹ For more information about different actors involved in the BTC Project, and their interests, see *Ibid.*

⁷² Notwithstanding comprehensive unilateral sanctions against Iran and Libya, the US Congress enacted the ILSA in August 1996 aiming to respond to these countries' support of international terrorism, acquisition of weapons of mass destruction, and efforts to undermine the peace process in the Middle East. The ILSA Act does not only prohibit US companies investing in the Iranian oil sector, but it also forces foreign companies into choosing to do business with Iran and Libya or the US. ILSA Act was extended an additional five years by President G. W. Bush on August 3, 2001. For more information see www.eia.gov/emeu/cabs/caspian.html

⁷³ "Testimony by Ambassador Richard L. Morningstar, Special Advisor to the President and Secretary of State for Caspian Basin Energy Diplomacy, Before the Senate Subcommittee on International Economic Policy, Exports and Trade Promotion" Caspian Sea Library March 3, 1999 at www.treemedia.com/cfrlibrary/library/policy/morningstar.html p.3

⁷⁴ *Ibid.* p.4

⁷⁵ *Ibid.*

term benefits to the general population, as well as efforts and to make meaningful progress in poverty alleviation.

Ethnic conflicts, violence and war threaten pipeline security

The region is plagued with ethnic conflicts, violence, and war, all of which constitute major obstacles to investments such as pipeline construction. The conflict and violence, for example, threaten the security of the pipeline, which could result in significant environmental and economic damage.⁷⁶ Additionally, these conflict zones often become breeding grounds for arms and drug trafficking, which can create mafia-like organizations and interest groups. Finally, these conflicts prevent regional cooperation that would enable economic development.

Since their independence, the regional countries have struggled to overcome ethnic disputes, economic dislocation, and porous borders. The majority of these conflicts are located in the Trans-Caucasus part of the Caspian region, where conflicts in Nagorno-Karabakh, Georgia, and the Chechen republic of southern Russia have hindered the development of export routes westward from the Caspian Sea. Other conflicts of the region include the conflict between Pakistan and India over Kashmir, the unstable situation in Afghanistan, following over 23 years of war, and the continued threat of Islamic fundamentalism in Central Asia, especially in Uzbekistan.

Both the Baku-Supsa and BTC Pipelines pass just north of the breakaway Azeri region of Nagorno-Karabakh. A recent six-year conflict in that region killed more than 30,000 people, and drove 1 million people—mostly Azeris—from their homes, ending in a Russian-mediated cease-fire in 1994. Despite the cease-fire, sporadic violence and mines continue to plague the 1,600-square mile mountainous region, a situation that poses a significant threat to the security of the pipeline.

In Georgia, both the Baku-Supsa and the BTC, along with several other proposed Pipelines, pass near several regions that have been sites of separatist struggles—namely Abkhazia (northwest Georgia), and Ossetia (north central Georgia). Abkhazia fought a civil war with Georgia in 1992-1993. Furthermore, a coup attempt in 1998 led Georgia to call for the North Atlantic Treaty Organization (NATO) or the United States to station a military contingent in Georgia to protect Caspian oil transport. The port of Supsa is just 12 miles from a buffer zone between Abkhazia and Georgia. Another regional conflict that involves serious risks to pipeline construction is the Kurdish conflict in Turkey. Despite a cease-fire between the Turkish forces and the Kurdish rebel groups, conflict could easily be re-ignited following the April 2003 war in Iraq, as many Kurdish rebels crossed into Turkish territories at this time. The BTC Pipeline avoids the predominantly Kurdish regions in the South.

US Activities In Iraq Could Influence US Need For Oil

The “war against terrorism” in Afghanistan and the invasion of Iraq also are major destabilizing forces in the region. As Iraqi oil (which is the world’s second largest oil reserve following Saudi Arabia) falls under U.S. control, the United States may reevaluate its need for Caspian oil, and pull out its support of the BTC Pipeline. The loss of U.S. support would create a major obstacle for the BTC Pipeline project.

⁷⁶ Even once a pipeline is successfully constructed, it is still vulnerable to attacks by terrorists. Attacks on the pipelines can cause significant financial and environmental damage. This became evident particularly in the aftermath of the war on Iraq. The Kerkuk-Ceyhan Pipeline—which carries Iraqi crude oil to world markets from the Marine Terminal in Ceyhan, Turkey—has been a target of attacks in which multiple explosions were set off in different sections of the pipeline, causing substantive damage. Such challenges to regional security render development of pipelines both expensive and risky.

Uncertain Legal Status Of The Caspian Sea And Other Resources Could Undermine Investments And Contribute To Violence

Another major dispute in the region involves the legal status of the Caspian Sea. Prior to 1991, the legal status of the Sea was governed by bilateral treaties between the Soviet Union and Iran—the two countries bordering the Sea at that time—signed in 1921 and 1940. With the emergence of the states of Kazakhstan, Turkmenistan, and Azerbaijan in 1991, the ownership and development rights of the Sea have been called into question. The legal issue becomes particularly important because most of Azerbaijan's oil resources—and a significant amount of Kazakhstan's and Turkmenistan's resources—are offshore. Development of the Sea's oil and natural gas resources, as well as the construction of potential export pipelines is hindered because of the unresolved legal status of the Caspian Sea.

As the Caspian oil reserves are becoming more significant for the world energy market, and as the associated environmental risks are rising due to extraction of these resources, the stakes for each country bordering the Caspian are also increasing. This situation is contributing to the intensification of conflicts among some of the littoral states. For example, in July 2001, Iranian military gunboats confronted a British Petroleum (BP) Azeri research vessel exploring the Araz-Alov-Sharg structure and ordered the ship out of the waters, which Iran claims as its own. Azerbaijan, on the other hand, has opposed Iran's decision to award Royal Dutch/Shell and Lasmo a license to conduct seismic surveys in a region that Azerbaijan considers to fall in its territory.⁷⁷ Other conflicts include, but are not limited to, the dispute between Turkmenistan and Azerbaijan over the Serdar/Kyapaz field, and the dispute over the Azeri and Chirag field, which Turkmen officials claim fall within territorial waters of Turkmenistan.

Negotiations between the littoral states have made slow progress in ironing out their differences. Although Russia, Azerbaijan, and Kazakhstan have agreed on dividing the Sea by a "modified median" principle, Iran still insists on an equal division of the Sea. For its part, Turkmenistan agrees on the principle of dividing the Sea, but not the method. A summit of the Caspian littoral heads of state was held in April 2002. This summit failed, however, to produce a multilateral agreement on the sea's legal status, prompting several states to sign bilateral agreements in an effort to solve the problem.⁷⁸ Such legal uncertainty could continue to cause further disputes once the proposed pipelines are constructed.

Instability Within Countries Threatens Projects Stability

The entire Caspian region, particularly Azerbaijan and Georgia, is highly unstable both politically and economically. Both Azerbaijan and Georgia are expected to hold elections in late 2003. It is very likely that the aging Presidents of these two countries, who are closely associated with the BTC Project and whose reputations have eroded due to corruption allegations, will be replaced by more nationalistic leaderships. If that is the case, the new nationalistic governments might challenge the legal and economic arrangements of the Project, which favors a small elite and the Consortium. These developments will most probably cause delays and add to the cost of the Project. Furthermore, these new nationalistic governments could intensify the existing conflicts in the region while seeking to enhance national interests of their countries. A situation with such actual and potential political instability certainly does not create an attractive environment for potential investors.

⁷⁷ Ibid.

⁷⁸ Ibid.

Instability and Corruption within Turkey Threatens Project Stability and Goals

The unstable political climate and the frequent turnover of the government in Turkey complicate the energy policy-making process even further. Each government that has come to power has had its own interests and priorities. Every time that the government has transitioned, the heads of various governmental institutions and companies, such as BOTAS and TPAO, have also changed. In addition, corruption allegations, especially in the energy sector, have shaken the country multiple times. In April 2001, the Minister of Energy, Cumhur Ersumer, was forced to resign, and the heads of BOTAS and TPAO were removed. The current government established a Parliamentary Commission to investigate corruption allegations, focusing on corruption allegations in the energy sector. On June 23, the Minister of Energy, Hilmi Guler, announced that various energy policies and agreements had caused or would soon cause significant legal and financial costs for Turkey. He stated that many of these agreements were detrimental to Turkey's interests and that Turkey's financial loss could exceed US\$41 billion.⁷⁹

According to media reports, the BTC Project was one of the cases under investigation by the Commission. The Turkish Parliamentarian Ugur Aksoz said in a recent interview that he supported the investigation, and stated that there was convincing evidence suggesting that those who signed BTC agreements had received bribes.⁸⁰ However, BTC General Director Gokhan Baldaci issued a public denial on January 2003 that any investigation was underway.⁸¹ The report of the Commission documented serious instances of corruption in energy-related projects, focusing on the Blue-Stream Project. Investigations about other corruption instances, continue, however, and the Turkish Minister of Energy, Mr. Guler, has expressed concern about concession agreements that impose the costs and risks on the government.⁸²

⁷⁹ Radikal Newspaper, June 23, 2003 at www.radikal.com. Recently, Turkey had initiated negotiations with the Russian gas company Gazprom the controversial Blue Stream Project. However, as the negotiations failed Turkey decided to take the case to arbitration.

⁸⁰ Interview with Ugur Aksoz Republican People's Party (CHP), Adana Parliamentarian. For more information see "Legal Impact of the Project" Section of this report.

⁸¹ See Mansley, *op.cit.* p.17

⁸² See Radikal newspaper, available at <http://www.radikal.com.tr/haber.php?haberno=78375&tarih=15/06/2003>

APPENDIX II: METHODOLOGY AND FIELD RESEARCH

From May 1st to June 2nd 2003, CIEL conducted a field research investigation in Turkey. The objective of the field research was to gather first-hand data on issues relating to the environmental situation, compensation and consultation processes, and the legal framework of the project. The research specifically focused on:

- whether the affected communities were sufficiently informed about the environmental and social impacts of the Project;
- whether the consultation process has been undertaken as stipulated in the Environmental Impact Assessment and Resettlement Action Plan (RAP);
- whether the compensation process has been in line with the standards set forth in the RAP;
- investigating the level of public discussions and transparency before the HGA was signed, and the awareness of the public as to the consequences of this agreement; and
- gathering the opinions of legal scholars and politicians as to the implications of the HGA;

Meetings And Methodology

To conduct the field research, the CIEL team traveled to the southern part of the pipeline route, focusing on two of the most important ecological areas, namely the Ulas region in the province of Sivas, and the Bay of Yumurtalik, Ceyhan in the province of Adana. The Ulas region is home to five lakes, which are considered by the Ministry of Environment as an Internationally Important Wetland under the Ramsar Convention. These lakes are located 1.2 km northwest and 930m southeast of the 100m Corridor.⁸³ The region is also home to at least eight globally threatened plant species, and supports at least two globally threatened bird species. Additionally, fourteen nationally threatened bird species have been recorded in the region, as well as several species protected under the Bern Convention.⁸⁴

The Yumurtalik Bay area also bears great ecological significance. The word “Yumurtalik” means “the hatching place” and refers to the significance of the area as a hatching place for various fish, birds and *Caretta caretta* turtles. There is a Nature Reserve in the areas for the turtles, endemic and migratory birds, as well as for the Syrian Pine tree. During the period of research, the team also recorded storks, a migratory bird species, breeding in the area.⁸⁵

As part of the field research, CIEL visited and interviewed various groups and individuals in Turkey. Specifically, these groups included:

- **Village Communities:** Fishermen in the Village of Yumurtalik, Adana and the villagers of Ulas, Sivas. The team also talked to villagers from the neighboring villages of Yesil Yurt and Kurtlu Kaya, Sivas while in Ulas.
- **NGOs:** In Istanbul the team met with Cevko, Turmepa, Natures Warriors, Society of Peace with Nature, WWF Turkey and, in Ankara, the team met with the Environment Foundation

⁸³ BTC Project EIA Turkey “BTC Pipeline Construction Impacts and Mitigation- Volume II Supplement I” June 2002, 6-541.

⁸⁴ See also *ibid*.

⁸⁵ More information on the ecological significance of both Ulas and Yumurtalik can be found under the “Ecological Impacts of the BTC Project” section of this report.

of Turkey, which focuses on environmental law. These NGOs were selected from the list of NGOs that BTC Co. has provided in the EIA.

- **Universities:** The director and faculty members of the Environmental Engineering Department at Cukurova University in Adana, Scholars of International Law from Bilgi University, and a faculty member of the Department of Sociology from Middle East Technical University, Ankara (Social Impact Assessment has been prepared by this department).
- **Government officials:** Adana Representative of the Turkish Parliament (from the opposition party) and an ex-deputy from DYP (DYP was the political party introduced the BTC project to Turkey), Deputy Director of the General Ministry of Foreign Affairs, Energy, Environment and Transboundary Waters, Manager of Project Coordination Division-Ministry of Energy and Natural Resources-Department of Transit Petroleum Pipelines. The team was also scheduled to meet with the head of parliamentary commission on corruption. However, due to the busy meeting schedule of the commission and team's limited time, this meeting was unable to take place.
- **Newspapers:** Zaman, Milliyet, and Financial Forum.
- BP, BTC Co. and BOTAS Representatives in Ankara and BOTAS representative in Yumurtalik, Adana. Although CIEL was able to meet with a BOTAS representative in Adana, the representative told the team that BOTAS was not authorized to comment on the Project unless BTC Co. representatives were present. Therefore the minutes of this meeting are off the record. For the same reason, the meeting with BOTAS in Ankara was held jointly with the BTC Co. representatives at the BTC Co. office.⁸⁶
- Various citizens of Turkey.
- **Conferences Attended:** During the the period of field research, two conferences in which the BTC Project was discussed were held in Istanbul. BOTAS and government representatives, including the Minister of Energy of Turkey were guest speakers at these conferences. These conferences included: Black Sea: Energy and the Environment, Istanbul Bilgi University, Marine Law and Policy Research Center, May 15, 2003 and Caspian and Black Sea Oil and Gas Conference, 27- 28 May 2003, Istanbul.

Prior to the field research, different sets of questions were prepared for the different groups that were interviewed. The interview process was based on semi-structured, open-ended questions about the consultation and compensation processes, people's views on and experiences of the project, as well as the level of public debate about the project and its legal framework. The semi-structured, open-ended approach was preferred in order to enable interviewees to comment on the Project, raise concerns, and express their feelings. Answers to CIEL's questions, comments submitted and concerns raised were written down during the interviews. Unless consented by the interviewees, the names of those interviewed are not disclosed in this report.

Initially, there was a general suspicion, especially among the NGOs as to why CIEL was doing this research, and asking questions about BTC. Most of the NGOs, as well as scholars and

⁸⁶ We would like to acknowledge that when we asked for an interview BTC Co. responded with great interest and enthusiasm and organized a meeting where they also invited BOTAS representatives and Manager of Project Coordination Division-Ministry of Energy and Natural Resources-Department of Transit Petroleum Pipelines. They also followed up our interview by sending us various documents that we asked for.

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politicians, stated that Turkey has many other, more pressing environmental and energy problems, including agreements signed between Turkey and various companies. Some of the problems that were mentioned included tanker traffic that threatens the Turkish Straits and Istanbul in particular, the Blue Stream and White Energy projects that involve issues of environmental damage, corruption and investment agreements that protect the natural gas companies against Turkey. The majority of the NGO's, the scholars and also the politicians stated that, in comparison to the Turkish experience with other energy projects (such as the Thermo-electric Plant built in Yumurtalik, the Blue Stream and the White Energy Projects, among others), BTC have been more transparent, and willing to work with NGO's and locals. However, all those who were asked for an interview were eager to meet with us and express their views. Therefore, CIEL would like to state its genuine appreciation for our many interviewees' time and willingness to contribute to this report.
