



AUDIT MONITORING REPORT
CLOSURE OF AUDIT

CAO Audit of IFC
CAO Compliance

C-I-R7-Y06-F079
April 20, 2009

**Karachaganak Project
Kazakhstan**

**Case of
Residents of the Village of Berezovka**

Summary

As of April 2009, CAO can confirm that the Project is now in compliance with IFC requirements identified in the 2008 CAO audit report. These requirements are the 1998 IFC policy provisions relevant to emissions to air that were applicable at the time when the IFC Board approved the investment. However, the following findings identified in the 2008 CAO audit report remain unaddressed:

- IFC's internal due diligence
- IFC's assurance process
- The underlying causes for non-compliance on behalf of IFC.

To date, the IFC has still not responded to the above issues, which continue to raise systemic concerns related to IFC processes. Given that Lukoil has ended its contractual obligations to IFC by prepaying its outstanding balance in January 2009, CAO will therefore close this audit leaving the findings pertinent to the functioning of IFC internal processes unaddressed.

Office of the Compliance Advisor/Ombudsman (CAO)
for the
International Finance Corporation (IFC)
Multilateral Investment Guarantee Agency (MIGA)

Background

IFC's involvement in the Karachaganak oil and gas condensate field in Kazakhstan began in 2000, and IFC received Board approval in 2002 to extend financing to Lukoil Overseas Karachaganak B.V. (Lukoil) to fund a portion of its share of the development of the Karachaganak oil and gas condensate field in Kazakhstan, the Karachaganak Petroleum Operation B.V. (the Project). In 2004, the CAO received the first complaint on behalf of residents of the nearby village of Berezovka. This complaint initiated a CAO audit in April 2007 of IFC's involvement in the Project. The audit responded to concerns raised about the impact of the Project on villagers' health and quality of life, particularly in relation to the effects of emissions to air.

In April 2008, the audit found IFC to be out of compliance on issues related to how IFC assured itself that emissions to air from the Karachaganak Project complied with IFC requirements. In its official response to the CAO audit, IFC failed to substantiate actions that assured CAO that IFC would move back into compliance. Therefore, the CAO kept the audit open and continued to monitor how IFC assured itself that the Project complied with IFC requirements.

On January 8, 2009, Lukoil ended its contractual obligations to IFC by prepaying its outstanding balance to IFC. This ended IFC's obligations to assure itself of Project performance, leaving the audit findings unaddressed.

Regardless of IFC's contractual relationship with its clients, the CAO has an obligation to try to fulfill its mandate to assure the President and the public that IFC's policy provisions have been adhered to: that is, that no harm occurs to people or the environment. CAO's technical audit panel visited the site in January 2009. The scope of the visit was for CAO to assure itself directly of the Project's performance by assessing it against applicable IFC requirements identified as audit criteria in the 2007/8 CAO audit.

CAO Findings

During the site visit, the CAO audit team addressed in detail the issues that were identified during the 2007/8 CAO audit and pertinent to the Project's performance. These were related to how IFC assured itself of the:

- Appropriate application of emission guidelines for incinerators
- Adequacy of stack emission monitoring programs
- Reporting of stack emissions
- Compliance of stack emissions with IFC requirements
- Adequacy of hydrogen sulfide and odor monitoring
- Completeness of ambient air quality monitoring programs
- Adequacy of ambient air quality monitoring programs

- Adequacy of the selection of ambient air quality monitoring sites.

During the site visit, the CAO audit team assured itself of the Project's compliance with applicable IFC requirements on a majority of the issues identified during the CAO audit.

This included: reviewing monitoring methodology and data reported on emissions from acid gas incinerators, clarifying requirements and planned monitoring of potential rotary kiln incinerators, assessing and verifying carbon monoxide (CO) and volatile organic compound (VOC) monitoring and assurance processes, clarifying reported "0" values in the reporting to Kazakhstan authorities, verifying the adequacy of the present stack emission monitoring programs and assessing adequacy of monitoring, and reported data, related to hydrogen sulfide and odor.

The following issues related to the Project's performance reporting remained outstanding after the January 2009 site visit:

- Reporting of stack emissions
- Completeness of ambient air quality monitoring programs
- Adequacy of the selection of ambient air quality monitoring sites.

On January 16, 2009, the Project committed to an action plan to address the outstanding issues identified by CAO. As of April 2009, CAO has received evidence and documentation from the Project that confirms that the agreed items have been acted upon. This has included; supplementary data on stack emissions; documented and verified actions in relation to the ambient air quality monitoring programs, and commitments to verify the adequacy of the selection of the ambient air quality monitoring sites.

CAO Conclusions

As of April 2009, CAO can confirm that the Project is now in compliance with IFC requirements identified in the 2008 CAO audit report. These requirements are the 1998 IFC policy provisions relevant to emissions to air that were applicable at the time when the IFC Board approved the investment.

However, the following findings identified in the 2008 CAO audit report remain unaddressed:

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To date, the IFC has still not responded to the above issues, which continue to raise systemic concerns related to IFC processes. Given that Lukoil has ended its contractual obligations to IFC by prepaying its outstanding balance in January 2009, CAO will therefore close this audit leaving the findings pertinent to the functioning of IFC internal processes unaddressed.