



ASSESSMENT REPORT

Complaint Regarding the Baku-Tbilisi-Ceyhan (BTC) Pipeline Project Tsemi, Georgia

February 2006

Office of the Compliance Advisor/Ombudsman
International Finance Corporation/
Multilateral Investment Guarantee Agency

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Introduction

The Office of Compliance Advisor/Ombudsman (CAO) is the independent recourse mechanism for the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA). The CAO reports directly to the President of the World Bank Group, and its mandate is to assist in addressing complaints by people affected by projects in a manner that is fair, objective, and constructive and to enhance the social and environmental outcomes of projects in which these IFC and MIGA play a role. In the first instance, complaints are managed through the CAO's Ombudsman function. The purpose of this assessment is to:

1. Provide a neutral assessment of the facts gathered during the assessment that are associated with issues raised in the complaint;
2. Recommend appropriate steps to assist parties to achieve resolution of this complaint.

The Baku-Tbilisi-Ceyhan (BTC) Main Export Pipeline project involves development, financing, construction, and operation of a dedicated crude oil pipeline system to transport oil from the existing Sangachal oil terminal near Baku, Azerbaijan, through Georgia, to a new export terminal at Ceyhan, Turkey, on the Mediterranean Sea. The 1,760- kilometer pipeline will be buried throughout its length as it passes through Azerbaijan (442 kilometers), Georgia (248 kilometers), and Turkey (1,070 kilometers). The pipeline is expected to transport up to one million barrels of crude oil per day from a cluster of discoveries in the Caspian Sea, known collectively as the Azeri, Chirag, deepwater Gunashli (ACG) field.

The project sponsor is BTC Co., a consortium of 11 partners established in August 2002. British Petroleum (BP), the largest shareholder in the project (30.1%), operates the pipeline. Other partners (in descending order) are SOCAR [State Oil Company of Azerbaijan] (25%), Unocal (8.9%), Statoil (8.7%), TPAO [Turkish Petroleum Corporation] (6.5%), Eni (5%), TotalFinaElf (5%), ITOCHU (3.4%), INPEX (2.5%), ConocoPhillips (2.5%), and Amerada Hess (2.3%). In its capacity as pipeline operator, BP leads the project design and construction phases. The total project cost is approximately US\$3.6 billion.

The International Finance Corporation's (IFC's) gross investment in the project is US\$250 million, \$125 million of which is for IFC's own account (referred to as an A loan), with an additional \$125 million in syndicated loans, (or so-called B Loan program).

The Georgia section of the pipeline starts in Gardabani at the Azerbaijani-Georgian border and passes through seven regions of the country, including the Borjomi Region where Tsemi village is located.

The Complaint

On June 9, 2005, the Office of the Compliance Advisor/Ombudsman (CAO) received a complaint related to the BTC oil pipeline project in Georgia, filed by a group of residents from the village of Tsemi in the Borjomi Region. The Tsemi complaint fulfilled CAO's acceptance criteria and CAO investigated it through desk reviews of related documents, followed by a field mission to Georgia in early December 2005.

The subject of the complaint is 1) ongoing presence of discoloring sediments in the village's drinking water supply, and 2) an alleged drop in tourism due to the water problems during the summers of 2004 and 2005.

In May 2004, erosion from a BTC pipeline right-of-way caused increased sedimentation in the spring that serves as the domestic water supply for Tsemi and three other villages. In July 2004, after several discussions with BTC about the problem, BTC agreed to install a new head facility at a location chosen by the Gamgabeli (mayor), and approximately 3.7 km of new water pipe. That facility, which approximately 4 kilometers to a reservoir which serves the three villages, was completed in October 2004.

Residents say they were without water for nearly six months, before and during construction of the new head facility. According to both residents and BTC staff, BTC Co. delivered spring water in tankers to specific locations in Tsemi village for just over two months – from 20 August to 31 October 2004.

The complaint states that during the 2004 season, the number of tourists in Tsemi dropped sharply, both in the village's health resorts and in private rental properties. As a result, the majority of residents lost income, a claim based on unofficial statistical data from the Tsemi Council Office.

During the spring of 2005, villagers claim the water quality grew worse, and the summer tourist season underwent an even more dramatic decline than the 2004 season.

In the fall of 2004, residents attempted to address the problem by registering a complaint with BTC's public relations department, demanding a working group be created which would include village representatives and BTC public relations personnel to study the extent of damage to the village. They also demanded each family be compensated for the lost tourism revenues. BTC rejected the complaint in January 2005 on the grounds that residents had no specific or objective evidence linking the poor water quality with a drop in visitation or tourism revenues.

In the complaint filed with CAO in June 2005, residents demanded that:

1. A working group be created, consisting of BTC public relations officers and village community representatives, to estimate the damage to residents;
2. The working group estimate the damage individually for each family;
3. The company reimburse each family according to the damage estimated by the working group;
4. The Company performs additional research into the reasons for the drinking water "contamination."

The CAO accepted the complaint on August 2, 2005. In December 2005, CAO undertook a field assessment in Georgia, which included meetings in Tbilisi, Tsemi, Bakuriani, and Borjomi with the following parties:

Tbilisi	
Green Alternative BTC Co.	<ul style="list-style-type: none"> • Kety Gujaraidze • Manana Kochladze (Bankwatch Network) • David Glendinning, Communications and External Affairs Manager; • Maria Aycrigg, Environmental and Social Programmes manager; • Dave Morgan, Engineering Manager; • Josée Lemieux, Senior Corporate Responsibility Advisor
Tsemi	
Twenty-four residents of Tsemi Village	Including: Ketino Tabatadze, Marina Gogoladze, Natela Tsitskishvili, Izo Gelashoili, Izo Sarkisiani, Zeinab Tabatadze, Ketino Tediashvili, Tsitso Gogoladze, Maquala Goshadze, Khetuna Vepkhvadze, Omar Tabatadze, Givi Dvalashvili, Darejan Tabatadze, Zaur Tabatadze, Mtuarisa Tabatadze, Mzia Nozadze, Manana Tvaradze
Bakuriani	
BTC Co.	<ul style="list-style-type: none"> • Dave Morgan, Engineering Manager • Mary Arnesen, Field Social Coordinator • Maka Gogia, community Liaison Officer
Borjomi	
Governor of Borjomi Region	George Talakhadze

Assessment Findings

On 2 December, CAO met in Tsemi village with approximately 24 residents to discuss the complaint and to follow up on residents' interactions with BTC in the four months since the complaint was accepted. Discussion focused on the complaint's two key issues: 1) the turbid community water supply and degree to which BTC's newly installed water delivery system addressed the issue; and 2) the alleged loss in tourism and revenues due to the bad water.

Villagers claim that despite completion of the new head facility, the 2-kilometer section that runs from the reservoir fed by the head facility into the village itself is still contaminated with sediments. They presented two discoloured tap water samples, collected on 2 September and 5 November, 2005, each of which contained obvious sediment.

According to meeting participants, erosion and excess sedimentation into the stream from the right-of-way re-occurred in August 2005, two months after the original complaint was filed with CAO. (BTC Co. confirmed this information in a conversation with CAO subsequent to the

community meeting.) After a number of allegedly contentious exchanges, BTC installed a second head facility and a 160 mm diameter plastic water pipe along the stream valley. This facility was completed in November 2005. Spring water was again delivered to Tsemi during construction of the facility, from 28 August and 11 November, 2005.

Tsemi residents say that during the periods of excess sedimentation from the right-of-way, the 2-kilometre stretch of pipe that runs from the reservoir into their village was continuously impacted, and is now impossible to clean. Complainants said they attempted on several occasions to clean it, but have been unsuccessful because the heavy, clay soil is too difficult to ream from the ageing steel pipes. According to residents, BTC's investment in the new head facility was an important remediation effort, but they will not consider the project complete until water runs clean from residents' taps.

Complainants are requesting that BTC provide the 2 kilometres of new pipe, which they have agreed to install themselves. The complainants told CAO that this final effort to remediate the contaminated water supply would satisfy their interests and close this portion of the complaint.

With regard to the impact on tourism, villagers feel strongly that visitation to Tsemi – and thus income to families – declined significantly beginning in 2004 and grew worse in 2005 as a result of problems with their water supply. They are requesting monetary compensation from BTC Co. for each family in Tsemi who suffered a loss.

Although villagers said they were prepared to take this case to court in the event they are not compensated by BTC Co., they also acknowledged that quantifiable evidence of their losses most likely would be required for a successful court ruling.

Complaints agreed that unless they can quantify their loss and demonstrate a clear connection between the turbid water and the alleged drop in tourism, BTC will be unlikely to compensate.

CAO asked whether complainants had considered alternatives to monetary compensation from BTC, such as forward-looking strategies to return tourism to the area. Villagers agreed such a strategy might help restore and improve their fledgling tourism industry. They decided to form a committee that will not only attempt to quantify the monetary losses, but also to formulate ideas for promoting tourism in Tsemi. The complainants said they will work through Green Alternative to complete and submit their quantitative evaluation of lost revenues for BTC's consideration.

On 3 December, CAO met in Borjomi with the BTC engineer who supervised installation of the newly completed drinking water deliver system, and with two Community Liaison Officers (CLOs). The BTC team led CAO on a tour of the old and new system – which supplies water to the villages of Tsemi, Tba, Libani, and Sadgeri.

During the tour of the old and new domestic water systems, BTC personnel explained that when the erosion off the right-of-way reoccurred in August 2005, a number of meetings were held between the company and residents to seek solutions. According to BTC, villagers initially agreed to provide land access for the temporary head facility, but then withdrew the commitment. After several subsequent meetings, the parties agreed in October 2005 to install the new temporary head facility and the 160-mm diameter water pipe along the stream valley. This resolved the issue surrounding land access, and allowed installation of the pipe to begin. After the work was completed in November 2005, BTC held a joint inspection with the Gamgabeli (mayor) on 12 November, 2005. BTC confirmed that spring water was delivered during construction to the village of Tsemi only, as the other three villages that draw from the

reservoir (Tba, Libani and Sadgeri) told BTC they did not require tankered water. Tsemi residents claim that of the four villages, theirs was hit hardest by the construction-caused erosion problems.

Also on 3 December, CAO met with the Governor of the Borjomi Region, George Talakhadze, to discuss the complaint and his perspective on the tourism situation in Tsemi. Governor Talakhadze said it will be very difficult for villagers to quantify their claim for compensation, because he believes they do not keep adequate records and have failed to report tourism revenues to the district tax office, as required by regional tax code. The Governor said he believes that while Tsemi did undergo a difficult period regarding the water, tourism has declined in the region primarily because of an underdeveloped service infrastructure and a dearth of amenities and conveniences for tourists. He supported the idea of a working group focused on growing the region's tourism industry, and said some portion of the campaign should be specific to Tsemi – to both compensate for their period without water, and because it is an important region with high potential for development.

On 5 December, CAO met in Tbilisi with BTC representatives to brief them on the field trip and discussions with complainants and the Governor. BTC agreed verbally to supply Tsemi village with the water pipe it is requesting, provided Tsemi residents will complete the installation.

Agreements

During the CAO field trip to Georgia, parties to the complaint reached several agreements toward resolution of this complaint. These include:

1. Mitigation of turbid water supply

BTC Co.

- BTC Co. understands that complainants are satisfied with the new water supply system built by BTC Co. upstream of the Andezit filter facility. This new water supply is outside the influence of the pipelines' right-of-way and cannot be affected by run-off from the right-of-way. In spring 2006, BTC Co. will replace the temporary head facility and bury the new pipeline, which is currently above ground, providing Tsemi Sakrebulo can provide unrestricted land access.
- BTC Co. will provide Tsemi Sakrebulo with approximately 2 km of water pipe to replace the section downstream of the Andezit filter facility.
- BTC Co. will provide the pipe free of charge to Tsemi Sakrebulo on the condition that Tsemi residents will take full responsibility for installation of the pipe delivered by BTC Co.

Complainants

- Representatives from Tsemi Sakrebulo will contact the BTC Co. Engineering Manager to discuss their requirements and arrange for delivery of the approximately 2 km of new water pipe.
- Tsemi Sakrebulo residents will take full responsibility for installation of the new water pipe.

- Delivery of the new water pipe will satisfy complainants' claim against BTC Co. regarding repair and mitigation of Tsemi Sakrebulo's contaminated water supply.

2) Compensation for decline in tourism

BTC Co.

- BTC Co. will await a report from complainants that quantifies the alleged drop in tourism revenues for the 2004 and 2005 tourist seasons and that demonstrates the alleged causal relationship between the turbid domestic water supply and tourists' decision to stay away. Upon submittal, BTC Co. will assess the validity of the claims.
- BTC Co. has acknowledged that construction runoff contributed to increased turbidity in the domestic water supply to Tsemi Sakrebulo. In an effort to further remediate the situation beyond the actions already taken to improve the domestic water system, BTC Co. agrees to take part in meetings with complaints and representatives of local- and district-level governments to discuss options for promoting tourism in the region through advertising and media outlets (television, radio, print).

Complainants

Complainants have formed a working group, comprised of residents and a local administrative official, who will work together to:

- Quantify the monetary impact on Tsemi Sakrebulo families of the turbid domestic water supply on the 2004 and 2005 tourist seasons (including a comparison of 2004 and 2005 revenues with revenues from previous years);
- Collect testimonials from individuals who intended to stay in Tsemi Sakrebulo on holiday but decided against it due to the water situation;
- Identify any other evidence they feel will establish a causal relationship between construction-related turbidity and declining tourism;
- Develop ideas for how best to promote future tourism in the Tsemi area, and a framework for working together with BTC and local and regional officials on a collaborative campaign to promote tourism.

Complainants will work through Green Alternative to produce and deliver the report to BTC and to CAO.

CAO Recommendations

1) Mitigation of turbid water supply

BTC Co. should meet with a representative(s) of villagers in Tsemi Sakrebulo at the pipeline to ensure that parties agree on the specifics of the materials to be delivered, including length, diameter and type of pipe. At that meeting, the parties also should agree on a specific date for

delivery of the pipe, and complainants should clarify any questions regarding appropriate installation of the pipe.

BTC should formally hand over the agreed-upon materials to residents, who will inspect the delivery to ensure it matches their requirements. BTC Co. and residents should be prepared to sign a written agreement that the transaction has been completed, and which designates Tsemi Sakrebulo as the responsible controlling entity if the pipeline requires maintenance or repairs.

Complainants should contact BTC Co. when the pipe installation is complete, to indicate it has been successfully installed and to confirm that the complaint regarding the discoloured water is closed.

2) Compensation for decline in tourism

By mid-February 2006, complainants should:

- Submit a final report to BTC Co. and CAO which quantifies the monetary impact of the turbid water supply on the 2004 and 2005 tourist seasons. The report should include comparisons of 2004 and 2005 revenues with revenues from previous years, tourist-income records from individual families, and any supporting documents from the local tax and/or tourism authorities.
- Finalize an outline of residents' ideas for promoting tourism in the Tsemi region. The outline should include at a minimum: 1) the specific features and attractions unique to the area which residents feel should be promoted; 2) a description of the various types and prices of accommodation available in Tsemi; and 3) attachments of any existing promotional materials that villagers have or are currently using. The outline should be submitted to the BTC Co. communications / public affairs department, along with a request for BTC Co. to convene a meeting involving Tsemi residents, local and regional government officials involved in tourism, and BTC Co. communications / public affairs personnel.

BTC Co. communications / public affairs personnel should convene a meeting at which the above named stakeholders can collaboratively discuss and develop a tourism promotion campaign that incorporates the ideas and interests of the parties. CAO is available to assist with agenda-setting or facilitation of a mid-February meeting of the parties.

As a way to further express its published commitment* that the pipeline "will help to pay for lasting economic, social and environmental benefits for the people of Azerbaijan, Georgia and Turkey," BTC Co. should consider leading a collaborative initiative, inclusive of all the impacted stakeholders, to promote the region's ecological and other tourist attractions.

* http://www.caspianddevelopmentandexport.com/ASP/BTC_LastBenefit.asp