



Disaster in the pipeline: Baku-Tbilisi-Ceyhan

Greg Muttitt
May 2004

The \$3.6 billion BTC pipeline project gave banks an early test of their implementation of the Equator Principles – a test which they comprehensively failed.

In February 2004, the BP-led Baku-Tbilisi-Ceyhan (BTC) pipeline received loans from 15 major commercial banks, 9 of which had adopted the Equator Principles.

A political project

Widely recognised to be far more of a political project than an economic one, the 1,700km pipeline will convey Caspian crude oil from Baku in Azerbaijan to Ceyhan on the Turkish coast of the Mediterranean. It was conceived in the 1990s by the USA, as a means to supply thirsty western markets with non-Middle Eastern oil, to undermine Iran and Russia, and to assert US dominance in a former Soviet sphere of influence.

However, as the pipeline plans developed it became increasingly apparent to civil society groups that this geopolitical meddling would prop up undemocratic regimes, exacerbate tensions in the region and contribute to human rights abuses and environmental destruction.

Worsening human rights situation

These fears were realised in November 2003, when Azerbaijan's Presidential election was won by Ilham Aliyev, the son of the previous long-term Azeri ruler. The election, described by official observers from the Organisation for Security and Co-operation in Europe as “fraudulent”, was followed by a brutal clampdown against opposition parties. In his inauguration speech, Aliyev promised that he would use oil revenues to build up the army, and threatened to restart the war with Armenia. These disturbing events were met with a deafening silence from the West, which was keen not to upset oil interests in the region.

Just a couple of weeks later, a revolution took place in Georgia, which was generally seen as a response to the corruption of the Shevardnadze regime, and its failure to relieve the poverty of the majority of the population. Since taking power, new President Mikhail Sakashvili has said that Shevardnadze overstated the benefits to the Georgian people of the BTC pipeline.

Meanwhile in Turkey, there is a history of decades of human rights abuses against the Kurds, and indeed of use by the state of infrastructure projects to displace Kurdish villages or to increase security measures.

The BTC route pipeline will run through a number of wetlands of critical importance for protected and endangered birds such as Dalmatian pelicans, black storks and imperial eagles. The route

runs through an area of high seismic activity, landslides and avalanches. A rupture in the pipeline and consequent oil leak could have devastating consequences. In Georgia, the pipeline will run through the Borjomi National Park, an important cultural and tourist site, and the source of Georgia's largest export – Borjomi mineral water, which is famous across the Former Soviet Union.

Against this background of political, environmental and human rights risk, the value of a tool such as the Equator Principles becomes apparent. But only if that tool is genuinely and effectively used.

Equator Principles not applied

The Equator Principles can be used in two ways – to exclude financing of projects which fail to meet certain minimum standards, and to set markers for improving projects' standards. In the BTC case, the banks failed on both counts.

One of the most disturbing breaches of the Equator Principles by the project was in the project sponsors' decision not to apply the World Bank's safeguard policy on Indigenous Peoples. That policy requires publication of a specific plan to ensure that ethnic minorities are not adversely affected by a project, and compliance with the policy is a clear requirement of the Equator Principles.

The impact of this failure is perhaps most stark in Turkey. There the BTC pipeline will be guarded by the notorious Gendarmerie, which has been repeatedly criticised by the Council of Europe and the European Court of Human Rights, and has been associated with displacement and destruction of villages, torture, and 'disappearances', especially against Kurdish people. It is almost inevitable that the Gendarmerie will use the pipeline as a pretext for carrying out raids on local Kurds – and the decision not to apply the safeguard policy leaves no protection against this.

Already since the financing decision, at least one Kurdish human rights defender has been arrested and tortured, following his work to help affected landowners to obtain the compensation due to them.

The breaches of the Equator Principles in fact go much wider. In October 2003, 14 organisations in 11 countries wrote to the Equator banks, pointing out that the BTC plans violated the Equator Principles on numerous counts including the Indigenous Peoples policy on 30 counts, 4 other World Bank standards (with which the Equator Principles require compliance) on 97 counts, and 9 other clauses of the Equator Principles on 30 counts.

For example, many landowners were poorly compensated for losing their land, and some not at all. The project environmental impact assessment failed to adequately assess the pipeline damage – for example, the whole 1,000 kilometres of the Turkey section of the pipeline was surveyed in just a few weeks, with even highly sensitive and protected sites being visited only on one day. Consultation procedures were cursory at best, and often in the wrong language, or only carried out after all decisions had already been made.

The banks commissioned a survey by consultants, which they said found the project in compliance with the Equator Principles – but refused repeated requests to disclose the survey.

In private, several banks admitted that they were not carrying out due diligence because they simply trusted BP and the International Finance Corporation to get it right. This despite the fact that the Equator Principles state "The adopting institutions view these principles as a framework for developing individual, internal practices and policies.... Banks are adopting and implementing these principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank."

Pipeline technical failings

That trust proved to be misplaced. In February 2004, the *Sunday Times* newspaper reported that the pipeline had been using an inappropriate weld coating, which risked causing major leakage. The findings came from a senior consultant, an international expert in weld coatings, who had worked on the pipeline and advised against using the coating. He wrote in a report to BP, "We are completely out on a limb ... I have witnessed many failures in specifications . . . but the situation on the pipeline is unique in my 41 years' experience. There is no question in my own and many other people's minds that the wrong system has been chosen through a seriously flawed selection programme."

Cracks have now appeared in the pipeline coatings, yet arguments continue between BP, financial institutions and contractors over whether wrongly coated sections of pipeline should now be dug up and re-coated.

In the ensuing correspondence, financial institutions have showed themselves to be in complete disarray over the issue, and contradicted themselves and each other in trying to explain away the problems. Meanwhile, the private banks, including the Equator signatories, have refused to comment at all, citing commercial confidentiality.

A British parliamentary committee recently criticised the Export Credit Guarantees Department for failing to carry out its own due diligence on BTC, especially on the coatings issue. Commercial banks appear to be guilty of the same omission.

Furthermore, rumours abound that there are more technical failures to come to light. A report by BP's own advisers stated that standards in the Turkish section of the pipeline were well below what BP was claiming.

Banks will be held to account

International NGOs have committed themselves to continuing to monitor the BTC pipeline, and to holding its financiers to account. As banks see themselves publicly associated with the problems of the BTC pipeline, including poor technical standards and increasing human rights fears, they should ask themselves whether the reputation damage and loss of credibility are really compensated by the returns from the BTC investment.

There are three sets of legal actions in process against the pipeline. Georgian environmental group Green Alternative alleges that the pipeline consortium and Shevardnadze government violated Georgian environmental law in routing the pipeline through the Borjomi-Kharagauli National Park. Green Alternative is appealing an unfavourable ruling on this case. Two international NGOs have initiated a case in the European Court of Justice, which argues that the project legal agreements so undermined Turkey's ability to legislate that it was in breach of its Accession agreements with the European Union. And 38 landowners living in Turkey have applied to the European Court of Human Rights, arguing that their property was expropriated unfairly and in violation of their rights.

The banks themselves are now also under direct attack for their failed due diligence on the BTC pipeline. A Belgian NGO, Proyecta Gato, has made a formal complaint against three Belgian banks (Dexia, KBC and ING – all three Equator signatories) through the OECD's Guidelines on Multinational Enterprises. The complaint centres on the pipeline coating issue and on the undue constraint over the host governments' ability to regulate that is imposed through the project legal agreements.

Banks can thus be sure they have not heard the last of the BTC project.

As Jules Peck of WWF has commented, "As a test case, the BTC pipeline would seem to expose the signing of these banks to the Principles as a public relations exercise which allows them to continue with business as usual whatever the risks to people and nature."

Key lessons for Equator banks from the BTC pipeline:

- The Equator Principles must be actively used to exclude projects which fail to meet their standards, not just as a vague statement of intent.
- Banks should carry out their own due diligence on projects, not simply rely on the sponsor or on the International Finance Corporation to vet projects.
- Banks should be prepared to stake their reputations on the projects they finance.
- Banks will only gain the trust of civil society if they are transparent in their decisions – it is essential that they disclose their assessments of projects' compliance.

Construction: summer 2003 – spring 2005

Lead arrangers: ABN Amro (E), Citigroup (E), Mizuho (E), Société Générale.

Other banks involved: Banca Intesa, BNP Paribas, Credit Agricole, Dexia (E), Hypovereinsbank (E), ING (E), KBC (E), Natexis, RBS (E), San Paolo IMI, West LB (E).
(E = Equator Principles signatory)