The Great Enablers

How Investments by International Financial Institutions Threaten the Fragile Caspian Sea Ecosystem

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Executive Summary

Currently International Financial Institutions (IFIs) are directly or indirectly intensifying the extraction of and trade in Caspian Sea hydrocarbons in Kazakhstan and Turkmenistan through investments in service, transport and infrastructure projects that allow their delivery to world markets. *The Great Enablers* examines a trail of investments made by the EBRD, ADB, IDB and the World Bank over the past several years that collectively loosen the logistical bottlenecks hampering the development of the Caspian's vast oil and gas resources.

The report reveals that seemingly uncontroversial IFI investments are in fact likely to harm the Caspian's fragile ecosystem. New vessels, ports and railroads will increase the extraction and transportation rate of hydrocarbons through especially vulnerable protected areas. Taking into account recent project implementation experiences and the general state of civil liberties in the two countries, the report argues that these IFI-supported projects will also harm people affected by the extractive projects if their rights are not fully respected.

In addition, a brief examination of political developments in the Caspian region casts doubt on the appropriateness of IFI involvement in resource-related projects there, particularly in light of unresolved territorial disputes and evidence of increasing tensions and militarization in the region. Moreover, both countries' poor track records on human rights and governance, particularly in the hydrocarbon industry, suggest that IFI involvement in resource-related projects undermines their core missions and risks their reputations.

The report concludes that IFI investments in projects that further the extraction of hydrocarbon resources will further entrench Turkmenistan's and Kazakhstan's economies in an environmentally perilous, centrally controlled, resource-dependent path—a poor, if not impossible, way to achieve sustainable development.

The report's four recommendations for IFIs call for:
1) A*bstaining from state-controlled resource-related projects* due to the governance issues involved;
2) *Incorporating specialized human rights risks assessments* at the project and institutional levels to guard against weak application of the rule of law;
3) *Avoiding environmentally fragile areas*; and,
4) *Adopting environmental and social safeguards by the Islamic Development Bank*, which currently lacks even basic safeguard policies.

The report recommends that environmental and rights-based civil society groups should:
1) *Take initiative in organizing consultative and approval processes* independently from companies and the state in order to counterbalance a conflict of interest between the regulators and companies; and,
2) *Build alliances with institutions* and international bodies to attract greater attention to the controversies connected with hydrocarbon development in Kazakhstan and Turkmenistan and to augment their advocacy power.

A New IFI Niche in the Caspian Sea
Loosening hydrocarbon supply bottlenecks

Forecasts estimate that Kazakhstan will double its crude oil exports between 2010 and 2015–20 to over 89 million tons per year, according to a World Bank study and independent media sources.[1] Kazakhstan's largest oil field, the giant Kashagan, is an offshore field that requires coastal support infrastructure and a crude transport fleet to tap into its reserves. The World Bank has estimated that without a future agreement on a trans-Caspian pipeline, Kashagan's development will remain wholly dependent on the limited capacity of oil tankers.[2] Turkmenistan also requires an upgrade of its cargo and transport infrastructure if it is to remain competitive in the regional oil market as new gas and oil refining plants come online. The Turkmenbashi port on the Caspian Sea is emerging as a significant cargo handling hub for Turkmenistan. In order to take advantage of its location and to bring its resources to markets to the north, south and west, Turkmenistan plans to expand its transport network and build a Caspian cargo fleet.

A master plan for a regional economic infrastructure development needs assessment has also been demonstrated by the World Bank's study on Caucasus Transport Corridor for Oil and Oil Products,[3] which lays out how underdeveloped marine and transport facilities create bottlenecks instead of supporting the growing oil and gas production in the Caspian.

In order to address this constraint on supply routes, international finance institutions (IFIs) are prepared to invest capital and offer technical expertise to the resource-rich governments. Priorities within European Bank for Reconstruction and Development (EBRD) country strategies for Turkmenistan and Kazakhstan include investments in regional transport and extractive infrastructure such as roads and port links of regional significance. Other IFIs—notably, the World Bank and the Asian Development Bank (ADB)—are also investing in road, rail and port infrastructure to facilitate trade as part of the Central Asia Regional Economic Cooperation (CAREC) transport corridor.[4] The World Bank and its private-sector arm, the International Finance Corporation (IFC), have also considered investments in ports and related infrastructure.

This report demonstrates how IFIs have made separate but complementary investments in the Caspian Sea basin that attempt to overcome the transportation hurdles in the hydrocarbon supply chain to the west. The EBRD, World Bank and IFC have taken under consideration investments in: the expansion of the Turkmenbashi port; the development of a shipyard facility at Turkmenbashi; the development of the Sartas support base and procurement of support vessels; oil clean-up emergency response mechanisms; and other projects. Each of these projects is linked to the development of the Kashagan oil field or other smaller projects and the transport of oil to European and Middle Eastern markets. IFIs have found a convenient and lucrative business niche in financing large infrastructure projects. Such projects are profitable; large project size makes them efficient to invest in, and IFIs can claim to bring expertise and added value through international experience, best practices and flexible financing schemes, such as Public Private Partnerships (PPPs).

Unfortunately, IFI involvement in hydrocarbon and affiliated industries takes place in a controversial setting of poor governance, political tensions and human rights violations.

[1] World Bank. Caucasus Transport Corridor for Oil and Oil Products, *World Bank*, (2008). p. 42
[2] *ibid*., p. 55
[3] *Ibid*., p. 1.
[4] Asian Development Bank [ADB]. 2009, January 13. *Framework Financing Agreement: Multitranche Financing Facility.*

INVESTMENTS IN KAZAKHSTAN

The government of Kazakhstan has ambitious hopes and plans for the development of its oil and gas industry. It claims to possess projected reserves of 100 billion barrels of oil, despite the fact that proven reserves are only estimated at 30 billion barrels. Moreover, Kazakhstan plans to ramp up oil extraction to 100 million barrels per year by 2015.[5] However, almost half of the existing reserves and most of the expected reserves to be extracted in the next decade will come from the seabed and shores of the Caspian Sea, the world's largest enclosed body of water. To execute this oil extraction, Kazakhstan requires technological know-how and massive investments into its coastal infrastructure, transport and service fleet. The government estimates that the next phase of development of the North Caspian oilfields will require construction of various off-shore man-made structures weighing in total over 550,000 tons. To complete the required work within five years as planned, the combined output of Kazakhstan's existing shipyards would have to triple.[6] In this environment, IFIs are willing to finance the transport and industrial capacities that would allow extraction and transportation of liquid natural gas (LNG), oil, and other petroleum products.

The ADB opted to finance on-shore rail, road and other transport infrastructure projects designed to link resource regions, key logistic nodes and markets East and South of the Caspian. The IFC considered investing in coastal support bases, while the EBRD invested in a range of projects from ports to industry vessels linked with resource extraction. The EBRD's 2010 strategy for Kazakhstan identifies upstream exploration and production and transportation as its primary and secondary priority sectors.[7]

[5] Embassy of the Republic of Kazakhstan to the United States. (n.d.). *Energy Sector: Hydrocarbons*.
[6] Butyrina, E. (2010, July 23). Implementation of state and regional programs and priorities to ensure the development of transportation in the Caspian Sea are the main objectives of the development of the sea port infrastructure in the long term.
[7] EBRD (2010). Strategy for Kazakhstan (p. 63).

EBRD PROJECTS

2012 Zhanros Group (pipeline)
The EBRD has disclosed its intention to issue a $15 million loan to the oil services/drilling company Zhanros Group, which benefited from EBRD financing in 2010.[8] The EBRD financing would allow Zhanros to acquire hydraulic fracturing technology to be used in oil fields in western Kazakhstan.

2011 Heidelberg Caspi Cement (dropped)
Since the spring of 2011, the IFC and EBRD considered a joint investment in a green-field cement plant near Shetpe village, not far from Aktau on the coast of the Caspian Sea. The plant's cement is expected to be in high demand for ongoing municipal construction projects in Aktau (Aktau city, its airport), but also for exports to Uzbekistan and Turkmenistan, and for the oil and gas industry.[9,10] Nevertheless, the EBRD dropped this project in late 2011, and the IFC also put its proposed investment on hold.

2010 Western Oil
In 2010, the EBRD offered a $50 million loan to Petrolinvest S.A., which was extended in 2012. The investment allowed Petrolinvest, a Polish oil and gas company operating in Poland and Kazakhstan, to complete its exploration activities at the OTG and EMBA concessions in northwestern Kazakhstan.

2010 RuanNalco
The EBRD invested $8 million in a joint venture by RuanNalco aimed at producing a wide variety of industrial chemicals used in oil extraction, transportation and processing. The EBRD's loan finances the construction of a new chemical plant in Atyrau designed to meet growing demand from Tengiz, Karachaganak and, in the future, Kashagan

[8] EBRD. (2012, September 28). *Zhanros Group Expansion Project*.
[9] EBRD. (2011, May 10). *Non-Technical Summary: Establishment of 2,000 tpd Clinker Capacity Greenfield Cement.*
[10] Caspi Cement. (n.d.). *HeidelbergCement in Kazakhstan*.

operators.[11] The EBRD's environmental impact assessment of the RuanNalco project included only the environmental impacts of constructing the plant, while ignoring the potential impacts of the chemicals themselves, which will be housed at the site. Additionally, the project is located on the edge of the city of Atyrau, whose population is approximately 145,000. Any accident at the site would put the urban population at risk. Civil society organizations have raised these and other concerns about the project's lack of due diligence with the EBRD.

2010–2011 Kaztemirtrans

The EBRD has been offering support to Kazakhstan's railway sector since 1999 by upgrading its telecommunication and safety features. Since 2009, however, EBRD investments have shifted their focus to help the state-owned Kaztemirtrans restock its freight wagons, some carrying oil or oil products. In 2009, a $50 million EBRD loan enabled the company to purchase a number of oil rail tankers. A larger $200 million loan from the EBRD in 2010 helped Kaztemirtrans acquire an additional 3,000 freight wagons,[12] which may have increased the company's rolling stock by up to 30 percent.[13] Also in 2010, the EBRD signed a $700 million Eurobond issued by Kaztemirtrans' parent company and the national railway operator Kazakhstan Temir Zholy. According to the EBRD press statement at the time, Kazakhstan Temir Zholy used bond proceeds to procure additional freight wagons for its subsidiary Kaztemirtrans.[14] While freight wagons purchased with EBRD financing help transport a wide variety of goods, one-fifth of the 3,000 freight cars are rail tankers used to transport petroleum and other liquid cargo.[15]

In recent years, Kazakhstan has accelerated investments in its railway system. Its vast, flat territory requires a developed railway system to carry wheat and oil products from the energy-rich northwest to the populous southeast of the country. In addition, two of Kazakhstan's three oil refineries are located in Pavlodar (northern Kazakhstan) and Shymkent (southern Kazakhstan). Given the country's goal to process more of its oil domestically and reach self-sufficiency in domestic fuel production by 2014,[16] a larger and more streamlined railway system is essential to efficiently transport oil to existing refineries and chemical plants. This ongoing demand for large capital investments in the railway sector has likely shaped the EBRD's current country strategy, which prioritizes the transport sector.

2010 Circle Maritime Invest Project

In December 2010, the EBRD issued a senior loan of $65 million to the Kazakhstan-registered firm Circle Maritime Invest to cover the post-delivery acquisition costs of three tugboats to service its main client, Agip KCO, which leads the development of the Kashagan oil field. According to the EBRD and Caspian Offshore Construction, an operating subsidiary of CMI, the EBRD-financed vessels will be used for the year-round servicing of Kashagan's off-shore oil platforms.[17,18]

2008 Bautino II Project

In 2008, the EBRD issued a second loan of $10 million for the construction of a vessel maintenance facility at the Bautino Atash marine base, which was previously financed by the EBRD. The Atash facility supports Agip KCO (now Shell) vessels serving oil and gas exploration efforts in the

[11] Grytsenko, S. (2010, December 27). *EBRD Finances Oil and Gas Field Chemicals Production In Kazakhstan.*

[12] EBRD. (2010, September 23). *Kaztemirtrans Restructuring Loan*.

[13] Kaztemirtrans. (n.d.). *Annual Report 2010*.

[14] EBRD. (2010, October 6). *KTZ Eurobond*.

[15] Based on public procurement bids, at least 202 of the wagons were 8-wheel tanks for petroleum products intended for Semipalatinsk in eastern Kazakhstan, according to the Public Tenders website (http://www.publictenders.net/tender/320931 and http://www.publictenders.net/tender/1013909.) Kaztemirtrans also sought a larger lot of 500 units of tank-wagons used to transport liquids, possibly petroleum products (http://www.publictenders.net/tender/523997).

[16] The President of the Republic of Kazakhstan. (2010, February). *Kazakhstan's Strategic Development Plan 2020.* The plan is an intermediary roadmap to the country's ambitious long term Strategy 2030. The 2020 Strategic plan sets specific development milestones.

[17] EBRD. (2010, November 22). *Circle Maritime Invest.*

[18] Caspian Offshore Construction. (n.d.). *Operation and Maintenance of Marine Fleet*.

northern Caspian, primarily by servicing vessels and shipping the rocks used to construct and maintain the artificial islands built at Kashagan. In 2009, marine bases at Bautino loaded some 1.9 million tons of various cargo.[19] However, the current workload of the port and amount of cargo traffic is limited by old infrastructure, delays in Kashagan field development and the lack of rail links to Bautino.[20] Once new facilities are built and a rail link is created, the port may increase its activity and output, thereby posing a considerably higher environmental and social risk than originally assessed.

The construction and operation of the Atash marine support base resulted in significant adverse environmental and social impacts, and as a result the two projects were graded Category A and Category B, respectively.[21] Environmental impact assessments revealed net negative impacts to the environment due to dredging and sea reclamation, and few social benefits for the surrounding communities. In fact, the project would be a detriment to the livelihoods of nearby communities; with the construction of the vessel maintenance facility as part of the Bautino II investment, 38 households would be relocated. Moreover, atmospheric emissions, access to potable water and waste contamination remain a concern for the local population, which relies on artisanal wells that lie downstream from waste dump sites.[22] However, citing the financial crisis, by 2009 it was clear that the owner Balykshy would not expand the territory of the base. As a result, the new management of Balykshy decided to postpone the resettlement indefinitely.[23] Nevertheless, the port owner continued with the construction within the existing port territory. Excessive noise and pollution from civil engineering works, aggrieved local communities, and continuing postponement and subsequent cancellation of the resettlement program led to the perception that the company misled the local community in order to obtain their approval during the initial consultations. A 2009 visit to Atash village by the Kazakhstani International Bureau for Human Rights and the Rule of Law logged complaints from local residents about odor and noise, the lack of an effective community relations mechanism, and the fact that EBRD staff had not been paying due attention to the growing concerns of local residents.[24] To date, the question of relocation and resettlement remains unresolved.

Meanwhile, those residents who opted for resettlement due to pollution and health concerns now have more reasons to be concerned as their neighborhood turns into an oil transshipment hub. The Kazakhstan government is set to build a railroad to Bautino and begin shipment of cargo and oil products through the existing ports.[25] The residents of Atash village will find themselves in the heart of an industrial, oil storage and shipment and drill waste storage zone. The EBRD should have taken into account the fact of future infrastructure development when negotiating and extending financing to Caspian Services Inc., especially since the EBRD has been involved in the construction of the Atash base and was familiar with how long-term development of the area will affect local residents.

In 2006, the EBRD made an investment of $28 million to fund the construction of the Bautino Atash marine base near the port of Aktau on the eastern shore of the Caspian. The new vessel supply and maintenance base operated by U.S.-registered Caspian Services Inc. was designed to service ships operating in the northern Caspian, in the Kashagan oil fields. An environmental audit

[19] CaspiEcology LLP. (2005). *Executive Summary of ESIA of Atash Marine Base.*
[20] *Ibid* 19.
[21] *Ibid* 19.
[22] *Ibid* 19.
[23] Correspondence with EBRD social and environmental specialists, January 13, 2012.
[24] Bureau of Human Rights and Rule of Law, monitoring field visits to the Atash residents, May 2009. Report is available upon request.
[25] Ural Railway Company. (2010, February 19) *Investment projects for construction of railways in Kazakhstan (Investicionnye proekty stroitelstva zheleznodorozhnyh linij v Kazakhstane).*

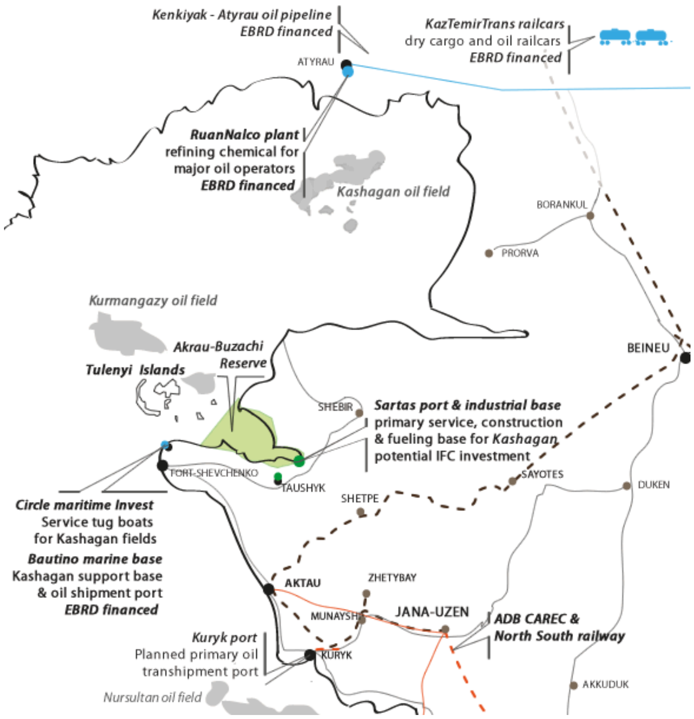

Figure 1: IFI investments in oil and gas infrastructure in Kazakhstan's North Caspian. Recent EBRD investments in blue, ADB in orange, and IFC investments in green.

conducted at the time of the second investment in Bautino in 2008 found that the base carried moderately significant cumulative impacts stemming from increased traffic and the combined impact of the Atash base and other bases, such as those owned by Agip's Tenis-Service, Caspian Service Group and others.[26]

2004 Kenkiyak-Atyrau Oil Pipeline

The EBRD provided $82 million in retroactive financing for the existing oil pipeline—which had been completed in late 2002—that connects the oilfields near Aktobe to the hub city of Atyrau, where oil is further pumped to Russia. With the completion of the pipeline to China, the Kenkiyak-Atyrau pipeline is now the western section of the longer Atyrau-China pipeline.

In this rather unusual investment, the EBRD could not conduct a full impact assessment as the pipeline already existed, and instead conducted only an environmental audit. Given the unusual nature of the investment, the environmental impact audit prepared for the bank had to justify the project implementation and mitigation measures used by the original developers, even though the audit indicated that the pipeline would merit a full and thorough impact assessment of a Category A project.

The EBRD's own audit notes that the project's risk mitigation is adequate in an accident-free scenario, but it warns that, as with many pipelines, "negative environmental consequences of potential accidents might have a major environmental factor."[27] The financing of this pipeline was criticized by public organizations as a dangerous precedent because of its piecemeal nature and lack of adequate and comprehensive impact assessments.[28]

2003 Atyrau–Aktau Road Project

The EBRD provided $119 million to finance the re-paving of 600 kilometers of road connecting Kazakhstan's main port of Aktau to the town of Atyrau, cities that are both important logistical and industrial hubs for off-shore and on-shore oil extraction. According to the EBRD, the road acts as a link in the Transport Corridor Europe-Central Asia (TRACECA) and supports development of the Tengiz field.[29] The road rehabilitation is an ongoing project, with the EBRD and Kazakhstan's public funds paying for about half of the road from Atyrau to Beineu. Beginning in 2011, the ADB began financing the reconstruction of the remaining link from Beineu to the port of Aktau.[30]

THE WORLD BANK GROUP

The World Bank plays a limited role in the development of oil and gas related projects along the coast of the Caspian Sea. However, the World Bank led a $3.4 billion project, along with other IFIs, to repair a transcontinental East-West road

[26] EBRD. (2008, February 4). *Bautino II.*

[27] EBRD. (2004, April). *Environmental Impact Assessment: MunaiTas NWPC CJSC (Republic of Kazakhstan).*

[28] Bank Information Center. (n.d.). *Kazakhstan: Extractive Industries*.

[29] EBRD. (2003, April). *Kazakhstan: Road Sector Restructuring—Atyrau-Aktau*.

[30] Ministry of Transport and Communications of Kazakhstan.

corridor across Kazakhstan that aims to link Asian, European and Russian markets.[31] The World Bank invested $2.2 billion of its own capital in this project.[32]

IFC PROJECTS

2012 Eastcomtrans Railroad Project
In what appears to be following in the EBRD's footsteps, the IFC is currently evaluating a potential $50 million investment in Kazakhstan's leading private rail freight carrier, Eastcomtrans. The company offers rail wagon rentals, logistics and shipment operations at the port of Aktau. Over 80 percent of its rolling-stock consists of oil cars and liquefied petroleum gas tanks that are leased by Kazakhstan's major oil and gas operators.[33] The IFC investment would enable the company to more than double the number of rail wagons available for lease from 6,000 to over 13,000 railcars,[34] or roughly 30 percent of Kazakhstan's entire oil freight railcar supply in 2010.[35] The IFC estimates that half of Kazakhstan's rail car fleet is dangerously out-of-date, with some cars in service well over 20 years awaiting a phased replacement.[36] The IFC investment would allow for a timely restocking of oil and LNG rail tanks, while also expanding the share of private businesses in the state-dominated railway sector.

Even though the World Bank–led portion of the project terminates in Aktobe, the rehabilitated road will play a key role in the international shipment of goods and resources across the Caspian Sea. The International Finance Corporation, in contrast to the World Bank, has taken a more active role and has recently considered supporting large infrastructure and transportation projects.

Eastcomtrans has one of the largest oil tanker fleets in Kazakhstan and transported 6 million tons of oil products in 2010, mostly from eastern to northwestern Kazakhstan and the Aktau port, but also to cities in the Eastern Europe.[37] Like other IFC investments in oil-gas support infrastructure that have a broad impact, this investment would benefit over twenty oil and transportation companies operating in the north Caspian, including such operators as Agip KCO, Tengizchevroil, KazTransOil and Lukoil.[38]

2011 Sartas Port
The IFC is also considering financing the Sartas port, another marine support base servicing the offshore oil and gas industry, designed to supplement the existing Bautino Atash base.[39] According to Kazakhstan's Ministry of Transportation, Sartas, along with Bautino, is expected to be one of the two main supply and support marine bases for off-shore oil extraction operations in Satbaev, Zhambil, Zhambay and Zhemchuzhina as well as the Kashagan oil fields in the north Caspian.[40]

The Sartas supply and support base will be a complex infrastructure node including a shipyard, a refueling station, a concrete mixing plant and a cargo storage facility. Like other similar bases, Sartas will also receive and process wastewater from ships. The original design also included a drilling waste processing plant with a capacity of 30,000 tons per year to process drilling waste from the north Caspian and future exploration activities.

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[31] Embassy of the Republic of Kazakhstan to the United States. (n.d.). Energy Sector: Hydrocarbons. *Website of* the e*mbassy of Kazakhstan to the United States, Economy of Kazakhstan.*
[32] The South-West Roads Project: The Western Europe-Western China International Transit Corridor is actually financed by a consortium of IFIs and the government of Kazakhstan. Other institutions are: EBRD, ADB, JICA and IDB.
[33] According to the company website, the share of oil and gas railcars is closer to 80%.
[34] International Finance Corporation [IFC]. (2012, March 13). *Environmental & Social Review Summary*.
[35] Eastcomtrans. (2010, August). *Corporate Presentation Eastcomtrans LLP.*
[36] *Ibid.* 35
[37] *Ibid.* 35
[38] Eastcomtrans LLP. (n.d.). *"Klienti i partnyori" (Clients and Partners)*.
[39] KazMarket. (2009, February 10). *Commercial News Update 2009* "According to experts, the implementation of the project will provide for the constant service of sea-based oilfield facilities through reducing the load on the Aktau and Bautino ports".
[40] Minutes of public consultation by the Sartas-Teniz Porty in Tauchyk village, 18 August 2011. Report available upon request.

Since existing infrastructure is inadequate, the Kazakhstan government plans to increase the capacity of existing marine infrastructure and build new off-shore oil support capacity with the financial aid of the IFC and several Korean investment companies. Shell, a client of the nearby Bautino supply base, is also looking to the Sartas port to supply services for the Kashagan field.

The environmental impacts of oil and gas development in the Caspian are well documented. Oil and gas development remains the greatest environmental threat to the Caspian region and has in the past encroached onto specially protected environmental areas.[41] At the same time, according to the IFC's own Environmental and Social Review, the Sartas marine base is located within a two-kilometer coastal buffer zone and only four kilometers from the *Aktau-Buzachi National Reserve*, home to critically endangered species such as the Caspian seal, steppe lynx and Central Asian gazelles, which are internationally recognized as rare and threatened species. The *Aktau-Buzachi National Reserve* is also the home and wintering ground for some 22 varieties of threatened bird species, the most famous of which are the flamingos.[42] The International Union for the Conservation of Nature designates most of Sartas bay as a protected area (*see Appendix 1, UNEP map of protected areas).*

Despite its vulnerability, the territory of the *Aktau-Buzachi Reserve*, as became apparent during public consultations held in Aktau in August 2011, lies within the boundaries of the proposed Sartas marine support base (s*ee Appendix 2, summary of public consultations on Sartas port project*). In 2005 a special commission formed by the Sartas-Teniz company reviewed the boundaries of the Reserve and suggested a "correction" of erroneous Reserve boundaries.[43] The government approved the proposed correction, thereby effectively carving up public land and marine real estate for the upcoming port infrastructure. Environmentalists from Mangistau Tabigat, pre-2005 Aktau University publications, and old maps available in Russian indicate that the *Aktau-Buzachi Reserve* is directly adjacent to local roads and the towns of Taushyk and Sartash, and its marine boundaries extend into Kochak bay.[44] An oil spill off- or on-shore would have dramatic consequences for biodiversity on Buzachi peninsula, especially for migratory birds wintering in shallow waters.

Moreover, the future ship routes to the supply base pass by the *Tulenyi Islands*, which provide habitat to Caspian seals (IUCN Red List of Threatened Animals) and are a "globally important habitat" for migrating birds according to Birdlife International.[45] The concerns about potential shipwreck pollution were exacerbated when on October 13, 2011, the tanker *Grigoriy Bugrov*, which was carrying heating oil at the time, partially sank near the environmentally sensitive area, although it was successfully recovered.[46] According to the IFC's own environmental screening of the project, Sartas may affect waters protected for the natural reproduction of sturgeon.[47]

Finally, Sartas port will be similar, yet larger, in function to the EBRD-financed Atash supply and service base. While the development of Sartas will have impacts similar to, if not greater than, those at the Atash base, IFC opted to assign the Sartas

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[41] UNEP/GRID-Arendal. (2000). *Environment and Security: Transforming risks into cooperation: The Case of the Eastern Caspian Region.*

[42] An online resource in Russian on the Mangishlak peninsula, including a section on the *Aktau-Buzachi Reserve*. Old map (pre-2005) indicates borders of the original Buzachi Reserve. (http://aqtau.narod.ru/buzachi.htm)

[43] Sundikov, chairman of the board of directors of Sartas-Teniz Porty in response to inquiry from Mangistau Tabigat environmental organization. A representative of Mangistau Tabigat noted that the territory of the Sartas port and supply base encroaches onto the territory of the Reserve.
Public consultation by the Sartas-Tenis Porty in Aktau, 20 August 2011. Document available upon request.

[44] Musaev, K. (2010, November 26). *Biologicheskoe raznoobraziye pribrezhnykh ekosistem Mangistauskoi oblasti i vliyaniye neftegazovykh mestrozhdenii na nego.*

[45] IFC. (2011, October 28). *Sartas Port Environmental & Social Review Summary.*

[46] Ministry of Transport of the Russian Federation. (2011, October 13). *Avariya tankera* Grigoriy Bugrov *na Kaspii*

[47] *Ibid.* 45.

investment a B-limited environmental and social category. The B-limited category means a more limited scope of impact assessment will not take into account impacts of other components of the port, even though IFC is well aware of the scale and nature of operations of the port.

In a response to an inquiry by the Kazakhstan-based environmental organization Green Salvation into the nature of the Sartas port and potential impacts on protected areas, the Mangistau Oblast branch of the Kazakhstan Ministry of Environment responded that Sartas was key to strategic objectives in developing resources in the northern Caspian. With respect to the potential impact to the Buzachi Reserve, the Ministry only advised that the development was a top government priority—one that was mentioned in Kazakhstan's president's address describing his 2020 vision.[48] The Ministry claims the project design takes into account environmental regulations for projects developed within protected areas and that risks will be adequately controlled. Moreover, in its response, the Ministry of Environment reassured Green Salvation that risk mitigation is outlined in the company plans; it says special risks such as those to the biodiversity in *Tulenyi* islands are negligible because dredging and other works will take place 80 kilometers away from the islands. The *Tulenyi* islands are located roughly halfway between the *Kurmangazy* field and Bautino port. Should the *Kurmangazy* oil fields prove to be productive, the vulnerability of these islands will increase, in addition to the risk already posed by increased shipping traffic and dredging.

The responses by the Ministry of Environment and company during public consultations address only the short-term benefits to communities and the short-term risks associated exclusively with the construction phase of the project. Even though the port will double as an emergency response base for possible oil spills and shipwrecks, the potential long-term adverse impacts of oil-linked traffic and risks of disasters near the Sartas port are not even mentioned by the company or state officials (*see Appendix 2*). Moreover, the response of the regional environmental ministry implying that certain national objectives trump environmental considerations when no win-win solution is at hand is an alarming indicator that sustainability considerations may be downplayed in future high-risk projects.

The controversy of IFI investments in sensitive oil and gas related projects is, on the one hand, a value the IFIs bring, given their requirement of more stringent safeguard standards. On the other hand, their contribution enables the building of even more risky projects. The combined investments of IFIs in Bautino, Sartas and potential investment in the future Kuryk port will allow Kazakhstan to meet its goal of a 1,000-strong oil and gas fleet—nearly triple the 2010 number.[49] Also, unlike other IFI investments, such as the World Bank's potential investment in Turkmenbashi port and IFI investments in the port of Baku in Azerbaijan, investments in Bautino and Sartas are designed exclusively to service oil extraction operations in the northern Caspian; these facilities could be framed as associated facilities of Kashagan, Tengiz and smaller oil extraction projects.[50] In fact, without the Kuryk, Bautino and Sartas Ports, oil extraction from the Kashagan oil field would not be possible.

The IFC support for the Sartas port is a very sensitive endeavor as it essentially supports one of the largest and exceptionally risky off-shore oil extraction operations in Central Asia. The manner in which the project was categorized and the open-ended delegation of subsequent EIA and mitigation measures to the client for a project of this scale and with such a potential impact is not in line with

[48] Response from the Mangistau regional branch of Ministry of Environment of Kazakhstan to public organization Green Salvation as of 28 March 2012. Available upon request.

[49] Butyrina, 2010. *Ibid.* 6

[50] Including concessions Жемчужина (Zhemchuzhina), Zhambyl, Zhambay, and block "H". The World Bank Group considers an investment as associated to the primary project when an associated facility cannot exist without and services primarily the primary project. In this case Kashagan is the primary project, supported by marine support bases Sartas and Bautino.

the precautionary approach the IFC should be taking in making investment decisions. Financing facilities that enable oil extraction in an environmentally fragile environment are not in line with the recommendations of the Extractive Industries Review. Public organizations may need to monitor the potential involvement of IFIs in the more risky Kuryk Port, intended to be the primary shipment terminal of Kashagan oil from the Eskene-Kuryk pipeline onto oil tankers at the Kuryk port (*see Appendix 3, a World Bank Map of Oil Transport Options in the Caspian Basin*). Moreover, by 2020 the planned terminal at Kuryk is estimated to be able to handle up to 20 million tons of cargo and oil—nearly as much as all ports of neighboring Turkmenistan combined (*see Appendix 4, Table of Projected Port Capacities in the Caspian Sea)*. The Kuryk Port will thus have the largest throughput on the eastern shore of the Caspian Sea located at the well-sheltered, ice-free bay of Bekovicha-Cherkaskogo.[51] One engineering company estimated that the pipeline for Kashagan and its oil terminal at the Kuryk Port will cost an estimated €2.5 billion ($3.2 billion), 70 percent of which will be borrowed.[52]

ADB PROJECTS

The Asian Development Bank (ADB) has made significant investments in the transport and energy sectors. The ADB has been a major financier of the road and rail links in Kazakhstan as part of the Central Asia Regional Economic Cooperation (CAREC) Program. The new Country Partnership Strategy for Kazakhstan adopted in August 2012 continues the emphasis on power generation and transmission, utilities and transport infrastructure.[53]

Of the various ADB-funded projects, one recent investment particularly highlights the ADB's contribution to the development of hydrocarbon resources of the Caspian region—a road reconstruction project in Mangistau province as part of CAREC Corridor 2. The ADB's involvement in the Caspian region can therefore be described as linking resource-rich regions to world markets over land transport corridors.

2010 CAREC Corridor 2

On December 20, 2010, the ADB Board of Directors approved a $283 million CAREC Corridor 2 project to reconstruct roads in Kazakhstan's Mangistau province. The project reconstructs road sections running from the port of Aktau to Munayshi, from Beineu to Akzhigit and from Zhetibay to Fetisovo.[54] The objective is to reduce congestion and travel time between the major oil and cargo port of Aktau and paved highways leading to Russia, Uzbekistan and Turkmenistan. The ADB investment rationale specifically refers to growing traffic due to increased construction and service work as new oil pipelines and other energy infrastructure are being built.

In helping upgrade Mangistau region's roads, the ADB is facilitating the industrialization of and growing energy trade in western Kazakhstan. According to the state-owned regional development corporation Caspiy, Mangistau oblast needs modern, paved roads for the region to position itself as an international transport hub linking Europe, Asia and Gulf countries. The ADB's investment also complements government efforts to build modern roads and a new railway link to the Kuryk Port.[55]

[51] Butyrina, 2010. Kuryk's annual loading capacity is planned to reach 20 million tons, larger than projected port capacity, according to the Panorama article citing the Ministry of Transportation. See also in Annex 4: *Projected Capacities and Estimated Loading of Caspian Ports between 2009 and 2018.*

[52] *Ibid.* 51.

[53] Asian Development Bank [ADB]. (2012, August). *Kazakhstan: Country Partnership Strategy (2012–2016).*

[54] ADB. (2012, June 8). *MFF Central Asia Regional Economic Cooperation Corridor 2 (Mangistau Oblast Sections) Investment Program—Project 1.*

[55] Note: Social and Business Corporations are state-owned companies that are tasked with the development of particular regions of Kazakhstan, including by investing in productive and social projects. (www.caspiy.kz/en/mangistau/transport)

INVESTMENTS IN TURKMENISTAN

Turkmenistan plans to increase its oil and gas exports and thus draw a larger share of international trade through its territory. With some of the largest natural gas reserves in the world and significant on- and off-shore oil reserves, Turkmenistan could easily supply gas and oil to Europe, China and points east. However, in order to assume a more prominent role in trans-Caspian trade, the country must invest in its own tanker fleet, new coastal infrastructure and vessel support services.[56] Countries in both Europe and Asia, eager for Turkmen energy, have encouraged IFIs to address transport bottlenecks, just as private investors and resource companies have been investing in oil and gas extraction both on land and on the Caspian seabed. Although IFIs were initially hesitant to invest in the Turkmen oil and gas industry, more recently the IFIs considered investments in transport and the hydrocarbon related projects.

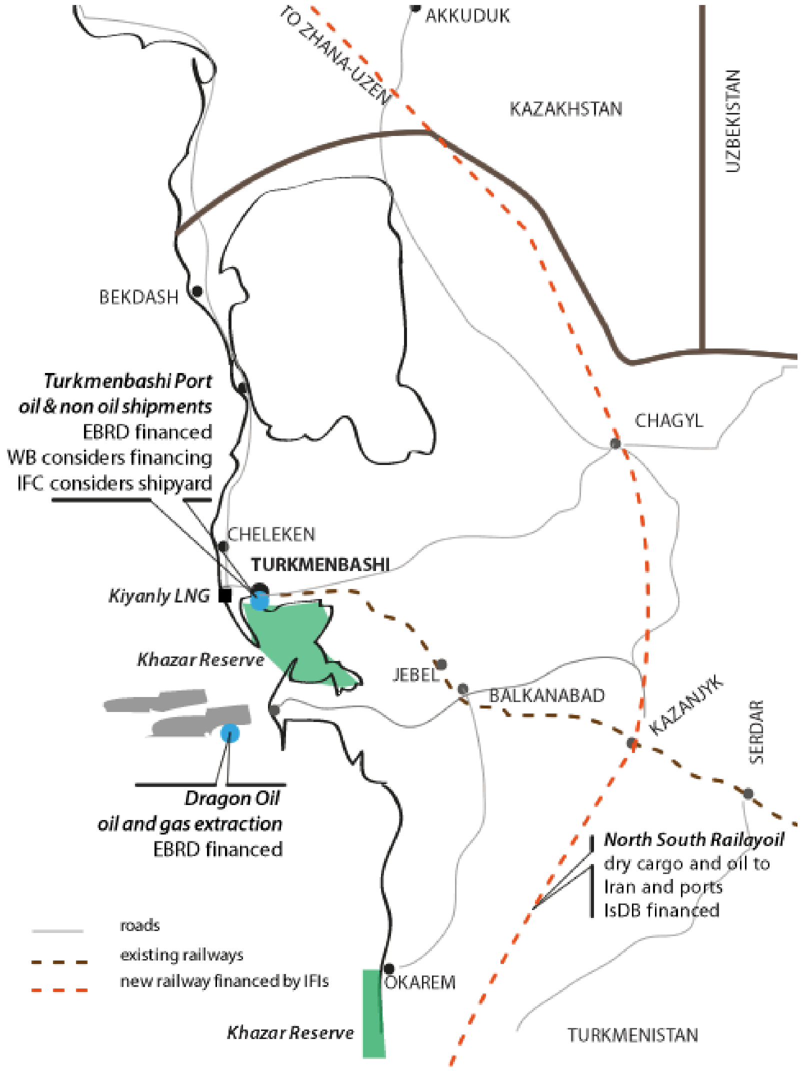


Figure 2: IFI investments in oil and gas and related transport infrastructure in Turkmenistan. EBRD investments are marked in blue, ADB financed infrastructure in orange.[58]

EBRD PROJECTS

2011 Turkmenbashi Shipyard

In early 2011, the EBRD considered supporting the construction of a shipyard in Turkmenbashi. The potential investment would allow the Turkmenistan State Service for Maritime and River Transport to construct a shipyard and a ship repair facility at the Turkmenbashi port. On November 21, 2011, the EBRD and Turkmenistan State Service for Maritime and River Transport signed a memorandum of understanding.[57]

The shipyard is meant to bolster Turkmenistan's own growing transport fleet as Turkmenbashi becomes a major Caspian shipment hub between Asia and Europe. The shipyard project is expected to be classified as a Category A investment,

[56] PortNews. (2010, December). Turkmenistan eyes moving oil exports via Russia. *PortNews*.

[57] The State Service of Maritime and River Transportation of Turkmenistan.

[58] Map based on sources from public sources: UNEP (http://www.grida.no/graphicslib/detail/00-protected-areas-03-new_98c7#) and Ministry of Transportation and Communication of the Republic of Kazakhstan, Organization for Security and Cooperation in Europe (2007, October 23). *Presentation on regional transport corridors*.

meaning it carries potentially significant social and environmental adverse impacts.'[59] As a result, in 2011 the EBRD allocated €180,000 for environmental and social impact assessments to ensure the shipyard complies with environmental and social standards.[60]

On February 16, 2011, a press release from the South Korean company Hyundai Amco announced that the company won a Turkmenistan government tender for the construction of the $130 million shipyard and repair facility at the Turkmenbashi port: Hyundai Amco will "execute repair facilities and berth facilities for ships, construction of residential complexes and dredging works for the harbor, with commencement in March and scheduled for completion in 2014."[61] At present, it is not clear whether the World Bank, IFC or EBRD will co-finance the project.

A partnership between Hyundai Amco and the EBRD is possible in theory, as Hyundai has also considered investing in the next phase of the Sartas marine base in Kazakhstan, potentially in cooperation with the IFC.[62] This is the third contract of this size awarded to the Hyundai Corporation by the Turkmen government. The other two major contracts included a massive $1.48 billion award to LG International and Hyundai Engineering for the construction of a natural gas purification plant in Turkmenistan's southeastern Yolotan province[63] and another LGI/Hyundai award for an oil refinery in Turkmenbashi.

1997 Turkmenbashi Port

In 1997, the EBRD issued a €30 million ($47 million) loan to rehabilitate the Turkmenbashi port by improving its cargo and ferry terminals. The project also invested in additional storage facilities and cargo handling equipment.[64] At that time, it was the EBRD's first investment in Turkmenistan's public sector.

1999 Dragon Oil

In 1999 EBRD issued a $75 million loan to Dragon Oil Ltd, a largely United Arab Emirates-owned exploration company, to develop the existing Zhdanov and Lam offshore oil fields in the Cheleken Contract Area of the Caspian. The EBRD loan financed structural works on off-shore platforms, seismic research and drilling, as well as developing a social and environmental management system. An environmentally sensitive project that carries and separates oil through sub-sea pipelines and by tankers, it was graded as a Category A investment.[65] Since the initial investment made by the EBRD, Dragon Oil average daily production has increased 8.5 times, from 7,000 barrels per day in 2000 to more than 60,000 today.[66]

According to the EBRD, it has avoided investments in Turkmenistan's oil and gas industry since the year 2000, due to the lack of transparency and off-budget nature of the management of extractive industry revenues accumulated in the Foreign Exchange Reserve Fund. While some progress toward more accountability has been made with the establishment of a stabilization fund under the auspices of the Ministry of Finance, the EBRD has not yet made major investments in oil and gas projects. The current EBRD Country Strategy for Turkmenistan stipulates that the EBRD may invest in oil and gas projects if progress towards accountability and transparency is made and projects will have significant transition impact and meet environmental and social standards.[67]

[59] DevEx.(2011). DevEx. Turkmenistan: Social and environmental expert with EBRD project. *DEVEX Website.*
[60] EBRD. (2011, April). *Memorandum to the Board of Directors*.
[61] Hyundai Amco. (2011, 16 February). HYUNDAI AMCO won an order for the Turkmenistan shipbuilding and repair complex. *Corporate news.*
[62] According to Sundikov, Chairman of the Board of Directors of the Sartas-Teniz Port, the company was in negotiations with investors like IFC, Hyundai Amco and Shinhan Investment Corporation. Minutes of public hearings organized by Sartas-Teniz Port, Aktau, August 20, 2011.
[63] Ho, C. (2012, May 24). Consortium of LGI and Hyundai E&C Won US$530 Million Contract. *Korea IT News*.
[64] EBRD. (1997, December 18). Turkmenistan Infrastructure Strengthened by Two-fold EBRD Financing.*News.*
[65] EBRD. (1999, December 14). *Project Summary: Dragon Oil.*
[66] Dragon Oil (n.d.), About Us. *Corporate Webpage.*
[67] EBRD. (23 March 2010). *Strategy for Turkmenistan.*

WORLD BANK PROJECTS

The World Bank has had a less than successful experience in Turkmenistan, where it has made few significant investments. Its mandate to fight poverty through support to the public sector in a closed, cautious and resource-rich state like Turkmenistan has not been met with much appreciation. Over the last 18 years, the World Bank has supported only nine significant projects, of which the last four have been dropped.[68]

2011 Turkmenbashi Port Improvement Project *(dropped at pipeline stage)*
The last project, the proposed reconstruction of the Turkmenbashi Port, remains in the pipeline even though the World Bank Board of Directors had planned to vote on the project in late January 2012.[69] The project has been delayed numerous times and was finally dropped, an indication of the World Bank's difficulties in operating in Turkmenistan. Moreover, the institution's efforts to develop a country strategy for Turkmenistan are still in the pipeline, with a date for the interim Country Strategy to go before the Board of Directors for a vote in early February. However, a definite board date has not been made public. Consequently, until a country strategy is developed, the question of whether the World Bank is able to finance projects in Turkmenistan will be on hold. Public consultation on the strategy is open until December 15, 2012. The World Bank published information about the interim country strategy on its website in July 2012.[70]

The World Bank's goal of financing the Turkmenbashi Port in order to make it Turkmenistan's largest logistics port is a move designed to facilitate greater trade turnover between Europe and Asia. International environmental civil society organizations, including Crude Accountability, have questioned whether the World Bank's bid to reconstruct the port is actually meant to facilitate the export of non-oil products. Indeed, by 2011 88.7 percent (€396 million) of Turkmenistan's exports to Europe were mineral fuels and related products.[71] When LG International/Hyundai completes construction of the new oil refinery in Turkmenbashi city in 2014, the port will likely serve as the primary export route for refined gasoline.

The port reconstruction and additional vessel traffic will further impact the already contaminated bay environment at Turkmenbashi. In addition, the World Bank project to develop the port is only the first stage of a larger plan to expand total port operations. Feasibility studies estimate that freight traffic will increase 10 percent per year, reaching 5.3 million tons per year by 2025.[72] The World Bank acknowledges that the long-term cumulative impact of increasing port capacity cannot be reliably estimated due to limited information about the port's future development strategy.[73] The World Bank detailed Environmental Impact Assessment (EIA) should also consider the potential impact the project will have on endemic and migratory bird species. The project territory borders the Hazar Nature Reserve, which was specially created to protect a major staging and wintering ground for migratory birds.[74] The

[68] List of World Bank projects in Turkmenistan, (http:/www.worldbank.org/tm)
[69] World Bank. (2011). *Turkmenistan—Turkmenbashi Port Improvement Project*.
[70] World Bank. (2012). *Turkmenistan—Notification of upcoming Strategy consultations*. Turkmenistan Country Webpage.

[71] European Commission. (2011). *Trade Statistics: Turkmenistan.*
[72] The European Union's TRACECA Programme for Central Asia. (December 2010). *International Logistics Centres/Nodes Network in Central Asia in the Republic of Kazakhstan, Kyrgyz Republic, Republic of Tajikistan, Republic of Uzbekistan and the Republic of Turkmenistan.*
[73] The Integrated Safeguards data states:
"The plan is of a general nature, though, without explicitly formulated priorities, implementation arrangements and financing sources. Therefore possibility of placing and analyzing the expected environmental risks of the proposed project in the context of cumulative impacts of the Port development is very restricted. This issue may be revisited at later stages of project preparation and during implementation as made possible upon refinement of the Port development plan".
The World Bank (updated, 2011, June 1). *The Integrated Safeguards Sheet.*
[74] Hundred of thousands of migratory birds winter at Hazar reserve each year, including five species of birds in the Red

expansion of freight traffic and increasing adverse impacts on sensitive wildlife habitats thus warrants a strategic environmental impact assessment, which has not yet occurred. Other concerns remain about the effectiveness of waste management. Expanded port operations will increase waste management requirements beyond those that are covered by the World Bank–funded reconstruction.

The EIA should also identify and take into consideration how logistics, warehousing and transportation infrastructure—a necessary investment to complement an increase in port capacity—would impact the environment. According to one particular design of a 12-hectare logistics center, land from Turkmenbashi Bay will be reclaimed—a move that would be detrimental to the environmental surroundings.[75] Furthermore, the second phase of the port development would involve building additional berths and widening access canals to allow for greater traffic. These associated facilities, subsequent civil works and greater traffic will ultimately increase the anthropogenic impact on bay waters, soil and sub-soil waters.

ADB PROJECTS

2011 North-South Railway Project

On July 20, 2011 the Asian Development Bank signed a $125 million agreement with Turkmenistan for the financing of a share of the costs of the 934 km North-South railway line (*see Appendix 4, Map of North-South Railroad*), connecting Uzen in Kazakhstan with Gorgan in Iran via Turkmenistan. The railway is a joint construction project of the governments of Kazakhstan, Turkmenistan and Iran with financial assistance from the Islamic Development Bank (IDB), the ADB and the government of Belarus.[76]

The ADB only equips the railway with signaling and communications, safety and maintenance systems and the electricity supply between the towns of Bereket and Buzhun in Turkmenistan. The ADB and Belarus jointly financed the power and telecommunications infrastructure between the border with Kazakhstan and Bereket, a station that connects the North-South line with the existing East-West railway running between Turkmenbashi and Ashgabat. The railway section from Bereket south towards the Iranian town of Gorgan will be financed with the assistance of the Islamic Development Bank.

When complete, the North-South railway will connect the transport systems of Russia, Kazakhstan and Turkmenistan to Iran, and on to India. It will also facilitate the shipment of oil products, agricultural products and other bulk goods to Persian Gulf ports.[77] The engineering review journal *ENR* reports that the line will ultimately shorten the total distance Kazakh and Turkmen exports need to travel to Iranian ports by 600 km and will help carry Kazakh and Turkmen oil, Turkmen cotton and grain to the Persian Gulf and on to world markets. The railway is, therefore, a critical link of the CAREC-supported North-South Trade Corridor, which is designed to reach an annual freight traffic capacity of 12 to 13 million tons of bulk cargo.[78] The Kazakh and Turkmen sections of the railway are already complete; the 70-km section of railway in Iran is expected to be completed by the end of 2012.[79]

Environmental and social assessments of the railway section funded by the ADB have identified little negative impact due to the location of the

Book. The area south of Turkmenbashi bay is habitat for flamingos, sturgeon and the Caspian Seal. For more information on threats to the Hazar Nature reserve, including from oil and gas projects, refer to the 2006 GEF report on Hazar reserve management.
and
Global Environment Facility. (2006). *Correspondence with UNDP.*

[75] The European Union's TRACECA Programme for Central Asia, (2010, December).

[76] ADB (2011). Environmental Assessment Report. *Turkmenistan: Proposed North-South Railway Project*.

[77] ADB (2011). North-South Railway Project. *Project Information Document*.

[78] Lewis, S. (2011, September 28). Central Asian Rail Link Will Redirect Export Paths. *Engineering News Record*.

[79] Universal Newswires. (2012, May 16). Central Asian-Iran rail developers form tripartite committee. *Kazakhstan Newswire*.

project in a very sparsely populated, mostly desert area. Nevertheless, as freight traffic increases, the railway's power lines may affect rare bird species in the Tekejik–Biynekyr area, or an oil spill could contaminate rare lakes along a few stretches of the new railway.[80]

However, despite the ADB's initial environmental assessment, no comprehensive environmental and social assessment has been completed for the entire railway project. Moreover, assessments of the potential social and environmental impacts of the southern sections of the railway, outside of the ADB's remit, may not have been conducted in accordance with established best practices and may therefore ignore potential serious issues.

The Turkmenistan-Afghanistan-Pakistan-India Gas Pipeline (TAPI), *(potential ADB investment)*

On May 23, 2012, the Indian national gas company GAIL, TurkmenGaz, and Pakistan's private Inter State Gas System signed a long-awaited Gas Sale and Purchase Agreement, which stipulates that Turkmenistan will supply India and, to a lesser extent Pakistan and Afghanistan, with 90 million cubic meters of gas per day.[81] Although the pipeline has yet to be financed and still needs investors, the agreement is a landmark event for the Asian Development Bank, which has been promoting the TAPI project through tumultuous negotiations and continuing instability in Afghanistan. With the Gas Sale and Purchase Agreement signed and approved by all parties involved, it is likely that the Asian Development Bank will continue the lead in mustering up international investors to build the 1,118 mile–long gas pipeline.

IDB PROJECTS

The Islamic Development Bank (IDB), a relatively young IFI, has made few investments in Central Asia and the Caspian region. The IDB is governed by rules and an investment philosophy that differ from other IFIs in that it complies with *shari'a* law. Compliance with *shari'a* law principally means that the bank: 1) is prohibited from earning *interest* from loans and sales and other financial transactions, and thus does not provide traditional loans, nor does it borrow from international markets; 2) invests only within its own member countries, and for the benefit of the *umma* (Islamic nations); in non-member states it supports only education and capacity building efforts; and 3) it shares investment risks and profits equally with clients. In this way, the IDB's investments are more akin to equity investments than loans.

The IDB's adherence to *shari'a* law principles may reduce the economic risks and long-term debt burden for its clients, as risks are more equally shared between the investor and the client. On the other hand, IDB's shareholders and limited geographic scope have shielded the institution from the political decisions and activist advocacy that have created and shaped the safeguard standards, accountability and transparency standards in other IFIs. The IDB has a policy and set of guidelines on anti-corruption and debarment, but it does not feature access to information and accountability policies such as grievance mechanisms for affected communities. The IDB does not have social and environmental policies.[82]

The IDB's current investment priorities fall into three categories: energy and transport; private sector development; and human development, which broadly includes investments in the health and education sectors.[83] In the Caspian region, the IDB invests primarily in Azerbaijan, Iran, Kazakhstan and Turkmenistan, often in partnership with other IFIs like the Asian Development Bank.

2010 North-South Railway Project (Bereket–Gorgan section)

Under the agreement between the IDB and Turkmenistan, the IDB invested $371 million for

[80] *Ibid. 77*

[81] Asian Development Bank. (2012, May 23). *Historic Agreements Bring Long-Awaited TAPI Pipeline Closer to Reality.*

[82] Islamic Development Bank. (2012). *37th Annual Report.* Islamic Development Bank.

[83] *Ibid.*

the construction of the final, 257-km section of the railway from Bereket in eastern Turkmenistan to the Iranian border and further on to the Iranian city of Gorgan.[84] The southern section of the railway passes through more populated areas adjacent to the Turkmen-Iranian border.

The IDB's focus on energy and energy transport services, which account for 25 percent of current disbursements, closely aligns its investment objectives with priorities of the ADB. As a result, the two banks have cooperated in financing different sections of the North-South Railway. However, since the two banks could not co-finance the same project due to fundamental differences in approach and structure, each had to conclude separate agreements with Turkmenistan. The IDB's investment principles are incompatible with debt financing. It also lacks the necessary social and environmental policies to meet the same level as ADB standards. Meanwhile, the ADB's European and North American shareholders would likely object to the bank's funding of a railway into Iran, construction of which would likely be executed by an Iranian contractor. Consequently, the IDB and ADB divided the railway into separately funded sections so both banks could participate in the project.

REGIONAL DEVELOPMENTS

Success in the sphere of economic development in the Caspian Basin has not been matched by success in the arena of political cooperation. The five littoral states cannot agree on the border delimitation of the Caspian. This disagreement is based on the Iranian demand for 20 percent of the sea or a joint ownership of the Caspian resources, while other states insist on border delimitation based solely on the coastline.[85] Due to the lack of an agreement, any large trans-boundary construction is problematic, as is evident in Russian and Iranian opposition to construction of the Trans-Caspian Gas Pipeline, which would transport Central Asian gas to Europe. The unresolved delimitation dispute grows particularly thorny as exploration reaches disputed territories.

Tensions have flared up between Azerbaijan and Iran on exploration in the Caspian along the disputed border. In addition, Turkmenistan and Azerbaijan dispute the ownership of the Kapaz/Serdar oilfield that straddles the maritime border of the two states. A new oil discovery by Iran in May 2012, its first in over a century,[86] could further complicate relations with Azerbaijan. Analysts suspect the discovered oil is located in a disputed area. [87,88]

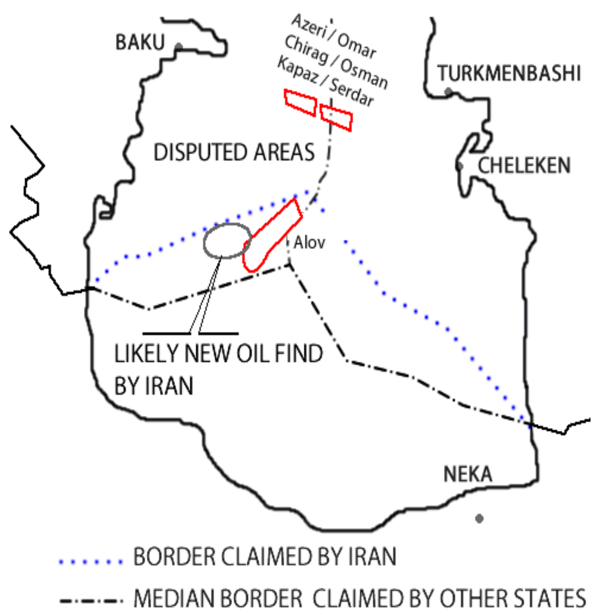


Figure 3: Disputed borders and oil fields among Azerbaijan, Turkmenistan & Iran[85,87,88]

[84] *Ibid.* 83.

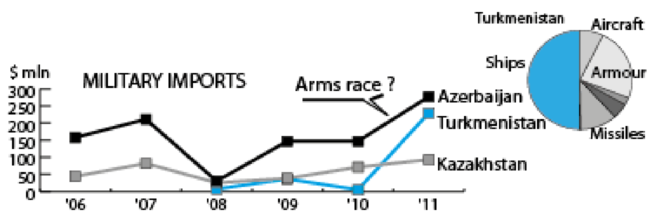
[85] O'Neil et al. (2011). *National Security and Caspian Basin Hydrocarbons.* International Association for Energy Economics.

[86] Daya, L. N. (2012, May 20). Iran Finds Its First Caspian Sea Oil for More Than a Century. *Bloomberg*.

[87] Texas at Austin. (n.d.). *Map: Southern Caspian Energy Prospects.*
Map based on the publicly available maps of the Caspian Sea provided by the University of Texas at Austin.

[88] Kucera, J. (2012, June 19). *Iran's New Oil Discovery May Be In Azerbaijan's Waters.*

Exacerbating the tension surrounding the Caspian border delimitation, Azerbaijan, Kazakhstan and Turkmenistan have been building up their navies. In May 2012 Azerbaijan, followed by Turkmenistan in August, held military exercises on the Caspian Sea, both of which were designed to exercise response in defense against a hypothetical aggressor state, instead of against terrorist outfits as is customarily presented.[89]



Source: SIPRI Arms Exports Database www.sipri.org/databases/armstransfers

Figure 4: Military imports among Caspian states growing since 2008[90]

Despite such political uncertainties, the hydrocarbon exporters and IFIs continue to expand trade routes around the Caspian via road and rail projects and to prepare coastal facilities (shipyards, terminals and ports, vessels) in order to take advantage of the upcoming hydrocarbon export boom. As IFIs help set the stage for large-scale oil and gas development in the Caspian, they may also inadvertently be contributing to the intensifying resource race, one that could revive unsettled disagreements.

Moreover, the quality of public governance in the Caspian states remains a concern. Turkmenistan continues to amass its hydrocarbon revenues in non-transparent wealth structures narrowly controlled by the country's top leadership.[91]

In neighboring Kazakhstan, despite early adoption of the Extractive Industry Transparency Initiative (EITI),[92] most of its economy, including the oil and gas sector, is managed through the Samruk Kazyna sovereign wealth fund, which until December 2011, was headed by the President's son-in-law, Timur Kulibayev.[93]

On December 16, 2011, the regional oil town of Zhanaozen descended into a state of chaos as police resorted to arms to quell oil workers and citizens whose protests turned into a riot.[94,95] The violence in Zhanaozen followed a seven-month-long strike at state-owned UzenMunaiGaz for wages, which resulted in a government crackdown that persecuted organizers, fired hundreds for taking part in the strikes, and sentenced lawyers who aided the striking workers.[96] The Kazakhstan government's poor handling of the strike—whose escalation into violence claimed at least a dozen lives—is indicative of Kazakhstan's inability to govern responsibly and manage wealth equitably. The manner in which such irresponsible companies as UzenMunaiGaz managed labor union demands underscores a distinct lack of accountability in state-controlled resource companies. IFI projects that invest in hydrocarbon-associated facilities are likely further empowering such irresponsible companies.

These investments undermine IFI commitments made following the Extractive Industry Review,[97]

[89] Valiyev, A. (2012, May 17). *Azerbaijan's Military Exercises in the Caspian: Who Is the Target?*

[90] Stockholm International Peace Research Institute (2012). Arms Imports Database 2005 to 2011 for Turkmenistan, Kazakhstan and Azerbaijan.

[91] Such wealth structures include the State Agency for the Management and Use of Hydrocarbon Resources, a quasi-sovereign wealth fund. Crude Accountability. (October 2011). *The Private Pocket of the President (Berdymukhamedov): Oil, Gas and the Law.*

[92] The Extractive Industry Transparency Initiative is a policy of public, audited verification of mineral and hydrocarbon revenue flows between developers and the public, as well as between national and subnational governments. EITI aims to reduce corruption but is limited to part of the extractive value chain.

[93] Øverland, K. F. (August 2012). Energy Elites in Central Asia: Kazakhstan, Turkmenistan and Uzbekistan. *RussCasp Working Paper.*

[94] Lillis, J. (2011, December 17). *Kazakhstan: State of Emergency Introduced in Troubled Oil Town.*

[95] Gorst, I. (2011, December 17). *State of emergency after Kazakhstan clashes.*

[96] Human Rights Watch. (2011, December 17). Kazakhstan: Investigate Violence in Oil-Rich Western Region.

[97] The Extractive Industry Review (EIR) evaluated the impact of the World Bank Group–financed extractive projects and suggested measures to mitigate such projects' negative impacts. The changes following the review affected other IFIs through common policies and practices.

which produced broad guidelines that the World Bank Group and regional banks have agreed to follow. The Review stipulated supporting extractive projects on the following preconditions:

1. Transparency of resource revenues;
2. Credible commitment to improve governance and pursuit of poverty-reduction goals;
3. Respect for "no-go" zones, or environmentally and socially vulnerable areas;
4. Absence of conflict or high *risk* of conflict;

However, investments made in the Caspian region appear to test and even violate some of these preconditions. Kazakhstan has made very little progress towards improved governance, and its reputation has been further tarnished by the Zhanaozen events. Similarly, Turkmenistan remains one of the most authoritarian regimes in the world, ranking third from the bottom on the Economist Intelligence Unit's Democracy Index.[98]

Despite the lack of agreement among the Caspian states on border delimitation, they came closer to concord on environmental matters. In 2011, the five littoral states signed the important Protocol Concerning Regional Preparedness, Response and Co-Operation in Combating Oil Pollution Incidents. The protocol, one of four envisaged protocols of the Tehran Convention, will legally oblige all states to develop measures to prevent and jointly respond to environmental emergencies such as oil spills.[99]

This is an area where IFIs could be more active in the environmental sphere. In October 2011, the EBRD entered into a memorandum of understanding with Kazakhstan to cooperate on oil spill prevention and emergency response mechanisms,[100] although the EBRD has yet to finance a dedicated project. The World Bank and IFC have included provisions to address oil spill risks; for example, they upheld a zero-discharge policy from sea ships within projects they finance.[101] Nevertheless, compared to the scale of IFI investments in facilitating hydrocarbon development and trade, IFI assistance to Kazakhstan in addressing oil spills has been inadequate in comparison to risks posed by the petroleum-related projects that IFIs have enabled thus far. In Turkmenistan, not only environmental projects, but even more traditional projects were modest in comparison with a single potential investment in the Turkmenbashi port and shipyard. For instance, since 2005 EBRD's investment in Turkmen SMEs totaled only around $16 million—a small share of the typical cost of a hydrocarbon-related project in the region.[102] Current financing of infrastructure projects by IFIs appears to have paved the way for even more substantial and environmentally sensitive projects, such as the construction of the Trans-Caspian gas pipeline, or development of future oil fields such as *Kurmangazy* and *Nursultan*.

CONCLUSION

Investments made by IFIs such as the World Bank, IFC, EBRD, ADB and IDB in the Caspian region enable Kazakhstan's and Turkmenistan's drive to export hydrocarbon resources. Their investments also fulfill the European Union's strategic interests to secure energy and trade corridors. Finally, IFI support for infrastructure development follows the

For a brief review of EIR and impact on the Bank, see: (www.halifaxinitiative.org/updir/IssueBrief-EIR.pdf).
For commitments of the Bank in response to the Review, see: (http://siteresources.worldbank.org/INTOGMC/Resources/eirchairmanssummary.pdf).

[98] Economist Intelligence Unit. (2011). Democracy index 2011: Democracy under stress. *Economist Intelligence Unit.*

[99] Tehran Convention Website. (2011, August 12). The Protocol Concerning Regional Preparedness, Response and Co-operation in Combating Oil Pollution Incidents. *The Tehran Convention.*

[100] EBRD. (2011, October 5). EBRD and Kazakhstan Support Emergency Response for Oil and Gas Operations, *EBRD Press release*.

[101] World Bank (2011). *Turkmenbashi Port*. World Bank. "… the acquisition of oil spill response equipment, response vessel and waste water collection vessel as well as consultants' services to achieve International Ship and Port Security certification."

[102] List of EBRD financed projects in Turkmenistan available at the EBRD *Projects* website. www.ebrd.com/saf/search.html?type=article&country=Turkmenistan

broader CAREC program that aims to integrate markets on all sides of Central Asia.

IFI projects with the potential to be socially and environmentally sensitive include the third phase of the Sartas port development, the development of the Eskene-Kuryk pipeline carrying Kashagan oil, and the Kuryk port and oil terminal. Once these facilities are completed in 2016, they will play a critical role in larger projects, like the Trans-Caspian pipeline.

IFIs will likely continue to support clients in which they have previously invested. Therefore, additional investments in Bautino, Sartas, Turkmenbashi and Kuryk are possible in the future. The ports of Sartas and Bautino may have been strategically placed to service the Kurmangazy oil field, estimated as the third largest field in the Caspian Sea.

In Turkmenistan, construction of the east-west pipeline to carry gas from the South Yolotan natural gas field, as well as the early feasibility studies for the TAPI pipeline, warrant attention from environmental and rights activists. The upcoming ADB country strategy may offer an opportunity to raise sustainability issues.

However, it is unclear why IFIs are helping mineral resource countries finance extraction and export of mineral resources. Unlike other developing Central Asian countries, hydrocarbon-rich Turkmenistan and Kazakhstan do not heavily depend on IFI assistance to finance their infrastructure projects. Consequently, IFIs have tenuous justification for investing in Caspian oil-related infrastructure (ports, industry, and fleet support bases). So far oil and gas companies have been able to independently invest in their own supply and service bases. Also, national governments appear capable of spending their own funds and attracting transnational corporate giants like LG and Hyundai to invest in multi-million dollar oil and gas projects. National governments, far from being dependent on IFI financing, draw on their own considerable hydrocarbon revenues to finance ports, and industrial and logistics hubs—even entire coastal cities on the Caspian.

Nor have the governments demonstrated responsiveness and accountability. As is evident from the development of the Karachaganak Oil and Gas Condensate Field and the Sartas Port, the state is willing to bend rules to realize its economic plans quickly (e.g., reclaiming real estate from protected areas). Public hearings for the Turkmenbashi Port, Atash marine base and Sartas Port demonstrate how public consultations serve only to justify already planned projects, and residents may be disappointed and left without recourse if project sponsors do not deliver on their promises. IFI participation in such projects does not always make a substantial difference if host governments do not cooperate.

IFIs were instrumental in the build-up of the infrastructure and trade routes that make full-scale development of the Caspian resources feasible. By financing the construction of roads, ports and rail systems, the IFIs have enabled transport of Caspian oil and gas to Europe and Asia. The unprecedented scale of oil extraction will come with very high risks of oil pollution and threats to endangered biological species, not to mention the risk of confrontation over resource disputes. Moreover, by strengthening the state-controlled hydrocarbon sector and related industries, IFIs have further concentrated economic and political power in the hands of authoritarian elites. Since it is known that amassed and unaccountable power rarely leads to inclusive economic development and democratic societies, IFIs may ultimately be undermining their own chief missions of reducing poverty and encouraging transition in Central Asia.

RECOMMENDATIONS FOR INTERNATIONAL FINANCIAL INSTITUTIONS

Abstain from state-controlled resource projects

IFIs should abstain from investments in state-controlled resource-related projects in the Caspian Sea, considering the outstanding governance issues: elite-capture, poor transparency, and political tensions linked to resource extraction. IFIs should reassess their role in the Caspian basin against their original missions and aim to diversify the target economies away from resource-dependency.

IFIs should equally abstain from projects related to or endorsing development of disputed resources.

Moving forward, each institution's next country strategies should be firmly grounded in an external assessment of the institution's poverty reduction and transition impacts.

Institute human rights risks assessments

Second, in light of the Zhanaozen events, IFIs should place human rights at the forefront of their engagement with state and private sector clients. Demanding compliance with the Voluntary Principles on Security and Human Rights could be a starting point for such an engagement.

Further, EBRD should consider instituting proactive governance and human rights risk assessments before the Bank commits financing for a project. EBRD's Project Complaint Mechanism could be given the mandate to evaluate risks of human rights violations and advise on ways to address systemic risks in a manner similar to the role of IFC's Compliance Advisor Ombudsman.

IFIs would benefit from establishing close working relations with Kazakhstan's ombudsman office and encouraging Turkmenistan to produce a true institution of an Ombudsman.

Avoid sensitive areas and scale up disaster preparedness assistance

Projects that bear long-term risks to protected areas should be avoided altogether as IFIs have no leverage to assure themselves of sound project management practices post-project completion. To balance growing risks of pollution in the Caspian Sea region, IFIs should increase their assistance to governments to build human and technical capacity in environmental stewardship and disaster risk reduction.

Adopt safeguard policies and procedures at the Islamic Development Bank

The Islamic Development Bank should urgently adopt environmental and social safeguard policies, improve access to information and establish a project grievance mechanism to meet the standards of a modern development-oriented institution. IDB's lack of safeguard policies lends additional reason for concern in countries where other redress avenues are limited.

In fact, the Islamic Development Bank stands to gain from adopting governance and safeguard policies because its more equitable risk-sharing philosophy exposes the bank to substantial liabilities.

RECOMMENDATIONS FOR CIVIL SOCIETY ORGANIZATIONS

Take initiative at approval processes

Remaining suspicious of the state's consultative and approval functions, civil society organizations should consider organizing their own public hearings, extending invitations to project sponsors and investors.

Public interest organizations would benefit from proactive engagement with the Islamic Development Bank to encourage it to adopt modern safeguard policies and procedures.

Team up with larger allies

Local public interest groups often operate in silos, which diminishes their reach and impact. Certain intergovernmental organizations, like the UN, share similar concerns with independent groups. Striking closer partnerships with larger institutions in advocacy and fact-finding can boost the voice of local advocates.

APPENDICES

Appendix 1: UNEP Map of Protected Areas in the Caspian Sea Basin

Source: UNEP GRID-Arendal, *Vital Caspian Graphics 2: Opportunities, Aspirations and Challenges, 2012*, available at www.grida.no/graphicslib/detail/00-protected-areas-03-new_98c7#

Appendix 2: Summary of Public Consultations on Sartas-Teniz Port, August 2011

Concerns raised by public	**State/Company responses to public concerns**	**Remarks about key points**
Dredging and civil works	No resettlement will be needed. A new settlement will be built for workers.	
Long-term environmental impacts	Only limited and localized impacts from dredging and civil engineering works is expected and will be mitigated. The project will include ship water and waste treatment, and impacts from waste processing can be predictably managed.	This response/approach to risk management omits or downplays environmental and social risks that accumulate over the years like sea traffic or on-shore pollution sources. Nor does such a vision account for unpredictable risks, e.g., from oil spills and their impact beyond the immediate project site, like impacts on Buzachi Reserve nearby. IFC's assignment of environment categorization "B" for this project does not adequately reflect all risks such an investment would lead to.
State priorities and company interest seem to have been able to circumvent environmental safeguards in the past.		This fact suggests that extra care in IFC due diligence and application of its own standards are warranted.
Local jobs and benefit sharing	Company entered into MOU with Taushyk village to start hiring local labor. A benefit sharing scheme, like assistance in residential homebuilding, will be put in place.	IFC should verify that local residents in fact have job opportunities. IFC should promote the practice of binding agreements among the company, state, and community on benefit sharing schemes.
Emergency response: consultations only deal with the current phase of the works (housing, warehouses). The company didn't address threats of fuel handling as the Sartas takes on the refueling/fuel storage role for ships in the subsequent phases.[103]	Mentioned future oil spill response capabilities of port and the fleet.	IFC should ensure that not only emergency response plans but also *capacities* are in place before waste and refueling operations can commence.
Has IFC assured itself of broad community support as its policy prescribes? Does this support reflect only the risks and benefits of the first phase of the project?		It is imperative that IFC ensure broad community support for the extension of next phases of the project, which pose risks to health and environment.

[103] Fuel storage, a waste processing plant, a reinforced concrete plant and other plants are planned beginning from 2013–2014. Butyrina, 2010.

Appendix 3: Oil Transport Options—Estimated Flow Capacities for 2015

Source: *Caucasus Transport Corridor for Oil and Oil Products*, World Bank, December 2008.
http://siteresources.worldbank.org/EXTRAILWAYS/Resources/CaucasusTransportCorridorDec08.pdf

Appendix 4: Projected Capacities and Estimated Loading of Caspian Ports Between 2009 and 2018

Ports	2009		2012		2018	
	capacity	factual load	capacity	factual load	capacity	factual load
Kazakhstan	**16,5**	**13,3**	**18,8**	**18**	**41,7**	
Aktau	14	11,4	15,8	15,5	15,7	11
Oil only	11,5	9,2	12,9	2,5	2,9	6
Kuryk	-	-	-	-	23	*20*
Bautino	2,5	1,9		3	2,5	3
Russian	**17**	**10,37**	**37**	**23,**	**37**	**27**
Astrakhan	6	5,2	7	7	7	7
Makhachkala	10	-	15	-	15	10
Olya	1	0,17	15	8,2	15	10
Turkmenistan	**10,6**	**5**	**18,4**	**17**	**21**	**20,5**
Turk-bashi	7	5		9	8,5	9
Alaja	2,4	-	5,9	5,5	7	6,5
Okarem	1,2	-	3,5	3	5	5
Azerbaijan	**34**	**6,8**	**42**	**34**	**42**	**39**
Baku	8	5,3	10	7,3	10	9
Dubendy	-	-	12	1,5	12	6,7
Sangachaly	-	-	10	-20	20	20
Iran	**17**	**13,2**	**32**	**26,5**	**46**	**38**
Amirabad	5	2	8	8	20	17
Anzali	5	5	7	7	9	9
Nowshahr	1,5	1,2	2	2	2	2
Neka	?	5,5	5	15	9,5	15

Source: Kassym TLEPOV Head of Water Transport Unit, Ministry of Transport and Communications interview with Panorama Kazakhstani newspaper. Text available at http://panorama.kz/index.php?option=com_content&task=view&id=9727

Appendix 5: Map of North-South railroad, Uzen (Kazakhstan) – Bereket (Turkmenistan) – Gorgan (Iran)

Source: Kazlogistics, Official Integrated Logistics Portal. Original map is in Russian.
www.kazlogistics.kz/en/zd/map

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