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Tim Burr
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151 Buckingham Palace Road,
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26 August 2008

Dear Mr Burr,

Regional Conflict and BTC Pipeline: Concerns over ECGD's due diligence and risks to the UK tax payer

In light of the National Audit Office's recent report on the "Export Credits Guarantee Department and Sustainability",¹ we are writing to express our grave disquiet over the recent resurgence of conflict in Turkey and in Georgia and its implications for the ECGD-backed Baku-Tbilisi-Ceyhan (BTC) oil pipeline. Although our primary concern is with the impacts of such conflict on the human rights and environment of those living along the pipeline – and their rights to redress from damage already inflicted – we believe that ECGD's support for the project has contributed to the general destabilisation of the region, not only placing considerable sums of public money at risk² but also raising serious concerns over the quality of ECGD's due diligence.

1. National Audit Committee, "ECGD and Sustainability", Briefing prepared for Environmental Audit Committee, June 2008, http://www.nao.org.uk/publications/0708_ECGD_and_sustainability.pdf.

2. The total sum at risk may be as high as \$292 million. In December 2003, ECGD approved a line of credit for the project of \$150 million (£81,703,893). However, documents released to Friends of the Earth (England, Wales and Northern Ireland) under the Freedom of Information Act indicate that additional \$300 million in support was requested for the project in the form of Overseas Investment Insurance (OII), to be co-financed with Japan's NEXI. Two figures are mentioned: \$300 million and \$500 million. ECGD does not disclose individual OII guarantees. However, if ECGD agreed to split the OII request with NEXI, then an additional \$150-\$250 million would be at risk. See: ECGD, Note of Decision: The Baku-Tbilisi-Ceyhan oil pipeline, 17 December 2003, http://www.ecgd.gov.uk/btc_-_note_of_decision-2.doc; ECGD, List of Guarantees 2003-04, http://www.ecgd.gov.uk/index/pi_home/pi_lgi/pi_lg2004.htm; ECGD, Briefing prepared for HM Treasury, "Baku-Tbilisi-Ceyhan Pipeline", 2 May 2003, p.5, 14 and 25, released by Department of Trade and Industry to Friend of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act.

Both before and after ECGD's decision to fund the BTC oil pipeline in December 2003, national and international non-government organisations (NGOs) repeatedly warned ECGD and other funders of the high risks posed to the project by conflicts in the region – and the strong possibility that the project itself would exacerbate such conflicts.³ NGOs also specifically drew ECGD's attention to statements by the Partiya Karkeren Kurdistan (Kurdish Workers Party or PKK) that the pipeline would be a target for military action by its forces in response to continued repression of Turkey's Kurdish minority by the Turkish State.⁴ Documents released in response to Freedom of Information requests cast severe doubt on the extent to which such risks were adequately assessed by ECGD or by the government departments on which it relied for advice. On the contrary, the risk that Russia in particular might view the pipeline as an incitement does not seem to have been addressed in any depth.

We believe there is an urgent need to reassure the public that the risks of conflict were adequately assessed prior to support for the BTC project being approved and that taxpayers' money was not put at unjustified risk. **We are therefore writing to brief you on the background to our concerns and to request that the National Audit Office undertake an investigation of ECGD to assess the quality of its due diligence for the project and to determine whether the premiums charged by ECGD for the guarantees it supported adequately protect the taxpayer.**

Recent Events

As you will no doubt be aware from recent news reports, the threats of regional conflict that the NGO community sought to bring to the ECGD's attention have now materialised, with tragic consequences:

- ***PKK Attack on Pipeline***

Last week, a major explosion ruptured the pipeline near Yurtbashi village in Turkey's eastern Erzincan province. The explosion, which occurred around 11pm on the night of August 5, caused a fire that sent flames up to 160 feet high shooting into the air.⁵ The fire was not extinguished until 11 August, by which time an estimated 12,000 barrels of oil had been burned off,⁶ spreading a dangerous cocktail of carcinogens and other health-threatening pollutants over a considerable distance.⁷ BP has said it cannot set a time for the repairs to the pipeline to be completed,⁸ although initial reports

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3. See, for example: NGO Letter and Proposals to IFIs, June 2002, Section 6 – Military Conflicts in the Region and new Militarisation in the Pipeline Corridor; “Memorandum from Concerned NGOs to DfID, FCO, UK Treasury, ECGD”, Section 9 – Pipeline Security, Human Rights, Conflict and Militarisation of the Region”, http://www.baku.org.uk/correspondence/DfID_memo_feb_2003.pdf; The Corner House et al, Review of BTC Environmental Impact Assessment, Section 3.3.2 – Absence of Analysis of Kurdish Situation in EIA, October 2003; Platform et al, Some Common Concerns, pp115-121 (A Region of Simmering Conflicts), <http://www.baku.org.uk/publications/concerns.pdf>; International Fact Finding Mission, BTC Pipeline – Turkey Section, Section 1.5 – Pipeline Security and the Gendarmerie, June 2003, http://www.baku.org.uk/publications/Tu_FFM.pdf; NGO letter to IFC Executive Directors, “BTC Pipeline Board Meeting”, 29 October 2003, http://www.baku.org.uk/correspondence/EDs_re_Board_report.pdf; The Corner House et al, Letter to Jeanette Swindon ECGD, “BTC Pipeline”, 10 November 2003, <http://www.baku.org.uk/correspondence/ECGDletter.doc>.
 4. See: Email from Nicholas Hildyard to David Allwood, “End of PKK ceasefire”, 3 June 2004; NGO letter to IFC Executive Directors, “BTC Pipeline Board Meeting”, 29 October 2003, http://www.baku.org.uk/correspondence/EDs_re_Board_report.pdf;
 5. Energy Tech, “Analysis: BTC pipeline explosion”, http://www.energy-daily.com/reports/Analysis_BTC_pipeline_explosion_999.html.
 6. “12,000 Barrels of Crude Oil Burn in BTC Explosion”, 6 August 2008, <http://capital.trendaz.com/index.shtml?show=news&newsid=1263902&lang=EN>.
 7. Pollutants including PM-10 particulates and polynuclear aromatic hydrocarbons will have contaminated an area reaching at least 500m from the fire. <http://www.fire.nist.gov/bfrlpubs/fire03/PDF/f03158.pdf>
 8. International Herald Tribune, “BP reopens Georgia gas pipeline”, 14 August 2008, <http://www.iht.com/articles/ap/2008/08/14/business/EU-Britain-Georgia-Pipeline.php>.

suggested that it would be repaired within two weeks.^{9 10} In the meantime, Turkey's state pipeline company, BOTAS, is carrying out an investigation into the explosion,¹¹ which is costing Turkey \$300,000 a day in lost transit fees.¹²

Following the explosion, the State Oil Company of Azerbaijan declared *Force Majeure* on its exports of Azeri crude, allowing the company to break its contractual agreements to supply oil.¹³ Although BP was initially reported to have done the same, the company later denied these reports.¹⁴ Nonetheless, reports to the contrary persist.¹⁵

Local government officials initially placed the blame for the explosion on a technical fault (all too credible in the light of well-documented evidence of poor quality welding¹⁶ and concerns over the pipeline coating¹⁷) but have since accepted that the fire was caused by sabotage.¹⁸ The Kurdistan Workers Party (PKK) has claimed responsibility for the explosion.¹⁹ The group has said that it will take further action,²⁰ including threats to attack tankers using BTC's terminal at Ceyhan on the Mediterranean.²¹ Separatist groups in South Ossetia²² and Abkhazia²³ have also made threats to the pipeline.

Commentators have stressed that the PKK attack means that the BTC pipeline has effectively "become a new front line in the nearly 30-year war between the PKK and Ankara."²⁴ The fear is that the local Kurdish population will now suffer from increased militarisation of the pipeline and "a military crackdown the likes of which the Kurds

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9. Carlisle, T., "Caspian oil exports under twin threat", *The National*, 10 August 2008, <http://www.thenational.ae/article/20080810/BUSINESS/884886899/0/FRONTPAGE>.
 10. Eric Watkins, "Socar declares Force Majeure on Azeri oil exports", *Oil and Gas Journal*, 6 August 2008, http://www.ogj.com/articles/article_display.cfm?ARTICLE_ID=336370.
 11. "Fire-hit Azeri-Turkish oil pipeline to remain close for 1-2 weeks", *Zaman*, <http://www.todayszaman.com/tz-web/detaylar.do?load=detay&link=149612&bolu=105>; "BTC Damage Study May Take a Week – BP", *Downstream Today*, 13 August 2008, http://www.downstreamtoday.com/News/Articles/200808/BTC_Damage_Study_May_Take_A_Week_BP_12350.aspx.
 12. "Turkey loses \$300,000 a day on BTC, exports to resume after repairs", *Hurriyet*, <http://www.hurriyet.com.tr/english/finance/9642716.asp>.
 13. Eric Watkins, "Socar declares Force Majeure on Azeri oil exports", *Oil and Gas Journal*, 6 August 2008, http://www.ogj.com/articles/article_display.cfm?ARTICLE_ID=336370.
 14. See also: "BP declares Force Majeure on BTC's oil deliveries", *Dow Jones Newswire*, 6 August 2008, http://www.downstreamtoday.com/News/Articles/200808/BP_Declares_Force_Majeure_On_BTC_s_Oil_D_12262.aspx; "BP – No Force Majeure on BTC Supply", *Dow Jones Newswire*, 6 August 2008, <http://www.smartmoney.com/news/ON/index.cfm?story=ON-20080806-000378-0557>.
 15. Bloomberg, "BP starts BTC assessment after pipeline cools down", 13 August 2008, <http://www.bloomberg.com/apps/news?pid=20601207&sid=asRUpCPm4sKg&refer=energy>.
 16. See: The Corner House et al, Letter to Jeanette Swindon ECGD, "BTC Pipeline", 10 November 2003, <http://www.baku.org.uk/correspondence/ECGDletter.doc>; See: Platform, "Memorandum", Trade and Industry Committee, "Implementation of ECGD's Business Principles", Ninth Report, Session 2004-05, <http://www.publications.parliament.uk/pa/cm200405/cmselect/cmtrdind/374/374we09.htm>.
 17. See: Michael Gillard, "Memorandum", Trade and Industry Committee, "Implementation of ECGD's Business Principles", Ninth Report, Session 2004-05, para 146, <http://www.publications.parliament.uk/pa/cm200405/cmselect/cmtrdind/374/374we07.htm>. Gillard points out that the coating for the Turkey section of the pipeline was disqualified for use on the pipeline in Azerbaijan and Georgia, due to failing key tests undertaken on behalf of BP, the company leading the BTC consortium.
 18. "Turkish official confirms BTC pipeline blast is a terrorist act", *Hurriyet*, 14 August 2008, <http://www.hurriyet.com.tr/english/finance/9660409.asp?scr=1>.
 19. "PKK claims responsibility for BTC pipeline explosion", *Zaman*, 8 August 2008, <http://www.todayszaman.com/tz-web/detaylar.do?load=detay&link=149686>.
 20. "Kurdish rebels 'threaten more attacks' after pipeline blast", http://news.yahoo.com/s/afp/20080808/wl_afp/turkeykurdsunrestpipelineoilblast_080808150051. Bahoz Erdal, a PKK commander, has stated: "As long as the Turkish state insists on war, such acts will be naturally carried out."
 21. Energy Tech, "Analysis: BTC pipeline explosion", http://www.energy-daily.com/reports/Analysis_BTC_pipeline_explosion_999.html.
 22. Carlisle, T., "Caspian oil exports under twin threat", *The National*, 10 August 2008, <http://www.thenational.ae/article/20080810/BUSINESS/884886899/0/FRONTPAGE>.
 23. According to the Kurdish News Agency, Abkhazian leader Sergey Bagaps has stated that if the conflict in South Ossetia continues, sabotage attacks will be conducted on energy pipelines in Georgia, especially the BTC pipeline. Paata Davitaya, a member of the Georgian parliament, is also reported as stating that there is a sabotage group of 30 people (called "Delfin") from Abkhazia waiting to conduct such attacks. According to the MP, this group trained in Russia.
 24. Energy Tech, "Analysis: BTC pipeline explosion", http://www.energy-daily.com/reports/Analysis_BTC_pipeline_explosion_999.html.

have not suffered since the height of Turkish-PKK clashes in the 1990s”.²⁵ Already there are unconfirmed reports that the Turkish authorities have placed sections of the pipeline off limits and of raids on Kurdish villages.

Meanwhile, the terms of the Host Government Agreements, which lay down the legal regime for the project, raise the strong possibility of future legal disputes over who will pay for lost revenues. Under the Agreements, project participants (that is, the companies involved in the project) may invoke Force Majeure for acts of terrorism. Turkey, however, may not. Turkey could therefore be liable for losses incurred whilst the pipeline is shut down due to the PKK bombing – but only if it can be shown that it failed to take reasonable steps to protect the pipeline.²⁶ Should the companies demand compensation from Turkey for losses sustained, the possibility of future arbitration proceedings cannot be ruled out. The Agreements thus provide the Turkish state with an incentive to further militarise the pipeline route.

• ***South Ossetia Conflict***

Two days after the explosion in Turkey, war broke out between Russia and Georgia over South Ossetia, a potential source of conflict that NGOs had highlighted since 2002 as being of particular risk to the BTC project. Russian jets bombed the pipeline, causing more than 50 deep craters in its immediate vicinity, with some missiles landing within 100 yards of the pipeline itself.²⁷ Despite these eyewitness reports, BP, the pipeline’s operator, has said it has no evidence that Russian forces attempted to bomb the BTC line.²⁸ The company has also stated that it is unaware of any damage to any of its Georgian pipelines.²⁹

Physical damage to the BTC pipeline aside, the long-term financial consequences of the conflict for the project are likely to be severe. The pipeline was built to secure an export route for oil from the Caspian to the West that bypassed Russia and Iran. If, as many commentators suggest, Russia’s actions in Georgia were primarily motivated by a desire to re-establish its hegemony over the Caucasus region, the political credibility of an “independent” export route has been severely undermined. The Lex column in the *Financial Times* wrote that “Russia has demonstrated its willingness to use force in ex-Soviet territories that step out of line, so forget new independent gas pipelines from central Asia. The Kremlin's grip on eastern supplies to Europe is now all but complete. Cue higher prices as Europe bids for the world's LNG.”³⁰ As Robert Cutler of the Institute of European, Russian and Eurasian Studies at Carleton University, Canada, notes: “The Russian invasion is not about South Ossetia. It is about regime change in Tbilisi, re-imposing a 19th-century sphere of influence in the South

25. STRATFOR, “Turkey: Implications of a blast on the BTC pipeline”, 6 August 2008.

26. Article 12.1 of the Host Government Agreement for Turkey states that Turkey “shall protect the Rights to Land, the Facilities [...] from all loss or Damage resulting from civil war, sabotage, vandalism, [...] terrorism.” However, Article 20.2 limits the circumstances in which force majeure can be invoked by the Turkish state: “Force Majeure with respect to State Authorities shall be limited to (i) natural disasters [...] (ii) wars between sovereign states where the Republic of Turkey has not initiated the war under the principles of international law and (iii) international embargoes of sovereign states other than the Republic of Turkey.” This would preclude *Force Majeure* being invoked by Turkey for an act of terrorism. No such limitation applies to the project participants: on the contrary, Article 20.3 specifically lists “acts of terrorism” as one of the triggers which allow project participants to invoke *Force Majeure*.

27. Damien McElroy, “Georgia: Russia targets key oil pipeline with over 50 missiles”, 11 August 2008, <http://www.telegraph.co.uk/news/worldnews/europe/georgia/2534767/Georgia-Russia-targets-key-oil-pipeline-with-over-50-missiles.html>.

28. International Herald Tribune, “BP reopens Georgia gas pipeline”, 14 August 2008, <http://www.ihf.com/articles/ap/2008/08/14/business/EU-Britain-Georgia-Pipeline.php>. The IHT reports: “BP has said it has no evidence that Russian forces attempted to bomb the BTC line, despite reports to that effect by Georgian officials.” See also: “BP-Azerbaijan refutes reports that Russian planes bombed BTC”, <http://en.apa.az/news.php?id=86626>.

29. “The reopening of BTC pipeline remains unclear as repair continues”, Hurriyet, <http://www.hurriyet.com.tr/english/finance/9676147.asp?sc=1>.

30. Lex, Financial Times, 12 August 2008

Caucasus, limiting the autonomy of the countries there, and through all these devices maintaining control of energy transmission lines to the West.”³¹

Indeed, Russia’s actions may prompt governments in Caspian and Central Asian oil-producing states to rethink plans to send their oil via BTC.³² In particular, analysts are questioning whether BP can rely any longer on future plans for oil from the Kashagan oil field in Kazakhstan to be shipped to the West via BTC.³³ Kazakh government officials have stated that they are reconsidering whether to export oil through BTC given the increased security concerns in the Caucasus, possibly pumping oil through Russia instead.³⁴ Over 50% of the oil passing through the pipeline annually is ultimately expected to come from Kazakhstan³⁵ – despite BP having claimed that the pipeline would not require Kazakh oil – and any move to transport Kazakh oil via other routes would adversely affect the economics of the BTC project.

Documents released by the Department of Trade and Industry (now the Department of Business Enterprise and Regulatory Reform) in response to a Freedom of Information request from Friends of the Earth (England Wales and Northern Ireland) confirm that, prior to the ECGD agreeing to fund the BTC pipeline, both BP and the UK Government were firmly of the view that the pipeline would not be financially viable without Kazakh oil. An internal DTI email dated 2 September 1999 was blunt: “*Essentially the route is uneconomic*”.³⁶ BP itself was reported by the Foreign and Commonwealth Office to have estimated that “*Baku-Ceyhan still fell USD 1 billion short of being commercially viable*” and that “*everything depended on making up the missing volumes from eastern Caspian production*.”³⁷ Even after the Intergovernmental Agreement³⁸ initiating the project had been signed in December 1999, Department for Trade and Industry officials again expressed concerns that “*the route is not commercially viable*.”³⁹

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31. Robert M. Cutler, “Oil in Troubled Mountains”, Asia Times Online, Aug 13, 2008, http://www.atimes.com/atimes/Central_Asia/JH13Ag04.html.
 32. Jad Mouawad, “Conflict in Georgia narrows oil options for West”, International Herald Tribune, 14 August 2008, <http://www.ihf.com/articles/2008/08/14/europe/14oil.php>. Mouawad quotes Cliff Kupchan, a political risk analyst at Eurasia Group and a State Department official during the Clinton administration: “Moving forward, multinationals and Central Asian and Caspian governments may think twice about building new lines through this corridor. It may even call into question the reliability of moving existing volumes through that corridor.”
 33. Jad Mouawad, “Conflict in Georgia narrows oil options for West”, International Herald Tribune, 14 August 2008, <http://www.ihf.com/articles/2008/08/14/europe/14oil.php>.
 34. “Kazakhstan considers to divert oil export route from BTC to Russia”, Hurriyet, <http://www.hurriyet.com.tr/english/finance/9714319.asp?scr=1>
 35. “Kazakhstan commits to BTC”, 30 March 2007, <http://www.kogiguk.com/news/index.htm>. “According to press reports . . . oil from the Kashagan and Tengiz field will be pumped to a new terminal on the Caspian coast via the planned Eskene-Kuryk pipeline. The oil will be loaded onto tankers at Kuryk, sent across the sea to one of two terminal facilities near Baku and then transferred via local pipelines to the BTC for export. The cost of establishing the pipeline-and-tanker route, which will be known as the Kazakh Caspian Transport System (KCTS), is expected to reach US\$3 billion. KCTS will be able to handle about 500,000 barrels per day in its first phase of operations. In the second stage, throughput capacity will rise to 760,000 bpd.”
 36. Email from Ken Forrest, Deputy Director IEP2, to J. Rhodes, “Subject - Re: BP and Azerbaijan”, 2 September 1999: “FCO (confidential) telno 754 of 27 August arrived on my desk today and is the latest in a line of telegrams reporting BP Amoco’s dilemma of the US govt pushing the Azeris and Turks and BP to build a pipeline from from Baku to Ceyhan on Turkey’s Mediterranean coast. Essentially the route is uneconomic, but the US have put a significant amount of political capital into the project (AI Gore has been backing it in public, as has Richardson).”
 37. Foreign and Commonwealth Office, Tel NO 524, “Caspian Energy – BP Amaco and Baku”, 25 October 1999. The telegram states: “After a recent visit to Kazakstan, Wolf [Special Advisor to President Clinton on the Caspian] was convinced that up to 400,000 bpd could be put together relatively easily from production there. But BPA [BP Amoco] continued to take a more pessimistic view.”
 38. “Agreement among The Azerbaijan Republic, Georgia and the Republic of Turkey, relating to the Transportation of Petroleum via the Territories of the Azerbaijan Republic, Georgia and the Republic of Turkey through the Baku-Tbilisi-Ceyhan Main Export Pipeline”, Agreed and executed on 18 November 1999 in Istanbul, Republic of Turkey, <http://subsites.bp.com/caspian/BTC/Eng/agmt4/agmt4.PDF>.
 39. Letter from Ken Forest, IEP2, to John Rhodes, “Meeting with Brown and Root”, 16 December 1999. “The intergovernmental declarations in Istanbul (and witnessed by Clinton) set the framework for governmental agreement over construction of Baku-Ceyhan. The problem is that the route is not commercially viable. There will not be the reserves in production to fill Baku-Ceyhan until around 2008 at the very earliest.”

Although BP was subsequently reported to have redone “its sums”⁴⁰ and found that sufficient volumes of oil existed to make the project commercially viable, such claims (which were challenged by NGOs even at the time in a detailed financial analysis of the project by Claros Consulting)⁴¹ must now be in doubt, given the high probability that Kazakhstan may now be deterred from using the BTC pipeline as their export route. **A key question is whether or not ECGD took adequate account of these conflict-related commercial risks in setting its premiums for the guarantees issued to BP.** We would point out that the PKK-Turkey and South Ossetian conflicts are not the only conflicts that put the BTC project at risk. Azerbaijan, which has been using its new oil wealth to rebuild its military, is again threatening to retake⁴² land it lost to Armenia in the Nagorny-Karabakh war of the early 1990s – and Armenia has stated that, if attacked, the BTC pipeline would be an immediate target. In March 2008, the two sides came close to war, with prolonged mortar exchanges.⁴³

Concerns over ECGD’s Due Diligence

As mentioned, non-governmental organisations repeatedly warned both of the risks that conflict posed to the project and of the risks that the project would inflame conflict.

From documents now in the public domain as a result of Freedom of Information requests, it would appear that ECGD and other government departments failed to assess either risk adequately. Although security concerns led to the pipeline being rerouted, at Georgia’s insistence, to avoid the Akhalkhalaki region of Southern Georgia, “since the Georgian government stated it could not guarantee security in this area”,⁴⁴ the risk that resurgent conflict in the South Caucasus might jeopardise the very viability of the project appears to have received scant attention. Instead, the emphasis was on the BTC pipeline acting as a “project for peace” – this despite the Foreign and Commonwealth Office recording that Russia viewed the pipeline “as part of a wider American plot to squeeze Russia out of the Black Sea and the Caucasus.”⁴⁵ Threats that the pipeline might be a target for PKK attacks or that security provisions would lead to a militarisation of

40. Teleletter from UK Embassy, Ankara, Turkey, 14 February 2001. “BP had done its sums and concluded that the project made strong commercial sense . . . The volumes necessary to make BTC viable existed: but not all ACG participants had committed their volumes. Exxon and Lukoil, who controlled 25 per cent of ACG’s reserves needed to be brought on board.”

41. Claros Consulting, “Building Tomorrow’s Crisis: BTC pipeline and BP – A Financial Analysis”, Platform, http://www.baku.org.uk/publications/building_tomorrows_crisis.pdf. The study warned in detail of the financial risks to the project arising from possible future conflicts: “Both Azerbaijan and Georgia are countries where there are significant political, security and corruption risks. The Control Risks Group assesses both Georgia and Azerbaijan as high political risk, and Georgia, together with Azerbaijan-Armenia border areas, are seen as having high security risks for international investors. . . . The pipeline runs through or near areas of significant conflicts – particularly Armenia and Azerbaijan are in a state of near hostility, with the edge of the disputed area of Nagorno Karabakh (currently occupied by Armenia) only 15km from the pipeline. In Georgia, there are several areas of conflict, notably South Ossetia and the Pankisi Gorge. In Turkey the pipeline deliberately avoids the majority Kurdish southeast but nonetheless runs through areas where Kurds make up about 30% of the population - and indeed, areas where the armed Kurdish PKK guerrilla group has been active in the past. It could be a target if the current cease-fire breaks down.”

42. “Azeris, Armenians spar after major Karabakh clash”, 5 March 2008, <http://www.reuters.com/article/latestCrisis/idUSL0572597>. Reuters reports: “Azeri President Ilham Aliyev said this week his country was ready to take back Nagorno-Karabakh by force if need be, and was buying military equipment and arms in preparation.” For further background, see: Jim Nichol, “Armenia, Azerbaijan and Georgia: Security issues and implications for US interests”, Congressional Research Service, January 2008, p.10 ff, <http://ftp.fas.org/sfp/crs/row/RL30679.pdf>.

43. “Armenian and Azerbaijani forces clash”, 4 March 2008, http://www.newsvine.com/_news/2008/03/04/1343361-armenian-and-azerbaijani-forces-clash.

44. ECGD, “BPU Review of Baku-Tbilisi-Ceyhan Pipeline Project”, 3 December 2008, p.4, released to The Corner House by ECGD under Freedom of Information Act.

45. Telegram, UK Embassy Moscow, “Subject – Caspian Energy: Baku Ceyhan: Russian Reactions to”, 24 November 1999. “Media reporting has reflected Russian fears that the West is gradually increasing its influence in the South Caucasus region. Nezavisimaya Gazeta portrayed the agreement as part of a wider American plot to squeeze Russia out of the Black Sea and the Caucasus”.

the corridor – with the high risk of communities along the pipeline being subject to human rights abuses – were also downplayed. And, although the ECGD sought assurances that security operations to protect the pipeline would respect human rights, it would appear that the assurances sought were not received.

More details of these concerns are outlined below:

- ECGD holds “150 or so” files relating to the BTC project. However, **there is not a single file that specifically addresses the risks of conflict.**⁴⁶ This may reflect ECGD’s view, as recorded in a 2003 briefing paper prepared for HM Treasury that **conflict was not a major “project sensitivity”.**⁴⁷
- Although the Department for International Development (DfID)’s conflict specialists, with whom ECGD worked to assess security risks to the BTC pipeline, warned that Russia was “displeased”⁴⁸ with the BTC project and that its military establishment was “wary of losing its grip”⁴⁹ on the Southern Caucasus, **there is no public record of either ECGD or DfID undertaking any detailed analysis of the risk that BTC might incite Russia to act to reassert its control over oil and gas exports from the Caspian.** The only published report – DfID’s “Strategic Conflict Assessment for Georgia”⁵⁰ – contains just 3 paragraphs dedicated to oil pipelines (out of 34 pages) and contains a far greater focus on the role of smuggling in exacerbating conflicts in the region.⁵¹ Although the study notes in passing that “*many Georgians fear that the Russians intend to impose control of Georgia by force*”, it dismisses this as “*unlikely*”. No further analysis is provided.
- Documents released to Friends of the Earth under FOIA reveal that, prior to ECGD agreeing support for BTC, senior Foreign and Commonwealth Office officials **identified the need for a detailed analysis of the foreign policy implications of current and future oil pipelines in the region**⁵² - **but that the study was never commissioned.**⁵³ The proposal for the study specifically

46. ECGD, “BTC List of files”, released to The Corner House under Freedom of Information Act request, IR(05)08 (request IAR(05)36b), 22 February 2006.

47. ECGD Briefing prepared for HM Treasury, “Baku-Tbilisi- Ceyhan Pipeline”, 2 May 2003, released by Department of Trade and Industry to Friend of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act. Conflict is not mentioned in the list of “ main project sensitivities” identified by ECGD: “The main sensitivities of this project are the environmental concerns (major construction project, pollution concerns), social concerns (disruption and compensation of local populations) and financial concerns (complex financing arrangements).”

48. Tony Vaux, “Strategic Conflict Assessment: Georgia – Report for the Global Conflict Prevention Pool, UK Government”, Conflict Studies 3, p.19, <http://www.humansecurity.org.uk/downloads/GeorgiaSCA.pdf>.

49. Tony Vaux, “Strategic Conflict Assessment: Georgia – Report for the Global Conflict Prevention Pool, UK Government”, Conflict Studies 3, p.21, <http://www.humansecurity.org.uk/downloads/GeorgiaSCA.pdf>.

50. Tony Vaux, “Strategic Conflict Assessment: Georgia – Report for the Global Conflict Prevention Pool, UK Government”, Conflict Studies 3, <http://www.humansecurity.org.uk/downloads/GeorgiaSCA.pdf>.

51. Tony Vaux, “Strategic Conflict Assessment: Georgia – Report for the Global Conflict Prevention Pool, UK Government”, Conflict Studies 3, <http://www.humansecurity.org.uk/downloads/GeorgiaSCA.pdf>. The study’s Forward (p.3) summarises its main finding: “In the immediate aftermath of independence Georgia was divided by exclusive forms of nationalism on all sides. Subsequently, vested interests built up around separatism and ethnic tension. One of the crucial issues today is smuggling and its pernicious effects on poverty and governance. The report suggests that interests in smuggling must be addressed if progress is to be made.”

52. Michael Arthur, “Pipeline Politics”, Restricted, 26 March 2006, released to Friends of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act. Michael Arthur was Director General of the FCO’s EU and Economics unit. In response to the proposal, Andrew Levi wrote: “Fascinating! Pipelines as an instrument for peace and stability; or perhaps the opposite . . . There is every merit in an analysis of existing and projected pipelines and their likely effects on their likely effects on the global energy market, on the countries served or transited, on the role of multilateral diplomacy in global energy security and on our own interests.” See: Andrew Levi, Email, “Restricted: Pipeline Politics”, 8 May 2003, released to Friends of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act.

53. Email from Colin Sykes, Foreign and Commonwealth Office, to Phil Michaels, Friends of the Earth, “Request for Information – Pipeline Politics”, 21 July 2008. The Foreign Office confirmed that no report existed in the file created after Michael Arthur’s proposal was made.

mentions the risk that political instability in the Caucasus posed to the “physical security” of pipelines, with Georgia being singled out as an example, as was the threat of Russia “misusing” its “*dominant position as transit country*”.⁵⁴ It was proposed that a BP staff member undertake the project.⁵⁵

- In response to an ECGD’s “Notification of a Sensitive Case”, requesting departmental comments on the BTC project, the Foreign and Commonwealth Office (FCO) replied: “*We are concerned that the pipeline runs close to minority ethnic areas in Turkey and that its construction may lead to an increased Turkish military presence in the area. I have discussed this point with the Turkey desk who are satisfied that it is unlikely to result in any problems.*”⁵⁶ There is no record in disclosed FCO files indicating that ECGD requested further details – or the basis for the Turkey desks conclusions, despite their being at odds with the views of others in the FCO. **In the light of the recent PKK attack, and reports of a security clamp down by the Turkish authorities, the apparent failure to make such inquiries may, with hindsight, be viewed a dangerously complacent.**
- ECGD raised only two security related issues in its 2003 briefing for HM Treasury: first, that any expenditure on security by Georgia did not exceed the limits laid down by the UK government in its Productive Expenditure Test⁵⁷ for countries receiving assistance from the World Bank’s International Development Association (IDA), which, in 2003, included Georgia;⁵⁸ and, second, the “possibility that the pipeline security forces could be used to repress specific groups or communities.”⁵⁹ Whilst these concerns are commendable, **the failure to raise the security risks to the pipeline or the risk of the pipeline inflaming conflict is of grave concern.**
- The only publicly available assessment by the ECGD of the security risks to the BTC pipeline appears to be a single sentence in field report filed by the Business Principles Unit (BPU). The report notes of the pipeline corridor in Georgia, which is close to the Baku-Supsa pipeline, also known as the Western Route Export Pipeline [WREP] : “*I visited several sections of the WREP in Georgia. The only indications of its existence below ground were the marker posts. There was no*

54. Michael Arthur, “Pipeline Politics”, Restricted, 26 March 2006, released to Friends of the Earth (England, Wales and Northern Ireland under Freedom of Information Act. “The impact of these trans-national economic links is considerable. Physical security becomes relevant (eg. instability in Georgia). Pricing policy affects end users (eg. Russian misuse of their dominant position as transit country).”

55. Michael Arthur, “Pipeline Politics”, Restricted, 26 March 2006, released to Friends of the Earth (England, Wales and Northern Ireland under Freedom of Information Act. It was suggested that one way of funding and authoring the study might be to “invite one of the energy majors (BP) to second someone, at their expense, to write this, on the basis that we would be giving him/her a very privileged inside perch, and contacts, from which to think this through, and providing value added from the various FCO sources he/she would tap.”

56. Email from FCO official (named redacted), “Subject: Notification of a Sensitive Case – Azerbaijan-Georgia-Turkey Oil pipeline”, received in Foreign and Commonwealth Office Registry 3 October 2002, released to Friends of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act.

57. Under its “productive expenditure test”, which applies to all Heavily Indebted Poor Countries (HIPC) and to countries receiving support through the World Bank’s International Development Association (IDA), ECGD “will only provide support to projects if these projects contribute to the economic and social development of the country and do not lead to the build up of unsustainable debt.” At the time that ECGD support for BTC was being considered, Georgia was receiving IDA assistance. The ECGD was concerned that its military expenditure on the pipeline did not break its productive expenditure rules. For further details see: ECGD, “BPU Review of Baku-Tbilisi-Ceyhan Pipeline Project”, 3 December 2008, p.42, released to The Corner House by ECGD under Freedom of Information Act.

58. ECGD, Briefing prepared for HM Treasury, “Baku-Tbilisi- Ceyhan Pipeline”, 2 May 2003, released by Department of Trade and Industry to Friend of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act. “As part of the Productive Expenditure analysis ECGD and DFID need to know what costs will need to be born by the Host Governments for the provision of pipeline security. (We have seen the press report of a US\$11 million grant from the US to Georgia for setting up a special battalion to protect the pipeline. This is apparently in addition to the US\$64 million to ‘train and equip’ the Georgian military and a similar sum for the Georgian border guards). BTC considers this to be strictly a host government issue and has provided no information. ECGD has contacted the UK embassy in Tbilisi requesting further information.”

59. ECGD, Briefing prepared for HM Treasury, “Baku-Tbilisi- Ceyhan Pipeline”, 2 May 2003, released by Department of Trade and Industry to Friend of the Earth (England, Wales and Northern Ireland) under Freedom of Information Act.

sign of any security for the pipeline or any need for it” (emphasis added).⁶⁰ We note that Baku-Supsa was shut down following the Russian invasion of Georgia due to security concerns.⁶¹

- The ECGD downplayed NGO concerns over the militarisation of the pipeline corridor, wrongly claiming: “When the project was first publicized the international NGOs claimed there would be a 4km-wide militarized corridor stretching from Baku to Tbilisi. Once it became clear that this was not the case, the NGOs became silent on the issue.”⁶² In fact, NGOs continued to raise concerns over militarisation throughout the public consultation period for the project.⁶³
- In its assessment of the BTC project’s compliance with the ECGD’s Business Principles, the ECGD’s Business Principles Unit raised concerns that “Terms of Engagement” for “the government security forces with responsibility for protection of the BTC project” had not been received. The issue was brought before the ECGD’s Underwriting Committee, which met on 5 December 2003 to consider ECGD support for the project. The minutes record “the difficulties of imposing approval of the terms of engagement” and note that “BTC Co was not in a position to dictate such terms to the three Host Governments”. It is not known how the issue was resolved. However, the minutes of a meeting held after ECGD had approved the project notes that the terms of engagement for Turkey were still only in draft form.⁶⁴ More worrying still, in 2005, ECGD was informed that BTC Co had met with the relevant Turkish Government ministries and had “received [a] direct refusal” to sign the “Voluntary Principles on Human Rights”,⁶⁵ a set of undertakings for businesses and governments initiated by the US and the UK in 2000. No reasons were given. **In light of reports of a security clampdown following the recent PKK bombing, ECGD’s failure to ensure that the Host Governments agreed to acceptable Terms of Engagement for their security forces prior to ECGD approving support for the project raises major concerns over the ECGD’s commitment to its Business Principles and its judgment over the conflict-related impacts of the project.**

Request for NAO Review

In light of the above, we believe there is an urgent need to reassure the public that ECGD has not placed taxpayers’ money at unjustified risk by supporting the BTC pipeline.

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60. “BTC Field Visit – Flash Report”, released to Friends of the Earth by the Foreign and Commonwealth Office under Freedom of Information Act. The field trip took place from 14-27 June 2003.
 61. “Bp shuts down Baku-Supsa pipeline”, Press TV, 13 August 2008, <http://www.presstv.ir/detail.aspx?id=66448§ionid=351020606>.
 62. ECGD, “BPU Review of Baku-Tbilisi-Ceyhan Pipeline Project”, 3 December 2008, p.42, released to The Corner House by ECGD under Freedom of Information Act.
 63. See, for example: The Corner House et al, Review of BTC Environmental Impact Assessment, Section 3.3.2 – Absence of Analysis of Kurdish Situation in EIA, October 2003; Platform et al, Some Common Concerns, pp115-121 (A Region of Simmering Conflicts), <http://www.baku.org.uk/publications/concerns.pdf>; International Fact Finding Mission, BTC Pipeline – Turkey Section, Section 1.5 – Pipeline Security and the Gendarmerie, June 2003, http://www.baku.org.uk/publications/Tu_FFM.pdf; Baku Ceyhan Campaign, “The Real Democratic Deficit – BP, the Baku-Ceyhan oil pipeline and public funding”, November 2003, in Ilisu Dam Campaign et al., “Listen to the Refugee’s Story – How UK Foreign Investment creates Refugees and Asylum Seekers”, <http://www.thecornerhouse.org.uk/item.shtml?x=52207#index-02-04-00-00>;
 64. “BTC Terms of Engagement”, Notes of meeting on 22 December 2003, released by ECGD to The Corner House under Freedom of Information Act. “Rules of engagement – BP has draft version hopes to be able to report good progress in 12 months.”
 65. “BTC Security Progress Meeting”, Notes of meeting on 13 June 2005, released by ECGD to The Corner House under Freedom of Information Act. The Voluntary Principles were developed for companies operating in the extractives sector at the initiative for the UK and US governments in 2000. They are available at: <http://www.voluntaryprinciples.org/principles/index.php>.

We are therefore writing to request that the NAO assesses:

- **Whether or not the risks of conflict were adequately assessed by ECGD;**
- **Whether the premiums charged to BTC Co realistically reflect the risks of conflict in the region;**
- **Whether the terms of ECGD's contracts for the BTC project adequately protect the UK taxpayer.**

Should you wish to have copies of any of the documents cited, we will be pleased to make them available.

We await your urgent reply,

Yours Sincerely

Nicholas Hildyard, The Corner House
Kerim Yildiz, Kurdish Human Rights Project
Mika Minio Paluello, PLATFORM
Manana Kochladze, Regional Coordinator for Caucasus, CEE Bankwatch Network
Nick Rau, Friends of the Earth (England, Wales and Northern Ireland)

cc.

Joe Cavanagh, NAO
Eric Lewis, NAO
Leo Watson, NAO