

Interim OPIC Management Response

February 7, 2007

Office of Accountability Compliance Review of OPIC's Environmental Due Diligence and Monitoring of the Baku-Tbilisi-Ceyhan Oil Pipeline Project

The Overseas Private Investment Corporation (OPIC) management welcomes the Office of Accountability Compliance Review Report (OA Report) of OPIC's environmental due diligence and monitoring of the Baku-Tbilisi-Ceyhan Oil Pipeline Project (BTC Project).

OPIC is encouraged that the findings of the OA Report found that OPIC followed its environmental due diligence process.

The following are general comments on the OA findings. OPIC will carefully review the recommendations in the OA Report, and will provide full consideration to the recommendations and other comments, reporting promptly on progress within 30 days.

Findings:

OA Finding: OPIC did comply with the seven steps in OPIC's due diligence process as stated in OPIC's environmental Handbook.

OPIC Management Response: OPIC concurs.

OA Finding: OPIC did collaborate with other lenders and insurers of the Project regarding assessment and mitigation of significant environmental issues.

OPIC Management Response: OPIC concurs.

OA Finding: As pipeline construction commenced during due diligence, OPIC did not access all material construction monitoring data.

OPIC Management Response: With the wide variety of sectors, countries and types of projects for which U.S. investors seek OPIC support, OPIC relies on specialized and industry recognized technical expertise and independent environmental consultants in the review of information on proposed projects to supplement the expertise of OPIC staff. To a reasonable and appropriate degree, OPIC defers to such experts as to the significance of construction issues, specifically as to when construction issues have a significant bearing on the outcome of OPIC's own environmental analysis.

OPIC works with other multilateral and bilateral organizations to achieve the highest level of environmental protection and necessary safeguards. In the context of BTC, the project has several different private and public sector sponsors, international lenders, investors and insurers whose interests in proper environmental monitoring are directly aligned with OPIC's interests. As a general matter, with regard to projects such as BTC, OPIC agrees that a review of all relevant construction reports by qualified experts is essential prior to the provision of financing or political risk insurance.

OA Finding: OPIC received two kinds of monitoring reports after close.

OPIC Management Response: OPIC concurs.

OA Finding: OPIC did not fully meet its requirements regarding third party monitoring in two instances.

OPIC did not enforce its requirements, as stated in the *Environmental Handbook and Environmental and Social Action Plan*, that the Project's annual Environmental and Social Annual Report must provide a summary of the environmental data; and

The Independent Environmental Consultant's reports to date have not included a section on the validation of self-monitoring methodology. The IEC should validate the methodology in at least one of its reports during the three-year period within which the *Environmental Handbook* calls for an independent third-party audit. OPIC has not enforced its requirement that these reports validate the clients self-monitoring methodology.

OPIC Management Response: OPIC disputes the finding that the agency did not enforce its requirements as stated in OPIC's Environmental Handbook and the Project's Environmental and Social Action Plan (ESAP). OPIC notes that the ESAP for the BTC project specifies the content of environmental reports. During the construction phase, environmental reports are due quarterly subject to requirements in Annex B of the ESAP. Post-construction environmental reports are due annually, subject to the requirements of Annex C of the ESAP.

For the purposes of project compliance with OPIC requirements, OPIC treated the fourth quarter report from BTC in 2004 as an "annual" report. This document, referenced on page 13 of the OA report is subject to the requirements found in Annex B of the ESAP. Annex B does not require reporting on emissions and discharges.

Annex C to the ESAP *does* require a summary of air emissions and environmental discharges. Annual reports issued after 2004, post construction, did report on emissions and discharges.

OPIC thus maintains that it did meet its requirements.

With respect to reporting on the validation of self-monitoring methodology, the Independent Environmental Consultant was asked to pre-validate all monitoring methodology to be employed by the BTC Project. The Independent Environmental Consultant did so during pre-commitment reviews. Although this validation was conveyed to OPIC, OPIC acknowledges that the information was not explicitly reported in audit reports issued post-commitment.

OA Finding: To OA's knowledge OPIC has not defined when the three-year client audit requirement commences.

OPIC Management Response: Determining the precise timing of an audit requires some flexibility and tailoring to the project lifecycle. For its 1999 Environmental Handbook, OPIC chose the three-year milestone based on OPIC's operational experience in 1998 that revealed most construction was completed within three years following financial close. While OPIC does customize the most appropriate audit schedule for a particular project on a case by case basis, OPIC is aware of the necessity to revise the OPIC Environmental Handbook to reflect current, international best practice regarding audit requirements.