

Report  
nr 11

# The Price of Oil

Nordic participation in environmental  
violations in Oil and Gas development  
on Sakhalin in Russia

SwedWatch



Svenska Naturskyddsföreningen



Miljöförbundet Jordens Vänner  
Friends of the Earth Sweden



Norwatch



FINNWATCH



SwedWatch is a non-governmental organisation whose task is to critically examine Swedish business relations with developing countries focusing on environmental and social concerns. SwedWatch consists of five member organisations: The Swedish Society for Nature Conservation, Church of Sweden Aid, Education for Aid Activities, Friends of the Earth Sweden and Fair Trade Center. SwedWatch is financed by the Swedish Development Aid Agency, Sida.



Norwatch is an independent journalistic unit owned by the Norwegian NGO Future in our hands. Norwatch conducts critical journalistic investigation on Norwegian businesses in developing countries, investigating whether the companies act in accordance with basic human rights, labour rights, safety and environmental standards. In addition, Norwatch covers issues concerning investment, export and import ethics.



#### FINNWATCH

FinnWatch collects, analyses and spreads information on Finnish companies. It is interested in the consequences of these companies' operations on human and labour rights, the environment and developmental and social consequences in the South and economies in transition. Started in October 2002, FinnWatch is a network of several organisations.



Svenska Naturskyddsföreningen

The Swedish Society for Nature Conservation (SSNC) is the largest non-governmental environmental organisation in Sweden. It was founded in 1909. The SSNC is governed by its 170 000 members and have 270 local branches. SSNC's international work aims to contribute to an ecologically, socially and economically sustainable development based on respect for human rights and democratic systems of governance.



Friends of the Earth Sweden is a radical voice in the environmental movement. The organization advocates fair distribution of the Earth's resources, and an adaptation of society to what is ecologically sustainable. FoE Sweden strives to increase democracy, and gender and cultural equality.

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# Foreword

The oil and gas industry are on the lookout for more oil reserves. The new places they explore in the search for these hydrocarbon resources are often in remote Arctic environments. These new environments bring several new challenges for the industry such as harsh climatic conditions in sensitive untouched wilderness areas. There is also another challenge; to act accountably even where there may sometimes be a lack of proper environmental legislation.

There is always a risk of companies thinking that since they are so far away, they need not take as much care in relation to environmental and social issues as they do at home. This seems to be the case with regard to the Sakhalin Energy Investment Company (SEIC). The company has not followed best practice in its activities on the remote Russian Island of Sakhalin; for example, it has dumped dredging material in the middle of a biologically sensitive bay, let out drilling waste in the sea, caused environmental damage by trench crossing of pipelines in rivers during the spawning season and gone through with installing the concrete basements of a platform very close to the only known feeding area of the threatened Western Pacific Gray Whale.

Nordic businesses have been keen to compete for multimillion dollar contracts for Phase Two of the huge oil and gas project Sakhalin 2. However, none of the companies have made any environmental or social risk analyses of the project before signing contracts with SEIC.

The Swedish Society for Nature Conservation (SSNC) and Friends of the Earth Sweden (FoE Sweden) believe that the Nordic suppliers have co-responsibility for the consequences of the project. At the end of the report we therefore make recommendations to these companies. Many Nordic companies are active in the engineering sector, where the ethical risks are mostly in relation to customers upstream in the supply line, not downstream towards the suppliers. We believe that many Nordic companies need to be aware of these risks and must develop strategies to meet them.

We are happy to announce that this report is the first joint report from all Nordic-watch organisations: Norwatch, FinnWatch and SwedWatch. This is significant, not least because of the ever increasing degree of cooperation between Nordic businesses, a very visible feature of the Sakhalin 2 project.

Svante Axelsson, Secretary General, Swedish Society for Nature Conservation .

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# Abbreviations

ABB	Asea Brown Boveri
CGBS	Concrete gravity base substructures
CLO	Community Liaison Officer
CSR	Corporate Social Responsibility
EBRD	European Bank for Reconstruction and Development
EIA	Environmental impact assessment
ESHIA	Environmental, social and health impact assessment
IFAW	International Foundation of Animal Welfare
IFC	International Finance Corporation
ILO	International Labour Organisation
ISRP	Independent Scientific Review Panel
IUCN	International Union for the Conservation of Nature
LNG	Liquid natural gas
LUN-A	Lunskoye Platform
MOU	Memorandum of Understanding
NGO	Non Governmental Organisation
OET	Oil Export Terminal
OPF	Onshore processing facility
PA	Piltun-Astokhskoye oil field
PA-A	Molikpaq platform
PA-B	Piltun-Astokhskoye platform
PSA	Production Sharing Agreement
SEIC	Sakhalin Energy Investment Company
SEW	Sakhalin Environmental Watch
WGWAP	Western Gray Whale Advisory Panel
WSC	Wild Salmon Center
WWF	World Wildlife Fund
UN	United Nations

# Executive Summary

The Sakhalin 2 project on the Russian Island Sakhalin is one of the world's largest oil and gas projects. It is run by Sakhalin Energy Investment Company Ltd (SEIC) with the majority owner Royal Dutch Shell. The project threatens the rare whale species the Western Grey Whale. Add to this is also the issue of indigenous peoples who suffer because of the project and heavy environmental impact of over thousand water sheds and two sea bays. SEIC says that it follows environmental law and international guidelines, but the investigations in this report show that this is not the case. The Nordic business involvement in Sakhalin 2 project is big. This SwedWatch report is done in cooperation with Norwatch and FinnWatch as well as Swedish Nature Conservation Society for Nature and Friends of the Earth Sweden. It is the first collaborative study between SwedWatch, FinnWatch and Norwatch. The question which the report elaborates on is what environmental and social responsibility the Nordic contractors have. Sakhalin Island is located in the Northeast of Russia, just North of Japan. Sakhalin Island is blessed with a rich and comparably untouched natural environment. The Russian oil company Rosneft has extracted oil in North Sakhalin for 70 years, but since the mid 90ties international oil multinationals like Shell, BP and Exxon have been standing in line to explore the oil and gas reserves onshore and off shore. There are at the moment at least six planned oil and gas development projects off Sakhalin. A researcher from SwedWatch visited the Island for one week and met with companies, local authorities, citizen groups, environmental groups and indigenous peoples.

Phase two of the Sakhalin 2 project is a 20 billion USD project including the construction of two 800 km pipelines across the island in order to export oil and gas all year around, a liquid natural gas (LNG) plant and two new offshore platforms. Phase two of the Sakhalin 2 project threatens to drive the Western Pacific Gray whale to extinction. It also threatens some precious wild salmon species; it means dumping of dredging material in Aniva bay and causes risk of oil spills and leakages in a sensitive nature. This venture has enormous consequences for the people living on Sakhalin and for natural environments both onshore and in the sea. A critical movement consisting of indigenous people, environmental movement and local citizens' groups have joined forces against the companies' behaviour during their operations.

Sakhalin 2 attracts contractors from all over the world, including Nordic companies. Swedish-Swiss ABB has three ongoing million dollars contracts. Norwegian Aker Kvaerner and Finnish Quattro Gemini have built two concrete basements to two platforms with the help of SWECO and Swedish Consafe Offshore will deliver service rigs to the platforms. Nordic involvement in Sakhalin II is, in total worth over 566 million USD. Aker Kvaerner, Quattro Gemini and ABB offer leading competence in the special area that SEIC require for and in that respect these companies are crucial for the development of Sakhalin 2. None of the Nordic contractors that SwedWatch have been in contact with have put any environmental or social demands upon SEIC, but several of them express that they believe that SEIC is taking on an environmental and social responsibility.

Since the project cost has doubled from 10 billion USD to 20 billion USD many have questioned the economic viability of the project for Russia, especially for Sakhalin and its people. The Sakhalin 2 project is operated under a Production Sharing Agree-

ment (PSA) between the Russian federal government and SEIC. The Audit Chamber of the Russian Federation has concluded that “the Sakhalin II PSA is extremely disadvantageous” for Russia.

SEIC have tried to secure a loan from the European Bank for Reconstruction and Development (EBRD). EBRD have evaluated the project for three years and have found breaches of its environmental policy and pushed for a better Environmental Impact Assessment as well as better practice. SEIC’s final social and health impact assessments (ESHIA) was not ready until November 2005, when more than half of the project was already constructed. This fact is heavily criticised by international environmental movements. In December 2005, EBRD finally announced that the bank considered the Phase Two of the Sakhalin 2 project to be “fit for purpose of consultation”. After a 120-day period of public consultation, the Bank will make the final decision whether to support the project financially or not. The decision of EBRD will be very important, since many other financiers are anticipated to follow the same decision. There are representatives from all the Nordic governments in the Board for EBRD. The Swedish Ministry of Finance has expressed their concern over the projects immense environmental effects.

The local organisation Sakhalin Environment Watch (SEW) is an independent non-political NGO created in 1996. Sakhalin Environment Watch has created a global network to campaign about Sakhalin 2, including Friends of the Earth International, World Wide Fund (WWF), Greenpeace, Pacific Environment, CEE Bankwatch Network, International Foundation of Animal Welfare (IFAW) and Wild Salmon Center. The oil and gas pipelines will cross around 1100 water sheds on its way from North to South. Sakhalin Environment Watch (SEW) has shown with pictures from spring and autumn of 2005 that salmon has been negatively affected by the sedimentation. SEIC has been forced to many changes in design and to implement erosion technics and monitoring teams etc. According to both Wild Salmon Center and SEW, SEIC has already contravened several important points for adequate action regarding river crossing methods. The company states that the criticism is unfair to the majority of the project and promises enhanced supervision.

The population of The Western Pacific Gray Whale (*Eschrichtius robustus*) consists of only about 100 individuals. The Western Gray whale’s principal summer feeding area is off Sakhalin Island, just by the oil and gas platforms. In particular, the PA-B platform of SEIC’s project is just seven km off the feeding ground of the whales. In 2004 The World Conservation Union was invited by SEIC to put together an Independent Scientific Review Panel (ISRP) that would conduct a review of the possible effects on the Western Gray whale from the Phase two construction. In February 2005 the expert panel came to the conclusion that there is a risk that the population of the Western Grey whale will not recover, even with no additional threats, but this is increased substantially because of the Phase Two construction. After the ISRP expert panel published their report, SEIC decided to change the undersea pipeline route so that the pipeline does not run right through the feeding area for the whales. SEIC however did not change its plan to go on installing the PA-B platform during the summer of 2005, against the recommendation of the panel. According to SEIC the company has spent about seven million USD on the Western Gray whale research in 1997-2005. 35 NGOs including WWF, SEW, Greenpeace and Friends of the Earth International argue that SEIC’s decision to install the PA-B concrete base violates the precautionary principle.



In Aniva Bay in the South of the island SEIC is busy constructing one of the biggest liquid natural gas (LNG) plant in the world including an Oil Export Terminal and a LNG jetty. SEIC have deposited all the dredging material from the construction in the middle of the Aniva Bay. According to Sakhalin Environmental Watch (SEW) and the local group Knowledge is Strength the dumping has had huge negative impact on the ecology of the bay. The organisations claim that the result of the dumping already had great damage to fish, scallop, crab, shrimp and other valuable resources. In January 28<sup>th</sup> 300 people from the local fishermen and citizens protested against the environmental destruction by the project and claimed that the calculation for compensation for lost fish stocks should be recalculated. One of the absolutely biggest long term risks connected with the project is the risk of oil spills. The weather conditions are extremely harsh and accidents are usual around Sakhalin. As the platforms are in a sea which is covered with ice approximately half of the year it is extremely difficult to clean up an oil spill in such an environment.

In addition to the environmental consequences there are also several negative consequences for the people of Sakhalin, not at least for the indigenous people. The Nivhk is the biggest group. In total the indigenous people of Sakhalin consist of more than 3 000 people. Approximately 30 percent of the indigenous peoples live in the Nogliki District, in North East of Sakhalin Island. SwedWatch met with them in October 2005 and they all complained about their problems with the oil companies. Some of them say that the inner organs of the fish do not look the same anymore. They also state that they nowadays can get the taste of some oil from the fish. In January 2005 a storage of pipelines for SEIC and Exxon was made on the graveyard of the indigenous people. After that the indigenous people protested and SEIC were forced to start negotiations. The Southern Korsakov district is involved in the project since both the LNG plant and some of the pipeline is built in this district. There is a strong anger in Korsakov against the construction. SwedWatch met with local people who affirm that their living environment is much worse now than before. There have been several public manifestations against SEIC on the Island.

Jim Niven, Deputy External Affairs Manager, SEIC, informs SwedWatch that SEIC has not yet been sued for any case even though he admits that there are many ongoing cases in courts. He does not want to comment on these. SwedWatch have however found two cases where SEIC have actually been filed and fined for acting in breach of the Russian legislation. This was considering environmental issues in 2002 and 2003. In 2005 the Department for Natural Resources was the plaintiff who got fined, because SEIC had not done proper public consultation before building the Temporary Jetty in Aniva Bay.

These lawsuits demonstrate that the Sakhalin 2 project lacked legal compliance. The decision to reroute the undersea pipeline in order to not cross the feeding area of the whales shows that SEIC did follow the precautionary principle, but the decision to go on with the installation of platform PA-B just seven km away from the feeding area and despite ongoing research, must be seen as a breach of the precautionary principle.



The conclusion in this report is that SEIC have acted in violation of the international guidelines that it says it will follow. When Swedish, Norwegian and Finnish firms do business with SEIC and help to construct the project, there are good reasons to argue that these firms have a co-responsibility for the affects of the project. The report demonstrates that the Nordic contractors have failed to show that they care about the social and environmental consequences of the Sakhalin 2 project. Even though they know about the controversial issues, they have not made any demands upon SEIC so far.



# Introduction

There is a drama going on at the moment on the Russian Island Sakhalin, situated North of Japan. The main actors consist of the big multinational oil companies on one side and the local citizen groups and local and international environmental movements on the other. What is “Development” and who defines it?, What is the correct balance between doing business and doing good for society and for nature?

Sakhalin Island is blessed with a rich and comparably untouched natural environment. Although the Russian oil company Rosneft has extracted oil in North Sakhalin for 70 years, it was not until the mid 90ties that Sakhalin opened up for foreign investments. But since then international oil multinationals like Shell, BP and Exxon have been standing in line to explore the oil and gas reserves onshore and off shore. There are at the moment at least six planned oil and gas development projects off Sakhalin. Exxon and Shell have both started production of oil already and Shell is now in the middle of the construction of a 20 billion USD project to build a pipeline across the island in order to export oil and gas all year around. This venture has enormous consequences for the people living on Sakhalin and for natural environments both onshore and in the sea.

Shell's project, Sakhalin 2, attracts contractors from all over the world, including Scandinavia. Swedish-Swiss ABB has three ongoing million dollars contracts. Norwegian Aker Kvaerner and Finnish Quattro Gemini have built two concrete base-ments to two platforms with the help of the Swedish consultant firm SWECO and Swedish Consafe Offshore who will deliver service rigs to the platforms.

At the same time a critical movement consisting of indigenous peoples, environmental movement and local citizens' groups have joined forces against the companies' lack of social and environmental concern during their operations. The criticism is massive and disparate. It consists both of voices against the risk of destroying immense natural resources forever as well as the voices from citizens who can no longer stand the noise of the thousands of lorries going through their town. Many local people ask themselves what benefit the project will bring to them. They see their local environment destroyed by pollution from construction of oil and gas development, but many of them do not even have permanent heating of their homes yet. Anger is growing that the foreign companies and the government in Moscow takes all of the revenues from the oil and gas development. The Sakhaliners risk to be left with polluted shores and eroded forests.

There are many things at stake: accusations of bribery, court rulings showing that some of the companies have not bothered to follow local law, contractors have stored pipelines on the graveyards of indigenous peoples' and the risk of making the Western Gray whale extinct. But on the other hand we have companies who maintain that they work with the best practices, follow the law and are doing business to high ethical standards.

In this report the accusations and the defence of the companies will be scrutinized and investigated. The investigation will be concentrated on the Sakhalin 2, phase two-project because it is the biggest investment and the most controversial project from the environmental and social point of view and also because it is the project

with most involvement from Nordic contractors. The responsibility shown by Scandinavian companies involved as contractors will especially be checked. Do they have a responsibility for selling their service and products to this and other controversial projects? What could they do to demonstrate social and environmental responsibility?

## Methodology

This report is the first collaborative study between SwedWatch, FinnWatch and Norwatch. SwedWatch is the responsible publisher of the report, but FinnWatch and Norwatch have contributed financially as well as with input to the text. The report will be published in Sweden, Finland and Norway at the same time.

A researcher from SwedWatch visited the Island for one week in October 2005 and met with companies, local authorities, citizen groups, environmental groups and indigenous peoples. In addition to the visit to Sakhalin, SwedWatch have collected information from organisations, experts, companies' representatives, printed material and authorities from august 2005 – January 2006. The source of the information is clearly marked in footnotes and can be found in the reference list in the end of the report.

During the visit to Sakhalin there where several interviews conducted including Jim Niven, Deputy External Affairs Manager at Sakhalin Energy Investment Company (SEIC), Dmitry Lisitsyn, chairman of Sakhalin Environmental Watch (SEW), Alexey Limanzo, President of the Association of Indigenous Peoples of the North of Sakhalin Region, Andrey Nagibin, chairman of political Green party and leader of the NGO "Green Patrol", Elena Dmitrievna Nevenchina, specialist of Oil and Gas Department of Sakhalin Administration, Valentina Prokoshina, local journalist, Deputies from the Sakhalin Regional Sanitary Service, members of the Korsakov citizen group "Knowledge is Strength", Galina Nikolaevna Panchenko, ecological inspector of Nogliki fish protection service, Victor Sereda, the Mayor of Nogliki and meeting with indigenous peoples.

SwedWatch also had the opportunity to visit pipeline construction for one and a half days and visited the capital, Yuzhno-Sakhalinsk, as well as the North district of Nogliki.

In November 2005 SwedWatch visited ABB's headquarters in Västerås to conduct a lengthy interview with Halvor Molland, Senior Vice President Communications and public affairs, ABB Norway, Curt Henricson, Head of Sustainability Affairs at ABB and Gunnel Wisén Persson, Sustainability Controller at ABB Sweden.

Both SEIC and ABB have read the report in advance and SwedWatch has also offered them the opportunity to comment the report in written. SEIC has done so, but ABB has declined.

# Chapter 1. Background

## Sakhalin Island

Sakhalin Island is located in the Northeast of Russia, just North of Japan. Sakhalin is the largest island of the Russian Federation, 948 km long, and 25 to 170 km wide, with an area of 76 400 km<sup>2</sup>. As a comparison, Sweden is 1 572 km long and covers an area of 449 964 km<sup>2</sup>. There is a rich natural environment both on land and off shore. The Sakhalin region is the third largest producer of fish products in the Russian Far East. The fish industry makes up a third of the island's income. A substantial part of the land is mountainous and the highest peak is 1 909 metres high.<sup>1</sup> A big part of the island is covered with taiga forest, dominated by spruce and fir trees. The watersheds of the island are biologically rich and diverse. Species of Pacific salmon, including pink, chum, masu-cherry, coho, and Sakhalin taimen spawn here.<sup>2</sup> Sakhalin has more than 6 000 watersheds and 1 600 lakes. In Sakhalin's forests, wetlands and grasslands there are more than 700 types of insect and over 350 species of birds.

The climate differs a lot between the northern and the southern parts of the island. The average monthly temperature in January ranges from minus 19.7°C to minus 23.3°C in the north and from minus 9.7°C to minus 13.7°C in the south. Winter on Sakhalin lasts from five to seven months and summer from two to three months. The island's population has grown to 645 000 inhabitants 2004, a majority of whom are ethnic Russians, followed by Koreans (five percent). The island is home to 170 ethnic groups.<sup>3</sup> The native inhabitants consist of the Nivkh, Oroch, Evenk and Nanai. Some of the indigenous peoples in the North still mainly support themselves by fishing and hunting.

The capital, Yuzhno-Sakhalinsk, a city of about 200 000 inhabitants, has a large Korean minority, many Koreans were forcibly brought to work in coal mines by the Japanese during World War 2. Most of the population lives in the southern half of the island, centred mainly around Yuzhno-Sakhalinsk and two ports, Kholmsk and Korsakov with a population of approximately 50 000 each.

The island was a tsarist prison colony during 1858 until 1906. In 1890 the famous author Anton Chekhov visited the island and made a survey and showed the brutal daily life of the island's prison population.<sup>4</sup> In 1905 the Tsarist government lost the Russian-Japanese war and the southern part of the island was taken over by Japan. The Japanese controlled the south part of Sakhalin until the end of World War 2. The Sakhalin Region, in its present form, was officially defined and integrated as a part of the Soviet union in 1947. Sakhalin Island was again used for prison penal camps during USSR rule.

### **The history of the oil and gas reserves in Sakhalin**

Major deposits of oil were found by geologists from the Soviet oil company Rosneft-Sakhalinmorneftegaz in the 70's. Before that, Rosneft-Sakhalinmorneftegaz's predecessor, the Sakhalinneft group, had started developing the Northern Sakhalin oil deposits as early as 1928.<sup>5</sup> After the collapse of the Soviet Union, the economy was liberalized and Sakhalin experienced an oil boom with extensive petroleum exploration and mining by most large oil multinationals. During the 1990's, all oil and gas development projects were onshore facilities.

Today the multinational oil and gas companies have to search for oil in ever more remote areas.<sup>6</sup> The Arctic is one of the regions that the companies are looking at with increasing interest, although it comes with increasing challenges as well. Sakhalin has an arctic climate and the island is located in the middle of a typhoon area. All platforms have had to be specially designed to withstand massive ice, heavy weather as well as earthquakes that frequently shake the island.

## Oil and gas development projects

There are now more than six different offshore oil and gas extraction and production projects in various stages of development outside the coast of Sakhalin. The projects are called Sakhalin 1, 2, 3, 4, 5 and 6. They are run by Russian oil and gas companies as well as some of the world's biggest oil companies, including Shell, BP and Exxon-Mobil. The Sakhalin 2 project, led by Shell, was the first off shore oil and gas project in Sakhalin, followed by Exxon led Sakhalin 1 project. Both Sakhalin-1 and 2 are done within Production Sharing Agreements (PSA) with the Russian government.<sup>7</sup> PSA's are made between the investor and the state and regulates the terms and conditions for the exploration and development of the resources. One of Russia's oldest oil and gas companies, Rosneft, is involved in most of the projects (1, 3, 4, 5 and 6).

The main operator of the Sakhalin 1-project is Exxon Neftegas Ltd, which is an affiliate of ExxonMobil.<sup>8</sup> Exxon Neftegas is going to explore oil and gas resources from three fields outside the North East coast of Sakhalin Island. Exxon Mobil announced the company's first oil and gas production from the Chayvo fields in 2005. The total project cost is estimated to be around 12 billion USD.

The Sakhalin 2 project is run by Sakhalin Energy Investment Company Ltd (SEIC), a consortium with Shell as the majority owner. The Sakhalin 2 project is covered in detail later in this report.

The major operator for the Sakhalin 3 project is Rosneft with 75 percent; the minority owner is a regional state unitary enterprise, Sakhalin Oil Company, which owns 25 percent. In 2003 Rosneft got a 5-year exploration license. The project has completed ecological and fishery works.

Rosneft also obtained two exploration licenses for both Sakhalin 4 and Sakhalin 5 in December 2003. Both of these projects are operated together with British company BP.<sup>9</sup> The Sakhalin 5 project have two owners, Russian Rosneft with 51 percent and British company BP with 49 percent.<sup>10</sup> BP and Rostneft have an alliance on Joint Interest Areas. The companies are currently doing seismic surveys and the drilling of exploration wells for both Sakhalin 4 and 5.

The Russian oil company Petrosakh plans to explore the oil-and-gas field in the Sakhalin 6 coastal shelf zone.<sup>11</sup> Petrosakh have completed a seismic survey and got a license to drill two test wells for the Sakhalin-6 project.<sup>12</sup> The company will report about the test drilling in 2006. It intends to bring together several international investors to develop Sakhalin 6.

The Oil and gas department at Sakhalin was established in 1994. The task of the department is to control oil and gas business and industry and present the interest of the region *oblast*<sup>13</sup>. Elena Dmitrievna Nevenchina, specialist at the Oil and Gas



Department of Sakhalin Administration, tells SwedWatch that all oil and gas companies need to obtain the license from the department before they start geological investigations. The companies also need to consult with the ecological service before getting permission for project operations. After that the companies will need to consult with all interested institutions in order to get the final license to be allowed to use the natural resources.

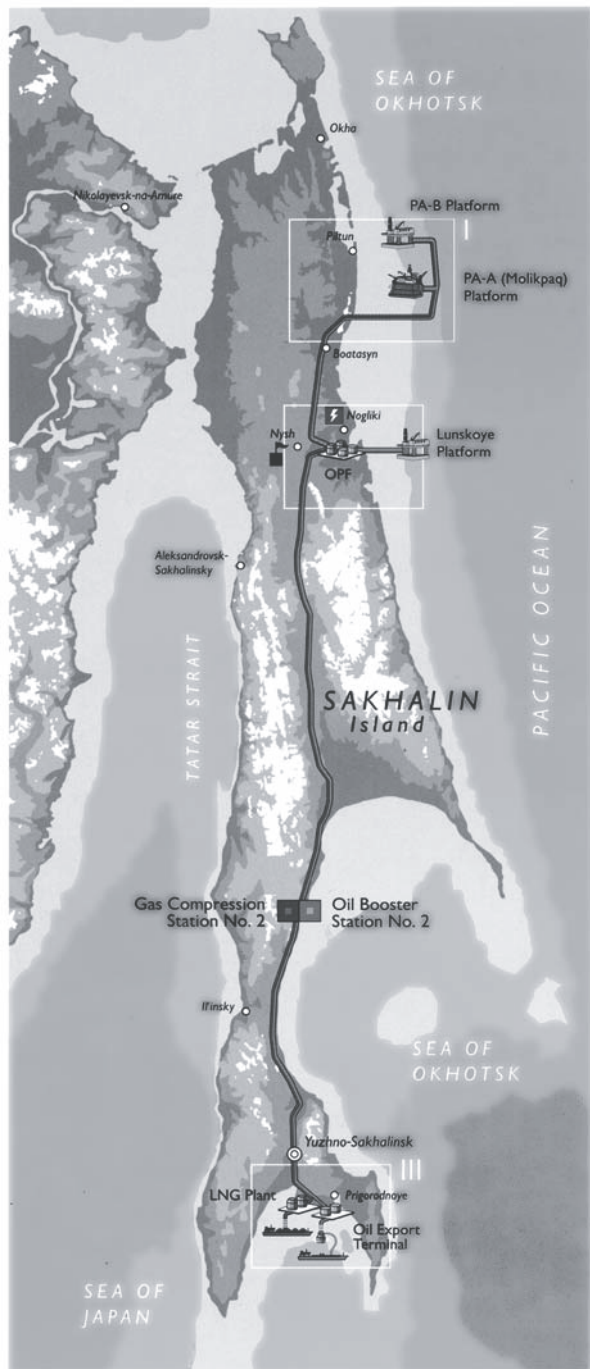
Elena Dmitrievna Nevenchina says that in Russia there is a law to preview the damage before the start of the project. She says that all of the international companies do not agree with this idea.

“Exxon could not understand why they should pay money in advance; they say “not even one fish has died yet”, but we have a special method where we count expected damage. Any construction work in the oil and gas business will cause damage”, says Elena Dmitrievna Nevenchina.

She believes that the oil and gas industry should be developed further in this respect. “It leads to employment opportunities in the North of Sakhalin. If you decided to close down the whole industry, what would happen? The North districts live off the oil industry”, says Elena.

30 percent of the economy comes from oil and gas industry in the Nogliki district, in the North of the Island. But Elena is not uncritical of the way the oil companies operate on the island.

“Usually the construction companies break the laws and the building regulations and this cause soil damage and water pollution. I like the organisations which make the oil and gas companies to comply strictly with the laws”, she says.



## Chapter 2. Sakhalin 2

The Sakhalin 2 project is one of the world's largest oil and gas projects run by Sakhalin Energy Investment Company Ltd (SEIC) with the majority owner Royal Dutch Shell. SEIC has been pumping oil from one platform during the ice free season since 1999. The second phase will allow year-round oil and gas production and export. Phase Two also includes the construction of Russia's first liquefied natural gas (LNG) plant, two new offshore platforms and two 800 kilometre onshore pipelines.

Since the project cost has doubled from 10 billion USD to 20 billion USD many have questioned the economic viability of the project for Russia, especially for Sakhalin and its people. SEIC have tried to secure a loan from the European Bank for Reconstruction and Development (EBRD).<sup>14</sup> EBRD have evaluated the project for three years and have found breaches of its environmental policy and pushed for a better Environmental Impact Assessment as well as better practice. At the same time Shell announced a record year 2005. Annual profits after tax have reached about 17.5 billion USD, which is a rise of 55 percent on 2004 figures.<sup>15</sup>

### Background and presentation

In 1991 a tender for the right to conduct a feasibility study for the development of Piltun-Astokhskoye and Lunskeye oil fields was won by a consortium with the Japanese company Mitsui.<sup>16</sup> This consortium was later joined by Shell and Mitsubishi. Shell, Mitsui and Mitsubishi created Sakhalin Energy Investment Company Ltd (SEIC) in April 1994 and a Production Sharing Agreement (PSA) was signed in June 1994 between SEIC, The Russian Government and The Sakhalin Region Administration. SEIC is registered on the Bermuda Islands. Since year 2000 Shell owns 55 percent of the shares, Mitsui owns 25 percent and Mitsubishi 20 percent.

SEIC is developing two fields which together contain recoverable volumes of over one billion barrels of crude oil and more than 500 billion cubic meters of natural gas. Phase One started with the installation of the "Molikpaq" platform 1998 which already has gone into seasonal production since 1999, while Phase Two is still being developed.

The sea around the Northern coast freezes for half the year, stopping tankers from reaching the offshore platform. This makes it impossible to load oil and gas to tankers in the winter season. The idea of Phase Two of the project is to be able to export oil and gas the whole year around. That is why SEIC decided to build an 800 km long pipeline across the Island to Aniva Bay in the South, where the sea is ice free throughout the year. There are two pipelines which are going to be built alongside each other, one for oil and one for gas. See figure 1.

"What we are doing is taking oil and gas from the north, taking it to the south and exporting it," says Jim Niven, Deputy External Affairs Manager, SEIC.

SEIC is building one of the world's biggest liquefied natural gas (LNG) plant at Prigorodnoye, by Aniva Bay, where it will export the LNG and the oil from two export terminals, one for oil and one for LNG. Phase two also involves the installation of two more platforms; The Piltun-Astokhskoye-B Platform and the Lunskeye Platform.

The new platforms and the old "Molikpaq" platform will all be linked to the shore by



pipelines. Phase Two also involves the construction of an onshore processing facility (OPF) where the gas will be processed and condensate extracted before transport to the south.

The deliveries of first LNG are scheduled for the summer of 2008. 75 percent of the capacity of the LNG is already sold to customers mainly in Japan, Korea and also in USA.<sup>17</sup> SEIC indicates that the Phase two project is around 60 percent complete at the end of 2005.

## The economic liability of the project

In July 2005 Shell announced that Sakhalin 2 Phase Two project costs were anticipated to amount to 20 billion USD.<sup>18</sup> That is twice the calculated cost at the beginning of the project. The Sakhalin 2 project is operated under a *Production Sharing Agreement (PSA)* between the Russian Federal Government and SEIC.<sup>19</sup> The PSA states that the government retains its rights and ownership of the oil and gas resources, but gives the right to the company to explore the oil and gas resources. In the PSA it is defined what sort of payments (bonuses, royalties and reimbursements) should be made for this right. It was agreed that taxes should be paid only after the project had started to give profit, which will most probably not be the case within the coming seven years at least.<sup>20</sup> According to Dr Ian Rutledge, an energy economist who analysed the PSA for Sakhalin 2, the original profit-sharing agreement was quite disadvantageous to the Russians.<sup>21</sup>

In the Production Sharing Agreement between SEIC and the Russian government it was decided that SEIC should pay a royalty of six percent of the oil and gas produced to the Russian government throughout the lifetime of the project. According Dr Ian Rudledge, the royalty level is quite low by international standards. "Among the countries which use PSAs and where the field size and production levels are comparable to those in Sakhalin, royalty rates generally fall within the range 10 – 20 percent".<sup>22</sup>

The Federal Government of Russia and the Administration of Sakhalin Oblast, two levels of government, negotiated amongst themselves on how the revenues from the project should be divided between federal and regional levels. The original split, in 1997, was that 60 percent of the Royalties for the utilization of mineral deposits would go to the local region and 40 percent to national federal level; reimbursements for the geological surveys and exploration etc, would be shared equally between the Sakhalin Region and the Federal side.<sup>23</sup> It was also decided that Sakhalin Oblast should receive some 22 percent of a total of 32 percent in taxes on the profits. All of this was estimated to give a substantial benefit to the Sakhalin Region, maybe some 25 billion US dollars over the 30-40 year duration of the project.

According to the local environmental organisation Sakhalin Environmental Watch (SEW), the benefits for the Sakhalin Island were gradually lowered due to a series of decisions from both the Sakhalin Oblast and the Russian Federal. SEW quotes a decision in the Sakhalin Oblast where the Oblast decided to free SEIC and all its contractors "from any and all taxes or collections of any other required payments, which once were to be made to the Oblast."<sup>24</sup>

The State Tax Services for Russia reacted to this decision and have stated that this decision was actually "unacceptable", since the agency estimates the lost revenues

for the region will amount to some 954 million US dollars over the course of the Sakhalin-2 project. Then, SEIC and all its affiliates and contractors were freed from all the municipal and county-level taxes for the project as well. Only the Deputies of the City Council for the city of Yuzhno-Sakhalinsk refused to take such a decision.

The other main issue was that the original agreement that the Sakhalin region should receive 60 percent of the royalties was changed and lowered gradually so that in December 2004, it terminated totally. The Russian Federal Government decided that the federal government should receive all royalties from mineral deposits from the sea.

“Sakhalin Island has thus been absolutely deprived of all income from this project, despite the fact that it is operating on Oblast territory. The only exceptions are the small payments of land - rents into several municipal treasuries, and payments of local taxes into the budget of Yuzhno-Sakhalinsk.”

Letter to EBRD from Dmitry Lisitsyn, Chairman of Sakhalin Environment Watch, 2005-07-11.

When SwedWatch confront SEIC with these facts Jim Niven, Deputy External Affairs Manager, SEIC, says:

“To be very frank, it is not up to us as a company to decide that split (between the federal government and the regional government). It is very much the matter for the authorities to decide.”

Jim Niven does not agree that the Sakhalin region will get only small benefits from the project.

“There are a lot of payments that are paid here locally so it would be very wrong to suggest that we do not contribute financially as well as socially to the Island,” says Jim Niven.

He mentions that SEIC have paid 100 million USD to the Sakhalin Development fund and that the company contributed to upgrading the infrastructure on the island to the equivalent of over 300 million USD. SEIC has also promised that it will undertake to achieve 70 percent Russian content (including labor, material, equipment and contract services) over life of the entire Sakhalin Project.<sup>25</sup> The company also claims that Sakhalin receives a lot of employment opportunities, although critics argue that this is mainly true during the construction phase. At the peak construction period, between 2004 and 2006, approximately 17 000 people will be employed on the Island. Jim Niven at SEIC agrees that the main period for job opportunities is during the construction phase.

“In the long term we estimate that we will need around 1 500 long term employees at SEIC and around 900 will be full time contractor working staff,” he says.

In October 2005 the Audit Chamber of the Russian Federation made an evaluation of the report of the Russian Government “On the Outcomes of Work for the Preparation and Realization of the Production Sharing Agreements (PSA) for 2004”. Auditor Alexander Beliakov told a correspondent from FK-News that “The production sharing agreement, ideally, should be profitable for our country and for the international

investor. Unfortunately, in practice the situation looks otherwise, and our country in the parameters of the Sakhalin 2 PSA is sustaining losses in the billions”.<sup>26</sup> The conclusion of the auditors report was that “the Sakhalin 2 PSA is extremely disadvantageous”.

## Difficulties meeting standards

So far the huge investments for the Sakhalin 2 -project have been made by the shareholders of SEIC; Shell, Mitsui and Mitsubishi. But SEIC have for several years applied for credits from both public and private banks. The most important credit from the European Bank for Reconstruction and Development (EBRD) is still pending. Most other banks, like the Japan’s JBIC and US Export-Import Bank are expected to follow the decision from EBRD. A credit to the phase one of the Sakhalin 2 project was already decided in 1997 by EBRD.<sup>27</sup> This credit was equivalent to 116 million USD.

EBRD has worked with SEIC since 2002 to bring the company’s environmental, social and health and safety impact assessments of Phase Two into line with the requirements of the EBRD Environmental Policy.<sup>28</sup> The bank has postponed its decision many times, because new facts about environmental issues have come up.

In December 2005, EBRD finally announced that the bank considered the Phase Two of the Sakhalin 2 -project to be “fit for purpose of consultation”.<sup>29</sup> During January to April 2006 the bank will collect input from the community, NGOs and other parties involved. After this the EBRD Board of Directors will make the final decision whether to finance Phase Two or not.

EBRD is quite critical about SEIC’s original Environmental Impact Assessment and the bank state that the EIA was not up to standard: the company had not, for example, been sufficiently concerned about the impact on the Western Pacific Gray whale and EBRD has demanded extensive improvements concerning the river crossings of the pipeline. EBRD also conclude that the decision from SEIC to choose the site of the Platform The Piltun-Astokhskoye-B Platform “was not in conformity with the policy”.<sup>30</sup> The EBRD also criticise SEIC’s dumping of dredging material into Aniva Bay (see below). EBRD officials uses the argument that the bank should finance phase two in order to keep the pressure on SEIC in regard to environmental issues extensively, even though SEIC have breached the policies of the bank in the past.<sup>31</sup>

It has not yet been determined what amount of financing the EBRD would provide if the Board eventually approves financing for the Sakhalin 2 project. The President of EBRD, Jean Lemierre has mentioned a sum of around 200 - 300 million USD.<sup>32</sup>

There is a broad NGO coalition that campaigns against EBRD’s possible financing of the Sakhalin 2 project. These NGOs were disappointed that the bank did not turn down the credit in the decision the bank made the 14th of December.<sup>33</sup>

“Today the EBRD has risked damaging its reputation severely by pronouncing that Sakhalin 2 is fit for purpose even though key aspects of the project are beyond repair,” said Dmitry Lisitsyn, Chairman of Sakhalin Environment Watch, following EBRD’s announcement. SEIC’s CEO Ian Craig, on the other hand, welcomed EBRD’s announcement in a press release by the company.<sup>34</sup>

It is the Board of Directors of EBRD which will eventually take the final decision whether or not to finance the Sakhalin 2 project. Finland, Norway and Sweden have two directors in the board that will have a vote.<sup>35</sup> The directors will consult their respective Minister of Finance who are governors in EBRD. On a recent meeting about EBRDs possible finance of the project in Stockholm, the State Secretary of the Swedish Ministry of Finance, Jens Henriksson, stated clearly that the Swedish government finds the project very controversial in many ways.<sup>36</sup>

The EBRD's environmental policies include a "mandate to promote environmentally sound and sustainable development". According to several international and local NGOs the Sakhalin 2 project does not live up to this fundamental policy requirement.<sup>37</sup>

To conclude: Sakhalin 2 is one of the world's largest oil and gas development projects which will have -and already has- grave consequences on economy, nature and social welfare. Several experts have questioned if the Production Sharing Agreement that Russia has negotiated with SEIC really brings enough benefit to Russia and especially to the Sakhalin region. SEIC have asked for public and private funding, and the decision of the European Bank for Reconstruction and Development (EBRD) that is to be taken in March 2006 will be important, since many other financiers are then anticipated to be ready to fund the project. NGOs also believe that it is a crucial decision, since EBRD will in a way give the Sakhalin 2 Phase Two project a "green stamp" if it decides to grant the project credit.

## Chapter 3. Nordic business involvement

The Sakhalin 2 project is a huge one and as such, contracts are signed with companies from all over the world. At the LNG Plant as well as the pipeline construction there are workers from all over the world present. Nordic business involvement is also quite big.

SwedWatch research demonstrates Nordic business contracts to be worth a total of some 566 million USD for Sakhalin 2. Several firms have not wanted to reveal the value of their contracts, but it would be reasonable to estimate that the Nordic involvement in Sakhalin 2 is, in total worth well over 600 million USD. It is also clear that Aker Kvaerner, Quattro Gemini and ABB offer leading competence in the special area that SEIC require and in that respect these companies are crucial for the development of Sakhalin 2.

### Swedish companies

#### **ABB**

Asea Brown Boveri (ABB) is a Swiss-Swedish multinational company with 103 000 people employees in around 100 countries.<sup>38</sup> The company works within power and automation technologies in five different main divisions. In Sakhalin ABB is mostly involved through ABB Automation which includes business contracts for drives, motors and generators, low voltage products, instrumentation and analytical and power electronics. ABB has signed the UN Global Compact and sees itself as a leading company when it comes to Corporate Social Responsibility (CSR) issues internationally.

ABB has for the moment five known contracts in Sakhalin worth more than 170 million USD.<sup>39</sup> Three of these are for ABB's Automation business and two are for the ABB Lummus Global that supplies production facilities, refineries and petrochemical plants. ABB also has one contract for electric distribution for Sakhalin 1 which is worth around 23 million USD.

For Sakhalin 2 ABB has one contract for telecommunications worth around 42 million USD and ABB Lummus Global has a contract worth 100 million USD for upgrading the Molikpaq platform. In addition ABB has a contract worth five million USD to deliver drilling equipment. According to Halvor Molland, Senior Vice President Communications and public affairs, ABB Norway, ABB's contracts to the Sakhalin projects amount to around 2 - 3 percent of the total investment of Sakhalin 2.<sup>40</sup>

"If you see every contract by itself the telecom contract is big for ABB Automation in Norway, for ABB Lummus the upgrade of PA-A platform is a middle contract and the contract on drilling equipment is small. But overall, these contracts are rather small if you compare them with ABB's normal orders," says Halvor Molland.

Halvor Molland tells SwedWatch that when ABB Lummus first got the big contract for the engineering, procurement and construction of onshore processing and well site support facilities for Sakhalin 1 this was a really huge order. Currently ABB Automation is responsible for telecommunications for the platforms, the pipeline and

the LNG plant. The company is also responsible for the electrical distribution at the oil processing facility.

Halvor Molland says that ABB won these contracts because ABB has much experience in dealing with complex projects like this. He also explains that small firms cannot get these sorts of contracts because there is simply too much paper work and approvals that need to be in order. Halvor Molland says that ABB Automation is satisfied with SEIC as a customer.

“I have asked people within ABB and according to their information everyone I talked to seem positive about how SEIC handle the environmental and social issues. This was the feeling among the ABB employees at Sakhalin and the people ABB hired,” says Halvor Molland.

ABB did not carry out a formal risk assessment regarding the overall environmental and ethical risks of the whole Sakhalin 1 or 2 projects before they bid for the contracts. The reason for this was that these contracts were signed before ABB decided to include the overall aspect of a project in its own risk reviews, says Halvor Molland.

“We have only analysed the risk of our own part of the project,” says Halvor Molland.

He explains that this means that ABB investigated the health, safety and environmental risks for its direct involvement. Curt Henricson, Head of Sustainability Affairs at ABB however, tells SwedWatch that they are aware of the criticism of the project. “We follow the whale issue and other factors affecting the project.”

Gunnel Wisén Persson, Sustainability Controller in Sweden, says that it is just the last two years that ABB implemented a model for carrying out overall risk reviews on bigger contracts. SwedWatch has asked for sight of ABB’s risk review model, but ABB state that it is internal and is being updated at the moment. Gunnel Wisén Persson and Curt Henricson both say that ABB would again bid for the contracts for Sakhalin 2, if they did a risk analysis following the model ABB use nowadays to evaluate projects.

“We would have checked the Environmental Impact Assessment and all the material available, but everything would probably have been without remarks. The criticism has been piling up continuously which makes it more difficult,” says Gunnel Wisén Persson.

Curt Henricson says that these issues are increasingly important for ABB and that it does happen that ABB refrain from contracts with controversial projects, because of ethical, social or environmental reasons. However he does not want to give any examples of ABB refraining from contracts, since these decisions may involve sensitive business secrets, according to Curt Henricson. ABB started its emphasis on corporate social responsibility by focusing on social and environmental aspects of its own manufacturing sites and is now expanded it to include its involvement in customer projects, he says.

### **Consafe Offshore**

Consafe Offshore AB operates in the offshore oil and gas sector and has its headquarters in Gothenburg in Sweden.<sup>41</sup> The company offers offshore support services,



through its accommodation and construction support service fleet, to international oil and gas companies. The Company was founded in 2000 by Christer Ericsson through the JCE Group. JCE Group is the majority owner of Consafe Offshore.

The Consafe Offshore Group fleet consists of four offshore accommodation and construction support service vessels, one of them being Safe Bristololia which will be used in the Sakhalin 2 project.<sup>42</sup> Safe Bristololia will operate on both Lun-A and PA-B. Safe Bristololia is an accommodation vessel with the possibility to accommodate 550 persons totally.<sup>43</sup> The service for Safe Bristololia covers a period during 2006 to 2007. The first contract is worth 30 million USD.

Peter Jacobsson, CEO, Consafe Offshore AB, tells SwedWatch that one of the criteria for SEIC in selecting an accommodation vessel for the project was noise level.<sup>44</sup> “Due to the sensitivity of the whales in the area noise was a critical criterion. As our vessel does not have any propulsion or propellers we came out well in that part of the evaluation. There are many rules and regulations that need to be followed in relation to the whales,” he says.

Peter Jacobsson also tells that Safe Bristololia is an accommodation rig which takes care of all the effluent and waste without discharging anything to the sea. He is very familiar with the active environmental organisations on Sakhalin and says: “My impression is that the majority of the Sakhalin people welcome the project, but a balance needs to be found between the environmental movement and the economic interests. My impression is that SEIC takes care of this in a proactive manner.”

## **SWECO**

Sweco is a consultancy firm working in the fields of engineering, environmental technology and architecture.<sup>45</sup> Sweco employs around 3 600 people and carry out projects in more than 45 countries every year and the company has subsidiaries in Sweden, Finland and Norway

The Norwegian subsidiary Sweco Grøner has been active within a group of consultants which have done the planning for the part of the Sakhalin 2 project that concerns the Concrete Gravity Base Structure (CGBS).<sup>46</sup> Sweco did their work as consultants to the Norwegian company Aker Kvaerner. The project ran for two years from August 2003 to August 2005 and involved around 30 consultants from Sweco. All the consultancy work has been performed from Oslo, but during spring and summer 2005 around ten people from the Swedish subsidiaries Sweco VVB and Sweco Bloco was working in Sakhalin.

Sweco Grønors Project Manager, Paal Berg, informs SwedWatch that the project was mainly handled by Aker Kvaerner as the contractor for execution of the work in Russia. “Sweco Grøner, as a consultancy company, has not been able to influence environmental issues to any large degree and none when it comes to social issues since we were situated in Oslo.”<sup>47</sup>

Sweco has joined the Swedish Partnership for Global Responsibility, the Swedish Government’s answer to Secretary-General Kofi Annan’s Global Compact, which was initiated by the UN and Sweco claim that they strive to meet the highest standards of business ethics in all their operations.



## Finnish companies

### Quattro Gemini

The Finnish company Quattro Gemini built two concrete foundations for the oil and gas drilling platforms, so called Concrete Gravity Base Structure (CGBS) for the Sakhalin 2 project. The contract had a total value of around 234 million USD.<sup>48</sup> The contract started April 2003 and ended in August 2005. The structures were built in Nakhodka, some 150 km southeast from Vladivostok, and were later shipped to Sakhalin. Jouni Sipiläinen at Quattro Gemini informs SwedWatch that at the peak of the project the company had 2 500 staff and labour working on site, of which 2 350 were Russian.<sup>49</sup>

According to Jouni Sipiläinen, Quattro Gemini did not put any environmental or social demands upon SEIC before entering the contract. He writes:

“SEIC is very concerned about the Health, Safety and Environmental (HSE) matters and its HSE requirements were already included in tendering documents. On site we followed these SEIC HSE requirements and local safety and environmental legislation strictly. We and SEIC also supported the local communities to a remarkable extent.”<sup>50</sup>

### AIP-Surveying

AIP-Surveying is a consulting company whose services include industrial process measurement control, as well as all types of building construction, renovation and property related measurements and computations.<sup>51</sup> AIP-Surveying worked with the Sakhalin Concrete Gravity Base Structure (CGBS) Project for Quattro Gemini. This contract was the biggest order ever for AIP-Surveying.<sup>52</sup>

### Ramboll Finland

The Ramboll Group is a leading Nordic consultancy with more than 4 000 employees at over 70 offices.<sup>53</sup> The company offers services within the fields of engineering, management and IT. Ramboll Finland Oy is supplying expert services in geotechnics, geohydrology and drainage to the Sakhalin 2 project.

### RR Offshore

RR Offshore (RRO) serves the oil and gas industry, for example with offshore platforms, production skids, drilling rigs, and other offshore components.<sup>54</sup> RR Offshore provides detailed engineering, procurement, fabrication, outfitting, testing and commissioning required for refineries, production facilities, drilling rigs and vessels. RRO was a subcontractor to Aker Kvaerner and Quattro Gemini Oy in these companies works with the two Concrete Gravity Based Structures (CGBS) for SEIC up to the summer of 2005. RR Offshore's contracts for the Sakhalin 2 project were worth around 47 million USD.<sup>55</sup>

### Talhu Ltd

For more than ten years, Talhu has served in all fields related to equipping construction work with machinery.<sup>56</sup> Talhu's turnover in 2005 was more than 12 million USD. Quattro Gemini Ltd and Talhu Ltd had contracts to supply tower cranes to the Sakhalin's oil and gas production platform construction site. Delivery took place during August-October 2003. Talhu has also supplied groundwater lowering pumps, a three kilometer long pipe system and suction heads to Quattro Gemini's construction basin.

### **Rautarukki**

Rautarukki manufactures and supplies components and systems to the construction and mechanical engineering industries.<sup>57</sup> The company has a wide selection of metal products and services. Rautarukki has operations in 23 countries and employs 12 000 people. Rautarukki's Metal Products Division has signed two major contracts with the Sakhalin 2 project.<sup>58</sup> The contracts are worth approximately five million USD and consider the supply of steel products. This is the first order of Rautaruukki from the Sakhalin oil and gas development projects.

### **Steel-Kamet**

Steel-Kamet innovates, designs and implements production systems of concrete. Steel-Kamet delivered the concrete factories to Quattro Gemini for the building of concrete gravity base structures for the Sakhalin 2 project.<sup>59</sup> This transaction included two concrete factories, one large cement storage with a total volume of 1,600 tonnes and two Turbomatic energy plants for the heating of water and mineral aggregate. The contract was commissioned in the autumn of 2003 and ended in February 2004.<sup>60</sup> The value of the contract is confidential.

### **Kvaerner Masa-Yards**

The Finnish subsidiary of Aker Kvaerner, Kvaerner Masa-Yards, signed a contract with ExxonMobil in September 2003, operator of the Sakhalin-1 project in Russia and Far-Eastern Shipping Company PLC (FESCO), Russia.<sup>61</sup> The contract concerned design and construction of icebreaking vessels for the Sakhalin-1 project. One vessel confirmed to be delivered in May 2005 and the contract price was around 76.5 million USD.<sup>62</sup>

### **Exportum Ltd**

Exportum is a Finnish consultancy that works with services for Finnish companies who want to invest abroad.<sup>63</sup> In 2004 Exportum Ltd organised joint commercial efforts for Finnish companies to enable them to receive contracts from the Sakhalin 2 project.

## **Norwegian companies**

### **Aker Kvaerner**

Aker Kvaerner is a company with engineering and construction services.<sup>64</sup> The company's activities include Oil and Gas, Pharmaceuticals, Metals, Power, Chemical Pulp and Shipbuilding. Aker Kvaerner is a multi-local group of businesses with nearly six billion USD in annual revenues and around 34 000 employees in more than 30 countries. In July 2003 Aker Kvaerner won a major contract with SEIC.<sup>65</sup> The contract was worth around 150 million USD and concerned the building of the two platforms in the Sakhalin 2 Phase Two project in Russia.

Aker Kvaerner was considered by SEIC to be the company with most experience in the construction of concrete offshore platforms and field development in harsh weather environments.<sup>66</sup> The company have earlier developed and delivered these sorts of platforms both in the North Sea and offshore Canada. Aker Kvaerner's contract included engineering, procurement, management and project services for two platform substructures.

“This is a major milestone as Russia is a strategically important market to Aker Kvaerner. The new assignment will strengthen our position when competing for other projects both in the Sakhalin region and elsewhere in Russia,” says Helge Lund, CEO of Aker Kvaerner, in a press release in July 2003.<sup>67</sup>

The two concrete gravity base substructures (CGBS) delivered by Aker Kvaerner and Quattro Gemini were installed in the summer of 2005. The topsides of the platforms are currently manufactured in Korea and are planned to be fitted to the substructures from the summer 2007.<sup>68</sup>

### **Stolt Offshore**

Stolt Offshore designs, procures, fabricates, installs and maintains complete subsea pipeline and riser systems for the global offshore oil and gas industry.<sup>69</sup> 14 percent of Stolt Offshore is owned by Norwegian shareholders and Stolt Offshore is registered on the Oslo Stock Exchange and Nasdaq. Several Norwegian board members as well as senior employees are present in the company.

Stolt Offshore have a contract from Nippon Steel to work on the Sakhalin 1 project for ExxonMobil.<sup>70</sup> The contract value was \$10 million for so called SURF-work which stands for Subsea umbilicals, risers and flowlines and involves connecting the well to the production platform or ship. The Seaway Hawk is a specialist subsea construction ship that has been fully occupied on the Sakhalin project for Nippon Steel. Stolt Offshore was involved in this project earlier 2005 and the company will work more for the Sakhalin 1 project in 2006 as well.

### **TGS-Nopec**

TGS-Nopec is a Norwegian company which provides geoscience data, software and services to energy companies worldwide. The company licenses seismic data and offshore surveys conducted in more than two dozen nations and have employees on three continents.

The company has made a seismic survey north and east of Sakhalin Island in the Sea of Okhotsk Northeast of Sakhalin in 2004 and 2005.<sup>71</sup> According to TGS-Nopec this was the first modern, high-quality, dataset providing coverage in these areas.<sup>72</sup> TGS is planning for further acquisition in the area during 2006 and several years ahead. According to Erling Frantzen, Business Development Manager Russia at TGS-Nopec, most of the active oil companies in Sakhalin region are buying the company's surveys on licenses.<sup>73</sup> TGS-Nopec has so far made investments in the region above 10 million USD, according to Erling Frantzen.

Nordic business involvement in Sakhalin oil and gas projects are quite extensive, perhaps not in terms of total worth of contracts in comparison with total costs, but certainly in terms of specific and unique knowledge. Many of the Nordic companies have special competence that is indeed crucial for SEIC in order to run such a complex project in such a challenging environment. None of the Nordic contractors that SwedWatch have been in contact with have put any environmental or social demands upon SEIC, but several of them express that they believe that SEIC is taking on an environmental and social responsibility.

## Chapter 4. Environmental Issues

Phase Two of the Sakhalin 2 project is a construction with obvious risks of environmental damage. These contains four main issues; 1) the pipeline which crosses over 1 000 water sheds which effects the fish, 2) the platforms lies close to where the threatened Western Gray whale feeds, 3) the pollution of Anviva Bay from the construction of the LNG construction and 4) the risks of oil leakage and spills.

There are strong criticism from experts, public lenders and environmental organisations that international environmental conventions and guidelines are not followed by SEIC.

### Compliance with international guidelines questioned

SEIC states that it will follow both Russian Environmental Law as well as a wide collection of international conventions regarding environment.<sup>74</sup> For example it mentions “United Nations Framework Convention on Biological Diversity” from 1992 and the “Aarhus convention on the access to environmental information and public participation in environmental decision making” from 1998.<sup>75</sup>

The international guidelines that SEIC refers to in their Environmental impact assessment (EIA) are those of the World Bank and International Finance Corporation (IFC).<sup>76</sup> In addition to this SEIC does also have its own environmental policy, where the company for example states that “SEIC shall seek to prevent pollution and minimise environmental impact from existing and planned activities. This includes identifying environmental hazards and risks and implementing appropriate controls to ensure that the risks are reduced to a level ‘as low as reasonably practicable’ and that the company shall: “Require our contractors to manage environmental matters in line with this policy. “<sup>77</sup>

In 2003 IFC and ten international banks adopted the Equator Principles.<sup>78</sup> The principles are voluntary guidelines for managing environmental and social issues in project finance lending and are based on the environmental and social standards of the IFC. By the beginning of January 2006, the Equator Principles had been adopted by almost 40 banks, representing about 80 percent of project finance funds worldwide.<sup>79</sup>

The Equator Principles categorize different investment projects as relatively sensitive, where Category A is considered to be the projects which are most sensitive. Category A projects may have irreversible consequences to a major natural habitat. In these cases the Equator banks should ask for a completed EIA with specified demands. In 2004, the UK based NGO Platform, which among other things investigates the oil industry, carried out an analysis comparing the Sakhalin 2 project with the Equator Principles.<sup>80</sup> According to the organisation SEIC breached several of the Principles.

Following the report from Platform, a letter signed by 40 international NGOs was sent to the 22 banks who had signed the Equator Principle. The NGOs urged the banks not to finance the Sakhalin 2 project. According to BankTrack, a network of NGOs that tries to hold banks accountable for environmental and social issues, a number of Equator Principles signatory banks have already indicated that they will not fund Sakhalin 2.<sup>82</sup> Citigroup has adopted the Equator Principles and according

to Dmitry Lisitsyn, SEW, Citigroup refrained from giving any credit to Sakhalin 2 project because the bank considered the project to breach the Equator Principles.<sup>83</sup>

The American organisation Pacific Environment has also made a similar analysis comparing SEICs conformity with the environmental and social demands of The World bank and IFC.<sup>84</sup> This organisation also came to the conclusion that Sakhalin 2 Phase Two breaches the very principles that it claims to follow. In March 2005 Platform published an update “Sakhalin 2 gas and oil project - Further Breaches of Equator Principles May 2004 – March 2005”<sup>85</sup>, and according to the briefing paper, SEIC still does not live up to the standard either on Whale protection or River Crossing techniques.

In April 2005 BankTrack, the Berne Declaration<sup>86</sup> and Greenpeace Switzerland protested outside Credit Suisse First Boston’s main office in Zurich.<sup>87</sup> The NGOs criticised the fact that Credit Suisse have signed the Equator Principles, but at the same time the bank is the financial advisor of SEIC.

“If the possible extinction of an entire whale species is the sort of risk that Equator Banks are ready to ‘determine, assess and manage’ with their principles, what good are such principles then? At the end of the day, principles are about having to make hard choices at times, and this is what we expect Equator Principles banks to do,” says Johan Frijns, coordinator of BankTrack.

### **A long way to an accepted Environmental Impact Assessment**

SEIC has made an Environmental Impact Assessment (EIA) which is also required according to Russian law.<sup>88</sup> The EIA was conducted by Environmental Resources Management Limited, a UK-based environmental consultant.<sup>89</sup> The Social and health impact assessment was conducted by SEIC itself. The preliminary EIA was published in 2001, but it was later updated in 2002.<sup>90</sup> After that the Russian Government undertook a specialist review of this document which meant that the phase two project could start. In addition to this EIA, SEIC published an international-style environmental, social and health impact assessments (ESHIA) in early 2003. This was in order to bring the impact assessment into line with international standards, which was requested from public and private finance. The total impact assessments amount to more than 2000 pages. Since the ESHIA was not considered up to standard by The European Bank for Reconstruction and Development (EBRD), an Environmental impact assessment addendum was published in December 2005.<sup>91</sup> This ESHIA is actually finalised when more than half of the project is already constructed.

SEIC’s EIA and the process of doing the EIA have met with heavy criticism. After more than two years of EBRD evaluating and working with SEIC to get the company’s EIA up to standard, the EBRD in May 2005 still came to the conclusion that SEIC’s EIA for phase two of Sakhalin 2 -project was “not fit for purpose”.<sup>92</sup> It was not until December 2005 that EBRD announced that the bank considered the Phase two of the Sakhalin 2 -project to be “fit for purpose of consultation” (see above).<sup>93</sup>

World Wildlife Fund, WWF UK, has conducted an extensive comparison between the EIA process undertaken by Shell on the Sakhalin 2 project and the group manual on EIA from Shell itself.<sup>94</sup> WWF says that Shell has been attempting to rectify the

## Platform's analysis against Sakhalin 2 Phase Two-Project<sup>81</sup>:

**The project's environmental impact assessment (EIA) is deficient on a number of counts. These include, inter alia:**

1. The environmental assessment fails to include key baseline data, including identification of specific information about endangered species (Breach of Equator Principle 3a).
2. The EIA fails to evaluate conflicts between the project Production Sharing Agreement and Russian environmental law, does not address legal challenges to the project, and is unclear about environmental protection status of Aniva Bay. (Breach of Principle 3b).

### **Principal Objections:**

3. Key environmental impacts are omitted from the EIA, including the impacts on many wild salmon-bearing streams and the impact of oil spills. Other important impacts are inadequately analysed, such as those on the Western Gray Whale. (Breach of Principle 3d).
4. Cumulative impacts with other oil and gas projects on Sakhalin Island are not considered. (Breach of Principle 3m).
5. The EIA does not systematically compare the project with feasible alternatives. (Breach of IFC Safeguard Policy OP 4.01 (Environmental Assessment) - compliance with which is required under Principle 3).

### **There are further problems in project design, which also constitute breaches of the Equator Principles:**

6. The siting of the offshore platforms and the routing of the offshore pipeline will degrade the Western Gray Whales' summer feeding ground, a critical natural habitat. (Breach of IFC Safeguard Policy OP 4.04 (Natural Habitats), and hence Equator Principle 3).
7. The project fails to apply the precautionary principle in relation to Western Gray Whale feeding grounds, to watercourse crossings, or to dumping of wastes in Gulf of Aniva. (Breach of IFC Safeguard Policy OP 4.04 (Natural Habitats), and hence Principle 3).
8. Consultation processes were flawed, the project failed to provide sufficient information to stakeholders, and did not take consultees views into account. (Breach of Principle 5).
9. The Equator Principles also require production of an Environmental Management Plan (Principle 4), which is yet to be published.

*"Principal objections Analysis of the Sakhalin 2 oil and gas project's compliance with the Equator Principles", May 2004:4, [www.carbonweb.org/documents/Sakh-EP-analysis.pdf](http://www.carbonweb.org/documents/Sakh-EP-analysis.pdf), edited and shortened by SwedWatch 2005-12-21.*



criticism from the EBRD by producing an EIA Addendum and therefore concludes that Shell is seeking to gain retrospective approval.

“The application of Shell’s own EIA procedures has been found to be unsatisfactory, with examples and evidence provided from a range of sources. This issue of sequencing is key if maximum environmental protection is to result, otherwise opportunities to change designs are lost. In this case, Shell has made decisions first, and then sought to justify them through the EIA process.”

Leaton, James, “Risky business – the new Shell”, November 2005, WWF UK, [www.panda.org/sakhalin](http://www.panda.org/sakhalin), 2005-11-27: 2.

WWF conclude that it is indeed a growing problem that companies “try to comply on paper once a project is half-built, rather than going through a legitimate, inclusive process of assessment prior to the project starting.”<sup>95</sup> According to WWF, there is not a single point on which SEIC does not live up to in its own standard, but there are several failures in the lack of baseline data on some species, in recognising the indigenous peoples’ issues and the failure to incorporate environmental information into decision making.<sup>96</sup>

### **Objections from the environmental movement**

The local organisation Sakhalin Environment Watch (SEW) is an independent non-political NGO created in 1996.<sup>97</sup> There are three working board members on the council of the organisation and four people employed. The mission of the organisation is to protect the wildlife and natural environment of the Sakhalin Region. Sakhalin Environment Watch has created a global network to campaign about Sakhalin 2. The campaign spans over at least 146 organisations in 22 countries in the form of a loose and internal network.<sup>98</sup> The most active NGOs, apart from Sakhalin Environment Watch, are; Pacific Environment, Friends of the Earth International, World Wildlife Fund (WWF), Greenpeace, BankTrack, Platform, CEE Bankwatch Network, Berne Declaration, International Foundation of Animal Welfare (IFAW) and Wild Salmon Center.

Locally on Sakhalin SEW cooperates with other environmental groups as Green Patrol, Knowledge is Strength, The Green Party and indigenous people’s groups, but it is SEW and its chairman Dmitry Lisitsyn who leads the criticism of the oil and gas operators and who gets a lot of international attention for its work. According to an article in San Francisco Chronicle the head environmental regulator on Sakhalin, Sergei Kotelnikov, says that he relies on the information that Dmitry Lisitsyn, SEW, supplies.<sup>99</sup> There is quite a lot of friction between SEIC on the one hand and the coalition of NGOs on the other hand, according to a research done by The Programme on NGOs & Civil Society Centre in Switzerland. Nevertheless, the campaign has made the NGOs much stronger on Sakhalin and the NGOs have succeeded in bringing the Sakhalin 2 project to international media attention. The issue has been covered extensively in among other media: BBC, Financial Times, World Street Journal, Guardian and Dow Jones and The Observer.

SEW does not only monitor the foreign oil and gas companies on Sakhalin. In December, Sakhalin Environment Watch uncovered an oil spill in northern Sakhalin



from a pipeline owned by Russia's state-owned Rosneft. Currently, however, SEW is preoccupied with Sakhalin 2 Phase Two, since the project will have major impact on the environment and the people of the Island, Dmitry Lisitsyn explains to Swed-Watch.

On January 28th 2006, SEW, Knowledge is Strength and the Green Party of Sakhalin organized a demonstration outside the main entrance of the LNG plant. Around 300 local people demanded a new evaluation of the damage of fish stocks caused by the construction of the pipeline and the Oil and gas terminals in Aniva Bay. There were also banners against EBRD's financing.



*The pipeline cuts a 40 meter wide gap in the forest throughout the pipeline route.  
Photo: Kristina Bjurling, SwedWatch.*

## Oil and gas pipelines crossing thousand rivers

The oil and gas pipelines will extend over most of the Sakhalin Island, 800 km from Piltun Bay in the North to Aniva Bay in the South. On the way it will cross around 1100 rivers, some bigger and some smaller. The geography is very hilly with high hills and steep slopes between each river. The rivers of Sakhalin are spawning rivers for the many fish species of the island, including the Sakhalin taimen (*Hucho perryi*), which is listed in the Red Book of endangered species of the Russian Federation.

There is more than one river crossing per km on Sakhalin. According to Dmitry Lisitsyn, Chairman for the local environmental organisation, Sakhalin Environmental Watch (SEW), no other pipeline in the world crosses such a huge river network. EBRD, who have worked extensively on the river crossing methods of SEIC the last year, state that SEIC now has committed itself “to ensure that there will be no net loss of salmon spawning habitats.”<sup>100</sup> But the environmental organisations involved are not at all convinced. According to SEIC the company has done extensive research on the river crossing issue for three years.<sup>101</sup> They promise to only lay down the pipes in the riverbeds in the winter time when the water is frozen and when there are no salmon present.

“Each river is assessed and treated individually. The general feature is that river crossings should be achieved with minimal impact upon the river”, says Jim Niven, Deputy External Affairs Manager at SEIC.

The pipeline cuts a 40 meter wide gap in the forest throughout the pipeline route. SEIC decided on the design of trenching the pipeline under earth along the whole pipeline route. According to Jim Niven, it is best practice worldwide nowadays to bury the pipelines.

“It is better that the pipelines are buried for security and safety reasons. It will not be hit by outside objects. It won’t suffer so much third party interference whatever it might be”, says Jim Niven.

### **Decision to trench the pipelines in the riverbeds criticised**

SEIC also has decided to trench the pipeline in the riverbeds in all watersheds, except at six rivers where the pipelines will actually be put in horizontal holes drilled under the rivers.<sup>102</sup> According to Jim Niven at SEIC the first prospect was that the river crossings would be done above ground, but the governmental agencies said that they wanted the pipelines to be buried. According to Dmitry Lisitsyn at SEW, this was a big mistake.

“It was possible for SEIC to build this pipeline without too much destruction to the environment, but now it is impossible. At a preliminary design stage, elevated bridge crossing was required, which means that on each river the pipeline should be built above river”, says Dmitry Lisitsyn.

Dmitry explains that the problems with river crossings in the river bed are that it affects the rivers a lot, both in the construction phase and later. In order to spawn, the salmon needs crystal clear water. If sedimentation is more than 220 mg/litre some salmon species cannot spawn, which means there will be no new fish next year. The salmon also needs special conditions on the riverbeds for the eggs to have a satisfactory environment in which to develop. With sedimentation in the water and filth on

the riverbed the eggs will be affected in their development.

Per-Erik Jansson, professor at The Royal Institute of Technology in Stockholm, does not think that it is very easy to judge which technique would be the most beneficiary to the environment.

“It is impossible to say which technology is best. The proper way to decide this is to conduct an Environmental Impact Assessment of both alternatives and then decide on the design”, he says.

In SEIC’s case, the company has presented the final international styled EIA only after more than half of the pipeline construction is complete. In SEIC’s position paper on river crossing it says:

“Watercourses will be crossed either by open trenching or horizontal directional drilling. The use of elevated crossings to span the watercourses was also considered, but due to the risks of pipeline corrosion and third-party interference, as well as the environmental impact this technique would convey, this method has not been selected.”<sup>103</sup>

### **Evidence of mismanage**

In the spring 2005 SEW leaked a photo session to The Observer where it was obvious that SEICs construction of the pipe line had negative impact on the rivers. The pictures were used as proof that SEICs promises of best practice were not actually followed in reality. When SwedWatch informs Jim Niven about the photos he says that it was a one-time mistake and that SEIC corrected the contractors that were responsible for this part of the construction.

“We recognise that some of the performance earlier this year was not optimal. The view was that some contractors’ performance did have to be upgraded”, says Jim Niven.



*Dead fish in Ozernaya River downstreams from construction work.  
Photo: A. Solov'ev, Sakhalin Environment Watch.*

At the end of September 2005, SEW presented new pictures on how SEIC broke their promises. In particular the pictures from the Ozernaya River show how fish died in masses in the dirty water downstream from construction work (See also the picture.).

“It is not a problem that they die. All salmon die naturally after spawning. The trouble here is that these fish died before spawning”, says Dmitry Lisitsyn.

When SwedWatch informs Jim Niven at SEIC about the picture he replies that this might have been a problem because of heavy rain on the days before, even though Dmitry says that there was no heavy rain before during those days. Jim Niven tells SwedWatch that SEIC have learnt a lot during the construction phase and that SEIC have taken more and more preventive measures to prevent erosion in the rivers.

SwedWatch was able to go out for one and a half days with SEW to actually look at the pipeline construction during the visit at the island. Some of the rivers were clear and the dead fish at the shore had died naturally after the spawning. Other rivers close to active construction sites are evidently muddy and we could see how the erosion fences do not really work in reality on many of the steeper slopes.

“Look, this is the way it looks now, just some months after construction, but I’m actually even more worried about the long term effects of erosion”, says Dmitry Lisitsyn.

But Jim Niven, SEIC, says that the company plans to plant grass and bushes after the pipeline is buried.

“The land will be reinstated completely, it will be re-grassed, seeded and so on,” says Jim Niven.

He also informs SwedWatch about different methods of erosion prevention measures that are implemented in order to prevent soil erosion and salt leakage into the watersheds.

### **Lack of independent monitoring**

Wild Salmon Center (WSC) is a US based non profit organization founded in 1992. The aim of the organisation is to protect and ensure a sustainable future for the Wild Pacific salmon, steelhead, char and trout stocks and their ecosystems.<sup>104</sup> WSC is worried about the impact of the pipeline construction on the wild salmon species on Sakhalin. WSC does not believe that SEIC has met the standards of the policies for the proper protection of the ecology in the water streams that are affected by the pipeline construction.<sup>105</sup>

“Lack of adequate background data has permanently flawed the project. SEIC has refused to consider aerial crossings at some sites, despite recommendations from Russian specialists. SEIC is crossing some rivers directly through spawning areas”, Dave Martin, Russia Far East Program Director at Wild Salmon Center, writes to SwedWatch.<sup>106</sup>

Jim Niven tells SwedWatch that the salmon has not been affected by the construction of the pipeline yet and refers to the fact that 2005 was a bumper year for Pink Salmon catch on Sakhalin. But Dave Martin explains that it is actually too early to see the effect on the Salmon species yet since the Salmon run in even and odd year cycles, with the odd-year run much larger than in even years.<sup>107</sup> Since the construction started 2004 you should see main effect on the catch rate for pink salmon 2006 and 2007.



In May 2005 The Wild Salmon Center and several other international NGOs demanded that SEIC should convene an expert review of pipeline river crossings and other related pipeline issues.<sup>108</sup> WSC also proposed an outline for an independent assessment, but SEIC did not approve this. Since then EBRD decided to hire consultants from the University of Birmingham to investigate the adequacy of SEIC's programme for pipeline construction especially on the river crossings. A first report from The Birmingham group was ready in November 2005, but it was not made public.<sup>109</sup> SEIC says that it is up to EBRD to take the decision of public disclosure of the Birmingham report, but according to EBRD it is still confidential by January 2006.<sup>110</sup> According to James Leaton, Senior Policy Adviser, WWF – UK, the reason for this is mainly that the Birmingham group was not satisfied with the first data presented by them by SEIC, in order for them to be able to make a serious independent study.<sup>111</sup>

SEIC has offered The Wild Salmon Center (WSC) to participate in some activities, but WSC is not confident in the seriousness of SEIC's offer yet. "While they have discussed cooperation in general terms, we have not yet been able to agree on any specific and meaningful cooperation to minimize project impacts," Dave Martin writes to SwedWatch. In a letter to SEIC in November 2005, Dave Martin, Russia Far East Program Director at WSC, put some conditions including demands on reasonable time for monitoring and transparency.<sup>112</sup> WSC also demands the disclosure of the Birmingham report. Dave Martin tells SwedWatch that he suspects that SEIC is unwilling to release the document because it is very critical of the project. Although Wild Salmon Center is very critical towards SEIC, the organisation does give some credit to SEIC for its work with river restoration and taimen research and Dave Martin states that WSC is still open to cooperation with SEIC.<sup>113</sup> He writes: "WSC is committed to doing everything we can to protect salmon. That includes working with SEIC if there is an opportunity, during both construction and operations".<sup>114</sup>

### **Irreversible damage**

According to both World Salmon Center and SEW, SEIC has now contravened several important points for adequate action regarding river crossing methods. Dmitry Lisitsyn, chairman for SEW does not believe that there is room for any further improvements in pipeline construction. "It was possible the preliminary stage when doing the pipeline design, but now it is impossible", he says.

Among several points, he takes the example that the Russian legislation forbids construction of the pipeline through spawning grounds, but SEIC has nevertheless already constructed pipeline crossings or planned crossings on 109 rivers through spawning grounds.<sup>115</sup> Dave Martin at Wild Salmon Center confirms that this breaks Russian law, but despite this SEIC got official permits to make constructions in spawning grounds. He also informs SwedWatch that SEIC was actually fined for several violations of Russia law in the spring of 2004, after an official government inspection.

Dmitry Lisitsyn is also very critical of the fact that SEIC constructs the oil pipeline, the gas pipeline and the optic-fiber cable at intervals from several months to one and a half years. According to him, this makes the rivers and the environment much more affected than if these operations were coordinated at the same time.

Elena Dmitrievna Nevenchina, specialist at the Oil and Gas Department of Sakhalin Administration, agrees with SEW. She also tells SwedWatch that SEIC initially got the license for doing the construction of the pipelines at one time.

“They got license to build the oil and gas pipeline at the same time, but later SEIC began to project one pipeline and then they did the other one later. Their technology was changing a lot. Now we believe the compensation should be doubled, because damage is doubled. If they had projected both the pipelines at the same time the damage would be less”, says Elena Dmitrievna Nevenchina.

Jim Niven, Deputy External Affairs Manager at SEIC, writes to SwedWatch that SEIC “is ready to cooperate and engage with Authorities and other stakeholders if the Authorities wish to reconsider the compensation calculation in the light of current project activities.”<sup>116</sup>

### **SEIC promise supervision**

On SEICs webpage the company states that the criticism is unfair to the majority of the project:

”Some NGOs have criticised recent onshore pipeline construction work over some river crossings along the route of the Sakhalin 2 oil and gas pipelines. We acknowledge that in a few cases the performance and standards are not as we would wish or expect. We very much regret this. However, the practices selectively highlighted by NGOs are not representative of the general standard of construction activities.”<sup>117</sup>

SEIC promises enhanced supervision of contractors by themselves as well as with independent external monitoring teams, increased transparency of performance by publishing reports from the monitoring teams on the web and implementation of additional measures for ensuring Contractor compliance. SEIC also says that the company has invited NGOs to visit the pipeline route and witness the river crossing activities, but it cannot yet explain more on which NGOs these will be and how this work is to be done.<sup>118</sup> Jim Niven, External Affairs, SEIC, explains to SwedWatch that the external monitoring teams are hired international environmental consultants.<sup>119</sup> Dave Martin, Wild Salmon Center, generally thinks that it is a good idea to have external monitoring teams, but points out that despite having inspectors in place in the winter 2005; there were still many breaches of policies. SEIC’s current documents on crossing construction show that the monitoring teams lack a key piece of equipment (turbidity meter) to measure sediments in many rivers.<sup>120</sup>

### **Pipelines cross seismic risk zones 24 times**

Another serious concern on the pipeline construction is that the pipeline crosses a highly seismic area. Sakhalin is generally regarded as a region of high seismicity or “earthquake hazard”, since it is located on the boundary of the Eurasian and North American plates. In May 1995 2 000 people died in an earthquake in Neftegorsk, Northern Sakhalin.<sup>121</sup> Smaller earthquakes happened every year between 2000 and 2003. The pipeline crosses 24 seismic faults and critics raise strong doubts about the wisdom of constructing an oil and gas pipeline over such earthquake risky area. “Pipeline crossing over seismic faults is not new; it happens in other places in the world also, says Jim Niven, Deputy External Affairs”, SEIC.

He explains that they can design the pipeline to hold during quite strong earthquakes.

But WWF and several other NGOs question if SEIC really safely can bury pipelines on Sakhalin.<sup>122</sup> They also argue that there is a lack of information about the assessment of seismic hazards and how SEICs plans to handle those hazards in the EIA. The NGOs recommend that the pipeline should traverse a fault area above ground in order to withstand movements in the ground. But SEIC believes that the current design will be safe. Also the LNG plant in Prigorodnoye is placed close to a minor fault, but according to SEIC “the risk can be safely handled by design and by siting beyond the 5-7 km buffer zone.”<sup>123</sup>

An additional issue is that the pipeline route crosses areas with a lot of leftover weapons from World War 2, including ammunition depots. Dmitry Lisitsyn, Chairman of SEW, tells SwedWatch that there is one place near Korsakov in the South of the Island, where an old ammunition depot lies just 300 meter from the pipeline route. According to him, it is illegal to build any construction within a 3 000 meter safety zone of an ammunition depot and in the case of any potential risk of an explosion, the safety zone is more than seven km. This was not known to SEIC and not mentioned in the EIA.

“This is just an example of the deficiencies in the EIA. Which means it is a glossy picture on paper but in reality, there are many more problems”, says Dmitry Lisitsyn.

## The Western Pacific Gray Whale at risk

Since the disappearance of the Gray Whale from the North Atlantic within the last 300–400 years, the two remaining Gray Whale species (*Eschrichtius robustus*) are found in the North Pacific in two different populations. In the Eastern population there are estimated to be around 26 000 individuals, but in the Western regions the population consists of only about 100 individuals. The Western gray whale’s principal summer feeding area is off Sakhalin Island, just by the oil and gas platforms of SEIC.

The Western Pacific Gray Whale is listed as critically endangered by The World Conservation Union (IUCN).<sup>124</sup> It was reclassified in the 2000 IUCN Red List from Endangered to Critically Endangered. There are 25 marine mammal species currently living off-shore of Sakhalin Island: 11 of these, including the Western Gray whale, are on the endangered species lists of the U.S. and Russia.<sup>125</sup> The current population contains only about 23 breeding females.<sup>126</sup> Both Exxon Neftagas Sakhalin 1-project and SEIC’s Sakhalin 2-project are close to the Whales feeding ground.

“Since the mid 1990s, whales feeding off Sakhalin Island have had to coexist with high intensity seismic exploration, placement of temporary drilling rigs, increased ship and helicopter traffic, and the installation of a major drilling and production platform; all within 10-20 km of their primary feeding habitat. Concerns about this development include threats of an oil spill to the whales and/or their food, and disruption to the whales by underwater noise from seismic surveys, drilling and production rigs, and associated support vessels and helicopters operating in the areas around the Sakhalin1 and Sakhalin 2 projects.”

*Brownell, Robert L. Jr. and Yablokov, Alexey V., “Endangered Sakhalin gray whales face cumulative threats on their feeding ground during summer 2001”, The Socio-Ecological Union (SEU).<sup>127</sup>*



In particular, the Piltun-Astokhskoye (PA-B) platform of SEIC's project is just seven km off the feeding ground of the whales. Since this connection is clear to the international environmental movement, there has been great pressure on Shell to act in a responsible way for the sake of survival of this species. But unfortunately the environmental organisations and SEIC do not agree on what should be a "responsible way".

The campaign concerned about Sakhalin 2 has successfully promoted the whale issue and pushed SEIC to act.<sup>128</sup> In 2004 The World Conservation Union was invited by SEIC to put together an Independent Scientific Review Panel (ISRP) that would conduct a review of the possible effects on the Western Gray whale from the Phase two construction. The expert panel consisted of 14 leading scientists from Russia, Europe and North America.

### **Most precautionary to suspend present operations**

In February 2005 the expert panel came to the conclusion that there is a risk that the population of the Western grey whale will not recover, even with no additional threats, but this is increased substantially because of the Phase two construction.<sup>129</sup> It also states that the long-term effects are more serious than the short-term effects. They made clear that even the loss of one additional female per year would probably lead to the extinction of the whole population.

The expert panel says that it was difficult for them to determine how SEIC's risk assessments were actually arrived at, since there was a lack of specificity in SEIC's application of its standards. For example, on the important decision on where to locate the PA-B platform, the panel concluded that it was "effectively precluded... from completing a reasoned and rigorous evaluation of some of the risks and mitigation strategies associated with Phase two."

The panel also found serious deficiencies in important scientific information about the whales. For example, the panel criticises SEIC for not having carried out proper investigation of the effects of noise levels during construction. The panel also criticises SEIC for not taking the issue of the physical disturbance of the seabed seriously and calls SEIC consideration "rather superficial".

"Before deciding where to install the PA-B platform and which pipeline configuration to use, it would have been appropriate to conduct a careful and detailed assessment of the associated risks... This was not done. Instead, the risks of damage to Gray whale feeding habitat from development activities were dismissed as insignificant."<sup>130</sup>

The panel moreover point out that Phase Two will eventually also have some benefits when it comes to reducing the risks for the whales, since the oil and gas will then be transported in pipelines rather than in tankers from the platforms. But at the same time they point out some new potential risks from phase two, that will remain throughout the lifetime of the project and therefore advise SEIC that:

"..the most precautionary approach would be to suspend present operations and delay further development of the oil and gas reserves in the vicinity of the Gray whale feeding grounds off Sakhalin, and especially

the critical near shore feeding ground that is used preferentially by mothers and calves.”

And later:

“Clearly, from the perspective of Gray whale conservation, any reasonable means to reduce platform-associated risks to the feeding grounds, including moving the platform farther away from them, should be taken.”

After the ISRP expert panel published their report, SEIC decided to change the undersea pipeline route so that the pipeline does not run right through the feeding area for the whales. The IUCN secretariat stated in a response to the report of the expert panel that the organisation, in spite of being worried, was optimistic about the possibility of combining oil and gas development around Sakhalin Island with protection of the whales.<sup>131</sup>

### **Whale experts leave in indignation**

There is some tension among the whale experts involved since some scientists are very disappointed with the fact that SEIC went through and installed the The Piltun-Astokhskiye platform during the summer of 2005, against the recommendation of the panel. According to Igor Chestin, WWF Russia, three members of the panel have so far left the cooperation with SEIC.<sup>132</sup> In July one of the ISRP Member, Professor Rick Steiner at the University of Alaska, urged Shell’s CEO Jeroen van der Veer to postpone the installation of the platform concrete base pending completion of the scientific work.<sup>133</sup> But Shell did not wait with the installation of the platform, which led to that Professor Steiner in protest would not continue his participation in the follow up work connected to the expert panel.<sup>134</sup> According to Jim Niven at SEIC there was “general agreement” that the expert panel understood that this was the best location for the platform.

“The location is determined because of the nature of the seabed. There are also technical limits”, says Jim Niven to SwedWatch.

In the EIA the company states that it has investigated and declined the option to move the platform away from the feeding area.<sup>135</sup> But Dmitry Lisitsyn from Sakhalin Environmental Watch, SEW, says that there was no independent research done on actual alternative sites for the platform.

“Our key demand is that the platform should be moved 12 nautical miles from shore. The platform was also installed before the independent research from the best experts on whales were ready”, Dmitry Lisitsyn says.

As a follow up to the expert panel’s report in February 2005, there was a meeting between the whale scientists, potential lenders and the scientific and technical people of SEIC held in Vancouver in September 2005. One of the outcomes of that meeting was that there is now a plan to set up an independent Western Gray Whale Advisory Panel (WGWAP). The mission for this panel would be both to review and advise SEIC on its mitigation measures as well as to seek to bring other oil and gas companies on board to address the issue of Western Gray Whales; the Exxon Neftagas run Sakhalin 1 project also affects the whales. According to Igor Chestin at WWF Russia, there is however problems to get together whale experts on the panel since many of them are disappointed with the earlier work.

### **Negative effects on whales shown**

During the installation of the Concrete Gravity Based Structure (CGBS) of the PA-B platform this summer (2005), both WWF and International Foundation of Animal Welfare (IFAW) conducted independent whale monitoring and research. According to WWF the area near the platform covers one fifth of the whales' known feeding grounds. The organizations found several gaps in SEIC's monitoring and therefore they decided to do their own monitoring. The observation team from WWF found that there was a statistically significant negative correlation between the observed whales and the construction vessels, given that the whales were fewer when construction vessels were more. Another observation was that the whales seemed to change behavior in the vicinity of the platform.<sup>136</sup> All in all WWF conclude that scientific proof now exist on the whales being negatively affected by the construction of the platform, something which SEIC denies.<sup>137</sup> Jim Niven informs SwedWatch that there was no observed effect on the whales when SEIC installed the concrete structures. "This helped us to say, okay, we can go ahead with this location and still manage the impact on the whales", he says.

He also state in a written answer that the WWF report "are not based on sound science" and refers to research funded by SEIC's and Exxon Neftagas that is expected to be public later in spring 2006. James Leaton, Senior Policy Adviser, WWF-UK is not surprised by the reaction from SEIC. "For us the burden of proof should be on them to demonstrate they had no impact, which they cannot", he writes.<sup>138</sup> James Leaton also point out that one of the original expert panel members was responsible for the study. "The fact that our work indicates there was an impact should be of great concern to them, not something they should try and dismiss."

### **In breach of the precautionary principle**

The question is if SEIC has followed the precautionary principle, which in the words of the UNs Rio declaration from 1992, states that;

"In order to protect the environment, the precautionary approach shall be widely applied[...] Where there are threats of serious or irreversible damage, lack of full scientific certainty shall not be used as a reason for postponing cost-effective measures to prevent environmental degradation."<sup>139</sup>

EBRD's environmental policy concerning the precautionary principle;

"[The Bank] supports a precautionary approach to the management and sustainable use of natural biodiversity resources (such as wildlife, fisheries and forest products) and will seek to ensure that its operations include measures to safeguard, and, where possible, enhance natural habitats and the biodiversity they support."<sup>140</sup>

35 NGOs including WWF, SEW, Greenpeace and Friends of the Earth International argue that SEIC's decision to install the PA-B concrete base violates the precautionary principle.<sup>141</sup>

"Thus, the rejection by Royal Dutch Shell to suspend operations and to delay further development and its reckless decision to install the PA-B

concrete gravity base prior to the completion of a comprehensive scientific review represents a grave threat to the critically endangered Western Gray whale, and a serious, fundamental and irreversible violation of EBRD policy.”

*Letter to Jean Lemierre, President, EBRD, from Sakhalin 2 campaign (signed by more than 35 organisations including WWF, SEW, Greenpeace and Friends of the Earth International), 2005-09-29.*

When SwedWatch ask Jim Niven at SEIC what he thinks of the argument that the company did not act in a precautionary way, he says:  
“We held up the laying of the sub sea pipeline for a couple of seasons, so to say that we did not take a precautionary approach I think is unfair. We convened the panel and extended our knowledge about the whales”.

According to SEIC the company has spent about seven million USD on the Western Gray Whale research in 1997-2005.<sup>142</sup>

“It is our job to balance the safe and responsible production of oil and gas with these environmental concerns”, says Jim Niven.

## Extensive pollution of sea bays

### Discharge of drilling waste in Okhotsk sea

From 1998 to 2004 over 23 600 tons of drilling wastes were discharged from Molikpaq into the Okhotsk sea, according to statistic from SEIC.<sup>143</sup> According to SEICs EIA the company has made investigations on the effects of these wastes in both Piltun Bay and Lunkoye Bay. The company writes;

“... results showed that discharge of water based muds and cutting from offshore platforms would have no significant impacts on the environment. This was also demonstrated by the results of four years of environmental monitoring around the Molikpaq after discharging water based muds and cuttings. Therefore it was decided that the water based muds and cuttings that will be used during the project, will be discharged to the marine environment.”<sup>144</sup>

The Best Available Technology for disposal of the wastes is “re-injection” of the waste down into the ground again. Jim Niven at SEIC does not know why the company did not use it from the beginning, but he guesses that the techniques to do this did not exist at that time. But according to Dmitry Lisitsyn, Sakhalin Environmental Watch (SEW), Exxon actually did decide to use zero-waste technology during the same time. SEIC says that it always has operated in accordance with regulations and that the company since 2004 disposes all the drilling fluids and cuttings back underground.<sup>145</sup> The company also informs SwedWatch that all oil spills are reported to the authorities and according to SEIC the performance is world-class, with less than one liters of oil spill per year.

There are contradictory figures however. The Audit chamber of the Russian Federation has made an evaluation of the Russian Government report about the implementation of Production Sharing Agreement regime in 2004. According to this

report published in October 2005, oil and diesel spills in the Astokh area amounted to 28,3 tons in 2004.<sup>146</sup> The Molikpaq platform operates in the Astokh area. SEIC withholds that the correct figure is only one litre of oil spill in Astokh area from SEIC's operations and says that the figure 28,3 tons refers to an oil spill in another area, that from the Cristoforo Colombo dredger accident (see below). But at that accident over 70 tons of oil and diesel was spilled.<sup>147</sup> SwedWatch have asked SEIC for clarification on sources for its information, however without reply so far.

The oil spills close to Piltun Bay affect the ecosystem in the bay which will obviously affect the living environment for the Western Gray whales as well as the different fish species in the bay. According to Galina Nikolaevna Panchenko, ecological inspector of Nogliki fish protection service in Nogliki, there have been several oil spills outside Piltun Bay already. This observation is shared by the indigenous people at Nogliki whom SwedWatch met (see below). She is upset that SEIC got permission to discharge drilling waste into the sea from the Molikpaq.

"Nobody did any research on this problem. I believe this will cause much greater damage than the river crossings", says Galina Nikolaevna Panchenko.

According to SEIC's official information, the company has spilled less than one litre of oil in the last two years.<sup>148</sup> When SwedWatch informs Galina Nikolaevna Panchenko about this, she just shakes her head.

"It is in their interest to make light of the damage to Nature. Of course it is not the truth. It is ridiculous," says Galina Nikolaevna Panchenko.

### **Deposit of dredging material in Aniva Bay**

In Aniva Bay in the South of the island SEIC is busy constructing one of the biggest liquid natural gas (LNG) plants in the world. Around 70 percent of the construction is completed by January 2006. At the same site the company will also construct an Oil Export Terminal (OET) reaching out nearly five kilometres into the bay.<sup>149</sup> In order to export the LNG the company is also building an 805-metre jetty in Aniva Bay. The total construction site is 490 hectares. A temporary facility during the construction phase also includes a materials offloading facility (MOF) in the Aniva Bay.

According to SEIC, the planned dredging was completed by the end of 2005 and the final volume of dredging material was 1.40 million m<sup>3</sup>.<sup>150</sup> All the dredged material is now disposed on the a disposal site located approximately 22 km offshore in 63 m water depth in the middle of Aniva bay.<sup>151</sup> In the EIA Addendum from December 2005 SEIC compares the disposal volumes with other big projects, like for example the Hong Kong airport, around the world in order to show that the dredging work is actually not that big in comparison.<sup>152</sup> Sakhalin Environment Watch (SEW) point out, however, that the dumping of dredging material for an artificial island for Hong Kong airport is much different than to dump dredging material in a rich and sensitive ecosystem as Aniva Bay. From the beginning SEIC planned to reuse the material, but when investigations showed that the material was not good for re-use, it decided to deposit the material into the bay.<sup>153</sup>

SEIC is stated in the EIA that the deposit is not expected to make any major impact on the environment in the sea bay because of the deposit:

"The predicted suspended solid concentrations associated with dredging



at the MOF and LNG Jetty locations are within natural variation. The zone within which the predicted concentrations during spoil disposal exceed the natural variation is likely to be small, 1 km at worst.”

EIA, “*Impacts, Mitigation and Monitoring Requirements*”, page 41, [http://www.sakhalinenergy.com/documents/doc\\_38\\_eia\\_5\\_chapter3.pdf](http://www.sakhalinenergy.com/documents/doc_38_eia_5_chapter3.pdf)

Throughout the document (chapter five of the EIA) it is stated that the impact of the construction of the LNG and OET are only expected to be “minor”. But according to Sakhalin Environmental Watch (SEW) the dumping has had huge negative impact on the ecology of the bay. SEW and the local group *Knowledge is Strength* (see below) claim that the result of the dumping already had great damage to fish, scallop, crab, shrimp and other valuable resources. The dredging works is also situated in immediate proximity to the mouth of the River Mereya, an important salmon spawning river. The marine pollution has affected the livelihood of the inhabitants of the south Island as well as the local fishing industry.

“The dumping zone is in the middle of the bay. Our proposal is instead to have the disposal zone further out of Aniva Bay, where there are much deeper waters and much fewer marine resources,” says Dmitry Lisitsyn.

SEW says that it checked SEIC’s own monitoring materials regarding the suspended soils and found that at least 250 000 cubic meters were spread around the bay, though this material is supposed to stay at the dumping site. Jim Niven, External Affairs, SEIC, rejects this figure. He does not either like the word “dumping”.

“There is nothing dumped in Aniva bay! What you have to do when you build the jetty is that you have to dredge in order to make it deep enough for vessels and when you dredge seabed materials, you have to redeposit it somewhere,” Jim Niven at SEIC says.

According to Jim Niven SEIC has got the redeposit site selected and approved by the authorities.



*The local people find the cost of Aniva Bay destroyed by the pollution from the LNG construction.  
Photo: Kristina Bjurling, SwedWatch.*



### **NGOs resorted to legal action**

Even at the approval stage, the local inhabitants, fishermen and environmentalists called for the relocation of the dumping site outside Aniva Bay into deep water with low biodiversity. They were also seriously questioning the wisdom of locating such construction works near to the mouth of a spawning river during the salmon migration season. But when SEIC did not change their plans, SEW and Knowledge is Strength launched a legal action against SEIC in April 2005.<sup>154</sup> The NGOs wants to prohibit, in their words “the environmentally harmful activity connected with the LNG jetty construction”. First the Yuzhno-Sakhalinsk Municipal Court refused to take legal action, but in December 2005 SEW won a legal appeal at the Sakhalin Regional Court when this court overturned the decision. The case will now return to the Yuzhno-Sakhalinsk Municipal Court for consideration by a new judge.<sup>155</sup>

“Our case maintains that so far, damage to fish stocks far exceeds so-called permissible damage, that there has been an increase in the amount of dredged material, and that the dredging work itself is being carried out differently from how it was specified in the project documents,” Andrey Kurbatov, Sakhalin Environment Watch says in a comment in the press release following the court decision.<sup>156</sup>

“The scallop has disappeared from the beginning of this June, and now it is almost impossible to find scallops on this shore. Many local people collected scallops as a tradition, there used to be thousands and now it is impossible to find here,” says Dmitry Lisitsyn to SwedWatch.

Jim Niven, SEIC, refuses to comment on any on-going lawsuits and so he would not give any comment about this lawsuit either. SEW have also filed a case against The Department of Federal Service for Inspection Related to Nature-Use (“Rosprirodnadzor”) for giving the grant to SEIC to build the Temporary Jetty without a proper consultation with the public.<sup>157</sup> In January The Sakhalin Regional Court judged in favour of SEW, against Rosprirodnadzor. SEIC and Rosprirodnadzor then left an appeal to the court which was turned down in July 2005 (see also below).

### **Fishermen want compensation**

Calypso is a medium scale fishing company with about 320 employees. The company’s main catching area is in the Aniva Bay. Calypso has announced a 70 per cent drop in catches in Aniva Bay since the construction started. It has asked for three million USD in compensation.<sup>158</sup> SEIC and Calypso is now negotiating to determine the sum for the damage for Calypso. Elena Dmitrievna Nevenchina, specialist at the Oil and Gas Department of Sakhalin Administration, explains that the fishing companies can receive compensation for damage, including profit, for next 30 years.

Alexey Tyndik, Calypso’s lawyer, writes to SwedWatch that SEIC says it will only accept compensation for an area one km from the mouth of river Mereya.<sup>159</sup> The company claims that Calypso can still fish in the other areas. Alexey Tyndik is afraid that means that the compensation will only be about 10-15 percent of the amount Calypso hoped for. In figures that could mean 300-500 thousand USD instead of the three million that Calypso has claimed. However, he says that he will not give up until Calypso has got a decent compensation. “I’ll continue my efforts even to court prosecution”, the lawyer writes.

The NGO coalition campaigning against SEIC writes to EBRD in September that

they believe the SEIC's dumping of dredged wastes into Aniva Bay is an irreversible violation of the EBRD's policies on environmental assessment and on the precautionary approach.<sup>160</sup>

## The risk for future oil spills and leakage

One of the absolutely biggest long term risks connected with the project is of course the risk of oil spills. As the platforms are in a sea which is covered with ice approximately half of the year it is extremely difficult to clean up an oil spill in such an environment. The Independent Scientific Review Panel (ISRP) said in its report that it believed that spill prevention is the key, since the ability to respond rapidly is limited. They point out that a large spill is most likely to occur in severe ocean conditions, storms, winter and ice.<sup>161</sup> There is considerable risk of an oil spill during the lifetime of the project and the company estimates the risk of a leak from a pipeline to be as high as 24 percent within the lifetime of the phase two project.<sup>162</sup>

SEIC has been much criticized from the NGO community because the company's EIA did not include the crucial issue of oil spill response.<sup>163</sup> In case of an accident, the North coast of Japan is also threatened. SEIC have made a Memorandum of Understanding (MOU) with Japanese Maritime Disaster Prevention Centre which will be updated to include Phase two of the project. When SwedWatch arrives at the coast at Aniva Bay there is a rusty wreck lying on the shore. Dmitry Litisyn, Chairman of SEW tells SwedWatch that this ship was grounded in a huge storm 12-15 years ago.

"It is a good example of how difficult these waters are to navigate," he says.

In September 2004 the Cristoforo Colombo dredger went on shore in the port of Kholmsk in a typhoon. The dredger was owned by a sub-contractor to SEIC's main offshore pipeline contractor.<sup>164</sup> Jim Niven, SEIC claims that the vessel was not contracted to SEIC at the time and that it therefore did not have the responsibility for rescue measures, but SEIC decided to do this anyway. The environmental organisations though take this as an example of how badly the oil spill response is developed so far.<sup>165</sup> SEW claim that there were several people that fell sick afterwards and that SEIC did not investigate the consequences and present it publicly afterwards. Jim Niven is irritated about these accusations.

"The important thing was to clean up. Here we are, lending a helping hand and you are suggesting that we did not do a proper clean-up," says Jim.

He also adds that SEIC contributed to some social programmes in Kholmsk to show good will. SEW also criticises SEIC for not complying with their promise to be on the spot with rescue team within one hour. But Jim Niven explains this by the fact that the rescue team was collected in the office in Yuzhno-Sakhalinsk within one hour.

"It was night time when the accident happened and actually getting to the area in the night time was not safe with the waves and the storm, so the team had to be moved later to Kholmsk," says Jim Niven.

The accident draws attention to the important issue of where SEIC draws the line for its responsibility. Jim Niven writes to SwedWatch that "SEIC is responsible for spills from SEIC owned facilities and for contractors working under SEIC direction. SEIC

will respond to any and all “third party” spills at the request of the spiller or Government agency”.<sup>166</sup>

In November 2005 there was another storm that caused three vessels working with the LNG plant construction in Aniva Bay to be blown onshore.<sup>167</sup> In just a few years there will be major oil and gas export from this bay all through the year. SEIC anticipates that when the Phase Two of the project is fully operational there will be in total approximately 239 oil and gas tankers per year or five tankers per week.<sup>168</sup> Local and international organisations are trying to raise their voices against the huge risks of spills in these rich waters. They criticize SEIC for not having presented a comprehensive oil spill response programme yet.

### **Lack of oil spill response plan**

Year round oil production is planned to commence in the end 2007. Jim Niven promises that SEIC will present a proper oil spill response plan in time for the first export of the oil and gas.

“The oil spill response plan is going to be developed now, remember we will not actually be producing oil for several years yet,” Jim Niven says.

He also tells SwedWatch that there is now a signed agreement between the different oil and gas operators and the authorities on the island.

“The agreement basically says that if there is an accident we will join our resources and we will work corporately,” says Jim Niven.

In the Environmental Impact Assessment Addendum published in December 2005 there is, however, an extensive chapter on oil spill response.<sup>169</sup> Friends of the Earth-Japan has gone through the new oil spill response addendum, but the organisation is not impressed.<sup>170</sup> It writes “Our conclusion about this document is that it is not an addendum, because an addendum means a supplement or something additional. This document states only “a plan to make an Oil Spill Response plan”. The independent scientific review panel pointed out that an oil spill in or near Piltun Lagoon could change the ecology of the lagoon so that the nursing and weaning of the whale calves would be disturbed.<sup>171</sup> In December 2005, Sakhalin Environmental Watch found and disclosed an oil spill from the Russian oil company Rosneft near Nogliki on the North of Sakhalin.<sup>172</sup> According to SEW, the oil covered lagoon lakes that were connected with Nabil bay on the North East coast of Sakhalin. This is the area where the Nivkh people, one of the indigenous peoples of Sakhalin, have their licensed fishing area. Dmitry Litisyn, Chairman of SEW, point out that there are still many lost bays on Alaska, in Prince William Sound, after the catastrophic Exxon Valdez oil spill of 1988 and he’s afraid that there could be a similar catastrophe on Sakhalin.

To conclude the environmental consequences from the Sakhalin 2 project are serious. The allegations from the local and international environmental organisations are very harsh; stating that SEIC has violated national law and international guidelines. Serious criticism has also been voiced by international whale experts. SEIC have made some important changes for the better, like re-routing of the undersea pipeline and re-injection of the drilling waste close to Piltun Bay, but there are still many issues which are highly questionable. Among these is the issue of deposit of dredged material in Aniva Bay, the issue of installing the PA-B platform so close to the feeding ground of the Western Gray whale and the effects on the precious fish species of Sakhalin.

## Chapter 5. Social Issues

All oil and gas development projects in Sakhalin have social impacts, but the Sakhalin 2 project is the project which demonstrates most impact, since it stretches its effects over the whole island, covering huge amount of land. SwedWatch has chosen to divide and present the social issues into three main issues: the indigenous people's situation, the local people in the city of Korsakov who live close to the LNG plant construction site and the issue of public consultation.

### Indigenous peoples suffering because of oil companies

The indigenous peoples of Sakhalin can be divided into four main groups: the Nivkh, Orok, Evenk and Nanai. The Nivkh is the biggest group. In total the indigenous peoples of Sakhalin consist of more than 3 000 people. Approximately 30 percent of the indigenous peoples live in the Nogliki District, in North East of Sakhalin Island.<sup>173</sup> The Nivkh are mostly fishermen and the Uilta and Evenk are mostly reindeer herders.

At a meeting with around 20 people, mostly women, from the indigenous peoples they tell SwedWatch about their living conditions and their view of the oil and gas industry. During our meeting the electricity fails which they explain, is common. The women's faces look grave in the candle light. They tell us that there is a lot of unemployment in their community, but some of them have work in companies and different organisations. Their traditional way of life is hunting and fishing, which they still do time to time. An old lady speaks up:

“Our traditional diet is fish, seafood and deer. But deer has become rare and due to lack of seafood we have worse living conditions nowadays.”

She recalls about the period of Soviet Union when the indigenous peoples got villages and support from the government and were able to live from fishing and hunting. But when the communist regime fell, the social security disappeared for the indigenous peoples as well as for the whole community. But for the indigenous peoples in the community, the fall was perhaps even harder.

The oil companies represent an additional hardship for the indigenous peoples. The elderly women tell SwedWatch that the fishes taste bad from oil and that there is not so much fish in the Piltun Bay anymore. Some of them say that the inner organs of the fish do not look the same anymore.

“Because the Molikpaq construction there is no cod, no herring and no fish at all. We expected herring but it did not come. And the taste of the fish is very bad, you can get the taste of some oil also,” one woman says.

There was massive death of herring in Piltun Bay in 1999. No one has been able to explain it and SEIC has not released its own monitoring of the discharge from the Molikpaq platform at the time either. One woman says that SEIC came to talk to them after this massive fish death.

“I could not understand anything; he was like a strong monster for us! He used so many technical terms that we did not know what these meant,” one woman says.

She explains that they can only see that the fish have disappeared, but they don't have any laboratories to show this and they do not trust the company.

“We are poor people in comparison with SEIC, but “money controls the world”,” she says.

“We couldn’t find a common language about the situation, the companies make the trenches and lay down pipelines in all the spawning rivers and the fish are not coming there and the rivers are dying. It affects us negatively,” another woman says. The women tell SwedWatch that they have got some help from the governmental authorities, such as permission to catch fish for their own use. “We would like to live, not only survive,” says one woman.

In January 2005 the indigenous peoples had enough and organised a protest directed towards the main oil operators in the Nogliki region; Shell, Exxon and Rosneft. “The island is very rich in resources and the companies are very interested in this but we, the people, get nothing from this. To attract the attention to us we carried out some actions, we closed some roads,” says one woman.

“The oil and gas industry had so many negative impacts on our life, mainly because of environmental destruction,” one woman says.

The protests got a lot of attention both locally and internationally. After that at least SEIC started to listen and consult with the indigenous peoples. But this was after the indigenous peoples had seen their land been taken over by construction of the pipeline and one contracting company had even made a storage of pipelines on the graveyard of their people.

“Our ancestors graveyards where used for storing pipelines. The company knew and accepted this. They just didn’t care,” one woman says.

“There is a road on the place of the tomb of my sister right now, says another woman. But now they have brought in good soil and planted some green plants so they have corrected their mistake now,” she says.

After this mistake, SEIC asked for a map of all graveyards and their places in order not to make the same mistake. But from the beginning they did not consult with the indigenous peoples.



*“There is no hope”, says this man from the Nivhk community who lives in the village Veni. Photo: Kristina Bjurling, SwedWatch.*



### **The Indigenous and Tribal people's convention**

The most comprehensive international instrument on the rights of indigenous peoples is the the Indigenous and Tribal Peoples Convention, ILO convention No 169.<sup>174</sup> The convention is binding to a country when the country has ratified it, but before that it serves as a guideline. So far there are only 17 countries in the world that have ratified the convention. Neither Russia nor Sweden have ratified it. SEIC claims that it will follow this convention in its operation.<sup>175</sup>

The Article 7 of the Convention states that indigenous peoples have;

“the right to decide their own development priorities and to exercise control over their own economic, social and cultural development”. One central part in the convention is that the indigenous peoples should be consulted when there are issues that concern them.<sup>176</sup>

One other important and central issue is the rights of ownership and possession over which the indigenous peoples traditionally used. It says that this land should be recognised and that “measures shall be taken in appropriate cases to safeguard their right to use lands not exclusively occupied by them, but to which they have traditionally had access for their subsistence and traditional activities.” Alexey Limanzo, Chairman of the Association of indigenous peoples of the North of Sakhalin, explains that one of the main problems is that the indigenous peoples of Sakhalin do not have possession rights to their traditional lands.<sup>177</sup> According to Viktor Sereda, the Mayor of Nogliki, the Russian constitution says that indigenous people cannot have a special right to land.<sup>178</sup> The ILO convention however, requires that governments shall “take steps to identify the lands which these peoples traditionally occupy and to guarantee effective protection of their rights to ownership and possession.” The convention also gives the right to the indigenous peoples to participate in the use, management and conservation of the resources on these lands.

The indigenous peoples have got some compensation for the damage on the deer pastures. All the compensation has been channelled by the administration of five districts of Sakhalin, so the indigenous peoples have not seen any compensation so far. This compensation was 800 million Roubles (approximately 27 million USD). They have not either received any compensation for reduced fishing or land use in general. In order for the indigenous peoples to get compensation, the Russian government required that the indigenous peoples tell concretely which resources they feel that they have lost and which areas they consider like their feeding areas.<sup>179</sup> But the indigenous peoples do not know how to count this, so now the indigenous people's key demand is to conduct an ethnological inquiry to collect facts about their people and make an independent investigation on what they can claim from the companies. The women say that SEIC so far has refused to go along with their demand for ethnological expertise, claiming that there is no such requirement in Russian law. And the other companies are even worse.

“Exxon, BP and Rosneft don't even bother to talk to us,” says one woman.

According to SEIC an ethnological expertise requires an assessment of all impacts on the indigenous people's livelihood, not only the impact from SEIC. The company refers to that it currently negotiates an Indigenous Minorities Development Plan with The Sakhalin Authorities and the indigenous peoples. SEIC has already published an interim plan on their webpage.<sup>180</sup>



The indigenous peoples tell SwedWatch that they hope that a specialist will assess the damage level.

“If the damage is real we will demand that the operators pay us compensation, but if not we will apologize,” says one woman.

One woman tells about SEIC’s community liaison officers. She says that there are a lot of them.

“There is no problem in meeting them, in SEIC they are always smiling and cooperate with us, but they don’t do much.”

In an update from Sakhalin Environmental Watch in January 2006 on the situation for the indigenous peoples, Dimitry Lisitsyn, Chairman, points out that while negotiations continue the indigenous peoples suffer from the concrete destruction of their livelihood.<sup>181</sup> He takes an example of families from the indigenous community in a village called Veni. The families can no longer fish in the river Malye Veni because SEIC’s pipeline operations has made the fish disappear.

## Korsakov citizens protests against the LNG plant

The Korsakov district is involved in the project since both the LNG plant and some of the pipeline is built in this district. The people in Korsakov city as well as those who live even closer to the LNG construction site are highly affected by the project. The Mayor, Gunardi Zlievko, has complained publicly on SEIC’s unwillingness to compensate the suffering of the town.<sup>182</sup> The mayor have been in tough negotiations with SEIC in order to raise the rent from 50 000 USD yearly for the 490 hectare area where the LNG plant is built.<sup>183</sup> The Mayor even accused SEIC of trying to pay him a bribe in one meeting in May, something that he later took back after pressure from the company.<sup>184</sup> Finally, Korsakov city sued Sakhalin Energy in a local court to obtain a rent increase. The two sides agreed in September 2005 to a 2.5 million USD annual rent for the land for four years. According to the Mayor there is huge negative impact for the residents and heavy pressure on the infrastructure from the construction site. He tells the BBC that around 2 000 heavy lorries pass through the city every 24 hours and points out that 40 000 people live in poor conditions around the construction site.<sup>185</sup>

SwedWatch had the opportunity to meet with a people’s movement group.

“Our group is called *Knowledge is Strength* because the more we will know, the more possibilities we have to change things, a local museum director,” Elena Lopukhina, explains.

She continues, explaining that they try to collect all information and distribute it to local people. There are about 20 women that have gathered to meet SwedWatch and explain their grievances.

“This project is influencing our lives in so many ways, both environmental and economically. Now we speak about survival because this project has a very heavy impact on our life here. The main question for many people is whether to live here or if we need to leave because of the impact of the project,” says Elena Lopukhina.

Many of the women start to talk about how the natural environment has changed fast over just a few years.

“I remember very well the very beautiful sea coast of Aniva bay, there was a lot of

seaweed and fish along the shore, but now the sea shore is completely empty! There is no seaweed and no fish. I don't know what is going on because no one shares the scientific data with us," says one woman.

Several women explain that SEIC have had so called public hearings, but they do not feel that they really get any information from these meetings.

"SEIC have been lying about everything to the local people, it is just the way they work. They always get very good write-ups in the papers, but in reality there is a very big disparity. It is like a game for the company," says Elena.

For example they tell SwedWatch about how SEIC invited them on a bus tour of the LNG plant, but no one was allowed to go outside the bus and they could not see much through the dirty windows. They also tell how a typical public hearing is organised. SEIC have made an announcement in a very small local paper which no one knows about, so very few people will come.

"If nobody comes, they will report that we had a public meeting and nobody can say anything, one woman jokes."

"There was one meeting where there were much more company representatives than citizens just because of lack of announcements. Nobody knew about it," one other woman state.

There were also some hearings before the project started. Only Elena went to these meetings and they all remember that most of them were actually positive about the project back then. Elena remember that because of the difficult times in the 90's everyone wanted to believe the former governor when he made a lot of promises about how good the project would be.

"He said that this project is our future. It was like an addiction for the local people to believe in the brighter future," says Elena.

Another woman says that she read all the minutes from the public hearings from the North to the South.

"It is obvious that the companies promised a lot and many people were positive toward the project in a preliminary stage, but now it is clear that step by step the promises are broken and it is much worse than expected, much worse," she says.

All the women mention one particular thing that made them change their minds and become critical of the project. One of them says:

"For me it was the beach near the LNG plant. Suddenly I understood that it was impossible to swim and use the beach. The company agreed to pay compensation for the lost beach, but nobody knows what happened to this because the company promised to repair the park, but it is not done. Nobody knows. No money, no park, end of story."

Another woman agrees.

"Yes, it was the sea and the beach. Now it is not alive, it looks dead because it became very dirty from all the dredging. The sea is not alive anymore."

Lina Lazebnik, a teacher at the Korsakov Middle School No. 2, member of Knowledge is Strength, has written a report in December 2004 where she lists all the

different problems they see from the LNG plant construction.<sup>186</sup> Apart from the environmental destruction, there were many social problems when thousands of workers came to the city before places for them to live were prepared, without enough health care etc. She concludes “it’s because of all the problems that we have begun to list here that the local people are starting to look at the LNG plant with more and more antipathy and aggression.”

Apart from the upset citizens of Korsakov, there is also the particular situation for the Dacha community. The community is just one kilometre away from the LNG plant construction. Their beautiful surroundings are turned into an industrial site. But SEIC have decided that they will get no compensation.

“A safety zone of 0.5 km has been established for the LNG/OET facilities by the Russian regulatory authorities. This means that neither the LNG/OET facilities nor the safety (exclusion) zone around them will encroach on the settlement of dachas (summer houses) that lies adjacent to the site, to the west.”

*Chapter 5, EIA, Development of Projects and Alternatives, page 27, [http://www.sakhalinenergy.com/documents/doc\\_38\\_eia\\_1\\_chapter5.pdf](http://www.sakhalinenergy.com/documents/doc_38_eia_1_chapter5.pdf), 2005-12-20*

But according Dmitry Litisyn, SEW, Russian law says that no one is allowed to live within a sanitary zone of 3.5 km around any industrial construction, so the people at the Dacha community cannot stay anyway.

“At the initial stage, two years ago, SEIC promised them that they would be compensated, but now the company breaks its promises,” Dmitry Litisyn says.

## Public consultations lack in democracy

In December 2005 EBRD decided to start off a 120-day consultation period for the Sakhalin 2 phase two project, which means that there will be an intensive period of extensive consultations, both in Sakhalin and between NGOs and their government representatives that will eventually vote for or against a loan from EBRD to SEIC.

SEIC says that they will engage in more public consultations and EBRD plan their consultations in several regions in Sakhalin. SEIC do have Community Liaison Officers throughout the construction area and have arranged public hearings before on the Island.<sup>187</sup> SEIC employ twelve Community Liaison Officers and SEIC’s contractors have another eight CLO’s engaged in consulting the local people.

Local NGOs such as Sakhalin Environmental Watch (SEW) and Knowledge is Strength as well as international NGOs as WWF and Pacific Environment are however worried that the consultations will not really be meaningful. In 2002 the organisation Pacific Environment evaluated the Public Hearings that SEIC organised in December 2001.<sup>188</sup> According to the organisation there were 90 minutes of presentations from the company and only 30 minutes questions and answers from the public. These hearings were visited by only around 40 persons in total. After this, SEW decided to organise alternative hearings with the public. These were visited by around 100 persons and lasted for five hours. SEIC was invited to these hearings but refused to come.

One important issue, since EBRD is going into the public consultation period, will now be what the population at large of Sakhalin thinks of the project. SwedWatch had the opportunity to speak to some people during our visit in October 2005. Our impression is that most local people understand that the oil and gas industry is needed, but they do not trust SEIC's information. There is quite a deep mistrust towards the foreign companies as a whole and especially towards SEIC. On the train, one lady who works in the oil industry in Nogliki says:  
"SEIC tries to tell us that the project is so good and that it will bring so many benefits to Sakhalin. They try to make us believe that it is not dangerous, that it is without any risks. But they do not fool me. I have worked in the oil and gas industry for 15 years, so they can't fool me! I know that it is dangerous business," she says.

A young girl in a restaurant says:  
"The companies don't give a shit. They are just here for the profit, they don't care about the environment or the people here."  
She tells SwedWatch that she thinks that the funds that SEIC pays to social welfare projects on Sakhalin is just given because of tax planning. The local journalist Valentina Prokoshina, who has own experience of the foreign contracting companies that use the local workforce, says:  
"We have become a third world country. The foreign countries come here and they do what they want."

However, the local people also understand the importance of the oil and gas industry to the economy. The lady on the train again:  
"The oil and gas industry is both good and bad. The good thing is for the economy, the jobs and possible development of society. The bad thing is the risks for Nature. And we have a very beautiful and unique natural environment that we need to preserve here at Sakhalin."

It seems as if the local inhabitants of Sakhalin are disappointed in the Sakhalin 2 Phase two project, since many promises were made in the late 90's when the project was still just at the planning stage. Since then they have heard about how SEIC dumped their drilling waste in the Okhotsk sea outside Piltun Bay and the dredging muds in Aniva Bay; they heard about the big catastrophe when tons of herring died 1999 in Piltun Bay and they have not seen any better conditions for heating or for local infrastructure.

SwedWatch receives many warnings that SEIC will just show the official, presentable facts. Andrey Nagibin, chairman of political Green party and leader of NGO Green Partol says:  
"There is one official truth where everything looks very good and then there is the reality reported by the citizens which is very bad."

Jim Niven, SEIC, however warns SwedWatch not to listen too much to some NGOs. Ian Craig, the CEO of SEIC has accused some NGOs of being fundamentalists who are against all oil and gas development.<sup>189</sup>  
"Obviously there are some issues and concerns from some members of the society. We will accept that and we try to work with them and talk to them. We want to be a good neighbour so we can help in local projects and communities and help them develop. This builds up good, neighbourly relations and it also helps preserve what is known as license to operate," Jim Niven explains.

To conclude: the social issues there are several consequences for the people on Sakhalin that comes with the phase two of Sakhalin 2 project. The main demand from the indigenous peoples is that an investigation should be done by an ethnological expert in order for them to be able to demand correct compensation. SEIC is currently involved in negotiations with the indigenous peoples about a five year plan, but at the same time the people suffer from consequences of the project in their daily life. The people in Korsakov are upset by the negative consequences of the construction of the LNG plant on their livelihoods. SEIC has not yet proven that they can handle this disappointment in a proper way. The question of public consultations will be even more important up to April 2006, when EBRD will end its consultation period and will have to take the decision whether to fund the project or not.



*Local protests outside the LNG plant on 28th of January 2006.  
Photo: Dmitry Lisitsyn, Sakhalin Environment Watch.*



# Conclusion and analysis

Phase Two of the Sakhalin 2 project is a highly controversial project; not least because of the fact that the project threatens to drive the Western Pacific Gray whale to extinction. Add to this the construction of an 800 km pipeline over 1100 water sheds with precious wild salmon species, the dumping of dredging material in Aniva bay, the difficulties for the local people, the unsolved social issues and the risk of oil spills and leakages in sensitive nature.

These issues have been presented in detail in this report and different views have been taken into account. Following is an analysis on the basis of this information in order to come to a conclusion on whether SEIC can be accused of violating legislation and/or international guidelines and if the Nordic contractors have done their part in taking on the CSR responsibility in this particular case.

## **Have SEIC followed Russian Law?**

Jim Niven, Deputy External Affairs Manager at SEIC, informs SwedWatch that SEIC has not yet been sued for any matters related to the project.<sup>190</sup> He admits that there are many ongoing cases in courts both in Sakhalin and in Moscow, but he does not want to comment on these. Jim Niven also points out that in most cases SEIC is not the main defender, but rather constitutes a third party. SwedWatch has, however, found two cases where SEIC have actually been filed and fined for acting in breach of the Russian legislation. Jim Niven later admits that there have been some fines “for minor inadvertent errors” and explains that his earlier denial referred to “significant litigation”.<sup>191</sup>

In June 2002 the Federal official entity Sakhalinrybvod imposed a penalty upon SEIC in the amount of 100 000 Roubles (approximately 3 400 USD) for refusal to provide updated, complete and credible information regarding environmental conditions.<sup>192</sup> SEIC made an appeal to the Arbitration Court of the Sakhalin District, but it was turned down in October 2002.

In April 2003 SEIC got another penalty of 40 000 Roubles (approximately 1 300 USD).<sup>193</sup> According to a decision by the Department of Natural Resource Management and Environmental Preservation, The federal entity Sakhalinrybvod has documented “considerable infringements of Nature Resource Protection regulations while platform “Molikpak” was in operation” during 2002. Sakhalinrybvod shows proof that the Molikpak platform exceeded water limits for industrial needs and among other things that the concentration of polluting substances in company sewage exceeded allowable norms.

“Thus, the legal entity-Sakhalin Energy Investment Company LTD-has violated the requirements of Article 92 “Water codes of the Russian Federation””.<sup>194</sup>

In addition to this there are two ongoing lawsuits concerning the legality of Sakhalin 2 activities at Aniva Bay. One of the lawsuits is filed against SEIC by Sakhalin Environment Watch and citizens of Sakhalin (see above for details). In another case regarding the legality of the EIA procedure for the construction of the Temporary Offloading Jetty, Sakhalin Environment Watch and other local plaintiffs won this



case in January 2005, and then won again on appeal on July 27, 2005 (see above for details). Here the Department for Natural Resources was the plaintiff who got fined, but it is still SEIC who built an illegal construction.

On March 2004, The Moscow-based legal centre ‘Rodnik’ filed a lawsuit against the Russian government and the Ministry of Natural Resources, with SEIC as third party.<sup>195</sup> Rodnik believes that the Sakhalin 2, Phase two is a threat to the lives of endangered species mentioned in the Russian Red Book of endangered species. According to the Russian environmental code, any activities harmful to the Red Book species should be stopped. Therefore Rodnik demands the immediate stop of the implementation of Phase Two of the Sakhalin 2 project. The case is ongoing. Swed-Watch have asked for a comment from SEIC, but Jim Niven, SEIC has informed us that they do not comment any ongoing lawsuits.

On the basis of the information, this report concludes that the Sakhalin 2 project lacked legal compliance, that means SEIC have acted in violation of the international guidelines that it says it will follow. In some cases it is strange that SEIC got approvals from authorities, says Dmitry Litisyn, Chairman at Sakhalin Environmental Watch (SEW) as well as Andrey Nagibin, chairman of political Green party and leader of the NGO Green Partol.

“If SEIC cannot get local permission they easily get it from Moscow,” says Andrey Nagibin.

The Russian paper Kommersant, gives an example of a change of the law to suite the oil companies.<sup>196</sup> Article 96 in The Russian Water Code clearly forbids the discharge into water objects. But nevertheless, in 1999, a governmental regulation permitted dumping of drilling agents during the work on the Sakhalin Northeast shelf. This change of regulations was most probably done because of the lobbying of the oil industry, according to the article. The Russian government repealed this regulation in 2000 after the Russian Supreme Court had ruled it unlawful. This forced SEIC to start to re-inject the drilling waste from its platforms.

SEW and Wild Salmon Center both point out that Article 144 in the Water Code forbids discharge of flows and drainage waters in spawning and wintering areas for valuable and protected fish species and in the habitats of Red Book protected wildlife and plant species, something which SEIC have worked in breach of.

SEIC’s legal compliance is therefore very doubtful even today.

### **Does SEIC follow international conventions and guidelines?**

Since international conventions and guidelines often refer to compliance with local law, it is already obvious that SEIC does not live up to these standards. All international conventions in the UN system are mainly directed towards governments, but since SEIC states that it will follow some of the most important conventions concerning environmental and social issues, these are very relevant for SEIC.<sup>197</sup>

As mentioned above (under the section about “The Western Pacific Whale”) WWF International, Greenpeace and Friends of the Earth International argue that SEIC does not follow the precautionary principle of the UN Rio Declaration from 1992.<sup>198</sup> The UN convention on Biological diversity from 1992, which is part of the Rio Dec-

laration and which SEIC says in their official papers that it will follow, says in Article 14 that:

“Introduce appropriate procedures requiring environmental impact assessment of its proposed projects that are likely to have significant adverse effects on biological diversity with a view to avoiding or minimizing such effects and, where appropriate, allow for public participation in such procedures; (b) Introduce appropriate arrangements to ensure that the environmental consequences of its programmes and policies that are likely to have significant adverse impacts on biological diversity are duly taken into account”.<sup>199</sup>

Since SEIC has evidently involved in a lot of work for the preservation of the Western Pacific Whales, it is not very clear if they act in breach of this convention. But as the expert panel of IUCN concluded in February 2005, the *most* precautionary way would be to halt the project until more research had been done. UN:s Global Compact elaborates what the precautionary principle means for business and states that the principle could lead to that companies; “ban or restrict an activity whose impact on the environment is uncertain”.<sup>200</sup>

The decision to reroute the undersea pipeline in order not to cross the feeding area of the whales shows that SEIC did follow the precautionary principle, but the decision to go on with the installation of platform PA-B just seven km away from the feeding area, despite ongoing research, must be seen as a breach of the precautionary principle.

The EBRD admits that SEIC evidently has failed to comply with some of EBRD’s demands.<sup>201</sup> The EIA has later been provided with information, but these changes were made when more than half of the construction was already done. In order for an impact assessment to play the role it should, it must be finalised before the start of the project. SEIC has made some important corrections of its project during the work, such as re-routing of the underwater pipeline away from the direct feeding ground of the Western Gray whales and some erosion prevention methods. These important changes, however, have been made only after strong public pressure from the environmental movement, international media attention and after demands put forth by EBRD. There are several ongoing lawsuits and question marks related to the trenching of the pipeline in spawning rivers as well as the very questionable decision of SEIC to go forward and install the PA-B platform so close to the feeding ground of the Gray whales.

The conclusion in this report is therefore that SEIC have acted in violation of international conventions and of the international guidelines that it states it will follow. It is also highly probable that SEIC still is acting in breach of these international conventions and of the international guidelines.

### **Do the Nordic contractors take their responsibility?**

As SwedWatch and our Nordic counterparts FinnWatch and Norwatch focus on the Nordic business connections to SEIC, we need to analyse the responsibility of the Nordic business partners. The question is how far their environmental and social responsibility can be extended. It is quite clear that the main responsible company

in this case is SEIC, as well as its majority owner, Shell. If Swedish, Norwegian and Finnish firms, however, do business with SEIC and help to construct the project, one may argue that these firms have a co-responsibility for the effects of the project as well.

The Danish Centre for Human Rights, the Confederation of Danish Industries and the Industrialization Fund for Developing Countries have started “The Human Rights & Business project” and published “Defining the Scope of Business Responsibility for Human Rights Abroad” which can be helpful in defining the responsibility in this case as well. The Human Rights & Business project defines the responsibility to be only relevant when the company has an immediate responsibility, not merely a collective responsibility.<sup>202</sup> The collective responsibilities are generally intended for states to look upon. But in the case of Sakhalin 2 Phase Two project there are a lot of immediate consequences: that should mean that there are also some immediate responsibilities that need to be taken by the companies involved. The distinction is, in other words: SEIC and to a lesser degree, its contractors, are not responsible for all the biological diversity on the Sakhalin Island (but the Russian state is) but SEIC and to a lesser degree its contractors, are responsible for the biological species that the project actually affect.

The Human Rights & Business project mentions complicity in human rights violations. In this case it is rather the environmental problems, but the definition of responsibility is similar. The Nordic contractors are indeed indirect contributors to the environmental violations of SEIC. It is SEIC who decided to install the platform PA-B close to the whales feeding area, but it is Quattro Gemini and Aker Kvaerner who build the constructions. It is SEIC who decided to draw the pipeline in the riverbed throughout thousands of sensitive watersheds, but it is ABB that construct the fiber optic cable for the pipeline. WWF has been able to show that the Western Pacific Gray Whales were affected by the installation of the PA-B platform and if it is affected so badly as to be made extinct (which it might be if only one female dies), both SEIC and the Nordic companies building the platforms would have a great responsibility for this. If the rare species of wild salmon in the rivers of Sakhalin are so badly affected by the pipeline construction that some species will become extinct, SEIC will have a major responsibility, but so will ABB.

While talking to the Nordic contracting companies it is obvious that these companies have not taking these issues seriously enough. Most of them have simply taken on contracts without first making any risk reviews. ABB explained that if it had made a risk review today, the conclusion would most probably still have been to accept the contracts and now, when it is active in the middle of the contracts, ABB is not doing anything special to influence SEIC. This could be argued to be against ABB’s environmental policy which clearly states that the company shall promote “environmental responsibility along the value chain by encouraging suppliers, sub-contractors and customers to adopt international environmental standards”. ABB, like most multinational corporations, has written in their official policies that they will comply with local laws. However, neither Gunnel Wisén Persson nor Curt Henricson at Sustainability Affairs, ABB, know how they would act if a customer breaks the law. Some of the lawsuits against SEIC were actually filed before some of the contracts between ABB and SEIC were finalised; ABB has however not reacted.

ABB was one of the first companies to sign the UN General Secretary’s Kofi Annan’s

initiative Global Compact. According to Global Compact companies should support a precautionary approach to environmental challenges, undertake initiatives to promote greater environmental responsibility and encourage the development and diffusion of environmentally friendly technologies.<sup>203</sup> Even though it is not pronounced in Global compact, exactly in what way contractors can influence customers, it is clear that Global compact encourages companies to take such initiatives. In the OECDs guidelines for Multinational Enterprises there is also an encouragement for suppliers to influence their costumers within their sphere of influence.<sup>204</sup> The sphere of influence is obviously larger if the company has a crucial role in the project, something which is true for several of the Nordic companies within the Sakhalin 2 project.

Dmitry Litsyn, chairman at SEW, says that the foreign contractors coming to Sakhalin should at least follow the Russian legislation.

“Secondly, they should know about the problems,” he says.

But he believes that it might be difficult for a contractor to make demands because the contractor is in a weak position in relation to its customer.

“The best thing would be to avoid participating in this bad project. It would be extremely effective if some companies said that they would not participate in such bad project,” he says.

If the companies are already present, however, there are a few things which could be expected by an environmentally and socially responsible company. One major point is to have *knowledge of the environmental and social implications*. Information should also be collected from local NGOs, local citizens and sources independent of the customer. Secondly the companies should *try to influence* the customer to comply with both local law and international guidelines. This could be done in written and verbal form through meetings. If companies feel that they are too small to influence, they could gather Nordic contractors together in order to make such demands.

Both ABB and Consafe Offshore seem to know quite a lot about the local situation, although they have not yet taken any contacts with local NGOs and they have not acted in any way to pro-actively influence SEIC to follow international norms. In the case of Quattro Gemini they state that they trust SEIC because the company mentions all the health, safety and environmental requirements. ABB, Consafe Offshore, SWECO and Quattro Gemini all have the impression that SEIC cares a lot about environmental and social issues. This is a key question since it shows that the companies listen mostly, or only, to the customer’s own information, and not to alternative information from local NGOs which oppose the project. The Nordic contractors have failed to show that they care about the social and environmental consequences of the Sakhalin 2 project. Even though they know about the controversial issues, they have not made any demands upon SEIC so far.

# Recommendations

## **Recommendations from Swedish Nature Conservation Society, Friends of the Earth Sweden and SwedWatch regarding the Sakhalin 2 Phase Two Project**

### **Recommendations to the EBRD and the Swedish Government:**

Based on the findings of this report, SwedWatch, SSNC and FoE Sweden recommends that The European Bank for Reconstruction and Development (EBRD) does not approve any credit to Phase Two of the Sakhalin 2 project. Public resources ought not to be invested in the project, because of the negative environmental and social impacts it brings about. Since EBRD itself acknowledges that the project has violated the bank's environmental policies, it is logic if the funding would not be approved by EBRD's board of directors, including the Swedish government.

SwedWatch, SSNC and FoESweden believe that an ESHIA (environmental, social and health impact assessment) should be finalised before the start of the construction of a project. In this case, the ESHIA was not ready until half of the project was already completed. By then, there will already be an irreversible negative impact.

*The recommendation is;*

EBRD should refrain from offering credit to the Sakhalin 2 Phase Two project. The Swedish government should vote no to EBRD lending money to the project. EBRD does not have to fund the project in order to keep pressure on SEIC, as EBRD is arguing at the moment.

### **Recommendations to Nordic contractors having ongoing business contracts with Sakhalin Energy (SEIC):**

SwedWatch's research shows that the operator SEIC has violated national legislation and international environmental guidelines. The recommendations below are developed especially for the Sakhalin 2 Phase Two project; they could, however, be used for all other similar contractor – customer business relationships.

Based on our findings, SSNC, FoE-Sweden and SwedWatch recommend Nordic contractors involved in the Sakhalin 2 Phase Two Project to take the following actions:

#### **1. Make the following immediate demands on SEIC**

*Environmental issues:*

- Minimize the impact on fish species in the watersheds by strictly follow the ban on trench crossings in rivers during spawning seasons and by simultaneous crossings of the optic-fibre cable and oil and gas pipeline. SEIC must also use strong erosion prevention and control measures, robust construction and operational monitoring and strong contractor control;
- demand a halt in the construction activities of the platforms in the sea area adjacent to Piltun Bay until the Western Gray Whale Advisory Panel is in place and the panel

has presented its independent research about how the Western Grey Whale has been affected.

*Social issues:*

- Make sure that the opportunity for the indigenous peoples to have an independent calculation of their right to compensation is given priority and promptly processed;
- demand public transparency, implying that all relevant publications about the monitoring process should be presented to civil society at large;
- demand that the public hearings shall be conducted in a democratic way, so that all parties can truly participate;
- give support to the Petition by Green Wave Action, January 28, 2006, where the local people demanded recalculating of the damage to fish stocks caused by the LNG plant construction and the pipeline construction and called for the protection of the dacha community (summer houses) from the impacts of the LNG plant.

**SSNC, FoE-Sweden and SwedWatch also recommend that Nordic contractors that are involved in the Sakhalin 2 Project Phase Two to take the following actions:**

**2. Monitor the social and environmental situation**

The collection of information should include sources like local NGOs, affected citizens and other sources independent of the customer (The OECD Guidelines for Multinational Enterprises<sup>205</sup>, 5.1.a and 5.2.b).

**3. Companies involved should *try to influence* the customers to comply with local legislation and international guidelines**

This should be done in both written and oral form through meetings with SEIC. Preferably, the Nordic contractors should cooperate in order to inform SEIC about their demands and discuss these with SEIC at a meeting. This recommendation is based on writings in both The OECD Guidelines for Multinational Enterprises<sup>206</sup> and the UN's Global Compact.<sup>207</sup>

**4. Develop risk review instruments**

In order to be proactive, the contractors should develop measures to avoid getting involved in projects similar to the Sakhalin 2 Project in the future. One way to do this is to develop risk review models. At a minimum level, the risk review should check that an international standard Environmental and Social Impact Assessment is carried out prior to the start of the project. These models must include information from sources that are independent from the customer and involve Non Governmental Organisations, researchers and civil society both during risk assessments before entering a project and afterwards. (The OECD Guidelines for Multinational Enterprises, Chapter 3 and 5.3<sup>208</sup>, Global Compact, Principle 8<sup>209</sup>).

SwedWatch, Swedish Nature Conservation Society and Friends of the Earth Sweden look forward to continuing dialogue with the Nordic companies involved in the Sakhalin 2 project regarding the project itself and the recommendations listed above.



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# Appendix 1

## Sakhalin Energy's Response

The International Energy Agency estimates that total gas supply will almost double between 2002 and 2030. Meeting this demand requires ever more complex frontier exploration in Arctic and sub-Arctic conditions. If rising demand for energy is to be met, Sakhalin II is the shape of projects to come and, with 27% of the world's natural gas reserves, Russia will play a central role. Over 40% of these reserves are located in offshore areas of Russia's continental shelf or internal seas, resulting in projects of similar complexity and scale to Sakhalin II.

The Russian government and the hundreds of Russian enterprises engaged on the project, working in partnership with international companies, are learning the skills, expertise and technology critical for future offshore oil and gas developments.

When completed, Sakhalin II will play a major role in helping Russia meet global energy demand. Sakhalin II's natural gas will be exported to Japan, Korea and further afield to North America, spurring regional growth and helping major energy importers (and Scandinavia's trading partners) continue the trend of using environmentally cleaner natural gas. Sakhalin II also provides a much needed diversity of supply for the region.

We acknowledge that, in a few isolated cases, our performance has failed to reach the high standards that we set ourselves. Whilst any such shortfalls are regrettable, the scale and complexity of such a frontier development make minor lapses difficult to avoid. Every effort is being made to continually improve performance.

We have demonstrated a willingness to listen to and, wherever practicable, take on board the views of stakeholders. Where the arguments presented to us have been well founded we have responded by making appropriate amendments to our plans. Examples include:

- Re-routing the offshore pipeline so to avoid the feeding grounds of the endangered western gray whale. In addition, a long-term advisory panel of independent scientists, funded by Sakhalin Energy, will now be established.
- Agreeing a development plan with and for the Indigenous People of Sakhalin, which will be published by the end of March.
- Revising our river crossings strategy in late 2005 in conjunction with the European Bank of Reconstruction and Development, setting new and transparent standards for environmental protection.
- Committing to funding and devising programmes for enhancing salmon spawning habitats on Sakhalin Island, as well as a special research and monitoring project to learn more about the rare Taimen species.



Having reviewed this report at SwedWatch's request, we conclude it is largely based on a selection of previously publicised secondary allegations and accusations that the Company has publicly addressed on many occasions. It is disappointing that the report over-focuses on selective arguments of lobby groups and thus missed an opportunity for a balanced and informed view. A lack of objectivity unfortunately renders the report's analysis and conclusions unsound.

Contrary to the tone and content of this report, Sakhalin II is setting new standards of performance. This would be impossible without using world-class contractors, some of which are from Scandinavia. For example, Aker Kvaerner and Quattro Gemini subcontracted work to Russian enterprises that accounted for a staggering 83% of the man-hours and 97% of the materials required to build the concrete bases for the two offshore platforms. This is particularly impressive given the design, technology and scale of construction had never before been undertaken in Russia.

Oil and gas investment in Sakhalin is also contributing to local economic prosperity. Living standards are steadily rising and the island's internal revenue has increased five fold since 2002, demonstrating that Sakhalin is the most economically dynamic of all the districts in the Russian Far East.

Investment on Sakhalin has helped drive unemployment in Sakhalin down to 1% - a record low for the Russian Federation. It is also helping to arrest chronic depopulation of one of the remotest regions in Russia. At the close of 2005, 17,000 people, 70% of whom are Russians, were working on the project on the island. In the operations phase, Sakhalin Energy and its contractors will employ around 2400 permanent staff for decades.

Growth is also being propelled by the Sakhalin II US\$400 million infrastructure upgrade programme, through the construction of improved roads, health care facilities, telecoms and waste disposal sites.

And this is no temporary boom. Sakhalin is a world-class energy province probably with more oil and gas reserves than remain in Europe. It is clear that Sakhalin will support subsequent offshore investments. To support all these projects a comprehensive oil and gas service industry will be needed, employing thousands of local people well into the 21st century.

As we have set out above, the challenges posed by Sakhalin II are significant and in some cases without precedent. To find out more and read a full response to this report, please visit Sakhalin Energy's website (<http://www.sakhalinenergy.com/>).



SwedWatch is a non-governmental organisation whose task is to critically examine Swedish business relations with developing countries focusing on environmental and social concerns. SwedWatch consists of five member organisations.

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