

**Inter-American Development Bank: Peru LNG**  
**Position of the United States**  
**December 19, 2007**

The United States recognizes that the Peru LNG project represents a tremendous opportunity for the Peruvian people to create a cohesive energy matrix, to improve energy security, and to make critical investments in poverty reduction in the project's area of influence.

When the IDB Board of Directors was asked in 2003 to approve the use of IDB funds for the Camisea project, the United States did not support that proposal because of our concerns over the availability of private sector finance and thorough implementation of environmental and social protections. These same concerns persisted at the time the IDB Management circulated its consultative note on the Peru LNG project in February 2006. We specifically raised concerns with respect to: (1) the IDB's financial additionality, (2) the impact of recent spills from the Camisea pipeline, (3) the Peruvian Government's capacity for environmental management, (4) the status of commitments by the Peruvian Government under the IDB public sector loan, (5) the adequacy of protection for indigenous peoples, (6) the status of FOCAM, and (7) the consultation process during the Peru LNG design phase.

Nearly two years later, much has been accomplished on these issues. That progress results from three important efforts. First, the sponsors of the Peru LNG project were willing to set a standard of environmental and social best practices well ahead of construction. Second, the ongoing learning process by the Peruvian Government has resulted in improved management of hydrocarbon development in the Lower Urubamba. And third, IDB management has incorporated the lessons learned from Camisea into the LNG project design.

The IDB engaged early and proactively in the creation of this LNG project and has taken a leading role in the lenders group by leveraging its participation in Camisea. This involvement has enabled further progress on environmental and social safeguards with the upstream consortium. The Corrective Action Plans that have resulted from the IDB-sponsored audits of the Camisea project will help address weaknesses resulting from what is now recognized as Camisea's rushed construction. Through its Environmental and Social Management Report (ESMR) for Peru LNG, the IDB has outlined the criteria for better management of the cumulative risks from other hydrocarbon activities in the Lower Urubamba.

We appreciate the efforts of the Peruvian Government to improve effective management of Peru's hydrocarbon resources through its extension of the GTCI and *Defensoria de Camisea* into the LNG project. The Government has also signaled its willingness to address a number of our concerns through a future policy based loan (PBL) for a sustainable energy matrix. The Government's enhanced protections of indigenous peoples, review of over-flight and transport routes in the N-K Reserve, and the removal of concession references by PeruPetro in the Reserve are all important actions. Furthermore, efforts made by the Finance Ministry (MEF) to simplify procedures for use of the Canon and FOCAM royalties have already enabled communities to benefit more directly and expeditiously from the Camisea project. With the Government's continued progress in managing the gas royalties, the Peru LNG project will extend these benefits. All of these actions took place in the context of a very complex decentralization and

reform process that continues to unfold, and all parties recognize that there is much work left to be done.

The Peru LNG sponsors have committed to using industry best practices for the mitigation of environmental and social risks. The Peru LNG project has a detailed environmental management plan and has cross-referenced the environmental requirements of its lenders. These practices also include the purchase of the maximum available emergency insurance to guard against the impacts of future spills or natural disasters. The sponsors' community development program is well designed and participatory, and the lead project sponsor has also agreed to improve community development efforts by coordinating its own efforts with the efforts associated with other funding sources.

This said, the Peru LNG project is not yet what we would consider a model project, largely due to the legacy issues from Camisea that remain unresolved and the not fully realized potential for transforming hydrocarbon resources into social capital. Over the last year, the United States Government has been engaging with the IDB, the Peruvian Government, and the project sponsors in providing our views on how to make progress on these issues and what lessons we have learned from the past. In our view, such resolution is critical not just to the success of the Peru LNG project, but to the Peruvian Government's goal of delivering national and regional economic benefits through hydrocarbon development in an environmentally and socially-sensitive region. We have been encouraged by the receptivity of IDB, Peru LNG, and the Peruvian Government to considering our recommendations and to adopt many of them.

Given the commitment to sustainable management of these hydrocarbon resources by all parties involved in the Peru LNG project, there are, in our view, several areas where more progress should have been made. As the IDB's public sector PBL becomes further defined, we will expect to see a clear emphasis on implementing the recommendations of the Strategic Environmental Assessment for the Lower Urubamba and on developing environmental standards for the energy sector. The decentralization process has complicated implementation of environmental, social, and developmental projects in Peru, most acutely in the context of isolated communities in the Bajo Urubamba. We encourage the Peruvian Authorities and especially the Ministry of Mines and Energy to achieve a balance between hydrocarbon investment opportunities and the risks they represent.

With respect to ongoing monitoring, the IDB management has informed us that it is willing to provide quarterly reporting to the Board of Directors as the project goes to financial closure and execution. We encourage IDB Management to use this reporting mechanism in a forthcoming and proactive manner to call to attention any issues that arise during execution of the project. We urge the IDB Management to work with other Peru LNG lenders to strengthen the independence and coordination mechanisms of the monitoring framework for this project, and to extend them retroactively to the Camisea project. Doing so would help diffuse some of the distrust and misperceptions that are associated with Camisea. The good work done by the lenders and the project sponsors for Peru LNG could go far in remediating problems associated with the earlier project.

The United States Government does not intend for its engagement on this project to end when the IDB Board of Director votes on the Peru LNG project. Most immediately, we've identified areas where we hope progress can be made before the IFC vote. For example, we would like to see measures taken to establish the voluntary producers group for the Bajo Urubamba and to identify which aspects of the ESMR need to be complete before proceeding with financial closure, disbursements, and project completion. Beyond that, we will be closely examining the reporting on this project (both with respect to safeguard and development outcomes), and will not hesitate to engage with management, the Government of Peru and the sponsors if there are indications that the project is not fully complying with all of its commitments.

We believe that development is a process and that incorporating lessons learned into our subsequent interventions results in an improved product. For these reasons, the Peru LNG project does represent an important step forward in development finance in the hydrocarbon sector. And for these reasons and the others mentioned previously, we support the IDB loan.