

Project Administration Manual

Project Number: 49451-002
Loan 3492
November 2016

Republic of Azerbaijan: Partial Credit Guarantee
Shah Deniz Gas Field Expansion Project

ABBREVIATIONS

ADB	–	Asian Development Bank
AzDL	–	Azerbaijan (Shah Deniz) Limited
bcm	–	billion cubic meter
ESIA	–	environmental and social impact assessment
FLMP	–	Fishing Livelihood Management Plan
JOA	–	Joint Operating Agreement
PAM	–	Project Administration Manual
PSA	–	production sharing agreement
SGC	–	Southern Gas Corridor Closed Joint-Stock Company
SGCU	–	SGC Upstream LLC
SPS	–	Safeguard Policy Statement (2009)

CONTENTS

I.	PROJECT DESCRIPTION	1
II.	IMPLEMENTATION PLANS	1
	A. Project Readiness Activities	1
	B. Overall Project Implementation Plan	2
III.	PROJECT MANAGEMENT ARRANGEMENTS	3
	A. Project Implementation Organizations: Roles and Responsibilities	3
	B. Key Persons Involved in Implementation	3
	C. Project Organization Structure	4
IV.	COSTS AND FINANCING	6
	A. Cost Estimates Preparation and Revisions	6
	B. Detailed Cost Estimates by Expenditure Category	7
	C. Withdrawal and Repayment Guaranteed Loan	8
	D. Guarantee Cover and Fees	8
	E. Detailed Cost Estimates by Financier	9
	F. Detailed Cost Estimates by Outputs and/or Components	10
	G. Detailed Cost Estimates by Year	11
	H. Contract and Disbursement S-Curve	12
	I. Fund Flow Diagram	12
V.	FINANCIAL MANAGEMENT	13
	A. Financial Management Assessment	13
	B. Disbursement	15
	C. Accounting	15
	D. Auditing and Public Disclosure: to be updated with PCG requirements	15
	E. Information and Reporting by Lenders	16
	F. Processes of cash call and payment notices	17
VI.	CONSULTING SERVICES	17
	A. Advance Contracting and Retroactive Financing	17
VII.	SAFEGUARDS	17
VIII.	GENDER AND SOCIAL DIMENSIONS	18
IX.	PERFORMANCE MONITORING, EVALUATION, REPORTING, AND COMMUNICATION	19
	A. Project Design and Monitoring Framework	19
	B. Monitoring	21
	C. Evaluation	21
	D. Reporting	22
	E. Stakeholder Communication Strategy	22
X.	ANTICORRUPTION POLICY	23
XI.	ACCOUNTABILITY MECHANISM	23
XII.	RECORD OF CHANGES TO THE PROJECT ADMINISTRATION MANUAL	23

Project Administration Manual Purpose and Process

The project administration manual (PAM) describes the essential administrative and management requirements to implement the project on time, within budget, and in accordance with the policies and procedures of the government and Asian Development Bank (ADB). The PAM should include references to all available templates and instructions either through linkages to relevant URLs or directly incorporated in the PAM.

The Government of the Republic of Azerbaijan (Government) and the Southern Gas Corridor Closed Joint-Stock Company (SGC) are taking part in the implementation of ADB-financed projects. ADB staff is responsible for supporting implementation, including compliance by SGC of their obligations and responsibilities for project implementation, in accordance with ADB's policies and procedures.

At counter-guarantee and indemnity agreement negotiations, the borrower and ADB shall agree to the PAM and ensure consistency with the counter-guarantee and indemnity agreement. Such agreement shall be reflected in the minutes of the counter-guarantee and indemnity negotiations. In the event of any discrepancy or contradiction between the PAM and the counter-guarantee and indemnity agreement, the provisions of the counter-guarantee and indemnity agreement shall prevail.

After ADB Board approval of the project's report and recommendations of the President (RRP), changes in implementation arrangements are subject to agreement and approval pursuant to relevant Government and ADB administrative procedures (including the Project Administration Instructions) and upon such approval, they will be subsequently incorporated in the PAM. The PAM will be updated to reflect the final agreed provisions of the loan agreement and the partial credit guarantee.

I. PROJECT DESCRIPTION

1. The proposed project will provide support in the form of a Partial Credit Guarantee (PCG) backed by a sovereign counter-indemnity, to be issued by the Republic of Azerbaijan (ROA) to Asian Development Bank (ADB) covering \$500 million in principal repayments plus regular interest accrued thereon to support the Southern Gas Corridor Closed Joint-Stock Company (SGC) investments in the Shah Deniz Stage II (Shah Deniz-II).

2. The project will increase the annual gas production capacity of the Shah Deniz Field from 9.8 billion cubic meters (bcm) in 2015 to 26 bcm by 2022. The additional gas will be exported to Europe, via Georgia and Turkey. It represents a first step in creating the southern gas corridor as an alternative for potential future gas deliveries to Europe from other sources in the Caspian region and the Middle East. Thus, the project supports regional cooperation and integration, one of ADB's core operational areas in Strategy 2020, and will improve Europe's energy security by diversifying the sourcing of its gas supply.

3. **Impact and outcome.** The impact of the project is aligned with sustained revenues from oil and gas exports, which will facilitate diversification of the country's economy. The outcome will be increased production and exports of gas from Shah Deniz gas field. Beyond the targeted impact, when complete, the project will help diversify Europe's energy sources and contribute to the development of a multi-seller, multi-buyer market.

4. **Outputs and beneficiaries.** The project's outputs are: (i) Shah Deniz-II natural gas production and processing facility under construction, (ii) greater efficiency in gas sector, and (iii) jobs created during construction and operations. ADB's PCG will help SGC secure financing and the project making progress with: (i) construction of two new bridge-linked oil platforms, (ii) drilling of 26 new subsea wells, (iii) construction of a new 500 kilometer subsea pipeline network, (iv) consolidation of government's interests in Shah Deniz within a single entity, and (v) creation of over 19,000 temporary and 1,800 permanent local jobs during construction and operation of Shah Deniz-II, respectively. At least 15% of the permanent local jobs are expected to be for women.

II. IMPLEMENTATION PLANS

A. Project Readiness Activities

Table 1: Processing Schedule

Indicative Activities	2016-2017													Agency Responsible	
	Month														
	9	10	11	12	1	2	3	4	5	6	7	8	9		10
PCG and CGIA negotiations		X													ADB, MOF, SGC
ADB Board consideration			X												ADB
PCG and CGIA signing				X											ADB, MOF, SGC
Sovereign Guarantee signing				X											ADB, MOF, MOJ
Commercial Loan Agreement Signing				X											Commercial Banks, SGC
PCG and CGIA effectiveness				X											ADB, MOF, SGC
Sovereign Guarantee effectiveness				X											ADB, MOF, MOJ
Commercial Loan Agreement effectiveness				X											Commercial Banks, SGC

ADB = Asian Development Bank, CGIA = counter-guarantee and indemnity agreement, MOF = Ministry of Finance, MOJ = Ministry of Justice, PCG= partial credit guarantee, SGC = Southern Gas Corridor Closed Joint-Stock Company.

III. PROJECT MANAGEMENT ARRANGEMENTS

A. Project Implementation Organizations: Roles and Responsibilities

Table 3: Management Roles and Responsibilities

Organizations	Management Roles and Responsibilities
<ul style="list-style-type: none"> • [Office of the Deputy Prime Minister 	<ul style="list-style-type: none"> • Overall coordination of inter-government agencies]
<ul style="list-style-type: none"> • Ministry of Finance (MOF) on behalf of the Republic of Azerbaijan 	<ul style="list-style-type: none"> ➤ Representative of Sovereign Guarantor
<ul style="list-style-type: none"> • Southern Gas Corridor Closed Joint-Stock Company (SGC) 	Borrower and Executing Agency <ul style="list-style-type: none"> ➤ Project execution ➤ Ensuring loan proceeds are used in accordance with the Loan and Guarantee Agreement ➤ Project progress reporting to ADB ➤ Meet all conditions precedents to withdrawals, comply with loan covenants, representations and warranties under the Commercial Loan provided by the Commercial Banks.
<ul style="list-style-type: none"> • [TBD] 	Commercial Banks <ul style="list-style-type: none"> ➤ Provide the Commercial Loan directly to the Borrower ➤ Be responsible ➤ Ensuring loan proceeds are used in accordance with the Loan and Guarantee Agreement
<ul style="list-style-type: none"> • Asian Development Bank (ADB) 	Guarantor <ul style="list-style-type: none"> ➤ Provide partial credit guarantee to the Commercial Banks. ➤ Monitor and review overall implementation of the project in consultation with executing agency including: the project implementation schedule, actions required in terms of poverty reduction, environmental impacts, and resettlement plans (RPs), as applicable; timeliness of budgetary allocations and counterpart funding; project expenditures; statement of expenditure when applicable; compliance with particular loan covenants; and the likelihood of attaining the project's immediate development objectives.

B. Key Persons Involved in Implementation

Executing Agency

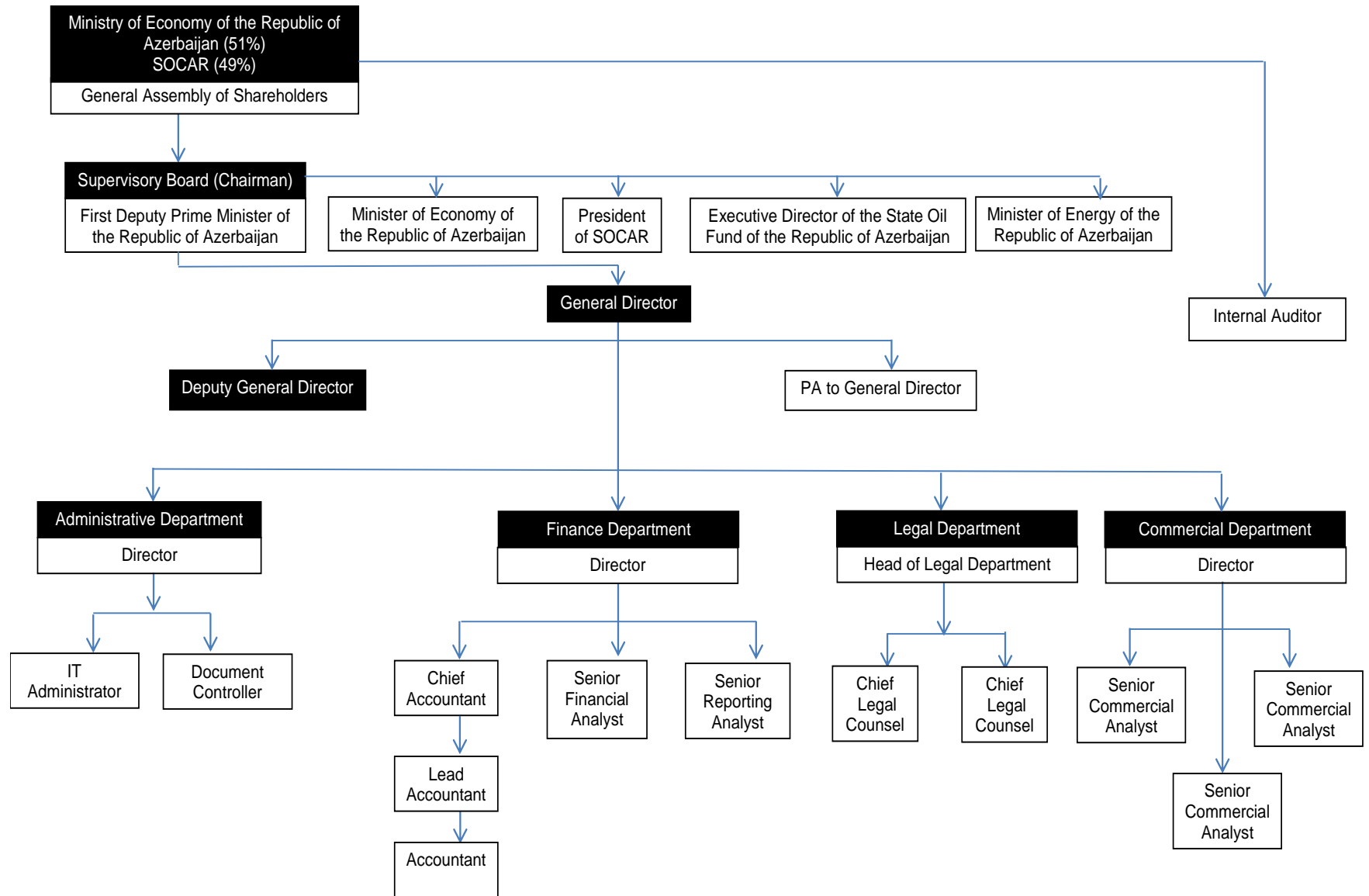
SGC	Officer's Name	Afgan Isayev
	Position	General Director
	Telephone	+994 12 521 3092
	Email address	afgan.isayev@sgc.az
	Office Address	121 Heydar Aliyev Avenue, SOCAR Tower, 4 th floor, Baku, AZ1029, Azerbaijan
ADB	Staff Name	F. Cleo Kawawaki
Division Director	Position	Director, Energy Division, Central and West Asia Department (CWRD/CWEN)

	Telephone No.	+63-2-632-6113/5950
	Email address	cwen@adb.org ; fkawawaki@adb.org
Mission Leader	Staff Name	Megan Wolf
	Position	Energy Specialist, CWEN
	Telephone No.	+63-2-632-6388/5391
	Email address	mwolf@adb.org
Mission Leader	Staff Name	Roland Pladet
	Position	Principal Public-Private Partnership (PPP) Specialist
	Telephone No.	+63-2-632-6918/6178
	Email address	rpladet@adb.org
Country Director	Staff Name	Nariman Mannapbekov
	Position	Country Director
	Telephone No.	+994437 6600
	Email address	nmannapbekov@adb.org

C. Project Organization Structure

5. SGC is a company dedicated to managing the Azerbaijan state's stakes in the projects of the Southern Gas Corridor. Its organizational structure acts as the project management structure.

SOUTHERN GAS CORRIDOR CLOSED JOINT-STOCK COMPANY ORGANIZATION AND MANAGEMENT STRUCTURE



SOCAR = State Oil Company of Azerbaijan Republic.

IV. COSTS AND FINANCING

6. The overall Shah Deniz-II project cost estimates are prepared by the designated operator of the project, BP. SGC estimates its cash requirements.

Table 4:[CONFIDENTIAL INFORMATION DELETED]

A. Cost Estimates Preparation and Revisions

7. Cost estimates for the whole of Shah Deniz-II project have been prepared by BP as the operator of the project. Projections (forecasts) are updated regularly as the project progresses. Total project costs (Master Cost Estimates) are updated once or twice a year. The estimates of cash call and payment invoice requirements are prepared by SGC for its portion of the project cash requirements based on the cost estimates by the operator.

B. Detailed Cost Estimates by Expenditure Category

Table 5:[CONFIDENTIAL INFORMATION DELETED]

C. Withdrawal and Repayment Guaranteed Loan

8. Provisions reflecting final PCG documentation to be inserted, [During the [TBD] month availability period starting from financial close of the Commercial Loan Agreement, draw-downs (withdrawals) may be requested from time to time by the Borrower from the Lenders to:

- (i) finance and/or refinance cash calls and payment invoices for the development the Shah Deniz gas field; and
- (ii) finance and/or refinance [up to the end of the [TBD]-month grace period,] all front end fees, commitment fees, interest, [breakage], ADB PCG fees, legal and other costs related to the Project.

9. The loan amount will be repaid by the Borrower to the Lenders [semi-annually in N] equal installments plus corresponding interest accrued on outstanding principal amounts, the first repayment to be made [TBD] months from financial close. To be determined based on PCG requirements.]

D. Guarantee Cover and Fees

10. The PCG will provide up to 95% in non-payment cover for up to \$526 million in principal, plus accrued regular interest, guarantee fees and potential breakage costs.¹ Following non-payment of principal and/or interest by the Borrower and, subsequently, MOF, the lenders will submit a claim with ADB under the PCG. Upon assessment of the validity of such claim, ADB will make a guarantee payment to the lenders. PCG. ADB will charge guarantee and commitment fees² based on ADB's equivalent pricing for sovereign loans.³

11. ADB will receive a sovereign counter-guarantee and indemnity from the Republic of Azerbaijan. Under the sovereign counter-guarantee and indemnity provided to ADB, the Republic of Azerbaijan will indemnify ADB for any payments made by ADB, or any loss incurred by ADB under the PCG.

12. [As security for the payment of the PCG fees, the ADB Guaranteed lenders shall maintain a PCG Fees Deposit with ADB in an amount equal to [N] from the [Effective Date] until the date on which all PCG Fees have been paid in full. The applicability of this requirement and mechanism to be negotiated and agreed between parties].

¹ In the event SGC opts for a fixed interest rate instead of a floating interest rate, the PCG cover amount may include a pre-agreed amount in breakage costs incurred by the guaranteed lenders following potential nonpayment by SGC and MOF.

² For each interest period, the guarantee fees are calculated over the guaranteed percentage of the disbursed loan principal outstanding and amount of interest payable during such period. Similarly, commitment fees are calculated over the difference between the amount of maximum aggregate liability under PCG and the guaranteed.

³ Subject to ADB's Pricing and Credit Enhancement Committee (PCC) endorsement.

E. Detailed Cost Estimates by Financier

13. Not applicable to this project.

F. Detailed Cost Estimates by Outputs and/or Components

14. Not applicable to this project.

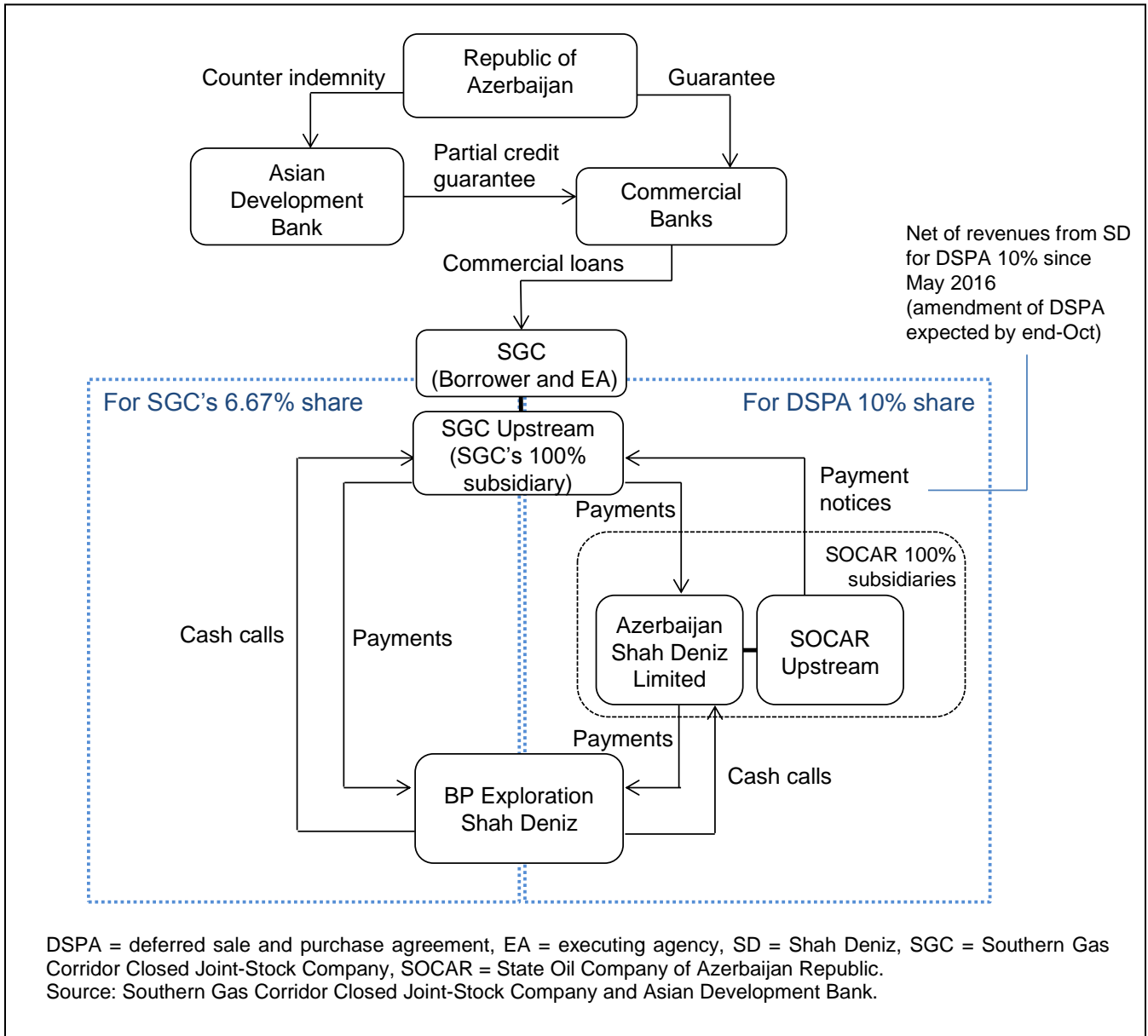
G. Detailed Cost Estimates by Year

Table 7:[CONFIDENTIAL INFORMATION DELETED]

H. Contract and Disbursement S-Curve

15. Disbursement will be made according to the financing agreement between commercial lenders and SGC, and not applicable in PAM.

I. Fund Flow Diagram



V. FINANCIAL MANAGEMENT

A. Financial Management Assessment

16. The financial management assessment (FMA) was conducted in September 2016 in accordance with ADB's Guidelines for the Financial Management and Analysis of Projects and the Financial Due Diligence: A Methodology Note. The FMA considered the capacity of the SGC, including funds-flow arrangements, staffing, accounting and financial reporting systems, financial information systems, and internal and external auditing arrangements.

17. SGC generally follows sound financial management principles. It has well documented financial management procedures and processes, and appears to be adequately staffed by competent professionals. It is externally audited by internationally recognized firms and has not incurred any material audit qualifications since its incorporation in 2014.

18. The requirements and management of multi-billion dollar cash calls for multiple projects is a challenge for SGC. SGC has centralized and efficient operations as a small entity of 24 staff as of September 2016 with a very focused mandate of managing investments in the pipelines and field development of the Southern Gas Corridor.⁴ It also benefits from a well-structured management processes of the whole of Shah Deniz-II project. One of the world's leading oil and gas companies, BP, is the designated operator of the project, in charge of field development and operations. Technical verification of progress is conducted by SOCAR Upstream for SGC. SOCAR Upstream is a 100% subsidiary of the State Oil Company of Azerbaijan Republic (SOCAR), Azerbaijan's fully state owned oil and gas company. Based on these multiple layers of verifications, SGC prepares financing and responds timely to cash calls. Securing sufficient financing in a timely manner is and will be the major challenge of SGC. SGC has already engaged an international financial advisory firm in preparing its financing plans and is procuring funds from the market and international financial institutions.⁵

19. The key financial management weaknesses is the absence of experience in executing a project funded by bilateral or multilateral development partners while a large portion of the financing is planned from ADB, the European Bank for Reconstruction and Development and the World Bank Group. SGC recognizes this issue and has engaged with these multilateral partners early on to mitigate the potential delays of securing funds. The overall risk assessment is "moderate." The challenge and risk of financial structuring is already partially addressed by SGC's engagement of a financial advisor. In case financing is delayed, SGC's shareholders are required by a resolution of the State Commission to inject additional equity sourced from State Oil Fund of the Republic of Azerbaijan (SOFAZ) to support the cash needs of SGC. The issue of the lack of experience with multilateral development partners is largely mitigated for ADB operations since ADB sovereign operations' involvement is through a partial credit guarantee and disbursements will be made from commercial lenders.

20. Table 8 summarizes the key financial management risks identified in the assessment.

⁴ Southern Gas Corridor as an initiative consists of the full field development of Shah Deniz (Stage I and Stage II), SCPX, TANAP and TAP pipeline projects.

⁵ Lazard Freres has been engaged as a financial advisor to SGC since 2014.

Table 8: Risk Assessment and Management Plan

Risk Description	Risk Assessment	Mitigation Measures / Management Plan
	Assessment	
Inherent Risk		
Country-Specific – External audit of public sector entities is effective and follow-up is comprehensive, however audit does not currently have sufficient coverage (only 30% of state expenditure is included) (from PEFA review in 2014).	Substantial	Through dialogue with the Government, ADB will request that public sector audit extends to power sector entities from 2016. ⁶
Entity-Specific – SGC's financing needs are large and on-going. Internal processes are well established and documented, but securing large funding in a timely manner, especially working with international financial institutions' specific requirements will be a challenge for SGC.	Moderate	Financial and legal advisors have been engaged by SGC's own funding. Their resources will be kept available (an action plan item) to support SGC's management of cash requirements for its projects.
Overall Inherent Risk	Moderate	
Control Risk		
Internal Audit – SGC currently does not have an internal auditor but is in the process of recruiting one.	Moderate	SGC will speed up the process and recruit an internal auditor within 6 months of PCG agreement signing (an action plan item). Internal auditor's mandates and manual are prepared and documented. Further, SGC has focused and rather straight-forward operations, the processes of which are well documented and followed.
Information Systems – although IT for financial management is strong and automated within each of SGC's project specific subsidiaries, the consolidation of accounts is conducted by Excel.	Moderate	All subsidiaries report in the same heading and format, facilitating the consolidation process by SGC. Further, external auditors will audit SGC's financial statements. SGC will also provide evidence of the use of proceeds to ADB through commercial lenders (copies of cash calls, payment notices from SOCAR Upstream, and bank transfer records).
Overall Control Risk	Moderate	
Overall (Combined) Risk	Moderate	

ADB = Asian Development Bank, IT = information technology, PEFA = public expenditure and financial accountability, PCG = partial credit guarantee, SGC = Southern Gas Corridor Closed Joint-Stock Company.

21. Based on this assessment, action plans to improve financial management capacity of SGC are the following.

⁶ ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranchise Financing Facility for Power Distribution Enhancement Investment Program*. Manila.

Table 9: Risk Action Plan

Action	Responsibility	Resources	Timing
Recruit an internal auditor.	SGC	SGC	Within 6 months from loan signing.
Continued engagement of the financial advisor for updating its financing plans and procuring funds.	SGC	SGC	Monitored every 2 months up to the end of external debt raising process.

ADB = Asian Development Bank, SGC = Southern Gas Corridor Closed Joint-Stock Company.

B. Disbursement

22. Proceeds from the ADB guaranteed commercial loans will be disbursed in accordance with the financing agreements between the Borrower and the commercial banks.

23. Pursuant to ADB's Safeguard Policy Statement (2009) (SPS),⁷ ADB-guaranteed funds may not be applied to the activities described on the ADB Prohibited Investment Activities List set forth at Appendix 5 of the SPS.

C. Accounting

24. SGC will prepare consolidated financial statements in accordance with the local accounting laws and regulations or with international accounting principles and practices.

D. Auditing and Public Disclosure: to be updated with PCG requirements

25. Audit and public disclosure provisions reflecting final PCG documentation and to the extent acceptable to SGC to be inserted. SGC will cause the consolidated company financial statements to be audited in accordance with International Standards on Auditing, by an independent and internationally recognized auditor, whose qualifications, experience and terms of reference have been evaluated by SGC.

26. The audited entity financial statements, together with the auditor's report and to the extent possible, the management letter including opinion on compliance with financial covenants (if any), will be submitted in the English language to ADB through the commercial lenders within 1 month after their approval by the relevant authority until the end of the ADB-guarantee term for as long as the guarantee is outstanding.

27. SGC will be required to provide cash call statements, payment notice statements and proof of payment for the project cash calls and deferred sale and purchase agreement (DSPA) progress payments directly or indirectly to ADB to substantiate the intended use of proceeds of the ADB-guaranteed loans.

28. Compliance with financial reporting and auditing requirements will be monitored by review missions and during normal program supervision, and followed up regularly with all concerned, including the external auditor.

⁷ Available at: <https://www.adb.org/Documents/Policies/Safeguards&/Safeguard-Policy-Statement-June2009.pdf>.

29. The Government and SGC have been made aware of ADB's approach to delayed submission for required reporting, and the requirements for satisfactory and acceptable quality of the audited company financial statements.⁸ While there will be no project specific audit reports, SGC will be required to provide cash call statements, payment notice statements and proof of payment for the project cash calls and DSPA progress payments directly or indirectly to ADB to substantiate the intended use of proceeds of the ADB-guaranteed loans. These audit requirements will be further detailed in the 'ADB Required Provisions' in the guaranteed loan.

E. Information and Reporting by Lenders

30. The PCG Agent shall provide to ADB as the Guarantor true and complete copies of the Commercial Loan Agreement, the Sovereign Guarantee and the other Financing Documents (together the "Transaction Documents") within [ten (10)] Business Days after the date of the Loan Agreement. The Sovereign Guarantee refers to the guarantee agreement dated [xx] by the Republic of Azerbaijan in favor of the Guaranteed Lenders.

31. The Transaction Documents must be either: (i) similar in all material respects to the draft copies provided to the Guarantor on or most recently prior to the Signing Date, or (ii) otherwise satisfactory in form and substance to the Guarantor acting reasonably.

32. The PCG Agent shall provide to the Guarantor copies of each Guaranteed Commercial Agreement within ten (10) Business Days of receipt by the PCG Agent of such Guaranteed Commercial Agreement.

33. [During the Guarantee Term; any period after the Guarantee Term in which the Lenders have a Demand pending; and [one year] following the payment of any Demand, the PCG Agent shall: (i) request under the Loan Agreement from the Borrower, within [six (6) months] after the close of each of its fiscal years, copies of its annual balance sheet and profit and loss statement and such other financial statements as may be required by the Guarantor, prepared (if available) in accordance with the International Accounting Standards and audited by an independent public accountant; (ii) retain the documents referred to at the PCG Agent's principal place of business or such other place agreed by the Guarantor; (iii) deliver to the Guarantor a copy of each borrowing or utilization notice delivered to the Guaranteed Lenders under the Loan Agreement and notify the Guarantor promptly after the date on which each disbursement is made under the Loan Agreement; (iv) promptly furnish to the Guarantor such statements, data or other information as the Guarantor may reasonably request which relate to this Guarantee, the Sovereign Guarantee, the Loan or the Guaranteed Commercial Agreements; if this Guarantee is issued prior to the execution or applicable amendment of any Guaranteed Commercial Agreement, then promptly provide to the Guarantor a copy of such

⁸ ADB's approach and procedures regarding delayed submission of audited project financial statements:

- (i) When audited project financial statements are not received by the due date, ADB will write to the executing agency advising that (a) the audit documents are overdue; and (b) if they are not received within the next 6 months, requests for new contract awards and disbursement such as new replenishment of imprest accounts, processing of new reimbursement, and issuance of new commitment letters will not be processed.
- (ii) When audited project financial statements are not received within 6 months after the due date, ADB will withhold processing of requests for new contract awards and disbursement such as new replenishment of imprest accounts, processing of new reimbursement, and issuance of new commitment letters. ADB will (a) inform the executing agency of ADB's actions; and (b) advise that the loan may be suspended if the audit documents are not received within the next 6 months.
- (iii) When audited project financial statements are not received within 12 months after the due date, ADB may suspend the loan.

Guaranteed Commercial Agreement or any amendment to such Guaranteed Commercial Agreement; promptly after the PCG Agent becoming aware thereof, notify the Guarantor in reasonable detail of:

- (a) any event or circumstance that in its opinion is likely to cause a default (regardless of the cause) under this Guarantee or an event of default under the Loan Agreement and/or the Sovereign Guarantee;
- (b) any notification received by it (by itself or from any of the Guaranteed Lenders) from the Government, the Sovereign Guarantor or the Borrower regarding any proposed or possible default under the Loan Agreement and/or the Sovereign Guarantee;
- (c) any event of default under the Loan Agreement and/or the Sovereign Guarantee;
- (d) any prepayment of the Loan (or part thereof);
- (e) the institution of any material court proceedings or arbitration against the Borrower (including insolvency or wind up proceedings); and
- (f) any change in the name, corporate identity or legal nature of the Borrower or any of the Guaranteed Lenders.

F. [CONFIDENTIAL INFORMATION DELETED]

34.

35.

36.

37.

38.

39.

40.

41.

42.

VI. CONSULTING SERVICES

43. Consulting services will not be required under the Project.

A. Advance Contracting and Retroactive Financing

44. There are no procurement activities under the Project.

45. **Retroactive financing.** Retroactive financing will be considered for SGC's pro rata share in 2016 cash calls and payment notices for the DSPA shares already paid by SGC subject to ADB's policies and procedures.

VII. SAFEGUARDS

46. **Environment.** In compliance with ADB's Safeguard Policy Statement (2009) (SPS), the

project is classified category A for environment. Potential environmental impacts of the project have been identified by the environmental and social impact assessment (ESIA) conducted for the project, and effective measures to avoid, minimize, mitigate, and compensate for the adverse impacts are incorporated in the environmental management plan in the ESIA. Furthermore, as required by SPS an environmental and social compliance audit for the existing facilities of stage I of the project (Shah Deniz-I) and ongoing construction activities as part of stage II expansion of the gas field (Shah Deniz-II) was carried out. The audit did not find any non-compliance of ADB policies associated with the ongoing construction activities, and no corrective action plan is needed. The institutional capacity and commitment of the borrower to cause the operator to manage the project's social and environmental impacts are deemed adequate.

47. The ESIA indicates that construction impacts are minimal, with fish having previously demonstrated avoidance behaviors. Fishing is the dominant threat to fish populations in the Caspian Sea. Existing fish population monitoring programs established for Shah Deniz-I are satisfactory to ADB and will continue. The contract area may have some overlap with Caspian seal migration pathways. BP engages with and provides support to the Caspian Sea conservation programs, which provide a whole-of-sea approach to seal conservation. BP has in place an ecological and wildlife management plan. The Borrower will be required to procure, to the extent possible under the relevant project agreements, that the operator implements the project in compliance with the relevant plans and ADB's SPS requirements.

48. **Involuntary resettlement:** The project is classified as category B for resettlement impacts. In line with ADB's Safeguard Policy Statement (2009) requirements for financing of existing facilities, an environmental and social compliance audit for the existing facilities of Shah Deniz-I and ongoing construction activities as part of Shah Deniz-II was carried out. The audit did not find any non-compliance of ADB policies associated with the past and ongoing construction activities. All lands required for siting the project facilities are government lands and have been transferred to the operator by SOCAR. No outstanding issues with respect to usage of the lands required for the project components exist. Furthermore, additional land acquisition or physical displacement impacts are not expected.

49. On the other hand, the audit confirmed that the livelihoods of 48 fishermen carrying out small scale fishing at the Sangachal bay have been affected for a period of 10.5 months (starting December 2014) due to the enforcement of marine exclusion zone for the installation of pipelines. A Fishing Livelihood Management Plan (FLMP) was prepared to address the economic displacement impacts in consultation with the 48 affected fishermen. While the entitlements under the FLMP have been fully paid to the affected persons, compensation for additional impacts due to increased transportation costs (reported by 6 of the 48 affected fishermen) are being finalized by the Operator, in consultation with the affected persons. The Operator will carry out monitoring of the implementation of the FLMP and prepare a closure report of FLMP implementation once all residual grievances are satisfactorily addressed.

50. **Indigenous people.** The project has been classified as Category C on indigenous peoples following ADB's Safeguard Policy Statement, 2009 (SPS). The Project is not expected to impact any distinct and vulnerable group of indigenous peoples as defined under SPS.

[Demand under PCG provisions reflecting final PCG documentation to be inserted.]

VIII. GENDER AND SOCIAL DIMENSIONS

51. The project will (i) provide revenues to support non-resource sector developments, (ii) modernize the oil and gas sector, (iii) promote efficient use of energy resources, and (iv) increase sector operation efficiency. Consultations carried out reveal the people's basic concern over the lack of employment opportunities, exacerbated by the lack of adequate skills to be employed in the recent development in the area. The community engagement plan and workforce management plan developed for the project recognizes the following key social issues in engagement efforts with the communities: (i) potential for influx issues, (ii) the need to enlarge the contractors' existing workforce significantly, (iii) proximity to vulnerable communities, and (iv) communities' expectations. In line with these issues, targets for recruitment from named communities were included in the construction contracts.

52. The project is categorized as 'No Gender Elements.' Women are not expected to directly benefit from the project as far as employment is concerned. The status of women—in relation to their employment status, level of maximum education attained, and participation in society—was discussed during women's focus groups held in each community. The socioeconomic surveys indicated a lesser likelihood of women being employed (19%) in the project compared with men (79%). Women were also less likely to be interested in undertaking technical training than men. In 2012, women's employment in the energy sector was only 15%. While job vacancies are generally lacking locally, particularly fewer opportunities are (perceived to be) suitable for women. While women are the primary users of energy in the home, making them more vulnerable to risks related to fluctuating energy supply and use, men continue to make the major decisions on sources and types of energy to use. Irregular power supply has a particularly negative impact on the elderly and women in rural or remote areas. Women lack information on efficient energy use. And despite the high income potential, the energy sector had no female private entrepreneurs in 2010.

53. The project is expected to directly benefit community members in the command areas who can avail of jobs through the project. Individuals included in the socioeconomic survey, who had previously worked on contracts with BP, consistently reported positive experiences—particularly in terms of increasing their household income, developing their skills, and improving future career prospects. To maximize benefits to the local population and address the key poverty issues associated with lack of employment opportunities, the project will encourage contractors to prioritize the recruitment of qualified local community members. Trainings on construction related jobs will be conducted before and during employment.

[Loan Safeguards provisions reflecting final PCG documentation to be inserted, disclosure to be agreed once the provisions have been agreed]

IX. PERFORMANCE MONITORING, EVALUATION, REPORTING, AND COMMUNICATION

A. Project Design and Monitoring Framework

DESIGN AND MONITORING FRAMEWORK

Impact the Project is Aligned with

Sustained revenues from oil and gas exports that will facilitate diversification of the country's economy
(Source: Azerbaijan 2020: Look into the Future)

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting	Risks
Outcome Increased production and exports of gas from Shah Deniz gas field	Volume of annual peak gas production from the Shah Deniz gas field (SD1 and SD2) of 26 bcm per annum achieved by 2022 (2015 baseline: 9.8 bcm per annum)	BP's annual progress report	Full operations of Shah Deniz-II delayed Pipeline projects are not completed as planned
Outputs 1. Shah Deniz-II natural gas production and processing facility under construction. 2. Greater efficiency in gas sector	1a. Progress in construction of two new bridge-linked offshore platforms to be commissioned by 2020 (2015 baseline: 0) 1b. Progress in drilling of 26 new subsea wells to be operational by 2020 (2016 baseline: 10) 1c. Progress in construction of 500 km of new subsea pipeline to be completed by mid-2020 (2015 baseline: 0 km) 2a. Progress in consolidation of government's interests in Shah Deniz within a single entity (2016 baseline: Government interests represented by SOCAR and SGC)	1a-c. BP's annual progress report. 2a. SGC annual financial reports	Unanticipated technical challenges during drilling of wells. Complex structure of contracts that involve many subcontractors and joint ventures leads to delays in project implementation and/or technical or safety problems during construction. Limited experience working with multilateral financing institutions while relying substantially on such financing, leads to delay in securing financing.
3. Jobs created during construction and operations	3a. Creation of over 19,000 temporary jobs during construction (2014–2020) (2015 baseline: 16,000) and 1,800 permanent local jobs (15% of which are expected to be for women) during operation of Shah Deniz-II by 2022 (2016 baseline: 0)	3a. BP's environment and social safeguard monitoring report	

<p>Key Activities with Milestones</p> <ol style="list-style-type: none"> 1. Commercial loan signing, counter-guarantee and indemnity execution, and ADB PCG execution (December 2016) 2. Satisfaction or waivers of conditions precedent for disbursements (December 2016) 3. Disbursement December 2016 to December 2017^a 4. Continued payments of cash calls by SGC to meet participation requirements until December 2017^a
<p>Inputs</p> <p>ADB PCG-covered commercial loan: \$526.0 million (utilizing OCR counter-guaranteed by the Republic of Azerbaijan)^b</p> <p>ADB: \$500.0 million nonsovereign loan^c</p> <p>Commercial Financing: \$1,141.0 million</p> <p>SGC's equity and bond financing: \$2,648.0 million</p>
<p>Assumptions for Partner Financing</p> <p>Not Applicable</p>

ADB = Asian Development Bank, bcm = billion cubic meters, km = kilometer, PCG = Partial Credit Guarantee, Shah Deniz-II = Shah Deniz Stage II, SGC = Southern Gas Corridor Closed Joint-Stock Company, SOCAR = State Oil Company of Azerbaijan Republic.

^a Should SGC's actual 2016 and 2017 financing needs be lower than currently estimated, SGC may use any undrawn principal amounts under the ADB-guaranteed commercial loan to its 2018 financing needs, resulting in potential disbursements and cash call payments in 2018.

^b This value may be reduced if cofinancing or other sources of funding can be obtained. Principal amount based on 95% coverage.

^c ADB's Private Sector Operations Department is also considering the provision of financing up to \$500 million.

Source: Asian Development Bank.

B. Monitoring

54. **Project performance monitoring.** Provisions reflecting final PCG documentation to be inserted. [The Commercial Banks will provide ADB with quarterly reports including that for disbursement and compliance with ADB policies and guarantee and loan covenants. These reports will provide information necessary to update ADB's project performance reporting system.]

55. **Compliance monitoring.** The EA will ensure that the project is undertaken, and that all project facilities are designed, implemented, operated, and maintained, in accordance with the applicable laws and regulations of the Government of Azerbaijan and the ESIA.

56. Loan covenants — policy, legal, environmental, and others — will be monitored through semi-annual project reviews and the midterm review.

57. **Safeguards monitoring.** Provisions reflecting final PCG documentation to be inserted.

58. **Gender and social dimensions monitoring.** : To be determined with PCG requirements.

C. Evaluation

59. **Inception mission.** ADB will field an inception mission after loan signing to (i) establish a working relationship between ADB, government and SGC; and (ii) to ensure that the government and SGC understand ADB's procedures.

60. **Review missions.** ADB will field annual review missions to review overall implementation of the project and update project implementation schedule based on mission findings.

61. **Project completion reporting and review.** ADB will prepare a project completion report or an extended annual review report based on SGC's quarterly and annual reports.

D. Reporting

62. SGC will provide ADB with (i) quarterly progress reports of the project; and (ii) consolidated annual reports including (a) progress achieved by output as measured through the design monitoring framework indicator's performance targets, (b) key implementation issues and solutions, and (c) updated implementation plan until project completion as defined by the design monitoring framework. To ensure that projects will continue to be both viable and sustainable, the executing agency's audited financial statement together with the associated auditor's report, should be adequately reviewed by ADB.

E. Stakeholder Communication Strategy

63. The following table outlines the framework of communication strategy to be adopted for the project.

Project Documents*	Means of Communication *	Responsible Party	Frequency
Project Information Documents (PID)	ADB website	ADB	Initial PID no later than 30 calendar days of approval of the concept paper, quarterly afterwards.
Design and Monitoring Framework (DMF)	ADB's website	ADB	Draft DMF after post fact-finding mission
Environment and Social Impact Assessment	ADB's website	ADB	At least 120 days before Board consideration
Resettlement Planning Documents	ADB's website	ADB	Post fact-finding mission
Report and Recommendations of the President	ADB's website	ADB	Within 2 weeks of Board approval of the loan
Sovereign counter indemnity	ADB's website	ADB	No later than 14 days of approval of the project.
Initial Poverty and Social Assessment	ADB's website	ADB	Within 2 weeks of completion
Project Administration Manual	ADB's website	ADB	After loan negotiations
Social and Environmental Monitoring Reports	ADB's website	ADB	Routinely disclosed, no specific requirements
Major Change in Scope	ADB's website	ADB	Within 2 weeks of approval of the change

Project Documents*	Means of Communication *	Responsible Party	Frequency
Progress Reports	ADB's website	ADB	Within 2 weeks of circulation to Board or Management approval
Completion Report or Extended Annual Review Report (as applicable, and prepared by ADB based on annual progress reports).	ADB's website	ADB	Within 2 weeks of circulation to Board for information
Evaluation Reports	ADB's website	ADB	Routinely disclosed, no specific requirements

ADB = Asian Development Bank, DMF = design and monitoring framework, PID = project information documents.

* Subject to exception to presumed disclosure under ADB's Public Communications Policy para. 97 to 101 as applicable, taking into account any confidentiality undertaking existing between the Southern Gas Corridor Closed Joint-Stock Company and ADB.

X. ANTICORRUPTION POLICY

64. While the facility agreement is to be negotiated and agreed, the government and SGC acknowledged that ADB will require the lenders to include in the facility agreement certain undertakings arising from ADB policy requirements pursuant to ADB's Anticorruption Policy with respect to the project including those concerning prohibition of corruption, money laundering, and financing of terrorism.⁹

XI. ACCOUNTABILITY MECHANISM

65. People who are, or may in the future be, adversely affected by the project may submit complaints to ADB's Accountability Mechanism. The Accountability Mechanism provides an independent forum and process whereby people adversely affected by ADB-assisted projects can voice, and seek a resolution of their problems, as well as report alleged violations of ADB's operational policies and procedures. Before submitting a complaint to the Accountability Mechanism, affected people should make an effort in good faith to solve their problems by working with the concerned ADB operations department. Only after doing that, and if they are still dissatisfied, should they approach the Accountability Mechanism.¹⁰

XII. RECORD OF CHANGES TO THE PROJECT ADMINISTRATION MANUAL

66. All revisions/updates during course of implementation are retained in this Section to provide a chronological history of changes to implementation arrangements recorded in the PAM.

Date	Changes made to the Project Administration Manual

⁹ ADB's Integrity Office web site: <http://www.adb.org/integrity/unit.asp>

¹⁰ Accountability Mechanism. <http://www.adb.org/Accountability-Mechanism/default.asp>.