

PUBLIC

**DOCUMENT OF THE INDEPENDENT CONSULTATION
AND INVESTIGATION MECHANISM**

**PN-MICI002-2011
PANAMA CANAL EXPANSION PROGRAM
COMPLIANCE PHASE ELIGIBILITY
(2027/OC-PN)**

This documents was prepared by the Panel Chair Person for the Consultation Phase

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MEMORANDUM

COMPLIANCE PHASE ELIGIBILITY DETERMINATION

FROM: Werner Kiene, Chairperson of the Compliance Review Panel
TO: Inter-American Development Bank Board of Executive Directors
The Panama Canal Authority
REFERENCE: Case PN-MICI002-2011
PROJECT: Panama Canal Expansion Program (Operation Number 2027/OC-PN and
Project Number PN-L1032)
COUNTRY: Republic of Panama
DATE: September 20, 2012

1. Summary

1.1 On October 10, 2011, Ms. Leila Shelton-Louhi, Director of the Panamanian NGO “Gatun Lake Defense Committee,” filed a Request before the Independent Consultation and Investigation Mechanism (“ICIM” or “Mechanism”)¹ expressing concern regarding the potential negative environmental and social impacts of the Panama Canal Expansion Program (the “Project” or the “Expansion Program”). The Project is partially financed by the Inter-American Development Bank (“IDB” or “the Bank”). It has been confirmed that Ms. Shelton is the representative of Alianza ProPanamá, a coalition comprised of 11 Panamanian non-governmental organizations, through an e-mail from Mr. Olmedo Carrasquilla II, representative of Colectivo Voces Ecológicas.

1.2 The Project is co-financed by several financial institutions. Among them are the European Investment Bank (the “EIB”), the World Bank through the International Finance Corporation (the “IFC”), the Japan Bank for International Cooperation (the “JBIC”), and the IDB. We understand that the independent accountability mechanisms (the “IAMS”) of each of those four organizations have received complaints or requests that are similar to the Request. The IAMS initiated their respective processes at different times with the following results: a) EIB has recently finished its Assessment Report; b) IFC’s CAO issued an Assessment Report in February 2012 concluding that the consultation process had to be terminated; the complaint was then to the Compliance Review and is currently in the final appraisal stage; and c) JBIC Office of Examiners for Environmental Guidelines declared the complaint admissible, but the Examiners

¹ The terms Mechanism, MICI, ICIM, Management, Executive Secretary, Project Ombudsperson, Panel, Mechanism Policy, Eligibility, Consultation Phase, Assessment and any other relevant term in this memorandum shall have the meaning assigned to them in the Independent Consultation and Investigation Mechanism (ICIM) Policy approved on February 17, 2010.

decided to delay their analysis until the other three IAMs reach conclusions on their next procedural steps.

1.3 On February 9, 2012, ICIM’s Project Ombudsperson declared the Request eligible for the Consultation Phase, which was terminated in June 2012, as the Panamanian Implementing Agency (the Panama Canal Authority or the “ACP”) opted out of the Consultation Phase exercise. The ACP’s decision was based on its belief that it had provided all the information available and had already embarked on redressing the concerns raised by the Requesters. On August 15, 2012, the Requesters asked ICIM to transfer the case to the Compliance Review Panel. The Panel formally received the case on August 24, 2012.

1.4 The Requesters, Ms. Shelton-Louhi as well as leaders and citizens represented by the members of COVEC, believe that the Panama Canal Expansion “has not started well.” They express concern about a number of Project design issues that according to them could have a direct impact on the livelihoods of Requesters and cause them direct material harm. They fear consequences from: i) an alleged underestimation of seismic risk that they believe would be associated with the current design of the planned Canal Expansion; ii) alleged negative impacts on biodiversity in the marine environments of the Atlantic and Pacific Oceans, due to the feared mixing of its waters; iii) possible financial loss due to overestimation of available water to manage the new locks; and iv) negative impacts due to a potential increase of salinity around the lakes that feed the locks to operate the Canal. The Requesters attribute some of their fears to negative experiences they have had with earlier construction work on the existing Canal and made references to an incident when a number of Panamanian citizens died due to an earthquake. These deaths, allegedly being caused directly or indirectly, in whole or in part by the construction work being undertaken at the time.

1.5 The Panel learned that some of these concerns had been voiced repeatedly. During the Project’s early design stages as well as during the Consultation Phase, IDB’s Management, and the ACP were actively engaged in discussions with the Requesters in hopes of addressing their concerns. IDB Management has pointed out that it had also included the other financial organizations in the dialogues organized among Requesters, ACP, and the IDB Project team. Nevertheless, conflicting assertions still exist about the Project, its potential harm, alleged non-compliance with IDB Operational Policies persist.

1.6 Conclusion and Eligibility Determination: As required by ICIM Policy, Section 55, the Panel analyzed the Request, relevant Project documentation, and statements from IDB Management and Requesters. Without entering in the merits of the case, the Panel Chairman subjected the available information to the criteria spelled out in ICIM Policy, Sections 30, 31, 37, and 56 and determined that the Request is eligible for the purposes of a Compliance Review.

2. The Project

2.1 The Panama Canal Expansion is one of the most ambitious infrastructure Projects of the Western Hemisphere. Projected total costs are estimated at approximately USD 5.25 billion.

According to the documentation currently available to the Compliance Review Panel, IDB is financing part of Panama Canal Expansion Project with a loan of USD 400 hundred million. The Project as planned consists of (i) constructing a third set of locks, including two lock complexes and water-saving basins at the Atlantic and Pacific ends of the Canal; (ii) deepening of the Pacific and Atlantic entrances of the Canal; (iii) deepening and widening of existing Canal navigational channels, including the Gaillard Cut; and (iv) raising the Gatun Lake to its maximum operational level. As part of the new infrastructure, as part of the Project two sets of one-lane locks will be built—one on the Atlantic side of the Isthmus and one on the Pacific side—with three chambers and three water-savings basins at each side of the chambers.

2.2 **The Expansion Program:** On July 17, 2006, the Canal Expansion Program was approved by the Panamanian National Assembly by Organic Law Number 28. A National Referendum took place on October 22, 2006: 77 percent of the people that voted were in support of the expansion, while 22 percent opposed. Organic Law Number 28 states in Article 2 that “[n]o reservoirs shall be built for the operation of the third set of locks” and “[f]unding for this project shall not bear State endorsement or guarantee.” Construction works began on September 3, 2007 with the excavation of the Pacific access channel and are expected to be completed in late 2014. As of September 14, IDB has disbursed USD 100 million. Until mid-2012, JBIC had disbursed USD 800 million, EIB had disbursed USD 100 million. IFC has not made disbursements yet.

2.3 The conditions for disbursement are stipulated in the Common Terms Agreement (“CTA”) executed by the Lenders on December 9, 2008. According to the latest ACP Quarterly Progress Report, during the first quarter of 2012 the ACP negotiated an amendment in the bilateral agreement with IFC related to the “extension of the margin and payment conditions.” No further information is available.

2.4 The third set of navigation locks will be larger than the existing locks so as to allow transit of larger vessels known as “Post Panamax,” which can carry as much as 13,000 Twenty-foot Equivalent Units (TEUs)—the standard of measurement for containers. In its background studies, ACP concluded that the optimal maximum size that the new locks should endure would be container ships measuring 12,500 TEUs. Nevertheless, given the number of vessels estimated to be available in the maritime market with the potential to use the Canal in future years, the ACP determined that the new locks would be transited, predominantly by vessels ranging from 8,000 to 9,000 TEUs.

2.5 On 24 January 2012, the consortium *Grupo Unidos por el Canal S.A.* (the “GUPCSA”) won the bidding process for the contract of design and construction of the third of locks reaching the contractual milestone of meeting all requirements for the design of the locks, gates and valves. The ACP received the final excavation design for the Atlantic Entrance Channel, made recommendations and requested that it be resubmitted.

2.6 The Panel was informed that at the conclusion of the Consultation Phase, overall progress in the Project stood at 36.3 percent, with 22 percent of the construction of the locks having been executed, which is about six months behind the baseline schedule. According to information available to the Panel, the expanded Canal is scheduled to start operations in the last quarter of

2014. The contract for the construction of the Borinquen Dam (a four-segment small dam to be built to the southwest of Miraflores Lake to serve as a long entrance channel for the new Pacific Locks) and for excavation works at the northern access of the Pacific site was also issued during 2012 second quarter.

3. The Request

3.1 On October 10, 2011, Ms. Leila Shelton-Louhi, Director of the Panamanian NGO “Gatun Lake Defense Committee,” filed a Request before the Independent Consultation and Investigation Mechanism (“ICIM” or “Mechanism”) expressing concern on the potential negative environmental and social impacts of the Panama Canal Expansion Program (the “Project” or the “Expansion Program”). The Project is partially financed by the Inter-American Development Bank (“IDB” or “the Bank.”)

3.2 On October 20, 2011, ICIM received an e-mail from Mr. Olmedo Carrasquilla II, a representative of a Panamanian non-governmental organization, Colectivo Voces Ecológicas (“COVEC”), confirming Ms. Shelton-Louhi as the legitimate representative of Alianza ProPanama, a coalition of NGOs comprised of the following groups and organizations: Gatun Lake Defense Committee, Coordinadora para la Defensa de Tierras y Aguas (CODETIAGUAS), Coordinadora Campesina por la Vida, Unión Campesina Panameña (UCP), Frente Campesino Contra los Embalses y la Minería de Coclé y Colón (FCCEM), Frente Campesino Colonense (FCC), Organización Campesina Coclesana 15 de Mayo (OCC-15 de Mayo), Unión Indígena y Campesina (UIC), Asociación Pro Defensa de las Cuencas Hidrográficas, and Frente de Resistencia Coclesano (Movimiento – Coclé del Norte).

3.3 The Requesters expressed concern about a number of Project design issues that according to them could have a direct impact on their livelihoods and cause them direct material harm. They fear consequences from: i) an alleged underestimation of seismic risk that they believe would be associated with the current design of the planned Canal Expansion; ii) alleged negative impacts on biodiversity in the marine environments of the Atlantic and Pacific Oceans, due to the feared mixing of its waters; iii) possible financial loss due to overestimation of available water to manage the new locks; and iv) negative impacts due to a potential increase of salinity around the lakes that feed the locks to operate the Canal.

The Independent Accountability Mechanisms of four of the organizations co-financing the Project—the European Investment Bank (the “EIB”), the World Bank through the International Finance Corporation (the “IFC”), the Japan Bank for International Cooperation (the “JBIC”), and the IDB—have received similar Requests. In this regard:

a. The EIB’s Complaint Mechanism was the first to receive a complaint on March 27, 2011. An initial site visit was carried out from August 29 to September 4, 2011. The EIB has recently finished its Assessment Report.

b. The IFC CAO received a complaint in May 2011, which was deemed eligible for a consultation process on July 27, 2011. A field-trip was undertaken in late October 2011 and CAO issued an Assessment Report in February 2012 concluding that the consultation process

had to be terminated for the unwillingness of the parties to engage in further dialogues. The complaint was then transferred to CAO's Compliance Review and is currently in the final appraisal stage.

c. The JBIC Office of Examiners for Environmental Guidelines declared the complaint admissible, but the Examiners decided to delay their analysis until the other three IAMS reach some conclusions on their next procedural steps.

3.4 On February 9, 2012, ICIM's Project Ombudsperson declared the Request eligible for the Consultation Phase, which was terminated in June 2012 because the Panamanian Implementing Agency (the Panama Canal Authority or the "ACP") opted out of the dialogue exercise with the Requesters. The ACP's decision was based on its belief that it had provided all the information available and had already embarked on addressing the concerns raised by the Requesters. On August 15, 2012, the Requesters asked ICIM to transfer the case to the Compliance Review Panel. The Panel formally received the case on August 24, 2012.

4. ICIM Actions thus Far and IDB Management Response to Allegations

4.1 **Prior Contact with IDB Management:** In early phases of Project design, IDB Management proactively engaged in multiple meetings with Requesters, in attempt to redress the concerns expressed in the Request. During such period, the Project Ombudsperson granted additional time in the Consultation Phase eligibility determination process on November 2, 2011, granting the parties time and opportunity for discussions about the issues raised in the Request.

4.2 The parties failed to meet within the initial timeframe and requested an extension of additional 45 calendar days. During this period, Bank Management arranged a meeting in Panama City on December 20, 2011, between the Requesters and ACP to discuss the issues raised in the Request. The Project Ombudsperson and members of her team participated as observers at the invitation of Bank Management. As condition for participation in the meeting, the Requesters submitted the following list of documents and other information that they wanted to see in relation to the concerns raised in the Request:

- a. Studies of salinization impacts of the selected lock design and configuration
- b. Application of earthquake design criteria to the expanded Canal system
- c. Copy of project design
- d. Copies and supporting documentation of analyses of lock options and configurations
- e. Reports issued by due diligence experts with respect to above studies and determinations.

4.3 Bank Management asked the ACP to provide the information to the Requesters. Some information was provided in early December 2011. After the meeting, the ACP provided additional information to the Requesters. The second extension period (of an additional 45 days) ended on January 17, 2012.

4.4 On February 1st, 2012, the Requesters contacted the Project Ombudsperson to renew their desire to proceed with a Consultation Phase. The Requesters reiterated their concerns about the long-term sustainability of the Project as designed and expressed again concerns regarding an

alleged lack of transparency from the ACP, because they had not received all of the information requested. This communication, along with supporting documentation, was added to the formal Request and filed as such.

4.5 On February 9, 2012, the Project Ombudsperson declared the Request eligible for the Consultation Phase; the Eligibility Memorandum was distributed to the Parties on February 14, 2012.

4.6 The Project Ombudsperson proposed to carry out the Assessment site visit during the week of April 9, 2012. The ACP responded favorably at first; however, a few days before the mission, on April 4, 2012, the ACP communicated to the Project Ombudsperson that it would no longer be available for meetings and that it would not participate in a Consultation Phase exercise. Among the reasons cited for this decision were the following: a) all information had been made available to the accountability mechanisms and the lenders via the lenders' website; b) the ICIM had accepted a complaint without the appropriate documentation and support; c) the burden of proof has been placed on the ACP; d) the representative of the Requesters has a conflict of interest since she is promoting her brother's design of the Canal expansion.

4.7 On June 27, 2012, the Project Ombudsperson concluded the Consultation Phase with an "Assessment and Consultation Phase Report." The Report stated the Requesters' concerns about the Bank's due diligence with respect to seismic risks inherent in the Project design. It furthermore recommended that IDB Management conduct a hazard risk assessment and delay disbursement until such assessment is carried out.

5. Harm-Related Issues Considered for the Panel's Eligibility Determination

5.1 The Requesters, Ms. Shelton-Louhi as well as leaders and citizens represented by the members of COVEC, believe that the Panama Canal Expansion "has not started well." Both in the Request and in subsequent interactions with ICIM, they linked their fears and concerns to several issues of the design process and the design itself. They express concern issues that, according to them, could have a direct impact on the lives and livelihoods of locals and cause them direct material harm. More specifically, they fear consequences from: i) an underestimation of the seismic risk that they believe would be associated with the planned Canal Expansion, which resulted in the lack of adequate risk identification and appropriate mitigation measures related to an important seismic fault, thus threatening the Canal's Pacific end; ii) potential negative impacts on biodiversity resulting from overlooking the potential intrusion of salt waters into the transited lakes of the Canal, which has the potential to generate a migratory saltwater pathway across the Panama Isthmus with consequent damages to the marine-ecology of the Atlantic and Pacific oceans; iii) possible financial loss due to underestimation of available water to manage the new locks; and iv) potential negative impacts due to an increase of salinity around the lakes that feed the locks to operate the Canal.

5.2 The Requesters attribute some of their fears to negative experiences they have had with earlier construction work on the existing Canal and made references to an incident when a number of Panamanian citizens died due to an earthquake, allegedly fostered by the construction work undertaken at the time.

5.3 In addition, the Requesters allege that:

- a. That the Project design process was not transparent due to incomplete disclosure of information and misrepresentation of Project-related facts among the local and international community. For example: a detailed design of the new locks was not made available publicly and was therefore not subject to in-depth public scrutiny. Public fora leading to the approval of the Expansion Program via National Referendum held in 2006, were structured and controlled to keep focus on pre-packaged themes; engineering details of the locks selected design were not revealed or fully discussed; discrepancies or questions about the soundness of the design were ignored by the Panamanian Implementing Agency and the authorities at large;
- b. An enhanced design comprising two-lane locks and Miraflores-sacrificial type lakes would increase the efficiency of the system and truly mitigate the higher earthquake threat now known;
- c. The international financial institutions have failed to truly independently verify and certify designs, procedures and assertions made by ACP; and
- d. The Project has unrealistic and inadequate projections of the effects/impacts on local and global communities.

5.4 As described above, the Request highlights a number of allegations that revolve around potential environmental and social issues that may occur due to the Project's activities. From a number of e-mails that ICIM has received, the CRP inferred that NGOs have collaborated to gather information to corroborate the fears and concerns expressed in the initial Request. This information includes proposals of design alternatives that would avoid "...building critical structures on top of active fault lines."

5.5 Documentation available to the CRP seems to suggest that the Requesters' allegations relate to potentially incomplete disclosure of information, inadequate disaster risk management, and potential failure to assess the impact of a Project of such magnitude. The documentation conveys the Requesters' fears that the Project's activities might cause direct material harm to livelihoods of local residents and their families.

6. Compliance Issues Considered for the Panel's Eligibility Determination

6.1 Correspondence, documentation, and statements made to the Panel seem to suggest that the Requesters' allegations may relate to potentially incomplete disclosure of information, inadequate disaster risk management, and potential failure to assess the impact of a Project of such magnitude on the livelihoods of local residents and their communities. This could suggest that there might have been compliance issues with the following Relevant Operational Policies (the "ROP"): Environment and Safeguards Compliance Policy (OP-703), Disaster Risk Management (OP-704), and Access to Information Policy (OP-102).

6.2 Given the Project’s magnitude and wide array of environmental issues at stake with the Canal’s expansion, the Requesters consider that they should have had a more meaningful access to information. They also believe that related to their concerns about environmental impacts and safety, the Project has not disclosed all the requested information during the 90 days of extension granted by the Project Ombudsperson in early 2012.

7. Eligibility Determination

7.1 ICIM’s Policy stipulates that the Panel has the duty to assess whether the Request satisfies the eligibility criteria for a formal investigation on compliance with ROP. During this eligibility review process, the Panel analyzed the Request, relevant Project documentation, and statements from IDB Management, ACP, and Requesters and explicitly subjected the Request to Sections 30, 31, 37, and 56 of the ICIM Policy.

7.2 The results of the eligibility review are summarized in the table that follows below:

| Eligibility Analysis | | |
|---|----------------------------------|--|
| ELIGIBILITY CRITERIA FOR A COMPLIANCE REVIEW PHASE (as specified in relevant sections of the ICIM Policy) | THE PANEL’S DETERMINATION | COMMENTS |
| 56.a) The names and contact information for the Requesters are available | YES | ICIM files contain information on names and contact of the Requesters |
| 56.b) The names and contact information for the Representative, if any, and proof of the authorization are available | YES | The original Requester identified herself as a representative of a Panamanian civil society organization. In October 2011, the NGO Colectivo Voces Ecológicas filed a letter confirming the original Requester as the representative of “Alianza ProPanama,” a coalition of Panamanian NGOs concerned with the Project |
| 56.c) The Bank-Financed Operation(s) at issue has been identified | YES | On October 8, 2008, IDB approved a corporate loan in the amount of USD 400 million to partially fund the Canal’s expansion (PN-L1032) |
| 56.d) The Requesters resides in the country where the relevant Bank-Financed Operation is or will be implemented (or a qualified Representative has been appointed) | YES | The Requesters reside in Panama |

| | | |
|---|------------|---|
| <p>56.e) None of the exclusions set forth in Section 37 applies</p> | <p>YES</p> | <p><u>Exclusion 37 (a) does not apply:</u> The Bank is responsible for the actions that are subject to the Request though co-financiers share in this responsibility</p> <p><u>Exclusion 37 (b) does not apply:</u> The Request focuses on the Bank’s omission in securing adherence to its Operational Policies. It does not relate exclusively to the laws, policies or regulations of the Government and the executing agencies</p> <p><u>Exclusion 37 (c) does not apply:</u> The Request deals with issues arising from an Operation that is supported by the Bank together with co-financiers. The Requesters’ concerns are plausible and may relate to Bank Operational Policies on Environment Compliance Safeguards, Access to Information, and Disaster Risk Management</p> <p><u>Exclusion 37 (d) does not apply:</u> The Request does not address procurement issues</p> <p><u>Exclusion 37 (e) does not apply:</u> There has not been a previous Review on the same matter</p> <p><u>Exclusion 37 (f) does not apply:</u> The Request deals with a recently approved Bank Operation.</p> <p><u>Exclusion 37 (g) does not apply:</u> The Request deals with operational issues germane to the Mandate of ICIM and is not subject to review by other bodies of the Bank</p> <p><u>Exclusion 37 (h) does not apply:</u> The Request deals with feared or actual harm to the livelihood of the Requesters and has not been submitted to gain a competitive business advantage</p> <p><u>Exclusion 37 (i) does not apply:</u> The Panel has no evidence that the Request submitted to ICIM raises issues under arbitral or judicial review by national, supranational or similar bodies</p> |
| <p>56.f) the Requester has reasonably asserted that it has been or could be expected to be directly, materially adversely affected by an action or omission of the IDB in violation of a ROP in an Bank-financed Operation and has described in at least general terms the direct and material harm caused or likely to be caused by such action or omission in the Bank-financed operation</p> | <p>YES</p> | <p>Details are presented in the preceding sections of this memo</p> |
| <p>56.g) With respect to an issue raised in the Request, a Compliance Review may assist in determining whether (and if so, how and why) any Bank action or omission, in respect of a Bank-Financed Operation, has resulted in non-compliance with a ROP and direct, material adverse effects</p> | <p>YES</p> | <p>The Project’s magnitude might trigger a number of environmental and socio-economic safeguards. The Bank has been involved in ensuring that its Operational Policies will be applied to avoid or mitigate potential negative impacts. Requesters have challenged the adequacy of adherence to provisions in these Operational Policies. Examining the adequacy of the application of Operational Policies may assist</p> |

| | | |
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| (potential or actual) to the Requesters | | in identifying potential shortcomings as well as contribute to possible corrections, and avoid possible harm and reputational risk. |
| 56. h) The Requesters have taken steps to bring the issue to the attention of Management. The Panel Chairperson shall consult with Management as to its response and if Management is involved in addressing the concerns raised, the Panel Chairperson shall allow forty-five (45) calendar days from the date of receipt by the Executive Secretary of the Request for purposes of the Compliance Review before it is deemed eligible. The Panel Chairperson may waive this requirement in his or her discretion if the 45-day period has been invoked by Management during the Consultation Phase | YES | The Panel has evidence that the Requesters took steps to bring their concerns to the attention of IDB Management during the Consultation Phase, as described in this Eligibility Report. The Panel has been informed by Management about its efforts to address the issues and concerns raised in the Request |

8. Summary and Conclusions

8.1 It is much appreciated that IDB Management and the Implementing Agency have engaged with the Requesters in hopes of addressing their concerns. However, it appears that there are still conflicting views on whether the Project design has been in line with provisions of IDB’s own Operational Procedures that ensure the minimization or mitigation of risks and potential negative impacts on the environment and people’s livelihoods. The analysis of the Request established that it meets the ICIM Policy criteria for a Compliance Review. A review of the Bank’s adherence to its own Operational Policies is important and fully in the interest of the Bank and other stakeholders involved in this important investment.

8.2 Pursuant to ICIM’s policies and with no judgment on the merits of the allegations, the Chairperson of the ICIM Compliance Review Panel considers that **the Request on the Panama Canal Expansion is deemed eligible for a Compliance Review.**

9. Processing of the Eligibility Determination

9.1 ICIM Policy, Section 55, and the ICIM Guidelines stipulates that “the Panel Chairperson shall cause the Executive Secretary to promptly register” the Eligibility Determination in the Registry and notify the IDB Board of Executive Directors, ACP and the borrower/recipient accordingly.