

MEMORANDUM OF DETERMINATIONS

Political Violence Claim of Sector Resources, Ltd.
Contract of Insurance No. F030

I. The Claim

By letters dated November 29, 2005 (later supplemented), and February 2, 2007, and further supplemented on March 29, 2007 and April 3, 2007 (Annex A), Sector Resources, Ltd., a U.S.-owned Cayman Islands company (“Sector” or the “Insured”), filed political violence claims under the insurance contract described below. The Insured alleges that two separate incidents occurred, involving the hijacking of trucks by two different rebel groups operating in the Republic of Colombia. According to Sector, on November 28, 2005, members of the National Liberation Army (“ELN”) stopped a truck owned by the Insured, forcibly removed the driver and took the Insured’s property (the “First Incident”). Nearly a year later, on November 8, 2006, members of the Revolutionary Armed Forces of Colombia (“FARC”) allegedly hijacked a truck and similarly removed Sector’s property (the “Second Incident”).¹ Both incidents occurred on the road between the site of the Las Animas precious minerals mine near the town of Santa Isabela in the State of Tolima, Colombia (the “Project”) and mine offices in the city of Ibagué, Colombia, all of which are located southwest of Bogotá.

OPIC has determined that the claim is valid and that compensation is now payable with respect to the First Incident and the Second Incident in the total amount of \$75,548.

II. The Insurance Contract

Contract of Insurance No. F030, an OPIC Form 234 KGT 12-85 (Second Revised) NS (the “Contract”) (Annex B) was issued effective August 18, 1999, to cover Sector’s \$3,500,000 equity investment in the Project. Current maximum coverage under the Contract (reflecting reductions for payment of previous claims) is \$7,522,062. The active amount of coverage on the dates of loss (November 28, 2005 and November 8, 2006) was \$3,150,000. Article VI (Political Violence-Scope of Coverage) and Article VII (Political Violence-Amount of Compensation) of the Contract have been deleted in their entirety and replaced in Sections 10.04 and 10.05, respectively, of Article X (Amendments). All references are to the amended Contract.

III. Factual Background

A. The Project and the Insured.

¹ Sector sent OPIC notice of the First Incident on Nov. 29, 2005 but provided the certificate of the Colombian Armed Forces, which constitutes the only independent confirmation that a rebel guerilla unit was involved in the hijacking, only on February 2, 2007, and so OPIC has treated the First and Second Incidents as constituting a single claim, as to which an application for compensation was filed on February 2, 2007 and completed on April 3, 2007.

The project involves the acquisition and expansion of the Las Animas underground quartz, gold and silver mine (“Las Animas”) in the State of Tolima, Colombia. Sector has made up to a \$3.5 million investment into its Colombian branch (“Sector Resources Colombia”).

B. Colombia’s History and Political Conditions

The history of modern Colombia began in 1819 with its independence from Spain and the formation of the first independent Colombian state, the new Republic of Greater Colombia. Its first government elected Simon Bolivar president and Francisco de Paula Santander vice president. Two political parties grew out of conflicts between the followers of Bolivar and Santander and their political visions--the Conservatives and the Liberals. These two parties have since dominated Colombian politics.

Although Colombia maintained a tradition of civilian government and regular, free elections, Colombia's history has also been characterized by widespread, violent conflict. Two civil wars resulted from bitter rivalry between the Conservative and Liberal parties², and the military has seized power three times in Colombia's history. Since 1957, the Conservative and Liberal parties have co-existed with one another within a framework of democratic elections² Nevertheless, the tradition of violent political conflict that has plagued Colombia’s history of democratic institutions has continued.

In Colombia’s recent past, violence has been primarily been employed as a means to achieve political influence by smaller, more radical groups, including Cuban-backed insurgent groups that lost confidence in the Liberal Party’s ability to achieve their purported goal of social justice within a democratic process and resorted to political violence to bring about a Cuban-style Marxist regime. The FARC, the oldest and largest insurgent group, grew out of the Communist Party of Colombia in the early 1960’s. Its stated goal is to replace the existing democratic government of Colombia with a Communist regime. This group has been linked to the Second Incident, as well as incidents of political violence against the project as to which OPIC paid earlier claims.

Towards the end of the 1980s, several guerrilla groups were successfully incorporated into a peace process that culminated in a national assembly to write a new constitution, which took effect in 1991. Just before this settlement was put in place, however, a cease-fire that had existed between the government and the FARC broke down. President Pastrana’s Conservative Party government attempted to resolve the cycle of political violence from 1998-2002. President Pastrana’s government met directly with the major guerrilla groups, conducted peace negotiations, and withdrew government troops from a guerrilla stronghold in southeastern Colombia, ceding an area twice the size of New Jersey to the FARC. Despite these overtures, serious peace talks stalled in mid-

² The War of a Thousand Days (1899-1902)—which cost an estimated 100,000 lives; and “*La Violencia*” (the Violence), in the late 1940s and 1950s—during which up to 300,000 people died.

July 1999. In mid-February 2002, President Pastrana abandoned efforts to reignite peace talks, and initiated the retaking of the guerilla enclave it had granted the FARC.

Alvaro Uribe, an independent who was elected president in 2002 on a platform to restore security to the country, announced a national security strategy that employed political, economic and military means to weaken illegal narco-terrorist groups. The Uribe government offered to negotiate a peace agreement with these groups on the condition that they agree to a unilateral cease-fire and to end drug trafficking and kidnapping.

The ELN, a smaller organization than the FARC, was founded about the same time but embodied a unique socialist philosophy combining Castroism with liberation theology. It began a round of talks with the Colombian Government mediated by the Mexican Government in mid-2004 but withdrew from the talks after the Mexican Government voted to condemn Cuba's human rights record at the United Nations in April 2005. In December 2005, the ELN began a new round of talks with the Colombian Government in Cuba that led to more meetings, the most recent in October 2006. The dialogue is expected to continue, but the government has refused to grant a safe haven enclave to the ELN.

Both the FARC and the ELN, if only by their willingness to negotiate with the Colombian government, may be seen as having moderated their ultimate political objectives and become less committed to Marxist ideology, but both still seek political change by violent struggle. Both are classified by the Department of State as terrorist organizations, both remain actively engaged in violence against Colombian political, military and economic targets, as well as foreign investors, with the objective of destabilizing Colombia's economy and undermining its democratic institutions, and, both, but especially the FARC, seek to maintain financial and territorial power in defiance of law and legitimate governmental structures. The FARC derives major funding from the narcotics trade. Both the FARC and ELN engage in kidnapping, hijacking and extortion, including extracting "taxes" from businesses operating in areas where the insurgents have a presence³.

The Uribe government established, for the first time in recent Colombian history, a government presence in all of the country's 1,098 municipalities (county seats). Attacks conducted by illegally armed groups against rural towns decreased by 91% from 2002 to 2005. Between 2002 and 2005, Colombia saw a decrease in homicides by 37%, victims of massacres by 63% and kidnappings by 72%. Aerial spraying of coca crops and cocaine and heroin interdictions are setting records.

³ The description of the groups that are allegedly responsible for the two incidents that are the basis for the claim are based on publicly available information, specifically, the U.S. Department of State annual Report on Terrorist Organizations (2005), the Memorial Institute for the Prevention of Terrorism (MIPT) Knowledge Base, and the Council on Foreign Relations Backgrounder on the FARC, ELN and AUC (November 2005). More generally, the historical background on Colombia is based on the State Department Background Notes on that country.

In Congressional elections on March 12, 2006, the three leading pro-Uribe parties (National Unity, Conservative Party and Radical Change) won clear majorities in both houses of Congress. President Uribe was reelected by 62 percent of the vote on May 28, 2006, and sworn into office for a second term on August 7, 2006.

C. Project Specific History:

1. Background Risks and Precautions

From its inception, political violence has been a significant concern for this project. As previously indicated, the Las Animas mine is located near the town of Santa Isabela, State of Tolima. While Tolima has not been one of the most active areas for political violence, sporadic guerrilla battles have occurred there. In addition, similar mines in neighboring states have had to suspend operations due to political violence.

Between 2002 and 2004, OPIC paid compensation in the aggregate amount of approximately \$3,150,000 with respect to eight claims of Sector arising from political violence by the FARC that resulted in loss of business income and physical damage to the project, as well as defaults under equipment leases (which were covered under a separate insurance contract that is no longer in effect). The mine had to be closed for several years due to the threat of direct attacks by the FARC, until the Colombian Armed Forces reasserted control over the area in 2004.

Recognizing that it was operating in a high risk area, in anticipation of reopening the mine, the Insured entered into an arrangement with the Colombian military consistent with Colombian legislation relating to protection of the mining sector and also retained private security consultants to take measures to reduce the risk of loss due to political violence. These measures included establishing communications with the local military that would permit a quick response to incidents, improving the physical security of the mine, instituting security-conscious personnel practices and operating procedures, and obtaining equipment such as GPS positioning systems for vehicles to facilitate quick response to incidents involving them. From the outset, Sector sought to diminish political risk by operating in a manner that would build ties with the local community and obtain its endorsement for development of the mine. Finally, Sector has established a practice of sending out gold concentrate in trucks at random times based on a computer generated program, which gives even the drivers little advance notice when modest quantities of gold concentrate will be sent from the mine to the offices of Sector in Ibague. The trucks are equipped with features that permit them to be stopped by a satellite device after an alarm has been tripped.

IV. Factual Background

First Incident

On November 28, 2005, a Sector truck set out from the mine site with about 194 kilograms (427 lbs.) of gold concentrate, bound for Ibagué. The mine is 26 kilometers from Ibagué, and the road travels through rugged terrain. Masked and armed men allegedly stopped the truck and driver with a roadblock, rode a short distance with the driver, who was then taken into the woods, tied up, and abandoned.

The local commander of the Colombian Army certified on January 19, 2007 that three armed individuals of the ELN and another rebel group, the ERP (the “Popular Revolutionary Army”)⁴, intercepted the Sector vehicle on November 28, 2005. The certification also says that 194 kilos of concentrate were stolen.

Sector estimated the value of the 194 kilos to be \$43,449.60.

Second Incident

On November 8, 2006, Sector sent a truck containing 74 kilos (163 lbs) of gold concentrate to Ibagué.

The driver reported that four armed individuals stopped him at a roadblock. He concluded that they belonged to outlawed armed groups due to their military green jackets and other clothing.

According to Sector’s letter of February 2, 2007, the truck was hijacked by alleged guerillas of the “Tulio Varón Front” of the FARC. The local Commander of the Colombian Army, in a certificate dated December 9, 2006, confirms this.

Sector estimates the value of the 74 kilos to be \$32,097.92. The trucks belonging to the Insured were recovered in both cases by the Colombian Armed Forces and returned to the Insured.

V. Determinations Under the Contract

A determination under an OPIC insurance contract addresses three categories of issues: (1) whether the acts complained of satisfy all the elements required to bring them within the scope of coverage; (2) the amount of compensation payable; and (3) whether the insured fulfilled its duties under the insurance contracts.

Political violence was the direct and immediate cause of the permanent loss of tangible property of the foreign enterprise used for the project

⁴The ERP is a small insurgent group that was once a faction of ELN.

According to Sector, two shipments of gold concentrate were hijacked while enroute from the mine to company headquarters. The issue is whether this constitutes political violence or ordinary highway robbery. Sector has provided certifications by the Colombian army attributing the First Incident to specific units of the ELN and ERP and the Second Incident to the same unit of the FARC that was held responsible for the acts of political violence that formed the basis of eight prior claims that OPIC found valid.

“Political violence” is defined in Section 6.01 of the Contract as a violent act undertaken with the primary intent of achieving a political objective, including insurrection and terrorism.

The organizations to which responsibility for the incident has been attributed have generally been described as insurgent groups and terrorist organizations. They are known to have engaged in hijackings and other criminal acts, both to finance other activities and as means of destabilizing Colombia’s economy while striking at its political and military institutions and attacking foreign investments.

In light of all these factors, OPIC determines that political violence was the direct and immediate cause of the loss.

None of the exclusions applies

Article 6.02 of the Contract provides that no compensation for political violence is payable if any one of five exclusions applies. OPIC determines that, as to the First and Second Incidents, none of the exclusions applies.

The first exclusion (6.02(a)) describes property that is excluded from the scope of coverage, including precious metals. The standard exclusion has been revised in the Contract, considering that the project is a gold mining project. Accordingly, concentrate that is held as inventory by the foreign enterprise, and substantiated by its records, is not excluded. The investor has provided detailed contemporaneous records showing the mine output, the methods of ascertaining its gold content, and the amount of gold determined to be present in each sample of concentrate. These records satisfy the Contract requirements.

The claimed loss exceeds the minimum loss of \$5,000, and so the exclusion contained in Section 6.02(b) is inapplicable.

Whether Sector took reasonable protective measures, as required by Section 6.02(c) is an issue. Sector treated security of the mine itself and shipments from the mine as a serious issue, obtained the advice of consultants, and secured the cooperation of local military commanders. The Colombian military and Sector worked together to recover the trucks quickly. The security device in the trucks worked properly to shut off their engines, and a GPS positioning system permitted the military to find them quickly. Sector’s security consultant notes that the

rough, mountainous terrain facilitates hijackings, and no system of security can guarantee that no losses will occur. For the purpose of this claim, OPIC determines that reasonable protective measures were taken. Nevertheless, the repetition of two almost identical incidents within one year suggests that additional measures may reasonably be required in the future.

Sector did not engage in any unreasonable action to provoke the loss, and so Section 6.02(d) is inapplicable. Section 6.02(e) applies to business income claims, whereas this is a claim for asset loss, and so the final possible exclusion is inapplicable.

Compensation is payable in the aggregate amount of \$75,548 on the basis of the adjusted cost of the lost property.

The Contract (Section 7.01) provides two possible bases for compensation in the event of asset loss, namely adjusted cost and replacement cost. Considering the nature of the property lost (gold concentrate from the mine), replacement cost would be meaningless. The contract provides three possible measures of adjusted cost, i.e., original cost, fair market value and reasonable cost of repair. Again, considering the nature of the property lost, only fair market value is appropriate.

Sector has provided documentation supporting a fair market value for the lost property in the aggregate amount of \$75,548. The documentation consists of laboratory records establishing the metallurgical content of the concentrate in each shipment, shipping records showing the weight of the concentrate, and evidence of the market price of gold on each date of loss. Together, these documents establish the fair market value of the property that was lost. Sector calculated the fair market value of the concentrate by determining its gold content in troy ounces through laboratory analysis of samples that were milled on the dates of loss and determining the fair market value by reference to the published London PM fix on the dates of loss. Thus, the loss on November 25, 2005 amounted to 87.6 troy ounces of gold, valued at \$496 each, resulting in a claim for \$43,449.60. (See Annex A, as supplemented on April 3, 2007 with detailed laboratory and production records.) Following the same method, Sector established the compensation due for the loss on November 8, 2006 at \$32,097.92 (55.505 troy ounces of gold at \$623.20 each).

None of the Limitations applies.

Section 7.03 of the contract provides three possible limitations upon compensation for loss of assets, none of which applies.

The Active Amounts (Section 8.06) on the dates of the First Incident and the Second Incident exceeded the claimed compensation as of each date. (Sec. 703(a)). The Insured still retains the risk of loss of at least 10% of the book value of its interest in the foreign enterprise (Sec. 703. (a), Sec. 901.3).

The amounts of compensation that have been determined to be payable do not exceed the book value of the insured investment at the time of loss. Based on the balance sheets of the foreign enterprise for 2005 and 2006, OPIC has confirmed that the amounts of compensation do not exceed the book value of the insured investment (Section 7.04) as of the date of the First Incident and as of the date of the Second Incident. None of the adjustments described in Section 7.04(b) is required in this instance.

Sector has complied with all of the duties of the Investor under the Contract

Sector provided notice of the First and Second Incidents within six months of their occurrence and filed an application for compensation within three years of the loss (Sec. 8.01(c) and (Sec. 9.01.8).

Sector has certified that it remains the beneficial owner of the insured investment and remains eligible for OPIC insurance (Sec. 9.01.2).

No issue has arisen as to Sector's compliance with the worker rights standards of the Contract. Sector provided to OPIC the final design documents and the Development Plan required by Sec. 9.01.15 of the Contract, all of which were found acceptable by OPIC, and OPIC is satisfied with the Insured's continuing environmental compliance.

VI. Conclusion

For the foregoing reasons, OPIC concludes that the claim of the Insured is valid. The aggregate amount of compensation to be paid for the two incidents of political violence is determined to be \$75,548.

OVERSEAS PRIVATE INVESTMENT CORPORATION

By: 

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Vice President and General Counsel

Date: ~~April~~ 2007

5-3-2007