Leveraging Project Finance for Development: The Chad-Cameroon Oilfield Development and Pipeline Project

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The Chad-Cameroon oilfield development and pipeline project was a major attempt by the international community to leverage an extractive industries project to promote development in a fragile state. The project is notable for its size and ambition, and for the intensive participation of multilateral institutions, multinational corporations, governments, and civil society. The centerpiece of the project was an elaborate revenue management program designed to funnel oil revenues to priority sectors in Chad. However, unanticipated developments, including a deteriorating security situation, gradually eroded the Chadian government’s compliance with the program, resulting in disbursement suspensions and renegotiations. The program was prematurely terminated when the government of Chad fully prepaid its remaining financial obligations to the World Bank after just seven years of the project’s anticipated 20-30 year lifespan. Once hailed as a newly emergent model for development, the project now offers important lessons stressing the need for greater pragmatism in the future.

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Introduction

Long-term economic growth in the developing world, particularly in emerging Asia and India, is expected to dramatically increase global energy demand over the coming decades. This will place increasing strain on existing hydrocarbon production and refining infrastructure, further inflating prices. As these pressures continue to build, untapped hydrocarbon resources located in fragile states will become increasingly attractive to energy investors.

This trend carries both opportunities and risks. Prudently managed oil revenues could be harnessed to fuel sustainable social and economic development. Some oil-rich states have leveraged their natural resources to accrue massive sovereign wealth funds, which can be tapped to finance long-term social, political, and economic investments. However, many other states have fallen prey to the so-called ‘resource curse’ or ‘paradox of plenty’ (Auty & Mikesell, 1998; Karl, 1997). In these circumstances the presence of oil revenues can contribute to economic instability, social unrest, political corruption, and even violence. As additional oil and gas projects come online in ever more remote and instable regions, the future of the resource-rich developing world approaches a precarious juncture.

Recognizing the high stakes involved, the major proponents of the Chad-Cameroon Oilfield Development and Pipeline Project created a financial structure designed to encourage appropriate fiscal management in Chad. They conceived of an innovative revenue management program that earmarked funds for the government to spend in priority sectors in order to promote development. Other complementary Bank-funded programs addressed capacity-building, the environment, and transparency. It was hoped that by imposing extensive conditionalities on the government of Chad that the project could become a positive catalyst for development, or at least not become a ‘curse’.

The Chad-Cameroon Pipeline Project

At a total cost of around $4 billion, the Chad-Cameroon Pipeline Project represented the largest foreign direct investment in sub-Saharan Africa to date (“Africa oil and gas deal,” 2002). The World Bank originally estimated that Chad would receive at least $2 billion in royalties, tax revenues, and dividends over the project’s lifespan, while Cameroon was expected to receive about $500 million from transit fees, taxes, and dividends (“Overview,” n.d.). However, due to high oil prices actual project-related revenues accruing to the government of Chad dramatically exceeded the original estimates. Chad had already received over $4.3 billion by the close of 2008, more than double what the project was expected to bring in during its entire 20-30 year lifespan (Chad export project, 2008).

Initial consultations for the project began as early as 1993 and financial negotiations began around 1996 (World
**Early Controversies**

The project was, and remains, highly controversial. It drew intense criticism from its early stages of conception, mainly from concerned environmental nongovernmental organizations (NGOs) and human rights organizations. These groups ultimately succeeded in pressuring the project participants to implement important programs addressing their concerns.

Large oilfield development and pipeline projects are environmentally disruptive and publicly controversial. Consultations aimed at addressing environmental concerns began as early as 1993. A draft environmental assessment was completed in 1997 and released for public scrutiny (“The Chad-Cameroon development and pipeline project,” n.d.b). Significant changes were made to the initial assessment, including a rerouting of the pipeline, and in 1999 the consortium submitted a 19-volume Environmental Management Plan (EMP), which was made public, subsequently reviewed, and later approved by the World Bank. A multifaceted environmental monitoring mechanism was established, including an independent External Compliance Monitoring Group, an International Advisory Group (with broader “social and economic” responsibilities), substantial NGO participation, EssoChad reporting requirements, and World Bank supervision, inter alia (“The Chad-Cameroon development and pipeline project,” n.d.b). Reaching agreement on the environmental plan was necessary before the World Bank and US Ex-Im could approve their participations in the project.

While most criticisms of the project were constructive, some of the earlier reactions were reflexive and could be considered unfair. In a July 2001 report, Amsterdam-based Friends of the Earth International declared the project “disastrous” only one month after the financing arrangements were closed (Broken promises, 2001; Williams & Castillo-Bernaus, 2001). As early as 1997 the Environmental Defense Fund (EDF) had already published a report citing numerous environmental, social, and other problems certain to result from the project. The EDF even took issue with the proposed financial structure for the project, inaccurately asserting that “the oil companies and the commercial banks are taking cover behind publicly funded or guaranteed institutions [referring to World Bank and export credit agency participation] in what amounted to an egregious case of ‘corporate welfare’ with costs ‘shouldered by public funds’” (Horta, 1997).

Most observers simply expressed concern that revenues accruing to the government of Chad might be misspent, suspecting that oil windfalls would exacerbate already rampant corruption. Throughout the course of the project NGOs remained vigilant in their surveillance in order to enhance transparency and reduce corruption.

**Addressing the Chadian Context**

In 2005 Chad ranked last out of 159 countries included in Transparency International’s 2005 Corruption Perception Index, scoring a 1.7 out of a possible 10 (Transparency International, 2005). The US Department of State’s annual country report on human rights practices in Chad described the government’s record in 2004 as “poor,” documenting 26 pages of “serious human rights abuses” (Country reports, 2004). The president of Chad, Idriss Deby, came to power during a 1990 coup and has been reelected several times in...
flawed elections. In late 2000, Deby’s government secretly siphoned $4.5 million of a $25 million signing bonus paid by the consortium to purchase weapons to fight rebels in the northern region of the country, violating agreements with the World Bank and the IMF (Raeburn, 2001, p. 92; Silverstein, 2003). Facing pressure from the World Bank and NGOs, the government later channeled the remainder of the funds through the country’s revenue management program. In May 2004 an element of the state’s security services staged a failed coup. Political problems still persist in the country and the government continues to battle rebels sporadically advancing on the capital. An internationally controversial referendum held in June 2005 eliminated the constitutional two-term limit for the presidency (Supporting human rights and democracy, n.d.) and subsequent government actions effectively terminated the revenue management program.

The project was initially designed to address specific difficulties afflicting the Chadian political and social context. Public administration in Chad was extremely poor, due in part to the 30 years of civil war that followed the country’s independence from France in 1960 (“CIA,” 2005). Capacity building programs instituted by the World Bank were intended to bring the country’s administrative capabilities up to speed before the project’s completion, but construction finished a year early and revenues began accruing to the government before adequate capacity could be established (Gary & Reisch, 2005, p. 12; Report, 2005).

Despite a windfall in oil revenues, the Chadian government remained mired in financial difficulties. Rigidities in the Bank’s revenue management program led to cash flow problems, causing the government to accumulate substantial payments arrears (Report, 2005). Chad began new assistance programs with the IMF in 2005, requesting help under the Poverty Reduction and Growth Facility (PRGF) and the enhanced Highly Indebted Poor Countries (HIPC) initiative (Chad: Requests for a three-year arrangement, 2005, p. 41).

For its part, the IMF generally deferred to the World Bank’s handling of the revenue management program. IMF best practices would have dictated a slightly modified program than what the World Bank instituted, which could have introduced tensions. The World Bank has taken the view that Chad is a special case and that emphasis should be placed primarily on poverty reduction, even if this is at the expense of optimal fiscal management. The Fund has taken the more technically correct view that oil-exporting countries ought to adopt particular fiscal policy objectives and seek to avoid certain undesirable macroeconomic consequences, but allowed the World Bank to execute its special programs without opposition (Katz, Bartosch, Malothra, & Cuc, 2004, p. 41). The IMF remains concerned, however, that fiscal arrangements in Chad are not consistent with basic principles of proper oil revenue management (Chad: Requests for a three-year arrangement, 2005; Katz et al., 2004).

**Project Structure**

World Bank endorsement was critical for attracting other participants to the project and moving the financing arrangements forward (“Africa oil and gas deal,” 2002). Bank participation also brought legitimacy and expertise, which in turn encouraged export credit agencies (ECAs) from the United States and France to join. Private investors were reportedly more comfortable with World Bank and ECA participation secured because these institutions are perceived to enhance the enforceability of contracts (“Pipeline paradigms,” 2003). With the ECAs carrying a significant share of the project’s risks, private investors stepped forward to provide financing. Ultimately, investors showed a high level of interest in the project despite the considerable risks.

Many commentators speculate that the project would have eventually gone forward even without significant World Bank involvement. James Wolfensohn, then president of the World Bank, poignantly commented:

If we withdrew . . . [the project] would have been financed separately by people who didn’t give a damn. So the question was: was it better for us to stay in, to try to monitor the situation and improve it, or just withdraw in the certainty that it would go down the tubes? . . . I get beaten up all the time. If we can pull it off it will be unique, and it will be for the benefit of the people. If we hadn’t gone into it, the project would have been financed elsewhere by people who certainly wouldn’t have done it like this. (Ford, 2004, p. 30)

The World Bank understood the risks and controversies surrounding the project and assumed a pragmatic position. It was probably apparent to most that the World Bank’s capacity building programs would not ramp up in time to safeguard all of Chad’s oil revenues. But economic and political forces much stronger than the World Bank were pushing the project forward regardless of these concerns. “It was not realistic to wait until capacity was fully developed to implement the project,” the World Bank defended on its website, probably in response to criticisms from the NGO community (“Chad-Cameroon development and pipeline project,” n.d.). If one
accepts the inevitability of the project, then the World Bank’s willingness to participate was commendable, especially considering the considerable reputational damage the Bank was willing to put on the line.

The three original project sponsors from the private sector - ExxonMobil (40%), Shell (35%), and Elf (25%) - formed a joint venture with EssoChad as operator. Shell and Elf later dropped out and were replaced by Petronas and Chevron, respectively, with no change in the project’s proposed structure (“Africa oil and gas deal,” 2002). The consortium fully funded the oilfield development portion of the project, and intended to contribute about $576 million and $109 million to the pipeline companies COTCO and TOTCO, respectively. Consortium participation in the pipeline companies was to fund about 85 percent of the cost of the export system. The remainder was to be provided by the governments of Chad and Cameroon.

The International Bank for Reconstruction and Development (IBRD) of the World Bank Group lent Chad $32.5 million and Cameroon $43.5 million to enable them to purchase equity shares in their respective pipeline companies. The European Investment Bank (EIB) lent $15 million to Chad and $26.5 million to Cameroon for the same purpose (Project appraisal document, 2000, Annex 12). The World Bank’s loans were conditional upon Chad and Cameroon implementing a number of domestic programs for which additional loans were made.

The Chad-Cameroon project utilized project finance as a method for mitigating political risk and securing outside participation from commercial banks. Normally, project finance is used as a means for attracting relatively high levels of debt financing, but in the Chad-Cameroon case the technique was employed more for its risk mitigation properties rather than to fulfill any unmet financing requirements (“Chad oil pipeline,” 2001).

World Bank involvement reportedly enabled US Ex-Im and France’s CoFace to participate, which was deemed critical to the project’s moving forward (“Ex-Im backs Chad pipeline,” 2000). One source close to the deal claimed that “The extent of the World Bank Group endorsement was the single crucial factor in banking [the] deal” (“Africa oil and gas deal,” 2002).

The ECAs bore the major financial risks associated with “failure to complete” as a result of political events. Combined, the ECAs offered to guarantee up to $600 million in loans to the two project companies (Project appraisal document, 2000, p. 2). US Ex-Im approved up to a $300 million loan guarantee, which covered only political risks during the pipeline’s construction and comprehensive political and commercial risks after completion (Ex-Im Bank, 2000). US Ex-Im provided 100 percent coverage and CoFace 95 percent (“Chad oil pipeline,” 2001). Ultimately, the total amount of debt financing for the pipeline companies was evidently reduced from $1.4 billion to about $600 million. US Ex-Im and CoFace ended up guaranteeing around $200 million each (IFC, 2001). The guaranteed lenders were ABN Amro North America and Credit Agricola Indosuez. Notably, this was US Ex-Im’s first nonrecourse venture in sub-Saharan Africa (Ex-Im Bank, 2000).

The International Finance Corporation (IFC), the private sector lending arm of the World Bank Group, proposed providing a $100 million ‘A loan’ from its own resources and arranging a $300 million ‘B loan’ for syndication to commercial banks (Project appraisal document, 2000). In the final structure, both loans were about $100 million each (IFC, 2001).

Commercial interest in the three tranches was reportedly strong. A spokesperson stated that the offers were 50 percent oversubscribed (“Chad oil pipeline,” 2001). The IFC syndication is believed to have been priced at between 250 to 300 basis points (bp), the US Ex-Im arrangement between 50bp and 60bp and the CoFace arrangement between 90bp to 100bp, reflecting the different risk levels perceived by investors (“Chad oil pipeline,” 2001).

The proposed $400 million in project bonds were apparently never issued, probably due to prohibitive costs. According to the World Bank/IFC Project Appraisal Document (2000), in the event that project bonds were not floated, the project sponsors were to contribute additional equity or quasi equity in the amount of the financing gap. The private consortium members, particularly ExxonMobil, are known to have had adequate capital.

Overall, creative financing involving multiple stakeholders succeeded in bringing the risky project to fruition. That the project structure and risk allocation system attracted sufficient private capital is a major accomplishment in itself. Moreover, World Bank participation played a singularly significant role which the private sponsors apparently preferred to ‘going it alone’.

The Project Revenue Management Program

The Chad-Cameroon project’s revenues and the related royalties, dividends, and taxes could potentially provide the government of Chad with the means for rapidly advancing development. But if revenues are poorly managed, the project could stymie development, shoring up corrupt patronage systems and depleting the country’s exhaustible resources.
during a period of ineffective governance. Indeed, the disturbing governance and human rights records of the Déby regime in Chad underscore some of the project’s downside risks. Safeguards were instituted with the Petroleum Revenue Management Program (PRMP) to help ensure that the project would serve as a vehicle for positive change and not as a catalyst for corruption and waste.

Due to the extreme conditions prevailing in Chad, the PRMP was more intrusive than its predecessors elsewhere. The program earmarked portions of oil revenues for priority poverty reduction activities, mandatory long-term savings, and oversight and monitoring mechanisms (Project appraisal document, 2000, p. 95). Chad’s 1999 Law on Revenue Management implemented the PRMP. It defined the priority sectors for oil revenue allocations as “public health and social affairs, education, infrastructure, rural development, environment and water resources” (Project appraisal document, 2000, Annex 11).

However, the law had several important weaknesses, many of which were publicized in a joint report by two NGOs (Gary & Reisch, 2005). First, the law applied only to certain modes of oil-related revenues, leaving substantial revenue streams outside the revenue management system. Second, the law only applied to oil obtained from three fields - Kome, Miandoum, and Bolobo - in the Doba region, despite significant exploration and development activities outside of that area (“Chad/Cameroon development project: Construction: Oilfields,” n.d.). Third, some observers argued that the law does not earmark enough revenue to the oil-producing region for compensatory purposes. Fourth, the priority sectors were defined too vaguely, leaving excessive room for political manipulation that could undermine the spirit of the PRMP.

Proponents of the PRMP broadly intended to maximize revenue allocations for the priority sectors via a rules-based system, given the government’s capacity constraints. Revenues available for discretionary spending in non-priority sectors were intentionally limited during the earlier stages of the project’s lifespan but were allowed to increase gradually as the government built capacity, increased transparency, and combated corruption.

Three main categories of oil revenues accrued to the government of Chad under the prevailing arrangements: royalties, dividends, and income taxes. Direct revenues - royalty payments from the consortium and dividends from Chad’s equity participation in TOTCO and COTCO - were deposited into an offshore escrow account with Citibank and subjected to the conditions and restrictions of the PRMP. Indirect revenues to Chad included corporate taxes on the consortium and TOTCO. Revenues accruing indirectly were not subject to the provisions of the PRMP (Project appraisal document, 2000).

Ideally, oil revenue management systems are designed to insulate government spending from shocks to oil prices. Under the PRMP, Chad’s overall revenue sensitivity to price shocks varied according to the revenue stream. Royalty payments were moderately sensitive, dividend income was insensitive, and corporate tax revenues were very sensitive (Project appraisal document, 2000). Generally, as oil prices increased, indirect revenues grew faster than direct revenues and an increasing proportion of funds fell outside the purview of the Law on Revenue Management and the PRMP.

High oil prices eroded the efficacy of the revenue management system. The base scenario for the PRMP assumed a Brent benchmark oil price of about $18 per barrel and a Doba price of about $15 per barrel, assuming a $3 per barrel discount for the inferior quality crude (Project appraisal document, 2000). EssoChad, the project operator, reported a Doba price of $38 per barrel and quoted a Brent price of $51 per barrel for the second quarter of 2005, implying a larger $13 per barrel discount at this higher price level (Chad export Project, 2005, p. 72). Even while discounted, the actual effective price for Chad’s Doba crude more than doubled from the $15 per barrel price projected in the base scenario in 2000 (for the life of the project) to $38 per barrel by mid-2005.

Oil production began ahead of schedule, resulting in substantially increased cumulative revenues in the first few years over the baseline assumptions. The original projections predicted that Chad would have accrued around $111 million by the end of 2005. But with earlier production and higher oil prices, Chad had already received $276 million by mid-year 2005, more than double the original estimates (Chad export project, 2005, p. 8; Project appraisal document, 2000, p. 79). Later that year some payments were suspended after the government of Chad revised its revenue management law.

Initially, it was estimated that direct revenues (subject to the PRMP) would constitute 85 percent of Chad’s total oil revenues during the first 10 years of the project’s operation (Project appraisal document, 2000, p. 96). The World Bank projected that a 20 percent upside shock to the base Doba crude price would cause the proportion of revenues governed by the PRMP to shrink to 63 percent (Project appraisal document, 2000, p. 100). The actual magnitude of
the upside price shock to Doba crude from the base scenario was 149 percent in the second quarter of 2005 (Chad export project, 2005, p. 72; Project appraisal document, 2000, p. 100). It is not clear why the projections did not game shock scenarios exceeding 100 percent to the Brent price, as these have been common historically. The Chad-Cameroon project was expected to span about 27 years from 2000 to 2027, generating recurrent revenues for Chad beginning in 2004. The 27-year period running up to the project’s approval in mid-2000 saw frequent and sustained price shocks well over 100 percent.

This is especially troubling considering the negative impact such shocks were thought to have on the situation in Chad with its administrative problems, high levels of corruption, and history of human rights abuses. Indeed, the PRMP was intended to preclude the very scenario that prevailed shortly after the project’s completion: relatively high levels of revenue for Chad in the context of inadequate absorptive capacity. To avoid this situation most of the government’s indirect revenues were intentionally back-loaded, with relatively minor tax revenues from TOTCO beginning to accrue in 2004 (when it was thought that the project would be completed) and the bulk of indirect revenues—from taxing the consortium—not accruing until 2014 (Project appraisal document, 2000, p. 79).

The overall impact of early project completion and higher oil prices was that the government of Chad received more direct and indirect revenues before the establishment of sufficient capacity to manage the funds properly. In the short-term, the increased revenues were held in special accounts, spent on general expenses, or channeled to priority sectors as per the PRMP. However, over time an increased proportion of the revenues escaped the controls of the PRMP, undermining the original intent of the program. The PRMP was ultimately terminated amid controversy in 2008 (World Bank statement, 2008).

**Effectiveness of the PRMP**

The World Bank’s stated development objective in Chad was to increase governmental spending in the priority sectors by at least $40 million per year throughout the period 2005 – 2009 (Project appraisal document, 2000, p. 4). Allocations for the priority sectors were additive on top of regular spending, which constituted about 15 percent of GDP in 2000, the year in which the project was approved. That magnitude presumably would have reflected Chad’s limited absorptive capacity. However, under the design of the PRMP, the first 21 months of the project’s operation brought more than $251 million in revenue to Chad, $201 million of which was allocated to the priority sectors (“Revenues and allocations,” 2005). Despite operating at well below export capacity, actual oil revenues for the priority sectors had initially amounted to roughly $114 million per annum, almost three times the World Bank's target.

Clear information regarding the balances and operations of Chad’s various accounts under the PRMP are difficult to obtain. However, it appears that the special account held at Banque des Etats de l’Afrique Centrale (BEAC) operated as the government’s primary fiscal stabilization mechanism. Of the royalties and dividends deposited into the special account at BEAC, 80 percent were deposited into a stabilization account. Disbursements were technically made from this second account, quarterly, according to approved budgetary commitments. The stabilization rule stated that if actual revenues differed from budgeted revenues by up to 20 percent, then the difference was to be credited or debited against the stabilization account. Beyond that the budget was to be revised (Gary & Reisch, 2005, p. 46). This implies that with higher than expected oil revenues the budget should have been revised to accommodate additional spending, otherwise the stabilization account would have ballooned.

It appeared that the additional revenues were allocated, and much of them disbursed - mostly in the priority sectors or for general operating expenses (“Revenues and allocations,” 2005).

Two mechanisms were to guard against wasteful spending beyond the government’s absorptive capacity (Chad: Requests for a three-year arrangement, 2005, p. 15). The first mechanism was the oversight committee, the Collège de Contrôle et de Surveillance (College), which had to approve all disbursements under the PRMP. The College approved approximately $38.6 million out of $51.4 million for the priority sectors in 2004, and had approved $62.9 million out of $179.8 million proposed for the third quarter of 2005 (“Revenues and allocations,” 2005). Unspent oil revenues were to be returned to the stabilization account, constituting the second stabilization mechanism.

It is not clear to what extent the excess funds were spent wisely, nor is it apparent exactly where the excess funds were being held. However, that the government was accumulating payments arrears in the presence of excess revenues indicates a lack of cash management flexibility in the PRMP’s earmarking scheme. Wherever the funds were being held, it may be inferred that rigidities in the program were preventing the government from drawing on its excess revenues to meet scheduled payments obligations elsewhere in the budget. The program “exacerbated the fragmentation...
of the budget process,” according to the IMF, “creating a parallel budget system, thus hampering the effective allocation of budget resources” (Chad: Requests for a three-year arrangement, 2005, p. 10). The Fund estimated that the cumulative financing gap for 2005 – 2008 was to total $270 million (Chad: Requests for a three-year arrangement, 2005, p. 17).

A further issue was the expenditure procyclicality to oil revenue variability inherent in the structure of the PRMP. The only insulation mechanisms available to prevent the transmission of oil revenue volatility to expenditures were: 1) the College expenditure approval process and 2) the debit or credit of the actual vs. planned revenue differential back against the stabilization fund. The differential could grow widely before the planned budget was to be revised, which required considerable lag, and even then only presumably to accommodate the differential into the budget rather than insulate against it. The structure of the PRMP and its earmarking attributes effectively ensured the presence of at least some expenditure procyclicality to oil revenues.

According to the IMF, the BEAC has its own framework for revenue stabilization and long-term savings that apparently differs from that which was implemented in Chad (Katz et al., 2004, p. 41). The BEAC offers a program where countries pay 50 percent of their excess oil revenue into a stabilization fund, where the benchmark is defined as a five-year average. Countries can also withdrawal up to 50 percent of a shortfall. A country’s net balance in the stabilization fund must remain positive, and deposits into the long-term savings fund cannot exceed 10 percent, but in 2004 no country was utilizing this framework. The BEAC, as a central bank, is obligated to keep a certain percentage of funds as foreign exchange reserves, which must be held in low yield, short-term, liquid assets. The IMF notes additional disincentives for utilization of the BEAC framework. Chad’s revenue management system adhered to similar principles (somewhat) but was not governed under the specific framework provided by the BEAC.

The World Bank reported that on September 30, 2005, the Future Generations Fund (FGF) had a balance of $27.4 million (“Chad-Cameroon pipeline,” n.d.). The theoretical rationale for the fund was to set aside some of Chad’s oil wealth for future spending. Doing so promotes intergenerational equity which helps stabilize government expenditures between Chad’s oil-producing years and the post-exhaustion years thereafter. In this particular case the FGF also served as a special savings fund, accruing deposits while the government’s ability to spend efficiently was weakest, and saving for the future when government programs could presumably be implemented more effectively. Considering the primacy of the latter function in this particular case, however, the Future Generations Fund was underutilized. By January 2006, the FGF had a balance of $36 million. At this time the Chadian government proposed amendments to its revenue management law to weaken the PRMP and eliminate the fund, citing security-related priorities (World Bank suspends disbursements, 2006). The World Bank subsequently suspended further disbursements to Chad until an agreement in mid-2006 that affirmed Chad’s commitment to spending 70 percent of its budget on poverty reduction programs and establishing a general stabilization fund in place of the FGF (World Bank, Government of Chad, 2006).

In a terse statement released in September, 2008, the World Bank announced that it had ended its involvement in the project. The statement noted that:

Over the years, Chad failed to comply with key requirements of [the] agreement. A new agreement was signed in 2006, but once again the government did not allocate adequate resources critical for poverty reduction… Regrettably, it became evident that the arrangements that had underpinned the Bank’s involvement in the Chad/Cameroon pipeline project were not working. (World Bank Statement, 2008)

By year-end 2008, more than 288 million barrels of oil had been exported since production began (Chad export project, 2008, p. 7). Following the onset of oil exports, GDP initially grew rapidly and then tapered off. The IMF estimated that GDP grew at 31 percent in 2004 while per capita GDP grew at more than 60 percent (Chad: Requests for a three-year arrangement, 2005, p. 24). Many health indicators have significantly improved (Chad export project, 2008). However, inflation has been rising (Chad: 2006 article IV consultation, 2006).

Although the oilfield development and pipeline project did provide the Chadian government and other stakeholders with resources that were used to promote development, the government failed to adequately prioritize poverty reduction and savings for the future. Official documents suggest that Chad’s oil revenues have been significantly diverted from the priority sectors to other areas such as territorial administration and security, which were comparatively neglected under the PRMP (World Bank suspends disbursements, 2006).
Financial Disputes
Chad’s oil is mostly sold to refineries owned by the producers themselves, and due to a lack of transparency it is not especially clear what price levels ultimately prevail. A source of great ambiguity and tension has been the transport cost that is deducted from the Doba sale price to arrive at the net price received by the government of Chad. ExxonMobil has been using a transport cost of about $10 per barrel, which Chad has disputed. According to an NGO report, “it is clear that the government has a distinct lack of capacity to monitor production, verify the accuracy of royalty payments on its own or to understand many technical aspects of the oil industry, including calculations of transport costs” (Gary & Reisch, 2005, p. 38). Four factors were supposed to determine transport costs: 1) operations and maintenance for the pipeline; 2) return on investment on the pipeline; 3) commercial debt servicing on the pipeline infrastructure; and 4) a transit fee of $0.41 per barrel for Cameroon (Gary & Reisch, 2005, p. 40).

In a confrontational communiqué the government of Chad attacked the consortium for “swindling, murkiness, and fraud,” among other charges, noting that out of about $900 million in oil sales, Chad only officially received about $40 million in profits (Communiqué, n.d.). That particular claim is misleading, however, because it ignores the structural characteristics of the project’s projected multiyear revenue streams.

Chad has disputed its arrangements with Exxon, the lead sponsor, citing a confidential 1988 concession agreement between the two parties known as the “Convention for Exploration, Production and Transportation of Hydrocarbons.” The Convention is confidential but reportedly stipulates a 12.5 percent royalty (Communiqué, n.d.; Gary & Reisch, 2005, p. 38).

In response to Chad’s accusations, ExxonMobil indicated that “there are dispute resolution mechanisms in the agreements, including arbitration, which may be used to resolve certain impasses” (Gary & Reisch, 2005, p. 49). The issue was ostensibly resolved in May 2004 when a new convention was signed that provided for a 14.5 percent royalty (Gary & Reisch, 2005, p. 39). During a subsequent October 2004 conference in Chad the government backed off its allegations (Gary & Reisch, 2005, p. 49). Subsequent reports indicated that Chad remained unsatisfied with its new terms and attempted to dismiss the new agreement as illegal because it was signed by an inexperienced government negotiator (Gary & Reisch, 2005, p. 39; Katsouris, 2004).

Dissatisfied with its share of project revenues, the government of Chad proposed revisions to its original Law on Petroleum Revenue Management. The changes were to allow the government to increase funding for the military and security forces and double the percentage of revenues available for discretionary spending. The Chadian Prime Minister stated that funds currently earmarked for the FGF would be better spent in the near-term (“Chad proposes revision of oil revenue management system,” n.d.). Some observers contended that “the problems facing the country do not stem from the text of the [original] law but from poor governance, including mismanagement of funds and widespread graft” (“Chad proposes revision,” n.d.). However, the IMF repeatedly indicated that the government’s original Law on Petroleum Revenue Management did have substantial shortcomings and “need[ed] to be reviewed” (Chad: Requests for a three-year arrangement, 2005, pp. 10, 50).

Numerous independent accounts of the government’s lack of absorptive capacity and general inability to effectively spend its current revenues undercut the government’s position at the time, although security threats to the Deby regime were substantiated.

As previously noted, Chad’s decision to amend its oil revenue law eventually resulted in the premature termination of the PRMP. Facing worsening domestic instability, the Chadian government repeatedly insisted that funds being spent on poverty reduction programs were more urgently needed elsewhere and that funds accruing in the Future Generations Fund were better spent in the short-term. These circumstances suggest that the PRMP might have been more effective had it allowed some accommodation for security-related spending. More pragmatic complementary programs designed to enhance territorial administration and security might also have lessened the impetus for Chad to abandon the program. A stricter escrow system combined with a rigorously enforced fiscal rule could have given the World Bank greater leverage over the Chadian government and provided a stronger incentive for Chad to have compiled with the PRMP. However, these modifications would probably have seemed unacceptably intrusive at the time, as even now they would raise serious reservations concerning the appropriate relationships between multilateral institutions, multinational corporations, and sovereign states, particularly as they relate to domestic security issues.

Conclusion: The Chad-Cameroon Model
Financially, the Chad-Cameroon pipeline project has so far proven largely successful. The project’s structure succeeded in allocating risk, return, and control to the various participants in a manner that attracted high levels of private sector interest.
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despite the extraordinary risks. While the government of Chad has chosen to take a confrontational attitude toward the project sponsors, its disputes do not appear to jeopardize the commercial viability of the project.

The consortium was cautious and made measured progress over many years to develop a structure that would address their most pressing concerns. They responded to international criticism constructively by inviting World Bank and NGO participation, which also served to bring legitimacy and momentum to the project. World Bank and IMF involvement was instrumental during the early phases in promoting confidence among the other participants. The project may even have helped establish informal precedents that could lead to better environmental and fiscal management systems for similar projects in the future. Financial legal scholars familiar with the project affirm that:

. . . the Chad-Cameroon pipeline has been a milestone project in more ways than one. The use of environmental and revenue management programmes in this region, on this scale and in this level of detail, is unique. Revenue management programmes (in one form or another) may well be here to stay, particularly for major projects in lesser developed jurisdictions. Acceptance of environmental and revenue monitoring is, perhaps, a small price to pay for gaining access to World Bank, EIB and other multilateral support and, ultimately, commercial funding. (Williams & Castillo-Bernaus, 2001, p. 10)

The Operations Evaluations Department of the World Bank concluded an “Evaluation of the World Bank Group’s Activities in the Extractive Industries” in September 2004 (Evaluation, 2004). The report struck a critical tone urging the Bank to be more selective, stressing the primacy of good governance and highlighting important risks to projects in states that lack critical capacities. The Bank’s management released its official response to the review just a few weeks later, endorsing only two of the reports main messages that “extractive industries can contribute to sustainable development” and that “there is a continuing role for the Bank Group in supporting [extractive industries]” (Striking a better balance, 2004). The official response generally reaffirmed the Bank’s commitment to work on strengthening governance and transparency, and included a pledge to integrate the report’s major recommendations into future efforts.

The World Bank’s enthusiasm for the project and the project’s potential to alleviate poverty in Chad clearly overshadowed many technical issues concerning spending efficiency, intergenerational equity and expenditure procyclicality. The IMF has expressed many concerns on technical grounds, but mindful of the unique and challenging circumstances in Chad, largely chose to defer to the Bank and its programs. Due to higher than expected oil prices, the risks so far have been upside, possibly the causal antecedent of the Chadian government’s ultimate noncompliance. But if oil prices fall, revenue procyclicality will have the reverse effect, introducing potentially severe fiscal problems that could have destabilizing political consequences.

The World Bank’s revenue targets for the government of Chad have been exceeded, although “grave weaknesses in public financial management” persist (“Proposed revision,” n.d.). Corruption continues, but by most accounts was somewhat contained through the oversight work of the College, World Bank pressure and NGO surveillance. Unfortunately, since Chad’s oil reserves are a finite resource, its wasted revenues are gone forever.

NGO pressure was remarkably constructive and ultimately important and effective. The relatively high level of transparency surrounding the project, while room for improvement remains, has generally contributed to an atmosphere of productive dialogue between civil society and the project participants. The World Bank and many NGOs played helpful roles providing and disseminating important documents relating to the project. The collaborative work of prominent NGOs set high standards for constructive NGO participation in complex international extractive industries projects. Civil society has found attentive audiences with multilateral institutions and even the oil and gas industry.

A new paradigm for extractive industries projects in less developed countries may be emerging. Referring to a recommendation presented in an NGO report, a prominent industry trade journal noted:

The oil and gas industry should pay special attention to this finding: ‘One of the most fundamental lessons that Chad offers today is the importance of ensuring that minimum conditions of respect for human rights, fiscal transparency, and demonstrated government capacity to implement pro-poor programs are in place prior to promoting investment in the extractive industries.’ That’s a high standard. It would preclude investment in many countries where international oil and gas
companies now work. Most companies probably prefer to think their investments and operations make possible and therefore should precede the stipulated conditions. They prefer to think the wealth created by their operations improves life for poor people in the countries where they work. Indeed, it can and should. Yet it too many places it does not. The Chad experiment is vitally important because it represents an attempt by the oil and gas industry, the World Bank, and governments to improve the record. And it’s a reminder to the industry that meeting a growing world’s energy needs – important as that is – isn’t enough. The real job is to make the world better tomorrow than it was yesterday. (“The oil experiment,” 2005, p. 19)

This changing mindset represents progress. Nevertheless, difficult tensions remain: the world demands rapidly increasing quantities of low-cost hydrocarbon energy, but at the same time it expects complex, time-consuming procedures to be implemented before exploiting the energy resources it so often takes for granted. Without concerted efforts to develop standards, procedures and capacity-building initiatives, many energy projects may come to fruition with little or no safeguards at all. The Chad ‘experiment’ suggests, albeit tenuously, that to be effective such initiatives must accommodate government mandates for the maintenance of domestic security.

Finally, the use of conditionalities, often derided by many activists and academics, seem to hold the key for successfully addressing many of the most difficult and delicate challenges that the oil and gas industry, as well as the energy consuming world, must inevitably confront. Some academics now seek to “encourage reluctant international institutions to pressure and accompany governments in adopting structural and political reforms in return for their support in bringing other investors to the table” (Delescluse, 2004, p. 43). In the future, successful programs will be more pragmatic if their proponents are serious about sustainable poverty reduction. Although it is unfortunate that the government of Chad ultimately chose not to comply with the revenue management program, perhaps the government might be forgiven if, in the heat of the moment, it viewed rebel advances on the capital as a more pressing matter than infrastructure construction. An old saying comes to mind, roughly translated: ‘in order to be obeyed, one must ask for reasonable things.’

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Endnotes

1. Author’s calculations based on monthly data.
2. A basis point is equal to 1/100th of a percentage point.
4. The discount is a result of the poorer quality of Doba crude, for which limited refining capacity and relatively unfavorable market conditions depress its price.
5. According to a UNDP/World Bank study, the discount deepens as the nominal benchmark price increases (Crude Oil Price Differentials and Differences in Oil Qualities: A Statistical Analysis. (2005). Washington, DC: World Bank and International Finance Corporation.). Industry estimates have placed the Doba discount in the range of $8 to $18 per barrel from Brent benchmark prices (Jury Is Out on Chad’s Cure for the Oil Curse. (2005, February 28). Petroleum Intelligence Weekly.).
6. The report offers a litany of criticisms, including a lack of transparency on the part of the private consortium. Its findings were heavily reported in the international news media and were received with genuine concern and seriousness by prominent oil and gas trade publications.