PDP/06/2

IMF Policy Discussion Paper

Strengthening Transparency in the Oil Sector in Cameroon: Why Does It Matter?

Stéphane Cossé

INTERNATIONAL MONETARY FUND

 PDP/06/2

IMF Policy Discussion Paper

African and Policy Development and Review Departments

Strengthening Transparency in the Oil Sector in Cameroon: Why Does It Matter?

Prepared by Stéphane Cossé[1]

March 2006

Abstract

There has been a growing recognition of the importance of transparency for economic growth and social development in oil producing countries. This paper analyzes transparency issues in Cameroon's oil sector. It shows that, while substantial efforts have already been undertaken, continued action is necessary to strengthen transparency. The paper seeks to identify why and how transparency, especially in the fiscal area, matters for economic development and poverty reduction in Cameroon.

JEL Classification Numbers: O11,O12, O17, O55, Q30, Q32, Q38,Q39, Q48

Keywords: Cameroon; African economies; transparency; fiscal transparency; oil sector; oil producing countries; EITI; governance; oil revenue; public expenditure

Author(s) E-Mail Address: scosse@imf.org

---

[1] The author moved to the Policy Development and Review Department when this paper was being drafted. The author would like to thank Doris Ross for her very helpful guidance in the drafting of this paper, as well as Michele Shannon and Hans Weisfeld for their insightful comments. He is also grateful to Francine Nyankiye for her assistance in compiling data and to the other members of the IMF's Cameroon country team for their help.

I. Introduction

There has been a growing recognition over the last decade of the importance of transparency and strong governance for economic growth and social development, particularly in oil-producing economies. The sharp rise in international oil prices over the last two years, resulting in large windfall profits for oil-producing countries, has also strengthened calls from civil society and a broader range of stakeholders for greater transparency and accountability. The International Monetary Fund has recently published a *Guide on Resource Revenue Transparency*, while the U.K.-led Extractive Industries Transparency Initiative (EITI) has garnered increasing international support in both oil-producing and consumer countries.[2] The EITI aims at fostering voluntary cooperation between governments, private oil companies, and civil society to enhance transparency in the oil and mining sectors.

Against this background, this paper analyzes transparency issues in Cameroon's oil sector. It shows that, while substantial efforts have already been undertaken to strengthen transparency, continued and sustained action is necessary to address the remaining gaps in this area. In the early 1990s, the authorities enhanced their supervision of the national oil company (Société Nationale des Hydrocarbures, SNH), including over the transfer of oil revenue to the budget. Efforts were also significantly renewed in 2005 as part of the authorities' broader commitment to enhance fiscal transparency and reporting in the context

[2] Nearly 20 countries have endorsed EITI, including the eight sub-Saharan African oil producing countries (see www.eitransparency.org). The Cameroonian authorities announced in March 2005 that they would adhere to the EITI principles and work with other stakeholders in the oil sector to improve transparency.

of the implementation of their programs with the IMF.[3] Looking ahead, further steps to enhance accountability are nevertheless needed to improve the use of oil revenue and to strengthen fiscal policies to meet the country's development priorities. Notwithstanding substantial oil-generated resources over the last 30 years, Cameroon has remained a low-income country with relatively weak social indicators.

The paper seeks to identify why and how transparency matters in Cameroon's oil sector. It stresses in particular that fiscal transparency can help economic development and poverty reduction. To this end, the government needs to include in the state budget all the oil revenue it should receive and to make related government receipts more predictable, thereby allowing notably more and steadier government spending. Furthermore, enhanced oil transparency can also lead to stronger accountability and in turn can contribute to improved governance and strengthened business confidence.

The paper begins with an overview of the oil sector in Cameroon. It then reviews the main benefits of increased transparency in the oil sector and identifies key specific gaps in Cameroon, underlining in particular progress that could be achieved in the fiscal area. Finally, it underscores the authorities' recent policy commitments and action to increase transparency and provides recommendations on further steps.[4]

---

[3] An IMF staff-monitored program agreed in early 2005 was replaced in October 2005 by a medium-term economic program supported by the Fund through a Poverty Reduction and Growth Facility arrangement.

[4] For a broad cross-country perspective on improving petroleum revenue management in sub-Saharan Africa, see Katz and others (2004) that outlines some of the issues discussed between IMF staff and African policymakers during a seminar held in Douala, Cameroon, in 2003.

II. How Important Is Oil Production for the Cameroonian Economy?

Production is declining, but at an uncertain pace.

Cameroon is the smallest oil producer in sub-Saharan Africa (Figure 1), and production levels are declining. Production started in 1976 and reached its peak in 1986 at 173,000 barrels/day. It declined by nearly 40 percent over the decade through 1996. However, the pace of the decline slowed to about 10 percent during the last eight years (to 90,000 barrels/day), reflecting the effects of improvements in technology that allow for higher oil extraction per well (Figure 2).[5] Private oil companies are responsible for exploration and exploitation, but the government remains a key actor in the sector (Box1).

Box 1. Institutional Arrangements in the Oil Sector

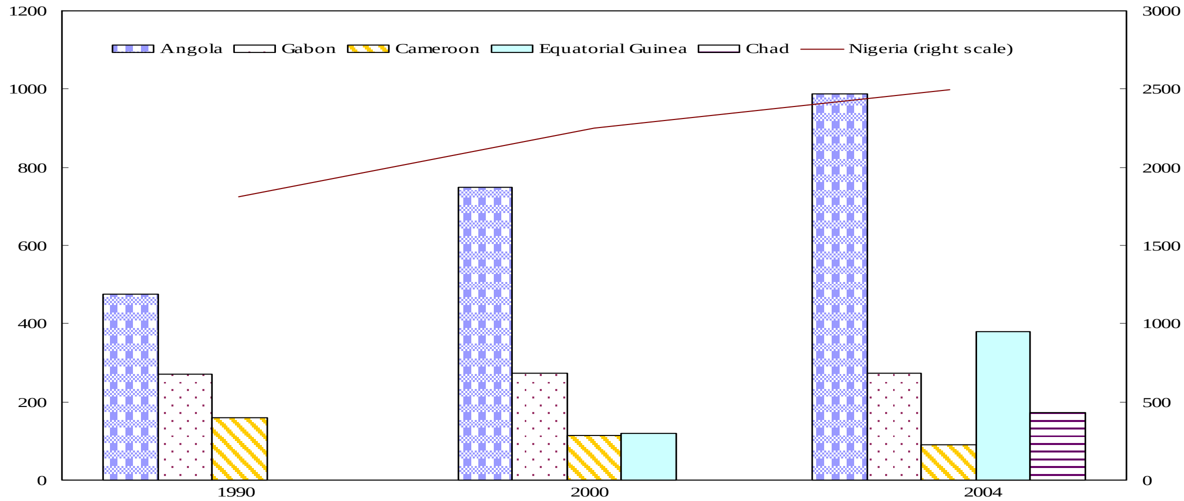
In Cameroon, the main oil-producing companies are Total (68 percent of total production), Pecten/Shell Cameroon (23 percent), and Perenco (9 percent).

The government is represented in the oil sector through the Société Nationale des Hydrocarbures (SNH), the national oil company under the aegis of the secretary general at the presidency. Its role is to assist the authorities in their financial relations with the private oil companies. SNH is also responsible for selling the government's share of oil output (both in the international market and to the national oil refinery), and for transferring the resulting oil revenue (after accounting for expenditures) to the treasury. SNH is marginally involved in oil production, as it exploits jointly with Perenco an oil field that accounted for 1 percent of the country's output in 2004. Finally, SNH holds a 20 percent stake in Total, Pecten, and Perenco and other stakes in companies involved in oil sector downstream activities and in non-oil-related activities.

The relations between the private oil companies and the SNH, including the tax regime, are contractually defined in the Production Sharing Agreements (PSAs). The PSAs are described in detail in the Appendix.

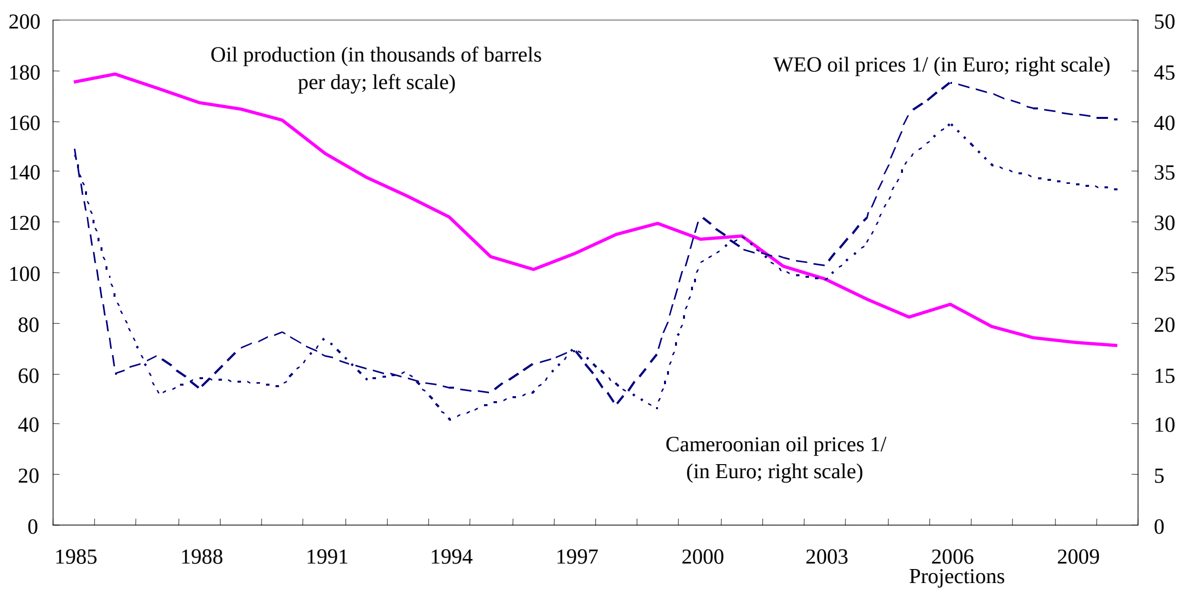
[5] Cameroon's crude is heavy. It was sold at prices on average US$2/barrel below the World Economic Outlook (WEO) price (a composite of three types of crude) over the two last decades. This differential recently widened as a result of an increase in the world demand for higher-quality crude.

Figure 1: Sub-Saharan Africa: Oil Production, 1990, 2000, 2004
(In thousands barrels per day)



Sources: National authorities; staff estimates.

Figure 2: Cameroon: Oil Production and Prices, 1985–2010



Sources: Cameroonian authorities; staff estimates.

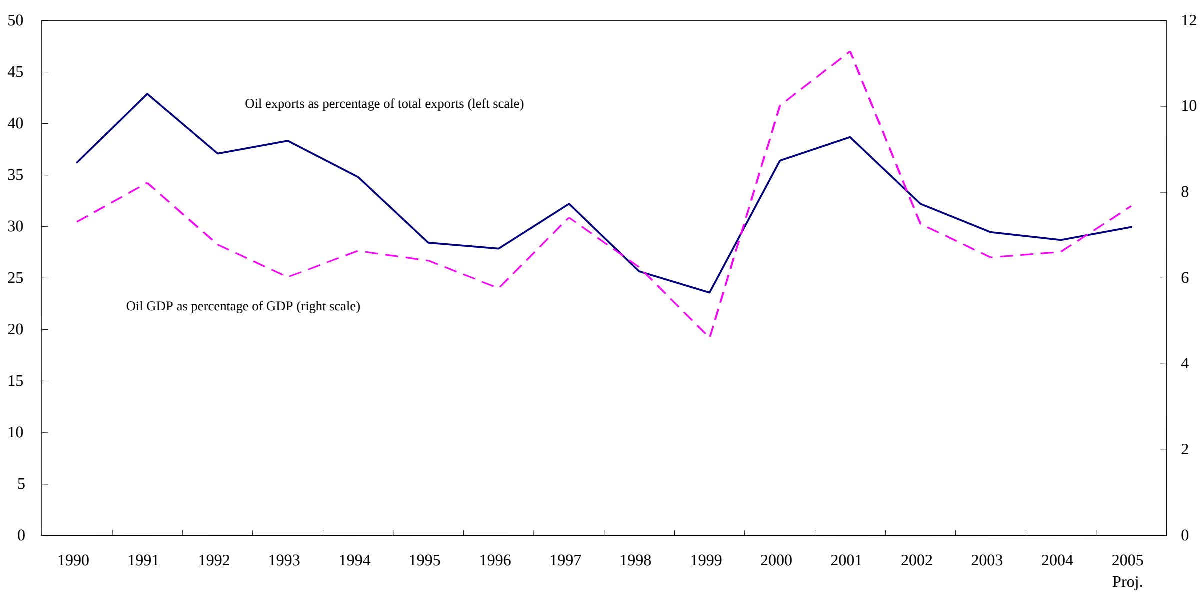
1/ The fixed exchange rate in euro has been applied to the French franc for the period 1985–99.

Oil experts project that the production will continue to decline over the medium to long term, but at an uncertain and likely slower pace. As a result of an intensification of deeper drilling in exploited fields, proven reserves have been revised upward by 13 percent in the past two years; as a result, the rate of output decrease is expected to slow in the coming years.

Furthermore, several new exploration contracts were signed. Although there has not been a major new oil field discovered, technology upgrades and rising international oil prices are expected to continue to provide a strong stimulus for exploration in the coming years.[6]

On a value basis, oil output accounted for 7.5 percent of total GDP in 2004, close to its level 15 years ago despite the decline in output (Figure 3). Favorable developments in both oil prices and the exchange rate have contributed to offset the volume effect.[7] In the same vein, the share of oil exports relative to total exports, amounting to nearly one-third in 2004, declined only slightly in the last 15 years.

Figure 3: Cameroon: Oil's Importance to the Economy, 1990–2005



Sources: Cameroonian authorities; staff estimates.

[6] The regional demand for natural gas and the level of proven reserves are not deemed sufficiently important at this stage to justify starting large-scale production.

[7] Oil prices in CFA francs were, in nominal terms, 3½ times higher in 2004 than in 1990 and, in real terms (CPI adjusted) twice as high. This mirrors two effects. First, world oil prices doubled. Second, the CFA franc depreciated against the U.S. dollar, mostly as a result of the devaluation in 1994 of the CFA franc against its peg—the French franc—by 50 percent (and notwithstanding some appreciation since the CFA franc was pegged to the euro in 1999).

Upstream activities in the oil sector in Cameroon consist mainly of off-shore production and pipeline services for the transit of Chad's oil production (about 200,000 barrels a day). Pipeline activities, however, do not provide significant value added (Box 2).

Box 2. The Economic Impact of the Chad-Cameroon Pipeline

The Chad-Cameroon pipeline project has had two economic effects in Cameroon:

- **A temporary contribution to construction activity in 2001–03**. Although most related equipment was imported, there was sizable spending with local business (such as construction services, transportation, and telecommunication). From the inception of the project in October 2000 to its completion in December 2003, local spending amounted to CFAF 264 billion, or 3.8 percent of 2002 GDP. Local employees were also hired on a short-term basis, peaking at almost 6,000 in 2002. Permanent employment has stabilized at around 700 local workers.

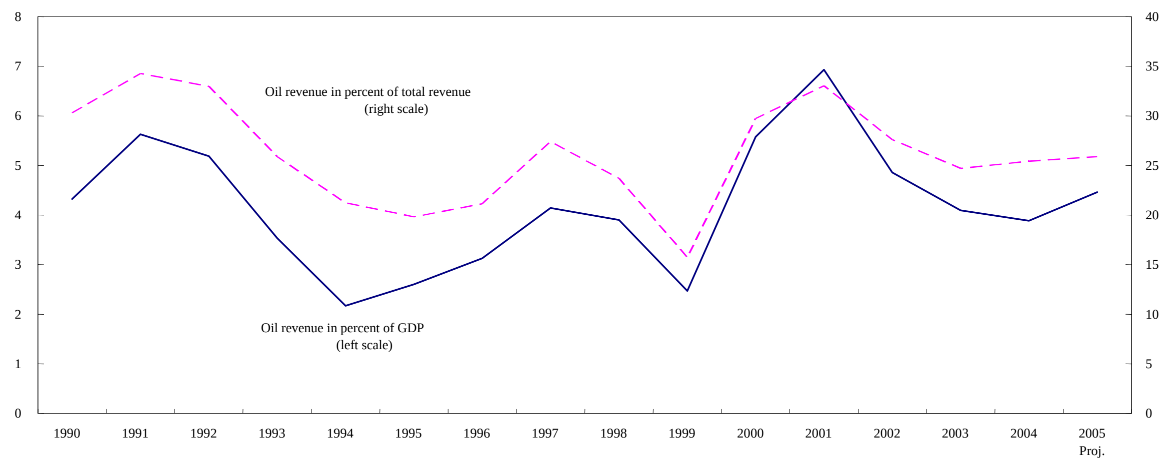
  In terms of GDP contribution, total pipeline-related investment in Cameroon in 2001–03 amounted to 3 to 5 percent of GDP per year. The net impact, excluding the spillover effects on local consumption, was less sizable (0.5 to 2 percent per year); as a result, there was a predominant reliance on imports of goods and services. The incremental effect on economic growth during that period was nevertheless relatively important, as shown by the slower rate of GDP growth in 2004–05 after completion of the project.

- **A relatively small increase in government revenue stemming from the transit fee (US 41 cents per barrel) on account of the pipeline**. Based on a projected flow of 200,000 barrels a day (expected to be the average in future years), government revenue collected from the transit fee amounted to about 0.8 percent of total revenue in 2005 (0.2 percent of GDP).

Oil revenue, though variable, provides a sizable share of government revenue.

Oil revenue collection has averaged 4.2 percent of GDP since 1990, with a low of 2.2 percent in 1994 and a high of 6.9 percent in 2001 (Figure 4). Based on current projections, this contribution will remain within the range of 3–5.5 percent of GDP through the end of the decade, reflecting in particular the impact of projected high international prices. Oil revenue has accounted for an average of about one-fourth of overall revenue since 1990. This share has fluctuated, however, between 16 and 35 percent, pointing to the need to take into account oil revenue volatility in formulating fiscal policy and in assessing medium-term fiscal prospects.

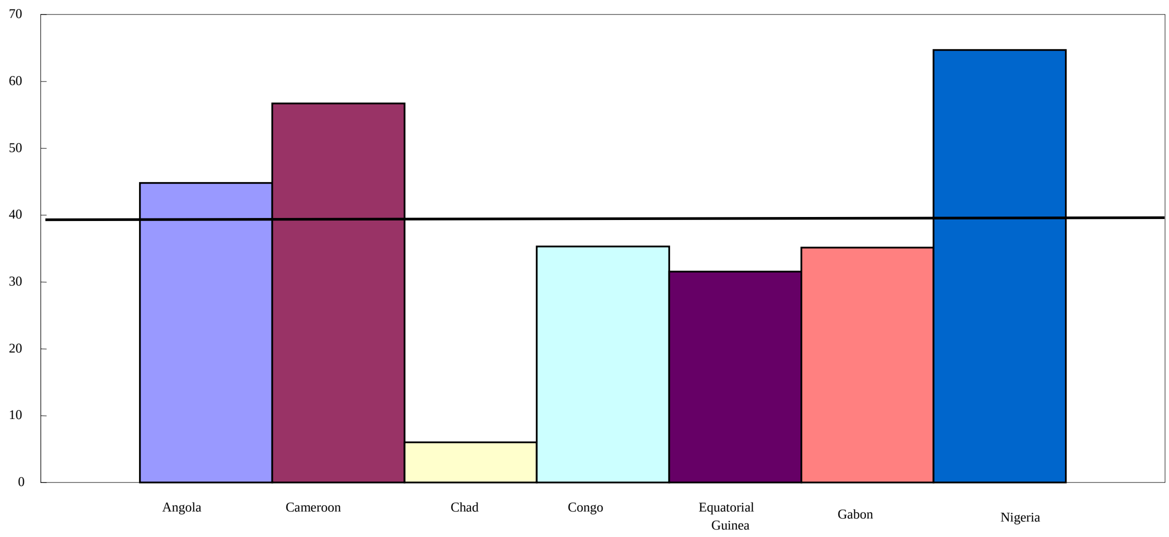
Figure 4: Cameroon: Oil revenue, 1990–2005
(In percent of GDP)



Sources: Cameroonian authorities; staff estimates.

Finally, the oil revenue accruing to the government accounts for almost two-thirds of the value of oil exports. This share (sometimes called the “oil take”) is relatively high when compared to an average of 53 percent in other sub-Saharan African oil-producing countries (Figure 5). The level of government revenue to exports depends in each country on the production and transportation costs and the contractual conditions agreed between the government and oil companies. In Cameroon, a large share of the fixed costs is now amortized while transportation costs from off-shore platforms are low.

Figure 5: Sub-Saharan Africa: Oil Revenue, 2004
(In percentage of oil exports)



Sources: National authorities; staff estimates.

III. Why Is Transparency Important in the Oil Sector?

Empirical work, particularly in the last decade, has demonstrated the importance of transparency and good governance to effective policymaking, economic growth, and poverty reduction.[8] The prevalence of weak transparency and corruption in public management is not limited to oil-producing countries, but oil-rich economies appear to be in this respect particularly vulnerable. The oil sector is prone to mismanagement and abuse because of the magnitude of the revenues at stake, its enclave-sector nature with few people involved, and the complexity of fiscal arrangements. Strengthened effort to enhance transparency in the oil

---

[8] See, for example, Kaufmann, Kraay, and Zoido-Lobaton (1999) and subsequent surveys carried out by the World Bank (www.worldbank.org/wbi/governance).

sector can therefore be instrumental in changing overall perceptions about governance in the country. [9]

Furthermore, specific attention needs to be given to the exhaustible nature of oil. Because oil constitutes nonrenewable national wealth, the principle of an intergenerational distribution of government income flows should apply.[10] Currently, the relatively modest level of government revenue from oil and Cameroon's ability to ensure quality spending is deemed sufficient to make immediate use of oil revenue (rather than to save a share of proceeds to generate a financial income). Quality spending, i.e., productivity-enhancing expenditures, is essential to ensure that future generations benefit equally from the oil wealth (which would take the form of a manmade wealth). It is in this context critical that oil resources be used in line with the medium to long-term priorities that have been set out in the country's Poverty Reduction Strategy Paper (PRSP) (which could be compared to the country's perception of how the future wealth of the country should be shaped). The PRSP, which was issued in 2003 and annually updated since then, was drafted in consultation with the civil society.

IV. What Are the Key Specific Gaps for Cameroon?

Although significant efforts were undertaken in the early 1990s to improve transparency in

[9] Cameroon was ranked 137th out of 159 countries in Transparency International's 2005 Corruption Perception Index.

[10] As discussed in Davis, Ossowski, and Fedelino (2003) and Katz and others (2004), national wealth can be approximated by the present value of the rent earned in its production (essentially, proceeds from projected future sales after deduction of the relevant costs). Using the principle of intergenerational equity, this national wealth should be used in a manner that will leave future generations at least as well off as the current one.

the oil sector (Box 3), there remains substantial scope for further improvements in four main areas.

Box 3. Efforts to Promote Transparency in the 1990s

Efforts were made to promote transparency in the 1990s, including in the context of Fund-supported programs. The first independent audit of SNH was conducted in 1991 by an international accounting firm and was made available to Fund staff. SNH also began to provide routinely to Fund staff data on oil production, exports, prices, revenues, and costs. Regular information on budgetary payments directly made by SNH through cash advances has been made available to Fund staff beginning only in 2005.

With stricter monitoring made possible by the improvements in available data, it appeared that oil revenue was not always transferred to the government on a timely basis. As a result, in the late 1990s, the authorities established a coordination mechanism, including monthly meetings between officials of the SNH and the government's Technical Monitoring Committee (CTS)—which also monitors the implementation of Fund-supported programs. Under this mechanism, SNH's cash payments are reviewed on the basis of effective production/revenue data. SNH also adopted a new accounting system in line with international standards in 2000.

An operational and managerial audit conducted in 2000 raised the issue of whether SNH should maintain activities beyond its initial mandate. The authorities agreed at that time to a review of the respective roles of the SNH and the private sector in the oil sector, but have not yet initiated it.

A broad perception of a lack of transparency in oil earnings and revenue.

Transparency is perceived to be lacking as a result of the complexity of the production-sharing agreements (PSAs), which limits the understanding of institutional arrangements in the sector. The PSAs are described in detail in the Appendix. Publication of basic information regarding these agreements (on the website of SNH), such as in Table 1, would support better public understanding of oil sector flows. For instance, it could usefully be explained that oil companies receive between 13 and 22 percent of the oil profit,[11] with the remaining portion accruing to the government either through corporate taxes paid by the private oil companies or through transfer by SNH of the oil profit generated by the sales of the government's share of oil output.

[11] Oil profit is defined here as production minus operating costs. The oil profit percentage per field will be higher for fields that are more difficult to access and carry higher exploration risks (which are not reimbursed if unsuccessful).

Table 1. Cameroon: Distribution of Oil Resources, 2003–04
(in percent)

	2003	2004
Sales	100	100
Operating costs	27	29
Government revenues	59	57
Oil companies' earnings 1/	14	14

Sources: Cameroonian authorities; staff estimates.

1/ This corresponds broadly to the net profit after tax of the private oil companies, mostly allocated to dividends; 20 percent of the dividends are redistributed to SNH as a shareholder.

A lack of well-specified and transparent rules for the transfer of oil revenue.

As a basic principle of fiscal transparency, all government revenues, including those deriving from oil, should be accounted for in the budget, unless well-specified and monitorable alternative arrangements are in place.[12] This is essential because full accounting for revenue facilitates the allocation and monitoring of budgetary resources consistent with spending priorities. In the same vein, spending must be fully accounted for, even when funded through the use of oil revenue. If oil revenue and spending are only partly recorded, policymakers and the public cannot assess the amount of available budgetary resources that can potentially be directed toward poverty-reducing expenditure out of the effective level of total expenditure and, thereby, verify whether the priorities defined in the country's Poverty Reduction Strategy are being implemented.

[12] On the specificities of these alternative arrangements, see the Fund's *Guide on Resource Revenue Transparency* (IMF, 2005).

In Cameroon, three main issues related to the transfer of oil revenues have been undermining transparency of budgetary operations and the assessment of the level of budgetary resources. First, the government does not always receive the full revenue amount it should receive. Theoretically, the government should receive at the end of each month SNH's collected revenue based on net receipts during the month—that is, SNH should transfer its oil profit to the budget with deductions only for the operating costs shared with the private oil companies. In practice, however, SNH makes additional deductions.[13] Some of these expenditures are directly related to SNH's oil activities (such as provisions for the decommissioning of oil fields), but others are not (such as administrative costs related to the construction of the Chad-Cameroon pipeline or fuel purchases for the government). This extrabudgetary spending would normally need to be included in the consolidated government accounts. Corporate tax payments to the treasury (which are made by the private oil companies in three equal installments based on the profits earned in the previous year) and the amount of dividends to be transferred to SNH are difficult to check for consistency because the companies are not legally required to disclose them publicly.[14]

Second, in addition to the deductions described above, the payments the government receives from SNH are reduced by the amount of the cash advances made by SNH in response to pressing payment requests by the government (typically spending for national security, sovereign entities, or public enterprises). Table 2 illustrates the size and nature of this

[13] These additional costs reduced the actual revenue transferred to the government by nearly 10 percent during 2003–04.

[14] Private oil companies' accounts are certified by auditors consistent with international standards and integrated in the consolidated accounts of the parent company abroad. These consolidated accounts are public.

spending. The corresponding expenditures and revenues are imputed ex-post in the budgetary execution, i.e., they circumvent normal budgetary procedures and are undertaken without ex ante authorization through a payment order (commitment) (as well as, until end-2004, without the minister of finance's authorization). This system of cash advances by SNH distorts the elaboration of the budget law. When the budget law is adopted, the allocation planned for some ministries is below the level the authorities anticipate to be their actual expenditures (e.g., ministry of defense, presidency), as it is expected that SNH's cash payments will cover the difference. At a later stage, while the budget is being executed, the reporting on a functional basis does not reflect the actual composition of spending; this is because in order to remain within the overall budget allocation, these expenditures for which budget allocations were initially insufficient need often to be attributed to ministries/common expenditure budget lines with budgeted allocations that have not yet been fully disbursed.

Table 2: Cameroon: Cash Advances by SNH
(in percent)

	2003	2004	2005 (Jan.-July)
Presidency	21.7	37.5	24.8
Ministry of Defense	34.1	32.8	63.5
Cameroon Airlines	32.0	15.0	5.7
Others	12.2	14.6	6.0
Total	100.0	100.0	100.0
In percent of SNH's revenue	24.6	23.0	19.3
In percent of total government revenue	5.1	4.9	5.0
In percent of budget expenditures 1/	13.1	10.8	14.4
Memorandum items			
In percent of budgetary allocation 2/			
Presidency	44.5	71.1	70.2
Ministry of Defense	59.7	54.0	92.6

Sources: Cameroonian authorities; staff estimates.
1/ Total expenditures excluding interest, salaries and pensions, foreign-financed expenditure, and restructuring expenditures.
2/ Excluding salaries and pensions.

The third issue about the transfer of oil revenue relates to the lack of clarity in the transfer of dividends received by SNH. SNH separates its activities between those carried out on account of (“mandated by”) the government (ensuring the implementation of the PSAs with the private oil companies) and those conducted as a commercial oil company. The latter includes a direct—but marginal—involvement in oil production and exploration, as well as management of various holdings in mostly oil-related companies in Cameroon.[15] This raises two questions. Should SNH be directly involved in oil production activities? With almost the entirety of production entrusted to private oil companies, the rationale for involving SNH at the production stage is not clear. Then, how should the dividends received from SNH’s stakes in oil companies be used? In recent years, the SNH Board has only partly redistributed these dividends. Some of the dividends were allocated to investment in oil production, while others were held as unused liquidity.[16] To the extent that SNH is holding shares in the private oil companies on behalf of the government, it should adopt a clear and publicly-stated policy on the use of dividends received from the private oil companies, including their systematic and complete transfer to the government, or any alternative uses.[17]

---

[15] As described in Box 1.

[16] Amounting to 0.7 percent of GDP at end-2003.

[17] According to SNH’s officials, these savings are needed to finance a possible (but yet unspecified) expansion of the company’s commercial activities.

A need to abide by a fiscal rule on the use of oil revenue for an effective conduct of fiscal policy.[18]

As part of the government's overall fiscal and economic objectives, the government should state in a transparent manner how oil revenue is used consistent with medium-term fiscal sustainability. Such a policy statement should also indicate how the variability of international oil prices will be addressed.[19] While Cameroon's economy is more diversified than that of many other oil-producing countries, price- (or volume-) driven variations in oil revenue—accounting on average for one-fourth of total revenue over the last 20 years—can disrupt fiscal and macroeconomic balances that are not conducive to private sector activity and growth. Furthermore, budgetary planning and prioritization become more complex and spending rigidities created during boom cycles can be difficult to unwind, threatening medium-term fiscal sustainability.

Over the last decade, the rules envisaged to smooth out the impact of the volatility of oil revenue on budgetary execution have been only implicit, at times difficult to implement, and not always applied. For instance, in the second Fund-supported PRGF arrangement (2000–04), the implicit rule was to target broadly the overall balance at zero and the nonoil balance negative by the amount of oil revenue. The nonoil primary balance was contingent on the level of oil revenue, implying adjustment in nonoil revenue or primary expenditure to keep the overall balance at zero. The implementation of the government's overall fiscal strategy

---

[18] For a discussion on the importance of a fiscal rule on the use of oil revenue, see Davis, Ossowski, and Fedelino (2003).

[19] For a discussion on possible tools for fiscal policymakers in oil-producing countries, see Barnett and Ossowski (2002).

required therefore a strict monitoring with strong ownership and coordination in order to anticipate and react to possible adhoc adjustments (even though adjustments in expenditures were limited to half of the change in oil revenue in order to mitigate swings in budgetary execution). Ownership and government coordination turned out, however, to be weak during the program period. Furthermore, the rule was applied on a cash basis, and at the same time Cameroon accumulated large domestic arrears in 2003–04, thus undermining the overall approach and putting at risk fiscal sustainability over the medium term.[20]

Limited dissemination of information undermining public scrutiny and accountability. Publication of data on the oil sector has been very limited in Cameroon, thus preventing effective public scrutiny and an active debate on the use of oil resources. In order to hold policymakers accountable and to strengthen governance, the public (particularly parliament and civil society organizations) needs information on how oil resources are generated and spent (or saved). Involving directly experts and/or nongovernmental organizations can also contribute to promote the public debate as they can help explain the often complex issues in this sector. Furthermore, encouraging active parliamentary engagement, particularly at the time of the discussion of the budget law and the *loi de règlement*, can support a more effective oversight.

[20] Net domestic arrears rose by about 5 percent of GDP, resulting in an increase of domestic debt to about 18 percent of GDP (excluding sizable contingent government liabilities in ailing public enterprises).

V. Progress to Date to Address Key Gaps

Against this background, as part of their economic program that was monitored by the Fund staff and subsequently supported by a Fund arrangement, the Cameroonian authorities took several steps in 2005 to address shortcomings in oil transparency. Box 4 summarizes key measures and initiatives that were implemented, particularly to strengthen the budgetary process and promote data dissemination. The remainder of this section focuses on the specific efforts to formulate a fiscal rule to smooth out the volatility of oil revenue.

Box 4. Oil Transparency Reform in 2005

Strengthening transparency in the budgetary process

Under the programs agreed with the IMF, the authorities have committed to (i) limiting the level of SNH's additional costs related to oil production activities to a fixed annual amount; (ii) limiting SNH's cash advances only to sovereign spending sector in the second half of 2005 and eliminating them in 2006; and (iii) undertaking cash advances only after prior approval by the minister of finance and within remaining budgetary allocations. Also, in September 2005, the prime minister signed a decree that increased the budgetary allocations for ministries that had relied on these advances above existing authorization levels (e.g. the ministry of defense) in order to reflect SNH's advances in the proper expenditure categories. This decree was to serve as a benchmark for the authorities in setting budgetary allocations in the 2006 budget law. Overall, these measures, if fully implemented, represent a major advance toward budgetary transparency and should enable better monitoring of the composition of spending, including poverty-reducing expenditures.

Encouraging public scrutiny and debate

Oil sector data are now published on the website of SNH (www.snh.cm) and of the prime minister's office (www.spm.gov.cm). They include quarterly production and revenues, as well as SNH's annual audits up to 2003, both for SNH's activities on account of the government and for its own activities. This also illustrates the attention that Cameroon gives to its participation to the worldwide Joint Oil Data Initiative (JODI) to raise the awareness of all oil market players of the need for more transparency in oil market data.

Civil society and other stakeholders in the oil sector have since July 2005 been increasingly involved in the sector as a result of the establishment of the committee (and its technical secretariat) in charge of monitoring implementation of EITI principles in Cameroon. In October 2005, a draft EITI action plan was sent for discussions with civil society and oil companies with a view to finalizing it in early 2006.

Clarifying the key elements of PSAs

The authorities approached oil companies to seek their approval to publish key parameters of the production-sharing agreements.

To address past weaknesses in the conduct of fiscal policy, the authorities' fiscal program for 2005–08 has been designed to free policymakers and the government from the need to make major adjustments in core fiscal operations on an ongoing basis and to allow them to focus on the overall fiscal strategy. The program allows for more predictability in setting the level of primary expenditure. The overall balance target is set at a level such that if oil revenue fluctuates, the level of primary expenditure does not need to be adjusted as long as the changes in the overall balance (especially its deterioration in case of a revenue decline) do not put at risk fiscal sustainability over the medium term. If oil revenue declines more than projected, primary expenditures are not adjusted but the initially projected domestic debt/arrears repayments is.[21] Lower net repayment of domestic debt/arrears offsets the deterioration of the overall balance. If oil revenue is higher than programmed, the windfall is used to accelerate domestic debt/arrears payments.

Using this rule raises the issue of forecasting oil prices and volumes, which are key parameters underlying the envelope for spending consistent with fiscal sustainability under the medium-term fiscal framework.[22] Both oil prices and volumes are conservatively set. The oil price is projected on the basis of the WEO but includes a safety margin and a discount to reflect Cameroon's lower crude quality. The program also includes a sensitivity scenario

---

[21] In Cameroon, around 80 percent of the government domestic debt/arrears is owed to banks and suppliers. About half of this debt is not securitized, which brings an element of flexibility in the repayment schedule. Alternatively, the government could borrow from local banks and keep the projected repayment schedule unchanged.

[22] Empirical works have shown that oil prices are more volatile than prices of other commodities; see Engel and Valdès (2000) and Bartsch (2005). The authors argue that the profile of oil prices over a 30-year period can be best described as nearly as close to a random walk process.

indicating the implications of a possible decline of oil prices assumed at € 25/barrel.[23] Given the initial projected fiscal path, the overall fiscal position remains at a sustainable level, although some adjustments would need to be considered beyond the program period.[24]

One of the main strengths of this approach is to facilitate the establishment of medium-term expenditure frameworks (MTEFs) in priority sectors in line with the country's Poverty Reduction Strategy. Furthermore, the fiscal path can be revisited, particularly at the time of the annual budget formulation, if, for instance, domestic debt payments are larger than initially projected owing to higher-than-assumed oil revenue over a sustained period, implying a faster-than-planned consolidation of the overall fiscal position. In such a case, primary expenditure can be increased, provided there is sufficient absorptive capacity.

VI. Conclusion: The Path Ahead

Despite a projected decline in oil output, the resources generated by the oil sector will remain of macroeconomic relevance in the years ahead. Continued action to enhance transparency and accountability in the oil sector will therefore help to further strengthen governance and enhance budgetary execution to direct budgetary resources toward priority spending. The

[23] The price is defined in euro to neutralize the exchange rate effects (the CFA franc is pegged to the euro). Cameroon's crude averaged €19/barrel over the past 20 years. It is projected to average €37/barrel during the program period.

[24] Based on projections in September 2005, the outstanding stock of domestic debt would decline from 18 percent of GDP in 2004 to about 10 percent in 2010 at program prices. The stock would increase to 23 percent if prices were instead at €25/barrel.

measures implemented in 2005 represent good progress on transparency reform. In the future, greater efforts could be pursued in several directions:

- Providing information on the production-sharing agreements would complement existing initiatives to improve the perception of governance. The authorities and the oil companies have explained that these contracts are confidential and therefore cannot be made public unless both parties agree. Oil companies argued that publishing contractual conditions would generate unfair competition and complicate ongoing and future negotiations in Cameroon and/or other oil-producing countries. Although the contract itself could remain confidential, key parameters could be published to illustrate how oil resources are allocated between oil companies, SNH, and the government.
- Budget transparency could be strengthened by the full and timely transfer of oil revenues to the treasury and gradually shifting to a classification by economic nature. The authorities' decision to avoid resorting to SNH's cash advances from 2006 and to instruct SNH to limit its "additional costs" to strictly oil-related activities is welcome; compliance will be key in the near and medium term. The formulation and publication of clear rules on the use of dividends collected by SNH on behalf of the government from private oil companies will also be key to enhance transparency on the transfer of oil revenues. Furthermore, provided budget reporting is sufficiently developed, the authorities should consider the benefits of presenting oil sector budget data based on the IMF's *Government Finance Statistics Manual 2001* (GFSM 2001).[25]

[25] This would allow to (i) make the relationships within the general government sector, the SNH, and the private oil companies more explicit in the sense that government's financial investment in those entities would be reflected as part of government accounts; (ii) improve the classification of "oil revenue" according to the

(continued…)

- Facilitating further public scrutiny would contribute to changing public sentiment on government accountability. Steps in this direction include making the technical secretariat of the EITI committee fully operational quickly, proceeding with consultations with the private sector and civil society, and formulating and implementing a specific consensus-based action plan. Other key measures in this area would include improving the timeliness of SNH's audits and their publication and routinely publishing on a quarterly (or monthly) basis information on total oil production, prices, and revenue to the government.
- Implementing the EITI principles, beyond the progress already made, would clearly indicate that Cameroon strives to comply fully with international standards on oil transparency (Box 5).

Box 5–Implementing EITI Principles

EITI mainly consists of entrusting an independent administrator to compare oil sales and revenue as declared by oil companies and as recorded by the government. Out of some 20 countries that have signed up to the EITI, eight were recognized at an EITI conference in March 2005 to be actively implementing the initiative: Azerbaijan, Ghana, Kyrgyz Republic, Nigeria, Republic of Congo, São Tomé and Principe (STP), Timor Leste, Trinidad and Tobago (source: www.eititransparency.org). So far only Azerbaijan is regularly publishing oil revenue information consistent with the EITI principles.

Other implementation measures noted on the EITI website include:

(i) publishing data on production and oil revenues (Azerbaijan, Timor Leste, Republic of Congo, Ghana)
(ii) publishing the main fiscal parameters from production sharing/concession agreements (Timor Leste, Republic of Congo, STP); and
(iii) conducting external audits of public oil companies on an annual basis and publishing them (Republic of Congo, Nigeria).

Cameroon established an EITI committee and secretariat in October 2005. Significant progress has already been achieved on (i) and (iii).

economic nature of the revenue; and (iii) add to the perspective that the natural resources are an asset that should be managed over time (and focus attention also on the stocks).

If these efforts to strengthen transparency are consistently pursued, economic and fiscal policymaking will be more effective, the business environment will improve, and more resources will be freed for investment in social sectors and basic infrastructure, thereby supporting economic growth and poverty reduction efforts in Cameroon.

Appendix. Production Sharing Agreements

This appendix describes the key elements of the production-sharing agreements (PSAs) in Cameroon.[26, 27]

The PSAs consist of the following arrangements:

Sharing production between the SNH and the private oil companies. Private oil companies receive from the government the right to explore/exploit a specific field, but have to share any production generated from the field with the SNH. The split varies from 70/30 in favor of SNH to 50/50.[28] On average, the split is 63/37 in favor of SNH.

Sharing operating costs (i.e., depreciated development costs, depreciated exploration costs, and financial charges). In most cases, the split is 50/50.[29]

Ensuring a minimum income for the oil companies. In the majority of the fields, the guaranteed fixed income is equivalent to 13 percent of the mining return (*rente minière*). The mining return is defined as the difference between total oil receipts (the sum of the sales by SNH and the private oil companies) and operating costs. However, to encourage oil companies to explore in areas within their field that require higher exploration costs (deeper funds), the guaranteed fixed income rate can go up to 22 percent.

Applying corporate taxation and royalties. Corporate tax is 57.5 percent. Given the specific U.S. regulations on dividends abroad, the rate is exceptionally set at 48.65 percent for U.S. companies. The guaranteed fixed income rate, however, remains identical for both U.S. and non-U.S. companies. A royalty (*redevance*) is paid either by the private oil company to the SNH or by the SNH to the private oil company to ensure that the guaranteed income is attained precisely.

---

[26] The report on Cameroon by Wood Mackenzie (2002) was an important source for this appendix.

[27] Under the 1990 Petroleum Code, oil companies can also sign concession contracts with the government. While some concession contracts have been signed, exploration has not been successful and therefore no government revenues have been generated so far under this concession regime.

[28] SNH is associated with Perenco for the exploitation of a small field (EBOME) where the split is 85/15 in favor of Perenco.

[29] Since it is not a direct producer (with the exception of EBOME), SNH needs to reimburse oil companies operating in the field. However, a reimbursement limit is set on operating costs for any fiscal year. Total reimbursements by SNH are limited to the difference between the value of SNH's share of production and the value of 40 percent of the total production. For instance, if the production split is 70 percent in favor of SNH, SNH retains at least 40 percent and the reimbursement limit amounts to 30 percent of field production. This would imply that operating costs would amount to 60 percent of field production with a cost split of 50/50, which is an unlikely situation for a "profitable" field.

References

Barnett, Steven, and Rolando Ossowski, 2002, "Operational Aspects of Fiscal Policy in Oil-Producing Countries," IMF Working Paper 02/177 (Washington: International Monetary Fund).

Bartsch, Ulrich, 2005, "An Oil Stabilization Fund for Nigeria," IMF Country Report 05/303 (Washington: International Monetary Fund).

Davis, Jeffrey, Rolando Ossowski, and Annalisa Fedelino, 2003, "Fiscal Policy Formulation and Implementation in Oil-Producing Countries" (Washington: International Monetary Fund).

Extractive Industries Transparency Initiative. Information and documents available at http://www.eitransparency.org.

Engel, Eduardo, and Rodrigo Valdés, 2000, "Optimal Fiscal Strategy for Oil-Exporting Countries," IMF Working Paper 00/118 (Washington: International Monetary Fund).

International Monetary Fund, 2005, *Guide on Resource Revenue Transparency*, (Washington). Available at http://www.imf.org.

Katz, Menachem, and others, 2004, *Lifting the Oil Curse* (Washington: International Monetary Fund).

Kaufmann, Daniel, Art Kraay, and Pablo Zoido-Lobatón, 1999, "Governance Matters," World Bank Policy Research Working Paper No. 2196 (Washington: World Bank).

Romania, Government of, 2003, *Poverty Reduction Strategy Paper* (Yaoundé). Available at www.imf.org.

——— 2004, 2005, *Annual Progress Report* (Yaoundé). Available at www.imf.org.

Wood Mackenzie, 2002, Report on Cameroon in "Global Oil and Gas Risks and Rewards" (London: Wood Mackenzie).