

**Statement by Mr. Jaime Quijandría before the United States Senate Committee on Foreign Relations on the development impacts of energy projects financed by Multilateral Development Banks.**

Washington, D.C., July 12, 2006

Mr. Chairman, Members of this Committee, thank you for inviting me to discuss this relevant aspect of the activities of Multilateral Development Banks.

First, let me start with a brief comment on my experience concerning the main subject of this hearing. Over the last 15 years I have been involved with energy issues and different ways of financing energy-related projects. During this period I held high level positions both in the public sector (Chairman of the state-owned petroleum company Petroperu) and the private sector (Chairman of the YPF's Peruvian subsidiary). I was also engaged in energy policy issues as I was Minister of Energy and Mines and Minister of Economy and Finance from July 2001 to November 2004, during President Toledo's government. It was during this period that the CAMISEA project was implemented in Peru.

At present, I represent Peru and other five South American countries as Executive Director at the Board of the World Bank.

In spite of what I have just stated, I would like to clarify that my opinions on the subject in question compromise neither the Bank nor the Government of Peru.

I will now address the questions submitted by this Committee in Mr. Chairman's kind letter of July 6, 2006, inviting me to this hearing.

I

CAMISEA was the biggest and most complex project in the history of Peru. That is why when assessing its impacts, both positive and negative, it is necessary to take a wide approach and remember the economic situation, and the situation of the energy sector, in the year 2000. Although Peru has significant reserves of natural gas, discovered by Shell in 1984, due to a lack

of political consensus on the most appropriate way to give value to this source of energy, the country was dangerously more and more dependent on over 1 billion dollars worth of imports of petroleum and its derivatives. Meanwhile, electricity rates, which are to some extent related to the prices of petroleum and its derivatives, threatened to go up significantly.

This scenario changed radically as of August 2004 when the operation of the CAMISEA project started. Two years later, the following positive impacts of its implementation were identified:

- An annual GDP increase of 1% throughout the life of the project (30 years)
- Fiscal revenues of 1.4 billion dollars (19% of total revenues)
- An annual reduction of \$500 million dollars in the fuel trade deficit (the balance of trade, however, remained negative)
- An average 30% reduction in electricity rates (these rates are calculated based on the effects of projects four years before the implementation phase starts). Obviously, this reduction benefited the poorest.
- 7,200 new permanent jobs and another 15,000 temporary jobs
- By law, 50% of the royalties were transferred to the producing region (Cuzco) and an intangible fund was created to finance projects in the regions affected by the project.

I would like to mention that there is no existing legislation in any of the other South American countries that mandates the transfer of such level of resources to the regional and municipal authorities.

Moreover, I have to add that putting a value on these reserves not only reduces the dependency on energy imports but it also opens a window of opportunity for the export of LNG to Mexico and the United States, as well as to other countries. In his recent visit to Chile, President-elect Alan García highlighted the importance of the second phase of the CAMISEA project.

## II

I have already referred to the benefits derived from the CAMISEA project for the population as a whole. In the case of the poorest, the project allows a

reduction in electricity rates just when the international price of crude oil jumped from \$25 to \$70 per barrel. Just imagine what would have happened in Peru in 2005 and 2006 if, as it was the case for the last two decades, the implementation of the project had been postponed.

Furthermore, the infrastructure resulting from this project is located in the departments of Cuzco, Huancavelica and Ayacucho, where a high percentage of the population lives under the poverty line<sup>1</sup>. It is precisely in these departments where health infrastructure, more than 600 kilometers of highways and 20 bridges were built.

### III

The CAMISEA project has certainly had negative effects on the populations living in the area involved. In particular, the indigenous people who live near the gas production facilities have been affected the most. The impact is even worse since some of these indigenous populations had had no contact with the outside world until the project started. In this respect, some of the lessons learned are taken from the recommendations made by different national and international organizations in order to mitigate the negative impact resulting from the implementation of the second phase of the project (exploitation of lot 56). In particular, I would like to refer to the set of detailed recommendations contained in the ombudsman's report<sup>2</sup>, which I think should be discussed and eventually implemented before starting the following phase of the project.

The main recommendations in the Ombudsman's report are as follows:

- Approve specific regulations to effectively protect the rights of the indigenous populations in isolation and at first contact;
- Determine assessment criteria that ensure fair compensation for the damages caused;
- Design and implement mechanisms that ensure fair negotiations and technical assistance to the indigenous communities;
- Modify the current legislation on right of way;

---

<sup>1</sup> According to the National Institute of Statistics, 48% of the population remained under the poverty line in 2005.

<sup>2</sup> "The CAMISEA Project and its Effects on the People's Rights", Ombudsman's Report No. 103, March 2006.

- Intensify the state control over the environmental and social commitments undertaken by the companies involved;
- Strengthen the performance of technical and multidisciplinary inspections of the works that the project entails;
- Extend the period between the release of the studies on environmental impact and the public hearings.

#### IV

When the decision to go ahead with the CAMISEA project was taken, the Government of Peru was aware that a project of this importance and complexity, and which touched very sensitive territories of the country, required compliance with careful social and environmental policies. It was with this aim in mind that the Government of Peru proceeded from start.

Thus the Department of Environment, within the Ministry of Energy and Mines, was responsible for holding public preliminary hearings on CAMISEA and its impacts and evaluating the studies on environmental impact presented by the companies involved in the project.

Additionally, the Government of Peru considered necessary to strengthen the capacity of the state agencies responsible for overseeing the environmental and social aspects of the CAMISEA project, to ensure the sustainable development of the area involved, and to protect the most vulnerable communities.

The Government of Peru also started a program, financed with a loan provided by the Inter-American Development Bank, aimed at strengthening supervision and monitoring capacities, protecting sensitive biodiversity areas and supporting regional and local governments.

With a staff of 25 environmental specialists, OSINERG is responsible for the supervision and monitoring of the environmental impact resulting from the CAMISEA project. So far, OSINERG has carried out 580 inspection visits to the project sites and detected up to 3,078 irregularities, 89% of which have already been corrected. Meanwhile, court decisions are pending involving 33 of the 329 remaining irregularities.

The project is also supervised by DIGESA, an agency within the Ministry of Health that monitors the quality of the water, and by INRENA, which is responsible for protecting the natural resources. Further monitoring of the project is carried out by the indigenous communities with the sponsorship of the Government of Peru, the companies and civil society organizations.

The coordinated work of these three agencies – OSINERG, DIGESA and INRENA – aims at ensuring adequate management of the environmental impacts and has led the companies involved in the CAMISEA project to comply with the guidelines set by the EIA

As an additional important measure, more than 7,000 deeds granting ownership rights over land along the gas pipeline were issued. There were 2,000 compensation cases for land expropriation, 95% of which were fairly settled. As for the pending cases, the Government of Peru is working on improving the existing legislation.

The Office of the Ombudsman was created, as an impartial entity within the Catholic University of Peru, responding to the Government of the Peru's concern about the need to establish a conflict resolution mechanism. So far, the Ombudsman has received 680 complaints, 87% of which have already been settled.

## V

I would like to make a general comment beyond the scope of the questionnaire I was provided with.

The Committee's concern about the role of the Multilateral Development Banks in financing big infrastructure projects, particularly energy sector projects, coincides with the discussion on the financing of extractive industries that took place at the World Bank's Board of Directors' meetings for the past two years. During these discussions, in which governments, private companies, NGOs and the academic world participated, maximalist positions were adopted such as the withdrawal of multilateral organizations from the financing of these industries. Final consensus was reached on the need to continue and increase the financial support to these projects but at the same time to incorporate the highest environmental and social standards when assessing these projects.

On the other hand, there is ample empirical evidence, provided by the World Bank and the Inter-American Development Bank, showing a high correlation between investments in infrastructure and growth of the GDP. Moreover, considering the deficit in infrastructure in the Latin American region, a recent study by the World Bank<sup>3</sup> shows that if the region had increased its levels of investment in infrastructure to equal those reached in the Asian region in the last 20 years, its GDP would have gone up two percentage points on average.

In the case of the CAMISEA project, out of the total investment required for the implementation of the first phase, which went up to \$1.6 billion, the Inter-American Development Bank contributed only \$75 million for the construction of the gas pipeline. Even if the Inter-American Development Bank, at the request of some NGOs, had decided not to participate in the financing, the project would still have been carried out. At some point even the sponsors of the project considered withdrawing the request for financing due to the delay and uncertainty of the procedure. At the request of the Peruvian government, the paperwork was completed and the loan was approved. For this reason, I clearly support the engagement of the international financial institutions in infrastructure projects, particularly energy-related ones. The design and evaluation of projects, especially those on social and environmental matters, will benefit from the lessons learned by these institutions.

In sum, urgent infrastructure projects like CAMISEA will be carried out with or without the assistance of multilateral financial organizations. There are clear environmental and social advantages if organizations like the World Bank and the Inter-American Development Bank continue to expand their portfolio of infrastructure projects, particularly energy-related projects.

To conclude, I agree with the statement of Domingo Cavallo, ex Minister of Finance of Argentina, before this Committee on Energy Security: “South America’s self-sufficiency in terms of energy has been deteriorating as a result of populist policies and short-term objectives”. In this sense, CAMISEA, with its second phase about to start, represents the step in the right direction and, depending on the magnitude of the reserves to be

---

<sup>3</sup> See Marianne Fray and Mary Morrison, *Infrastructure in Latin America and The Caribbean: Recent Development and Key Challenges*, World Bank Report No. 32.640-LCR, August 2005.

discovered and exploited in Peru, will also contribute to the security of South America and, eventually, of the whole hemisphere.

Thank you very much.