INSTITUTE FOR FISCAL STUDIES

POLICY BRIEF

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ASSESSING MANAGEMENT OF GHANA NATIONAL PETROLEUM CORPORATION REVENUE

1.0 SUMMARY

Ghana National Petroleum Corporation (GNPC), the national oil company, receives close to one-third of the total petroleum revenues of Ghana, placing it at the core of the country's aspirations towards effective management of its hydrocarbon resources. This policy brief presents the findings of a study which assessed transparency and efficiency in the management of the petroleum revenue allocated to GNPC. To begin with, the legally-enshrined mechanism for allocating revenue to GNPC is transparent and has generally worked well in practice. However, GNPC's own transparency has room for improvement, since the Corporation's public disclosure of information is limited, despite its extensive reporting obligations. To improve efficiency, Parliament should rein in the quasi- fiscal and corporate social responsibility activities of GNPC, and enact a new law for the Corporation to strengthen its transparency and accountability, while reflecting the changing dynamics of the oil and gas industry. Furthermore, GNPC should eliminate recurrent losses in its downstream trading activities and be divested of its non-petroleum-related investments.

2.0 CONTEXT AND POLICY ISSUE

Since commercial hydrocarbons production began in late 2010, Ghana has passed several legislations to govern the sector and guide the management of petroleum revenues. There has also been strong public interest in the management of petroleum revenues by the government, reflecting the high expectations among Ghanaians of the benefits from the sector. At the same time, problems with transparency and efficiency in petroleum revenue management have surfaced from time to time. Studies into these problems have largely focused on petroleum revenue allocated to programs in the public budget—referred to as the Annual Budget Funding Amount (ABFA)—while the rest of the revenue, which includes the portion (approximately 31% of the total revenue in 2011-2017) allocated to Ghana National Petroleum Corporation (GNPC), the national oil company, has received less scrutiny. This policy brief presents the key findings and recommendations of a study which sought to fill this gap by assessing transparency and efficiency in the management of GNPC revenue.[1]

3.0 KEY FINDINGS ON TRANSPARENCY

The PRMA has specified a transparent mechanism for revenue allocation to GNPC that has largely been respected and worked well in practice.

To enhance budgeting and long-term planning, and to avoid politicization of the process, the funding for GNPC has been set up on earmarking basis and is taken from the carried and participating interest revenue earned by the state from petroleum operations. The earmarked transfers to the Corporation are of two types: (i) an amount meant for equity financing costs, which represent the country's share of development and production costs in each petroleum agreement; and (ii) an additional allocation, determined by the Minister of Finance and approved by Parliament, from the carried and participating interest after deducting the equity financing costs. From 2011-2017, GNPC was allocated US$1.24 billion, representing 31.1% of total petroleum revenue for the period.

GNPC has extensive reporting obligations to various authorities, which it generally complies with. However, its overall transparency is weakened by its limited and inconsistent public disclosure of information.

The GNPC Law (PNDC Law 64) and other statutes oblige the Corporation to provide wide- ranging information on its operations to various authorities, such as Ministry of Energy, Ministry of Finance, State Enterprises Commission (SEC), Parliament, etc. In general, GNPC provides the requisite information to the relevant authorities. The main problem with the Corporation's transparency, however, is that the extent of its public disclosure of information does not match the extent of its reporting to various authorities. This is largely because the Corporation, in the main, is not legally mandated to publish or publicly disclose information. The consequence is that except in those cases where the authorities to whom GNPC reports are legally obliged to publish the information, public disclosure of information by GNPC itself is, in theory, discretionary and, in practice, inconsistent. For example, whereas information on petroleum production, sales and revenue, and on petroleum projects, is reported publicly by the Ministry of Finance in accordance with law, information such as the Corporation's annual work program and budget, which is submitted to Parliament, and its performance management reports, which are submitted to SEC, is not published, since there is no legal requirement to do so. Furthermore, a key source of data on the Corporation's operations—its annual audited financial reports—is not published in a consistent and timely fashion.

GNPC spends most of its revenue on direct petroleum activities. However, a portion of the revenue is used to cover persistent downstream trading losses, a situation that detracts from efficiency.

The direct petroleum activities, comprising exploration, development and production activities, accounted for an average of 64% of total costs in 2011-2016. The remaining costs were personnel emoluments (8.8%), general operating expenses (8.7%), and other operating expenses (11%). The last-mentioned category includes losses, amounting to 9.3% of total costs in 2011-2016, incurred persistently by the Corporation from trading in refined petroleum products. This situation detracts from efficiency in the management of its revenues.

[1] *The study, which was sponsored by the UK Department for International Development (DFID) through the Ghana Oil and Gas for Inclusive Growth (GOGIG) program, assessed management of all non-ABFA petroleum revenue, viz. revenues allocated to GNPC and the Ghana Petroleum Funds (GPFs). The methodology entailed a desktop review of key sector reports, policies and legislation, as well as meetings and workshops with stakeholder organizations in petroleum revenue management in Ghana, namely: Ministry of Finance, Ghana National Petroleum Corporation (GNPC), Bank of Ghana, Petroleum Commission, Public Interest and Accountability Committee (PIAC), Ghana Revenue Authority, Mines and Energy Committee of Parliament, Finance Committee of Parliament, and relevant civil society organizations. A separate policy brief deals with the findings and recommendations on the GPFs.*

GNPC engages in activities outside its core mandate, which either do not produce commercial value for the organization or compromise efficient utilization of revenue.

GNPC's core mandate is to "undertake the exploration, development, production and disposal of petroleum." It is also permitted by law "to do any other things and perform any other functions necessary or expedient for the purpose of attaining its objects and carrying out its activities." This power given to GNPC has led it to indulge in extra, noncore activities that not only overstretch its mandate but also compromise efficient utilization of its revenue.

GNPC's noncore activities can be grouped into three: (i) non-petroleum-related investments; (ii) quasi-fiscal transactions; and (iii) corporate social responsibility expenditures.

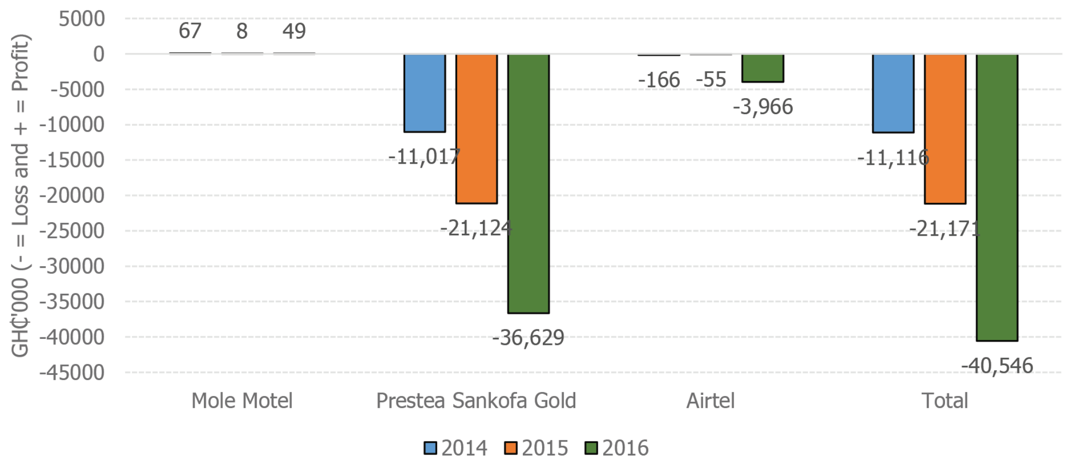
- Non-Petroleum-Related Investments

GNPC holds equity stakes in Mole Motel Company Ltd. (60%), Airtel (25% in 2016 but reduced to under 1% in 2018), and Prestea Sankofa Gold Ltd. (90%).

These investments, and others that have been already liquidated, were made before commercial oil discovery in 2007 in order to generate income to support GNPC's upstream activities then. Carrying these investments into the post-discovery era has, however, not served the Corporation's interest commercially.

This is because Airtel and Prestea are loss-making investments, and Mole Motel, though profitable, contributes nothing to the Corporation's cash flows as it pays no dividends (see Figure 1). Of particular concern is Prestea, which, despite shutting down in the last quarter of 2016 after years of financial losses and decline, continues to weigh on GNPC's finances. In 2018, for example, GNPC set aside US$24.78 million in its budget to pay off the mine's liabilities.

Figure 1: Net Profit (Loss) from Non-Petroleum Investments of GNPC



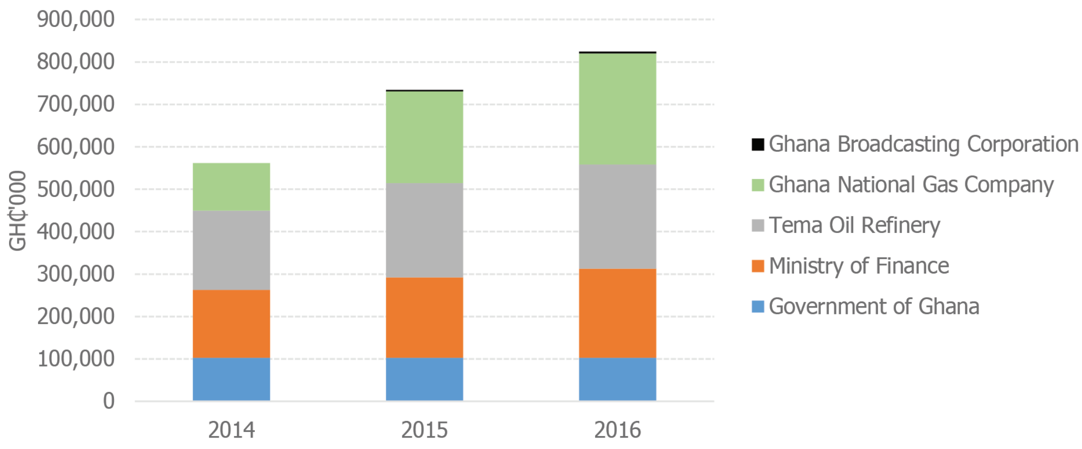
- Quasi-Fiscal Transactions

A number of transactions by GNPC border on quasi-fiscal operations and do not represent the best use of the Corporation's funds. Among these are loans and guarantees issued for the benefit of the government or other state-owned companies, and expenditure on road construction. In 2014, for example, GNPC advanced a loan of US$50 million to the Ministry of Finance, an amount equal to 28% of the Corporation's petroleum receipts for that year. The loan was not backed by a formal agreement and had not been paid as at mid-2018.

Given GNPC's relatively strong balance sheet and cash flows, and the government's disinclination to issue sovereign guarantees in support of state-owned enterprises, the Corporation has become a de facto "guarantor of last resort" in the energy sector, providing guarantees on behalf of Electricity Company of Ghana (ECG), Volta River Authority (VRA), Tema Oil Refinery (TOR), and Bulk Oil Storage and Transportation Company (BOST).

The loans and guarantees have resulted in huge and mounting claims on the beneficiaries (See Figure 2). In addition, since 2015, GNPC has spent funds on road development in the Western Corridor gas enclave to facilitate gas evacuation. Between 2015 and 2017, the Corporation spent US$39.7 million on this project, with further expenditure of US$27.6 million included in its 2018 budget.

Figure 2: Amounts Owed by Government and its Agencies to GNPC

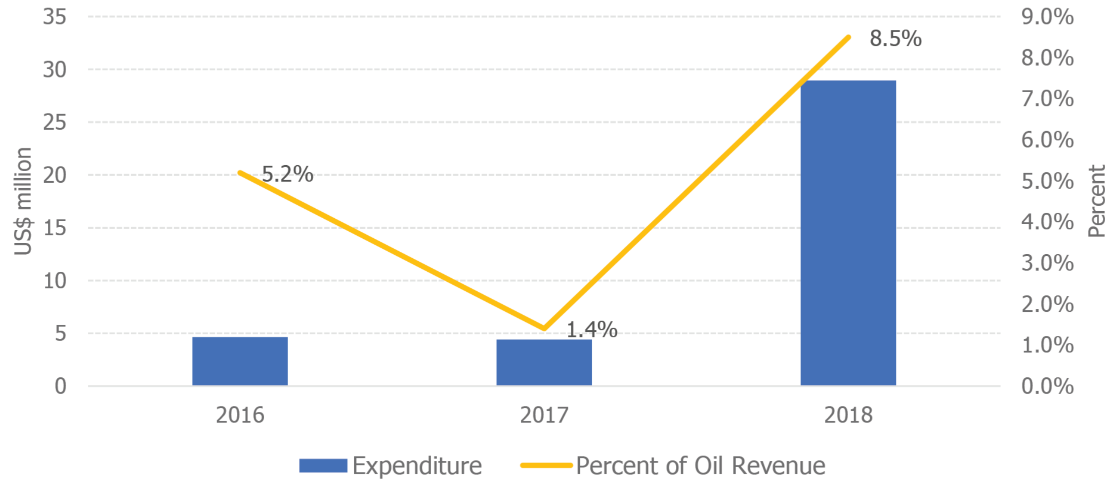


- Corporate Social Responsibility Expenditures

GNPC engages in wide-ranging CSR activities, which in 2018 were reorganized under three main focal areas, namely: Education and Training; Economic Empowerment; and Environment & Social Amenities. While it is common practice for companies, both private and government-owned, to engage in CSR as a means to benefit society and also boost their brand, CSR expenditures should be controlled to avoid diverting too much resources from a company's primary commercial mandate, which can hinder its performance and efficiency. This seems not to be the case with GNPC, as CSR has been diverting increasingly more resources away from core operations.

As Figure 3 reveals, GNPC's CSR budget spiked from US$4.4 million in 2017 or 1.4% of petroleum revenue to US$28.95 million in 2018 or 8.5% of petroleum revenue. It is worth noting that the 2018 CSR budget exceeded the personnel emoluments budget (US$25.03 million) and the general expenses budget (US$17.10 million) of the Corporation. The growing scale and cost of GNPC's CSR activities, especially since the reorganization in 2018, raises questions about the opportunity cost of such expenditure against the background of the Corporation's gaping financing needs and substantial investment requirements.

Figure 3: CSR Budget of GNPC



4.0 KEY FINDINGS ON EFFICIENCY

Parliament should enact a new statute for GNPC.

The founding law of the Corporation, PNDC Law 64 of 1983, has become redundant in many parts and also falls short of satisfying the strong and fervent public demand for transparency and accountability from a national oil company in contemporary times. A new law would offer the opportunity to revisit or incorporate the following issues, among others:

- The considerable latitude given the Corporation to engage in diverse kinds of activities may need to be curbed. Legislators should consider specifying in the new law the things the Corporation cannot do.
- Expansive public information disclosure requirements should be mandated to strengthen transparency and accountability.
- The corporate governance of the Corporation should be given a second look, in particular the powers to appoint the board and the board's composition. Thought may be given to granting Parliament a role in appointing the board and providing for some institutional representation on it.

Parliament should impose a limit on the Corporation's CSR budget

The limit could be set as a ratio of GNPC's revenue, cost or other financial metric. This will restrain the scale and cost of the CSR activities and protect revenues needed to expand investments in the oil sector.

Parliament should exercise its oversight effectively by reining in the quasi-fiscal activities of the Corporation.

Parliament should mandate GNPC to report to it specially, and in comprehensive detail, on quasi-fiscal undertakings and should demand urgent recovery of the current associated claims.

The Ministry of Energy, together with GNPC, should take a policy decision to divest the Corporation of what is remaining of its non-petroleum-related investments. In addition, GNPC should reassess its downstream business and take steps to make it profitable.

GNPC should be proactive in reporting information broadly about its operations to the public, except possibly for commercially sensitive information.

Such key information as the annual work program and budget, annual financial report, performance management report, and procurement information, among others, should be published by the Corporation in a timely and consistent fashion. Making information available to the public to the broadest possible extent will enhance transparency, accountability and public confidence in GNPC.

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