Africa Centre for Energy Policy

GNPC'S LOAN FACILITY AND PARLIAMENTARY APPROVAL

COMMENTS BY THE AFRICA CENTRE FOR ENERGY POLICY (ACEP)

14th November 2014

1.0. Introduction

Recently, there have been concerns raised by some Ghanaians about the propriety of the Ghana National Petroleum Corporation (GNPC), the national oil company (NOC), contracting a loan of US$700 million without parliamentary approval. Others have doubted GNPC's capacity to spend the loan efficiently and for the right purpose. As part of our oil governance work, ACEP has analyzed the matters involved and can state that the concerns expressed do not only border on constitutionality but also expose the character of NOCs that operate with opacity.

We have been studying GNPC for sometime now especially following the commencement of oil production from the Jubilee fields, and we are confident to express that we have seen the corporation make progress in shedding off the secrecy that characterized its past operations. However we have observed with worry that the recent case of avoiding parliamentary scrutiny in securing the loan facility for its capital programme somehow reminds us that GNPC is not far from following the path of NOCs that are poorly governed, have become cash cows for politicians, and have brought heavy financial burden on their countries.

Ghana is a democratic state and the least we could do is make GNPC a model of a modern NOC, which can combine sound commercial operations with good governance. We believe that the Government, GNPC and the good people of Ghana will support our observations and recommendations on the matters relating to the loan facility to renew our optimism for a reformed GNPC that puts our country on the path to avoiding the "curse" of oil.

2.0. GNPC Financing

The establishment of NOCs underscores the policy of countries to participate actively in their oil industries. Based on industry policy, an NOC can play multiplicity of roles including regulatory roles (Saudi Arabia and Angola) or commercial role (Nigeria, Mexico). Ghana's current policy confers on GNPC the role of a commercial operator, holding the state's interest and promoting the upstream potential of the country.

In fulfillment of these objectives, the corporation has defined its strategic focus of becoming an active player in the industry, attaining the status of an operator by 2020. The strategies for achieving these include:

i. Building institutional capacity
ii. Using cutting edge technology and Developing own technology
iii. Securing adequate capitalization and financial autonomy
iv. Reducing external administrative bottlenecks (e.g. review of Public Procurement Act)
v. Adopting good corporate governance practices that would enable the Corporation to compete over time with majors and super majors

There is no doubt that the corporation requires substantial capital base to achieve these fiat, and this requires financing options that are competitive without imposing undue burden on the country. Indeed, the law that established GNPC, PNDC Law 64, gives the corporation a portfolio of financing options including borrowing (Section 4(2)a), issuing debt securities (Section 17a) and state financing (Section 18). The mode of state financing is detailed in section 2 and 7 of the Petroleum Revenue Management Act 2011 (Act 815).

In this respect, we find nothing wrong with GNPC's resort to debt financing of its operations. The issue of contention however is whether the appropriate due process for raising capital has been followed; and whether GNPC has the absorptive capacity to properly apply such huge loans (These are addressed in the following sections).

3.0. GNPC's Justification for the Loan Facility

GNPC has justified its decision to contract the loan and assured of its spending capacity. It argued that the loan would be used to support its increasing oil and gas infrastructure investment and cash requirements from its participating and commercial interests. Like every financing facility, GNPC has given copious reasons for contracting the facility, some of which are:

i. To augment its working capital, including oil and gas trading working capital needs;
ii. To build up capital since state capitalization for its operations ends 15 years from the commencement of PRMA in 2011;
iii. To ensure lower gas price to Ghanaian consumers and for cheaper electricity; and
iv. To secure a low interest facility at 4.43% for a 5 year tenure. This is better than the 22% interest which the state would pay on the OCTP project ($493 million) or the 15% interest which the state will pay on the TEN Field Gas project (US$36 million) if the investors were to pre-finance the projects.

The facility is expected to finance a number of projects:

i. Provide guarantees for the Offshore Cape Three Points (OCTP) contractors for the off-take of natural gas from the field.
ii. Raise a bank guarantee of about $200 to US$300 million.
iii. An immediate requirement of US$105 million to pay part of natural gas price negotiated with the OCTP partners.

iv. Paying for the pipeline and receiving facility in the OCTP (Sankofa-GyeNyame field) gas development project expected to cost $493 million.
v. To pay $36 million, being 40 per cent of the pipeline cost to connect TEN gas to the Jubilee FPSO.
vi. Investing $54million to increase its stake in the Deepwater Tano Cape Three Points block in which together with Hess it had made seven discoveries.

Overall, the corporation estimates that about $15billion to $20 billion is expected to be invested within the decade to appraise and develop new discoveries as the industry is growing in size and is expected to reach $20billion by 2015 and $60billion by 2022.

We are of the view that the oil industry is capital intensive and GNPC must position itself to play its rightful role as industry leader in the same way as Petrobras of Brazil and Petronas of Malaysia. We believe that if we are to give meaning to local content, the corporation has to finance a significant proportion of this capital requirement.

However, we also strongly believe that if GNPC is to play the role of an industry leader, and able to finance these operations from such huge debts as it is seeking to do, then it is certainly jumping ahead of its strength, exposing the country to significant credit risks given the size of our reserves, and the many unsuccessful efforts from exploration.

Further, the governance risks associated with this are very high, given that GNPC continuous to have weak financial oversight, whose management decisions are influenced by Government. We cite for instance GNPC’s use of US$26.3 million on staff costs for 3 years (2011-2013) without publishing its staff strength and indeed without any major results on its exploration and development operations; the application of US$31 million of its 2013 share of petroleum revenues to pay Central Government debt to PNB Paribas for crude oil lifted for the Tema Oil Refinery (TOR) in 2009; and the accumulated unspent cash of US$141 million as at end 2013 from its share of carried and participating interests on account of delayed procurements. About US$60 million of this money was carried forward from 2012 and another US$80 million not spent in 2013 was carried forward into 2014.

This is particularly of interest because some Ghanaians think that Government is hiding behind GNPC to borrow in the face of Ghana’s negotiations with IMF, which is likely to frown on further borrowing. This perception may not be the case as GNPC has indicated already its intention to apply the loan to some capital projects. However, the corporation’s financial governance over revenues transferred to it so far leaves much to be desired.

Clearly, GNPC has demonstrated weak spending capacity, low absorptive capacity and weak financial governance. The potential for GNPC to become a slush fund such that most of the loans contracted by it would be used by central government cannot be underestimated. The example of Sonangol, the Angola’s national oil company is fresh to guide the appropriateness of heavy capitalization of GNPC without strong financial oversight. This is where Parliament’s role becomes very important. Unfortunately, GNPC posits that Parliament does not matter in this process.

Alternatively, GNPC must adopt the International Financial Regulations Standards or list on the Ghana Stock Exchange to improve on its financial governance. Providing the corporation with a blanket cheque to borrow and raise financing without parliamentary scrutiny is therefore to ask the mouse to eat the elephant, an obvious route to disaster.

Also, it smacks of double standards for the Minister of Finance to have approved the loan facility when the same Minister only a year ago justified why GNPC did not need much money. In the 2012 allocation of oil revenues to GNPC, the Minister of Finance allocated 30% of the net carried and participating share of petroleum revenues to the corporation (US$106 million) instead of 40% allocated to it in 2011 (US$75 million). Whilst the Minister argued that petroleum receipts for 2012 was higher, hence 30% of the higher receipts resulted in more revenues for GNPC, the Minister could have given the corporation the maximum of 55% if it thought that the corporation needed more money.

We know that this loan deal is not new but has just been reactivated. In 2010, GNPC started negotiating a syndicated loan of US$500 million in which the Deutsche Bank was pooling together four other Banks to secure the deal. The deal was to be collateralized against GNPC's future oil production from its share of 13.75% in Jubilee (See African Energy, Issue 199, 3rd December, 2010). GNPC thought it would have control over the carried and participating interest; but following the enactment of the Petroleum Revenue Management Act, which put restrictions on the allocation of proceeds from the participating interest to the corporation, it lost control over it. Unfortunately for GNPC, it's restricted share of proceeds from the participating interest, which now provides security for the US$700 million loan, requires parliamentary approval. Therefore, in the event that Parliament begins to tighten the approval process for GNPC's share of oil revenues, the repayment schedule for the loan will face significant risks. **The lender must take note of this**.

Further, we know that in this current transaction Trafigura, commodity trader, is leading a number of Banks to lend this loan facility to GNPC; but like the previous one, we do not know which Banks are involved. It does not make sense for a state corporation capitalized by the state to enter into a loan agreement on the blind side of the people. In view of the interest shown by Ghanaians in the loan saga and the uncertainty of whether parliamentary approval is required or not, we wish to know which Banks are involved in this current syndication.

In our opinion, whilst we agree that the corporation could not continue to fund its operation from its resources on a sustainable basis given the national consensus for increased national participation in the industry, we also insist that debt financing of its capital operations without financial oversight through parliament carries significant risks for the state. We also believe that GNPC's ambitious plan to grow into an industry leader must be tempered with caution and moderation to avoid the temptation of accumulating too many debts without operational results.

4.0. The Loan Facility and Due Process

The most controversial of all the issues raised about the loan is the appropriateness of the process used by GNPC to contract the loan. GNPC insists it followed due process and cited Section (15(2)) of GNPC Law which requires the "Corporation to borrow money only on the recommendation of the Secretary and with the approval of the Secretary responsible for Finance as to the amount, source of the loan and the term and conditions under which the loan may be effected". Thus, the corporation concluded that it did not require parliamentary approval.

In our opinion, the application of section 15 of GNPC law as justification for avoiding parliamentary approval raises two due process concerns.

In the first instance, GNPC is selectively applying the law by its insistence that it only needed an approval by the Minister which it got. For example, Section 24(1) of the same GNPC Law requires GNPC to enter into petroleum exploration and production agreements only on the approval of the Minister. This is also backed by Section 1 of the Petroleum (Exploration and Production) Law (PNDC Law 84), which prescribes that - "Any petroleum agreement entered into by the Secretary shall be deemed to be approved by the Council unless the Council within a month of the entry by the Secretary into such an agreement disallows the agreement".

However, since the coming into force of the 1992 Constitution, all petroleum agreements the corporation entered into were subject to parliamentary approval in line with Article 268(1) of the Constitution. This is because any provision in any law or statute, which is not consistent with the Constitution is null and void. Therefore any action prescribed by Section 15 of GNPC Law relating to the corporation's borrowing without parliamentary approval as prescribed by Article 181(3) must be viewed with suspicion.

Some have argued that this view of GNPC would seem to have juristic blessing by the Supreme Court in ***Felix Klomega v. Attorney-General & 3 Others***. There the Supreme Court considered whether the Ghana Ports and Harbours Authority was an entity whose international transactions required parliamentary approval (just like loan agreements) under Article 181 of the 1992 Constitution. The Supreme Court was forthright in laying the general rule that a statutory/public corporation need not procure parliamentary approval for its international transactions. In our opinion, this case can be distinguished from the circumstances surrounding the GNPC loan transaction.

We note that, unlike in the ***Felix Klomega case*** where the is issue related to the interpretation of Article 181(5) of the Constitution (dealing with international transactions other than loan agreements), the GNPC transaction is a loan transaction that, in our opinion, strictly falls within the ambit of Article 181(3) and therefore ought to have been approved by Parliament under Article 181(4)(a). In any case, if we consider that the GNPC transaction falls within Article 181(5) of the Constitution, then it must be noted that the Court in the ***Felix Klomega case*** did not lay down an absolute rule. As Date-Bah JSC (as he then was) put it:

> *"This court should, however, not lay down an absolute rule. If, on the facts of a particular case, central government were found to have made a particular statutory corporation its alter ego under the circumstances of that particular case, the possibility of holding that that statutory corporation comes within article 181(5) should not be ruled out…Whilst we do not consider that the facts of the case before us can reasonably be interpreted as falling within the notion of an agency of government constituting an alter ego for the Government, we nevertheless consider that the idea that a statutory corporation, though legally distinct from the Government, can in appropriate circumstances be held to be an alter ego of the Government is one that should serve the useful purpose of an exception to the general rule on the basis of which this case has been determined.* ***In appropriate future cases, the doctrine of alter ego could be adopted and adapted to serve the purposes of Ghanaian law, after due and rigorous review… The mischief that the [alter ego] doctrine would be helpful in suppressing is the possibility of the central Government seeking to evade Parliamentary scrutiny and approval of its qualifying agreements by getting a statutory corporation to enter into international business or economic transactions that would otherwise fall within the ambit of article 181(5)****. The alter ego doctrine has the potential for development to respond to this loophole.* ***In short, article 181(5) is to be interpreted as follows: generally, the contracts of statutory corporations are not within the ambit of the provision. However, in exceptional circumstances, through the application of a customized Ghanaian version of the doctrine of alter ego, the contracts of a Ghanaian statutory corporation could be brought within the intendment of article 181(5)****." [our emphasis]*

We endorse the above passage of Date-Bah JSC and argue that GNPC's loan transaction should be seen as the exception rather than the norm in terms of the principle established in ***Felix Klomega***.

In the second instance, borrowing to spend on unapproved projects undermines Section 7(3b) of the Petroleum Revenue Management Act. The Act mandates Parliament to approve the annual programme of GNPC every year. This implies that the corporation cannot spend or borrow to spend on projects outside the approved programme. This practice is not peculiar to Ghana. Even Brazil's Petrobras with great success at raising capital from the market, which GNPC aspires to, subject its capital programme budget to approval by the Brazilian Congress. The interesting part of this is that, Petrobras is owned 56% by the Brazilian Government and yet subject its programmes to parliamentary approval unlike GNPC, 100% owned by the Government of Ghana.

Against this background, we have not seen any approved programme by Parliament on which the projects to be financed with the loan facility are captured (See Section 3 above for the projects). Therefore, it amounts to an illegality if GNPC goes ahead to finance with a loan projects not approved by Parliament as part of its annual programme.

The GNPC in our view might not have been worried about Parliament approving the loan since the ruling party (as it has always been with all ruling parties in Ghana since 1992), could use its numbers in Parliament to secure approval for the facility. What we think the

corporation was worried about is the transparency associated with parliament debating the terms of the facility in an open environment and for citizens to follow the debate. This exposes the character of a trustee that does not want the owners of the oil resources it has been entrusted to manage, to know how it is managing the resources.

5.0. Conclusions

Based on our analysis, we make the following observations:

a. We recognize that GNPC has a strategy to grow into an industry leader and therefore requires substantial financing to achieve this. We also cannot contest that the law provides it with a portfolio of financing options including debt financing, and it is within its mandate to explore this.
b. GNPC in exercising its mandate to raising capital over-stepped constitutional and legal due processes which undermine good financial governance and expose the country to credit and governance risks.
c. GNPC's resort to only Ministerial approval of the loan facility as prescribed in GNPC law is a selective application of the law. There are other provisions in the same law which before coming into force of the 1992 Constitution required only Ministerial approval, but which are now subject to parliamentary approval in accordance with the constitution (e.g. Petroleum Agreements).
d. Spending or borrowing to spend by GNPC on projects, which do not form part of its programme approved by Parliament violates Section 7(3b) of the Petroleum Revenue Management Act. Since most of the projects to be financed by the loan are not part of the approved programmes of the corporation, disbursing the loan facility to the projects amounts to an illegality.

We therefore call on GNPC and the Government to suspend the facility until:

i. Parliament approves the projects for which the loan facility has been contracted in line with the Petroleum Revenue Management Act;
ii. Parliament approves the loan facility in accordance with constitutional processes prescribed in the 1992 Constitution;
iii. Parliament's Committee on Energy and Mines and Public Accounts develop a comprehensive programme to monitor GNPC's utilization of funds either from the state equity or debt financing.

Our opinion