



**Africa
Centre for
Energy Policy**

A Simplified Analysis

of the

Petroleum Agreement among Government of the Republic of Ghana, Ghana National Petroleum Corporation, GNPC Exploration and Production Company Limited and AGM Petroleum Ghana LTD in respect of the South Deepwater Tano Contract Area

Introduction

This simplified analysis of the Petroleum Agreement between the Government of Ghana and AGM Petroleum Ghana approved by Parliament in late 2013; is intended at providing Ghanaian citizens with relevant information on the petroleum contracts entered into by the Government. The analysis it is hoped will increase public understanding of contracts and contractual relationship between the Government and Oil companies. Petroleum Contracts are very complex to understand and are often formulated in legal and financial language which is not easily appreciated by citizens. As primary owners of Ghana's petroleum resources, this simplified analysis will deepen public accountability by increasing public participation in the debate on petroleum contracts as well as in monitoring the commitment of Government and the Oil Companies. The provisions on fiscal terms in particular will help the public predict the potential fiscal contributions from petroleum contracts and demand proper use of the resources for development.

This analysis is not an attempt to present the entire Petroleum Agreement. It is

focused on a few areas that are of public interest and mainly highlights the financial and economic commitments of the parties to the Agreement.

The Contract Area

The South Deep Water Tano Block of 3,482 km² is located in deep to ultra-deep water part of the Tano basin, with water depth ranging from 2,000m to about 3,500m. It is in close proximity to the Hess-operated Deepwater Tano – Cape Three Points block, where seven discoveries have been made, and the Vanco/Lukoil Deepwater Cape Three Points block, which has a discovery.

Ownership Rights and Control

The GNPC has a commercial participating interest of 32% in the Joint Operating Company whilst AGM holds 68%. AGM is owned by AGR (49.5%), Minexco OGG (48%) and MED Songhai (2.5%).

Fiscal Provisions

These define the fiscal benefits of the two Agreements to Ghana. In the Ghana-AGM Agreement, the fiscal terms include oil royalty of 10%, gas royalty of 5%, initial

participating interest of 10%, and additional participating interest of 15%; and corporate tax of 35%. The fiscal terms are major improvements over the pre-discovery contracts including the Jubilee Field Agreements. This is expected because the exploration risk profile of Ghana's hydrocarbon basins where oil discoveries have been made has significantly reduced, hence the justification for higher fiscal terms in post discovery contracts.

Financing of Development Costs of GNPC's Additional Participation

As already stated, the Agreement provides GNPC with the option to take additional participating interest of 15% upon commercial discovery of oil and which shall be responsible for financing the development costs relative to this interest. However, GNPC can elect to have the Contractor advance up to 50% of the total proportionate share of the development cost for financing the additional interest. However, in the event of a default, the Contractor will recover the default amount with interest.

Local Content and Local Participation

There is a local Ghanaian firm, MED Songhai, in the Ghana-AGM Agreement subsumed in the Contractor, AGM Petroleum Ghana. MED Songhai owns 2.5% in AGM Gibraltar, the parent company of AGM Petroleum Ghana which has a participating interest of 68% in the Joint Operating Company. This means that the participating interest of the local Ghanaian firm translates to 1.7% in the JOC. This falls far below the minimum equity of 5% participation for Ghanaians in a petroleum license as prescribed in the Petroleum (Local Content and Local Participation) Regulations (LI2204).

Exploration Period and Performance Bonds

The exploration period is a very important phase of oil operations and the

Government must be able to protect Ghana's interest by ensuring that exploration companies have the necessary finances to fulfil their obligations. This is why in most countries, exploration companies are expected to demonstrate their ability through performance bonds.

In the Agreement, except for the first exploration period, the Contractor is not required to post a performance bond. The only performance bond required is US\$100 million for the initial period of 3 years, less than half the minimum expenditure requirement of US\$259 million for the period. The GNPC recognizes that this is potentially problematic by providing for an additional performance bond when it realizes that the contractor is not fulfilling its obligations as expected.

Relinquishments

Relinquishments provisions are used to compel accelerated performance of exploration companies. They also prevent speculative exploration in which companies hold on to oil blocks whilst waiting for exploration results of adjacent or nearby blocks to raise the value of their blocks.

The relinquishment provision in the Agreement is more punitive than what we have seen in other contracts. The Contractor relinquishes 30% of the original size of the acreage at the beginning of the first extension if it elects to go into the first extension period and at the beginning of the second extension period, the contractor shall hold not more than 45% of the original block.

Approval of budgets

Provisions have been made for the constitution of a Joint Management Committee (JMC) with responsibility to review and approve budgets and other decisions during exploration, development and production phases. In this respect, the Agreement provides that where the

contractor makes expenditure, outlays or advances for which Contractor will be required to make on a 100% basis, it shall require the approval of the Contractor's representative only. This is dangerous as costs approved by the Contractor only could provide room for cost inflation usually through transfer pricing or through hidden costs. Thus the Agreement has loose ends on budget control which must be reviewed.

Amendments of Work Program or Budget

As is required in most contracts, variations may occur in the work program or budget. To accommodate this, the Agreement requires that any amendment to any work program or budget shall be submitted to the JMC for review and approval provided that the amendment leads to increase in excess of 5% of the total budget of a line item or of the total budget of the project. In this case, the increase is said to be of material significance. However, in this industry an increase of less than 5% in repeated amendments could amount to more than the prescribed material significance in the contract budget. This is another loose end on budget control which should not be allowed in the contract.

Other Important Provisions

1. Introduction of capital gains tax (Article 12.1b). This is the first time Ghana is applying capital gain tax in a petroleum contract largely due to the fact that the Petroleum Income Tax Law (PNDC Law 188), the industry specific law, does not sanction it. This is however consistent with the Internal Revenue Act 2000 (Act 592) in Section 95(1).
2. Conditions under which confidential data can be disclosed include the need for Government agencies to have access to this data for the purpose of issuing relevant permits and authorizations (Article

16.5). This allows the Petroleum Commission to access confidential data and can facilitate the fulfillment of Section 3k of Act 821 which mandates the Commission to issue annual report on all petroleum resources and activities.

3. The cost of cleaning pollution or repairing damage as a resulting from petroleum operations shall be declared as petroleum cost unless it is done by negligence or willful misconduct by contractor or affiliates or subcontractor (Article 17.5). This is problematic as Ghana is associated with low level of regulatory capacity which may make it difficult to prove the claim of negligence on the part of the contractor.
4. Stabilization clause in previous contracts has been removed. In the event that any new law or regulations which affect the original terms and conditions of the agreement and which has a material adverse effect on the rights, obligations and benefits arising from the economic, fiscal and financial provisions, any party to the agreement may request to negotiate possible modifications to restore the economic equilibrium (Article 26).

Some Key Conclusions

1. The Ghana-AGM Agreements has significant improvements over previous Agreements signed before the discovery of oil in the Jubilee Fields. This was expected considering that the commercial discovery and production of oil reduced the risk profile of most of Ghana's hydrocarbon basins.
2. The Agreement presents Ghana with improved fiscal benefits, more ownership control, more local participation and other

contributions in financial advances to the GNPC that could improve on the capacity of the GNPC to improve on its strategic development and position itself as future Operator.

3. The Agreement is potentially more risky as a result of its non-comprehensive financial cover and the significant exposure to risks associated with the dispute between Ghana and Ivory Coast over the western part of the contract area.
4. The Agreement appears more flexible because it has several loose ends in the contract particularly in the areas of budget control and financial requirement for work obligations; which provides room for potential abuse of Ghana's interest.

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