REVIEW OF THE PETROLEUM REVENUE MANAGEMENT ACT 2011 (ACT 815)

PROPOSALS PRESENTED TO THE MINISTRY OF FINANCE AND ECONOMIC PLANNING BY THE AFRICA CENTRE FOR ENERGY POLICY (ACEP), THE CENTRE FOR PUBLIC INTEREST LAW (CEPIL) AND FRIENDS OF THE NATION (FoN)

INTRODUCTION

The Petroleum Revenue Management Act 2011 (Act 815) was passed by Parliament in March 2011. The law was described by stakeholders as most progressive and provided a transparent framework for managing Ghana's petroleum revenues. However, like many new laws, the implementation of the law has brought to the fore some challenges which must be addressed to ensure the smooth application of the progressive provisions in the law. The Government of Ghana recently announced its decision to review the law and invited proposals from Ghanaians for consideration. This paper contains proposals from Civil Society Organizations. The proposals cover the fiscal framework, financing of GNPC, the Annual Budget Funding Amount, transparency and accountability among others.

1.0. THE FISCAL FRAMEWORK FOR PETROLEUM REVENUES

The current fiscal framework connects transfers to the GNPC, the benchmark revenue, the ABFA and the GPFs. The application of this framework over the last three years has however become problematic for some reasons.

1.1. The Fiscal Framework

In the last three years, both the PIAC and Civil Society Organizations observed the problems associated with revenue forecasting and its potential to undermine the counter-cyclical objective of the fiscal framework for managing revenue inflow and outflow. As a result of Government's inability to meet its targets for oil receipts, transfers to the ABFA and the Ghana Petroleum Funds (GPFs), have been adversely affected. This has been blamed on over-estimation of oil revenues. It is also due to the fact that the fiscal framework is revenue based rather than price based. For instance, the law provides that transfers to the Ghana Petroleum Funds are possible only when quarterly collections of

revenues exceed the ABFA by one quarter (Section 11(2) and Section 23). Thus, in periods of over-estimation when the ABFA is not fully realized, there will not be transfers to the GPFs. This places more attention on spending at the expense of savings. This circumstance also creates room for Government to deplete the Stabilization Fund.

The law also provides the Minister of Finance the power to determine ceiling on the Ghana Stabilization Fund (Section 23(3)) but does not provide guidelines for determining the ceiling. This is too discretionary as Parliament is unlikely to disapprove the ceiling determined by the Minister. The law also allows the Minister to transfer any excess over the ceiling to the Contingency Fund or used for debt payments (Section 23(4)). But since the PRMA does not govern the spending of the Contingency Fund, discretionary spending of the Fund could lead to non-prudential management of the revenues. For instance, since the PRMA does not govern the utilization of the funds in the Contingency Fund, and by extension the areas in which funds in the contingency fund will be spent on, it will be difficult to hold the Minister responsible if the Minister decides to spend that money outside the priority areas defined in the Act. Where there are no tight regulations for the determination of the maximum ceiling of the Stabilization Fund, the Minister may unduly swell the size of this seemingly discretionary fund.

Equally the Act has failed to state the type of debt that Parliament should approve for the revenues in excess of the maximum determined by the Minister will be used for repayment. Thus it will not be out of place if the Minister uses the excess revenue to pay debts unrelated to the priority areas under PRMA.

On the part of the Ghana Heritage Fund, the law provides that Government can relax the restrictions on the Fund after 15 years and allow for the spending of the accumulated interest based on approval by simple parliamentary majority. This also puts the growth of the Heritage Fund in danger.

Recommendations

a. Independent projections could address the fear of over estimation of petroleum receipts

The suspicion that Government could deliberately over-estimate crude oil prices and the Benchmark Revenue and fall on the Stabilization Fund when revenue targets are not met can be resolved if the projections are made by an independent Committee as already recommended for the independent certification of the Benchmark Revenue.

b. Transfers to the Budget should not compromise savings and future fiscal sustainability

Savings and future financial sustainability should not be compromised by current spending. In this case, the percentage allocation to the ABFA and Ghana Petroleum Funds should be consistent with the principle of reserving some of the petroleum revenues at all times. Thus, a fixed percentage (say 70%) of actual receipts of the Benchmark Revenue should be transferred as ABFA and the balance of 30% to the Ghana Petroleum Funds.

c. Ceiling on the Ghana Stabilization Fund should be benchmarked to an important economic indicator rather than a subjective discretionary process

The method for transferring revenues to the Ghana Petroleum Funds should be revised to ensure that the Stabilization Fund has sufficient balance to ensure that it is significantly liquid to cushion the effects of revenue shortfalls. In this case, sufficient balance (ceiling) in the Ghana Stabilization Fund should be based on an economic benchmark (say 10% or 15% of the Government annual budget starting from the current budget). This makes more economic sense than the more subjective discretionary process provided in the law. Consequently, there should be guidelines on the determination of the ceiling on the Stabilization Fund.

After reaching the statutory ceiling of the Stabilization Fund, all excess revenues due the Stabilization Fund should be transferred to the Ghana Heritage Fund rather than being

transferred to the Contingency Fund or used for debt repayment. Thus, the provision for Contingency Fund and debt repayments should be removed from the law.

d. Conditions for lifting restrictions on the Ghana Heritage Fund to allow for the spending of the interest should take account of the need to grow the Fund

Also, to ensure the growth of the Heritage Fund without undermining Government's fiscal plans, the provision that allows the restrictions on the Fund to be lifted should be re-examined. It is important to base the condition for relaxing the restrictions on the Fund on a certain financial balance (say 40% of Government Budget) rather than on number of years (15 years as specified in the PRMA). This ensures that the Fund can grow to serve the intergenerational equity objective it has been set up for (Section 10(2)a).

Where there is an urgent need to spend part of the money in the Ghana Heritage Fund, the use of simple majority in lifting the restrictions on the use of the Fund as provided in the law, only describes a process but does not provide the basis of the urgency of lifting the restriction (the uses to which the revenues will put). To address this, the law should be revised to include the following conditions before the restrictions on the Fund can be lifted

(i) The withdrawal does not exceed 5% of the balance standing in the Ghana Heritage Fund,

(ii) The investment to be made should be one that can benefit future generations and must be approved by Parliament; and

(iii) Such withdrawal should not be repeated more than once over a 5 year period.

2.0. GNPC FINANCING FROM PETROLEUM REVENUES

2.1. Conflicting Provisions on Transfers to the GNPC

In the current regime, the mechanism for determining the amount transferable to the GNPC is somehow conflicting. In section 2(2), all petroleum revenues are expected to be deposited in the Petroleum Holding Fund before any transfers are made in accordance with the provisions of the law. Thus, the amount transferable to the GNPC is made from the Petroleum Holding Fund. Contrary to this, section 7(2) provides that payment into the

Petroleum Holding Fund shall be net of the equity financing cost, advances and interest on the carried and participating interests of the Republic; and the cash or the equivalent barrels of oil that shall be ceded to the national oil company. So far Government has applied the mechanism in Section 2(2).

Recommendation

The law must provide one mechanism for financing the GNPC's equity cost and investment obligations. The common practice in emerging oil producing countries including the most recent example in South Sudan is that, all petroleum revenues must be brought under the microscope of the budget process. This favours the provisions in Section 7(2) of the PRMA.

2.2. GNPC's Control over Cash Flow

The most important contention on GNPC financing is the extent of control the GNPC should be given over its share of revenues and how long the corporation should be capitalized. There have been proposals for the GNPC to raise its own capital and become a full commercial operator. However, this depends largely on the level of control the corporation should be given on its cash flow.

Clearly section 7(2) gives the corporation more control over its cash flows, but this provision has not been applied so far. Allowing GNPC to receive its share before the revenues are deposited in the Petroleum Holding is consistent with the Petroleum Law of Sierra Leone and Liberia, which allow its National Oil Company to collect all petroleum revenues due the state and retain not more than 25% before transferring the rest to the treasury. However, in this situation, the process could be abused where there is weak accountability and where the national oil company could manipulate its cost to justify retention of the statutory 25% of revenues.

It is also important to state that where the Central Government has control over the finances of the National Oil Company through the budgetary process, the Minister of Finance could apply the funds to other urgent development budget. The long and bureaucratic budgetary process could also delay the National Oil Company from meeting its obligations in a joint operating agreement which could attract interest charges.

Recommendations

To address the potential effects of the budgetary process on the financial obligation of the National Oil Company and to insulate its finances from the control of the Minister of Finance, the following proposals should be examined.

a. The law should specify a fixed time within which the corporation should receive its share of revenues once deposited into the Petroleum Holding Fund.
b. The law should also prohibit the possibility of the Minster applying the corporations share to uses other than for the operations of the corporation. This could be reassuring to GNPC's investing partners that it will not default in its financial obligations.

2.3. How much to Allocate to GNPC

There have been arguments that the GNPC has been receiving more oil revenues at the expense of the Government budget. This has influenced the allocation to the corporation by Government, declining from 40% to 30% in the 2014 Budget Statement.

However, the law recognizes that the GNPC has obligations in respect of its equity in joint operating agreements; and the need for new investments. In the current regime, the period of capitalization of the corporation is 15 years from the commencement of the law (Section 7(3)). This requires that not more than 55% of the net carried and participating interest should be allocated to the corporation. In the last three years, Government allocated 40% annually to the corporation.

There are two important questions here:

i. How much is appropriate to capitalize the corporation without having a toll on the Government development budget.
ii. What duration is appropriate for the capitalization of the corporation before allowing it to operate on its own.

Recommendations

The recommendation in this case must recognize that there are trade-offs between transfers to GNPC and ABFA. As a fiscally constrained country, it is to decide as a policy whether to maximize current spending or future spending in the Budget. Two proposals are made here.

a. Allocate the current 30% of net carried and participating interests to the corporation and maintain a capitalization period of 15 years as provided for in the law.
b. Allocate up to the maximum 55% of the net carried and participating interests to the corporation and reduce the period of capitalization to 5 years. This will build the GNPCs financial base quickly and allow it to leverage on this to raise its own capital. It will also allow more revenues to be released for maximizing Government's development budget earlier than the 15 years provided for in the law. This is preferable.

3.0. THE ANNUAL BUDGET FUNDING AMOUNT

3.1. Collateralization of the ABFA

The law allows the collateralization of the ABFA and specifies a limit on the tenure of collateralization, 10 years from the commencement of the law (Section 18(7)). However, the law does not provide limit on how much can be borrowed against the ABFA. This could provide room for accumulating the size of debts that could overlap the horizon of oil production within the allowable 10 years and undermines fiscal sustainability. This also promotes mismanagement of revenues in an economy associated with low absorptive capacity.

Recommendation

Collateralization of the ABFA should be prohibited. If it is not possible, then a rule limiting the amount that can be borrowed against it should be introduced into the law. For instance,

the size of debts collateralized against the ABFA should not exceed the estimated size of ABFA accumulated over 5 years.

3.2. Priority Areas for spending the ABFA

In section 21(3), the law outlines some 12 areas where the ABFA can be spent in the absence of a long-term national development plan. These are:

i. Agriculture and industry;
ii. Physical infrastructure and service delivery in education, science and technology;
iii. Potable water delivery and sanitation;
iv. Infrastructure development in telecommunication, road, rail and port;
v. Physical infrastructure and service delivery in health;
vi. Housing delivery;
vii. Environmental protection, sustainable utilization and protection of natural resources;
viii. Rural development;
ix. Developing alternative energy sources;
x. Strengthening of institutions of government concerned with governance and the maintenance of law and order;
xi. Public safety and security; and
xii. Provision of social welfare and the protection of the physically handicapped and disadvantaged citizens.

However, in order to maximize benefits, Section 21(5) of Act 815 requires that the Minister of Finance prioritizes not more than four sectors for spending the ABFA.

Whilst it is impracticable to apply the ABFA to all the 12 areas listed above as the law itself recognizes, it is equally not realistic to maximize benefits from prioritizing four areas considering the size of revenues that are being disbursed. Government has also not complied with the proposal to develop a long-term national development plan, a necessary

condition for spending petroleum revenues (Section 18(2)). The issues in contention therefore are as follows:

a. Whether we still need Section 21(3) with 12 areas where the ABFA can be spent.
b. Whether we still need to prioritize not more than four (4) areas subject to review every three years or reduce the priorities to two (2).
c. Whether we should limit the priority areas to two by law and subject to review every 15 years to ensure maximum effect.

Also, the allocation of the ABFA to capitalize the Ghana Gas Company as well as finance gas infrastructure must be regularized. Although the areas for the spending of the ABFA are not limited to the 12 areas prescribed in the law, it is safe to suggest that those specified are the prioritized areas according to the law. However, just as the dividend policy of the National Oil Company is provided for in the law (Section 7), that of the Ghana Gas Company should equally be provided for.

Recommendations

a. The ABFA spending portfolio should be reduced to two priority areas preferably agriculture (crops, livestock and fisheries) and education.

Following the experiences of other resource rich countries, Ghana's law appeared too ambitious in spite of the modest levels of oil production. Countries like Brazil, Botswana, Indonesia, Malaysia and Trinidad and Tobago limited the areas where their resource revenues are invested to either one area or two areas; or one dominant area and two other areas. It must be stated however that whilst all sectors of the economy are important, the level of development of a country dictates the sectors that need more attention given additional non-renewable fiscal relief. Experience in these resource rich countries where prioritization are mainly targeted to areas that have quick multiplier effect on the economy has shown that resource revenues can provide the catalyst for poverty reduction.

b. To ensure efficient spending of oil revenues, there should also be a requirement for a Public Investment Management Plan as a condition for disbursing petroleum revenues.

The law requires that allocation of the ABFA should be guided by a Medium–term Development Plan. However, such plans are only indicative and do not guarantee that the best standards of public investment management are adhered to. Issues such as poor procurement practices overrun times and overrun costs, project management issues such as project selection and value for money considerations; are not addressed by Development Plans. It is therefore important for the law to require an Investment Management Plan which must be published as pre-requisite for disbursing the ABFA to prioritized projects. This will ensure efficiency of spending.

4.0. TRANSPARENCY PROVISIONS

4.1. Confidentiality of Information

The general transparency section of the PRMA (Section 49) exhibits an interesting inconsistency. Subsection 1 sets the lofty requirement that "management of petroleum revenue and savings shall always be carried out with the highest internationally accepted standards of transparency and good governance." This provision is directly undercut by subsection (3), which grants the Minister authority to withhold any information or data that, in his discretion, could "prejudice significantly" the performance of the Funds. Instead of creating a presumption in support of information disclosure, the law errs on the side of secrecy and protecting political or business interests.

Although this broad discretion is somewhat mitigated by the requirement that the Minister prepares a written explanation any time he declares information to be confidential, this explanation does not have to be released to the public, nor is it subject to judicial review. In fact, it appears that the explanation itself may be kept confidential until three years after the decision is made (Section 49(6)).

Recommendations

a. In other to ensure broader transparency in the management of the oil and gas revenues, the power of the Minister to withhold information from the public should be removed.
b. In the alternative the law should give specific examples of acts that could "prejudice significantly" the performance of the fund.
c. The reasons given by the Minister for withholding any information or data as confidential should not also be held as confidential but should be available to the public.

4.2. The Investment Advisory Committee (IAC)

As with any large asset portfolio, investment management is very important to preserve and maintain value. The Act places primary responsibility for investment strategy or management on the Minister (Section 25). Although the Act establishes an Investment Advisory Committee (Sections 29, 30), its guidance is, unfortunately, not binding on the Minister. Furthermore, the Minister is responsible for nominating members of the Committee and also determining the allowance to be paid to members of the committee. There is the possibility the Minister could exert improper influence over Committee members. Also, the conflict of interest provisions applicable to the Committee members are very inadequate.

Section 38 also permits the Minister to "take an urgent investment" or make an "overall management decision" in consultation with the Governor if the Investment Advisory Committee cannot provide advice to the Minister within 10 working days or the Minister may request the Committee to act within an even shorter time frame (Section 38(1) (2)). There are no provisions defining "urgent" or limiting the circumstances under which the Minister can invoke this procedure. The Minister is essentially free to make "urgent" decisions when he wishes. Although the Committee must be informed within 48 hours if the Minister acts without the Committee's advice, the damage from a poor or risky investment decision would already be done.

Recommendations

a. The Act should make the advice of Investment Advisory Committee if taken by majority of the members as is the case with Public Interest Accountability Committee be bidding on the Minister.
b. The circumstances under which the Minister may make investment decisions without the committee's advice should be restricted and clearly specified.
c. Also what should constitute an "urgent" investment decision must also be clearly defined in the Act.

4.3. The Public Interest Accountability Committee (PIAC)

There appear to be some serious weaknesses in the Act's provisions related to the Public Interest and Accountability Committee that will undermine its ability to monitor and serve as an independent watchdog over the Petroleum Funds. Ideally, this Committee should serve as an important link between Petroleum Fund managers and the public, providing independent assurance that the funds are being managed properly. As the law is currently written, however, the Committee's authority and responsibilities are not well-defined. At best, the role of the Committee can be described as "advisory to Parliament and the Executive" which is contrary to what the Ghanaian public demanded. Since its establishment, its advisory role to Parliament has been weakened by Parliament's inability to assign a Committee that considers the PIAC's reports. Parliament has also not debated all the reports of the Committee.

Furthermore, the Committee does not appear to have any authority to investigate issues on its own initiative or request or compel the production of information from government agencies, companies, or individuals involved with petroleum development or petroleum revenue management, or to convene appropriate experts to assist with the Committee's duties.

The most significant threat to the integrity of the Committee is the fact that members are appointed by the Minister (Section 54(2)). The Minister is responsible for overseeing and administering the Petroleum Funds and, yet, to appoint the "independent" Committee that

is charged with the responsibility for ensuring that the Funds are being managed prudently and in accordance with the law and also to determine the compensation of the Committee members.

The most serious weakness of the provision on PIAC is on funding its operations. The law imposes heavy financial burden on PIAC by providing it with very important responsibilities. The Committee is required to; consult widely with citizens (Section 53(1)), have its own Secretariat (Section 53(2)), publish semi-annual and annual reports in the news papers (Section 56a), publish its reports on its website (Section 56b); hold public meetings twice a year (Section 56c) and submits its reports to the President and Parliament (Section 56d). However, apart from allowances of Members of the Committee provided for in the law (Section 57), there is no provision on how the Committee funds its operations outlined above.

Recommendations

a. The law should provide for a dedicated source of funding for PIAC in the Act. This should be one of the exceptional payments that could be made from the Petroleum Holding Fund.
b. The Minister should not be responsible for determining the allowances paid to members of PIAC.
c. PIAC should be empowered to investigate issues on its' own including the power to compel information provisioning and calling official to answer queries.
d. Specify public reporting requirement to the public, parliament or executive.

4.4. Conflict of Interest

The conflict of interest provisions throughout the law are very inadequate and inconsistent. Members of the Public Interest and Accountability Committee are not required to disclose or declare conflicts. Similarly, the Minister of Finance, key officials at the Bank of Ghana (responsible for day-to-day operations of the Funds), as well as staff working in public

agencies directly involved in the management of oil revenues are not covered by conflict of interest rules.[1]

In the one area of the Act where conflicts of interest are addressed, with regard to members of the Investment Advisory Committee, the language is very inadequate and incomplete (Section 34). The conflict restrictions apply only if a Committee member "has an interest" in a matter under consideration by the Committee. As the restrictions are currently written, the scope of coverage does not extend to Committee members' families or business associates. Thus, a Committee member would be free to deliberate and make decisions on a matter that could directly benefit a family member or other associate. And, although a Committee member with a conflict is barred from deliberations by Section 34(1)(b), it appears that he or she would not be barred from voting on a matter that is the source of the conflict.

Recommendations

a. The conflict of interest rules should be made to cover the Minister of Finance, key officials at the Bank of Ghana (responsible for day-to-day operations of the Funds), as well as staff working in public agencies directly involved in the management of oil revenues.
b. The conflict of interests' provisions must be strengthened to include indirect interests.
c. It should be specifically stated in the Act that any Committee member with a potential, perceived, or actual conflict of interest should not participate in the deliberations and voting on the matter.
d. Thus PIAC & IAC should be encouraged to develop rules and procedures including rules dealing with direct and indirect conflict of interests.

[1] For an example of conflict of interest regulations pertaining to employees of the U.S. government who oversee mining, oil, and gas activities, see 43 C.F.R. § 3501.104 (available at http://edocket.access.gpo.gov/cfr_2010/janqtr/5cfr3501.104.htm).

5.0. PROJECTION OF PETROLEUM REVENUES

5.1. Reference Crude Oil Price

Petroleum receipts are based on a seven year moving average of crude oil prices (First Schedule, Section 1). However, the law does not provide the reference crude oil whose price is being projected. In the last three years, the seven year moving average formula based on jubilee oil prices could not be applied because oil production is barely three years. Government has also not indicated whether in its place, an alternative crude oil price (say Brent Price) was applied.

Recommendation

The law should provide for a reference crude oil in the choice of crude oil prices for projections – whether jubilee crude oil or Brent crude oil benchmark. It is also possible to apply both prices whichever is higher after the projections. This could also be done through regulations.

5.2. Certification of the Benchmark Revenue

The law requires an independent certifier appointed by the Minister of Finance in accordance with the Public Procurement Act to certify the benchmark revenue estimated by the Minister (First Schedule, Section 11). The essence of this provision is to provide an environment that eliminates bias in the estimation process. However, this is still problematic as procurements can be influenced especially in this era of sole sourcing. Further, the terms of reference for the independent certifier is not provided in the law which lends itself to potential bias in the certification process.

Recommendation

There should be an independent Committee to undertake crude oil price projections rather than in the current regime where the Minister does the projections and endorsed by his appointed certifier. This provides credibility to the process. However, as a result of implications for costs and maintaining a new bureaucracy, the mandate of the PIAC should be expanded to include crude oil price projections for use in determining expected

petroleum receipts. The use of an independent Committee to perform price projections is working well in Chile.

6.0. VALUATION OF OIL IN KIND

The law requires that where Ghana receives petroleum in lieu of cash, valuation of the receipts in the Petroleum Holding Fund should be based on the crude oil price of the date of lifting of oil (Section 4). Also, whilst crude oil lifting by Ghana and sale of the oil lifted may not occur on the same date, there will be differential reporting prices. Moreover, the actual cash receipts in respect of any petroleum lifted is required to be credited to the Petroleum Holding Fund within sixty (60 days) from the date of receipts of petroleum, which creates a lag period during which oil price conditions could change where a sales transaction has not occurred. Worse still, where Ghana hedges its crude oil ahead of lifting, the hedge price will likely differ from the price on the date of lifting. These all create valuation problem when the ultimate sales price differs from the price of the lifting date.

Recommendation

The valuation should be based on the ultimate sales price, but there should be a mechanism for accounting for the volume of crude oil from production, date of lifting and sales point.

7.0. EXCEPTIONAL EXPENDITURES

Section 24 provides for transfers from the Petroleum Holding Fund (PHF) for exceptional purposes including paying compensation to communities who are adversely affected by petroleum operations (Section 24(3)).

It is not clear why PHF is to be used to compensate communities adversely affected by petroleum operations arising from a negligent conduct of an oil company. It is also not clear if the government is going to impose fines on companies whose negligent activities adversely affect communities which fines will be paid into the PHF and used to pay compensation to such communities. The new Petroleum (Exploration and Production) Bill applies exclusive liability principle on oil companies when they cause any problems that require compensation. In this case, the provision in Section 24(3) may not be necessary.

However, where compensation shall be justified at the expense of the State, it will be appropriate for using revenues from the Petroleum Holding Fund. But since such occurrences that may warrant compensation are unpredictable, Government neither plans nor budget for them under the current regime.

Recommendation

Government should set up a separate Fund as Compensation Fund and allocates part of the PHF to it annually. The Fund will be used to address issues of compensation including an insurance against the loss of economic livelihoods of communities directly (or indirectly) affected by oil and gas activities.