ACEP’s COMMENTS ON THE OCTP GAS UTILIZATION CHALLENGES
16th January, 2019

Background

In 2015 the government of Ghana approved the Plan of Development of the Offshore Cape Three Point (OCTP) Oil field. At the time, the country faced power challenges and unreliable supply of gas from Nigeria. The proposed seven billion Dollars ($7bn) OCTP investment had clear objective; to promote energy self-sufficiency, that is also clean, for Ghana’s sustained economic growth through the supply of natural gas. This objective was pursued by the government of Ghana even if it meant paying more for the gas. The World Bank provided an unprecedented $700-million security package, the largest ever by the Bank to Ghana, to guarantee the project and, by extension, the attainment of the objective. The World Bank, at the project initiation, indicated that the power sector was the primary market for the commodity and the justification for financing the project. Ostensibly, a robust plan and action to utilize the 171 mmscf of gas per day to generate 1000 MW of power was not negotiable to douse the risk of non-utilization of the gas that bore a monthly $52.9 million take or pay tag.[1] In other words, government’s responsibility to pay $52.9 million every month, whether or not gas is utilized, was the incentive to nudge the government into action.

The issue

Unfortunately, Ghana is unable to consume all the 171mmscf of gas per day as planned. This is a manifestation of defective dutiful commitment to project, and confirms that Ghana failed to plan adequately for the commissioning of the gas. Misplaced gas infrastructure investment priorities and political excuses constitute the fundamental causes of the issue at hand.

In-between the time of approving the Plan of Development (PoD) in 2015 and July 2018 the OCTP partners raised $7billion to finance the project and developed the required infrastructure including the ginormous FPSO John Agyekum Kuffour and onshore receiving facilities. The Government of Ghana (the risk bearer), on the other hand, needed to align planned investments in power generation systems to be ready for the first gas from the OCTP project. Surprisingly, significant power generation additions were located in the Eastern power enclave while the gas was expected in the West. This therefore required remediation infrastructure to send the gas to

[1] At the original price of $9.8 per MMBtu

the East. The existing West Africa Gas Pipeline (WAGP) provided opportunity to reverse gas from the West to East. However, it took four years for government to negotiate the tolling fee.
The required interconnection pipeline, initiated under the NDC government, has also delayed beyond the scheduled first gas. Government is now promising that the interconnection will be completed by the end of January, 2019.

In recent times the Ghanaian public has been subjected to the political debate about which political party is responsible for the inability of the country to put in place the required infrastructure to consume the OCTP gas. The truth is, neither the NDC nor the NPP can be absorbed from the fiscal threat the country is beginning to endure from the OCTP project. It is true that the NDC could have located all the emergency power plants close to the OCTP onshore receiving facility to allow consumption to coincide with the first gas from the project. It is also true that one and a half years of the NPP in office was enough to have at least relocated the Karpower barge to the western region and completed the WAGP interconnection.

Effects

1. **Government's current financial liability under the take or pay agreement**

The total production volume that underpinned the project is 180mmscf of gas per day. Out of the expected production volume, the Gas Sales Agreement (GSA) recognized a downtime of 5% and put the take or pay commitment at 171mmscf per day. After a successful renegotiation by government to bring the gas price down from $9.8/MMBtu to $7.89/MMBtu, government's take or pay liability translated to about $42.6 million every month in revenue. Lower gas price was achieved through expenditure of cost saving on the project to optimize oil production.

It is important to note that the VRA consumes 60mmscf of the contracted gas quantity per day but is unable to pay for what it consumes ($14.9 million/month). Due to challenges with infrastructure, the power sector is unable to consume the remaining 111mmscf/d of the gas. In order to avoid paying the entire $42.6 million every month under the take or pay agreement, the government of Ghana has deferred its 5% royalty and GNPC's 20% share of production. This reduces government's financial burden by about $10.3 million each month. Thus, per the current arrangement, the Government of Ghana, through GNPC, has to pay the private contractors $32.3 million every month, including VRA's incurred debts for gas consumed.

If VRA is able to redeem the cost of the 60mmscf/d it consumes, GNPC will have to pay a difference of $17.3 million a month. However, indications are that GNPC will have to pay the full value of 32.3 in the meantime, until the power sector begins to assume the cost of gas consumed.

Table 1: Summarized breakdown of gas volumes and associated monetary value

	Volume breakdown (mmscf/day)	Volume breakdown (MMBtu/day)	$ revenue/month at $7.89/MMBtu/month)
Total volume	180	187,200	
5% downtime volume	9	9,360	
Take or pay Volume	171	177,840	42,655,991.04
5% Royalty	9	9,360	2,245,052.16
Partners' volume (less royalty)	162	168,480	40,410,938.88
GNPC's Share of Partners' volume	32.4	33,696	8,082,187.78
Private Contractors' Share of Partners' volume	129.6	134,784	32,328,751.10
Less volume supplied to VRA	60	62,400	14,967,014.4
Un-utilized gas (53% of Contractors' share)	69.6	72,384	17,361,726.7

Source: ACEP, 2019

2. Drawings from the Escrow Reserve Holding Account and Ghana's eminent reputational damage

The $7.7bn OCTP Project came with certain guaranteed payment securities to ensure that the Sankofa Partners are able recoup their investments. The first tier of these payment securities is a designated gas sales account to be drawn by the partners. In a situation where the receipts of the gas sales are inadequate, the partners will draw their payments from an Escrow Reserve Holding Account (ERHA), a buffer account which is supposed to contain 4.5 months of estimated gas revenue of $191.95 million. The GNPC could only provide $100 million into the escrow.

ACEP is reliably informed that the $100 million security package provided for in the ERHA has been encumbered already by the private parties. That the partners have had to draw from the escrow account is an indication that in addition to VRA not paying monies into the designated account for the gas it consumes, the government has also defaulted in paying for the gas under the take or pay agreement ever since gas production was commissioned.

If the escrow is not replenished in time, other guarantees will be the next target. The partners will be forced to draw down on the World Bank Guaranteed Letter of Credit of $500m financed

by HSBC and Standard Charted Bank, of which Ghana National Gas Corporation (GNPC) has 12 months to pay. This means GNPC shall incur more debt, and failure to pay within the stipulated time will result in accumulation of debts and interests payable by the nation.

If the World Bank guarantee is attacked, the reputation of the country will be impacted negatively on the international financial market. The Ghanaian public deserves firm commitment and communication of strategy by government to ensure that the forgoing situation can be remedied immediately. The strongest signal yet must go to the power sector that the era of free gas is over.

3. **Gas revenue losses to the State**

It is important to clarify that the monetary value of the currently deferred 111 mmscf of gas per day is approximately $28 million per month. According to the Ministry of Energy, paying for gas that is not consumed does not constitute loss to the state. This is because once capacity to off-take the gas becomes available, the Sankofa partners will supply the unutilized gas which has already been paid for. This creates an assumption that Ghana has the comfort to pay for gas in situ and to defer revenue of $28 million a month. Though the deferred gas will be produced for Ghana in the future, this is subject to future availability of the FPSO to produce more than the optimal take or pay volume and existence of infrastructure to consume more than the 171mmscf per day. This coincidence could take three years or more if Jubilee and TEN gas remain on schedule. This creates revenue loses when analyzed through the lenses of time value of money and the opportunity cost of investing the $28 million now. Ghana is also exposed to certain technical and geological risks that may, in reality, alter projected production levels. A case in point is the Jubilee fields. The projected production capacity from Jubilee Fields was 120,000bopd but current actual production levels indicate about 90,000bopd. This means that gas in the ground is not an automatic revenue at will.

Conclusion

The OCTP project and subsequent gas production provides Ghana the opportunity to improve power generation to spur economic growth and development. However, delays in putting in place appropriate infrastructure to realize the benefits from the project has had financial implications which the government has sought to address with short term but costly measures.

If the government of Ghana would speed up infrastructure delivery to take the gas, much of the financing challenges would be addressed. In the meantime, VRA must pay for the gas it utilizes, while GNPC replenishes the escrow account to prevent partners from resorting to World Bank guarantees.