Africa Centre for Energy Policy

Plugging The Two-Decade Leak: Strategic Options for the Sustainability of Tema Oil Refinery

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1.0 Background

The Tema Oil Refinery (TOR) has a refinery capacity of 45,000 barrels per stream day (bpsd) and remains a major refinery of crude oil in Ghana. The refinery was constructed in 1963 and was 100 percent owned by ENI as Ghanaian Italian Petroleum (GHAIP) Limited, a tolling refinery to process crude oil from multinational companies into finished petroleum products at a fee. In 1977, the company was acquired by the government of Ghana and continued to operate as a tolling facility until 1996, when its business strategy changed to integrate upwards. This change allowed TOR to procure its own crude and market refined products to recover the cost of the crude, refining and operating margins.

The extended business exposed the company to both political and market risks. These risks largely emanated from price regulation and excessive interference from the government, which led to the accumulation of debt over the years.

By 2003, TOR had accumulated so much debt that it became financially unsustainable and required state intervention. Parliament, therefore, passed the Debt Recovery (Tema Oil Refinery) Fund Act, 2003 (Act 624), which imposed a levy on petroleum consumers to raise revenue to defray TOR's debt. The total debt by the end of 2003 stood at **GH₵430.7** million. Between 2003 and 2020, the public has paid **GH₵3.8** billion in nominal terms (present worth of about **GH₵8.6** billion), yet the current outstanding debt of TOR is in excess of **GH₵2** billion. This is in spite of many efforts at paying down the debt and raising loans to retool the operations of TOR over the years.

The fundamental question that remains is what strategic options are available to fix the problem with TOR after 18 years of public support to fix the company through the levies. It does appear that Ghana is holding on to a company that generates no value to the taxpayer, rather an unnecessary burden that is passed down several generations.

This continues to question the effectiveness of tax policy and the affinity of the government to sustain such a non-performing asset without a coherent exit strategy.

This report examines the operationalisation of the TOR Debt Recovery Levy and the reasons accounting for the unsustainable growth of the TOR debt. Specifically, we examine the governance breaches of the Act, debt accumulation and, managerial and operational inefficiencies of TOR and provide recommendations on the strategic options for lifting the burden of TOR off the shoulders of the Ghanaian public.

2.0 The Establishment of the TOR Debt Recovery Levy and its governance principles

At the time of establishing the TOR Debt Recovery Levy in April 2003, the total debt of TOR was less than **GH₵400** million. Between 2004 and 2008, the average annual revenue from the levy was about **GH₵115** million. The governance principles in the Debt Recovery (TOR) Fund Act, 2003 (Act 624) required that the revenues from the levy must only be used for payment of debts incurred by TOR and the interest accruals from the debts. If this principle had been followed, TOR debts would have substantially reduced, if not settled, by 2008. However, by the end of 2008, TOR's debts had increased to **GH₵1,484.4** million, which accumulated to **GH₵2,107** million as of August 2017. The persistent violation of the governance principle, coupled with poor management and political interference, has worsened the problem over the years, although substantial revenues continue to accrue from the levy.

Between 2009 and 2016, the average annual revenue from the levy was **GH₵230** million. Again, between 2017 and 2020, the levy generated average annual revenue of **GH₵326** million. However, governments over the years have sustained an illegal practice of releasing part of the funds accrued from the levy to settle the debts. As a result, the debt has been accumulating. The periodic intervention is to raise funds from issuing bonds to pay creditors of TOR, essentially to change the debt structure. The practice of issuing bonds for TOR debts cuts across all political regimes between 2000 to date.

Table 1: Bonds raised to settle TOR's Debt

Year	Bond raised (GH₵)
2000	240 million
2006	110 million
2011	572 million

These bonds and intermittent payments could not resolve the financial challenges of TOR. The establishment of the Energy Sector Levies Act (ESLA), Act 899, in 2015 subsumed the TOR Debt Levy and repealed the Debt Recovery (TOR) Fund Act. In 2017, ESLA Plc was established as a special purpose vehicle to manage energy sector debt through debt securities. At the time of introducing ESLA in December 2015, the outstanding debt of TOR was **GH₵2,873** million. This was reduced to **GH₵2,107** million before ESLA Plc was established.

Between 2017 and 2020, ESLA Plc raised a total of **GH₵8,294** million in bonds to settle energy sector debts, out of which **GH₵8,056** million was used to settle debts owed by State-Owned Enterprises (SOEs).

Table 2: Breakdown of Payment by SOEs between 2017 and 2020

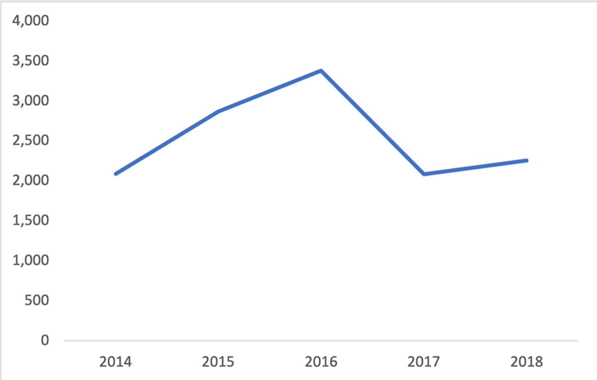
SOE	Amount (GH₵ million)
Volta River Authority (VRA)	3,408
Tema Oil Refinery (TOR)	2,834
Electricity Company of Ghana Limited (ECG)	1,604
Bulk Oil Storage and Transport (BOST)	140
Ghana Grid Company (GRIDCo)	70
Total	**8,056**

Data Source: 2020 Annual Report on the Management of the Energy Sector Levies nd Accounts (Ministry of Finance)

From Table 2, **GH₵2,834** million was used to settle TOR's debts from ESLA Plc. This amount is higher than the outstanding debt of **GH₵2,107** million as of 2017. However, TOR, in a 25th May 2021 statement, indicated its current debt is in excess of US$400 million (more than **GH₵2.3** billion). The total debt accumulation and the exact settlement between 2008 and 2020 remain unclear. Between 2014 and 2018, TOR's debts stayed above **GH₵2** billion, with a peak of **GH₵3.3** billion in 2016 (See Figure 1).

The settlement of the debt through the ESLA Plc bonds essentially moves the debt from TOR's books to ESLA Plc for subsequent servicing and amortisation. It implies, therefore, that the public will continue to bear the debts through the payment of the Energy Sector Levies until an undetermined future. This is aggravated by the fact that TOR continues to accumulate debt through political interference, operational inefficiencies, and inadequate investments without any strategic handle on the problem.

Figure 1: TOR's Liability Profile Between 2014 and 2018

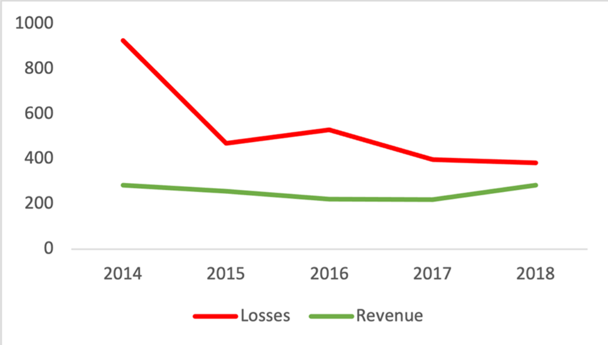


Data Source: State Ownership Reports, 2016-2018 (Ministry of Finance)

3.0 TOR's Debt Accumulation

The challenge with resolving TOR's financial problems and difficulties can be traced to the company's inability to contain the debt accumulation. This has made it difficult for public interventions to provide a needed solution to the company's financial problems. The consequence is that the more the public pays, the worse it gets. As a result, year on year, TOR continues to make significant losses. Between 2014 and 2018, the company's losses were above **GH₵300** million annually, recording the highest in 2014 at **GH₵927** million and the least in 2018 at **GH₵382** million. At the same time, annual revenues have stayed below **GH₵300** million. Cumulatively, the total loss over the five-year period amounts to **GH₵2.707** billion against the total revenue of **GH₵1.263** billion, as shown in Figure 2.

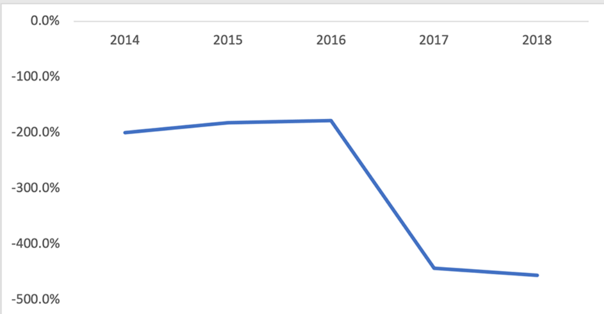
Figure 2: TOR's losses and revenues between 2014 and 2018



Data Source: State Ownership Reports, 2016-2018 (Ministry of Finance)

Between 2014 and 2018, TOR's total liabilities have stayed above its total assets, resulting in negative equity values and worsening gearing ratios. Over the period, the company's gearing ratios have worsened. Typically, in finance, a gearing ratio above 50 percent is considered high risk for any business. In TOR's case, the gearing ratio worsened from negative 200 percent in 2014 to over negative 450 percent in 2018 (see Figure 3). TOR's significantly high and unusual negative gearing ratios mean that the company has become a highly indebted and high-risk asset. Essentially, TOR is surviving on government guarantees and not thriving as a business on its own.

Figure 3: TOR's gearing ratios between 2014 and 2018



Data Source: State Ownership Reports, 2016-2018 (Ministry of Finance)

4.0 Drivers of TOR's Debt Accumulation

TOR's debt accumulation problem is primarily induced by political interference, lack of accountability, and operational challenges.

4.1 Political Interference and lack of accountability

The corporate governance of TOR has, over the years, been riddled with unbridled political interference. Instability in management has been the foremost political challenge TOR has faced. With the period 2004 to 2009 as an outlier, the average tenure for an MD of TOR is about two years (Table 3).

Table 3: TOR MDs and their tenures since 2004

No.	MDs	Tenure
1	Francis Boateng	May 2020 – June 2021
2	Asante Berko	January 2020 – May 2020
3	Isaac Osei	January 2017- 2019
4	Kwame Awuah Darko	June 2015 - 2017
5	Dr. Alphonse Kwao Dorcoo	Dec 2013 – 2015
6	Ato Ampiah	May 2010 -2013
7	Kwame Ampofo	January 2009 -2010
8	Dr K.K. Sarpong	2004 -2009

The tenure of these MDs is directly linked to the political system and the wishes of the appointing authority and power brokers. This has had implications on the MDs' performance. They respond to political pressures for the procurements of inputs and staff recruitment, which lead to suboptimal contracts and ever-increasing staff strength.

- ***Political procurements:*** Some suboptimal contracts are often imposed by the political system through sole-sourcing, which eventually leads to losses and dubious claims on the company.
- ***Political Staff Recruitment:*** With all the challenges in 2003 which necessitated the TOR debt recovery levy, the staff strength of TOR was about 350. This has ballooned to about 950 by 2020, including about 350 contract staff. At the same time, the company's output has reduced from 45,000 bpsd to about 25,000 bpsd. TOR's staff strength is comparable to refineries with capacities of about 2.2million bpsd.

  The high level of overstaffing increases operational and administrative costs, which contribute to the company's annual losses over the period. Beyond the numbers, the quality of the recruitments is also a significant concern. Recruitment as a political reward has, over the years, descended from top management to lower levels, creating political groupings in the business environment and breeding internal saboteurs to the success of the company. Depending on the regime, staff found to be non-aligned are seconded to unrelated institutions while their wages continue to sit on TOR's books.

The effect of these problems at TOR has been the micromanagement by the political system, which deflects the attention of management from the real challenges facing the company to constantly looking over their shoulders to please their political masters. This has weakened accountability and proper corporate governance in the management of TOR. Successive Boards of the company are unable to check the excesses of management because the management often wields much political power to ignore the Boards. This makes the Board a mere rubber stamp for management decisions and actions. In fact, the Board have been reduced to a component of the political reward mechanism. As a result, not a single manager has been held to account for the mismanagement of the company. The worst sanction for an MD is to be sacked. In 2015, the government's own investigation identified this problem as one of the contributors to debt accumulation. The investigation recommended questioning past management and MDs of the company for major crude contracts undertaken without board approvals. However, such questioning never took place to signal any semblance of accountability on the part of the MDs.

4.2 Operational challenges

The operations of TOR have largely been inefficient. This has affected revenue generation and the ability to respond to their financial responsibilities. These inefficiencies manifest in the lack of working capital, exchange rate losses, underutilised infrastructure, trading losses and contractual claims against the company.

a. Working Capital

TOR does not have working capital and has largely relied on purchase credits and loans to finance its operations. For the past two decades, this has been the case when the company shifted its operational model from a tolling company to procuring its own crude for refining, exposing the company to crude oil price risks. TOR's reliance on credit requires robust operational efficiency that accounts for the value of inputs (mainly crude oil), interest and margins. However, the required operational efficiency has not existed in the company to allow it to offset the operating costs and recurring liabilities.

b. Exchange rate losses

The company's debt profile is mainly denominated in foreign currency and is susceptible to the depreciation of the local currency it operates with. Therefore, the inability to repay loans and credit purchases has led to significant growth in its liabilities due to penalties on defaults and loan interests, mainly dollar denominated. This is worsened by the fact that TOR borrows at a higher rate because of its high credit risk.

c. Underutilised infrastructure

The revenue-generating potential of the company is further hampered by underutilised infrastructure. TOR currently operates at a capacity of about 25,000 bpsd, which is lower than its established operating capacity of 45,000 bpsd. Again, the plant hardly operates throughout the year, creating more idle time for the machinery resulting in a higher rate of deterioration. The combined effect of longer idle times and lack of investments in efficient equipment contribute to the company's operational losses, compounding the debt accumulation problem.

d. Trading losses

Much of TOR's losses emanates from their trading activities. This rehashes the fact that the problems of TOR started when it changed strategy from its tolling business to procuring its own crude and selling refined products. Over the years, the company continued to make significant losses through trading activities, yet it lacks everything a trading company should have; specialised trading units, systems and trading capital. This problem was identified by a committee set up by the Ministry of Energy in 2015 and the situation has remained the same for six years on. This makes the company highly uncompetitive and exposed to higher trade risks.

TOR borrows to trade; hence when the company makes losses, it has cascading effects on interest payments and capital amortisation. However, anytime the company goes back to its tolling arrangements, there is evidence of stability in operations, which indicates that the company suffers less risks on the tolling business model.

e. Contractual Claims

The company is saddled with recurrent claims from breaches of agreements and a lack of commercial attitude to manage the corporate business effectively. TOR often gets into disputes with its clients over reconciliation of storage volumes and credit defaults which occasions multiple claims, some of dubious validity, against the company. TOR has problems verifying the amounts of products coming into tank and exiting; thus, it is unable to put up any proper defence when these claims are brought against it. Besides, TOR consumes some products for its operations without accounting accurately for how much. For example, when TOR's power is cut, they use available products to run their own power generation systems regardless of whether a third party owns the product. Essentially, the company is being run with no commercial mindset. These contribute to litigations over reconciliations and delays in payments.

Moreover, the reconciliation of the claims between the claimants on one side and the Ministry of Finance (MoF) and TOR on the other side lacks transparency and proper documentation. On many occasions, MoF has intervened in the negotiation and payment of claims against TOR without the knowledge of TOR or official communication to TOR on the offset of their liabilities. Again, the company does not have a mechanism to track debt settlements made on its behalf by the MoF apart from the instances where the Ministry had informed them. The situation generates the recurrent need for reconciliation of settlement data between the MoF and TOR. It also introduces the risks of some debts settled by the MoF to still sit on TOR's books as claims and continue to accrue interests, fuelling the perception of a scheme for contractors to make multiple claims from a single contract.

5.0 Conclusion

TOR remains a viable business as a tolling refinery. In its current state, the company is still able to attract partnerships with established oil traders such as BP, Vitol etc. However, its sustainability continues to be threatened by inefficient trading, political interference, and managerial inefficiencies, all of which accumulate debt for the company. As a result, public intervention through the TOR Debt Levy has failed to salvage the situation almost two decades on. Currently, TOR's cumulative outstanding debt is in excess of **GH₵5.5** billion i.e., **GH₵2.8** billion with ESLA Plc and over **GH₵2.3** billion sitting on TOR's books.

TOR's cumulative outstanding debt could be yielding an average annual interest of about **GH₵1** billion (about 1145 percent of projected government capital expenditure in the social sector for 2021) at the average interest rate (18 percent) on the ESLA bonds. This interest payment would be a significant drain on scarce national resources. Moreover, it defies prudent fiscal management of tax revenues, particularly when the GoG's projected capital expenditure in the social sector (**GH₵87.37** million) for 2021 only represents about 8 percent of interest payments on TOR's debts.

Table 4: Government of Ghana Capital Expenditure Allocation for the Social Sector in 2021

Social Sector MDAs	Total Capital Expenditure
Ministry of Education	24,500,000
Ministry of Employment and Labor Relations	4,717,508
Ministry of Health	45,500,000
Ministry of Youth and Sports	2,300,000
National Commission for Civic Education	1,150,000
Ministry of Gender, Children and Social Protection	6,900,000
Ministry of Chieftaincy and Religious Affairs	1,150,000
National Labor Commission	1,150,000
Total	**87,367,508**

Data Source: 2021 Budget Statement (Ministry of Finance)

Similarly, without interest payments on TOR's debt, GoG capital expenditure on infrastructure could double. The **GH₵1** billion can also triple GOG's capital budget of about **GH₵290** million for the economic sector. This harrowing picture still does not account for the continuous debt accumulation of the company through annual average losses of over **GH₵300** million.

6.0 Recommendations

To avoid the Business-as-Usual situation that has not worked to prevent waste of public resources in the management of TOR, we present two options for government to consider:

1. **Government's Continued Ownership of TOR** – Under this option, significant governance reforms that take away control and management of the company by politicians are required. The persistent political interference curtails accountability that holds management in check. For the company to remain a profitable entity under state ownership, the government must allow the company to operate under sound corporate governance where management and Board are held strictly accountable for inefficiencies and mismanagement. This requires:
    a. The appointment of an MD with industry experience who can show a strategic pathway to profitability and the repayment of the existing debts and held strictly accountable to an agreed set of Key Performance Indicators (KPIs).
    b. Management should have the free hand to restructure the company, including staff strength, to an optimal level that leads to profitability.
2. **Privatisation of TOR** –This option is the most sustainable given the uncertainties around political behaviour associated with change in governments and within the same government. Privatisation provides the opportunity to offset some of the debt and freeze the debt accumulation to allow ESLA to address the existing debt situation. We recommend a phased approach through initial partial privatisation and the state's eventual exit to test the effectiveness of privatisation.