

# *Oil & Gas Matters*

April 2011





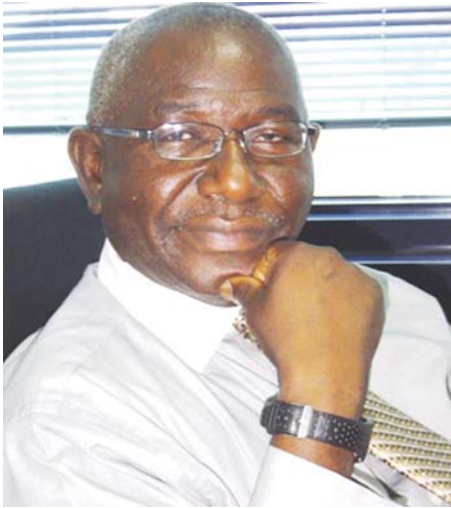


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# Foreword



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***The Oil and Gas industry in Ghana is still at its early stages with companies coming in to set up shop as the quest for Oil continues.***

As this industry continues to grow, the face of Ghana's business environment continues to change with prospects for the Ghanaian economy appearing positive with economic growth.

The tax arena has also had its fair share of change and recently the revenue management bill was passed with some proposed amendments. Though not specifically discussed in this publication as it is yet to be gazetted, the general thrust of this bill and other tax matters have been addressed at various levels.

Also mentioned in the publication, is capital funding avenues as oil & gas organisations compete to meet the ever-increasing demand for energy. With growth, comes risks; and one of the risks that we talk about is fraud.

The fraud article highlights some of the fraud triggers and ways forward to combating fraud. With growth also comes resourcing issues and operating at maximum effectiveness and these too have been addressed in the publication.

I hope that you find this general overview highlighting some of these changes that are affecting the Oil and Gas industry in Ghana useful and informative. I do encourage you to respond to me or to my colleagues mentioned in the contacts page, with your comments and queries.

**Felix Addo**  
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# How fit is your finance function?



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*A challenge faced by many companies in their journey to success is the availability of relevant, timely and accurate information*

**Oil and gas prices have fluctuated wildly in recent times. Despite the price cycles, energy companies know that they have to focus on the medium to long term situation when it comes to achieving growth and making sound decisions.**

Investments in Research & Development, people and technology are crucial to maintaining a long term competitive edge. While making these important investments, oil and gas companies also have to focus on controlling costs, improving controls and managing risks.

A challenge faced by many companies in their journey to success is the availability of relevant, timely and accurate information. This is particularly relevant in the oil and gas industry due to its peculiarities, giving rise to unique challenges including:

## **Addressing sustainability issues**

Air, water and soil quality are at risk in many areas of the world. A key challenge for energy companies is developing business strategies and practical implementation plans while

demonstrating high standards of environmental and social responsibility. Many energy companies are successfully addressing this challenge through several means, including the development of robust performance indicators to increase the transparency of their disclosures.

## **Complying with regulatory and reporting requirements**

The regulatory and reporting landscape is particularly complex for oil and gas companies. Not only do they have to conduct operations in a variety of regulatory and tax regimes but they also have big upfront investment needs, with great uncertainty about long-term outcomes. The natural resource supply and trading environment, combined with often complex stakeholder and business relationships, adds to the complexities oil and gas companies face. In addition, the advent of International Financial Reporting Standards and section 404 of the Sarbanes-Oxley Act for US registrants has added to the challenges. All of this demands careful judgement around corporate governance, internal controls and external reporting.

## **Improving performance and operational effectiveness**

As a mature industry, energy companies must achieve enhanced profitability, largely through best in class performance and disciplined cost control as market demand for their products is strong, but not without fluctuation. In the face of fluctuating

demand and cyclical pricing, operating an efficient and streamlined business, as well as squeezing costs, is critical.

## **Industry transactions and consolidation**

The scale of today's oil and gas organizations dwarfs that of many other industries. The size and scale of the industry will continue to grow to meet the world's ever-increasing demand for energy. Today's demand of 200+ million barrels of oil equivalent per day is predicted to double by 2050. To feed the world's increasing demand for affordable and reliable access to energy sources requires greater capital, larger workforces, better technology, and effective risk management. Ongoing consolidation across the industry is resulting in larger, more complex organizations with globally expanding operations and greater challenges.. Managing these global operations, across borders and product lines, involves carefully balancing enterprise risks with financial goals.

## **Managing financial risk**

Highly publicised business failures are requiring companies in this sector to establish and strengthen financial, trading and risk management capabilities. There is increasing pressure on financial officers to demonstrate that risk identification and financial management are grounded in timely, accurate forecast and performance data on which top management can base strategic decisions.

## **Your Finance function's role as a partner in addressing these challenges**

In their role to assist businesses to manage the above mentioned risks, Chief Finance Officers (CFOs) are juggling to achieve the right balance between three competing agendas; insight, efficiency and control –

### **1. Insight**

There are concerns about whether most finance teams are equipped to deliver the kind of support CEOs are demanding. A benchmark survey conducted on our audit and non-audit clients in the UK revealed that more than 80% of participants are dissatisfied with the quality of management information (MI). Particular concerns centre on whether MI is sufficiently meaningful and forward-looking to drive business decisions in an increasingly complex and uncertain business environment, such as the oil and gas industry.

### **2. Efficiency**

Streamlining operations and standardising processes continue to be high on the finance agenda as finance functions seek to reduce costs, enhance efficiency and free up more time for insight and analysis. The fundamental challenge they face is how to take cost out of the business without heightening risk or jeopardising the firm's ability to capitalise on opportunities – eliminating the flab without cutting away the muscle.

### **3. Control (and Compliance)**

CFOs in Ghana are accountable to their businesses and to the financial community, and have consequently put control and compliance at the top of

their agenda. For many, responses have been tactical rather than strategic. More deeply embedded and sustainable solutions are now required. Flexibility to respond to future regulatory change is also increasingly important.

### **What does management expect of the finance function?**

Boards are looking to their finance functions to provide more active input into decision-making. In practice, however, it is not always clear how finance functions should fulfil this business partnering role.

### **Business partnering defined**

Business partners are finance employees with the skills and experience to work alongside the business; influencing, designing and executing business strategy and planning. Business partnering requires the ability to understand both finance and business realities, to challenge decisions and, in many ways, act as a business consultant.

Following recent global trends, the heat is now on for finance to demonstrate its ability to add value above and beyond its traditional responsibilities. However, when it comes to business partnering, our analysis indicates that finance's ambitions often outrun its abilities.

In many cases, finance is struggling to meet expectations either because of a shortage of the right skills or under-investment in the necessary tools and

infrastructure. Finance's ability to deliver on the promise of business partnership will be critical in its ability to navigate through the tough new global landscape that has become more competitive and regulated.

Finance functions which can rise to this challenge will play a pivotal role in enabling businesses to capitalise on unfolding opportunities and build a platform for long-term profitability and growth.

PwC Ghana is about to commence a benchmark assessment of the finance functions of a range of leading Ghanaian and international firms operating in Ghana. We compare performance both between internal business units or divisions, and versus a relevant group of peer organisations. Companies can then identify improvement opportunities and formulate a plan to realise them. The results enable companies to assess the size, shape and nature of their finance function, and the ability of the function to deliver the needs of the business. The benchmark can be used to chart progress and sustain momentum and is one of the services offered to PwC's audit and non-audit clients.

### **How to participate**

*If you would like to complete a benchmark assessment of your company operating in Ghana, or would like more information please contact Felix Tamathey - [felix.tamathey@gh.pwc.com](mailto:felix.tamathey@gh.pwc.com)*





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## ***Listing as a route for local participation***

***The Government of Ghana has been emphasising the need of local content and local participation in the Oil and Gas industry. Key players are expected to implement programs that ensure that Ghanaians share in the challenges and benefits that oil presents. Listing on the local stock exchange might be one of ways attracting local participation.***

### ***Recent deal activity in Ghana's oil industry***

On 14 March 2011, Kosmos Energy announced in its filing to US regulator that it plans to raise up to \$500 million in an initial public offering on the New York Stock Exchange. The company plans to use proceeds from the offering to help fund its capital spending. Its capital spending budget for 2011 is \$400 million. Kosmos Energy owns a 23.49 percent stake in Ghana's Jubilee offshore oilfield which holds around 1.6 billion barrels of light crude. Kosmos Energy has tried to sell its assets in Ghana, but encountered difficulties because of the desire for local participation. In a saga that unnerved some potential investors, Kosmos Energy in August 2010 called

off what sources close to the deal said was a \$4 billion pact to sell its stake to ExxonMobil after resistance from state oil company Ghana National Petroleum Corporation (GNPC).

On 10 November 2010, Tullow Oil, in a press release, announced that in order to create a more accessible opportunity for Ghanaian individuals and institutions to invest in the future of their oil industry through Tullow Oil, the Group is planning a secondary listing, and issuance of up to four million new shares, on the Ghana Stock Exchange. Tullow Oil is the operator of the Jubilee field and has a 34.7% share in the offshore oilfield which lies approximately 60 kilometres off the coast of Ghana.

### ***Why companies list***

The scale of today's oil and gas organizations dwarfs that of many other industries. The size and scale of the industry will continue to grow to meet the world's ever-increasing demand for energy. Today's demand of 200+ million barrels of oil equivalent per day is predicted to double by 2050. To feed the world's increasing demand for

*In Ghana, the need for local participation is another important reason why multinationals should list on the local stock exchange*

affordable and reliable access energy sources requires greater capital, larger workforces, better technology, and effective risk management. Some companies turn to the capital markets to finance their growth.

The typical reasons why companies list on local stock exchange are to:

- raise new capital
- provide an exit mechanism for early investors
- provide stock compensation for key employees
- acquire local currency
- get greater public profile

In Ghana, the need for local participation is another important reason why multinationals should list on the local stock exchange.

### **The Ghana Stock Exchange**

The Ghana Stock Exchange (GSE) has 35 companies listed including downstream oil operators like Total Petroleum Ghana and Goil Ghana Limited. It has been calling for companies operating in the country to list shares locally, make it easier for Ghanaians to invest in them and generate more interest in a bourse where trading volumes remain small.

The GSE is aware of the challenges, and has been looking at ways to boost the liquidity of the exchange by pushing for additional, in particular foreign, listings. It has low liquidity because large largest shareholders of listed companies particularly the Government of Ghana and SSNIT (the national pension fund) have no interest in trading their shares. A more active approach by the Government and SSNIT would also free up liquidity and lead better price discovery.

### **Way forward**

For companies seeking to raise debt or equity capital in the capital markets, PwC can provide an independent view of the critical issues involved in accessing a particular capital market. Our advice is tailored for the oil and gas industry, the size and complexity of the business, and the scope of the transaction. For companies considering going public, or spinning off part of their business, we have the experience and expertise to position the entity to go public and then take an active part in making the event successful when it happens.

Deals are crucial to many energy companies' strategy, driven by the need to secure supply, extend market footprint, or free up cash and capital. Whether it is a full-scale merger, or sale or purchase of producing properties, or evaluating options, PwC is well known in the marketplace for our knowledge and experience in all types of financial

transactions including mergers and acquisitions, valuation, growth or divestments, and exit strategies.

We focus on the deal continuum from strategy through execution and post-deal integration, including financial and operational due diligence, accessing the capital markets and valuing, negotiating and structuring deals. We provide advice on the implications of financing projects, corporate debt, restructuring, investments, mergers and joint ventures. We advise on ways to better manage assets and large capital investments amidst increased competition, or in times of uncertainty. Our advisors can evaluate technical, operational, market and financial risks.



# Fraud: A recipe for disaster



***In 2010, Ghana, after several years of exploration, joined the prestigious League of Nations producing oil. Ghana, prior to that has relied principally on agriculture and various minerals for her foreign income earnings.***

The discovery of oil and gas in some many nations has been described as a curse due to the failure of governments to use its vast benefits for the development and betterment of its people. Various reasons have been assigned to this but the general notion is that, the production of oil is extremely volatile and unpredictable. Furthermore, its relative significant value as compared to total export, government revenue or gross domestic product makes its management difficult.

Various researches have noted that extractive resources that are localised—such as oil, gas, and minerals actually slow down economic development much more than resources that are spread across the country such as rice and maize.

Extraction of oil and gas and other minerals is capital intensive and by extension only a few companies with the financial muscle can invest in this space. This creates a politically powerful small group or oligarchy and a conducive environment for non-transparent

mechanism of accounting for and distributing resources and wealth. This situation feeds corruption.

## **What is Fraud?**

The Oxford dictionary defines fraud as a wrongful or criminal deception intended to result in financial or personal gain. This could include violations of laws, regulations, and internal policies with an intention from the onset to make some financial gains. According to the World Bank, fraudulent and corrupt practices include the solicitation, payment or receipt of bribes, gratuities or kickbacks, or in the case of financial institutions, the manipulation of loans or Bank Group-financed contracts through any form of misrepresentation.

Fraudulent or corrupt practices also include any situation in which staff members have abused their position or misused World Bank Group funds or other public funds for private gain.

The Oil and Gas industry by its nature attracts big companies and institutions into the exploration areas. They generally would have to rely on the locals to understand the terrain, the regulations as well as the culture of the areas of operation. Some of these areas see bribery and corruption as the way things are done, i.e., it is business as usual.



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*The best way to stop fraud is by instituting measures and procedures that could prevent fraud within the culture of the organisation*

Within the last 10 years or so, the West African Coastal belt has become an important area for oil and gas exploration. This has become more pronounced as a result of the volatility and conflicts in certain parts of the world. Most policy makers of the USA are looking for other areas and avenues for energy sustainability. First mover advantage in West Africa has therefore become imperative and with that comes the likelihood of fraud and corrupt practices with the acquisition of blocks and licences for exploration.

Furthermore, in the case of Ghana, there is a perceived weakness in the regulatory framework within the oil and gas industry. For example, the Petroleum Revenue Bill has only recently been passed even though the first crude has been exported. This, analysts believe, is an incentive for people to take advantage of the system and make quick gains before the regulations set in.

#### **What can be done about Fraud?**

It is a fact that business can be done without the element of fraud and corruption and still generate significant returns for the shareholders. Many companies have instituted fraud risk assessment and compliance into their modus operandi and have pushed for ethical ways of business and have avoided the negative press that comes with fraudulent and corrupt practices.

The best way to stop fraud is by instituting measures and procedures that could **prevent** fraud within the culture of the organisation. Unrealistic targets and ambitions have led to executives and employees going the unethical extra. Regulatory bodies are encouraged to ascertain the qualifications and competencies of the

Board, audit committees as well as top management of companies doing business in Ghana to ensure their unquestionable integrity and clean records. This, the Directors can do by establishing a robust control environment with an enforceable and consistent code of ethics under the watch of a very senior personnel, say a Chief Compliance Officer.

Clear description of duties of the audit committee, internal audit and the Compliance Officer should be documented to avoid ambiguities. The Chief Compliance Officer should be given the role of planning, implementing and coordinating the company's fight against fraud and corruption. This approach should be extended to all third parties who want to do business with that institution.

It is acknowledged that the risk of fraud and corrupt practice is always present in organisations and to **detect** fraud at its early stage, companies should create a safe atmosphere for employees to raise the alarm whenever there are any suspicious activities. Companies should also establish multiple channels of reporting fraud and corrupt activities and assure whistle blowing employees of complete confidentiality.

The Whistleblowers Act, 2006, empowers anyone to report on waste, appropriation or mismanagement of public resources. It provides for the manner in which individuals may in the public interest disclose information that relates to unlawful, corrupt or other illegal conduct or practices in the country. These reports can be made to employers, the Attorney General, the Commission for Human Rights and Administrative Justice among others.



Some companies have even gone further by establishing hotlines to encourage employees to report fraud and related activities and still remain anonymous.

Reports from both internal and external auditors should be scrutinised by the audit committee for any possible acts that compromise the image and reputation of the company.

To encourage the above, it is crucial that management is seen to **respond** timely and appropriately should there be any reports of fraud. In responding, management should thoroughly investigate reports, bring culprits to book, including instigating criminal proceedings should there be any adverse findings. Fraud risk policies should also be continuously reviewed and updated to avoid any future occurrence. This should include adequate public relations work to assure the business community that it frowns on fraud and corruption.

### ***The Role of the Regulatory Bodies***

Regulatory bodies should insist, as part of the licensing process, on a detailed fraud risk policy of potential investors. These policies should clearly define the way the companies plan to deal with fraud and corruption and adequate measures to be taken on detection. This will compel all companies looking to invest in the Oil and Gas industry to put in place appropriate measures to prevent, detect and respond to fraud and corruption.

### ***The way forward***

The lack of transparency in the oil and gas sector of many nations has created mistrust and in some cases violent reactions from the very people whose lives are supposed to be positively affected by the discovery of the “black gold”.

All stakeholders, including government and regulatory bodies should be seen to

put the fight against fraud and corruption at the forefront of all activities and pronouncements.

Companies who are willing to invest in the sector should be commended and rewarded for having a comprehensive fraud risk policy. These policies should be reviewed on a regular basis to ensure they stand the test of time.

Ghana, cannot afford to miss out on the many benefits of being an oil exporting country. The country should not only rely on the activities of investigative journalists etc to fight fraud and corruption after their occurrence. All preventative measures should be put in place to ensure that all sectors of the economy derive the required benefits from the oil and gas industry.



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# Tax in Ghana's Oil & Gas Sector

## A Subcontractor's outlook

*A Subcontractor is a person who has a contract with any Contractor for the provision of works or services relating to petroleum operations*

### **Introduction**

A Subcontractor is defined under the Petroleum Income Tax Act, 1987 (PNDCL 188) (PITL) as:

***“Any person who enters into a contract with a Contractor for the provision of work or services (including rental of plant and equipment) in Ghana for or in connection with the Petroleum Agreement to which such Contractor is a party”.***

A Contractor is defined under the same law as a person who is a party to a Petroleum Agreement (PA). It should be noted that all PA's in Ghana although unique are based on the Ghana National Petroleum Corporation (GNPC) Model Petroleum Agreement (MPA).

From the above definitions, a Subcontractor can be said to be any person who has a contract with any Contractor for the provision of works or services relating to petroleum operations. This article is focused on Subcontractors and highlights the key

tax areas they should be aware of whilst doing business in Ghana.

### **(i) Withholding Tax**

The PITL provides that, payments from a Contractor to a Subcontractor are subject to a final tax which is detailed in each Contractor's PA. The rate of tax is usually 5% and applies to payments for works and services including payments relating to the rental of plant and equipment.

It is not clear whether these provisions apply to persons who supply goods exclusively to Contractors. These persons may therefore be subject to the normal fiscal regime in Ghana which applies a 25% corporate income tax on a net profit basis.

What will be the applicable tax rate for an entity that provides a mix of goods and services? A possible separation of income derived from both revenue streams, thereafter subject to tax at different rates (5% and 25%) may be sufficient.

It may also be possible that the Ghana Revenue Authority (GRA) may agree to a 5% final withholding tax rate for the supply of goods by a Subcontractor to a Contractor. Further guidance from the GRA on this issue would help to harmonise the various approaches discussed above.

**(ii) Value Added Tax (VAT)**

The MPA states that a Contractor and its Subcontractors and Affiliates are not subject to VAT. This does not however exempt a Subcontractor from charging and paying VAT. Subcontractors do not have the authority to issue VAT Relief Purchase Orders (VRPOs) which would have served the purpose of reducing the input VAT paid when settling their supplier invoices. This has resulted in Subcontractors having large VAT refund positions which may take some time to recover from the tax authorities. Effective VAT planning is required to minimise this occurrence.

**(iii) Double Tax Treaties and the creation of Permanent Establishments (PE or taxable presence) in Ghana**

Ghana has double tax treaties with France, Belgium, South Africa, the Netherlands, the United Kingdom, Switzerland, Germany and Italy.

A majority of these DTA's contain a clause which exempts the creation of a PE where an enterprise resident in any of the DTA countries maintains a facility for the maintenance of goods for delivery, display and storage in Ghana. The ability to maintain goods in a country does not preclude the creation of a PE if the goods stored or delivered are deemed to be sold in Ghana.

It is important to realise that where goods are stored and later sold to a Contractor in Ghana a taxable presence will still be created by the foreign entity in Ghana.

These are areas that should be considered within the tax and financial planning objectives of the wider group of companies in order not to create additional entities in various countries where this is not in line with group policy.

**(iv) Expatriate Staff**

Expatriate employees of Subcontractors are subject to personal taxes in Ghana at the prevailing tax rates for residents and non-residents depending on which category they fall into at a particular point in time. An expatriate will generally be considered non-resident for tax purposes where employment is exercised in Ghana for less than 183 days. In addition, if expatriate employees of a Subcontractor are present in Ghana for 30 days or less in a calendar year (the number of days varies depending on the PA used), they are not taxable in Ghana. This point should be noted especially since most Subcontractors operate a 28 day rotational cycle in Ghana for their employees.

**(v) Branch profit and other profit distributions**

Where a Subcontractor registers a branch for the purpose of carrying out its operations in Ghana, distributions of profit to the head office are subject to a final withholding tax at 10%. This issue has been widely debated since subcontractors are subject to a 5% final withholding tax on income activities related to petroleum operations (which include exploration, development and production). A branch is simply an extension of a head office and not a company on its own, all taxes have been duly paid on income derived from petroleum operations in Ghana.

# The long arm of the law



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## Introduction

Ghana made significant discoveries of petroleum (oil and gas) in commercial quantities in 2007 although exploration for oil and gas started as far back as in 1896 in onshore Tano basin in the Western Region. As is expected of a country with future prospects, Ghana enacted a number of laws including one for the setting up of the National Oil Company (NOC). This Company – Ghana National Petroleum Corporation – is tasked with undertaking exploration, development, production and disposal of petroleum.

The Government of Ghana (GoG) is currently reviewing some of the existing petroleum related legislation with the view to reflect current industry conditions and reduce the challenges in the implementation of the laws. Ghana is now more than certain of being an oil producing country as crude oil is produced from the “Jubilee field”, a field believed to be of world class standards.

## Overview of the business environment in the oil and gas industry

The upstream oil and gas industry in Ghana is principally regulated by:

- Ghana National Petroleum Corporation Law, 1983 (P.N.D.C.L. 64) (GNPC Law);
- Petroleum (Exploration and Production) Law, 1984 (P.N.D.C.L. 84) (PEP Law);

- Petroleum Income Tax Law, 1987 (P.N.D.C.L. 188) (PIT Law);
- Petroleum Agreements (PA); and
- Internal Revenue Act, 2000 (Act 592) as amended (IRA) and its regulations.

The PEP Law empowers the GNPC to spearhead petroleum operations in Ghana. Currently a number of oil and gas companies have signed PAs which is an agreement among the GoG, GNPC and the Contractor(s) or Investor(s) for the conduct of petroleum operations. GNPC, the NOC and regulator assists the Ministry responsible for Petroleum to monitor all PAs to ensure compliance with applicable laws and industry best practices.

Besides the friendly environment, the macro economy of Ghana has shown robustness in the past few months with consistently falling inflation rates since January 2010. In December 2010, inflation fell to 8.5% and this is the lowest inflation rate achieved in about 20 years.

Many oil and gas investors are finding it relatively easier to operate in Ghana than other African countries due to the rather favourable terms of their contracts which includes but not limited to: negotiable royalties (normally 10%), negotiable income tax rates (normally 35%), no import duties on exploration and production equipment and materials, no export duty on crude oil, and no restriction on repatriation of funds.

## M&A opportunities and scheduled licensing or bids

For several reasons, some investors have formed consortiums and together as one group signed PAs with the Government and GNPC. We are also aware of some farm out agreements between Contractors in the industry, possibly with the aim of diversifying risks.

### **Topical issues in the industry (including new/proposed regulations and taxation)**

Once a PA is signed the other parties other than the investor(s) (i.e the GoG and the GNPC) are required to be consulted before an investor attempts to sell all or part of its stake. An attempt by Kosmos Energy to sell its stake in an oilfield was met with snags and resistance from the GoG due to their claim that due process was not followed. Eventually the sale was called off. Generally, such sales are permitted if the investor follows the stipulations in the PA in respect of notice and procedure.

The laws governing Contractors and Subcontractors are expected to be changed as Parliament is expected to pass into law the Petroleum (Exploration and Production) Bill in place of the PEP Law and in addition, repeal the PIT Law and consolidate it in

### **Local content and technology transfer requirements or proposals (if any)**

A draft policy framework on “Local Content and Local Participation in Petroleum Activities” has been approved by Cabinet and is yet to be ratified by Parliament. The policy, when developed into legislation is to ensure that Ghanaians derive maximum benefits from the oil find. The draft policy proposes the following:

- At least 5% equity participation by the Ghanaian private sector for petroleum license, permits and contract operators;
- At least 10% equity participation for providers of supplies and services whether directly or indirectly to the operator of any license;
- At least 90% local employment and in-country spend within 10 years of a petroleum lease in certain supplies and services; and
- In evaluation of bids, the bid with the highest level of Ghanaian content is selected where all else are the same.

Concerns have been raised that the percentages for staffing requirements are quite ambitious. Also the number of competent Ghanaians may not be available given the industry is new and people are in the skills development phase of their careers in order to fully participate in the oil and gas industry in the near future.

Other concerns are that it may be challenging for Ghanaians to obtain the required capital in order to contribute equity to petroleum operations and it is questionable what value would be added by such local investors. Such measures of local shareholdings in the multi-national companies have not been viewed as successful or effective by most companies in other countries.

### **Conclusion**

The oil find in Ghana should continue to give the country good prospects if well managed. The GoG has put measures in place and continues to do so in an attempt to address administrative and other concerns raised by operators in the industry. Hopefully, this should make the industry much more attractive to investors.



the IRA. Even after the new law is passed, it is expected that some Contractors, as far as their PAs permit, can choose to either operate under the new or old law. The change in laws is expected to reduce ambiguities and rather make the future more predictable. It proposes a fixed income tax rate of 35% and an opportunity for Contractors to carry over tax losses for not more than 10 years, and an increase in the final withholding tax rate applicable for income earned by non-resident Subcontractors from 5% to 15% of the revenue from petroleum operations.

# The view from the top

## Oil companies and tax in Ghana

**Ghana's oil discovery has sparked interest from all over the world and has made the possibility of consolidating Ghana's economy from low income to middle income status a reality.**

This article highlights a few key areas oil producing and exploration entities should pay attention to as they conduct their tax affairs in Ghana.

### **Key Definitions**

**Contractor:** means any person which is a party to the Petroleum Agreement with the Republic and the Corporation.

**Petroleum Income Tax Law:** means the Petroleum Income Tax Law, 1987 (PNDCL 188).

**Petroleum Agreement:** means an agreement entered into between the Republic, the Corporation and a contractor for the exploration, development and production of petroleum by the Corporation in association with the contractor.

**Model Petroleum Agreement:** means the model petroleum agreement between the State, GNPC and Contractor including the Annexes attached to it after which all petroleum agreements take after.

**Petroleum Exploration and Production Law:** means the petroleum law guiding the operations of oil Contractors in Ghana.

### **Minor Taxes**

The Model Petroleum Agreement (MPA) states that Contractors will be subject to taxes, duties, fees or other imposts of a minor nature. However the agreement does not define the term a "minor nature" and this has led to disputes regarding Contractor's total tax liabilities especially the 6% Communication Service Tax (CST) on communication services received, stamp duties (ranging from 0.5% to 1%) outside of the stamping and registration of a particular PA and lastly administrative charges (2%) relating to customs importation duties. These percentage rates may seem insignificant, however when applied to large baseline amounts are not so "minor" after all.

### **Additional Oil Entitlement**

The Government of Ghana has a share or a percentage interest in the crude oil being produced in a development and production area by Contractors. The Additional Oil Entitlement (AOE) indicated in the petroleum agreements seeks to measure Ghana's entitlement to the crude oil and acts as an additional windfall tax. Some debate has arisen regarding whether AOE should be paid out of profits after tax, thus acting as a distribution out of profit, or should be applied before tax thus acting as deduction before profits. The differences in treatment clearly have a significant impact on tax.



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### ***Filing of Returns***

Entities in Ghana including those in the oil and gas sector are required by law to file their annual returns four months after their year end. Such returns must include an estimate of the tax liability due on chargeable income, a certified statement of accounts, a statement of price paid for the sale or export of the share of petroleum produced, a statement of the amount of production of petroleum and a statement containing the full names, addresses, nationality, salaries, wages, fees, allowances and other remuneration of the Contractor's employees in Ghana. It should be noted that returns are required to be filed even if no activities are conducted during a year of assessment or production has not commenced. This must be strictly adhered to otherwise penalties may apply.

In addition to this, quarterly returns are required by the PITL to be filed when production of oil commences.

### ***Farm-out Agreements***

Contractors often enter into farm-out agreements to acquire an interest in another Contractor's (assignor) petroleum agreement mainly with the aim of diversifying risk. These transactions may have various tax implications such as VAT, Corporate Income Tax and Capital Gains Tax. However, each farm-out agreement should be analysed against the framework of the applicable joint venture accounting standards in order to determine which specific taxes may apply if any.

### ***Branch v Subsidiary***

The PEPL Law clearly states that Contractors and Subcontractors should register subsidiaries (incorporated entities) in Ghana. In the recent past, branch registrations have been accepted, however this is likely to be an area which will be closely looked at by the Government of Ghana going forward.

# Our people working alongside you

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