

# **AN ANALYSIS OF THE POLICY, LEGAL AND INSTITUTIONAL REGIME GOVERNING THE OIL AND GAS SECTOR IN UGANDA: A POLICY ANALYST’S PERSPECTIVE.**

## **INTRODUCTION.**

Uganda is endowed with over 12 billion standard cubic feet (339 million cubic meters) of natural gas reserves in its Albertine Graben region in addition to oil reserves of more than 6.5 billion barrels of crude oil. About 1.4 billion of the 6.5 billion barrels of oil, located mostly on its western border with the Democratic Republic of the Congo are estimated to be economically recoverable and as such, Uganda has undertaken steps and measures to process its oil in a bid to propel economic growth.

For instance, Uganda has designed projects to process its crude oil as well as the construction of a tens of thousand oil pipeline from Uganda to Tanga port in Tanzania to transport its oil to the outside world. Among the internally developed oil infrastructure, the Tilenga project will have a processing facility with capacity of up to 190,000 barrels of oil per day while the Kingfisher project will have the capacity to process 40,000 barrels per day. These processing facilities will feed into the refinery and the 1,445km crude oil pipeline.

Ultimately and inevitably, huge investments will be made to harness Uganda’s oil potential. It has been estimated that about \$20billion will be pumped by investors in

the oil sector once the Final Investment Decision (FID) is signed into force. The oil and gas revenues will certainly dramatically increase the government’s resource envelope and grant it access to revenues that can be invested in building the country’s infrastructure, agricultural transformation, and human capital development. The investment is very necessary for the development of Uganda. However, Uganda faces the challenges of enhancing the capacity to plan to effectively absorb expected oil and gas revenues and to properly account for the application of the oil and gas revenue given the capacity of the human resources.

Institutional, legal and policy lacunas still abound as regards the successful execution of the projects and ensuring that Uganda does not fall victim of the usual “oil curse”. For Uganda to produce and process its abundant oil resources, it needs a robust legal framework, policy direction and strong institutional mechanisms because of the huge financial resources expected to accompany and accrue from the oil boom; the strong foreign interests and the adverse environmental ramifications that oil production poses for nature and the environment.

This paper analyses the institutional, legal and policy environment in the oil and gas sub sector, identifies the lacunas inherent herein and makes policy recommendations to **i)** prevent an impending oil curse; **ii)** to mitigate the adverse effects of the oversights made in the oil and gas sector socially, politically, economically and environmentally and **iii)** to enable Uganda enjoy the full benefits accrued from its abundant oil resources.

## **Legal framework**

In a bid to improve accountability of government revenues and expenditures, the Public Finance Management Act was enacted as legislation by the 9<sup>th</sup> Parliament of Uganda in 2015. The hindsight behind this legislation was the proper management of the oil revenue as oil was initially anticipated to flow out of the ground by 2019. The PFM Act created the office of the Accounting officer for the Petroleum Authority (PAU). Under Article 164 of the Constitution of the Republic of Uganda, 1995 (as amended) and Section 45 of the Public Finance Management Act, 2015, the Accounting Officer is accountable to Parliament for the funds and resources of the Petroleum Authority of Uganda.

According to the prevailing legal framework, the Accounting Officer is responsible for the preparation of financial statements in accordance with the requirements of the Public Finance Management Act 2015, and the Financial Reporting Guide, 2018, and for such internal control as “management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error”. The 2017 and 2018 reports by the Auditor General, have however, found serious inconsistencies in the execution of the duties stated above by the PAU Accounting Officer.

This is exacerbated by reports from the Ministry of Finance, Planning and Economic Development which revealed that Shs. 200bn was from the Petroleum Fund to finance budget deficits.

This is contained in a semi-annual report by the Ministry of Finance, Planning and Economic Development submitted to Parliament on the inflows, outflows and assets of the petroleum fund for the period that ended 31<sup>st</sup> December, 2018 indicating the money was withdrawn to finance the 2018/2019 budget priorities. It should be noted that Section 61 of the Public Finance and Accountability Act, 2015, mandates the Minister of Finance to report to parliament on the status of the Fund in terms of inflows, outflows and assets every after six months.

On legal lacunas surrounding the illegal and suspicious withdraw of Petroleum Fund revenues by government, a 2017 Auditor General’s report reveals that Shs 125 billion was transferred from the Petroleum Fund in November 2017 to the consolidated fund to finance budget. This is not only irregular but also increasing transmoglofying into a threat to how oil revenues are being used even before oil is extracted. As a matter of fact, official government reports from the Ministry of Finance, Planning and Economic Development (MoFPED) gesticulate that Petroleum Fund monies have dwindled from shs. 507 billion to shs. 288 billion.

In an effort to strengthen the legal framework governing the oil and gas sector in Uganda, two pieces of legislation, that is, The Exploration, Development and Production Bill 2012 and The Refining, Gas Conversion, Transportation and Storage Bill 2012 were presented to Parliament. Sadly, however, these Bills have not been passed into law as of today. Promotion and regulation of the oil and gas sector has

been initially undertaken by the Ministry of Energy and Mineral Development through the Petroleum Exploration and Production Department (PEPD).

Under the National Oil and Gas Policy, the Ministry handles the policy aspects, while regulatory and commercial aspects are handled by the Petroleum Authority of Uganda (PAU) and Uganda National Oil Company (NATOIL) which was created by Article 49 of the Petroleum (Exploration, Development and Production) Act, 2013. The role of the company is to manage Uganda’s commercial aspects with regard to petroleum activities and the participating interests of the state in the petroleum agreements. However, as will be discussed in the subsequent section, there are serious institutional lacunas as regards financing of the PAU and UNOC.

From the policy perspective, there is a National Oil and Gas Policy which was approved by cabinet in 2008. Objectives of the Oil and Gas policy are as follows:

To ensure efficiency in licensing areas with potential for oil and gas production in the country.

- ☐ To establish and efficiently manage the country’s oil and gas resource potential.
- ☐ To efficiently produce the country’s oil and gas resources.
- ☐ To promote valuable utilization of the country’s oil and gas resources.
- ☐ To promote the development of suitable transport and storage solutions which give good value to the country’s oil and gas resources.
- ☐ To ensure collection of the right revenues and use them to create lasting value for the entire nation.

- ☐ To ensure optimum national participation in oil and gas activities.
- ☐ To support the development and maintenance of national skills and expertise.
- ☐ To ensure that oil and gas activities are undertaken in a manner that conserves the environment and biodiversity; and
- ☐ To ensure mutually beneficial relationships between all stakeholders in the development of a desirable oil and gas sector for the country.

One of the biggest legal lacunas is the fact that Uganda still uses an obsolete legal regime in the administration of the oil and gas sector. The Petroleum, Exploration and Production Act of 1985 and the Petroleum, Production and Exploration regulations of 1993 are being used to regulate the sector and this presents strong legal and policy challenges as well as impeding smooth implementation of the government policy direction for the sector. In an effort to operationalize the Policy, a new legislation for the oil and gas administration is underway.

#### **INSTITUTIONAL ENVIRONMENT: THE PAU AND UNOC UNDER SCRUTINY.**

The Auditor General's report of 2018 show that the Petroleum Authority of Uganda is i) underfunded having made a budget request of UGX.20 billion and receiving only UGX.19,002,659,618 (95%) was resulting into a shortfall of UGX.997,340,382 (5%), ii) not well suited to optimally utilize the budget funds allocated with a total of UGX.631,552,896 remained unspent at the year end and iii) has no requisite institutional mechanisms as it lacks a strategic plan.

Administratively, there has been revealed inconsistencies in submitting statements of expenditure by oil operators contrary to Regulation 37(1) of the Petroleum

(Exploration, Development and Production) regulations, 2016 which requires licensees to submit to the Authority statements of expenditure that are consistent with the applicable law and the financial and accounting procedures prescribed in a petroleum agreement and the chart of accounts approved or issued by government.

Review of the PAU Annual Report 2017/18 indicated that on average, Ugandans employed by IOCs at management level are 36.5%, at technical level 68% and in other staff categories 78%, contrary to section 17 (4) of the Upstream National content Regulations 2016, which requires percentages of 70% at management level, 60% at Technical level and 95% at other levels.

#### **AMBIGUOUS ROLE OF THE UGANDA NATIONAL OIL COMPANY.**

Article 49 of the Petroleum (Exploration, Development and Production) Act, 2013 created the UNOC whose main role is to manage Uganda’s commercial aspects with regard to petroleum activities and the participating interests of the state in the petroleum agreements. This is in addition to the management of the business aspects of the state with regard to petroleum, proposing new upstream, midstream and downstream ventures, both locally and internationally and developing expertise in the oil and gas sector.

However, there is no clear financing strategy of the UNOC. A 2017 report from the Office of the Auditor General (OAG) reveals a systemic failure by the Ministries of Energy and Mineral Development and Finance, Planning and Economic Development to pay their share holders’ worth of 51% and 49% respectively. This is 10,000 shares



shares worth Shs10 billion each with a share value of Shs. 1 million each. Failure to find a clear and consistent revenue stream for a company that is mandated with overseeing state interests in the oil and Gas Sector and being a critical actor in the joint ventures and production sharing agreements and government representative in the refinery and pipeline projects raises policy and legal eyebrows. This may explain why the Final Investment Decision (FID) is yet to be taken and why oil production is always getting postponed.

#### **SOCIAL IMPACT POLICY AND PROGRAM AREAS.**

After the discovery of commercial oil reserves, an estimated 7118 people were automatically classified as Project Affected Persons (PAPs) who were supposed to be resettled in a period of 8 months and end by 2013. Failure to relocate the PAP endeared the Auditor General to make a value for money report covering a span of 6 years that found a Shs. 295 million to government and Shs. 16 million to the project affected persons while the price of the resettlement consultant shot up by an extra Shs 1.2billion.

The failure to effectively relocate the communities affected by the oil discovery runs a risk of turning local communities against the oil development projects, investors and governments in the long run. It is also plugging the government into unnecessary and planned for expenditures as the cost of land is skyrocketing each day in the oil areas. It is also delaying all efforts to have the Final Investment Decision signed and making oil investments riskier.



**RECOMMENDATIONS.**

After analyzing the policy, legal and institutional environment under which the oil and gas sector is being managed, this paper therefore recommends that government undertakes the following measures;

- ☐ Cease the suspicious and illegal withdraws of monies from the Petroleum Fund. This is one way of creating public trust that Uganda has better management practices to handle the oil boom and use it to rebuild its economy and boost people out of poverty
- ☐ Increase the numbers of Ugandans in the value and supply chains as service providers in the oil infrastructure projects and as suppliers of labour. This will ensure that the benefits of the oil boom tickle down to each and every Ugandan
- ☐ Seriously begin fast-tracking the implementation of environmental protection legislations and mechanisms. Petroleum industry is one of the biggest polluters and poses serious environmental challenges that should be addressed from the word go
- ☐ Fasttrack the relocation of all project affected persons after fully compensating the, and expedite measures to use the land
- ☐ Revise the 2008 Oil and Gas policy and make it more relevant
- ☐ Find a funding mechanism and financing strategy for the Uganda National Oil Company. The two principal shareholders, Ministry of Finance and the Ministry of Energy should immediately fulfill their shareholding obligations.



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