EXTRACTIVES HUB POLICY BRIEF FOR UGANDA

"Project approval process in Government and its effect on investments by the Uganda National Oil Company"

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1. Summary

Since the discovery of commercial reserves of oil in Uganda in 2006, a few policies and legislation have been put in place to ensure proper and efficient management of the resource. Through this legislation, the Uganda National Oil Company Limited (UNOC) was created to cater for government's commercial interests in the sector. UNOC has several projects lined up in preparation for commercial production of oil. However, since it is owned by government, UNOC has to follow the public investment management framework for approval of projects which is a long and bureaucratic process. Any delays in meeting its cash calls for its proportion of state participation can lead to penalties or dilution of interests. This is also a challenge since UNOC does not have access to the Petroleum Fund in which all the monies collected from activities in the oil and gas sector are deposited. Therefore, government need to devise a mechanism that can give UNOC quick access to funds to meet its participating interest in these projects whenever the need arises. Access to the Petroleum Revenue Investment Fund within the Petroleum Fund would be one of the ways to address this challenge.

2. Background

Petroleum exploration in what is now Uganda dates as far back as 1925 before the country became an independent state. In 2006, Uganda made the first commercial oil discovery in the Albertine region and since then, several policies and legal frameworks have been put in place to ensure the smooth governance of the oil and gas sector as well as to benefit both the current and future generations. The confirmed Stock Tank Oil-Initially-In-Place is 6.5 billion barrels of which between 1.4 – 1.7 million barrels are recoverable (PAU, 2018; UNOC, 2020a).

Since then, a number of policies and legal frameworks have been put in place to ensure that the resources are efficiently utilized for the benefit of both the current and future generations. Some of the legal frameworks include: a) the National Oil and Gas Policy (2008); b) The Oil and Gas Revenue Management Policy (2012); c) the 2013 Petroleum (Exploration, Development and Production) Act; d) the 2013 Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act; e) The Public Finance Management Act (2015); to mention but a few (UNOC, 2020b; GoU, 2012).

Section 42 of the 2013 Petroleum (Exploration, Development and Production) Act and section 7 of the 2013 Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act provided for the establishment of the Uganda National Oil Company (UNOC). UNOC is a fully government owned and was incorporated under the 2012 Companies' Act as a limited liability. UNOC's overall mandate is to handle government's commercial interests in the oil and gas sector as well as to ensure that the resource is not mismanaged (UNOC, 2020b)

2.1 UNOC Operations

UNOC's business is in the Upstream, Midstream and Downstream. In the Upstream, UNOC's mandate is State Participation with Joint Ventures Partners as well as to explore new sites and discover new partners. UNOC is mandated to hold 15 percent participating interest on behalf of Government in the production licenses covering the fields that have been planned for development. In the midstream, two subsidiaries wholly owned by UNOC i.e. Uganda Refinery Holding Company Limited (URHC) and National Pipeline Company Limited (NPC), will drive this sector. URHC is to hold up to 40 percent participating interest in the refinery while NPC will hold up to 14 percent participating interest in the East Africa Crude Oil Pipeline (UNOC, 2020a).

In the downstream, UNOC is responsible for developing, managing and operating storage terminals. Currently, there is one operational storage terminal, Jinja Storage Terminal, located in Eastern Uganda. UNOC is in the process of identifying a strategic partner for a new storage terminal, Kampala Storage Terminal (KST), which will be located in North-West Kampala (UNOC, 2020a).

UNOC has also been mandated to develop and manage the Kabaale Industrial Park (KIP), a petro-based industrial park which is located near the Albertine Graben Region. This park will accommodate the following: Uganda's second international airport, construction is on-going; the refinery; the crude oil pipeline hub; polymer and fertilizing industries; agro-processors; warehousing and logistics; to mention but a few (UNOC, 2020a).

All these operations mentioned above are projects that need financing and since UNOC is fully owned by government, all the financing or participating interests are to be financed by government. Government of Uganda has a number of financing options namely; domestic revenues, grants, loans both domestic and external.

2.2 Public Investment Management in Uganda

A diagnostic study was carried out on Uganda's Public Investment Management System (PIMS) in 2016 and it was observed that a comprehensive framework for project review and approval was needed. Before projects set to be implemented that particular year were only reviewed and approved and there was no inventory of Bankable Projects. Since then, significant progress has been made in strengthening PIMS in Uganda. The Ministry of Finance, Planning and Economic Development (MoFPED) has taken steps to ensure that it keeps track of government's public investments that require budget resources. Some of the steps include setting up Development Committee guidelines and the setup of the Development Committee that is mandated to review projects under preparation and to ensure that projects that get approved have a high rate of return and are beneficial for the development of Uganda at large (IMF, 2019).

Before a project can access loan financing, it must follow the Public Investment Management System (PIMS) Framework. The project needs to be agreed to by the Sector Working Group (SWG) which is comprised of the technocrats within the sector and Development Partners. Once the SWG clears, the project concept is then forwarded to the Development Committee (DC) that is chaired by MoFPED with clarity on the objectives and its alignment to the National Development Plan (NDP). Usually at this point, the potential financier has been identified. Once DC clears the project and appraisals are done, then MoFPED prepares for negotiation of the financing terms with the identified partner.

The draft financing agreement is shared with MoFPED and MoFPED assembles the team to be part of the negotiations. Before the negotiations with the partner are held, pre-negotiations must take place. Pre-negotiations is only to prepare the government team to have one voice in the negotiations. The next step after negotiations are completed is the Financing Partner's Board Approval. After all the above is completed, the draft terms need clearance from Cabinet and approval by The Parliament of Uganda. This whole process can take between 6 months to one year (GoU, 2018).

3. Statement of the Problem

UNOC has several projects that require immediate cash for investment. Since it is fully owned by the Government of Uganda (GoU), UNOC's funding and operations are similar to a Ministry or department. Any projects under UNOC therefore need to follow the PIMS process for approval before funding of the project can be realized.

Given UNOC's mandate to handle government's commercial interests in the oil and gas sector, there is need for immediate access to funds to cater for it participating interests in the joint ventures. Any delays to answer to these cash calls, usually within a period of five days, attracts penalties and dilution of rights when in default. All funds that are generated from oil and gas operations are immediately paid into the Petroleum Fund, which UNOC does not have access to. According to the Public Finance Management Act (2015) as enacted, the funds from the Petroleum Fund can only be withdrawn under Appropriation from Parliament and a warrant of the Auditor General to support the government annual budget as well as to the Petroleum Revenue Investment Reserve for investments (GoU, 2015; GoU, 2019a).

In FY 2019/20, Members of Parliament called for increased funding to the UNOC for it to cater for the government's equity in the oil and gas projects. This limitation in funding hinders UNOC to carry out its role for state participation in its projects, for example Kampala Storage Terminal, East African Crude Oil Pipeline and Kabaale Industrial Park. All revenues from oil and gas projects go to the Petroleum Fund which UNOC does not have access to (GoU, 2019; allAfrica, 2019). Given that the approval process for projects takes a minimum period of 6 months, this will subject UNOC or the government to huge penalties. Since UNOC also doesn't have immediate access to the Petroleum fund also hinders its work. It has to rely on what has been appropriated for it by Parliament and this is detrimental to the commercial interests of government.

4. Recommendations

MoFPED and GoU need to devise means to provide timely funding for these oil and gas projects as they have a high return on investment and are beneficial to the economy at large. One of these ways is to:

- Prioritize the funds in the Petroleum Fund especially the Petroleum Revenue Investment Fund for the projects under UNOC. UNOC projects should take a first call on those funds as they have a high return on investment. This would also be a way of saving funds for the future generation as they would be re-invested in the oil and gas sector;
- UNOC should be treated as a private company and not to follow bureaucracy tendencies of government. If a decision has to be made in a day or less than a week, which is usually the case for commercial projects, then processes like PIMS and approvals from Parliament will delay investment decisions and potential financiers will not be that patient as well as the penalties that come with delays in fulfilling any cash calls; and
- Government should find a longer lasting solution for funding UNOC operations and this should be embedded within the law. Once legal framework is in place for the financing of UNOC operations, this will then give UNOC the leeway to focus on protecting government's interest. It goes without saying that UNOC will and should still be subjected to regular audits to ensure no misuse of funds.

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