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OIL AND GAS LAWS IN UGANDA:

A Legislators' Guide

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We have been working in Uganda since 2007 using research, dialogue and advocacy approaches to promote peaceful recovery of Northern Uganda; positive outcomes from oil discoveries; and a peacebuilding role for Ugandan business leaders.

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OIL AND GAS LAWS IN UGANDA: A LEGISLATORS' GUIDE

Foreword

The current phase of oil exploration in Uganda offers a unique and exciting chance to alleviate poverty and create broad-based development and improved standards of living across the country. At the same time, many Ugandans are well aware that much has been written and discussed about the “resource curse”.

In July 2010 International Alert, a peacebuilding NGO operating in Uganda since 2007, together with the Greater North Parliamentary Forum, convened around 40 MPs to dialogue with central government, as well as oil companies and civil society, about current developments in the sector. As discussion turned to the anticipated new legislative framework, Alert was requested by participants to commission a simplified guide for legislators setting out the main provisions of the proposed framework, and how these differ from existing provisions.

Oil and Gas Laws in Uganda: A Legislators’ Guide is our response to that recommendation. Written by a lawyer with particular expertise on oil and gas developments in Uganda, the guide has been reviewed by a number of parliamentarians and civil society organisations, as well as other experts. Given that Uganda’s new oil and gas legislation is expected to be presented in the first session of the 9th parliament, following the 2011 parliamentary elections, it is our hope that this publication will serve as a helpful tool for incoming legislators as well as incumbents, as they take up their historic task of developing Uganda’s regulatory framework for its nascent oil industry.



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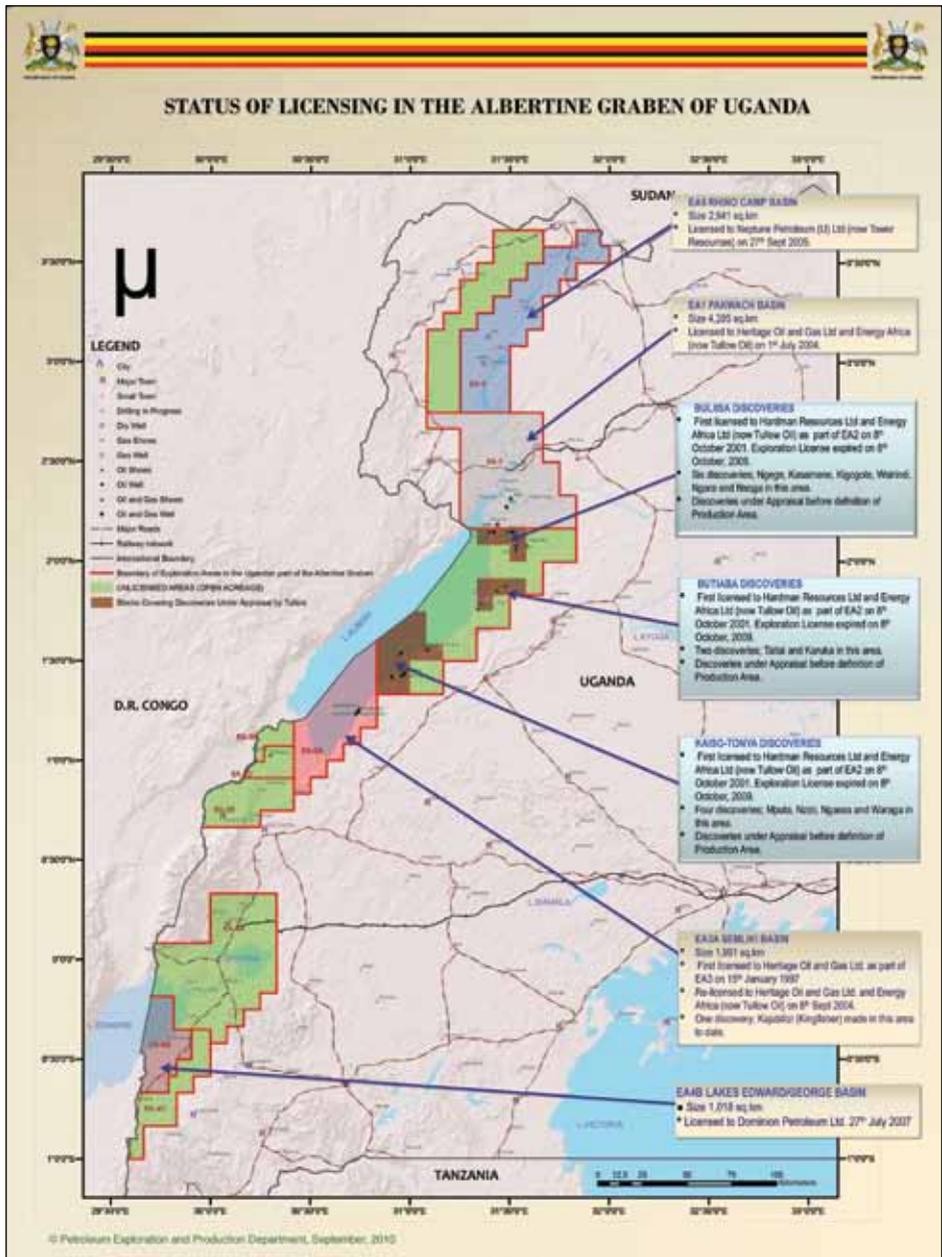
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Contents

Map of exploration areas	5
Acronyms	6
1. Introduction	7
1.1 A Constitutional Responsibility	8
1.2 International Guidance for Legislators	9
1.3 Challenges in Exercising Parliamentary Role	10
2. Uganda's Oil and Gas Legislation: Summary of Existing and Proposed New Laws	13
2.1 Resource Management and Administration	15
2.1.1 Relevant aspects of the Bill	16
2.1.2 International best practice	21
2.1.3 Resource management and administration advocacy points	24
2.2 Revenue Management	26
2.2.1 Relevant aspects of the Bill	27
2.2.2 International best practice	29
2.2.3 Revenue management advocacy points	35
2.3 Environmental Management	37
2.3.1 Relevant aspects of the Bill	40
2.3.2 International best practice	41
2.3.3 Environmental advocacy points	42
Further Reading	46

Map of exproation areas



Acronyms

CSCO	Civil Society Coalition for Oil in Uganda
CSOs	Civil society organisations
EBI	Energy and Biodiversity Initiative
EIA	Environmental Impact Assessment
EITD	Extractive Industries Transparency Disclosure Act
EITI	Extractive Industries Transparency Initiative
EPs	Equator Principles
IFC	International Finance Corporation
ISODEC	Integrated Social Development Centre
ITA	Income Tax Act
MoFPED	Ministry of Finance, Planning and Economic Development
NATOIL	National Oil Company
NEMA	National Environment Management Authority
NFA	National Forestry Authority
NGO	Non-governmental organisation
NOGP	National Oil and Gas Policy
NRC	Natural Resource Committee
PFOG	Parliamentary Forum on Oil and Gas
PPDA	Public Procurement and Disposal of Assets Act
PSAs	Production Sharing Agreements
PWYP	Publish What You Pay
SEC	US Securities and Exchange Commission
UNEP	United Nations Environment Programme
UWA	Uganda Wildlife Authority

1. Introduction

Uganda has been described by the oil industry press as Africa's 'hottest inland exploration frontier'. Exploration is taking place across the entire Albertine Rift in Uganda, with five out of nine oil-prospecting blocks established by the government currently allocated to companies for exploration purposes. Current estimates put the country's oil potential at around 2.5 billion barrels of recoverable reserves from the three blocks that have so far been drilled. Some analysts anticipate Uganda's Albertine Graben may hold more than 6 billion barrels of oil, placing Uganda among the foremost African oil producers. Given the volatility of oil prices, it is difficult to estimate Uganda's likely revenues from oil. Yet, if production goes ahead without hitches, the country's budget looks likely to receive a major windfall – potentially doubling Uganda's revenue base within six to ten years.¹

This boost to national income offers Uganda a unique and exciting chance to alleviate poverty and create broad-based development and improved standards of living across the country. But international experience points to challenges which are often faced by resource-rich developing countries in translating mineral wealth into peace and prosperity. Much has been written about the "resource curse". Developing countries that become reliant on oil and minerals can see a deepening of a range of political, economic and social challenges. In order to ensure the resource will be used to yield lasting benefits to present and future generations, key issues of public debate are:

- The need for a regulatory environment that fosters transparency concerning all revenues and in negotiation and award of contracts;
- The importance of balancing petroleum production with conservation – of the different exploration areas' unique biodiversities, and wider environmental wellbeing;
- Ensuring other sectors of the economy will withstand fluctuating petroleum prices;
- Enforcing high standards of corporate responsibility and compliance on the part of investing companies;
- Ensuring that the anticipation of wealth from Uganda's oil does not intensify land insecurity, sectarian competition and other conflicts; and
- Building public participation and capacity to understand the new sector.

Tackling the above issues requires sound policy leadership at all stages. A wide range of stakeholders needs to work together for this to happen: government technocrats and

¹ World Bank (2010). *Country Assistance Strategy for the Period FY 2011–15*. p.60.

politicians, local government officials, law-enforcement agencies such as the judiciary and police, international and national civil society organisations (CSOs), the media, opinion leaders, traditional institutions and religious leaders, companies, as well as development partners.

Among all these, parliament has a pivotal responsibility fulfilling its function of representing all the above actors and its constituents (wider society) in shaping public policy; enacting relevant and effective legislation; providing checks and balances on the executive's performance; overseeing policy implementation; and advocating for Ugandans' long-term interests.

1.1 A Constitutional Responsibility

Article 77(1) of the 1995 Constitution of Uganda (the Constitution) establishes the parliament of Uganda, vesting parliament with powers to make laws on any matter for the peace, order, development and good governance of Uganda. Article 79 goes on to specify the following duties:

- (a) Protect the Constitution and promote the democratic governance of Uganda;
- (b) Give legislative sanction to taxation and acquisition of loans, in order to finance the work of government; and
- (c) Scrutinise government policy and administration, and approve presidential nominations for ministers, judges, ambassadors and other positions specified in the Constitution.

Legislators are further tasked to represent constituent interests under Article 38(1) of the Constitution which provides that 'every Ugandan citizen has the right to participate in the affairs of government, individually or through his or her representative in accordance with the law'.

Box 1. Parliament's Role

Parliament's role can be summarised as threefold: **legislation**, **oversight** and **representation**. *Legislation* is about passing the laws which constitute a country's legal framework. *Oversight* is about keeping an eye on the activities of the executive, and holding the executive to account on behalf of citizens. A particularly important element of oversight concerns the budget, checking that spending decisions are in line with national priorities. *Representation* is about collecting, aggregating and expressing the concerns, opinions and preferences of citizen-voters.

To exercise their legislative powers, MPs can:

- Introduce legislation (a private member bill) to address specific issues; and
- Review, debate and amend government bills presented by the executive branch and introduced for debate by the majority caucus.

According to the 2008 National Oil and Gas Policy² (discussed in further detail below), the specific role of parliament in Uganda's petroleum sector is:

- To enact petroleum legislation;
- To enact the proposed legislation for the management of petroleum revenues; and
- To monitor performance in the petroleum sector through policy statements and annual budgets.³

1.2 International Guidance for Legislators

A number of international policymaking and advocacy institutions have issued guidance on how parliamentarians in different countries can fulfil their responsibilities to promote positive outcomes from natural-resource exploitation.

Box 2. International Guidance for Legislators on Influencing Extractive Industry Management

EITI Guide for Legislators: How to Support and Strengthen Resource Transparency

Legislators need to know what the extractive industries pay and what governments receive, and the Extractive Industries Transparency Initiative (EITI) (discussed in further detail below) can help. EITI is a simple idea that can shed light on the income generated from oil, gas and minerals. In EITI, companies disclose the payments they make to governments, and governments reveal the income they receive. Identifying discrepancies between the two can be a powerful deterrent to corruption and a vital step towards accountability. Legislators can play several critical roles in making sure EITI is established and works effectively, and this guide shows how. Its first objective is to introduce the EITI process. The second is to offer specific suggestions about how a legislator may contribute to the EITI process in any particular country.⁴

² Available at <http://conserveuganda.files.wordpress.com/2010/06/national-oil-and-gas-policy-for-uganda.pdf>

³ Chapter seven spells out the roles of various institutions including parliament.

⁴ EITI (2009). *EITI guide for legislators: How to support and strengthen resource transparency*. Available at http://eiti.org/files/MP_EITI_Guide.pdf

Natural Resource Charter

The Natural Resource Charter is a global initiative designed to help governments and societies effectively harness the opportunities created by natural resources. It sets out 12 overarching principles, with related guidance, on how this can be done. The Charter has been proposed by an independent group of the world's foremost experts in economically sustainable resource extraction, assembled by Paul Collier, Director of the Centre for the Study of African Economies at Oxford University.⁵

Transparency and Accountability in Africa's Extractives: The Role of the Legislature *National Democratic Institute (NDI)*

This report is an effort to help elected political officials – particularly those in the legislative branch of government – serve as constructive leaders in improving the oversight and management of their countries' natural resources. It highlights effective policies, structures and techniques for monitoring extractive industry revenue flows. The report identifies the challenges that African legislators face in overseeing their countries' oil and mining industries, as well as best practices in use around the world and recommendations for future engagement.⁶

World Bank Institute's (WBI) Parliamentary Strengthening Learning Program

The WBI's Parliamentary Strengthening Learning Program has developed a series of 13 learning modules for parliamentarians and parliamentary staff, which can be used in self-paced, online and face-to-face learning platforms. The main objectives of these learning modules are to strengthen the capacity of parliaments to oversee the allocation and use of public funds, reduce poverty, improve public participation in the policy process and reduce corruption, among others. Issues of extractive industries governance are included in the series.⁷

1.3 Challenges in Exercising Parliamentary Role

Despite the important role provided for legislators in the Constitution, Uganda's parliamentarians may face challenges that are common in many countries around the world in discharging this function. Parliaments can come under pressure from the executive to move legislation forward quickly due to the prevailing political context, limiting the available time for debate and scrutiny. Given the technical issues implied in the aspects of policymaking relevant to the oil sector, and how new this debate is

⁵ See www.naturalresourcecharter.org

⁶ NDI (2007). *Transparency and accountability in Africa's extractives: The role of the legislature*. Available at http://www.ndi.org/files/2191_extractive_080807.pdf

⁷ See <http://parliamentarystrengthening.org/>

in Uganda, legislators face a further challenge in developing the necessary expertise as quickly as possible to achieve meaningful oversight.⁸ In cases where the ruling party has a large majority in the house, parliamentarians may struggle to exercise an independent voice where parliamentary and constituents' perspectives differ from that of the executive. At times, parliamentarians may find themselves excluded from the details of contracts between the government and oil companies, as a result of confidentiality clauses – or misunderstandings about these, as has been the case with Uganda's Production Sharing Agreements (PSAs) over the past few years.

Box 3. PSAs and Parliament

PSAs are a common type of contract signed between a government and a resource extraction company (or group of companies) concerning how much of the resource extracted will be received by each of the company/companies and the government. They often contain detail on initial fees and payments made by companies to the government.

In July 2008 the 8th parliament's Natural Resource Committee (NRC) received copies of the PSAs signed by that time between oil companies and the government, but did not move to disseminate these more widely – nor, according to some accounts, were the critical documents shared across all members of the NRC. The government argued that the PSAs contained confidential information that would reduce its negotiating position on subsequent blocks if released. Some critics and observers stated that the terms of the early agreements signed were not favourable to the government.⁹ At least three cases have been filed in court over this issue, with media and non-governmental organisation (NGO) complainants seeking access to documents.¹⁰

8 In a recent survey, concerns were raised about the capacity of legislators to understand and contribute to extractive sector and management, in part due to educational qualification and in part due to high turnover of representatives. See NDI (2007). *Op. cit.*

9 Credit Suisse, a private bank; Ernst and Young, an audit firm; and the Civil Society Coalition for Oil (CSCO) in Uganda, an NGO coalition, share this view – as summarised in World Resources Institute (WRI) (2011). 'Avoiding the resource curse: Spotlight on oil in Uganda'. *Working Paper*. Available at http://pdf.wri.org/working_papers/avoiding_the_resource_curse.pdf

10 *Ibid.*

Members of the NRC requested and secured a meeting with the Ministry of Energy and Mineral Development which took place in April 2009 in Entebbe, seeking clarification on a number of issues including the PSAs, as well as the new legislation. Members of the recently formed Parliamentary Forum on Oil and Gas (PFOG) have also lobbied for these to be shared, with 19 MPs signing a petition for release of information on the five PSAs in effect by 2010.

The discovery of oil and gas in Uganda presents a unique opening for legislators to establish themselves as credible actors providing critical input in leading the country towards transparent management of these resources. Even in countries where the ruling party may dominate the house, parliament should never be used to rubber stamp executive policy. Legislators themselves must engage in efforts to raise their own capacity to assume this task, make use of the constitutional powers available to them and build the resource base necessary for them to fulfil their responsibilities. They are among the key drivers in harnessing oil for peace and development in Uganda.

2. Uganda's Oil and Gas Legislation: Summary of Existing and Proposed New Laws

In February 2008 Uganda's Ministry of Energy and Mineral Development published the National Oil and Gas Policy (NOGP), which explicitly recognises many of the challenges associated with natural-resource wealth, including the need to mitigate the potential for negative economic and fiscal impacts that often stem from a sudden influx of revenue in the extractive industry sector.¹¹ The NOGP outlines internationally recognised mechanisms for managing such impacts, with the aim of turning finite oil wealth into sustainable development outcomes. It also highlights the need for a long-term national strategy to ensure optimal impacts from oil and gas exploitation by maximising benefits to Ugandans along the industry "value chain".

The overarching goal of the policy is that oil and gas development in Uganda will 'contribute to early achievement of poverty eradication and create lasting value to society'. In particular, the NOGP concurs with the emerging global consensus on the critical importance of transparency in handling all aspects of natural-resource management, with transparency and accountability towards stakeholders enshrined as a guiding principle in Uganda's future governance framework:

*'Openness and access to information are fundamental rights in activities that may positively or negatively impact individuals, communities and states. It is important that information that will enable stakeholders to assess how their interests are being affected is disclosed. This policy recognises the important roles different stakeholders have to play in order to achieve transparency and accountability in the oil and gas activities. This policy shall therefore promote high standards of transparency and accountability in licensing, procurement, exploration, development and production operations as well as management of revenues from oil and gas. The policy will also support disclosure of payments and revenues from oil and gas using simple and understood principles in line with accepted national and international financial reporting standards.'*¹²

The NOGP is a very important document and sets a high standard for the future governance of oil in Uganda. It is, however, more a set of principles than a detailed governance guide. The focus of government has since been on developing new

¹¹ Available at <http://conserveuganda.files.wordpress.com/2010/06/national-oil-and-gas-policy-for-uganda.pdf>

¹² NOGP, section 5.1.3.

legislation implementing the NOGP across different areas of policy by creating new and adding to existing legal frameworks.

The laws that currently exist specifically to regulate both upstream and downstream petroleum activities in Uganda are outdated, having been enacted at a time when large-scale exploration and production activities were not envisaged in Uganda. They include:

- 1985 Petroleum (Exploration and Production) Act, Chapter 150 laws of Uganda
- 5th of December 1957, Petroleum Act Cap 149
- Petroleum Supply Act of 2003.

These laws are accompanied by subsidiary regulations or statutory instruments, such as:

- Statutory Instrument No. 150—1, the Petroleum (Exploration and Production) (Conduct of Exploration Operations) Regulations
- Statutory Instrument 149—1, the Petroleum (Spirit) (Licensing, Testing and Possession) Rules
- Statutory Instrument 149—6, the Petroleum (Spirit) (Marking) (Approval of Marker and Prescription of Fees) Notice.

Oil and gas management cuts across policy areas of taxation and revenue management, government accountability, corporate regulation, environment, land security, etc., so it is important to recognise that there are other existing laws relevant to the overall framework for managing the new sector. In addition to the Constitution itself, these include:

- Land Act, 1998
- Access to Information Act, 2005
- National Environment Act, chapter 153
- Investment Code Act, chapter 92
- Penal Code Act, chapter 120
- Income Tax Act, 2002
- Wildlife Act, chapter 200
- National Forestry and Tree Planting Act, 2003
- Public Health Act, chapter 281
- Water Act, chapter 152
- Public Procurement and Disposal of Assets Act.

Following publication of the NOGP in 2008, and in order to update and amend the law regulating oil activities in Uganda, the Petroleum (Exploration, Development, Production and Value Addition Bill (the Bill) was approved by cabinet in 2010, and is expected to be tabled before parliament during 2011. A complementary revenue management policy is soon to follow (although, as this document went to print, a precise timeframe has not been confirmed), and is currently being devised by the Ministry of Finance, Planning and Economic Development (MoFPED).

The remainder of this guide reviews the legal provisions related to oil and gas under the key broad policy clusters of:

- (1) Resource management and administration;
- (2) Revenue management; and
- (3) Environment.

Each section includes information about international best practice, concluding with key advocacy points arising from the discussion for parliamentarians engaging in the development of the new legislation due to be tabled before parliament this year.

2.1 Resource Management and Administration

The foundation for effective resource management and administration of Uganda's oil and gas is the Constitution, which provides for the protection of natural resources, including water, wetlands, minerals, oil, fauna and flora, on behalf of the people of Uganda.¹³

In 2005 the Constitution was amended to the effect that control of all minerals and petroleum in or under any land or waters in Uganda is vested 'in government on behalf of the republic of Uganda'.¹⁴ Even with this new amendment, the Constitution still re-echoes the public trust doctrine, whereby natural resources are held by the government in trust for its people; or, in other words, envisaging people as the principals appointing the government to manage resources on their behalf. This relationship obliges the government to account to its people as principals/owners, ensuring they participate in the management of their affairs either by themselves or through elected representatives. The Constitution gives parliament a mandate to pass laws for regulating the exploitation of minerals and petroleum; the sharing of royalties

¹³ Objective no. 13 of National Objectives and Directive Principles of State Policy.

¹⁴ Article 244 of the Constitution was wholly replaced by section 43 of the Constitution Amendment Act number one of 2005.

arising from oil exploitation; the conditions for payment of indemnities arising out of exploitation of petroleum and minerals; and the restoration of derelict lands.¹⁵

Petroleum activities are regulated by the 1985 Petroleum (Exploration and Production) Act (the Act), which was enacted to make provision for the exploration and production of petroleum.

2.1.1 Relevant aspects of the Bill

This section identifies new aspects of the Bill.

Overview

By section 2(1), the purpose of the Bill is to operationalise the NOGP, and to a large degree it follows the guidelines and principles set out in the NOGP. However, there is some omission, related, for example, to its assertion of the need for national participation, the importance of transparency and accountability, and environmental conservation, which are highlighted in the relevant sections below. Some expert commentators on the Bill have also recommended separating out the component parts into different pieces of legislation to assist with clarity.

Ownership of oil

Ownership of petroleum in its natural condition is still vested in the government on behalf of the republic of Uganda in the Bill, as was also the case in the Act.¹⁶ Going beyond section 2 of the Act, however, the Bill explicitly prohibits any petroleum activity without due authorisation, and penalties are harsher, levying a fine of 10,000 currency points or 10 years' imprisonment or both for individuals, and 100,000 currency points for a corporate entity.¹⁷ Whereas these penalties could be a deterrent, the language used in the Bill is still *'is liable'* rather than *'shall'* or *'sentence not less than'*, which gives room for the punishing levying authority to impose any fine below the prescribed maximum.

Institutional arrangements

The NOGP recognises the need to enhance the current institutional framework for effective exploration, development and production of oil and gas, and optimum national participation in oil and gas activities. Three separate institutions are proposed in the NOGP:

- An oil and gas policymaking and monitoring body (a Directorate of Petroleum in the Ministry responsible for oil and gas);

¹⁵ Section 43(2) of the Constitution Amendment Act.

¹⁶ The Bill, section 5.

¹⁷ According to schedule one of the Bill, a currency point is equivalent to 20,000 shillings.

- A regulatory agency (transforming the current Petroleum Exploration and Production Department into the Petroleum Authority of Uganda); and
- A separate commercial entity (the National Oil Company (NATOIL)).

As anticipated in the NOGP, the Bill establishes a new Petroleum Authority as a body corporate with perpetual succession and an official seal with capacity to sue and be sued in its corporate name.¹⁸ The powers of the Petroleum Authority include monitoring and regulating exploration, development and production; processing; transportation; and storage of petroleum and gas in Uganda. Its functions include:

- a) Participating in the negotiation and administration of petroleum agreements;
- b) Assisting with assessment of licensees and operators;
- c) Assessing of field development plans and making recommendations to the Minister;
- d) Measurement of petroleum to allow for estimation and assessment of royalty, production bonuses and profit petroleum due to the state;
- e) Ascertaining the cost oil due to licensees and ensuring that licensees uphold laws, rules and contract terms; and
- f) Contribution to national (budgetary) planning and control, etc.¹⁹

The Petroleum Authority is to be independent in the performance of its functions and duties and exercise of its powers, and shall not be subject to the direction or control of any person or authority. However, the Minister of Energy and Mineral Development (the Minister) has power to give directions in writing to the Petroleum Authority with respect to the policy to be observed and implemented, and the Petroleum Authority is supposed to comply with those directions.²⁰ The Minister also appoints members of the board of directors among whom he or she can appoint a chairperson; yet it is the same board that is mandated to oversee the operations of the authority.²¹ It further appears that there is no clear separation of roles and responsibilities between the board and the authority, because the board can, by instrument, delegate to an officer of the Petroleum Authority any of the powers, duties or functions of the board.²²

As also envisaged in the NOGP, the Bill establishes NATOIL, with the responsibility to manage, on behalf of the state, the commercial aspects of petroleum activities and the participating interests of the state in the licences. NATOIL is to be incorporated under and managed in accordance with the Companies Act.²³ However, the Bill does

¹⁸ The Bill, section 9.

¹⁹ *Ibid.*, section 10.

²⁰ *Ibid.*, section 13.

²¹ *Ibid.*, section 23, lists functions of the board.

²² *Ibid.*, section 25(1).

²³ *Ibid.*, section 42.

not detail its mandate or organisational structure any further. Other than the brief reference to “participating interests” by setting up NATOIL, there is no provision at all for government participation.

Rather than having one commissioner as was provided for in the Act, the Bill establishes two. The Commissioner for Petroleum Exploration, Development and Production will be responsible for facilitating and assisting in policy development, promotion and licensing of exploration, development, production and transportation of petroleum up to off-take points. The Commissioner for Petroleum Processing, Transportation and Storage will facilitate and assist in policy development, promotion and licensing of the processing, transportation and storage of petroleum and gas processing. He or she should also draw a future utilisation plan that outlines the utilisation of petroleum and the development of required facilities.

However, the Bill does not state the relationship between the office of the commissioners and the Petroleum Authority – and/or the Ministry. Yet, in the absence of a clear mandate, there is a risk that the system could create unnecessary duplication or bureaucratic delays, and multiply the potential for bureaucratic competition, corruption or mismanagement.

Issuing petroleum licences

As was also the case in the Act, the Minister has wide latitude to issue a petroleum exploration licence, but, rather than four years stated in the Act, the licence period in the Bill is shortened to two years, though can still be renewed for up to a further two years. The Bill does not clearly state whether the Minister should always seek advice from the commissioners and the Petroleum Authority in case of issuing licences, etc. Under section 62(2) of the Bill, the Minister shall not renew a petroleum exploration licence where the licensee has violated any of its provisions or a condition of the licence. This is different to the Act, which gives the Minister power to consider special circumstances for renewal even where the licensee is in breach. Similarly, the Minister has power to issue a petroleum production licence; but the grant does not exceed a period of up to 15 years and is renewable for a period not exceeding 5 years, compared to the 25 years non-stated period for renewal stated in the Act.

No provision exists in the Bill for competitive bidding. Sections 57 and 64 establish that exploration and production licences, respectively, can be awarded via direct applications to the Minister. Yet the award of blocks via competitive auctions would give the government a better opportunity to assess the pros and cons of various applicants for a licence, and thus could result in a better overall deal for the country.

The Public Procurement and Disposal of Assets (PPDA) Act asserts that bids have deadlines, and are open to public view. Following the approach of the PPDA in the Bill would help dispel suspicion and raise public trust in the bidding process.

Requirements of licensees – national content, compensation, health and safety

The Bill also covers aspects of state participation and national “content” (involvement in the sector). The government may participate in petroleum activities through a specified share of a licence, permit or contract and by a joint venture. Furthermore, the licensee, its contractors and subcontractors must give priority to competent citizens of Uganda and registered entities owned by Ugandans in employment opportunities and for provision of goods and services. Licensees are also required to recruit and train Ugandans in their petroleum operations, and to offer scholarships and direct financial support for education.²⁴ However, specific levels of Ugandan content across these areas are not stated explicitly.

The Bill makes certain provisions concerning social issues, including on compensation that may arise from development of the sector; however, these are not fully elaborated. Moreover, the Bill deals exclusively with situations of private land ownership, without addressing the reality that a large part of land in the Albertine Rift is communally owned and subject to traditional rules related to its disposal and use.

Sections 144 to 155 deal with health and safety. The licensee is required to comply with public health and safety standards, as well as emergency standards that deal with accidents and emergencies which may lead to loss of life or personal injury, pollution or major damage to property.

Beyond the basic legal requirements on environment, health and safety and local content, the Bill does not specifically refer to companies’ corporate social responsibility practices.

Role of parliament

Article 119(5) of the Constitution provides that, in agreements where the government is a party, the Attorney General must provide legal advice; and Article 119(6) states that, where foreign entities/companies are involved, the Attorney General must give advice. Under the Act, there was no provision requiring parliament to give approval to oil contracts involving either domestic or foreign companies. The Bill does not address this gap; on the contrary, parliament is remarkably absent across the different sections on institutional arrangements, licensing, development and production, etc. This is a major challenge that requires urgent rethinking.

²⁴ *Ibid.*, sections 127 to 130.

Access to information

Under the Act, while the state has the power to get any information or data relating to exploration or development operations from any individual or institution, no information furnished, or information in a report submitted, by a licensee can be disclosed to any person who is not a government minister or an officer in the public service except with the consent of the licensee.²⁵ Releasing such information is actually an offence punishable by a fine of 5 million shillings or two years' imprisonment or both.

However, subsequent to the Act, the Constitution provides that every citizen has a right of access to information in the possession of the state or any other organ or agency of the state except where the release of such information is *likely to prejudice the security or sovereignty of the state or interfere with the right to the privacy of any other person*.²⁶ In 2005 the Access to Information Act was enacted, section 5 of which re-echoes the above constitutional provision. The limitation with this law is that it restricts release of information perceived to put a third party at a contractual or commercial disadvantage; in the case of the oil sector, this could imply protection of oil companies over the ability of citizens to participate in the oversight of petroleum activities.²⁷

According to section 156 of the Bill, in accordance with the 2005 Access to Information Act, the Minister must make available to the public:

- (a) Details of all agreements, licences and any amendments to the licences or agreements whether or not terminated or valid;
- (b) Details of exemptions from, or variations or suspensions of, the conditions of a licence;
- (c) The approved field development plan; and
- (d) All assignments and other approved arrangements in respect of the licence.

The information is available upon payment of the required fee. It is also subject to confidentiality of the data and commercial interests – raising questions as to its actual availability. And sections 153 and 155 also itemise certain information related to a licence to be held by the licensee ‘at an address in Uganda notified to the authority’ – implying that relevant information may not actually be held by the state, which could mean accessibility may not apply. Further, all data submitted to the government by a licensee shall be kept confidential and shall not be reproduced

²⁵ Section 59.

²⁶ Article 41 of the Constitution.

²⁷ Section 27(c) (1) of the 2005 Access to Information Act.

or disclosed to third parties by any party. If the government is to disclose such information, the licensee must consent and vice versa. Penalties for releasing information – which are set out in section 165 – go far beyond what is allowed in other countries and, arguably, as with the Official Secrets Act, provide an incentive to officials to always err on the side of caution in withholding information from the public.²⁸

Even with such information being accessed, there remains a challenge in ensuring that Ugandans – the majority of whom may be illiterate or have only basic English, if any – are able to be included in its dissemination and debate. This highlights quite how important the function of parliament becomes, with a particular need for MPs to advocate for the translation of relevant laws and provisions into local languages.

2.1.2 International best practice

Available guidance states that investments in the oil and gas sector should be explicitly tied to a country's national development strategy; ensure transparent procurement and financial management for particular projects; favour development of the non-oil economy in order to counteract Dutch Disease; and mitigate negative economic, social and environmental impacts of oil development.

The Dutch Disease syndrome has been evident in Nigeria, Equatorial Guinea and Angola, and is especially felt in economies that are otherwise dependent on agriculture. Nigeria was a net exporter of food before the discovery and exploitation of oil and gas. Once oil started to flow, Nigerian agriculture took several steps back. Uganda should learn from this and consciously invest a specific percentage of revenue to improve research, teaching and other vital inputs in agriculture.

Box 4. What is the “Dutch Disease”?

The Dutch Disease occurs when oil windfalls push up the real exchange rate of a country's currency, rendering most other exports noncompetitive. At the same time, persistent Dutch Disease provokes a rapid, even distorted growth of services, transportation, and construction, while simultaneously discouraging some industrialization and agriculture. Agricultural exports – a labor-intensive activity particularly important to the poor – are adversely affected by economic dynamics set off by the exploitation of petroleum. The languishing of the agriculture and manufacturing sectors of oil countries not only makes

²⁸ For more detailed discussion on access to information in the Bill, see WRI (2011). Op. cit.

them more dependent on petroleum, thereby exacerbating other problems of dependency, but it can also lead to a permanent loss of competitiveness. Meanwhile, the oil sector cannot make up the shortfall’.

Source: I. Gary and T. L. Karl (2003). *Bottom of the barrel: Africa's oil boom and the poor*. Baltimore: Catholic Relief Services. p.22. Available at http://crs.org/publications/showpdf.cfm?pdf_id=183

For oil to be effectively managed, there should also be a policy environment that encourages national participation. Technocrats and company staff should be hired transparently and on merit, and people should be able to participate either directly or through their elected representatives in managing the oil resource. This implies a far greater role for parliament scrutiny across the stages of oil and gas activity than is currently provided for in the Bill. Relevant policies should be translated and disseminated, with a much greater emphasis on community dialogue and outreach than has hitherto been felt in the sector. There are well-established and tested international guidelines on stakeholder engagement on such issues.²⁹

International discourse on combating the resource curse has recently evolved from its initial prioritisation of revenue management (reviewed below) to a broader concern with good governance along the whole “value chain” of extractive sector development. This extends from the award of exploration rights right through to the implementation of sustainable development policies and projects. A recent World Bank working paper on the extractive industries value chain outlines five steps for improving extractive industry revenue management, transparency and accountability at each link of the value chain.³⁰ The five steps are awarding of contract and licences; regulation and monitoring of operations; collection of taxes and revenues; revenue management and allocation; and implementation of sustainable development policies.

Best practice as set out in the World Bank paper highlights the need for a proper legal, contractual and institutional framework to regulate access to natural resources by investors. Ideally, this should separate commercial activities from the state regulatory function so that any national oil company involved in exploration, production and marketing of oil should be distinct from those bodies performing regulatory functions, such as the energy ministry and petroleum agency. The risks inherent in not separating

²⁹ The Participation and Civic Engagement Group of the World Bank: <http://www.worldbank.org/participation>; International Finance Corporation (IFC) Guidance for Preparation of a Public Consultation and Disclosure Plan: <http://www.ifc.org/enviro/EnvSoc/ESRP/Guidance/guidance.htm>

³⁰ E. M. Alba (2009). ‘Extractive industries value chain: A comprehensive integrated approach to developing extractive industries’. *Extractive Industries for Development Series No. 3, Africa Region Working Paper Series No. 125*. Washington DC: World Bank. Available at http://siteresources.worldbank.org/INTOGMC/Resources/ei_for_development_3.pdf

the commercial functions can be seen in the case of Angola's national oil company, Sonangol. Sonangol is not only the sector regulator responsible for monitoring the operations of other companies (including setting the terms for licensing rounds), it also acts as a fiscal agent for the government (collecting taxes, royalties and profit oil, and making expenditures) and takes part in upstream activities of exploration and production itself. The opacity of Sonangol's finances and the "twin-track" financing system that has resulted from this confusion of roles has had negative effects on Angola's use of the resource.

In addition, although there is no model bidding system of strategy that governments can adopt globally, licensing rounds should ideally be open, competitive and transparent, and bidders should be suitably qualified in terms of technical expertise and financial capability to carry out exploration and production activities. Many countries pre-select or pre-qualify bidders in order to ensure in advance that they are competent, and, again, it is essential that this is done in a genuinely transparent manner so as to prevent abuse. The Natural Resource Charter recommends disclosure of the true beneficial owners of each pre-qualified company so as to 'prevent conflicts of interest and authorities steering business to firms in which they may have a share', for instance. While there is no "one-size-fits-all" model for contracts, setting some bidding parameters in advance (for instance, royalty or other tax and revenue rates, the work programme to be carried out, etc.) usually reduces the government's and investors' transaction costs. Deciding the specific fiscal regime set by the contractual terms will also depend on variable factors, such as market conditions, government policy, and geological and country risks. However, one underlying principle is that, whatever the fiscal regime, it should be "progressive", that is, the percentage due to the government on the basis of tax and other payments increases as the revenue basis increases, so the government's share of the profits increases as the investors' costs of exploration and production are reduced.

Analysts of international best practice recommend that governments try to enshrine as many details of the operational and financial regime governing the petroleum sector into law as is possible, and to leave relatively little open to individual negotiations between the government and extractive companies.³¹ There are two major reasons for this: first, international oil companies have the greatest advantage over national governments during the contract drafting phase; and, second, enforcement of agreements is substantially easier if there is standardisation of key terms. Enforceability is a key concern for countries such as Uganda that are in the early stages of developing administrative capacity in the petroleum sector.

³¹ See, for example, the Natural Resource Charter proposed by a group of international experts to assist societies and governments with new extractive industries. Available at <http://www.naturalresourcecharter.org>

State bodies charged with monitoring the operations of oil companies – for instance ministries of energy, petroleum and exploration departments, national environmental management agencies, etc. – must have clearly defined roles and responsibilities, plus sufficient technical capacity to carry out their roles and be able to coordinate their actions effectively. In addition, development of accurate information on the extractive sector through setting up a national data bank is seen as key to improving transparency, certainty of rights, knowledge of the resource base, and the quality and reliability of government revenue estimates. Norway, for instance, has a “petroleum register” to hold all the data collected by companies for the use of both private and state agencies. It is also important to note that the most successful examples of environmental and social impact mitigation and monitoring involve early consultation and participatory monitoring practices at the local community level.

Building local capacity to engage in the industry through training is also critical – again looking to the example of Norway, within 15 years of discovering oil, they had built Norwegians’ skills through a major national drive on training to see Norwegians at the helm of the industry. Uganda’s new Petroleum Institute should ensure that entry is based on merit, addressing widely believed rumours that it is currently driven according to ethnicity.

2.1.3 Resource management and administration advocacy points

General

There is an urgent need to develop a national debate on how the growth of the oil and gas sector is to be explicitly linked into Uganda’s national development plan, including both the intended use of its likely revenues and planning for mitigation of common negative effects on other sectors such as agriculture and tourism.

Transparency

The provisions in the Bill related to disclosure of information are more restrictive than in the Access to Information Act and should be closely reviewed. Access to information legal best practice would imply that additional exemptions should only be included in a new law, such as the Bill, where they can be justified on the basis of strict necessity set out in the law.

Competitive bidding

The Bill should provide for competitive bidding for contracts, but currently states that these can be awarded via direct application to the Minister. The award of blocks via competitive auctions would enable the government and parliament to assess the pros

and cons of various applicants for a licence, and thus result in a better overall deal for the country. It would also minimise opportunity for corruption. The Bill should enshrine the approach set out in the PPDA Act.

Parliament

The role of parliament in scrutinising new oil developments needs to be clearly detailed in the Bill – currently the Bill does not provide for this. One key recommendation is that all new contracts and lease extensions/renewals should be brought before parliament in all cases, as should appointments to the Petroleum Authority and indeed commissioners. Such checks and balances are essential for ensuring proper management of the oil and gas sector, and for building wider transparency and public confidence.

Institutional arrangements

Proper checks and balances on the powers of the Minister should be articulated in the Bill. This relates both to influence on the Petroleum Authority – which as currently drafted extends to policy directives as well as appointment of the Petroleum Authority's board of directors (which is also responsible for oversight) – and to the actual award of contracts – which in the current drafting rests with the Minister. At the same time, other key responsibilities of the Minister that appear in the NOGP are not fully spelled out in the Bill. These include undertaking resource assessment; initiating, developing and implementing oil and gas policy; negotiating, endorsing and administering PSAs; promoting and sustaining transparency in the oil and gas sector; and ensuring dissemination of information related to oil and gas activities. A separate section on the powers vested in the Minister, as well as the overall Ministry in light of the new institutions proposed under the Bill, included in Part 3 (Institutional Arrangements) would help set these out.

Concerning the Petroleum Authority, there is a need for clearer segregation of the roles and responsibilities between the board and Petroleum Authority staff. There is also a need for clearer articulation of the mandate and organisational structure of NATOIL, as well as clarity on the government's proposed role in its administration – who will be the directors and how will they be appointed, who are the shareholders, etc. And there is a need to clarify the relationship between the two proposed commissioners, and between them and the Petroleum Authority, to avoid future administrative power struggles emerging.

Social impacts

A clause ought to be added to the Bill specifying particular levels of Ugandan citizen and company participation in each category of technical/service provision to help fulfil

the vision of national content. These should be embedded in future PSAs in the form of percentages of participation.

In addition, further clarity on how compensation is to take place is needed, not least given the expectations and rumours currently at large in oil-affected regions on this point. Will market or replacement values be used? What will be the process for compensation and/or settling grievances and complaints? How can compensation and arrangements for exploration be made in instances where land is communally owned? All these issues need to be addressed to ensure that a solid compensation system, which is equitably implemented and addresses health, livelihood and property aspects, can be put in place.

The Bill is also quiet on other benefits, such as community development and infrastructure development. The government should take a lead on these issues and set out guidance on corporate responsibility and wider undertakings of companies in host areas, ensuring that such initiatives are encouraged and, where they take place mandatorily, linked to local government development plans and priorities, ensuring community consultation and zero tolerance on corporate corruption. Corporate social responsibility activities should also be transparently reported on and monitored by the government and civil society. Provisions on company training fees paid to the government should be made more specific to ensure that Ugandans receive training in all aspects of the industry, with clear targets set.

2.2 Revenue Management

In addition to the anticipated benefits from the oil sector in terms of employment and business opportunities for Ugandans, investment capital and abundant fuel for electricity, the major potential benefits to accrue from the industry lie in the revenue streams to be paid by companies and from the sale of oil once production starts. Given current indications, anticipated revenue from oil could double Uganda's revenue base within six to ten years, providing an unprecedented opportunity for public spending on infrastructure; economic productivity-enhancing measures in key sectors such as agriculture, quality education, health, water and sanitation service provision; local government capacity; and town and urban planning. Given experience in other oil-rich countries, these potential benefits may not come to pass unless there is a clear and concise framework ensuring revenues are indeed well managed in the interests of current and future generations.

The relevant current laws governing taxation of oil are mostly to be found in the 1985 Act, the 1997 Income Tax Act (the ITA) and the 2010 Income Tax Amendment Act. The latter amends section 21 of the ITA by clearly stating that the sale of shares in a private limited liability company is not exempt from tax; in other words, clearly introducing a tax obligation on any exploration company that intends to sell its exploration and production rights. Section 4 defines petroleum revenue as income on petroleum operations, government share of production, signature bonuses, surface rents, royalties and other duties and fees payable under the petroleum agreement.

The ITA provides for taxation of the production of petroleum and natural gas. Cost oil and allowable deductible expenditures are ascertained in the ITA. It also provides for the mode of taxing petroleum companies in case the companies transfer their interests to other parties. The ITA lays down accounting principles to be applied in taxing contractors and taxation of cross-boundary shared petroleum resources. Timelines for filing returns and payment of taxes are also stipulated and it is an offence not to furnish returns or to file inaccurate returns, and the fines are quite a deterrent.³²

2.2.1 Relevant aspects of the Bill

The Bill addresses some of the issues required for governing revenue management, and these provisions are discussed in this section. However, it should be noted that these provisions, together with the relevant provisions of the ITA, are far from complete. Further details are expected to be included in the pending revenue management policy that is, at time of writing, still being drafted by MoFPED.

Transparency

As noted above, according to section 2(1), the purpose of the Bill is to operationalise the NOGP. However, as currently drafted, not all values espoused in the policy are, in fact, reflected in the Bill. One important example is the commitment to the EITI – discussed in further detail below – and more generalised statements found in the policy on transparency in the sector, which are not reflected in the Bill. It is critical to the performance of the oil sector that these aspects will instead appear in the revenue management policy.

The Uganda Revenue Authority publishes its monthly revenue collections. MoFPED publishes its monthly releases to districts and other public institutions. Given these transparent and well-established government practices, it should be mandatory for oil and gas companies to publish their revenues regularly, and for the government to publish royalties received from companies in the same way.

³² Section 23 of the 2010 Income Tax Amendment Act.

Fees paid to the government by licensees

In section 61 of the Bill, the holder of a petroleum exploration licence must pay an annual fee in respect of the licence; the Bill further adds that failure to pay the fee will lead to cancellation of the licence. Mandatory disclosure of cooperation agreements by several applicants is provided for; in effect, where two or more applicants enter into a cooperation agreement with a view to applying for a petroleum production licence, the cooperation agreement shall be submitted to the Minister, who may require alterations to be made in the agreements as a condition of granting the licence. This helps in ascertaining the taxable amounts for each of the licensees.

A holder of a production licence shall pay an annual area fee calculated per square kilometre for the acreage held under the licence area.³³ Section 86 of the Bill introduces an annual fee on facilities for gas refining, gas processing, transportation and storage of petroleum, etc. Even after cancellation, surrender of rights or lapse for other reasons, the licensee must discharge his or her financial obligations.

Section 191 gives powers to the Minister to make regulations for the annual charges payable and the fees to be paid in respect of unforeseeable incidences on any matter or thing done.

The Bill does not provide for any sort of progressive revenue collection whereby the state's share of benefits increases as project profitability rises. Progressive systems allow a nation to capture a larger share of rents from oil in times of commodity price booms without regularly renegotiating the contract.

Royalties

Under section 106 of the Bill, the licensee must pay a royalty to the government on petroleum extracted in the form of crude oil and natural gas as well (this differs from the Act which did not specify a royalty on natural gas). In addition, 'the paid royalty is to be shared among central government, regional governments and local governments in an area where petroleum is discovered'. Schedule IV of the Bill prescribes a share of 85 percent for central government and 15 percent for regional and local governments, but no additional information on the sharing of royalties (or how these percentages have been determined) is provided. There is no provision for cultural institutions.

Other payments

There are no suggested or minimum levels set for any of the anticipated payments, which include production share, bonus bids, royalties, tax payments, training budgets

³³ The Bill, section 73.

and land rents. Sections 106 and 159 suggest that many of these key elements are to be determined on a licence-by-licence basis. It is essential that the revenue management policy will also elaborate further, as such details go to the heart of both risk and opportunity in the sector.

Financial risks

Under section 131, the licensee can use his or her share of the licence as part of the financing of the activities associated with the licence. Whereas it is normal for companies to borrow for completion of their projects, default by a licensee runs the risk of having Uganda's oil resources in the hands of overseas financiers.

Provision for auditing

Sections 39 to 41 detail a system of audit and reporting for the Petroleum Authority, but, as petroleum revenues will not be housed in the Petroleum Authority, this provision does not, on its own, provide strong oversight of the funds to be generated by the oil sector.

The above legal provisions form a basis for future direction, but it is critical that the forthcoming revenue management policy follows up to create a detailed and transparent management system. Key recommendations in this regard are included in Section 2.2.3 below.

2.2.2 International best practice

Emerging international norms for good governance of natural resources emphasise good fiscal governance, especially revenue transparency. The key recommendation is that all revenue streams and transactions should be clearly traceable and accounted for in the state budget. Moreover, the state needs to have adequate accounting and auditing capacity to ensure that revenues are collected and managed according to internationally recognised standards of accounting and reporting. Finally, regular public disclosure of revenues is also recommended, along the lines of initiatives such as the EITI.

Box 5. Publish What You Pay and the Extractive Industries Transparency Initiative

Two key and synergistic initiatives – one of which promotes a mandatory approach to revenue transparency and one which takes a voluntary approach – are the international civil society campaign Publish What You Pay (PWYP), launched in 2002, and the multi-stakeholder initiative launched by the UK government in the same year called the Extractive Industries Transparency Initiative (EITI).

PWYP is a global civil society coalition, working with member organisations in over 70 countries, that helps citizens of resource-rich developing countries hold their governments accountable for the management of revenues from the oil, gas and mining industries. As its name suggests, it does so mainly by advocating for mandatory disclosure by extractive sector companies of the payments they make to governments for access to oil, gas and minerals, and of government revenues earned from the extractive sector, 'as a necessary first step towards a more accountable system for the management of natural resources'. Part of PWYP advocacy to achieve this end promotes changes to stock market listing rules requiring extractive sector companies to publish payments to foreign governments on an individual country basis. In 2008 the efforts of the US PWYP coalition in this direction culminated in the introduction of the Extractive Industries Transparency Disclosure Act (EITD) in the US Congress. This is a bill which, now that it has been passed, requires disclosure of payments by all oil, gas and mining companies listed on the New York Stock Exchange, where 27 out of the 30 largest extractive sector companies that operate internationally are listed. PWYP also calls for bilateral and multilateral agencies 'to require public disclosure of revenues and contracts for all extractive industry investment projects, development policy lending, and technical assistance programmes'. More recently, PWYP has moved beyond advocating for transparency in collection and expenditure of revenues to call for public disclosure of extractive industry contracts and for licensing procedures to be carried out transparently in line with best international practice.

EITI was launched in response to PWYP's call for greater extractive sector transparency. It is a voluntary initiative in which participating mineral- and oil-rich governments agree to publish their receipts from oil, gas and mining activities, and extractive sector companies their payments, as a block figure of all company payments per country, leading to an independent reconciliation of the reported figures, with any discrepancies being published and explained. Although participation is voluntary, there are specific steps a government must implement in order first to become a "candidate" and then to reach "compliance" within

two years. Compliance with all six binding criteria of the EITI process is validated independently.

Twenty-five countries are currently candidates of the EITI, though only one (Azerbaijan) has achieved compliance. Many candidates are African resource-rich countries including Cameroon, Congo-Brazzaville, DRC, Equatorial Guinea, Gabon, Ghana, Nigeria and Tanzania. Norway is the only industrialised country that has signed up to implement the EITI. Around 40 oil, gas and mining companies support and participate in the EITI, which is also supported by donor countries such as Canada, France, Norway, the UK and the US, plus the international financial institutions and investors. The EITI has a secretariat based in Norway, an international board and a multi-donor trust fund to finance technical assistance to candidates. CSOs such as PWYP also participate in the EITI, and have lobbied hard for independent civil society participation to become one of the binding criteria of the EITI process, which it now is. CSOs must participate actively in the multi-stakeholder committees implementing the EITI at the national level, and civil society is also represented on the international board. In the four years of its existence, the EITI has achieved global recognition as a revenue transparency standard, and – uniquely for a multi-stakeholder governance initiative of this sort – it has also been endorsed by the UN, G8, G20, AU, OIF and EU.

However, the EITI has also incurred criticism precisely because of its limited, voluntary and non-binding nature, which can mean that implementation depends on the political will of the government in question. In some countries, CSOs have been victims of intimidation, and overall there has been limited progress in countries achieving compliance status. These concerns have led to a renewed effort by the EITI secretariat to increase the robustness of the initiative.³⁴

³⁴ For more information, see www.publishwhatyoupay.org and www.eitransparency.org. For a discussion of some of the limitations on countries achieving compliance status to date, see Oxfam America and Integrated Social Development Centre (ISODEC) (2009). *Ghana's big test: Oil's challenge to democratic development*. Boston: Oxfam America. p.15. Available at <http://www.oxfamamerica.org/files/ghanas-big-test.pdf>. See also 'Civil society protection a priority; other measures needed to complement EITI implementation', PWYP (press release), 17th February 2009. Available at <http://www.publishwhatyoupay.org/en/resources/doha-2009-civil-society-protection-priority-other-measures-needed-complement-eiti-implemen>

Box 6. 2010 US Wall Street Reform Act – Implications for Uganda

In 2010 US President Barack Obama signed into law the Wall Street Reform Act. Towards the end of this 2,300-page Act, there is a provision requiring extractive industry companies registered with the US Securities and Exchange Commission (SEC), to produce annual reports detailing payments made to any foreign government. Companies must be registered with the SEC in order to trade on US stock exchanges.

Twenty-nine of the world's thirty-two largest multinational oil companies and eight of the world's ten largest mining companies are registered and must file annual reports with the SEC – meaning that this provision represents a major victory for campaigners who have long argued for better information disclosure by the corporate sector. The information disclosed about payments to governments will help parliamentarians, media and civil society track these funds and promote accountability in the sector.

Advocates are working to encourage similar legislation to be taken up in Europe. If successful, two of the three most significant oil companies operating in Uganda – Tullow Oil and Total – would be required to start detailing this information. To this end, CSCO in Uganda together with PWYP Uganda recently sent a letter to the UK government stating the case for taking this forward. Some Ugandan parliamentarians have reiterated the argument, with Hon. Banyenzaki having an open letter published on the issue in the UK *Financial Times* in March 2011.

Revenues should be managed in the context of an overarching macro-fiscal framework that recognises the volatility, uncertainty and cyclical nature of their prices, and over time the exhaustibility of oil, gas and mining resources, and ensuring they are linked to national budget processes. All revenue streams and transactions should be clearly traceable and accounted for in the state budget, independently audited and there should be regular public disclosure of revenues, along the lines of initiatives such as the EITI (see Box 5 above). The importance of transparent decision-making over whether revenues are used for current spending, as opposed to setting them aside for expenditure smoothing or saving for future generations, and the importance of good governance in managing any saving or stabilisation are also highlighted. There should also be “rule-based” and transparent criteria for sharing benefits between central and local government.³⁵ The development of mechanisms and policies to

35 E. M. Alba (2009). Op. cit.

enhance transparent collection of revenues from oil, gas and mining activities so that they can be mobilised for development and poverty reduction is key. The rationale for this is that ‘by increasing transparency and public information, civil society groups, journalists and parliaments can play a more active role in “following the money” and building systems of democratic decision-making on how resource wealth should be managed and spent’.³⁶

In considering mechanisms for harnessing oil and mineral wealth for long-term development, experts have explored different “expenditure-smoothing” mechanisms governments can opt for to counteract revenue volatility, and to set aside revenues for future spending, especially post-oil. To date there is some debate as to whether or not this should be done through the establishment of a stability and savings fund for the revenues (as is the case in one model revenue management scheme, the São Tomé and Príncipe Oil Law, see Box 7 below). One expert argues that ‘saving the money into a sovereign wealth fund is wrong for these countries, as their big problem is lack of domestic capital’; though at the same time, ‘neither should the revenues be used in the ordinary state budget because they come from a depleting natural resource. Instead, nations should invest in investing, by increasing the mass of domestic capital available.’³⁷

Others may disagree with this view. As the World Bank’s *Extractive Industries Value Chain* notes, ‘to avoid wasteful expenditure and/or the resource curse, special “oil and mineral funds” have been created in a number of producing countries’. The purpose of such funds can be to smooth expenditures over time or to save revenues “for a rainy day”, to combat the negative impacts of price volatility; to set money aside for future generations; and as an emergencies fund to be drawn on in case of extraordinary events, such as natural disasters.³⁸

The best-known example of such an oil fund was set up in 1990 by Norway; it has now become the country’s pension fund. All oil revenues are channelled into this fund, which is managed by Norges Bank and at the end of 2008 was valued at around US\$330 billion. Around 4 percent (considered to be a normal rate of return) is transferred annually to the state budget. Other examples of countries that have set up stabilisation and/or future generations funds include Timor-Leste and São Tomé.

Whether these saving funds are seen as effective forms of managing revenues or not, there is consensus on how they should be managed, if established. Firstly,

36 Oxfam America and ISODEC (2009). Op. cit.

37 P. Collier (2007). *The bottom billion: Why the poorest countries are failing and what can be done about it*. Oxford: Oxford University Press.

38 E. M. Alba (2009). Op. cit.

there should be transparent oversight procedures, including independent audits, preferably enshrined in a legal framework. Secondly, the fund should be integrated within the state's overall fiscal management, that is, good fiscal discipline should be maintained; and finally, they should have prudent asset management guidelines.

Box 7. Models for Best Practice in Oil Governance: The São Tomé and Príncipe Oil Law

São Tomé and Príncipe's 2004 Oil Revenue Law contains many elements of the best practices outlined above. It is inspired by two explicit underlying principles: the first takes into account the finite nature of oil resources, thereby introducing mechanisms that will allow São Tomé and Príncipe to face the post-petroleum era with minimum economic distress. The second centres on oil revenue management auditing, transparency and oversight mechanisms. São Tomé is also drafting, with the help of experts at Columbia University's Earth Institute, a National Development Plan, which 'will include a range of public investments and policy changes needed for the elimination of poverty on the islands'.

Some of the key elements of the São Tomé and Príncipe Oil Revenue Law are as follows:

- Collection and management of all oil revenues will be centralised through a single National Oil Account. Any deposits made in the Oil Account can only be channelled to the State Treasury Account 'as authorised by the National Assembly'.
- All revenues must explicitly be used for sustainable development and as part of a poverty-reduction strategy. All budgetary and accounting procedures have to be approved by the National Assembly.
- Revenue-sharing between the central government and the Autonomous Region of Príncipe is also defined in law (7 percent annually).
- The law establishes an 11-member Petroleum Oversight Committee 'with independence, and administrative and financial autonomy to ensure its effectiveness', which includes one judge, one representative of the Autonomous Region of Príncipe, one member appointed by the president, three MPs nominated by parliament, including one opposition MP, two members of local government, one representative from business associations, one representative from the unions and one civil society member. This committee has responsibility for overseeing compliance with all aspects of the law and it has wide-ranging oversight and sanctioning powers, including the power to initiate investigations into any irregularities.

- The law stipulates that there must be a debate in the National Assembly every legislative session on general oil policy and on the oil account reports, and public debates will also be organised prior to this by the Petroleum Oversight Committee.
- The law also establishes a permanent fund for savings and stabilisation purposes. There is only one annual transfer from this fund to the state budget, and this amount is defined in law according to certain parameters according to the rate of return on investments, with a ceiling on this amount.
- The fund has an oversight mechanism, the Investment and Management Committee, composed of the planning and finance minister, the governor of the Central Bank, three members appointed by the president and two MPs nominated by parliament, including one opposition MP.
- The fund is to be audited annually not only by the Auditor General's Office, but also independently by a firm chosen by the Petroleum Oversight Committee.
- Transparency is established as the underlying norm of all oil revenue management and there is to be full public disclosure of all data relating to oil resources, and management of oil revenues, including contracts, is enshrined in the law. The law stipulates the establishment of a Public Registration and Information Office, overseen by parliament.
- Confidentiality clauses in oil contracts are null and void. The only exemption is 'information concerning proprietary industrial property rights', but any exemptions must be proven, and exemptions can never apply to 'any financial information'.
- There are specific provisions to safeguard against corruption, including clauses in all oil contracts and other instruments and against conflict of interest. No public office holder can directly or indirectly hold an interest in any oil-related activity. There are also clear sanctions established if this does occur, including confiscation of the value of any economic advantage gained plus a fine.
- There is to be competitive tendering for all oil-related contracts.

Source: J. Sachs, W. Masters, V. Modi, A. Teklehaimanot and the Columbia University Advisory Project in São Tomé and Príncipe 2004, revised 2005. *Towards a consensus plan of action for São Tomé and Príncipe*. New York: Center on Globalization and Sustainable Development, The Earth Institute at Columbia University. Available at http://www.earthinstitute.columbia.edu/cgsd/stp/documents/TowardsConsensusPlanOfAction_000.pdf

2.2.3 Revenue management advocacy points

Revenue management policy needed

It is critical that the new revenue management policy will supplement the basic provisions in the Bill on revenue by setting minimum levels for each of the anticipated

payments, which include production share, bonus bids, royalties, tax payments, training budgets or land rents; clarifying the formula of 85 percent revenue to central government and 15 percent to local government, detailing how these are to be collected, managed and used – and how oversight and audit can be ensured.

Progressive revenue collection

The Bill should provide for progressive revenue collection whereby the state's share of benefits increases as project profitability rises. Progressive systems allow a nation to capture a larger share of rents from oil in times of commodity price booms without regularly renegotiating the contract.

EITI

The EITI offers great potential to ensure high standards on oil revenue transparency in Uganda, both through its institutionalisation of an international peer review mechanism and its insistence on a role for self-selected civil society representatives in scrutinising revenue management. In a context where government is wary of civil society, formalisation of this function through membership of the EITI would bolster the aspirations of Ugandan civil society to perform its critical oversight function, as well as develop its own capacity, and would also contribute to building much-needed public trust.

Saving for the future

The NOGP states the government's intention to 'put in place a sustainable asset in the form of a petroleum fund to store revenues not used in the national economy and creation of a permanent source of wealth as a provision for intergenerational equity' which would be administered by the Central Bank.³⁹ A supplementary policy balancing the use of petroleum revenues between current domestic investment and receipts retained for future use; the terms for management, including the rules for deposits into the fund, investment strategies, withdrawal provisions; and systems for oversight and audit are needed, ensuring regular disclosure requirements for amounts received, on hand and amount spent. There will be considerable monetary problems from sudden inflow of oil revenues into the Ugandan economy. The inflation likely to result will undermine all efforts to improve the life expectations of Ugandan citizens; plus there is the potential corruption and political interference; the fund should be established via an amendment to the Constitution or by legislation that cannot easily be revised by the normal operations of politics.

³⁹ NOGP, 6.2 and 7.2.

2.3 Environmental Management

Oil development can bring great benefits, but it also comes with great risks to the environment as has been seen in oil development zones from the Gulf of Mexico to the Niger Delta. The significance of these risks cannot be overstated, and it is critical that Uganda's legislative framework puts laws in place that will ensure that these risks are minimised. Most of the current foreign exchange earnings and livelihoods come from industries that rely directly on the environment – namely, agriculture and tourism. If oil development is undertaken in a way that compromises the natural endowment of Uganda, the short-term gains will be more than offset by long-term losses.

The Albertine Rift is the most bio-diverse region of Uganda and, in fact, one of the most species-rich areas in the world. It is frequently identified as a globally important area for conservation, and is Uganda's largest draw for tourism, hosting more species than any other area on the continent, including the rare mountain gorilla. Some scientists have estimated that the region is home to 30 percent of Africa's mammal species, 51 percent of its bird species, 19 percent of its amphibian species and 14 percent of its plant and reptile species.⁴⁰ Most of the oil exploration is taking place in protected areas. Fishing and agriculture throughout the Rift are also critical economically and socially and are completely reliant on healthy, non-polluted ecosystems.

Contamination of the Albert Nile must also be protected against, as it would have far-reaching political ramifications due to the impacts on downstream nations – where interstate relationships are already strained.

The Constitution obliges the state to ensure that natural resources are managed in such a way as to meet the development and environmental needs of present and future generations of Ugandans. The state is charged with promoting and implementing energy policies that will ensure that people's basic needs and those of environmental conservation are met. By article 237(2)(b) of the Constitution, the government or a local government holds in trust for the people and protects natural lakes, rivers, wetlands, forest reserves, game reserves, national parks and any land to be reserved for ecological and touristic purposes for the common good of all citizens.

Article 39 of the Constitution instructively provides that every Ugandan has a right to a clean and healthy environment. This provision is reiterated under section 3 of the 1995 National Environment Act Cap 153; and section 5(2) of the 2003 National Forestry and Tree Planting Act No. 8. This right has been defined to include:

⁴⁰ WRI [2011]. *Op. cit.*

- (a) the right to freedom from pollution, environmental degradation and activities which threaten life, health or livelihood;
- (b) protection and preservation of air, soil, water, flora and fauna;
- (c) healthy food and water; and
- (d) a safe and healthy working environment.

Box 8. National Environment Management Authority (NEMA) – A Critical Oversight Function

NEMA is the principal agency established by the National Environment Act for the management of the environment, charged with initiating legislative proposals, standards and guidelines on the environment. Among other duties NEMA is obliged to:

- (a) Ensure the integration of environmental concerns in overall national planning through coordination with the relevant ministries, departments and government agencies;
- (b) Liaise with the private sector, inter-governmental organisations, NGOs and governmental agencies of other states on issues relating to the environment;
- (c) Receive, review and approve Environmental Impact Assessments (EIA) and environmental impact statements;
- (d) Promote public awareness through formal, non-formal and informal education about environmental issues; and
- (e) Prepare and disseminate a “state of the environment” report once every two years.

The National Environment Act provides for maximum participation by the people of Uganda in the development of policies, plans and processes for the management of the environment. Additionally, before EIAs are carried out, they should be officially announced and published by the government at least once in the mass media, no less than 30 days before they occur.⁴¹

NEMA has to ensure that the principles of environmental management are observed, as follows:

- (a) To assure all people living in the country of the fundamental rights to an environment adequate for their health and wellbeing;
- (b) To establish adequate environmental protection standards and to monitor changes in environmental quality;

⁴¹ Regulation 19 of the EIA Regulations.

- (c) To require prior environmental assessment of proposed projects that may significantly affect the environment or the use of natural resources; and
- (d) To ensure that the true and total costs of environmental pollution are borne by the polluter.

Section 19 and paragraph 6(j) of the third schedule provide that projects for the exploration of petroleum require a project brief and EIA. Sections 24 to 32, among others, provide for the establishment of standards to establish the criteria and procedures for the measurement of air quality and water quality, and standards for control of noxious smells, noise and vibration, etc. Section 52 makes it an offence for any person to fail to minimise the waste generated by his or her activities.

NEMA's ambitious mandate, and critical role in ensuring oversight of environmental aspects of the oil and gas sector, including through ensuring public consultation about potential impacts, positions it as an essential actor in securing minimal damage to Uganda's environment by the industry. However, it is underfunded, overstretched and lacks the trained human resources to monitor and enforce environment and social impact regulations contained in its mandate. If these gaps are left unaddressed, there is a real danger that environmental risks associated with oil will not be effectively managed.

The NOGP asserts the need to protect the environment as part of management of the petroleum sector. Objective 5.3.9 seeks to ensure that oil and gas activities are undertaken in a manner that conserves the environment and biodiversity. To achieve this objective, the state is required to carry out due diligence on oil companies applying for licences in the country with regard to their technical and financial capabilities together with their environmental standards.

The NOGP further tasks the government with doing the following:

- Ensure availability of the necessary institutional and regulatory framework to address environment and biodiversity issues;
- Ensure presence of the necessary capacity and facilities to monitor the impact of oil and gas activities on the environment and biodiversity;
- Require oil companies and their contractors/subcontractors to use best practices in ensuring environmental protection and biodiversity conservation; and
- Require oil companies and any other operators to return all sites on which oil and gas activities are undertaken to their original condition as an environmental obligation.

The policy also realises the need to upgrade the relevant environment and biodiversity legislation to address oil and gas activities.

2.3.1 Relevant aspects of the Bill

Compliance

Section 3 of the Bill introduces the need to comply with environmental principles, and every licensee must take into account and give effect to the national environmental laws and other applicable laws, including international environmental conventions such as the Kyoto Protocol and the Rio Declaration. Arguably, however, the phrasing ‘take into account’ is weak, and the Bill should demand compliance. As currently drafted, it does not go further than the Act.

Activities in gazetted areas

The Bill’s provisions on surface and sub-surface rights remain similar to those in the Act, but with a few modifications. For example, oil activities can no longer take place in a national park or wildlife reserve without the written authority of the Uganda Wildlife Authority (UWA); or, for activities in a forest reserve, the written consent of the National Forestry Authority (NFA) must be sought.⁴² Under the Act, this consent is vested with the line ministers.

Pollution

Under section 104, a licensee is not to flare or vent petroleum in excess of the quantities needed for normal operational safety, unless authorised by the Minister on the advice of the Petroleum Authority. The allowed disposal of gas by flaring or venting for normal operational safety still requires the consent in writing of the Petroleum Authority, although, in case of an emergency, the licensee may vent or flare without such consent.

According to sections 132 to 138, a licensee or licensees are held liable for pollution damage hazardous to public health, safety or welfare; to animals, birds, wildlife, fish or aquatic life; or to plants; or that causes a contravention of any condition. Legal action for compensation for pollution damage shall be brought before the court in the court area where the effluence or discharge of petroleum has taken place or where damage has been caused. But the mention of generic pollution liability needs to be specified to, for example, the placement of tailings, use of chemicals and drilling fluids, as well as wellhead/pad activities, spillage and discharge due to overreliance on diesel to generate field power. The operator should be held liable not simply for activities directly related to drilling, but also for all ancillary activity in the fields.

⁴² The Bill, section 139; see also up to section 143.

Under section 191, the Minister can make regulations for the conservation and prevention of the waste of natural resources, whether petroleum or otherwise, and the carrying out of EIAs for that purpose.

Decommissioning plans

Section 118 of the Bill requires a licensee to submit a decommissioning plan to the Petroleum Authority before a petroleum production licence or a specific licence to install and operate facilities expires or is surrendered. The plan should be submitted at the earliest two years, but at the latest one year, before the use of a facility is expected to be terminated permanently. The Bill also provides for a decommissioning fund to implement the decommissioning plan, and, where the monies in the decommissioning fund are not sufficient to cover implementation, the licensee and, where applicable, the owner of the facilities shall cover the costs and expenses.⁴³

2.3.2 International best practice

There are a number of international organisations that have been closely monitoring the oil and gas industry's environmental footprint and standards of operation for decades. Among the multilateral agencies these include the United Nations Environment Programme (UNEP) as well as the World Bank and International Finance Corporation which together provide a large share of financing for capital-intensive oil and gas projects around the world, and promote higher standards of EIA to inform decision-making about such investments. IPIECA is a global industry association set up in the 1970s by UNEP focused on social and environmental issues related to oil and gas, and offers guidance and publications in its focal areas, such as biodiversity; climate change; and oil-spill preparedness, on its website www.iecea.org. Global advocacy NGOs such as Greenpeace, Global Witness and WWF, as well as a vast number of country-specific coalitions, have also produced evidence-based recommendations concerning management of environmental impacts from the industry.

Many oil and gas companies have adopted internal best practice policies, ensuring that they will meet the criteria set out at international level such as the Equator Principles (EPs).⁴⁴ These are broad principles adopted in June 2003 by 10 of the world's major private banks as a condition for lending money to oil and gas companies – all of whom depend on raising capital to conduct their activities. The EPs are a voluntary set of standards for determining, assessing and managing social and environmental risk in project financing. They are considered the financial industry “gold standard”

⁴³ Ibid, section 121.

⁴⁴ See www.equator-principles.com

for sustainable project finance, and are based on the IFC ‘Performance Standards on Social and Environmental Sustainability’ and the World Bank Group’s ‘Environmental, Health and Safety General Guidelines’. EP financial institutions commit to not providing loans to projects where the borrower does not comply with the standards.

When companies are bidding for exploration blocks, one of the major considerations should be their corporate biodiversity policies. Statoil of Norway, for example, has the goal ‘zero harm to the environment’. This objective is defined as conserving biodiversity, limiting emissions and discharges and limiting land use. The goals include:

- No habitat destruction;
- No introduction of foreign species; and
- No effects on population levels.

Statoil states, *inter alia*, that it will act according to the precautionary principle; comply with applicable regulations and legislation; set specific targets and implement measures based on relevant knowledge of the area affected and by applying risk analysis to assess environmental and health effects; and consult and cooperate with relevant stakeholders and strive for solutions acceptable to all affected parties.

Local knowledge and traditional uses of biodiversity in those areas where oil and gas are being explored should also be validated. The Albertine Graben is famous for its rich concentration of biodiversity, some of which are threatened, while others are on the verge of extinction. It is proposed that some of these species be collected in botanical gardens established close by. Such a project can constitute an aspect of an oil company’s corporate social responsibility.

2.3.3 Environmental advocacy points

General

The Bill’s articulation of responsibilities of licensees to observe environmental impacts should be strengthened to demand compliance.

Most oil development is taking place in the areas that draw the most tourists. It is relatively easy to assess the financial impacts of taking agricultural lands out of production, but much harder to determine how much tourism revenue is lost through impacts to natural areas. Where possible, impacts to tourism should be minimised. For example, in national parks, wells should not be placed on hilltops or in other highly visible areas; signage should be kept to a minimum,

etc. It should be recognised that tourism has the ability to provide revenue long after the oil has stopped flowing.

Clear guidelines need to be established around areas that will *not* be accessed for oil development due to environmental sensitivity, such as critical wetland areas (implying a need for the government to conduct in parallel a strategic environment assessment helping to determine these). The oil below these areas could still be accessed by horizontal/directional drilling methods. At this time the oil companies often claim that it is not economically feasible to use those methods, but that should simply be included as a cost of doing business in highly sensitive areas. The government should set guidelines stating in which areas directional drilling *must* be used.

Pollution

The proposed section on Liability for Pollution Damage (Part 10) could be made stronger by requiring bonds posted by licensees/operators to cover their liability for any pollution damage. Otherwise, it is unclear how liability can be enforced. It should also be made explicit that NATOIL is equally liable for any damage.

Given the certain increase in oil sector activity in coming years, and the environmental risks associated with this, further legislative detail is required on industry practices and potential issues such as gas flaring; pipeline construction and pipeline leaks; drilling technologies that prevent water and soil contamination; control of adverse effects of oil spills to the atmosphere, surrounding lands and nearby water bodies; noise and light that may scare away wild animals from their natural habitats; emergence of human domestic waste and disease due to population increase in the areas; destruction of forests and grass cover; disposal of oil waste; environmental restoration after the oil production stops; strategic assessments of environmental impacts; comprehensive biodiversity management strategy for the Albertine Rift; payment for environmental services; air quality management and monitoring; compliance with the national EIA system and procedures; appropriate penalties; and enhancing capacity and modalities for multi-stakeholder engagement in monitoring the impact of the oil industry on the environment.

The Bill should clearly prohibit companies from entering into private arrangements with landowners concerning disposal of toxic waste or other polluting substances.

Oil companies should be required to have the equipment and staff necessary for spill clean-up *on hand* for the worst disasters that can be reasonably expected. It is not sufficient for them to have this equipment regionally, as an immediate response is required, particularly when the spill is in water. Even though drilling is not taking

place in Lake Albert right now, regulations need to be in place for possible future developments. In addition, responsibility for clean-up of spills that happen during transport by pipeline, train or truck should be established. Financial liability should also be determined for loss of livelihood for fishermen, farmers, etc., whose livelihoods are affected by pollution/spills.

Special guidelines should be developed for operations that could affect endangered species. This could be another situation where directional drilling could be required, or where a licence could be refused.

Decommissioning

The Decommissioning Plan and Fund that appears in the Bill should be in place earlier than is currently indicated, ideally even before the licence is issued or the facility commissioned. The Decommissioning Plan should be updated during operations, and needs to contain provisions for rehabilitation of the affected areas (currently missing from the Bill).

It should mandatorily include a baseline to which sites should be restored. Requirements for baseline environmental surveys around drilling sites should also be established to ensure impacts can be properly assessed and sites can be restored to their original state when production is completed.

Institutional capacity for managing environmental impacts

The institutional arrangements for enforcing compliance with the environmental aspects of the Bill are not articulated. NEMA's role is clearly critical, yet the agency finds itself under-resourced to cope with the increase in demand and technicalities related to oil and gas. Provisions for its expansion and empowerment should be made explicit in the Bill. NEMA should be among the first government institutions to be empowered through accelerated training of more human resources by using some of the funds obtained from exploration licence fees.

The Bill should provide for impact assessment and monitoring teams to include at all times an independent, non-governmental third party. Results of monitoring should be made available to the public, both positive reports and records of infractions, to incentivise the companies to remain in compliance. What is the stopping mechanism if environmental impacts are determined to be too great? Who determines how much impact is "too much"? Who is liable for legal fees under the inevitable "breach of contract" battles if an operation is shut down?

Chain of authority needs to be established for granting licences in protected areas when there is a gap in leadership at the UWA or the NFA as there is now. The following questions also need to be addressed: Who else is able to assess whether potential impacts are acceptable? What input are they required to get from which protected-area agency staff? And, when executive leadership is re-established in these agencies, what authority do they have to reassess the agreements?

Further Reading

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