PARLIAMENT OF THE REPUBLIC OF UGANDA

REPORT OF THE COMMITTEE ON FINANCE, PLANNING AND ECONOMIC DEVELOPMENT ON THE PUBLIC FINANCE MANAGEMENT (AMENDMENT) BILL, 2021

OFFICE OF THE CLERK TO PARLIAMENT

DECEMBER, 2021

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PUBLIC FINANCE MANAGEMENT (AMENDMENT) BILL, 2021

REPORT OF THE COMMITTEE ON FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

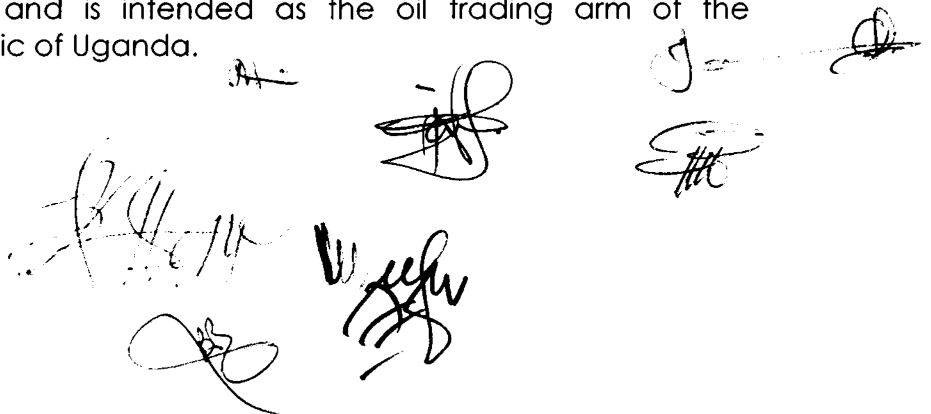
1.0Introduction

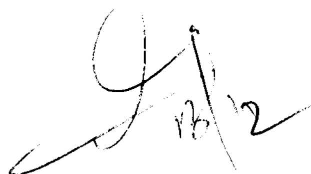
The Public Finance Management (Amendment) Bill, 2021, herein referred to as 'the Bill', was read for the first time on 5th October 2021 and referred to the Committee on Finance, Planning and Economic Development for consideration, in accordance with Rule 130 of the Rules of Procedure of Parliament No.30 of 2021.

The Committee has now considered it and we now beg to report.

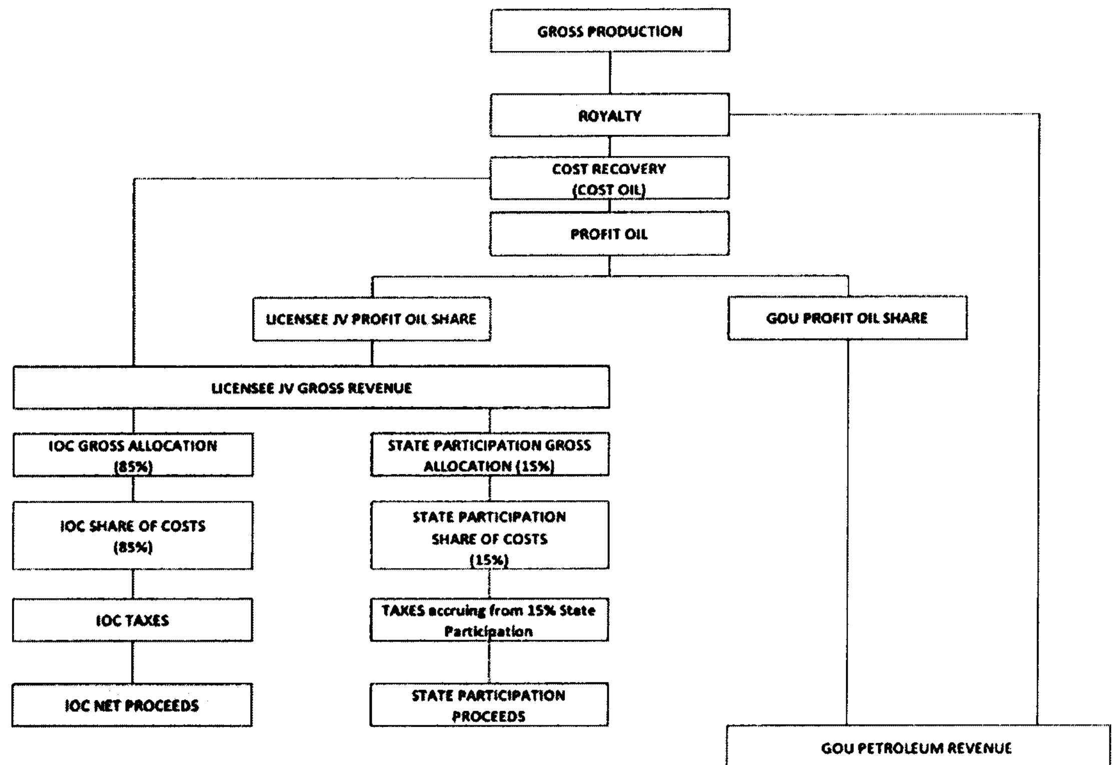
2.0 Background:

Uganda Operates a production sharing regime where international Oil companies (IOCs) come in, invest and explore oil and gas; at their own cost and risk. If a discovery of oil is made, the International Oil Company is repaid by receiving a portion of the eventual oil and or gas discovered and produced. As such, Uganda as a resource owner benefits by receiving royalties, various taxes, profit oil and the proceeds from the actual state participation in the joint venture as illustrated in **table one** below. This participation is managed by Uganda National Oil Company Limited (UNOC), a Petroleum limited Liability Company set up under the Petroleum (Exploration Development and Product) Act 2013 of Uganda. UNOC is wholly owned by government, and is intended as the oil trading arm of the government of the Republic of Uganda.





2.1 Table Showing the Basic Revenue-sharing Structure under the P.S.A's



Partly enacted as a result of emerging challenges of managing revenues from oil and gas, the Public Finance Management Act, 2015 (PFMA 2015), which is in nine Parts, has part VIII dedicated to the management of Petroleum Revenue, with 23 sections. Section 56 establishes the Petroleum Fund and provides that all petroleum revenue accruing to government shall be paid into the Petroleum Fund. Whilst, section 57, sets stringent measures to ensure that petroleum revenues collected are deposited into the Petroleum Fund. Section 58 deals with withdrawals of petroleum revenues from the Petroleum Fund. It requires that withdrawals from the Petroleum Fund only be made under the authority granted by an Appropriation Act and warrant of the Auditor General. Section 58 further delineates the purposes for withdrawals from the Petroleum Fund as;-

a) To the Consolidated Fund to support the annual budget;

b) To the Petroleum Revenue Investment Reserve, for investments to be undertaken in accordance with Section 63 of the Act;

Against that background, therefore, the purpose of the Bill is to amend the Public Finance Management Act, 2015, (PFMA 2015), to allow UNOC retain a portion of the proceeds from the sale of petroleum accruing from the 15% Government's State Participating Interest in the Production Sharing Agreements (PSA). The Bill categorically makes it clear that the proceeds

UNOC is seeking to retain shall only be used to help UNOC meet its financial obligations in the Tariff and Transportation Agreements (TTA) and in the Joint Operating Agreements (JOA). And that UNOC's operating and investment expenditures shall continue to be appropriated by parliament.

Movers of the Bill; Ministry of Finance, Planning and Economic Development and the Ministry of Energy and Mineral Development argued that Section 56 of PFMA 2015 establishes the Petroleum Fund into which all petroleum revenues must be deposited. They argued that, unfortunately, this does not allow UNOC as a licensee, to meet its financial obligations under the PSAs and the JOAs in a manner consistent with the key contractual provisions, including cost recovery under the PSAs and JOAs. Secondly, that the PFMA 2015 does not provide for payments of tariffs obligations under the Host Government Agreement (HGA) and the Transportation and Tariff Agreement (TTA), before the proceeds can be deposited into the Petroleum Fund, as required. As it is at the moment, the movers of the Bill argued that it undermines the confidence of the joint venture partners, of UNOC's ability to meet its cash-calls in a timely manner.

2.2 Principles of the Bill:

As a cure, therefore the Bill seeks to amend the PFMA 2015 to allow UNOC access the proceeds from the sale of its interest in crude oil, meet its financial contractual obligations as per the applicable agreements and then any balances, thereafter, can be deposited in the Petroleum Fund as required. It is envisaged that this then will allow UNOC, operate with a degree of independence as a limited liability company. Secondly, that this will give its venture partners confidence that UNOC will meet its financial obligations in a timely manner; maintaining the integrity and sanctity of the PSAs regimes.

3.0 Methodology

The Committee held consultative meetings, received written memoranda and reviewed relevant literature from a cross range of stakeholders.

3.1 Meetings and written submissions

The Committee held meetings and received written submissions from the following stakeholders:

a) The Minister of Finance, Planning and Economic Development, the mover of the Bill;
b) The Attorney General;
c) Uganda Law Society;
d) Petroleum Authority of Uganda (PAU);
e) Uganda National Oil Company (UNOC);
f) Civil Society Budget Advocacy Group (CSBAG);

3.2 Document review

The Committee reviewed and made reference to the following documents;-

i. The Constitution of the Republic of Uganda, 1995;
ii. The Public Finance Management Act, No,3 of 2015;
iii. The Uganda Revenue Authority Act Cap 196;
iv. The East Africa Crude Oil Pipeline Bill, 2021;
v. The Report of the Committee on Environment and Natural Resources on the East Africa Crude Oil Pipeline (Special Provisions) Bill, 2021;
vi. The Production Sharing Agreements pertaining to oil and gas exploration, development and production in Uganda to which UNOC is a party;
vii. The Petroleum (Exploration, Development And Production) Regulations, 2016;
viii. The National Oil and Gas Policy;
ix. The Public Finance Management Reform Strategy 2018 – 2023

3.3 International Benchmarks

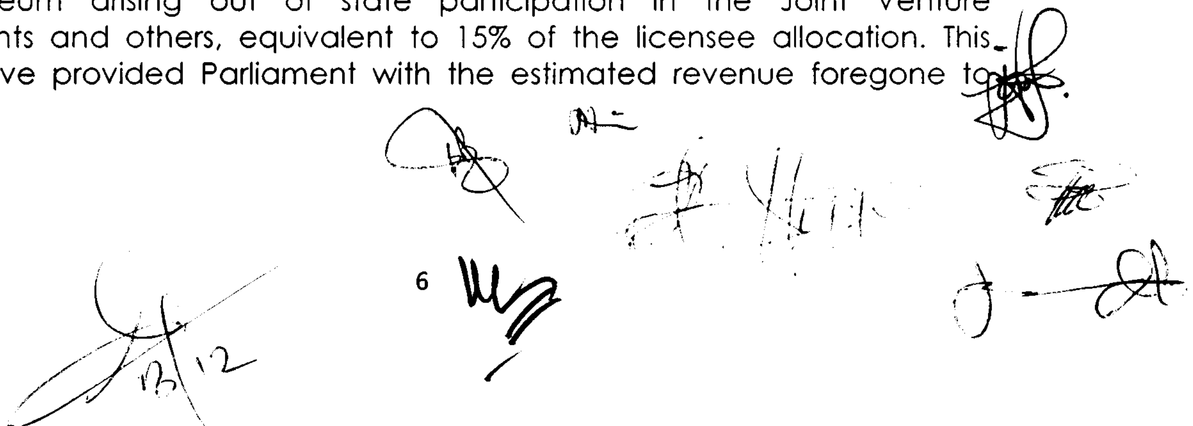
The Committee further analysed the oil and gas policies and laws of various countries including;- Ghana; Cameroon; Iran; Nigeria; Malaysia; Mexico; Vietnam; Angola; Brazil; Norway; Saudi Arabia.

4.0 Compliance Of The Certificate Of Financial Implications Of The PFM Amendment Bill, 2021 With The PFM Act 2015

The Committee noted that **Section 76** of the PFM Act requires all bills to be accompanied by a Certificate of Financial Implications (CFI) issued by the Minister for Finance, Planning and Economic Development. This was complied with by the Ministry of Finance.

However, subsection (2) requires the certificate to indicate the estimates of revenue and expenditure over the period not less than 2 years. This requirement was not met.

The definition proposed in the bill excludes proceeds from the sale of petroleum arising out of state participating interest in the applicable petroleum agreements. This implies that the Certificate of Financial Implications ought to have spelled out the revenues that will accrue from sale of petroleum arising out of state participation in the Joint Venture Agreements and others, equivalent to 15% of the licensee allocation. This would have provided Parliament with the estimated revenue foregone to UNOC.



In summary the annual cost structure for UNOC will be as follows

Financial Year	Financial Year- 1	Financial year- 2
Revenue (US$)	3.65 million	3.86 million
Expenditure (US$)	2.25 million	2.25 million
Surplus/ deficit- to Petroleum Fund (US$)	1.4 million	1.61 million

Source: PBO Computations

Note: *Second FY projection is based on assumption that production increases by 10% from previous year and recoverable costs are capped at US$ 15 per barrel.*

The Committee further noted that Section 76(3) of the PFM Act requires the Certificate of Financial Implication to indicate the impact of the Bill on the economy. The bill allows UNOC as illustrated above to retain huge sums of money resulting from state participating interest. In event of an increase in international oil prices this amount of money held by UNOC will be significant and could affect the prices of non- tradables in the economy. Price increases in the non- tradable sector will trigger high prices in the export sector making the economy uncompetitive.

This in turn will require the central bank to incur higher costs to stabilize prices, if inflation pressures resulting from the above actions are to be contained. Further the capital requirement by the Central bank needs to be estimated. Therefore the CFI ought to have indicated the magnitude of these effects to the economy over a two year period.

5.0 Key issues in the Bill

The main issues that the committee sought to determine and report on were:

Issue 1: Whether Section 3 of the PFMA 2015 defining petroleum revenue should be amended to exclude proceeds arising from sale of petroleum arising out of State Participating Interest in the applicable petroleum agreements.

Issue 2: Whether section 57 of the PFMA 2015 should be amended to allow UNOC to retain proceeds from the sale of petroleum, arising from state participating interest, to meet its financial obligations, borne by its self or on behalf of government, based on applicable oil agreements, but without parliamentary approval.

Issue 3: Whether as proposed in section 5(b) of the Bill, the National Oil Company shall deposit the balance of the proceeds retained after expending moneys for the purposes of subsection (5a) into the Petroleum Fund and submit a copy of the record to the Minister, the Uganda Revenue Authority, the Secretary to the Treasury, Accountant General and the Auditor General.

6.0 Stakeholders' Views

The various stakeholders that appeared before the committee, including the Uganda Law Society and as mentioned above, with the exception of CSBAG, commented in support of the three proposed amendments. However, CSBAG on behalf of the Civil Society had strong objections to the amendments. Their objections are returned to, later, hereafter. On the first issue about definitions, it was noted that the amendments was consequential. It was as a result of amending section 57 of the PFMA 2015.

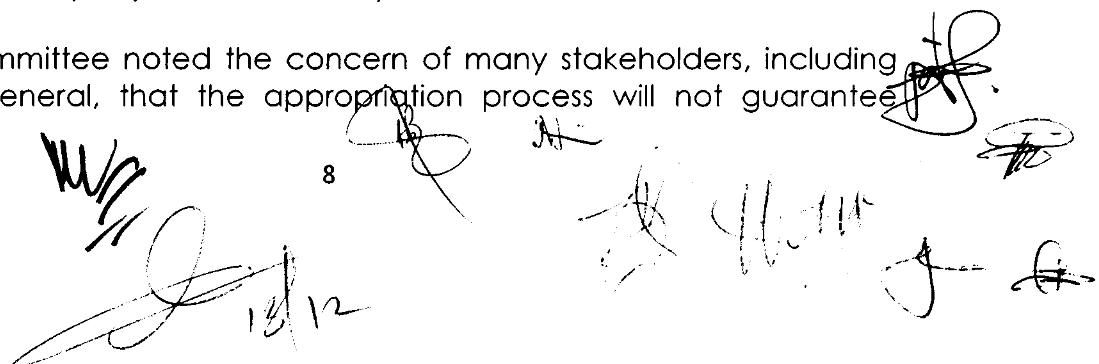
On Issue 2 as to whether Section 57 of the principal Act should be amended, a passionate appeal was made to the Committee to allow UNOC retain and spend money at source without parliamentary approval. Several arguments were advanced in favour of the amendment.

Firstly, that what was in the current law will stifle UNOC's ability to pay its monetary obligations. That UNOC is now a partner in the Upstream projects and is therefore expected to meet its obligations like the other International Oil companies that have been operating for several years and have built significant financial capacity. As an example, **Total Energies** (formerly "**Total**") has a market capitalization (the worth of the company derived from the value of its shares held on the stock market) of **US$ 121.74 Billion** while **CNOOC** (a National Oil company from China) has a market capitalisation of **US$ 53.21 Billion.**

Secondly, that the current law as it is will stifle UNOC's ability to pay its monetary obligations and as per the applicable agreements. They argued that UNOC will have significant financial requirements to ensure that the projects are developed beyond the first oil and minimise the penalties that may accrue from delayed payments of cash calls and that the provisions will allow the company to grow without external debt and therefore remain profitable.

Various stakeholders feared that whereas it is possible for UNOC to receive funding through annual appropriations from Parliament, international experience has shown that such approach is extremely costly. It subjects a business venture to numerous delays and uncertainty that are characteristic of Government budgeting. This usually results in unpaid cash calls thus leading to significant penalties to the National Oil Company and delayed growth of the National Oil Company and the country's Oil and Gas sector.

Further, the Committee noted the concern of many stakeholders, including the Attorney General, that the appropriation process will not guarantee



UNOC timely and complete provision of the necessary revenues to meet cash calls as they may be required and that this would put UNOC in a precarious situation of default as detailed hereunder.

6.1 The Adverse Consequences of defaulting on the cash calls:

Dilution: Under Article 8 of the Joint Operating Agreements, UNOC would be required to withdraw from the Joint Operating Agreements and lose its participating interest to the non-defaulting Parties. This would in effect dilute UNOC's participating interest in part or in whole depending on the level of default. It is exercisable if the default persists for **30 days** from the time the cash call is made, and default occurs.

Loss of production entitlement: Under the same Article, the other parties are permitted to seize and sell UNOC's crude oil entitlement to cover the default. This would mean that UNOC's entitlement to crude oil would be taken over and sold by its joint venture partners thereby reducing proceeds expected from the 15% State Participation to the State. This remedy is exercisable **10 days** from the date the default occurs.

Loss of access to information. As the projects are executed, extensive data is continuously generated and this is important for the parties to understand production projections, performance of individual fields and other information necessary for the tracking of the country's interest in the projects. UNOC would lose rights to this information in the period of default. The Committee noted that UNOC would not be able to advise Government, in its forecasts and planning without this information.

Loss of voting rights. UNOC would not vote in the joint venture until the default is cured. This means UNOC would cease to participate in decisions if it defaults.

Loss of right to participate in meetings: UNOC would not be permitted to attend meetings and will be deemed to have approve all items discussed in such meetings even if it has not attended.

That the work programs and Budgets are designed on annual basis based on a calendar year January to December whereas our budgeting process is from 1st July to 31st June. That based on this misalignment, UNOC would have to base on assumed figures for portion of its annual budget which could potentially lead to cash shortfalls and or default on payments.

Regarding how checks and balances, as per the letter and spirit of the PFMA 2015 will be maintained, witnesses argued that the amendments reflect the uniqueness of the requirements of the Oil and Gas sector and UNOC as an institution. They argued that UNOC is not the only entity allowed to spend at source. They cited other institutions with a similar provision include URA and

UCC among many others. Additionally, that UNOC will remain under the supervision of Parliament as Parliament will be receiving UNOC's annual work plans and budgets and the Auditor General will be annually auditing UNOC to ensure compliance with the provisions of the amendment. Further, that the Regulator (The Petroleum Authority of Uganda) shall annually approve the upstream work plans and budgets from which the cash calls will be paid and shall be supervising the activities of the Joint Venture Partners.

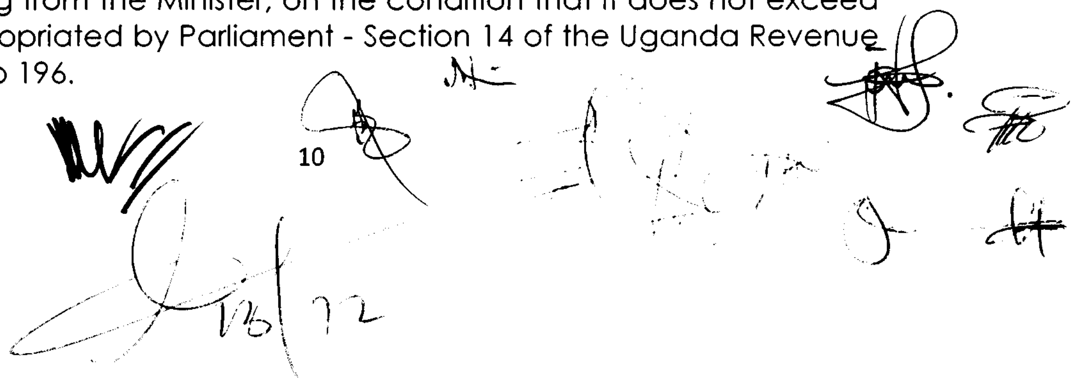
6.2 Submission by Civil Society Budget Advocacy Group (CSBAG)

In their robust submission, CSBAG argued that the PFMA, 2015 envisioned that ALL public expenditure is based on an approved work-plan and not on special considerations or ad-hoc implementation. And that as such, any reform that allows expenditure without public scrutiny, especially using Oil Revenue, is likely to attract allegations of mismanagement and in some instances actual corruption since Parliament through the relevant committee and by extension of the citizens, will not be privy to some of the claims that will be categorized as tariffs and or other obligations.

CSBAG further submitted that the proposed amendment, in its entirety, seeks to enable the Uganda National Oil Company (UNOC), which is a state-enterprise, operate outside the confines of the Public Finance Management Act, 2015. If passed into law, UNOC will have the leeway to collect revenue and keep it outside the Consolidated Fund and or Petroleum Fund and spend the same without approval or appropriation by Parliament. This will have the effect of eroding the accountability and oversight methods that are already in place to safeguard prudent financial management.

In addition, CSBAG submitted that this provision undermines fiscal consolidation and can be abused as such, as the Company will be given provision to spend at source. They argued that the purpose for the move highlighted in the proposed Section 57(5)(a) (i and ii) is unreasonable and that our annual budget process is sufficient to accommodate any emerging financial needs of all Government parastatals, state enterprises and companies like the Uganda National Oil Company (UNOC). They cited existing agencies like the Uganda Revenue Authority (URA) whose mandate is to collect revenue on behalf of Government of Uganda. However that it has clear guidelines to enable them to meet their urgent expenditure obligations.

"This in our view is the last nail in the coffin of the story of oil in Uganda because all safeguards and public scrutiny regarding oil revenues will be lost", they said as they asked the Committee to reject the amendments, pointing out that the bill attempts to do away with the benefits of having all bodies in contact with public funds remit the same to the 'fund". CSBAG was in strong support of the URA model which permits URA to request for additional funding from the Minister, on the condition that it does not exceed the amount appropriated by Parliament - Section 14 of the Uganda Revenue Authority Act Cap 196.



7.0International Experience

A wide range of countries were cited by witnesses as part of their presentations on this Bill. Please refer to **Table 6.1** below. Most of the companies were cited as on the extreme; they have full autonomy and it is only the net revenues after costs that are transferreds to the treasury. These included SNH of Cameroon; NIOC of Iran and many others. However, there were those like the Nigerian National Petroleum Company (NNPC) which are operating under parliamentary appropriation. But as of **January 2016**, NNPC had an unpaid cash calls (debt to the IOCs) of **US$ 5.6 Billion**. This was negotiated extensively and after waivers and payments have so far only been brought down to **US$ 1.57 Billion** as at the end of **January 2021 (Seven years later)**.

Ghana under their Petroleum Revenue Management Act of 2015, offered what appeared to be a better example, protecting its oil company from defaulting whilst subject to parliamentary approval. Section seven of Ghana's Petroleum Revenue Management Act, 2015 allows GNPC of Ghana to retain proceeds arising from state participating interest in petroleum operations but subject to Parliamentary approval. There was emphasis that, that numerous National Oil companies around the World, especially in their infancy, including in Africa utilise the funding mechanism that the stakeholders were supporting and that therefore the amendment proposal were in line with International Best practice.

7.1Table Showing National Oil Companies' Petroleum Management Systems

COUNTRY	NOC REVENUE MANAGEMENT SYSTEM
Cameroon	The National Hydrocarbons Corporation of Cameroon (SNH transfers revenues net of Costs to government.
Iran	The National Iranian Oil Company retains cost recovery from oil revenues and transfers the rest (plus profit oil from "buyback" service contracts) to government.
Nigeria	The Nigeria National Oil Corporation (NNPC) does not retain revenue; revenue passes through the company to the state. NNPC is in perennial default

	as a result of rigid appropriation cycles against the urgency of cost recoveries and cash calls.
Ghana	The Ghana National Petroleum Corporation pays revenue in the petroleum fund but can retain "equity financing cost" and additional amount as approved y parliament (not to exceed 55 percent of net cash flow from government interests).
Malaysia	PETRONAS retains profit earning and transfers from dividends, royalties, export duties to the state; it also pays heavy taxes on its own profits.
Mexico	Pemex retained revenues and paid income taxes (official rule) share of gross revenues (frequent practice).
Vietnam	Petro Vietnam retains a set percentage of carious revenues (e.g., 50 percent of dividends and royalties) and pays the rest to the state.
Angola	Formal rule has been for Sonangol to transfer revenues to treasury with minimak retention, but in practice, Sonangol retains massive amounts of revenue, with little formal constraint.
Brazil	Petrobras, a highly commercialised, partially privatised pays taxes/dividends to the state.
Norway	Statoil retains revenues, pays income taxes and dividends to the state.
Saudi Arabia	Saudi Aramco retains revenue to cover its costs, then it pays royalties and dividends equivalent to 93 percent of its profits.

8.0 Committee Observations and Recommendations

The Committee appreciates the business-oriented establishment of UNOC and that it may need uninterrupted access to financial resources to enable it meet its obligations, and might face inefficiency challenges should there be delays in accessing resources. The committee also acknowledges that given that UNOC is the trading arm of government, participating in the State's Joint Ventures, it must be empowered to meet its financial obligations.

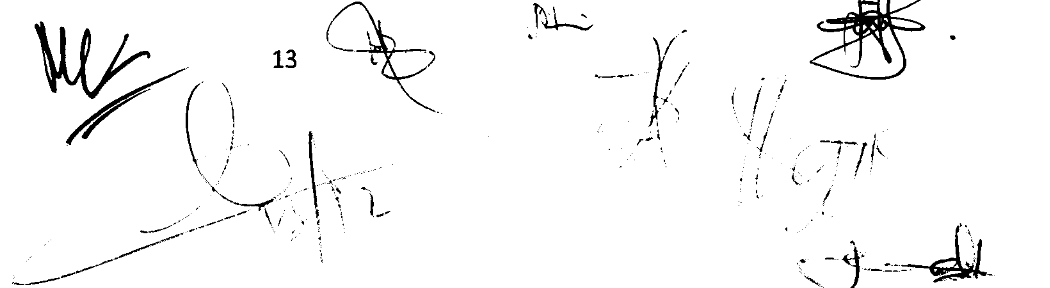
However, the Committee also observed that the Government of Uganda has undertaken a series of reforms, guided by the PFM Reform Strategy 2018 – 2023 to enhance transparency and increased accountability which must be upheld. One of such reforms has been to encourage all Government Ministries, Departments and Agencies (MDAs) that collect revenue to declare it through the Consolidated Fund, especially Non-Tax Revenue (NTR). These reforms saw the provisions for Appropriation-in-Aid repealed from the entire relevant legal framework. As such, parastatals like the Uganda Security Printing Company, the Uganda Driving License System, Public Universities, Immigrations and Passports, and the National Identification Registration Authority (NIRA), collect and remit resources to the Consolidated Fund, like the Uganda Revenue Authority (URA), without spending at source. This enables Government to ascertain its revenue (cash) position more clearly in the Treasury Single Account (TSA) and as such, rationalize expenditure.

Secondly, the Committee fears that if the amendments are passed in their current form, they are likely to undermine the original intention of passing the Public Finance Management Act, 2015. The Public Finance Management Act, 2015 provides a mechanism whereby budgeted money is spent and where shortfalls and emergencies arise, such can be planned for in a supplementary budget.

The Committee is also cognisant of the adverse likelihood that this amendment if approved in its current form, shall weaken the accountability mechanisms of the existing State institutions, yet oil is an important resource which should be jealously guarded to ensure that the implementation of programs in that regard is in line with the Government of Uganda's approved accounting and auditing procedures.

The Committee is further wary that this amendment if passed in its current form, shall further undermine the oversight role and power of the Parliament as an independent Arm of Government charged with the duty of supervising planning and expenditure of Ministries, Departments and Government Agencies.

Resultantly, the Committee maintains that Parliamentary appropriation is an important tool of prudent financial management. The Committee therefore seeks to avoid the erosion of Parliament's oversight and supervisory authority



over Government bodies as engraved in the Public Finance Management Act, 2015 and the Constitution of Uganda 1995. In the absence of such oversight and supervisory authority, there will be a clear breakdown of checks and balances on the operations of UNOC, allowing it unfettered authority.

However, the Committee observes that UNOC shall be implementing something unique and may require special measures but whilst maintaining the PFMA 2015 principles in place. The Committee also recognizes the need to protect UNOC's State Participating Interest as a party in the Joint Venture from defaulting on its various petroleum agreements.

The Committee was cautious that Parliament must also ensure that accountability mechanisms including parliamentary appropriation are not eroded by UNOC's operational mandate.

Therefore, picking on experiences on how the challenges faced can be addressed, the Committee recommends a hybrid model which protects UNOC's participating interest without undermining the core principles of PFMA in Uganda, including parliamentary appropriation.

On amendment of section 3 of the Act 3 of 2015, whilst accepting the amendments as consequential the committee recommends an amendment to add as a last sentence but..."***excludes proceeds retained to meet the National Oil Company obligations arising from petroleum agreements as approved by Parliament from time to time, and cost oil attributable to state participation".***

On Amendment to Section 57 of Act 3 of 2015, the committee agrees that UNOC can retain some money at source. This is intended to mitigate the risk of money being remitted to the Petroleum Fund and then is used for other competing demands. Retaining revenue at source, is the considered opinion of the committee that this will assure partners in the joint venture that, in any case, money is available.

However, conscious of the fact that money from state coffers must be appropriated by parliament based on annual workplans and budgets, ***the committee recommends that the proceeds retained should only be used after approval by parliament.*** The Committee also notes the misalignment between the budgets of the Joint Venture Patrners which are based on a calendar year as opposed to our national annual budgeting process which starts 1st July to the 30st June. ***The Committee therefore recommends a special budgeting calendar and process for UNOC.***

Thirdly, the committee also notes the serious consequences in the event that appropriation is delayed. *The committee therefore is recommending that the process of handling UNOC work plans and budgets, shall be handled expeditiously to ensure that a decision is given within 15 days, in order for*