THE INFLUENCE OF UGANDA'S FISCAL POLICY IN PROMOTING SUSTANABLE FINANCING IN THE OIL AND GAS SECTOR IN UGANDA

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JANUARY, 2022

DECLARATION

I, Lydia Kambedha, declare that this thesis is my work and it has not been submitted before to any other institution of higher learning for fulfillment of any academic award whatsoever.

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APPROVAL

I certify that this thesis entitled "**THE INFLUENCE OF UGANDA'S FISCAL POLICY IN PROMOTING SUSTANABLE FINANCING IN THE OIL AND GAS SECTOR IN UGANDA**" was done under my guidance and satisfies the partial fulfillment of the requirements of the award of the Master of Laws Degree (LL.M) in Oil and Gas.

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Signature……………………………… Date 04th, January 2022

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DEDICATION

This work is dedicated to my wonderful husband, Bagatya Matia for his unwavering support. And to my children Kitibwa Adonai Harvey and Kwikiriza Heidi Alayne for being so understanding when I had to take time out to study. I wouldn't have done it without you.

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ACRONYMS

APT	Additional Profit Tax
CAPEX	Capital Expenditure
CETs	Common External Tariffs
CTL	Commercial Transaction Levy
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
IFFs	Illicit Financial Flows
IOC	International Oil Companies
ITA	Income Tax Act
MEMD	Ministry of Energy and Mineral Development
MoFPED	Ministry of Finance, Planning and Economic Development
NOC	National Oil Company
NRCs	National Resource Companies
PEPA	Production and Exploration Act
PIT	Petroleum Income Tax
PSC	Production Sharing Contracts
UCMP	Uganda Chamber of Mines and Petroleum
UFR	Ugandan Fiscal Regime
UIA	Uganda Investment Authority
URA	Uganda Revenue Authority
VAT	Value Added tax

ABSTRACT

This study focused on analyzing how fiscal policy is related to oil and gas in a given economy like Uganda in anyway would play a significant role in encouraging capital investments from foreign direct companies, thus ensuring sustainable financing of the sector.

The study discussed a comparative analysis with other countries, where the extractive industries develop and operate through relationships between host governments and international companies. The fiscal policies that govern the relationship between these parties determine how the financial benefits and risks of extractive projects will be divided. These can be seen in the host government's legal frame work and National policies ***and*** if managed successfully, it will generate large revenue streams thus influencing sustainable financing through striking a balance between attracting the best investors and getting a good deal for the country.

A fiscal regime that does not provide sufficient incentives for investors can result in production or revenue levels that fall short of government goals. But a fiscal regime that fails to distribute enough revenue to the host country can fail to effectively compensate the country for the value of its depleting resources, and can foster citizen dissatisfaction and national instability. Yet sustainable financing seeks to reconcile economic performance with positive social and environmental impact.

The researcher used a doctrinal research methodology in which data was collected using a systematic literature review methods. The researcher used both thematic and content analysis techniques to analyze the study data findings.

The study findings disclosed that Uganda has a comprehensive flexible legal framework that has fair content including; Production Sharing Agreements, royalties, tax holidays, stabilization clause and others. The researcher recommends that the government take a key interest in fighting corruption in implementing the provision of the legal regime and fiscal policy in order to reap the benefit in oil and gas blessing to the nation of Uganda

Figure: 1. Map of Uganda showing the Albertine Graben Region

Source: NOGTEC, 2014[1]

[1]NOGTEC, 2014 (06 Feb.), 'Uganda signs MoU with oil firms over production',
Online (from http://www.nogtec.com/ugandasigns-mou-with-oil-firms-over-production/, 18 Feb. 2020). Nogtec is the prime source of Africa oil and gas industry news, information and analysis. It provides you with leading industry news updates and information, jobs,company directory, operational well and rig data, events, focused regional information, and many more. Nogtec covers the global oil and gas industry, with particular focus on Africa from upstream to downstream, new projects, discoveries, investments, new markets to mergers and acquisitions, policies and regulations as well as related political developments.

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- Tax Appeals Tribunal (TAT) Act. Statutory Instrument 345—1 of 2012.
- Anti-Corruption Act, 2009 (Act No. 6 of 2009).
- Income Tax Act (ITA) 1997, CAP. 340.

Statutory Instruments/ Regulations

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- Target well control (U) Ltd vs Commissioner General Uganda Revenue Authority (HCCS NO. 751 OF 2015) [2019] UGCOMMC 16 (19 June 2019).

- Tullow Uganda Limited and Tullow Operational Pty Ltd vs Uganda Revenue Authority.The Republic of Uganda in the Matter of the Tax Appeals Tribunal (Tat) Application No. 4 of 2011.

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- Enhancing National Participation in the Oil and Gas Industry in Uganda:Strengthening the Management of the Oil and Gas Sector in Uganda: A DevelopmentProgramme in cooperation with Norway (2010).
- National Content Policy for The Petroleum Subsector in Uganda: Ministry of Energy and Mineral Development (February 2017).
- National Oil and Gas Policy for Uganda: Ministry of Energy and Mineral Development (Feb. 2008).
- Oil and Gas Revenue Management Policy, February 2012.
- Taxation Handbook: A Guide to Taxation in Uganda. © Uganda Revenue Authority 2015. ISBN 978-9970-02-977-8.
- The National Content Study in the Oil and Gas Sector in Uganda, September 2011
- The Petroleum Authority of Uganda; Implementation of the national Content Policy: Progress and Challenges (September 2018).
- Uganda Vision 2040.

CHAPTER ONE

GENERAL INTRODUCTION

1.1 Introduction

Since the discovery of oil in Uganda in the 19th century, Uganda has struggled to come up with a fiscal system that would render her mining of this delicate but rather phenomenal resource a success given that exploitation is expected to commence in or about 2026 now the most anticipated oil pipeline Agreement has been signed between Tanzania, Uganda and International Oil Companies; China Nation Offshore Oil Company (CNOOC) and Total EP Ltd.[2] Generally due to discovery of oil and gas, foreign investment companies strategically running to 'young' oil producing countries as they see these are fertile grounds of investment but notwithstanding the urge to invest, these countries must be persuaded to maintain their investments in the country.

Throughout the study, it was established that Uganda has established its fiscal system through the establishment of taxation models under fiscal system of Product Sharing Agreements unlike Concessions and Service Agreements employed in other countries like Nigeria although there is arguably a minimal distinction between these regimes. Under this fiscal regime, for example, stabilization clauses are employed to enable the oil company cope up with existing Uganda laws, countries are allowed to explore oil without paying taxes before exploration among others.

Additionally, the study concurred that there are mechanisms within which the country to oversee the sustainability of these fiscal policies including joining the Extractive Industries Transparency Initiative (EITI)[3] among others. But it is noteworthy that this system will stand a test of time as Uganda's major problems of corruption are likely to also take root under the oil and gas sector but prima facie, the system shall maintain further investment in the country and in the sector since the fiscal system is constructed to favor the investor (International Oil Company) more than the Host Government.

[2]https://www.theeastafrican.co.ke/tea/business/uganda-oil-pipeline-deal-3358700 (Accessed on the 19th day of April 2021)

[3]https://eiti.org/news/uganda-joins-eiti (Accessed on the 19th day of April 2021)

Further, the study found out that this fiscal policy adopted by Uganda under the oil and gas will encourage and sustain investment in the country as has been observed through the literature review of this paper. Hence recommendations shall be made to merely improve the existing fiscal policy in order for the country to avoid what has overtime been termed as the "Resource curse.[4]"

Chapter one of this research study highlights the introduction and general overview of this paper, chapter two states the literature review of the works consulted during the study, chapter three highlight the methodology used throughout this research, chapter four will bear the finding of the study while chapter five carries the conclusions and recommendations of the study.

1.2.0 General background to the Study

Uganda confirmed the existence of commercially viable oil deposits in the Albertine region in 2006 and by 2019, 6.5 billion barrels of oil have been discovered with 1.4 to 1.7 billion barrels recovery rates, a 500 billion cubic feet of non-associated gas and under 200 billion feet of associated gas, just from 40 per cent of the exploration.[5] In 2006, Uganda confirmed the existence of commercial deposits of hydrocarbons in the Albertine Graben region and then embarked on the development of its legal and policy framework aimed at facilitating oil and gas exploitation. The government went ahead to pass the National Oil and Gas policy of 2008,[6] the petroleum (Exploration, Development and Production) Act[7] and Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act.[8] The 1999 product sharing agreement model (PSA) , the 2012 production sharing Agreement model and the 2016 model production sharing Agreement[9] and the local content regulations of 2016 and many others.

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[4]Caspary, G: Practical steps to help countries overcome the resource curse: The Extractive industries transparency Initiative. Global Govern.18 (2), 171–184. Cornell, Svante E. Azerbaijan since Independence M.E Sharpe Inc. New York. (2011)

[5]Fiona N Magona (2017), The state of oil and gas in Uganda – 31st July 2017.

[6]Uganda National oil and Gas policy, 2008.

[7]Petroleum (Exploration, Development and Production) Act, 2013

[8]Act no 4 of 2013 (parliament of Uganda)

[9]Production sharing model of 2016.

The Uganda National Oil and Gas Policy (2008) advocated for the use of the country's oil and gas resources to contribute to early achievement of poverty eradication and create lasting value to society. The policy in part states that:

"Oil and gas operations will provide opportunities for both forward and backward linkages in the country's industrialization drive. On one hand, oil and gas activities will provide raw materials which will be used as inputs during the manufacturing process. On the other hand, oil and gas activities will act as a market for industrial products, both directly and indirectly. Oil and gas operations will provide the country an opportunity to develop a petrochemical industry. This will include industries like oil refining; the offshoot industries utilizing the refinery by-products to produce soap, plastics, pesticides, paints, medicine, asphalt, chemicals and others; together with industries arising from the utilization of natural gas like cement production, iron ore smelting and production of fertilizers."[10]

However, to achieve the goal of the National Oil and Gas policy (2008), the petroleum must first be pumped out of the ground. Oil and Gas industry require extensive capital which is not readily available in Uganda thus the need to attract foreign direct investments (FDIs). According to the study by Sachs and Warner,[11]it was noted that the presence of oil can be a blessing or a curse depending on how it is handled. In this regard the proper management of oil and gas resource has caused overall development in many countries (for example, Norway) and improper handling has led to devastating effects (for instance, Nigeria).

Oil exploration and production has a number of positive effects on the economy but also comes along with negative impacts on the environment if not handled well. Petroleum activities have played a key role in the development of today's welfare state in Norway. When the first production

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[10]National oil and Gas Policy for Uganda (2008): Executive Summary: Linkages of the National Oil and Gas Policy to the Country's key policy frameworks, p. x.

[11]Sachs, J.D. and Warner, A. (2001): The curse of National Resources. European Economic Review (2001). Vol. 45, Issue 4-6 p. 827-836. Also See, Karl, T. (1997): The paradox of plenty; oil booms and petrol states. Berkely: University of California press, p. 23; O' Lear S. (2004): Resources and conflict in the Caspian Sea, Article *in* Geopolitics 9(1):161-186 · March 2004 p.162; and Karl, T. (1997): The paradox of plenty; oil booms and petrol states. Berkely: University of California press, p. 44.

licenses were awarded in the mid-1960s, hardly anyone realized what a huge impact the industry would have on the Norwegian economy.[12] Fifty years later, it is more important than ever. Figures for the petroleum industry's share of total value creation, investments, exports and revenues over the years show this very clearly. Activity on the Norwegian shelf will continue to be vital to the Norwegian economy in the years ahead i.e. there are large remaining resources, and major new projects such as the development of Johan Sverdrup are under way.

However, in 50 years of increasing oil and gas production, Nigerians remain among the poorest in the world,[13] and social infrastructure in the country is in state of decay, or has collapsed.
As a classic example of the "resource curse",[14] Nigeria, the 6thlargest exporter of crude oil in the world, fares miserably in development index. Nigeria's Human Development index (HDI) value for 2018 was 0.534[15], which put the country in the low human development category, positioning it at number 158 out of 189 countries and territories.[16] Nigeria is the largest oil producer in sub-Saharan Africa and has received over 300billion US dollars in oil revenue over the last twenty-five years.[17] However, despite this natural resource wealth, Nigeria has high levels of absolute poverty and high-income inequality. Natural resources are a large part of the wealth of many countries,[18] and the way in which their potential contribution to government revenues is managed can have a powerful impact for good or ill on their prosperity and economic development.[19]

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[12]Norwegian Ministry of Petroleum and Energy (May, 2020): Norway's Petroleum History

[13]Yomi Kazeem (2018): Nigeria has become the poverty capital of the world. Africa Reporter Quartz Africa. June 25, 2018

[14]Vanessa Ko (2014): Nigeria's "Resource Curse": Oil as Impediment to True Federalism; See, Oyefusi, Aderoju. "Oil Dependence and Civil Conflict in Nigeria." Centre for the Study of African Economies: 1-27.

[15]Human Development Report 2019: Focus on Nigeria: Inequalities in Human Development in the 21st Century, Briefing note for countries on the 2019 Human Development Report

[16]Central Bank of Nigeria, (2007). Economic and Financial Review, Vol. 35, December, No. 3

[17]Augustine Ikein, DSP Alamieyeseigha, and Steve Azaiki, *Oil, Democracy and the Promise of True Federalism*, (Lanham, MD: University Press of America, 2008), chap. 1-28, 42

[18]Kumar (1991): Taxation for a cyclical Industry, Resource Policy p. 133-148.

[19]Nakhle, C. (2008): Petroleum, sharing the oil wealth, a study of petroleum taxation yesterday, today and tomorrow (London, Routledge, 2008) p. 149-150.

Uganda is aiming at becoming a middle-income country by 2040[20] and the nation is focusing on the oil resource commonly referred to as 'the black gold" as a key contributor to attaining multiple sustainable development goals (SDGs). Full production is now set to commence in 2022. At full production, the fields are expected to produce up to 230,000 barrels a day.[21] Tullow estimates the cost of production at $25 a barrel.[22] Uganda expects to earn USD 3-3.5 billion dollars annually from the resource.[23] If President Yoweri Museveni's revelation that the cost of delivering Uganda's crude oil to the Tanzania Port of Tanga will be US$12.2 per barrel,[24] then Uganda's oil will be one of the most competitive in the world.

1.2.1 Global Context

Theoretically, all economies regard capital financing as the driving force for societies' economic growth and development.[25] All models and patterns of economic development are also established on the same basis. In societies without adequate capital financing for domestic development, resorting to foreign capitals then becomes a must if they are to attain economic development through heavy capital investments.[26]For example economies rely most heavily on oil for development[27] using oil revenue as a share of gross domestic product (GDP). Saudi Arabia comes

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[20]Uganda's Vision 2040.

[21]Petroleum Authority of Uganda (PAU) (2019): Uganda's oil Reserves: How much are recoverable? (June 4, 2019)

[22]Ibid.

[23]Ibid.

[24]Total (9th August 2017): Uganda's oil production cost per barrel at US$12.2 is one of the best globally.

[25]Hostelling H. (1931): The Economics of Exhaustible Resources, Journal of the Political Economy, April. Quoted in Griffin and TEECE.

[26]Nakhle C. (1982): Taxation of oil, Theoretical Background, Sharing the oil wealth, study of petroleum Taxation, Today, Yesterday and Tomorrow, p. 5-28.

[27]World Bank data 2012.

third, after Kuwait and Libya, with roughly 45% of GDP depending on oil followed by Iraq, Angola and Oman. Russia about 15% of GDP while Norway about 10% of GDP.[28]

It is important to note that domestic investment and attracting foreign capitals are among the ways for resolving lack of capital in developing countries and relieving the community from poverty. The issue of foreign capitals attraction for sustainable financing is different for oil-producing and oil-exporting countries because of the huge financing involved as compared to other sectors. As the main energy material, oil and gas has a special status in global economy.[29] This exhaustible resource has two major economic functions. On the one hand, it provides fuel required for domestic consumptions, and on the other hand, oil export brings income for a country and deeply affects its economic activities. Increase in investment depends on sustainable financing which in turn is influenced by the fiscal policy of the nation. Based on previous studies[30] regarding the effect of various variables on investment, oil income variable was considered to be one of the main variable explaining investments in oil-exporting countries.

This is because investment is a function of return rate and income, in macroeconomics discussions. Since oil incomes considerably affect national income or production, it can be used as a substitution for income. Hence oil incomes provide financial resources required for investment and make investment more appealing by increasing demand across economies. Although other studies[31] have assessed the link between fiscal petroleum regime and foreign investments, none

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[28]World Bank data 2012.

[29]Garnut and Rodd (1983): Taxation of Mineral Rents, chapters 2-3 p. 15-28.

[30]Kimuli Anthony (2013), Is Uganda's Petroleum fiscal system efficient? A dissertation for the award of an MSc Degree in Oil and Gas Accounting - Aberdeen Business School, The Robert Gordon University Aberdeen (Unpublished).

[31]Kaiser, M.J and Pulsipher, A.G. (2004), "*Fiscal System Analysis: Concessionary and Contractual Systems Used in Offshore Petroleum Arrangements*" US Department of the Interior Mineral Management Services MMS 2004-016 p. 1-78.

has examined the direct influence of fiscal policy in attracting foreign investments and sustainable financing in the country.[32]

1.2.2 African Context

Africa's oil and gas industry holds the potential for further growth mainly driven by an increase in FDIs and a rebound in prices.[33] New oil and gas deposits discovered off the coast of Africa have led to an increase in investment in infrastructure, technological advances, updates in regulation and improved governance, as well as the development of new skills. Rossouw[34] asserts that: -

"Renewed optimism has returned to Africa's oil & gas industry on the back of a rebound in prices and increased investor interest. The African oil & gas industry has been through some difficult and challenging years in the wake of the oil price crash. However, the industry has restructured itself and is more competitively placed in terms of efficiency and operational performance. The outlook for the industry continues to improve with oil & gas companies targeting cautious growth in areas less vulnerable to external volatility while maintaining their cost and operational margins."[35]

One of the most dramatic discovery in Africa over the past decade was Mozambique's natural gas estimated at over 180 trillion cubic feet,[36]which has already unlocked the first three large-scale liquefied natural gas (LNG) projects. These projects, together with project expansion phases and additional exploration have the potential to position Mozambique as the third largest LNG producer in the world after Qatar and Australia by 2030.

Although Africa's oil production increased slightly in 2018, (7.643 million barrels of oil per day in 2016 to 8.133 million barrels per day in 2017 per day in 2017 to 8,193 million barrels per day

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[32]Nakhle C. (2015) Licensing and the Upstream Petroleum Fiscal Regimes. An Assessment of Lebanon's Choices, Lebanese Center for Policy Studies.

[33]PwC's (2019) annual *Africa oil & gas review 2019*. www.PwC.com

[34]Andries Rossouw (2019), PwC Africa Energy Utilities & Resources Leader 4th November 2019.

[35]Ibid

[36]US Energy Information Administration (2018): Focus on Mozambique -May 2018.

in 2018) [37]the continent was unable to keep up with global output, resulting in a 0.1% drop in share. Africa's share of global oil reserves has declined by 1% from 124.47 billion barrels per day in 2017 to 125.3 billion barrels per day in 2018 amounting to 7.2% of the world's proven reserves.[38]At the end of 2018, Africa is reported to have 509.6 trillion cubic feet of proven gas reserves, up 4.5% from the prior year, which amounts to 7.3% of global proven reserves. Nearly 91% of African gas production continues to come from Algeria, Angola, Egypt, Libya and Nigeria, and saw an overall increase of 4.8% from last year.[39]Africa's oil and gas reserves production has also led to a series of successful liquefied natural gas (LNG) projects resulting in a liquefaction capacity of 18% of the total global capacity.[40]

1.3 Problem Statement of the Study

In any huge business undertaking like in the oil and gas industry, capital in form of technology and finance plays a critical role in ensuring the success of the business. According to Hostelling,[41] all economics regard capital as the driving force for societies' economic growth and development.[42]Traversing across any African country particularly Petro States, ideally the need to attract foreign direct investment is through creating an effective petroleum fiscal regime that influences promotion of sustainable financing into the oil and gas sector.

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[37]Statista Accounts (June 18, 2019): Africa's oil Production 1998- 2018. Published by M. Garside. This statistic shows Africa's total oil production from 1998 to 2018. In 2018, Africa's total oil production amounted to around 8.19 million barrels of oil per day. According to the source, oil production includes crude oil, shale oil, oil sands and NGLs (the liquid content of natural gas, where this is recovered separately), and excludes liquid fuels from other sources such as biomass and coal derivatives.

[38]Ibid

[39]Statista Accounts (June 18, 2019): Africa's oil Production 1998- 2018. Published by M. Garside.

[40]Ibid

[41]Hostelling H. (1931), The Economics of Exhaustible Resources, Journal of the Political Economy, April. Quoted in Griffin and TEECE, 1982.

[42]Hostelling H. (1931), The Economics of Exhaustible Resources, Journal of the Political Economy, April. Quoted in Griffin and TEECE, 1982.

According to the World Bank, [43]Uganda was ranked one of the lowest countries among the countries that encourage investments especially in the oil and gas sector. In order to encourage more direct foreign investments, the government introduced a set of tax reforms and measures in the oil and gas sector including, tax incentives and tax exemptions to investors among others as a way of encouraging more investments in the oil and gas sector. Although, it is notable that the system has been improved to accommodate the demands of the investment companies, this has been through negotiations regarding realisation and improvement of existing product sharing agreements. This has led to companies like Total and CNOOC to continue their investment within the country and made commitment to building the Tanga oil pipeline.[44]

However, despite the increasing effort by the Ugandan government to improve the efficiency of its petroleum fiscal regime as a way of promoting more sustainable financing through increased investments in the country's oil and gas sector by offering investors a number of incentives, Uganda still remains less attractive to investors in its oil and gas sector and till lacks finances to be able to support its idling oil and gas sector.[45] This study therefore, sought to examine the influence of Uganda's fiscal policy in promoting sustainable financing in the oil and gas sector in Uganda; does the current system maintain the already existing investments or even encourage more investment?

1.4 General Objective

This study investigated Uganda's existing fiscal system and its impact on influencing and promoting sustainable financing in the oil and gas sector. The study therefore explored what investors considers before partaking to put their funds into a project and established that a fiscal regime of a given country plays a paramount role in persuading investment. Hence a comparison was made between the Uganda fiscal system and other countries within.

[43]World Bank Report 2018.

[44]Ibid (note 2)

[45]Easterly, W. and Sergio R. (1993): Fiscal Policy and Economic Growth Journal of Monetary Economics 32, No.3) 417-458.

1.5 Specific Objectives

a) To examine the extent to which the fiscal policy regime influences sustainable financing in the oil and gas industry of Uganda

b) To analyse the factors that impact on sustainable financing in the oil and gas sector in Uganda

c) To ascertain if Uganda's fiscal regime encourages and promotes sustainable financing in oil and gas sector in Uganda.

1.6 Research Questions

a) Does a country's fiscal regime influence sustainable financing in the sector of oil and gas, to what extent?

b) What are the factors that impact on sustainable financing in oil and gas sector in Uganda?

c) To what extent does Uganda's fiscal policy encourage and promote sustainable financing in the oil and gas sector in Uganda.

1.7 Significance of the Study

This study was conducted in the new and developing sector of oil and gas, that appears to have little and scanty information domestically since it has been recently given attention. Therefore, it cannot go without saying that the study provides a demonstrative view of what Uganda's fiscal policy entails.

Secondly, the study can be a resourceful tool to the policy makers in the sector of oil and gas by providing rich content, suggestions and recommendation to the better and improvement of fiscal policy within the oil and gas sector in Uganda.

The findings of the study will be shared with other institutions especially those that are involved in encouraging more investments in the oil and gas sector, for example Uganda Investment Authority (UIA). The UIA can lobby for tax policy implementation relating to oil and gas sector and how those incentives can be used to encourage foreign direct investments (FDI) in Uganda's oil and gas industry to maximise this potential.[46]

[46]McKinsey Global Institute (2013): Reverse the curse, maximizing the potential of resource driven economies.

Through the extensive research that was carried out, the findings tax policy makers will be availed new practical approaches pertaining to the promotion of sustainable financing in Uganda's petroleum fiscal regime. It will also create amicable tax policy and fiscal instruments that will enhance, promoting and strengthening the fiscal petroleum regime in Uganda's oil and gas industry in order to attract more finances into the petroleum sector.

This study is of significance in that it will be used by students who would want to learn more about the issue of promoting sustainable financing in Uganda's petroleum industry through fiscal tax policies that attract long-term investment in the oil and gas industry. Pertinent issues that will be discussed will not be for oil and gas sector but the knowledge acquired will be for the extractive industries at large.

The study will further be used as a source of information from which students can refer in case of any serious issues concerning the study in question. Finally, the study is also significant for the award of the Master of Laws (LL.M) (Oil and Gas) of Uganda Christian University.

1.8 Scope of the Study

The scope of the study is divided into three perspectives; these include content, time and geographical scopes.

1.8.1 Content Scope

The study examines the influence of fiscal policy regime in promoting sustainable financing in Uganda's petroleum industry and also in attracting foreign investments in Uganda's Oil and gas Sector. The content of this study therefore resolves on examining the influence of Uganda's petroleum fiscal regime in promoting sustainable financing in the oil and gas sector through encouraging foreign direct investments in Uganda's oil and gas sector.

1.8.2 Time Scope

This study focused on span for a period of 15 years considering the time period from the year 2006 when Uganda declared its discovery of oil and gas to date. This period was used because of the availability of good quality and reliable data relevant to the topic under investigation since there were many changes that were made in Uganda's fiscal petroleum regime. The oil and gas that has

been discoverer in Uganda is about 6.5 billion barrels and the recoverable oil is about 1.8 to 2.2 barrels of oil.[47]

1.8.3 Geographical Scope

This study was carried out in Uganda, because as country in terms of assessing and sustainably financing its oil and gas industry. However, I further made comparison with other oil producing countries and how these countries have managed to attract and maintain investment within the sector. These countries include Kenya, Mali, Nigeria, and Tanzania among others.

1.9 Legal Research Framework

A research framework has been defined to mean a structure that provides guidance for the researcher as study questions are fine-tuned, methods for measuring variables are selected and analyses are planned.[48] There are two main established research designs/frameworks used in academic research and these are conceptual and theoretical frameworks.[49] The conceptual framework is the researcher's idea on how the research problem was explored while the theoretical framework dwells on time tested theories that embody the findings of numerous investigations on how phenomena occur.[50]

1.9.1. Conceptual Framework

The conceptual framework is the researcher's construction of the concepts to aid the study of the two variables in the study topic. Hence, conceptual framework merges the existing views in the literature concerning a given situation.

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[47]Oil in uganda <https://www.oxfordinstituteforenergystudies.org> accessed on 26 September 2020

[48]Liehr P, Smith MJ 1999. Middle range theory: Spinning research and practice to create knowledge for the new millennium. Advances in Nursing Science, 21(4): 81-91.

[49]Sitwala Imelda, Is There a Conceptual difference between Theoretical and conceptual Framework?, University of Zululand, Kamia-Raj 2014, Page 188

[50]Ibid, page 189

Figure: 2. Conceptual Framework showing the relationship between fiscal policy and sustainable financing in the oil and gas sector.

Independent Variable	**Dependent Variable**
Fiscal taxation policy Regime.	Attracting investments in oil and gas sector.
Taxation policy (PSA, C & CSC)	sustainable financing.(tax incentives)
Fiscal instruments.	Tax Allowances
Income tax	Tax Credits
Corporate tax	Tax deductions
Capital Gain Tax	Tax Holiday

Lydia Kambendha: 2020.

The conceptual frame work above was constructed by the researcher. However, the attributes to the variables where built through extensive review of literatures related to the study

The framework explains the relationship between a country's fiscal system under this study, it was established that a country's fiscal system plays a big role in influencing sustainable financing of the sector through investment. It also indicates the factors that are affected by the fiscal policy to enable sustainable financing.

1.9.2 Theoretical Framework

Whereas the conceptual framework specifies the variables (and its attributes) that were explored in the investigation, the theoretical framework provides a general representation of relationships between things in a given phenomenon. It describes a broader relationship between things.[51]

[51]Ibid, page 189 & 190

In the course of the study, the theoretical framework was adopted over the conceptual framework. This is because the framework discusses the already existing conclusions and findings by prominent models.

This study was guided by the *Dunning theory* which establishes the existence of certain company's advantages from the interaction with the country that should be taken into account before investment decisions are made. This theory was propagated by Dunning in 1977[52]. Dunning's eclectic paradigm tries to explain the existence of multinational corporations (MNCs) and their relative success in comparison to domestic firms.[53] The eclectic paradigm is a view on the international production of firms, that is, on the production undertaken in foreign countries through the realization of foreign direct investment (FDI). The core of the paradigm is to provide a more integrative form to explain the motives and reasons (why), location (where) and the manner (how) the international operations of MNCs are carried out.

The eclectic paradigm, in its initial formulation, according to Dunning,[54] seeks to explain why the MNCs decide to manufacture internationally using the three criteria, or advantages.

Indeed, for the foreign firms to compete effectively with the domestic firms in the host countries, they must hold some sort of competitive advantage. This competitive advantage must be sufficient to overcome the costs and liabilities of foreignness[55] and the costs of installing and operating a subsidiary abroad. That is, the foreign firm needs to generate more value added than the domestic

[52]Dunning (1977), Theories of Taxation in extractive industries.

[53]Dunning, J. (1988) The eclectic paradigm of international production: a restatement and some possible extensions. *Journal of International Business Studies,* 19(1): 1-31; Dunning, J., Kim, C. & Lin, J-D. (2001) Incorporating trade into the investment development path: A case study of the Republic of Korea and Taiwan. *Oxford Development Studies*, 29: 145-154; Dunning, J. &Wymbs, C. (2001) The challenge of electronic markets for international business theory, *International Journal of the Economics of Business*, 8(2): 273-301.

[54]Dunning, J. (1988) The eclectic paradigm of international production: a restatement and some possible extensions. *Journal of International Business Studies,* 19(1): 1-31.

[55]Hymer, S. (1976) *The international operations of national firms: A study of FDI.* Cambridge, Mass.: MIT Press; Zaheer, S. (1995) Overcoming the liability of foreignness. *Academy of Management Journal*, 38(2): 341-363

firms. The three advantages that need to be simultaneously present for the MNCs to prefer to conduct FDI are:[56] ownership, location and internalization advantages.

This theory explains the importance and the influence of an effective fiscal regime in promoting sustainable financing in the oil and gas sector in countries that are less developed through creating conditions for investors that will increase their appetite for investing in such countries. These may take the form of offering tax incentives and also improving the countries investment climate. Dunning model[57] illustrates why some factors are more important than others during decision making of which country an investor can invest his or her resources and also which kind of sector can an investor invest in depending on profit pullback and the certainty and attractiveness of the fiscal taxation policy in place. Investors prefer fiscal taxation policy that is more favourable to them in terms of them retaining more profits on their investments. However, this theory is recognised as the most overarching factor of foreign direct investment (FDI) determinants which includes tax incentives and tax credits among others.

Through the application of Dunning's theory, the researcher managed to assess the factors or considerations undertaken by Multinational companies before making an investment decisions and make a comparison with Uganda's FDI. By ascertaining the weight attached to a factor that influences investment, attention was drawn to its impact on sustaining financing, for example if the taxes in a country are low or the PSAs allowed creation of tax havens, it is easier for Multinationals to continue investing in the country's oil and gas sector. However, when the taxes are strict and harsh, few corporations will have the zeal to invest, which in the due course reduces sustainable financing. This assisted the author in making recommendations for improvement in the country's fiscal system,

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[56]Dunning, J. (1977) Trade, location of economic activity and the MNE: A search for an eclectic approach, in Ohlin, B.; Hesselborn, P.; Wijkman, P. (Eds.) *The International Allocation ofEconomic Activity*, London: Macmillan, 395-418; Dunning, J. (1981a) Explaining the international direct investment position of countries: Towards a dynamic or developmental approach, *WeltwirtschaftlichesArchiv*, 117: 30-64; Dunning, J. (1981b) *International production and the multinational enterprise.* London and Boston: Allen & Unwin; Dunning, J. (1988) The eclectic paradigm of international production: a restatement and some possible extensions. *Journal of International Business Studies,* 19(1): 1-31; Dunning, J. (1995) Reappraising the eclectic paradigm in the age of alliance capitalism. *Journal of International Business Studies*, 26(3): 461- 491; Dunning, J., Kim, C. & Lin, J-D. (2001) Incorporating trade into the investment development path: A case study of the Republic of Korea and Taiwan. *Oxford Development Studies*, 29: 145-154.

[57]Dunning 1977, Theories of Taxation in extractive industries.

1.10 Chapter characterization.

The thesis is organized into five chapters. Chapter one will comprise the general introduction to the research. It will contain the problem statement, purpose, the research questions, justification, significance and scope of the study plus theoretical framework. Chapter two explores the literature reviewed in the study; the already existing articles, journals and scholarly materials on the subject. Chapter three discusses the methodology undertaken by the researcher, chapter four deals with study findings and analysis, and chapter five deals with study recommendations and the conclusions.

CHAPTER TWO

LITERATURE REVIEW

2.1. Introduction

This chapter focused on reviewing scholarly literatures and the legal provision related to fiscal policy and their possibility to influence capital investments in the oil and gas industry of Uganda. The purpose of the review is to collect data that the researcher will use to answer the research questions in order to fulfill the objectives of the study

2.2 Uganda's Fiscal Regime

The petroleum fiscal system for a country is a combination of the taxation structure established by legislation, together with the contractual framework under which an international oil company operates with the host government. Fiscal systems vary widely between countries and in some countries there is more than one system. The taxation structure for instance, includes royal payments. The contractual framework may be based on concessionary arrangements or on service and production sharing agreements[58].

In most countries, except the United States of America, the owner of the mineral resources is the government. In the USA, the owners are private individuals or companies that pay taxes on production to the State. Worldwide, every country has developed its own petroleum fiscal systems to be applied, under the concessionary systems, the government transfers title of the oil and gas to a company if they are produced. The producing company then pays royalties and taxes.[59] Contractual systems are in most cases either production sharing agreements or service contracts. The State companies either self-produce or share the production and selling of the oil or gas, revenues then flow into the finance ministries' treasuries.

In most contractual systems, the facilities installed by the contractor within the host government's territory become the property of the State either as soon as they are landed or upon start up or

[58]Muhammed Mazeel: **Petroleum Fiscal Systems and Contracts. Herstellung: Diplomica Verlag GmbH, Hamburg, 2010 Dieses**

[59]Ibid (Note 14)

commissioning. Sometimes, the asset or a facility does not pass to the government until the expended costs have been recovered.

This transfer of title for asset facilities does not apply to leased equipment or to equipment brought in by service companies. The difference between service contracts and production sharing contracts depends on whether the contractor receives compensation in cash or in crude. Under a production sharing agreement, the contractor receives a share of production and hence takes title to this crude. In a concessionary system, the transfer of title occurs at the point of export instead of at the wellhead. In a service contract, there is no issue of title since the contractor gets a share of profits rather than production.

Under some service agreements, however, the contractor has the right to purchase crude from the government at a discount. Despite the differences between the systems the same economic results are achieved[60]. When the contractor is paid a fee for conducting exploration and production operations, then this system is a risk service contract. The difference between risk and pure services contracts depends on whether there is a fee on the profits or not. The pure service contract is without risk in exploration and development. Consequently, this is usually used by conservative nationalized companies or by states that have capital but are lacking in technology and management capability. In regards to this study and the context of Uganda, it should be noted that Uganda employs the use of Production Sharing Agreements.

2.2.1 Production Sharing Agreements.

Product sharing regime involves the payment of a share or value of production to the government or its agency after allocation of a fixed share of production to the investor to cover costs[61]. Under Production Sharing Agreements, there is a fixed maximum percentage of production known as *cost recovery or cost oil* which is allocated to the Multi-National Company for recovery of costs in a period and the production remaining after cost recovery, that is profit oil, is shared between

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[60]Telly Eugene Muramira& Jacob Manyindo: Sharing Oil and Gas in Uganda. October 2018.

[61]JOHNSTON. D: International Petroleum Fiscal Systems and Production Sharing Contracts. (1994) Tulsa, Ok: PennWell Books

the government and the international oil company.[62] Since the discovery of oil adopted a number of four Production Sharing Agreements Models including the *Kanywataba Agreement* in 2012 plus formulation of the 2016 Production Sharing Agreement Model as the current used, that sets out the phenomenal aspects of tax collection and administering in respect of the oil sector including royalty, annual fees, product sharing[63], cost recovery[64] and state participation.[65]

Production sharing agreements in Uganda derive their legality from Section 6 of the Petroleum Exploration, Development and Production Act 2013[66], which provides that the government may enter into an agreement governing the grant of a license, including conditions for grant or renewal, and for the conduct of operations. Under the Production Sharing Agreements created by the Petroleum Exploration, Development and Production Act 2013, the government always retains the rights to the resources on the ground.

The government and the Oil Company agree on how the production will be shared after the royalty and tax liabilities have been paid by the International Oil Company. The host government will meet exploration and development costs and in return for a share of any production that may result. Therefore the host government has no right to be paid if there is no discovery.[67] Production Sharing Agreements always adopt instruments of tax collection that include royalties, cost recovery, profit oil and state participation among others as shall be discussed below.

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[62]Nakhle. C: Petroleum fiscal regimes; Evolution and challenges. In Daniel, P., Keen, M., McPherson, C., eds. The Taxation of petroleum and Minerals: Principles,Problems and Practice. Routledge

[63]Article 12 of Uganda PSA Model 2016

[64]Article 11 of Uganda PSA Model 2016

[65]Article 10 of Uganda PSA Model 2016

[66]The Petroleum Exploration, Development and Production Act 2013.

[67]Thomas Lassord Andrew Bower: Fiscal Rule Options for Petroleum Revenue Management in Uganda. Revenue Watch Institute (2014)

2.2.2 Royalty.

This is the compensation for the exploitation privileges of natural resources to the government by the oil company. The royalty is paid from the initial oil production by the contracting international oil company. According to Nichols[68] royalties are a fixed proportion of production but can vary basing on sliding scale of production either daily or monthly. They guarantee that the government obtains its share revenue regardless of whether the international oil company earns a profit out of the undertaking or not. Section 154 of the Petroleum (Exploration, Development and Production) Act 2013 provides that the licensee shall pay royalty to the government on petroleum recovered at the delivering point as will be stipulated in that particular petroleum agreement. Failure for the payment of this royalty, dealings with the company may be suspended or halted by the government and suit for recovery may be instituted thereafter.[69]

Subsequently, the requirement of payment of royalty has been reflected in the Uganda Production Sharing Agreement Models for example Article 9 of the 2016 Model[70] stipulates the payment of royalty by the licensee the Gross Total Daily Production in Barrels of Oil Per Day (BOPD) for each Contract Area and the respective criteria set out under Clause 2 of Article 9 of the Model[71]. Projections indicate that by 2020, Uganda's royalty will be secured at a higher prospect with the stabilization of the oil prices and more deals being secured by the government.[72]

2.2.3 Profit Oil

This is the amount of revenues or production that the government shares with the International Oil Company after royalties and cost oil are recovered from the gross revenues. The Ugandan

[68]NICHOLS. M. LINDA: Accounting Implications of Petroleum Sharing Contracts Petroleum Accounting and Financial Management Journal, Vol.29, No.2 (2010)

[69]Section 154(3) ibid

[70]Uganda Product Sharing Agreement Model 2016

[71]2016 PSA Model

[72]Kiana Wilburg: Uganda Secures 12.5% royalty for more than 7000 barrels of oil per day. Available via https://www.kaieteurnewsonline.com accessed on 23rd of October 2020

Production Sharing Agreement Model 2012[73] described profit oil or gas as the net revenue that remains after deducting royalty payments and costs recovered during the period under review[74]. This profit oil is therefore shared between the international oil company and the host government, and the share of the company is the chargeable income of the company subject to be taxed. However, it should be noted that the Uganda Product Sharing Agreement Model 2016 substitutes profit oil and with 'product sharing' under Article 12[75] where the government shall be entitled to the share of the 'profit petroleum' calculated using the R-Factor based on Cumulative Net Revenues and Cumulative Capital Expenditures. This profit petroleum arises out the state participation that is the government purchasing shares within the oil production. Under the current Model[76] state participation is restricted to the agreement of the parties[77] i.e. host government and the oil company.

The government participation can interchangeably be so used as profit oil as under government participation, the production contract stipulates the percentage extent to which the government shall be response for through her national oil companies or parastatals although the international oil company bears the risks of production and exploration.

2.2.4 Cost Recovery.

This is the recovery of money by the oil company after the oil has started actually to flow.[78]These costs include exploration costs that accrued in identifying areas that may warrant examination to the prospectus of containing oil and gas reservoirs like the cost of drilling. The costs are incurred in the accessing and maintaining the oil reserves. Under Uganda Production Sharing Agreement

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[73]Uganda Production Sharing Agreement Model 2012

[74]Article 13 of Uganda Production Sharing Agreement Model 2012(ibid)

[75]Uganda PSA Model 2016

[76](ibid)

[77]Article 10 of the 2016 PSA Model.

[78]Johnston D; International Exploration Economics, Risk and Contract Analysis (2003) (1st Edition Tulsa Oklahoma, USA Penn Well, Corporation)

2016, cost oil recovery is provided for Clause 3 of Article 11; Under Article 11(4) of the Mode,[79] the company recovers 'cost oil' which is the a 'reimbursement' for the costs incurred in the exploration phase and some (or all) of the costs incurred during the development and production phase.[80] The cost recovery is the opposite of royalty, i.e. cost recovery is paid to the Oil Company to recover its costs in the exploration costs. Therefore, it is the assurance of the oil company that it will recover the costs incurred throughout the production at a certain percentage as will be agreed.

2.2.5. Income Tax

The Uganda fiscal system also applies the use of income tax and thus charges an income tax of 30% from the oil company under the contract the tax is deducted over the capital costs of the oil company in the life time of the project. Although with income tax investors usually cannot recover their costs immediately which can distort investment decisions, the Government gets early revenues.

2.2.6 Signature Bonuses.

This is the one-time fee for the assignment and securing of a license paid irrespective of the economic success of the licensee. These bonuses are paid upon the signing of the agreement by the oil company. Recently, the Uganda government received over $316,000 from the Australian Armour Energy Limited as signature bonus.[81]

2.2.7 Resource rent tax

This is sometimes referred to as Additional Profits Tax. It provides the government with a greater share of natural resource wealth and it distorts investment decisions less. It should be noted that resource rent tax arises if the accumulated net cash flow from the oil and gas project is positive.

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[79]Uganda Production Sharing Agreement 2016 (supra)

[80]PWC; Financial reporting in the oil and gas industry International Financial Reporting Standards 2nd Edition *https://www.pwc.com/id/en/.../financial-reporting-in-the-oil-and-gas-industry.pdf*accessed on 20th October 2020

[81]Government gets sh1 trillion in oil signature bonuses by John Odyek accessed via https://newvision.co.ug/new_vision/news/1461677/government-sh1-trillion-oil-signature-bonus retrieved on the 25th of October 2020

Resource Rent Tax is categorized into two, namely the R- factor and the rate of return scheme. R factor based Additional Profits Tax links taxation to the investment payback ratio also known as the R-factor. R-factor is the ratio of the IOC's cumulative receipts over the cumulative costs including the upfront investment. Additional Profits Tax in this case applies when the R-factor exceeds one.

2.2.8 Capital Gain Tax.

This is the tax charged on the gains on an asset, i.e. the difference between the price of the asset at purchase and its price at the sale. The recent dispute in Uganda regarding capital gains tax was the famous dispute of Uganda and Tullow Oil Plc which was resolved and parties agreed that Uganda shall get $250 Million as Capital gains tax.[82]

2.2.9 State Participation.

Production Sharing Agreements provide an option for the state-owned oil company to participate in development of the oil project. While the contractor bears the cost and risk of exploration, the government through the national oil company can elect to participate at a level of working interest up to a maximum of 51% upon the discovery of oil and gas. Normally, the government participation is automatically assumed whenever a percentage of it is quoted, although some key aspects of it should be first determined i.e. the point at which the government backs in (usually at commerciality), the scale of participation in management of the venture large range), the costs to be borne by the government (usually prorated share of development costs), the ways of funding the government portion of costs (often out of production) split.[83]

2.3 Uganda's Legal Fiscal Regime

The Uganda's legal framework that embodies the fiscal regime under which oil companies operate, if observed and utilised adequately shall, together with geographical and political factors make a

[82]Tullow Oil, Government of Uganda Resolvge capital Gain Tax Dispute accessed via https://www.infrastructure.co.ug/tullow-oil-government-uganda-resolve-capital-gain-tax-dispute-0 retrieved on the 26th of January 2021

[83]Jonhston (supra)

country more or less attractive for investment. Sustainable resource management require an inclusive and comprehensive national strategy.

The country's legal fiscal regime imports the application and the use of laws, regulations and policies among others. These include, the Constitution of Uganda 1995, as amended, the Petroleum (Exploration, Development and Production) Act, 2013 and the regulations made thereunder, and the National Oil and Gas Policy, 2008.

Firstly, Article 244 of the 1995 Constitution of the Republic of Uganda, 1995 (as amended), states that all minerals and petroleum in, on or under, any land or waters in Uganda are vested in the government on the behalf of the people of Uganda.

This is thus supported by the existing legislations made thereunder. Forexample, in the management of natural resources, The National Oil and Gas policy 2008 is the key legally binding document guiding the sector. The goal of the policy is to use the country's oil and gas resource to contribute to early poverty eradication and create lasting value to society.

The oil and gas Revenue management policy of 2012, the public management Act of 2015, were enacted and established the petroleum fund.

Other laws enacted include the **The Income Tax (Amendment) Act, 2019; The Tax Procedures Code (Amendment), Act 2019; The Value Added Tax (Amendment) Act, 2019; The Excise Duty (Amendment) Act, 2019;** East African Excise *Management* Act (Amendment) Act, 2012; and The Public Finance Management Act, 2015 among others. All these laws and regulations are aimed at ensuring that the oil and gas sector is managed well in terms of attracting more investors into the sectors and also maximising more revenues into the oil and gas industry. Some of the laws governing tax in Uganda include, among others.

2.3.1. The 1995 Constitution of the Republic of Uganda (As amended)

Provisions about taxation in the Constitution of the Republic of Uganda include: Article 152, (1) which states that no tax shall be imposed except under the authority of an Act of Parliament. This

article- therefore empowers the Parliament as the only institution to make such laws on all matters concerning tax and taxation policy in Uganda.

From the above provision, Article 152 (3) is to the effect that the same Parliament shall make laws to establish tax tribunals for the purpose of settling tax disputes. In brief it is the sole responsibility of parliament to make laws for taxation but also establish administrative tribunals to deal with disputes arising from tax related matters.

Articles 191 (1) states that local governments shall have powers to levy, charge, collect and appropriate fees and taxes in accordance with any law enacted by parliament by virtue of Article 152 of this Constitution. Under Clause (2) of Article 191, the fees and taxes to be levied, charged, collected and appropriated under clause (1) of this article shall consist of rents, rates, loyalties, stamp duties, personal graduation tax, fees on registration and licensing and any other fees and taxes that Parliament may prescribe.

Article 192 entrusts Parliament with the power to allocate the collection of certain taxes to local governments or on behalf of the Government for payment into the Consolidated Fund. Article 196 (a) instructs Parliament to make laws requiring each local government to periodically draw up a comprehensive list of all its internal revenue sources and to maintain data on total potential collectable revenues.

The second component of natural resources regulation, under the Constitution can be found within The National Objectives and Directive Principles of State Policy that is under Objective 9, the right to development, in order to facilitate rapid and equitable development, the State shall encourage private initiative and self-reliance, under Objective 11, the State shall give the highest priority to the enactment of legislation establishing measures that protect and enhance the right of the people to equal opportunities in development. Further, under Objective 13, The State shall protect important natural resources, including land, water, wetlands, minerals, oil, fauna and flora on behalf of the people of Uganda.

2.3.2. Income Tax Act (Cap 340), as amended.

The Income Tax Act (ITA) commenced in 1997 with the aim of consolidating and amending the law relating to income tax and for other connected purposes.

Section 4 of the Act imposes income tax on individuals or persons, as a tax to be known as income tax shall be charged for each year of income and is imposed on every person who has chargeable income for the year of income.

Under Section 7 of the Act, the Rate of income tax for companies. The chargeable income of a company for a year of income is charged to income tax at the rate prescribed in Part II of the Third Schedule to this Act while section 15 provides Chargeable income.

The main objective of this Act was levying tax on a residence basis, ensuring simplicity and promoting a flat tax rate scale. It took away power to grant discretionary exemptions from the Minister of Finance. It also: provided for accelerated and simplified depreciation allowances on productive assets; removed tax holidays offered under the Investment Code; introduced a presumptive tax for businesses; eliminated exemptions (e.g., for public servants and parastatals) and/or made them more stringent; introduced a capital gains tax on certain business transactions; and streamlined the withholding tax regime.[84]

2.3.3. Value Added Tax (Cap 349)

Value Added Tax (VAT) was introduced in 1996 at a rate of 17 per cent, replacing the sales tax and commercial transaction levy (CTL). Section 5 of the Value Added Tax Act, gives persons liable to pay tax as (a) in the case of a taxable supply, is to be paid by the taxable person making the supply; (b) in the case of an import of goods, is to be paid by the importer; (c) in case of an import of services, is to be paid by the recipient of the imported services.

Section 23 defines Taxable value of an import of goods as The taxable value of an import of goods is the sum of - (a) the value of the goods ascertained for the purposes of customs duty under the laws relating to customs; (b) the amount of customs duty, excise tax, and any other fiscal charge other than tax payable on those goods; and (c) the value of any services to which section 12(3) applies which is not otherwise included in the customs value.

[84]AfDB. (2010). Domestic Resource Mobilization for Poverty Reduction in East Africa: Uganda Case Study. Regional Department East Africa (OREA).

Section 18 defines Taxable Supply as (1) A taxable supply is a supply of goods or services, other than an exempt supply, made by a taxable person for consideration as part of his or her business activities; (2) A supply is made as part of a person's business activities if the supply is made by him or her as part of, or incidental to, any independent economic activity he or she conducts, whatever the purposes or results of that activity; and (3) The business activities of an individual do not include activities carried on by him or her only as part of his or her hobby or leisure activities, among others.

The VAT Act was generally easier to understand and interpret, [and therefore] huge strides were made to help compliance and improve transparency; and removed the Minister of Finance’s power to grant exemptions on a discretionary basis.[85] The VAT Act was amended in 2015 to: define certain terms used in the Act; increase the annual registration threshold; provide for tax treatment of the oil and gas and mining sectors. The VAT impacts capital inflow for sustainable development.

2.3.4. Excise Management Act (Cap 335)

The Excise Management Act, regulates the excise duties in the country.

Excise duties are levied on beer, wines, spirits, soft drinks, cigarettes and fuel, which are manufactured in or imported into Uganda, as well as mobile airtime. Section 39 specifies that duty shall be paid by a licensee on excisable goods manufactured by him at the rates and in the circumstances specified in the appropriate Partner State legislation: Provided that where any excisable goods on which duty has been paid are converted into any other excisable goods liable to a higher rate of duty, whether specific or ad valorem, then such converted excisable goods shall only be liable to duty at a rate equal to the difference between such higher rate of duty and the duty originally paid thereon. This affects the supply of petroleum products in the country.

2.3.5. East African Excise Management Act (Amendment) Act, 2012

The Act underpins the establishment of Common External Tariffs (CETs) and elimination of internal tariffs. It also brought about the harmonization of customs principles and procedures; and

[85] Ibid

removal of suspended duty. Section 114. (1) defines the Exemption regime. Duty shall not be charged on the goods listed in Part A of the Fifth Schedule to this Act, when imported, or purchased before clearance through the Customs, for use by the person named in that Part in accordance with any condition attached thereto as set out in that Part; (2) Duty shall not be charged on the goods listed in Part B of the Fifth Schedule to this Act when imported in accordance with any condition attached thereto as set out in that Part. Duty payable affects capital investment plans for the country.

2.3.6. Tax Procedures Code Act, 2014

The Tax Procedures Code Act provides for a code to regulate the procedures for the administration of specified tax laws in Uganda; and to harmonize and consolidate the tax procedures under the existing laws.

The objectives of the act are to: adopt uniform procedures for the registration, assessment and collection of all domestic taxes; promote efficiency in domestic tax administration by harmonizing, consolidating and regulating tax procedures in a single law; and streamline and simplify the administration and collection of taxes.[86]

2.3.7. The Local Government Act (Cap 243)

Section 80 of the Local Government Act 1997 (as amended) allows LGs to levy, charge and collect fees and taxes, including: Local Service Tax (LST); LG Hotel Tax (LGHT); Property rates and land-based charges like premium, building plan approval fees, land fees, etc.; Ground rent; Business licences; User fees (include market dues, parking fees), user charges and permits; Royalties from electricity generation, mineral mining and exploration and protected areas; Other revenues (such as forest fees; veterinary fees; registration of births, marriages and deaths; fines, among others.). In addition, Section 77 (1) empowers LGs to formulate, approve and execute their budgets and plans and to collect revenue and spend it.[87]

[86] URA. (2016). Tax Policy Changes FY 2016/201.

[87] Republic of Uganda. (1997). The Local Governments Act (CAP 243), as amended.

The study established that these legislation support the implementation of a better fiscal regime that would raise funds for the government but at the same time be balanced to attract and maintain investment.

These laws help in regulating the flow of the oil and gas sector and majorly how taxes shall be collected, setting up penalties to curb corruption and bribery in the sector and further encourage reporting; given that Uganda has now joined the EITI.

2.4 Uganda's fiscal policy as compared to other Oil and gas production countries.

It is quite clear Uganda's fiscal system is not a precedent, i.e. most of the provision within the fiscal regime have been tried and applied in other oil producing countries.

The World Bank[88], while commenting on the impact of fiscal policy in Uganda observes that inclusive economic growth in Uganda depends upon access to high quality services such as education, health, water and sanitation, better human capital development , and targeted social protection to reduce the vulnerability of the population to adverse shocks.

2.4.1. Uganda, Norway and United Kingdom

Norwegian petroleum system[89] is based on the taxation of the entity rather a specific asset and licensee and it doesn’t have ring fencing, its taxes includes among others royalty bonuses, income tax rate resource rent tax, production sharing agreement etc.

The united kingdom applies the low marginal rate taxes compared to Norway that almost charges similar taxes like royalty tax that was abolished in United Kingdom because of its declining oil reserves which have become uneconomically viable for the United Kingdom government to charge more revenues.

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[88]The Impact of Fiscal Policy in Uganda. November 19, 2019; via https://www.worldbank.org/en/topic/poverty/publication/the-impact-of-fiscal-policy-in-uganda accessed on 17th December 2021

[89]Section 23 of Norwegian petroleum Act.

When compared to Uganda and Norway, this is a huge determinant in designing the fiscal regime of any country. However higher taxes must not be attributed to vibrant fiscal effective regime but rather the type of oil and its uplift costs to that effect and costs of production are also very critical in an effective fiscal regime. Therefore, its Uganda and Norway that still maintain the royalty tax since Britain abolished this form of tax due its dwindling oil reserves.

Britain rather offers a more generous tax policy compared to Norway and Uganda that have progressive income taxes that are very high compared to U.K which includes royalty, bonuses and many other taxes. All these taxes are aimed at ensuring that the countries benefit from its oil and gas resource.

2.4.2 Uganda and Angola

Angola is a long-established petroleum province with exploration and production activities that can be traced back over I00 years. However, sustainable activity in the petroleum sector did not really get into gear until the 1980s, several years after independence and the end of the civil war. Initial efforts were focused on the onshore production and shallow water provinces and by 1990 production had reached nearly 500 thousand barrels per day. However, the real success story for Angola is the deep water which was licensed in the early 1990s and has resulted in a series of world class discoveries.[81] many of these are now in or soon to enter production. As a result, Angolan production is on steeply rising trend passing 1.7 million barrels per day in 2007 and expected to reach 2.5 million barrels per day by the early years of the next decade.

The Angolan Petroleum Fiscal taxation is often regarded as a model that succeeded in establishing a balance between investors' and the state's interests. Some argue that Angolan PSCs have onerous components, including relatively low and fixed cost oil, as well as high income tax plus high signature bonuses to secure the initial concession.

It should be noted that though, the signature bonus is a cost freely volunteered by the investor to win a competitive bid for the lease in question. Moreover, these elements are somewhat balanced by the absence of explicit royalties and an IRR-based sliding scale for profit oil (the higher the achieved rate of return, the higher the government share of profit oil);Very high prospectively also underpins the fiscal structure; recent exploration success in Angola has been amongst the best of any offshore basin, with a number of large discoveries.

Given this balance, Angola has clearly designed a fiscal regime that both encouraged a sustained high level of investment from and generated substantial revenues to the state.

Angola has built a solid reputation in the oil industry both in Angola and abroad. This is a direct result of strong relationships with the wide range of oil companies which operate, or which have interests and investments, in Angola. As a signal of Angola's capability, the company secured its first operated license in 2003. Most of Angola's exploration costs are carried by the IOCs and reimbursed with interest from its share of production.

The Angolan government encouraged inward investment from the IOCs by offering a stable and competitive fiscal regime based on production sharing contracts.

The fiscal terms for each PSC differ and are tailored to expected opportunities from each license area. Nevertheless, there are many common features and similarities between contracts are greater than differences. Typical features among others are: No royalty; Cost oil 50 per cent; Uplift - 40 per cent of capex; Depreciation 4 year's straight line; Profit oil splits are formulaic-ally linked to an earned project rate of return. Typical IRR-based profit splits are given in Table 3 below. This became the basis of all licenses awarded since 1991.

Prior to this date the profit splits on PSCs were linked to cumulative production, application and effective utilisation of the Production Sharing Agreements which Uganda has to borrow leaf in order to effectively maintain sustainable investment. There is indeed need to strike a balance between the state and economy interests and the interests of the International Oil Company.

CHAPTER THREE

STUDY METHODOLOGY

3.1. Introduction

This chapter centred on discussing the methodology used in the research study. It explores the research design, the data collection strategy/methods and the data instruments used in the study, how the data was managed and the analysis of the data, reliability, validity and the ethical considerations. Hence, this section reflects on the data collection strategy used during the research for example, reading different literature review and carrying out a comparative analysis. The primary research method for this study is literature review and theoretical framework. The research was undertaken to find out the impact of Uganda's fiscal system in encouraging and sustainable financing in the oil and gas sector.

3.2 Research Design.

A research design is the overall strategy chosen to integrate the different components of the study in a coherent and logical way, thereby, ensuring that one will effectively address the research problem.[90] The purpose of a research design is to ensure that the evidence obtained enables the researcher to effectively address the research problem logically and as unambiguously as possible. In this study, the researcher adopted the use of case study research design. A case study design is a study of a particular research problem rather than a sweeping statistical survey or comprehensive comparative inquiry.

3.3 Research approach:

The research approach implemented in this study was the qualitative research approach. This was because the study involved analyzing data collected through reviewing published literatures and the existing laws and policy related to fiscal policy. The justification for adopting this study approach is because it comprehensively facilitates the center of attention on obtaining relevant

[90]De Vaus D.A; Research Design in Social Research. London SAGE, 2006.

data that are collected through unrestricted tools and narrative in nature. As such, in this study the researcher collected qualitative data with the support of systematic literature review method.

3.4 Data collection method:

Data collection method is one of the key attributes that leads to an informed study findings; the methods used in a research undertaking must be sound and relevant. Arrays of[91] allude to the fact that in legal research systematic literature review is one of the most preferred method for collecting data in research particularly those that are secondary type of research. In this study, the researcher in essence adopted systematic literature review method to collect sufficient data. A systematic review identifies, evaluates, and synthesizes research results from authentic study reports to create a summary of current evidence that can contribute to evidence-based practice[92]. It's important to emphasize that systematic review methodology employs the same principles and rigor required in primary research. This method also facilitated the collection of legal documents such as the laws, policies.

3.5 Data Analysis:

In this study, the researcher adopted a content analysis technique to be able to validly analyze the various data that was collected with the aid of systematic review methods. Content analysis is a research data analysis technique used to make replicable and valid inferences by interpreting and coding textual material. The researcher supported this technique by using thematic analysis as well: thematic analysis is a qualitative data analysis method that involves reading through a data set for instance, transcripts from in depth interviews and thereafter identifying patterns in meaning across the data[93]. These two techniques played a key role in helping the researcher to be able to identify common themes in the data collected that are relevant to answer the research questions in order to fulfill the objective of the study in general.

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[91]Jindal-Snape, D., Hannah, E. F., Cantali, D., Barlow, W., & MacGillivray, S. (2020). Systematic literature review of primary–secondary transitions: International research. *Review of Education*, *8*(2), 526-566.

[92]Mulrow, C. D. (1994). Systematic reviews: rationale for systematic reviews. *Bmj*, *309*(6954), 597-599.

[93]Joffe, H. (2012). Thematic analysis. *Qualitative research methods in mental health and psychotherapy: A guide for students and practitioners*, *1*, 210-223.

3.6 Research Methodology

The study was conducted by way of qualitative doctrinal legal research which provides a systematic review of the rules governing a particular legal category, critically analyses the relationship between rules, and explains areas of difficulty and, perhaps, predicts future developments. Conventional legal research takes place in a law library to locate authoritative decisions, applicable legislation and any secondary discussion, reads and analyses the material, formulates a conclusion and writes up the study results.[94]

The nature of a qualitative doctrinal legal research methodology henceforth enabled me to analyze the literature reviewed. The need to appreciate and articulate the legal aspects of this research such as laws, statutes, case law doesn't require me to undertake data collection as this is knowledge that can be acquired through desk and library research methods. This was in furtherance of desk research method which reviewed review government published data such as laws, policies and regulations, textbooks and articles were reviewed to obtain and contextualize scholarly opinions for the guidance of this research.

3.7 Challenges faced in doing the study

There were some methodological challenges that were experienced by the researcher that to some degree affected the time of completion of the study and others affected the study findings to some minimal degree. A case in point, it was very challenging to get scientific scholarly information about the study; some publications required money to be paid. This challenge was overcome by the support of the supervisor who guided on where and how to get journals from authentic sources. There was difficult in carrying out data analysis and discussion; most of the techniques were strange to the researcher. However, the researcher had to consult widely, and the supervisor was very instrumental in overcoming this hiccup in the study undertaking.

3.8 Dissemination plans

In this study, the researcher plans to carry out a dissemination of the study findings using the following means; firstly, the researcher do thesis defence and thereafter there is plan to share the study findings inform of policy brief to the relevant stakeholders especial the concerned line

[94]Ibid.

ministries. And importantly, researcher stares to write a complete journal manuscript for journal publication, and finally a copy of the thesis will be share with the University for Library Usage such that students and the public can access it.

3.9 Study Limitations

It is of essence to acknowledge the fact that this study relied on secondary data and mostly yhe legal aspects; therefore, it may not be precisely correct to generally conclude that the independent variable perfectly informs the dependent variable is the study findings disclosed.

3.10 Ethical considerations.

Since this was a secondary analysis research, the researcher endeavoured to follow the associated ethical principles as indicated below; firstly, the researcher used referencing and citations to avoid plagiarism in this thesis hence maintaining the credibility of the information contained in this paper. Secondly, the researcher endeavoured to work with the appointed university supervisor throughout the research process, thirdly; all university rules concerning research ethics and procedure were followed including proposal defence and ultimately thesis defence.

CHAPTER FOUR

A COMPARATIVE ANALYSIS OF FISCAL POLICY AND SUSTAINABLE FINANCING OF SELECTED AFRICAN COUNTRIES

4.1 Introduction

In this chapter, the researcher ventured to carry out a comparative analysis considering how other oil producing countries in Africa have structured their fiscal regimes to enable sustainable financing of the oil and gas industry. The idea behind the comparative analysis is to figure out if Uganda is performing fairly well, and thus make appropriate recommendations if she is not.

4.2.1 Kenya

Previously before 1992, the exploration of oil and gas in Kenya was carried out under a Royalty Tax system under the mining Act 306. Subsequently, this Act was repealed or amends by the Petroleum Exploration and Production Act in 1992 which changed Kenya's fiscal system to the application and use of Production Sharing Agreements. Therefore, the fiscal system employs a sliding scale linked to daily production targets to determine production targets to determine the profit oil split between the national oil companies of Kenya where the later expects a fair share of return upon discovery of commercial quantities of hydro carbons.

When comparison is made with other East African countries like Uganda, Kenya is considered to have one of the toughest fiscal regimes because of its high state take.[95] This is because previously, the state participation was high in the oil and gas sector, which filled the sector with corrupt tendencies and the system was not effectively used to serve its intended purpose. Investment reduced and monopolies took over but steadily, this is being done away with. However, it should be noted that Kenya's current Production Sharing Agreement does not provide for payment of Royalties which makes the system more like a concession. This is the most preferred for oil majors but has been criticized government the first trench payments to meet citizenry demands [96]

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[95]Barrows, GH, World Fiscal systems for oil, Van Meurs & associates limited, Calgary Alberta1997.

[96]Deloitte: Kenya's petroleum Fiscal Regime. Expansive coverage October 2014.

Njeru[97] therefore argues that that the Kenya Fiscal Regime does not meet the Kenya Government objectives because it is regressive and inflexible to fluctuations of oil prices and costs. However, the Kenyan fiscal policy has transformed slowly to include royalty payments and given that the oil prices have subsequently stabilized. It is therefore safe to conclude that East Africa's fiscal system is now fully service contracts led, although this uniformity will be challenging as this bandwagon is disastrous in any event of catastrophe, change of environment conditions or social welfare.

4.2.2. Ghana

The government of Ghana opted for a hybrid system of production sharing and concessionary regime to govern contractual arrangement in the upstream petroleum industry11[98].The Ghana fiscal regime comprises of royalty, rent and income tax. Under this mixture of production sharing agreements and concession; both the host government and multinational company benefit through the collected profits as per the percentage that shall be defined under the agreement for each party. Given the fact that production sharing agreements the host government shall get royalty before the exploration or production is done and hence under concessions the cost oil shall be recovered by the international oil company which is fair to both the parties and also economically beneficial. This in turn promotes investment and on the other hand raises the revenue of the government.

4.2.3. Nigeria.

According to Ameh,[99] the Nigeria government formerly employed the use of joint venture agreements but since 1973, the country has adopted the usage of Production Sharing Agreements but they are concurrently used with Join Venture Agreements.[100] Joint Venture arrangements are guided by the joint operating agreements (JOAs). This specify the interest of each party and also is used as a basis for determining each party's share of costs, profits and losses accruing from the

[97]Karembu Antony Njeru: Kenya Oil & Gas Fiscal Regime; An Economic Analysis on Attainment of the Government Objectives.

[98]The Ghana policy Journal 2010 page 9

[99]A. O. AMEH: The Shift from Joint Operating Agreement to Production Sharing Contracts in the Nigerian Oil Industry: Any Benefits for the Players? CEPML Annual Review. 2006

[100]Ameh (ibid)

oil and gas operations. The Nigerian Joint Ventures however, registered some weaknesses like; late payment of government share of cash-calls to the Joint Venture operator. The biased sharing of revenues and costs and reduced government control of oil and gas resources.[101]

As earlier noted the Nigeria government also applies the usage of Production which were introduced by the Nigerian Petroleum Act of 1969 and put into use in 1973. Production Sharing Agreements were embraced for offshore activities because of the advantages including; provision bigger part of the capital needed for exploration by the International Oil Company, more control of operation by the Host Government of oil and gas operations. The Nigerian government unlike other developing countries which adopt one fiscal regime, is wiser in that in appears two regimes intertwined in that it gives options to the contracting oil company to choose what shall benefit its interests hence promoting investment through the policy being favorable.

After a comparison of the countries' fiscal regime, it can be with authority stated that all these countries employ the application of PSAs within their fiscal regimes. However, as will be observed, much as these Agreements are conducive to apply by low developing countries as they are easy to manage, but in the long run the country loses income because of the many favors created for the International Oil Company. But by far and large, fiscal agreements in most cases provide efficiency in the accumulation of capital by the Oil Company and the availability of capital itself leads to the development of sustainable financing.

4.3 Uganda's Fiscal policy Potential and Sustainable financing in oil and gas industry

The European commission defines sustainable finance to be the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects[102]. Environmental considerations might include climate change mitigation and adaptation, as well as the environment more broadly, for instance the preservation of biodiversity, pollution

[101]AL-ATTAR. O. and O. ALOMAIR: Evaluation of upstream petroleum agreements and exploration and production costs. OPEC review, 29() (2005), pp. 243-266

[102]https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en accessed on the 3rd day of March 2021

prevention and the circular economy.[103]Social considerations could refer to issues of inequality, inclusiveness, labor relations, investment in human capital and communities, as well as human rights issues.[104] It should be noted that in this study, the researcher linked sustainable financing as it's attributable to the following factors including but not limited to availability of capital, capital investment efficiency, impact investments, and lasting benefits.

According to Nicholls[105], availability of capital depends on how a country can align her will to meet the investors' preferences to fit the demands of the economy. It is through the availability of capital that the MNC will derive the will to provide investment of that capital to bring returns and benefits to the investor. Therefore, for an MNC to undertake a specific exploration in a given country, and to make a decision about where to inject their funds, they do consider the above ESG, and specifically in the oil and gas sector, an investor will look at how the fiscal system is structured in a given country. Basically, it is argued that a favorable fiscal system should provide room for the benefit of both the host country and the oil company.[106]

A system should be designed to balance between the state's objectives and those of the company that is, the state is all concerned with collecting revenue. Therefore the fiscal system must put on mechanisms that ensure that the investor or funder earns her return of investment.[107] Uganda's fiscal policy provides for allowable deductions which include initial allowances, decommissioning costs, loss carried forward and tax exemption of machinery and equipment and depreciation allowances. Therefore, it is pertinent to observe that is this would enhance sustainable financing. The fiscal system of Uganda has a few of the instruments that move forward to encouraging sustainable financing.

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[103]Ibid (Note 46)

[104]Ibid (Note 46)

[105]Alex Nicholls; Sustainable Finance: A primer and Recent Developments Accessed via www.adb.org

[106]Daniel J: International Petroleum Fiscal systems and Production Sharing Contracts. Tulsa, Oklahoma, PennWell Publishing Co. 1994.

[107]Daniel. J: International Fiscal Systems and Production Sharing Contracts. Tusla (Oklahoma), 1994

4.3.1 Resource Rent Tax.

Resource rent is intended to capture the economic rent. It is progressive tax based on profitability after the international company earns a minimum rate of return. In principle the Resource Rent Tax applies after a target real rate of return on the investment has been realized. In practice, the target rate of return is often set as a mark-up on the return from a safe alternative investment, with the mark-up representing a country specific risk premium. Resource Rent Tax is calculated by increasing the annual cash flow (typically without deductions for interest cost and depreciation allowances), which is initially negative because of the investment outlay, by the target rate of return, and continuously carry this forward until it turns positive.

The ideal reason behind this policy/tax is that it serves as a tax holiday to the Oil Company as it is it is taxed on the cumulative profits of the Company. The implication is that the capita for investment will always be available and if managed well, it will be efficiently utilized.

4.3.2. Brown Tax

This is the tax according to the cash flow of the venture and this normally incorporates the different costs incurred by the oil company in the process of exploration and normally encourages risk sharing between the parties[108]. Although it is taken as a huge gamble for the government to encourage this tax because it puts a huge level of risk onto the government, in Uganda the losses made before production are allowable deductions.

Given this leeway for investment, a company (MNC) will find it comfortable to go ahead with financing the oil or gas projects undertaken; give that no tax will be incurred at the start of the exploration process. Further, this ensures that the company has its capital always available for investment instead of it going to taxes for no production done or mineral got yet. This serves as a tax holiday to the oil company.

4.3.3. Tax Holidays.

Under tax holidays, the government waives tax obligations of oil companies during a specified period of time, as agreed by the parties. Tax holidays persuade the oil company through providing

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[108]Carole Nakhle; Petroleum Taxation: A critical evaluation with special Application to the UK continental shelf. Page 35-36

definitive terms of exemption from tax which will mean that the company operates without remitting fee in tax to the government.

As earlier observed, among the elements of sustainable financing include long lasting benefits. Countries through holidays provide subsidy to an oil company for a quiet period of time to even a period of five years' tax free, rarely will a company take down this offer. The company considers its interest and long term investment benefits before anything; after all MNCs are money-centered entities who care much about profit than anything else.

4.3.4. Tax Abatement.

Abatement of tax is the reduction of the tax that the licensee primarily ought to have paid. In 2015, the Parliament of Uganda passed a resolution under the **VAT Amendment Bill (now Act) 2015** that the country will no longer charge the 18% VAT on oil production companies. This move came in a bid to encourage more investment in the country. Like other tax holidays, exemption of VAT on oil production companies basically is a benefit to the company as there is currently no given period within which this will be revoked. But this reduces the tax burden of the company and in turn raises the capital availability of the company and will encourage further investment and subsequently boost sustainable financing.

CHAPTER FIVE

STUDY FINDINGS AND ANALYSIS

5.1 Introduction

This chapter presents the results of the research study undertaken and provides an insight of the findings of the research. The chapter goes ahead to point out what Uganda's fiscal regime entails and if indeed it sustains financing in the oil and gas sector. The researcher presents views of notable writers about the issue at hand and their perception of a favorable fiscal system to attract investment and marinating sustainable financing.

5.2. Uganda's Fiscal Regime and Sustainable Financing.

Throughout the study, the researcher discovered that Uganda uses Production Sharing Agreements in the exploration and exploitation of oil and gas in the region. Production Sharing Agreements involve understanding between the Host country and the International Oil Company (IOC). Under this arrangement, the government has control other crucial Investment decisions that is, makes the Final Investment Decision (FDI) in the exploration of the oil but does not interrupt or interfere with the operations of the International Company, which is privately owned.

PSAs are agreements in which the government contracts a private company to carry out oil or gas operations while the government retains ownership over the oil or gas reserves. If oil or gas is discovered and subsequently extracted, the contractor is entitled to a share of production to recover capital expenditure and reimburse operating costs, usually up to a ceiling, or 'cost recovery limit'. This share of production is called 'cost oil'. The rest of production ('profit oil') is shared between the government and the contractor according to the shares set out in the PSA. In addition the contractor is normally required to pay corporation tax on 'taxable income', or profit.[109] Uganda's Production Sharing Agreements in its nature encourages investment as taxation of the product oil is made after exploitation.

[109]Johnston B (supra)

5.2.1. Royalties.

In addition to the single royalty in the pre-2008 PSAs that is based on daily production, the 2012 PSAs contain an additional royalty based on cumulative production which is an unusual PSA revenue provision in favor of Uganda. With the additional royalty, revenue will continue to accrue even when oil extraction starts declining because the cumulative royalty it is assessed based on the amount of oil extracted from the time production started. This implies with increased rate of oil production, the rate of royalty.

Therefore, PSAs of Uganda provide for incremental royalties. Because royalties are deducted from production before cost recovery, they guarantee upfront revenue for government soon after production begins. The royalty on gross daily production will be charged at rates between 5-12.5% depending on the level of production, while additional royalty on cumulative production will be charged at rates of between 2.5-15%. Thus, Uganda's royalty regime has an in-built profit element[110]. Royalty payments are tiered, so if daily production was 6,000 barrels then the company would pay 5% on the first 2,500, 7.5% on the next 2,500 and 10% on the remaining 1,00021.[111]

5.2.2. Cost recovery

The recoverable costs are pooled together each year and reduced by the cost oil received. In other words, cost oil refers to an oil company's entitlement to production as cost recovery under a PSA. This means an oil company gets cost oil from which it deducts recoverable cost when commercial oil production has commenced. The company recovers '*cost oil'* which is the '*reimbursement*' for the costs incurred in the exploration phase and some (or all) of the costs incurred during the development and production phase.[112] The Uganda PSAs provide that the amount to be retained as cost oil is 60% of total oil production after deducting royalty. If cost oil is less than the costs available for recovery, any unrecovered costs are carried forward to subsequent years until their full recovery.is completed. However, if cost oil is more than the recoverable costs, the excess of

[110]Global Witness, A good deal better? Uganda's Secret oil contracts explained accessed via https://www.globalwitness.org/en/reports/good-deal-better/ on the 7th day of May 2021

[111]Global Witness (ibid)

[112]PWC (supra)

the cost oil forms part of the profit oil. The recoverable costs incurred in respect of license area can only be offset against oil produced from that area.

This practice, called "ring-fencing", prevents companies from recovering costs for areas where no commercially viable oil reserves are found. Therefore, costs for areas where no oil is found are borne by the company. The government must approve recoverable costs before they can be reduced from cost oil. This is likely to raise governance issues such as rent-seeking and corruption, which might ultimately pose a risk of revenue leakage.

5.2.3. Ring-fencing

Corporate tax is a key element of oil PSA imposed on the 'taxable income' of a contractor computed on a block-by-block basis. The costs incurred in respect of one block cannot be used to reduce income from other blocks. Ring fencing bars consolidation of income and deductions for tax purposes across various t oil activities and projects undertaken by the same taxpayer. 'Ring-fence' applies to both income and expenditures. By ring-fencing tax accounts of individual blocks in accordance with the provisions of the PSAs, corporate tax deferral is effectively curtailed. This measure helps to streamline oil taxation in order to secure government revenues.

5.2.4. State Participation

Under the 2012 and 2016 PSAs, Uganda will get 15% of the oil company's share of profit oil under state participation provisions should government opt to exercise its right to participate in oil development and production. Indeed, through the UNOC, government elected to take its participating interest in all the eight production licenses so far issued at a level of 15% in accordance with the PSAs. The oil companies will meet Government's costs but the companies are entitled to recover these costs, including interest at the London Inter-Bank Offer Rate (LIBOR), out of the cost oil. The government is therefore entitled to a proportion of the oil produced and saved from each contract area equal to its 15% interest in the joint venture assets. UNOC will dispose of the state's share of profit oil at a price determined by the Multi-institutional committee28 and remit the sales proceeds to the Petroleum Fund operated and managed by Bank of Uganda as per the Public Finance Management Act, 2015.

5.2.5. Capital Gains Tax

Capital Gains Tax (CGT) Capital Gains Tax (CGT) is imposed on a gain made on the assignment or transfer of an interest in an oil license from one contractor to another.[113]

The determination of a gain on disposal of an interest in an oil license is governed by the provisions of the Income Tax Act. Taxable gains arise on disposal of business assets such as company shares or commercial property and an interest in an oil license either directly or indirectly. An indirect transfer takes the form of the sale of shares in a company whose assets are principally immovable property located in Uganda. It often involves non-resident shareholders selling their interests to a resident company. Because of the difficulty of collecting taxes from nonresidents, the CGT is paid by the resident oil company acting as an agent of the non-resident company.

For example, the CGT of USD 449m on the Heritage's transfer of its assets to TUL was paid by TUL acting as agent of Heritage. It should be noted that CGT is not a reliable revenue source because it arises only when a business asset is transferred or assigned. Besides, it is difficult to determine the cost base of an oil interest in case the interest in question is being transferred to a third owner. For instance, one of the issues[114] contested when TUL disposed of the interest it had acquired from Heritage to Total E&P and CNOOC was the determination of the cost base. In practice, the cost base is the base price paid for the interest plus incidental costs of the disposal. The incidental costs include contingent, guarantee and commitment fees, stamp duty on acquisition, legal fees and signature bonuses.

As a result of the CGT disputes, the current PSAs clearly provide that a transfer of an oil interest shall attract CGT in accordance with the ITA, and that tax disputes in relation to the PSAs shall be handled in accordance with the dispute resolution mechanisms stipulated under the Laws of Uganda. Global Witness (2014) maintains that the UgandaHeritage arbitration in London over the CGT assessment relating to the 2010 farmdown to TUL was far from settled.[115]

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[113]89G (a) of Income Tax Act cap 364 as amended

[114]https://www.casemine.com/judgement/uk/5a8ff74860d03e7f57eaad02 accessed 23rd April 2021

[115]Global witness (supra)

5.2.6. Renegotiation and Stabilization Clauses.

The oil and gas production contains a lot of uncertainties which include, political instability, change in climate and change in fiscal regimes.

While both governments and investors share a common objective (to maximize the exploitation of the hydrocarbon resource) governments generally want to ensure a fair share of the resource for the nation; investors, on the other hand, wish to ensure a minimum return on investment and a simple and stable tax regime. The difficulty with these objectives is that the interaction between governments and investors is dynamic, making enduring fiscal stability a very challenging proposition in practice.

Investors and governments attempt to neutralize these uncertainties by putting in place stabilization clauses; these come in different forms, but their main objective is to lock in fiscal terms for the duration of a project. The term 'stabilization' refers to the attempt to avoid potential conflicts or risks with respect to the alteration of the regime in which the project takes place.[116]

In the case of Uganda, a stabilization clause can be traced under Article 30.2 of the 2012 Production Sharing Agreement Model which provides for renegotiation of the agreement to fit the terms of the agreement/contract in case of a regulatory change within the host government.

5.3. Influence of Fiscal Policy and Sustainable Financing in Oil and Gas Sector in Uganda

Uganda's fiscal policy/regime is premised on Production Sharing Agreements i.e. the host government and the oil company agree that the oil company; which has the funds will explore the oil and gas fields and is entitled to a share after production and on the other hand, the government earned through taxation in royalties and capital gains tax among others.

5.3.1. Royalties and Cost recovery

Uganda's Production Sharing Agreements allow the oil company to recoup up to 100% of gross production after the deduction of royalties. Thence, the oil profit after cost recovery is shared

[116]Erkan, Mustafa: International Energy Investment Law: Stability through Contractual Clauses', Walters Kluwer Law & Business. 2010, page 101

between the government and the licensee. This implies that the licensee (oil company) is highly likely to keep injecting her funds in the project since all that was incurred by the company shall be reimbursed after production. This is persuasive enough to the investor or any funder and stimulates production. A study can be seen at the competitive desires by companies like Total EP and CNOOC to take over exploration of Uganda's oil fields.

It should be noted that in a delicate area like oil and gas where the resource has in many countries turned disastrous because of the oil curse,[117] it is crucial that a perfect or suitable fiscal policy is adopted by a country. Lessons have been learnt from other oil producing countries by the Uganda government and the current fiscal policy is a reflection of the same, that is, the construction of the current fiscal model indicates that there is need for transformation for the betterment of the sector.

Further, it was observed that the fiscal policy provides for advance payments in form of signature bonuses that will be reimbursed to oil companies by allowing future cash flow to be discounted at higher rates, which is an incentive for oil companies to finance more in the country. Royalties generate government revenue as soon as production commences and will enable oil companies to make minimum payments for oil extracted.

5.3.2. Stabilization clauses.

Further, Uganda's PSAs contain stabilization clauses that assist both the government and the oil companies to renegotiate the contracts for example in the event of change is geology or hydrocarbons.

Oil and gas projects are, by their very nature, long term, particularly those that are offshore and in locations remote from markets. They are also capital extensive with large sunk costs. The main expenses incurred in the initial stage of investment relate to exploration and development; the bulk of such expenses cannot be recovered if the economics of the project change at the time of production and commercialization because of changes in domestic laws. There is also a significant time lag, often of several years from the initial discovery of oil or gas reserves to the time of first production. Payback on the initial exploration investment can take decades.

[117]For example Nigeria, Sudan, Angola

Therefore, time creates the time/dynamic inconsistency problem, which occurs when a government starts with a specific policy but, after conditions change, finds it welfare-increasing to go back on the commitment implied by the policy.

Hence, a stabilization clause is a contractual risk-mitigating device to protect investments from variations in the legal environment. This would include risks deriving from a possible exercise of host state sovereignty such as: expropriation, the obsolescence bargain, or any other change which the government might utilize in order to impose new requirements on investors.[118] Existence of these clauses enables the oil company to skip the risk of loss in case of changes in geology or political environment. With such a policy, the oil company will not have to hesitate to make decision to continue with financing oil and gas in Uganda.

5.3. Extractive Industries Transparency Initiative (EITI)

Recently, the Uganda Government joined the EITI in a bid to promote transparency in the oil and gas sector. According to the *Statement of Principles and Agreed Actions*[119], the Iinitiative encourages governments, publicly traded, private and state-owned extractive companies, international organizations, NGOs and others with an interest in the sector to work together voluntarily to develop a framework to promote transparency of payments and revenues. The Initiative is grounded in a shared belief that the prudent use of natural resource wealth has the potential to provide the basis for sustainable economic growth and development.[120]

It should further be noted that the EITI is based on twelve principles to sustain its operation which include that the prudent use of natural resource wealth should be an important engine for sustainable economic growth that contributes to sustainable development and poverty reduction,

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[118]Jardim, Pedro Henrique: 'Are Investment Protection Mechanisms Provided by Brazilian Law as Effective as Stabilisation Clauses for Petroleum Investments?', Centre for Energy Petroleum Mineral Law and Policy, University of Dundee, 2011.

[119]Statement of Principles and Agreed Actions: EXTRACTIVE INDUSTRIES TRANSPARENCY INITIATIVE (EITI) London Conference, 17 June 2003

[120]Ibid (note 81)

but if not managed properly, can create negative economic and social impacts, as the first principle.[121]

Globally, the EITI has provided significant effects in the extractive sectors especially among the member countries, which include promoting accountability and ensuring good governance. The standard operates through regular implementation and outreach progress reports. These are confidential Reports prepared by the International Secretariat and the Implementation Committee and submitted to the Board prior to a Board meeting monitoring validation results, key performance indicators of the International Secretariat, External evaluations of the EITI.[122]

On the country basis, every year, each implementing country is required to update a fully-costed work plan to reflect the objectives and actions of the national EITI. The work plan is required to reflect how the EITI relates to progress, At the end of each year, each implementing country is required to produce an Annual Progress Report (APR) that reflects and monitors the progress against the objectives and actions set out in the work plan and any impact the EITI has had.[123] The joining of the EITI by the Uganda government boosts the confidence of oil companies in the government and its intention to promote transparency by fighting corruption in the sector of oil and gas. This is seen as an effort to fight the 'oil resource curse.'

5.3. Bribery and Corruption in the Oil and gas sector and the extractive sector.

The term corruption has been defined as "the abuse of entrusted power for private gain."[124] Corruption has many adverse effects and it weakens the development of countries.

The African Union Convention on Preventing and Combating Corruption in its preamble acknowledged the negative effects of corruption and impunity on the political, economic, social

[121]Ibid (Principles) note 81

[122]https://eiti.org/outcomes-impact-of-eiti accessed on the 20th March 2021.

[123]Ibid (note 27)

[124]Transparency International, http://www.transparency.org

and cultural stability of African states and its devastating effects on the economic and social development.

According to the Convention, corruption undermines accountability and transparency in the management of public affairs as well as socio-economic development on the continent.[125]

While linking corruption to the crisis of underdevelopment, Michael stated thus: "Corruption has led to bad roads and decaying infrastructure, inadequate medical services, poor schools and failing education standards and disappearance of foreign aid and loans and of entire project without trace."[126]

Uganda has always had a reputation of being corrupt. Corruption has entered into every fabric of existing systems in the country and according to the Transparency International Corruption Perceptions Index 2019,[127] Uganda ranked 137 out of 180 countries and territories with a very low score of 28 out of 100,[128] the level of corruption still in the country cannot be said to be satisfactory, and there is still a long way to go to eradicate corruption in the country. The effect of corruption on the Uganda's economy is grave; corruption is in virtually all the sectors of the country. Corruption influences foreign investment decision in the country and therefore should be eliminated.

Studies have shown that at least a half of the revenue that should be collected can be lost by government treasuries through corruption and tax evasion.[129] Opportunities for corruption among tax officials arise in the context of corruption-perpetrating networks, wage differentials, corrupt

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[125]The African Union Convention on Preventing and Combating Corruption, available at http://www.africaunion.org/root/AU/Documents/Treaties/Text/Convention%20on%20Combating%20Corruption.pdf

[126]Michael O. B (2012), "The Place of Law and Other In The National Transformation Agenda: The Nigerian Experiment." Text of speech delivered by at the annual lecture organized by the Nigerian Bar Association, Ado-Ekiti Branch Law Week

[127]Transparency International, http://www.transparency.org/cpi2012/results.

[128]Transparency International Corruption Perception Index 2019. The Corruption Perceptions Index ranks 180 countries and territories by their perceived levels of public sector corruption, according to experts and business people. The 2019 analysis shows that corruption is more pervasive in countries where big money can flow freely into electoral campaigns and where governments listen only to the voices of wealthy or well-connected individuals. In 2019 Uganda scored 28/100 (0- very corrupt and 100 very clean- zero corruption) and ranked number 137 out of 180.

[129]SEATINI Uganda, TJNA & Oxfam Novib, 2012

management, and in the context of poor internal detection and punishment mechanisms. Officials' corrupt actions often take one of two forms: they are either abusive, whereby officers extort from honest taxpayers; or are collusive, in which case they condone and benefit from the corrupt behaviour of tax avoiders.[130]

Although Uganda Revenue Authority has tried to counter corruption through computerized tax processes which reduced the contact between taxpayers and tax officials, the vice is still rampant in Uganda.

In the extractive sector, the existence of corruption drives on the what has been termed by many writers as 'the oil curse.' This curse has been far more existent in developing countries; which Uganda is among.

Throughout the research, the researcher was able to establish that corruption case exist in the country and more so in the oil and gas sector. For example, up to date, the government has failed to release the real four Production Sharing Agreements of 2016 signed by the government, on behalf of the people and, the multinational oil companies. Further there has been reported cases of forced land evictions and acquisitions in the Albertine region and failure of compensation of the lawful land occupants[131] Furthermore, the licenses by Uganda to Tullow, Total and CNOOC were granted in direct, non competitive closed negotiations.

In 2013, Ministers, Hillary Onek, Sam Kuteesa and the Prime Minister Hon. Amama Mbabazi were accused of high revenue manipulation and embezzlement offences in collusion with oil companies and most recently, the Southern District Court of New York found Hon. Sam Kuteesa received about USD 500,000 from a chinese company for purposes of promoting the company's interest in the Uganda oil and gas sector.

Corruption is an in depth vice that puts the roots of every economy on the balance and when the case comes to the oil and gas sector, especially in developing countries like Uganda, the effect is

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[130]Bridi, A. (2010). Corruption in tax administration. U4 Expert Answer. Transparency International.

[131] Years After Eviction by an oil extraction project, a Ugandan Community waits for justice; https://globalvoices.org/2019/06/21/years-after-eviction-by-an-oil-extraction-project-a-ugandan-community-waits-for-justice/amp/ accessed on 18th December 2021

lethal. It among others leads to poor policies (biased), laws and a regime that less taxes the oil multinational companies like the case with Uganda oil laws. This implies that the the implementation of the Extractive Industries Transparency Initiative will be quiet challenging since the implementers are the implicated perpetrators at the same time. But that notwithstanding, a well streamlined fiscal policy in the country shall curb this habit although it shall be quiet challenging.

CHAPTER SIX

CONCLUSION AND RECOMMENDATIONS

6.1. Introduction

In this chapter, the researcher presents summary of key study findings; this study findings are informed by the research objectives, the researcher also makes some recommendations which are based on the study findings, and finally make a general conclusion regarding the purpose of the study.

6.2. Summary of findings and conclusions

It's obvious; the motive of the government for participating in the oil and gas activities is to maximize the economic rent as part of their take from oil and gas production revenues. Although, there are other related benefits for example access to technology, capital, knowhow and market.[132]

It has been observed that efficient fiscal systems as those that encourage exploitation, promote development of both small and large reserves, allows special incentives for difficult to explore/develop and enables equitable sharing of economic benefits.[133] The government thus is interested in an adequate return for the state and its economic development. But it is also fundamental to provide terms that would permit the International Oil Company to get a return commensurate to their investment.[134]

It has already been noted that Uganda's fiscal regime applies use of Production Sharing Agreements, these agreements provide for realization of profits for both the parties therefore the country has managed to pull royalties amounting to 12%.[135] The 2012 Production Sharing

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[132]Johnston (supra)

[133]DEMIRMEN.F: Win-win Upstream Fiscal Systems: What They Are and How to Achieve Them", SPE Hydrocarbon Economics and Evaluation symposium, Dallas, Texas, USA, 8-9 March 2010, Society of Petroleum Engineers.

[134]Faruque, Abdullah, Shifman, Bette, and Hascher, Dominique: 'Validity and Efficacy of Stabilisation Clauses Legal Protection vs. Functional Value', *Journal of International Arbitration*, vol. 23, number 4, pp, 317–36.2006

[135]See note 8

Agreements provide for a possibility of collecting windfall profits taxes in cases of a rise in oil prices, which adds to the amount of revenues potentially collectable from the oil sector.

It can be noted out of the 2012 PSA Model that it provides for daily and cumulative production royalties. Thus, as overall cumulative production rises, so will government revenue from this additional royalty. The cumulative production royalty is a rare revenue clause of PSA which will generate more revenue for Uganda based on the magnitude of the oil produced in a given licensed area.[136]

Further, it can be pointed out that the Uganda Production Sharing Agreements regime employs the usage of stabilization clauses. Piero Bernardini[137]notes that stabilization clauses are aimed at preserving the contractual terms and conditions as originally agreed by the parties but not modifying the agreement.

Stabilization clauses therefore protect international oil companies against regulatory changes that impact project profitability and thus provide assurance to the oil companies who meet upfront costs and risks that they will recoup their investment without government having to impose undue regulatory burdens on them by encouraging companies to undertake oil sector investments.

However, **Bahati and Beyeza**[138] note that cumulative royalty may lead companies to opt out of the project early because it may reduce profit that the company expects as companies pay higher royalty rates even while production is falling and that the royalties discourage investments by increasing the marginal cost of oil extraction. This notwithstanding, the Uganda fiscal system has successfully managed to attract oil exploration and production companies that include Tullow Oil, Heritage among many others and the construction of these agreements has proven encouraging and favorable to both parties under the contract.

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[136]Wilson Bahati Kazi & Babra Beyeza: Getting a Good Deal? An Analysis of Uganda’s Oil Fiscal Regime. CRPD Working Paper No. 64 December 2018

[137]Piero Bernardini; Stabilization and adaptation in oil and gas investments. Journal of World Energy Law & Business, Vol. 1, No. 1 (2008)

[138]Ibid Note 28

Uganda's fiscal regime is well designed to encourage the flow of investors in the country and is planned exactly to fit the needs of the country to develop it if this policy is well utilized not to turn into the oil curse.

6.3 Study recommendations

Current government fiscal measures in the oil and gas sector should be focused at unlocking the expected and retaining investments and promote sustainable financing in the oil and gas sector. Bottlenecks to sustainable financing like regressive taxes should be eliminated or avoided.

A fiscal regime/policy plays a significant role in balancing the interests of the oil majors and those of the host country. A fiscal regime should not only protect the interest of the host Government but also provide incentives to the oil majors who have invested in the sector in order to be retained or attract new investors in the sector.

It is recommended that the government should put more effort on implementation of this regime and fight corruption that has started to engulf the sector. For the petroleum fiscal regime to be competitive, it should be designed to reflect neutrality, equity, stability and certainty. There should be tax diversification with efforts being directed from over concentrating on oil taxes to non-oil tax bases.

There is also need for the Uganda Petroleum Authority to continue updating information and data in connection with geology of prospective blocks.Given the volatile nature of the industry investors are easily attracted and maintained if the geological prospects are clear. This is practiced in Indonesia and Uganda should adopt this best practice.

The financing charges as cost recovery item should be removed from the model PSA .As recommended in the World Bank Technical Assistance Report[139], since a PSA is analogous to an un incorporated joint venture where each party is obliged to provide financing, irrespective of the source whether (equity or debt) and doesn't change interest costs to the venture as a whole It follows that calculations of PSA are made as cash flows of total funds not on returns to equity with the result that recovery of interests as a cost is not warranted. This will generate enough revenue for the state and will not hurt sustainable development.

[139]Fiscal Regimes for extractive industries .International monetary Fund Uganda ;Report 2015

Uganda's fiscal regime should be tailored to take into account of the volatile nature of the petroleum industry and the peculiar features of the industry nature like the long lead time from exploration to production, capital intensive nature and high risk profile.

6.4 General conclusion

In conclusion, it can be observed that the study largely attained its intend objective of analyzing the legal regime especially the fiscal policy related to oil and gas financing. From the study findings, it's clear, without any doubt, if and when the existing fiscal regime is carefully implemented it will invariable play a vital role in attracting foreign direct investments thus providing capital for a sustained financing of the activities of oil and gas in Uganda

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