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BUILDING STRONG INSTITUTIONS AS A PREREQUISITE FOR PREVENTING THE OIL CURSE SYNDROME: HOW PREPARED ARE THE NATIONAL AUDIT INSTITUTIONS IN PREVENTING THE OIL CURSE SYNDROME?

A CASE STUDY: OFFICE OF THE AUDITOR GENERAL OF UGANDA.

By

GODWIN BOB MONDAY

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A Dissertation submitted to the Centre for Energy, Petroleum, Mineral Law and Policy of the University of Dundee in partial fulfilment of the requirements for the award of the Degree of Masters in International Oil and Gas Management

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I, therefore, dedicate this piece of work to my entire family and especially my dear mother (RIP), and for God and my Country.

Abbreviations

AAG	Assistant Auditor General
ACCA	Association of Certified Chartered Accountants
AFROSAI-E	African Organization of Supreme Audit Institutions –English speaking
AG	Auditor General
bbd	Barrels per day
CAATS	Computer Aided Auditing Techniques
CG	Central Government
CNOOC	China National Offshore Oil Corporation
COSASE	Committee on Statutory Authorities and State Enterprises
CPAU	Certified Public Accountants of Uganda
CPI	Corruption Perception Index
DRC	Democratic Republic of Congo
EIA	Energy Information Administration
FCM	Full Cost Method
GDP	Gross Domestic Product
HR	Human Resource
IAS	International Accounting Standards
ICBF	Institutional Capacity Building Framework
IFRS	International Financial Reporting Standards
INTOSAI	International Organization of Supreme Audit Institutions
IOC	International Oil Company
ISSAI	International Standards for Supreme Auditing Institutions
IT	Information Technology
LG	Local Government
LGPAC	Local Governments Public Accounts Committee
MEMD	Ministry of Energy and Minerals Development
MIS	Management Information System
MOU	Memorandum of Understanding
MPs	Members of Parliament

NAA	National Audit Act
OAG	Office of the Auditor General
PAC	Public Accountability Committee
SAIs	Supreme Audit Institutions
SLM	Straight Line Method
SORP	Statement of Recommended Practices
UAE	United Arab Emirates
UK	United Kingdom
UOP	Unit of Production
US	United States
VFM	Value for Money

Abstract

Uganda is one of the developing economies in Sub-Sahara Africa. The recent discovery of oil in the country raises greatest hopes amongst many Ugandans that the oil revenues will turn around the economic path of the country, thus improving their welfare significantly. But this is always not guaranteed, especially, when the revenues from the petroleum resources are poorly managed, thus leading to a resource curse syndrome. This Project, through literature review and empirical evidence found out that many resources rich countries in sub-Sahara Africa have not benefited from their natural inheritance due to reasons, which included: corruption; rent seeking; inequality; inadequate industrial policies, such as un controlled government spending, ineffective stabilization funds, and lack of economic diversification; lack of good governance and the rule of law; underdeveloped financial systems; and more so, the poor institutions, which lack institutional capacity to properly manage the oil revenues. This Project further found out that supreme audit institutions (SAIs) were in a better position, due to their autonomous independence and strong legal mandates, to prevent the resource curse syndrome through auditing thereby promoting sound financial systems and in their ability to play an oversight role. However, taking the SAI of Uganda as a case study, the project found out that SAIs needed much more preparation to gain total audit independence, especially the financial independence; obtain leverage on their existing organizational setups; acquire competent staff and skills in the field of petroleum audits; greatly improve their audit methodologies, and review auditing standards to accommodate the intricate transactions associated with the petroleum sub sector; and improve on the ways they communicate their audit results to promote accountability and transparency. This Project concludes by emphasizing that building strong institutions, especially, SAIs will go a long way to preventing the resource curse syndrome.

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CHAPTER ONE

1.0 INTRODUCTION

1.1 Research Background

Uganda is one of the developing economies in Sub-Saharan Africa. The country's GDP per capital of US Dollars 572 ranks it among the poorest countries in the world. With a population growth rate of 3.3%, it ranks 6th amongst countries with highest rates (World Bank, 2013)[1]. According to the World Bank, the country's current population is estimated at 37.6[2] million people with a low life expectancy at birth of an average age of 58.6 years. Unemployment rate grew from 1.9% in 2006 to 4.2% in 2010, and 24.5% of the population are poor[3].

The discovery of oil in Uganda in 2006[4] and Government's ambitions of starting early production in the next 5 years[5] raises hopes amongst many Ugandans that the oil revenues will turn around the economic path of the country, thus improving their welfare significantly through government's provision of better services, such as: Education, Health and road infrastructure, etc. (National Oil and Gas Policy, 2008, Sections, 4.3 and 4.8).

Parliament of Uganda is constitutionally entrusted with the oversight role of ensuring that the Executive performs its responsibilities and as a result it established the Office of the Auditor General (OAG) to facilitate conducting its oversight role.

The National oil and Gas policy, 2008, Section 5.1.7, identifies capacity and institutional building as one of its key guiding principles in enabling the country to participate in, and benefit

[1] http://data.worldbank.org/indicator
[2] The National Statistics projects the population to be 35.4 million as of mid-2013, using 2002 census figures
[3] The National Statistical Abstract 2013 has no current records on unemployment and population of the poor people. The last recorded figures on the indicators was in 2010.
[4] By Lawrence Bategeka, Julius Kiiza & Sarah Ssewanyana, Economic Policy Research Centre and Makerere University, 2009

[5] http://www.worldfinance.com/markets/energy/energy-efficiency-in-demand-for-uganda

from, oil and gas activities. This calls for the development of the necessary regulatory framework, infrastructure and manpower for both the authorities (including OAG).

1.2 Problem Statement

Oil revenue is critical in economic growth and development of a country (Rosser, 2006) as cited in Enisan, (2012). If properly utilized, oil revenues can propel the country from a stage of underdevelopment to that of industrial 'Take-off (Enisan, 2012). The oil revenue has the potential to: attract Foreign Direct investments (FDI); provide intermediate inputs to other sectors; create both direct and indirect employment opportunities; and rise incomes of both the people and host government through increased taxes and a widened tax base; (Dooley et al., 2004; Al-Moneef, 2006 and Ramire, 2006 as cited in Enisan, 2012).

However, research and surveys have shown that possession of natural resources can offer negative effects to the country alongside benefits (Frankel, 2010). Although the oil revenue may significantly improve the economic conditions of a country, it is not guaranteed without the country managing well its oil revenues (Grynspan, 2012). Poor revenue management can lead to negative effects to the national economy; such as: crowding out other sectors of the economy, overdependence on oil revenues, and overvaluation of the national currency. The negative effects are commonly referred to as the "oil curse"(Morrison, 2013, Ross, 2012, Enisan , 2012 and Mitchell, 2009).

There is a growing expectation amongst many Ugandans that the discovery of oil will, indeed, increase their socio-economic well-being[6] as it has happened with other resource-rich countries such as, Norway, UK, USA and Australia (Ross, 2012 and Enisan, 2012), but at the same time

[6] National Oil and Gas Policy, 2008, Section 4.8

there is a great fear that resource may bring a 'curse' to the nation if the oil revenues are not properly utilized for the betterment of the populace (Grynspan, 2012).

The OAG is a critical institution in the overall accountability and governance framework of the country[7] and this puts it in a greater position to enforce proper oil revenue management, thus playing a vital role in the prevention of the resource curse syndrome.

This Project examines how prepared (how strong) are the National Audit Institutions, as one of the key institutions, in preventing the oil curse 'syndrome' in a case study of the Office of the Auditor General of Uganda.

1.3 Research Aims and Objectives

The research aims to contribute to an understanding of the 'oil curse syndrome' and its effects on the socio-economic environment of the country. The objectives of the research are:

a) To ascertain the effects of the resource curse, using the oil revenue management model, on the socio-economic environment of the resource-rich countries;
b) To ascertain how prepared the national audit institutions are in preventing the oil curse syndrome, using as case study, the office of the Auditor General of Uganda.

1.4 Organization of the project report

This project report is presented in five chapters. Chapter one gives an introduction to the work by describing the background, defining the problem, and stating the research aims and objectives. Chapter two reviews and discusses literature on: the 'oil curse syndrome', to include the oil curse and the Dutch disease; oil revenue management, including, characteristics of oil revenue, oil revenue management mechanisms, oil revenue management environment, country

[7] http://www.worldfinance.com/markets/energy/energy-efficiency-in-demand-for-uganda

experiences and the proposed case for Uganda; National audit institutions; governance and accountability in Uganda; and the petroleum sector in Uganda, including reserve monetization. Chapter three describes the methodology used to conduct the research, noting also the challenges and limitations of employing the selected methods in the selected research context. Chapter four discusses the preparedness of national audit institutions, taking a case study of the office of the Auditor General of Uganda. Lastly, chapter five makes a general conclusion and suggests some recommendations to audit institutions on their effort to prevent the oil curse syndrome in their countries.

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 The Oil Curse Syndrome

2.1.1 The Oil Curse

The phrase 'Oil Curse' was first formally used by an economic geographer, Richard Auty, in 1993 and it became popular in explaining the paradoxical phenomenon in resource-rich countries (Ross, 2012). The paradox, sometimes referred to as the 'paradox of plenty', explains that although some countries are much endowed with the natural resources, their economies do not grow as expected compared to countries that do not have such resource abundance (Morrison, 2013, Ross, 2012 and El Anshasy, 2012). For example, Nigeria is Africa's highest oil exporter and tenth-world oil producer and despite its abundance of oil resources, poverty and income inequality have long persisted (Adeniyi and Ushie, 2013).

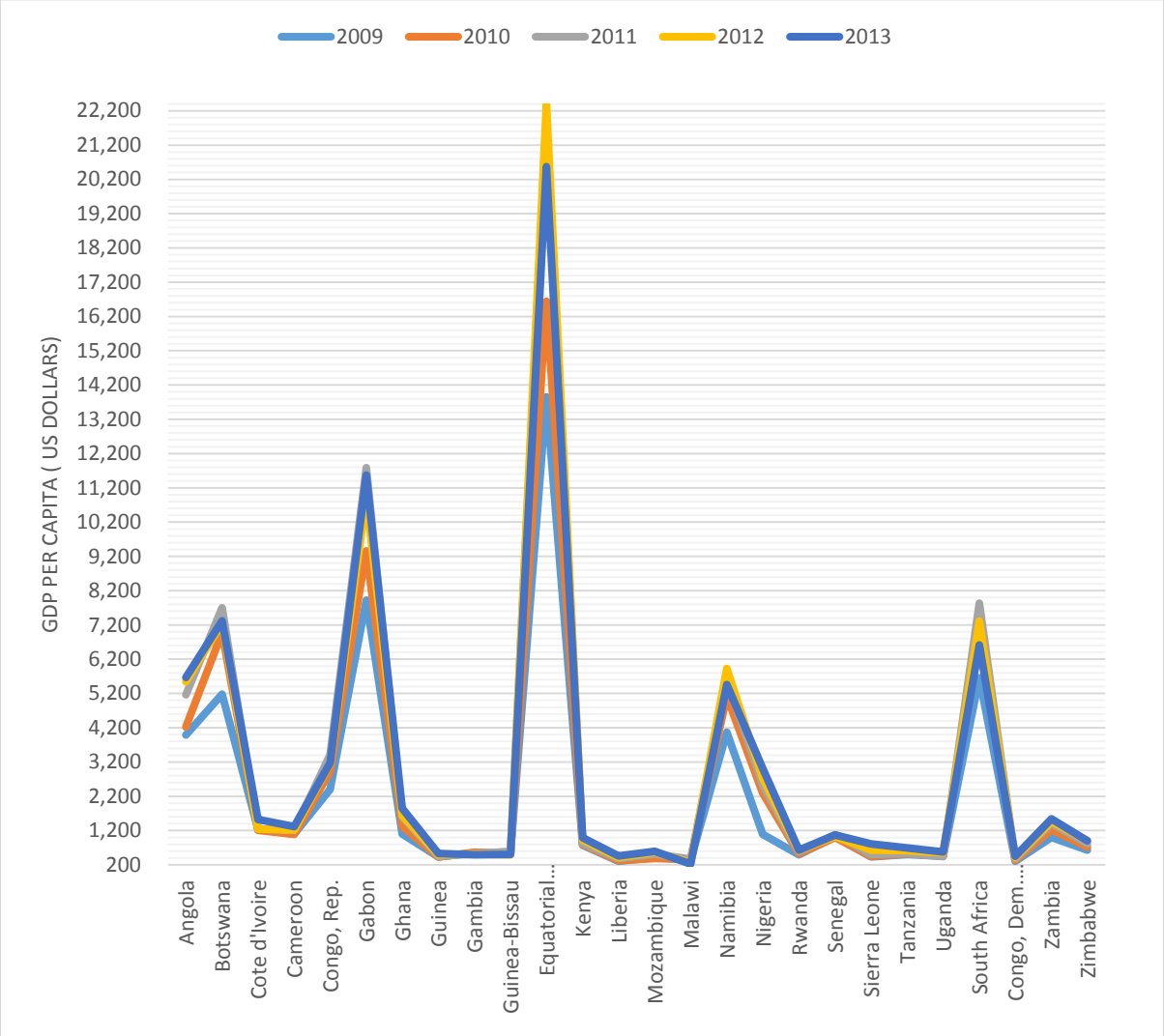
The challenging and recurring issue in international oil and gas investments is the need to understand what oil curse means, its causes, and how it can be avoided (Morrison, 2013, Ross, 2012 and Ploeg, 2011b). According to Morrison (2013), although much research has been made on the subject, to-date, it still appears not to be clearly understood. Economists (Sachs and Warner,), social scientist (Ross, 2012) and political scientists (Fearon, Laitin, Collier and Hoeffler: as cited in Ross, 2012) all describe the resource curse from different perspectives. Economists suggest that high ratio of natural resource exports to GDP is correlated to lower growth, controlling for other factors (Ross, 2012). Ross (2012) says the high resource ratio to GDP is correlated with less democracy, again controlling for other factors, and the political scientists say the high ratio is correlated with civil wars. However this Project, observes that all schools of thought seem not to agree on what causes the resource curse, but agree that it impacts negatively on society.

According to most research conducted between 1971 and 1989 by, for example Jeffrey Sachs and Andrew Warner, concluded that resource abundance causes a resource curse (Ross, 2012). However, between 1990 and 2006, the economies of oil-producing countries experienced faster economic growth rates of over 40 percent than the rest of the world. Going by this Ross (2012) concluded that the challenge faced by the oil-producing countries by then was not less economic growth, but more economic volatility.

A trend analysis of the World Bank records revealed that between 2009 and 2013 some oil producing countries in Sub Saharan Africa (Angola, Gabon, Equatorial Guinea, and Nigeria) experienced high GDP per capital than their non-oil producing counterparts (Cote d'lvoire, Guinea, Gambia, Guinea Bissau, Kenya, Liberia, Mozambique, Malawi, Namibia, Rwanda, Senegal, Sierra Leone, Tanzania, Uganda, Zambia and Zimbabwe). However, it should also be noted that some non-oil producing countries had higher GDP per capita than some oil producing counterparts (South Africa, Namibia and Zambia vs. DRC, Ghana, and Cameron). Again some much more endowed countries, such as Nigeria (2,520,000 bbd) and Angola (1,777,050 bbd) posted lower GDP per capital than Equatorial Guinea (289,400 bbd and Gabon (242,330 bbd), which were less endowed due to the high population of the former group of countries[8]. So the issue is all about how you manage your oil resource revenues to create more economic activities (Ross, 2012).

[8] http://data.worldbank.org/indicator/NY.GDP.PCAP.KD, 2013 figures

Figure 1: GDP per capita in oil and non-oil producing countries in Sub Sahara Africa (2009-2013)



Source: Author's analysis of the World Bank Data on Country GDP figures[9]

The Oil curse has been attributed to many factors, such as: corruption, rent seeking, inequality, inadequate policies, and weak institutions (Ross, 2012 and Adeniyi and Ushie, 2013). Ploeg (2011b) also itemise lack of rule of law, corruption, presidential democracies, and underdeveloped financial systems as contributing factors to resource curse syndrome (Kopinski et al., 2013). However, Morris (2012) concludes that the problem with oil is not the 'theoretical

[9] http://data.worldbank.org/indicator/NY.GDP.PCAP.KD

oil curse', but the issue of economic and political development. Ross (2012) opines that the effects of oil resource are 'conditional' and are dependent on the institutional environment in which they occur, such as regime type, the degree of 'clientelism', and whether institutions are "grabber- friendly" or "producer-friendly". Kopinski et al. (2013), using the Ghanaian experience, observes that the oil curse is a 'treatable disease' that countries should insulate themselves from using their 'immune system' of strong legal framework, good transparency and accountability practices, and modest attempts of strengthening non-hydrocarbon sectors of their economies.

It is, therefore, believed that building strong institutions (an observation missed by earlier research) is among the key prerequisites for preventing the negative effects of the resource curse (Morrison, 2013; Grynspan and Parayil, 2012; Kopinski et al., 2013; Ploeg, 2011b; Adeniyi and Ushie, 2013 and Mitchell, 2009).

2.1.2 Oil curse vs. The Dutch disease

The term oil curse has been synonymously used by many to mean the 'Dutch disease', but the two are not exactly similar. The oil curse as discussed in the preceding paragraphs is a much bigger phenomenon looking at the holistic issues of resource management and its negative effects (of which the 'Dutch Disease is a part). Economists specifically use the term 'Dutch disease' to explain a process that causes a boom in the country's natural resources sector to produce a decline in its manufacturing and agriculture sectors (Ross, 2012; Ploeg, 2011a and Thorvaldur, 2001 as cited in Kopinski et al., 2013). The decline in the manufacturing sector affects developed countries, for example, Norway and UK whereas the effects on the agriculture sector are more pronounced in developing economies such as Nigeria, Angola and Ghana, where cocoa, palm oil and rubber agricultural sub sectors have been affected (Ross, 2012).

According to Ross (2012) andPloeg, (2011a), the Dutch disease has two major effects. The first is the 'resource movement effect' whereby, because of the boom in the petroleum sector, labour and capital are drawn from the manufacturing and agriculture sectors, thus rising their production costs (crowding-out effect). The second effect is the 'Spending effect', as 'petrol money' from the booming petroleum sector enters the economy, it raises the exchange rate of the local currency (overvaluation of the local currency) making locally produced goods more expensive.

According to Kudrin (2007); Adeniyi and Ushie (2013) and Ploeg (2011b), the Dutch disease may also lead to imbalances in the monetary-credit system, accelerated inflation, rising real effect of exchange rate, increasing economic risks, deteriorating quality of fiscal and general economic policies, declining Gross Domestic Product (GDP) rates and increased budget volatility due to unpredictable oil market prices, thus requiring countries to engage in long-term fiscal policies and state expenditure strategies.

2.2 Oil Revenue Management

Management in its general sense refers to a process of creating an environment to enable the attainment of agreed upon organizational goals and objectives (Koontz and Wiehrich, 1990). It comprises planning, organizing, decision making, and leading and controlling organizational/country resources to efficiently and effectively attain the intended objectives (Griffin, 2002). Oil revenue management is geared at creating an environment that will ensure that oil revenues are properly utilized for sustainable economic growth and development of a country (Grynspan, 2012; Enisan, 2012; and Schilling and Chiang, 2011). Oil revenue management requires an understanding of the oil revenue characteristics, management mechanisms, and management environment, as well as drawing experience from others.

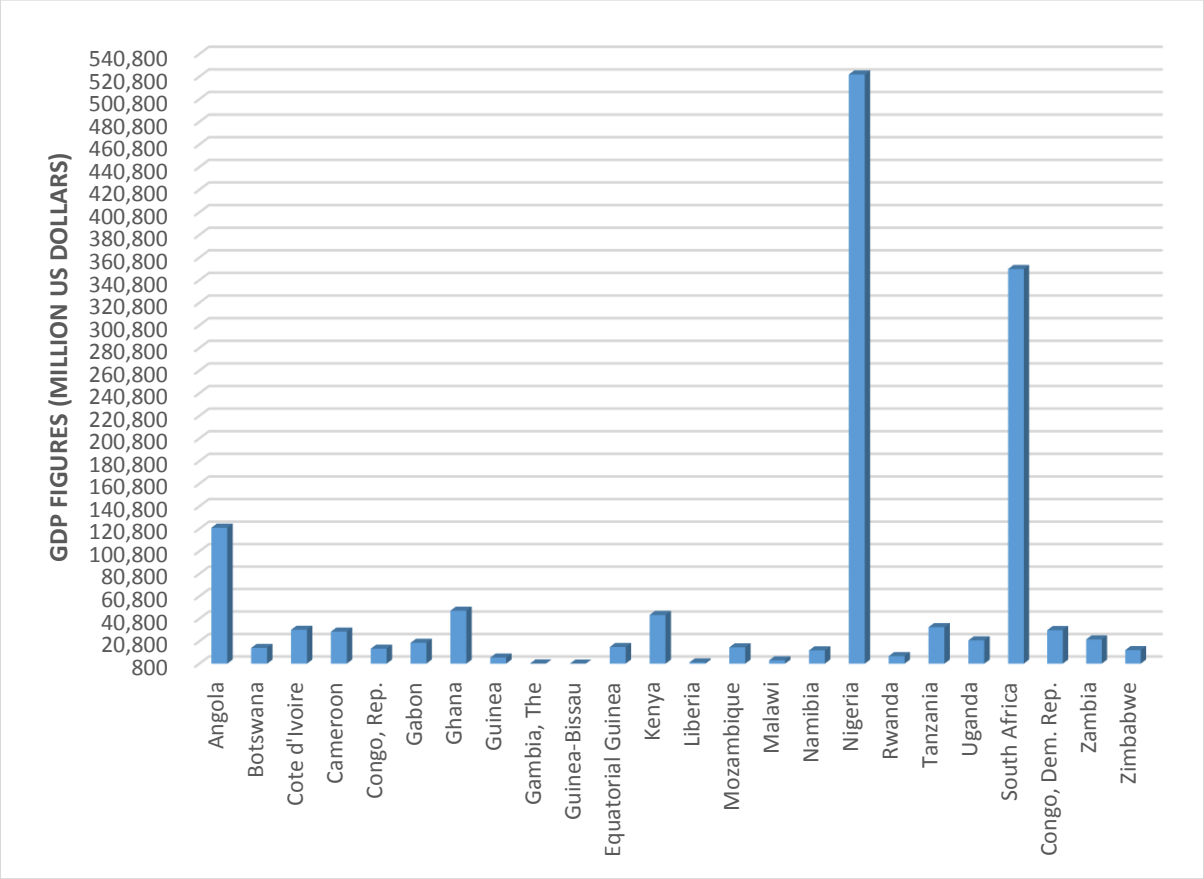
2.2.1 Characteristics of oil Revenue

Oil revenue has four uncommon qualities: (1) the revenues are large in size; (2) they are not the usual source of government revenue ; (3) they are unstable; and (4) they are secret (Morrison, 2013 and Ross, 2012). According to Ross (2012), these unusual qualities stem from the distinctive economic properties of the petroleum industry. These include: oil reserves are owned by governments; the resource can be depleted; substantial up-front investment is required; there are windfall profits involved; the negative effects the petroleum sector can have on others (crowding-out effect and overvaluation of the local currencies); and the sensitivity of oil price to relatively small changes in supply and demand.

Size of oil revenue

Most oil producing countries have substantially greater revenue than their counterpart non-oil producing countries, which sometimes is not easy to relate to oil production because most countries hide information on oil revenues (Ross, (2012). The above was also observed through an analysis of the World Bank GDP figures of oil and non-oil producing countries in sub-Sahara Africa as shown in Figure: 2. Again to the contrary, some non-oil producing countries had higher GDPs than their oil producing counterparts (South Africa vs. all oil producing countries in Sub Sahara Africa; Kenya and Tanzania vs. DRC, Congo Republic, Gabon, Cameroon and Cote d'Ivoire; Uganda vs. Gabon and Congo Republic).

Figure 2: GDP (Million US Dollars) of oil and non-oil producing countries in Sub Sahara Africa (2013)



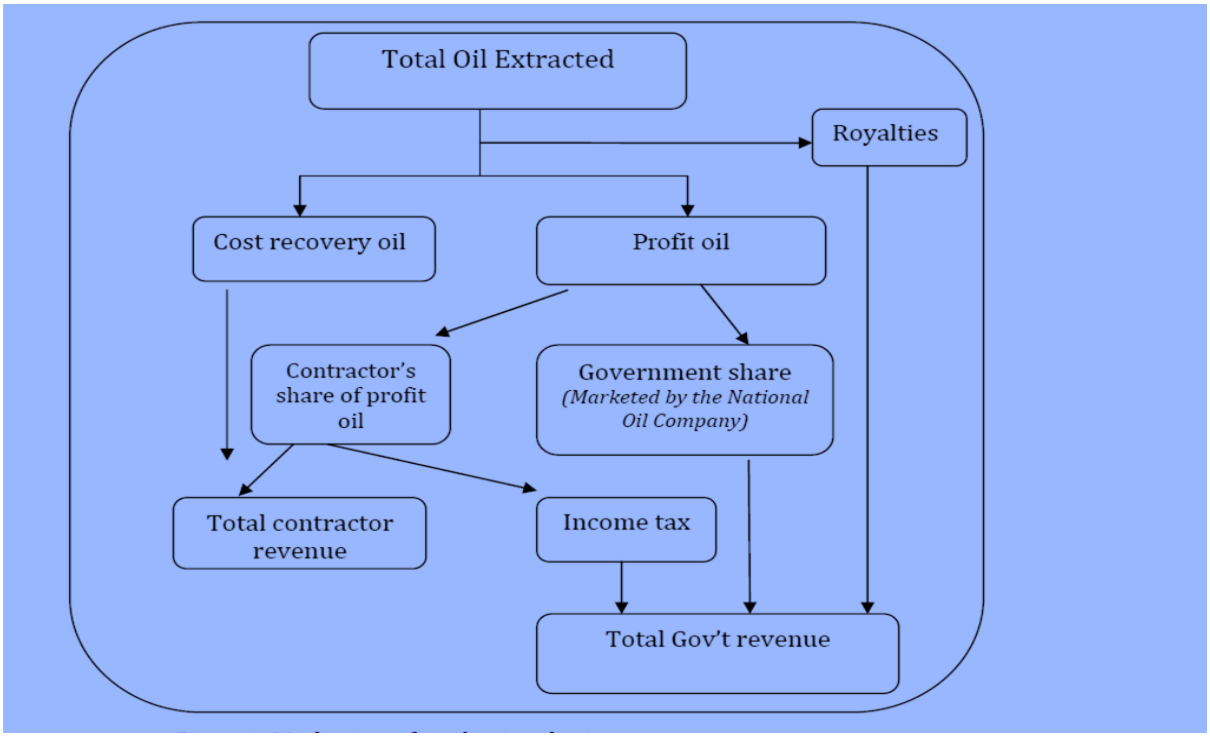
Source: Authors analysis of the World Bank Data on Country GDP figures[10]

Source of government revenue

Most governments are funded through taxation, but as governments discover oil resources, they become increasingly over-dependent on oil as a major source of funding budgets (Ross, 2012). Most oil revenue accruing to governments or oil-rich countries comes from royalty payments, revenue sharing, dividends, payroll taxes, withholding taxes and income tax or corporation tax (Ross, 2012 and Kopinski et al., 2013) and through the common use of Production Sharing Agreements (PSAs) and concessions (Ross, 2012). Figure: 3 shows a typical revenue sharing mechanism under the PSA arrangement.

[10] http://data.worldbank.org/indicator/NY.GDP.PCAP.KD

Figure 3: A typical revenue sharing mechanism used under the PSA arrangement



Source: Oil and Gas Revenue Management policy, 2012, Uganda

Oil Revenue instability

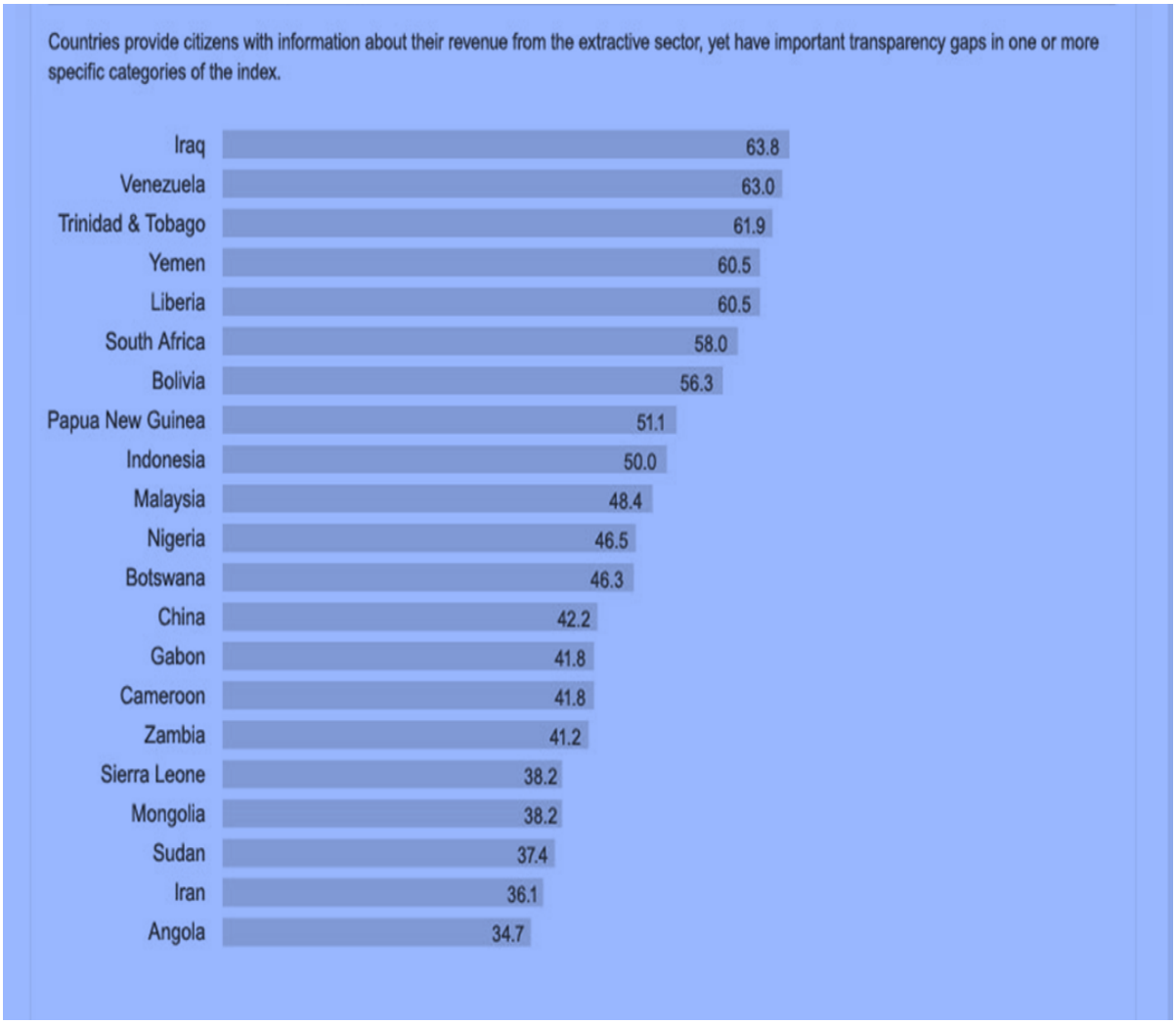
Revenue from oil is very unpredictable because of its dependence on crude oil prices, which are internationally determined and keep fluctuating. According to Ross (2012), there are three factors which are responsible for the revenue volatility, which include: changing oil prices, change in production rates, and the nature of clauses in contracts signed between governments and the oil companies.

The Secrecy of Oil Revenue

Most oil producing countries hide information on oil revenue from the public. However, some democratic countries, such as: Brazil, Norway, Russia, Mexico, Chile, Colombia, Kazakhstan, Peru, Azerbaijan, Ecuador, United States and Timor-Leste, in that order, are highly transparent, providing substantial information about oil revenue (Revenue Watch Institute, 2010). They exhibit strong reporting practices and provide detailed or disaggregated data on different areas

of the industry. According to the Revenue Watch Institute (2010), there are other countries that provide information, but with some significant flaws in the transparency system, for example, Iraq, Venezuela, Nigeria, Gabon, etc. as indicated in Figure: 4 below:

Figure 4: Countries with significant transparency gaps, but providing oil revenue information



Source: Revenue Watch Institute, 201011.

According to the Revenue Watch Institute (2010), the countries which disclosed less information had the poorest reporting practices and they included: Saudi Arabia, Ghana, Kuwait, Algeria, DRC, Equatorial Guinea and Turkmenistan, in that order. A survey of the national budget policies in ninety-four countries, by International Budget Partnership (2010)

[11] http://www.revenuewatch.org/rwindex2010/rwindex.html

as cited by Rossi (2012), revealed that the national budgets of oil producing countries were less transparent compared to those of non-oil producing countries.

2.2.2 Oil Revenue Management Mechanisms

Restrained government spending

When countries obtain windfall revenues, economists argue that they should invest in domestic investments with sufficiently high rate of return and save the surplus to cater for future cyclical changes resulting from oil revenue volatility; this will help governments implement their countercyclical fiscal policies (Humphreys, et al., 2007; Collier, et al., 2009; Gelb and Grasman, 2010 as cited in Ross, 2012; and El Anshasy, 2012). According to Ross (2012), most governments do not restrain their spending and always let the size of their revenue reserves determine the size of their national budget. There is a need for appropriate industrial policy mix, such as: strengthening non-oil tax base, increasing capital spending during oil revenue wind falls, applying stricter investment criteria and political commitment to fiscal rules (El Anshasy, 2012).

Establishment of special oil funds

International experience has shown that if a country's budget revenues significantly depend on exportation of products whose prices are determined on a worldwide market (such as oil), the country should set up a stabilization fund (Afanas'ev, 2004). Stabilization funds can either be established from contributions related to resource prices (for example, Oman, Venezuela and Chile) or contributions that are not related to resource prices (for example, Norway, Alaska State and Kuwait) (Kudrin, 2007 and Afanas'ev, 2004). However, the choice of the model will depend on whether the country is a low cost oil producing country or has limited budget fund sources (Afanas'ev, 2004). Governments set stabilization funds to: (1) counteract revenue volatility through implementing countercyclical fiscal tools, (2) counteract resource depletion

or (3) implement both 1 and 2 simultaneously (Ross, 2012 and Kudrin, 2007). The challenge, however, has been that the special funds have not been effective due to abuses by the same governments which creates them. The funds depository and withdrawal rules/procedures are not complied with; and governments have adopted parallel policies (IMF, 2007 and Davis et al., 2003 as cited in Ross 2012). Kudrin (2007) also observes that stabilization funds have failed due to lack of financial and fiscal discipline by governments. He advises governments to keep expenditure in real terms at constant levels or increase it when there is an actual increase in GDP. The funds have also not been effective, especially, those that are resource-price based, due to the difficulties involved in determining long-term and medium-term average market price of crude oil (Afanas'ev, 2004).

The Hartwick Rule and Economic Diversification

The 'Hartwick rule', according to Ross (2012) and as also discussed by Ploeg, (2011b), El Anshasy, (2012) and Collier, et al (2009), suggests that, governments should not spend all their revenues obtained from their natural resource capital. It being an exhaustible resource, they should instead invest a fraction of the resource revenue into other national capital assets, such as physical capital (infrastructure) and human capital (education), and in addition, they should invest in other non-hydrocarbon sectors, such as: agriculture, manufacturing and services sector. The problem has also been exacerbated by countries investing in 'white elephant' projects which end up wasting public funds (Ploeg, 2011b). It is advisable that countries should instead be investing the excessive revenues abroad as their economies grow to accommodate 'home grown capital' (Ploeg, 2011b). However, Collier et al. (2009), departs from this view and suggests that oil revenues should be invested at home, but while maintaining the balance between investment and the rate of resources extraction.

2.2.3 Oil Revenue Management Environment

Government Institutions

The aforementioned revenue management mechanisms require strong institutions with adequate capacity in terms of personnel-numbers and skill competencies, equipment and logistical support (Adeniyi and Ushie, 2013 and Kenneth et al., 2008) . In addition, the institutions should be backed by the relevant operational and legal frameworks to enable them formulate, implement, and review strategies, policies and procedures and hold institutions accountable to the public (Adeniyi and Ushie, 2013 and Kenneth et al., 2008).

Ross (2012) urges that 'sick' government institutions are like a sick doctor - weakened by a disease, who cannot treat his/her patients. He urges that the oil revenue makes institutions ineffective, thus impairing their ability to positively think a head and they suffer from 'short-termism'. Many scholars, have ambitiously urged that oil wealth creates 'administrative chaos' and 'bad institutions' which are corrupt, inefficient, less competent and weak to implement sound economic policies (Chaudhry, 1989 and World Bank reports 2008) as cited in Ross, 2012, and Ploeg, 2011b).

According to Karl (1997), in his famous book *'the paradox of plenty'*, revenue from oil diminishes state's authority and creates a situation where both public authorities and private interests are all centred at 'rent seeking'.

Governance

Good governance is about being accountable, allow participatory approach and be transparent to ensure that political, social and economic priorities are based on broad consensus in society and that the voices of the most poor and vulnerable are considered in decision making and in resources allocation (Kenneth et al., 2008).

Governments and their leaders face constant pressure from the citizens, who think that oil revenue should be spent on infrastructure , health, improving their working conditions including increased salaries (Morrison, 2013) and at the same time, the leaders want to stay in power and fear antagonising with the electorates (Ross, 2012). However, sometimes leaders with much desire to stay for longer will spend less on patronage and turn out to be dictatorial (Humphreys and Sandbu, 2007 as cited in Ross, 2012). Other studies have also found out that it is not only important to have democracies, but what matters is to understand the level of corruption within those democracies and they concluded that democracies in developing world with higher corruption levels exercised poorest fiscal policies compared to democracies with low corruption levels (Alesina et al., 2008 as cited in Ross, 2012).

The World Bank Group (WBG), has introduced a voluntary multi-stakeholder approach, the Extractive Industries Transparency Initiative (EITI) as its key governance promotion program (Caspary, 2012). Under EITI countries are urged to improve on the sector reforms to ensure capacity building and private sector participation, thus: (1) triangulating the cooperation between governments, business and civil society; (2) promote transparency in revenue streams; (3) acquire capacity to manage revenues responsibly; (4) taking into account social and environment concerns; and (5) support governments to develop modern policies and legal framework.

2.2.4 Some Country Experiences on Oil Revenue Management

Norway

Norway established its State Oil Fund, which is non-resource-price based fund, in 1990, with an objective of keeping its national budget stable in the long term thereby maintaining macroeconomic and long-term fiscal stabilization irrespective of fluctuations in revenues from oil exports (Afanas'ev, 2004). The Fund is managed by the country's central bank, Norges

Bank, and the crafting of the overall Fund's investment strategy is a responsibility of the Ministry of Finance (Afanas'ev, 2004). Funds can only be transferred to finance the central government budget with the approval of parliament (Kudrin, 2007). The fund was also created to help government solve the pension challenges resulting from an aging population and on realisation that oil production was starting to decline (Afanas'ev, 2004). The Fund grows its own finances from investments, such as: low-risk foreign fixed income assets and stock (foreign government securities and bonds from credible financial institutions (Afanas'ev, 2004). Government may ask for parliamentary approval to use money from the Fund to cater for budget shortfall resulting from a fall in the oil price or for maintaining intergenerational equalization (Afanas'ev, 2004).

Russia

Russia started operating a stabilization fund in 2004-05 due to the high degree of dependency of both its economic and financial systems on external economic factors. For example in 2005, twenty six percent of the country's GDP was contributed by oil and gas sector and 59 percent of exports were from the hydrocarbons, which were highly dependent on world market conditions (Kudrin, 2007 and Afanas'ev, 2004). According to Kudrin, (2007) about 50% of excess revenue a rising from an increase in world market prices of oil was paid to the stabilization fund. The Fund's source of revenue are: (1) Transfer from earnings of state extraction companies; (2) Budget balances at the end of a financial year; (3) a dedicated fixed proportion from the government revenue budget; and (4) proceeds resulting from management of the fund (Kudrin, 2007). The fund is also used to repay ahead of schedule the federal government's debt, thus saving on interest payments charged on foreign debts. In addition, the fund plays a pivotal role in stabilizing state finances and the monetary- credit system (Kudrin, 2007).

Venezuela

Venezuela established its macroeconomic stabilisation Fund in 1998 and it receives funding from the only state oil company calculated as the difference between the current oil price and the long-term average oil price- for five years. Money can only be spent from the Fund with the approval of the Congress when the oil export prices fall below the base figure in the budget or when the amount accumulated in the fund exceeds 80 percent of average annual oil export revenue for the last five years, and in this case, money is only used to pay off foreign debt. (Afanas'ev, 2004).

United Arab Emirates

United Arab Emirates, despite the huge revenues it gets from the non-renewable resources (4th world largest exporter of oil and gas), it does not operate a national oil fund. It observes strict fiscal policy and excess monies are invested in foreign countries after financing the bulk of the central government budget (Kudrin, 2007). UAE has largely diversified its economy with great emphasis on light manufacturing, telecommunication, finance, tourism, agriculture, quarrying cement and shipping services and as a result, it has created jobs, modernized its infrastructure and kept inflation at its lowest figures (Ploeg, 2011b).

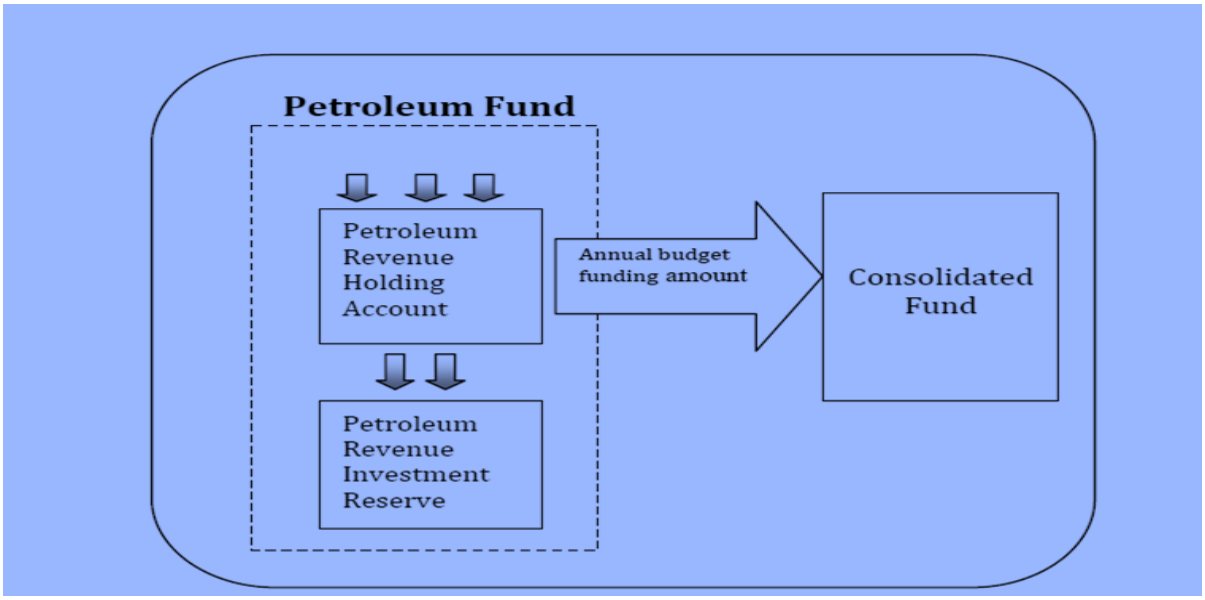
2.2.5 Proposed Oil Revenue Management in Uganda (Public Finance Bill, 2012)

Uganda proposes a Petroleum Fund, which shall consist of two accounts: the Holding Account and the Petroleum Revenue Investment Reserve. The holding account shall be a petroleum revenue collection and depositary account, whereas the petroleum revenue investment reserve shall cater for financing investments for the benefit of both current and future generations. Withdrawals from the Holding Fund shall be made under an appropriation Act of Parliament and on issuance of an audit Warrant by the Auditor General. The money in the petroleum revenue investment fund shall be invested in accordance with the Petroleum Investment Policy

issued by the Minister of Finance in consultation with the Investment Advisory Committee. The investment shall be diversified and of low risk in order to guarantee availability in case of domestic emergencies. The Bank may employ an expert investment manager on competitive terms to run the PRIR. Government has also prohibited the borrowing from the fund or using it as collateral and has proposed that seven percentage of revenue from royalties will be shared amongst the districts within the petroleum, exploration and production areas.

A critical review of the Ugandan oil revenue management mechanism reveals that the Fund does not provide for a stabilisation fund to cater for budget volatilities, in case of oil prices fluctuations, more so when oil prices significantly drop. Mixing the functionality of the PRIR to cater for both budget volatility and providing for the future generation may inhabit operational challenges, especially, when making investment decisions of the Fund. It is advisable for the government to split the PRIR into two funds, that is, the stabilization fund (to cater for budget volatilities) and the heritage fund (to cater for the needs of future generations). Figure: 2 below illustrates the country's revenue management mechanism.

Figure 5: Oil Revenue Management mechanism, Uganda



Source: Oil and Gas Revenue Management policy, 2012, Uganda

2.3 National Audit Institutions

National Audit Institutions are supreme audit institutions (SAIs) responsible for auditing government accounts and report their findings to either Parliament or the presidency, depending on the governance setup. Majority of SAIs are members of the International Organization of Supreme Audit Institution (INTOSAI)[12], which is an autonomous, independent, and non-political organization responsible for coordinating SAI activities world over, including building SAI institutional capacity. Building strong institutions is a critical challenge to development and fighting corruption, according to Kenneth et al. (2008). SAIs are among the key public institutions responsible for promoting sound financial management and check whether governments are accountable and transparent while performing their (governments) duties (Kenneth et al., 2008). However, the ability of the SAIs to check

[12] http://www.intosai.org/about-us.html

corruption in institutions has not been fully exploited due to limited understanding of overall SAI capacity (Kenneth et al., 2008).

The Office of the Auditor General (OAG) is the Supreme Audit Institution of Uganda, and a member of INTOSAI[13] and its regional body, AFROSAI[14]. It is established by Parliament under Article 163, of the Constitution of the Republic of Uganda, 1995 (as amended)[15] and has its specific powers, authority, rights and functions clearly stipulated in the National Audit Act (NAA), 2008[16]. Under Article 163 (3) of the Constitution and Section 13 of the NAA, the Auditor General (AG), who is the head of SAI-Uganda, is mandated to audit and report to Parliament (Article 163 (4) of the Constitution), on the public accounts of Uganda and all public offices, including the courts, the central and local government administrations, universities and public institutions of like nature, and any public corporation or other bodies or organizations established by an Act of Parliament; and conduct financial and value for money audits of any projects involving public funds. The NAA, Section 13 and Sections15-22, further amplifies the AG's powers to conduct various audits; such as: Financial Audits, Value for Money Audits, Environmental Audits, Procurement Audits, Gender Audits, Special audits and investigations, and any other audits that he (AG) may deem fit for the purpose of increased transparency and accountability.

[13] http://www.intosai.org/about-us/organisation/membership-list.html
[14] http://afrosai-e.org.za/search/node/members
[15] http://www.parliament.go.ug/new/index.php/documents-and-reports/the-constitution
[16] http://www.oag.go.ug/docs/NAA_2008.pdf

2.4 Governance and Accountability in Uganda

Governance

Uganda is a parliamentary democracy country, with an established Parliament of Uganda[17] composed of the elected Members of Parliament (MPs) and representative MPs of special interest groups, such as: women, army, youth, workers, and persons with disability[18]. The President of the Republic of Uganda is an elected president[19] and is the Head of Government and the Executive[20]. The country observes the principles of separation of power and the rule of law with the three independent arms of government working together: Legislature (Make laws, protect the constitution and promote democratic governance of the country); Executive (determine, formulate and implement government policies); and Judiciary (Administration of justice) clearly provided for in the Constitution of the Republic of Uganda[21].

Accountability cycle

Accountability is one of the twenty-nine national objectives and directive principles of the state policy as stated in the Constitution of the Republic of Uganda[22], which makes all public offices in Uganda to be held in trust of the people. The directive principle also states that*: "All lawful measures shall be taken to expose, combat and eradicate corruption and abuse or misuse of power by those holding political and other public offices"*[23]. The President is required to ensure that the financial year estimates of revenue and expenditure are prepared, submitted and laid

[17] Article 77 of the Constitution of the Republic of Uganda
[18] Article 78 of the Constitution of the Republic of Uganda

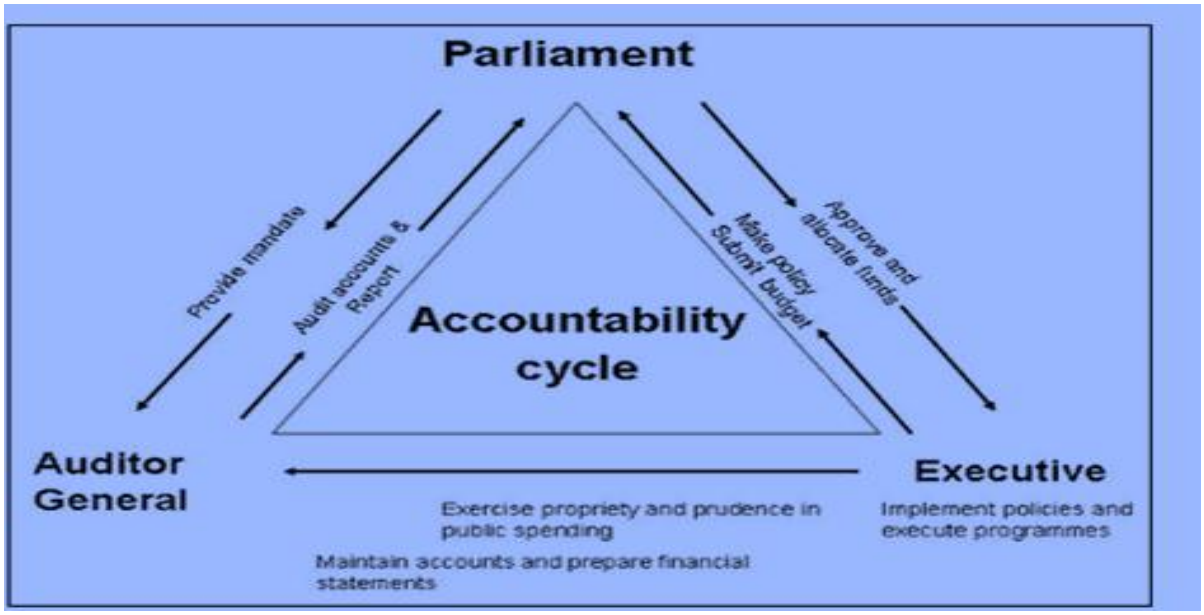
[19]Articles 98, 103 & 105 of the Constitution of the Republic of Uganda

[20] Article 99 of the Constitution of the Republic of Uganda

[21] Articles 77- 97 (Legislature) Articles 99, 108A, 111(Executive); Articles 126-151 (Judiciary) of the Constitution of the Republic of Uganda
[22] Page 21 of the Constitution of the Republic of Uganda
[23] Page 28 of the Constitution of the Republic of Uganda

before Parliament in each financial year not more than the 15th day of June, to include also fiscal and monetary programmes and plans for economic and social development[24]. Parliament discusses the national budget and approves it by appropriating funds to the Executive[25]. The executive then implements policies and programmes while exercising propriety and prudence and it maintains proper records and prepares financial statements for audit by the AG[26]. The AG audits the financial statements and records and reports to Parliament in accordance to Article 163 (4) of the Constitution. Parliament, thru its three Accountability Committees (Public Accountability Committee-PAC, Committee on Statutory Authorities and State Enterprises-COSASE and Local Governments Public Accounts Committee-LGPAC), discusses AG reports and makes recommendations to the Executive.

Figure 6: Accountability cycle in Uganda



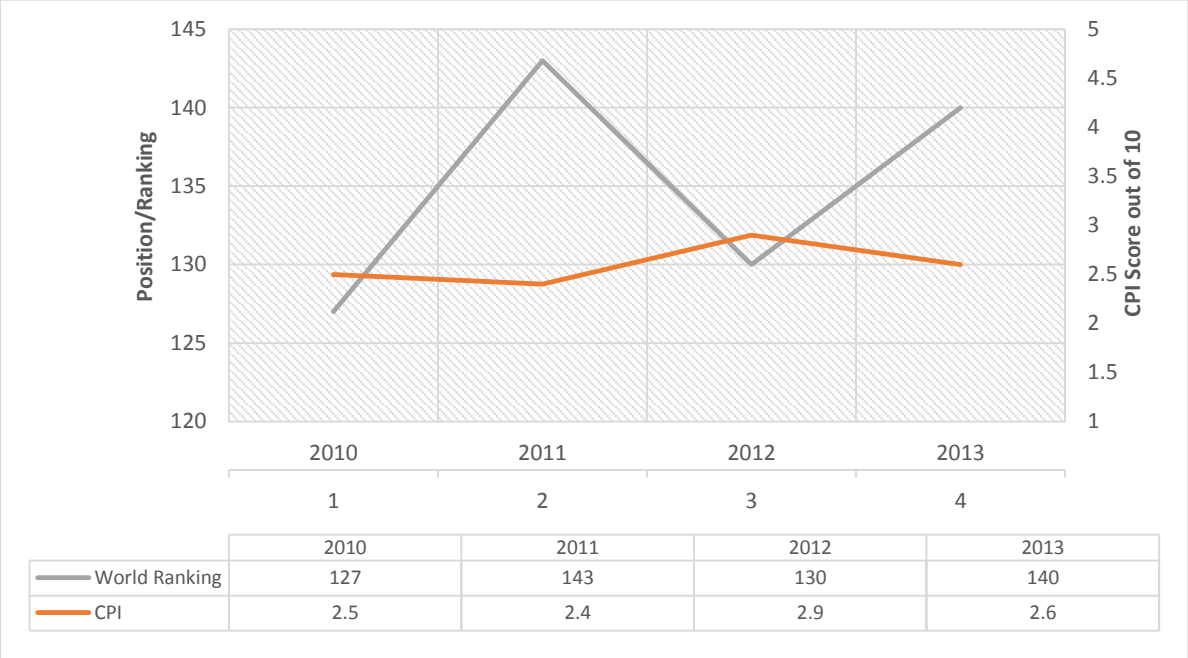
Source: Office of the Auditor General, Uganda[27]

[24] Budget Act, 2001, section 3
[25] Budget Act, 2001, section 11
[26] http://www.finance.go.ug/dmdocuments/PFAA2003.pdf
27 http://www.oag.go.ug/index.php?option=com_content&view=article&id=25&Itemid=67

The OAG is a critical institution in the overall accountability and governance framework in the country[28] and this puts it in a greater position to enforce proper oil revenue management, thus playing a vital role in the prevention of the resource curse syndrome.

However, based on the Corruption Perception Index (CPI)[29] by Transparency International, Uganda still faces corruption challenges. The country ranked 127/178 (2010), 143/178 (2011), 130/174 (2012), and 140/177 (2013), thus making it among the highest ranked countries in the world. Figure: 3 shows the trend of the country's corruption levels over four years, showing low levels of CPI of less than 3. Some improvement was registered in 2012 when the country's CPI was at its highest (2.9).

Figure 7: Corruption Perception Index of Uganda (2010-13)



	2010	2011	2012	2013
World Ranking	127	143	130	140
CPI	2.5	2.4	2.9	2.6

Source: Author's analysis of Transparency International data on country CPI rankings

[28] http://www.oag.go.ug/index.php?option=com_content&view=article&id=25&Itemid=67

[29] http://www.transparency.org/cpi

The AG has also, in his published reports, indicated corruption and misuse of public funds, for example, in his current published report for the financial year 2012/13[30], an equivalent of $18.9 million[31] was forcefully refunded to development partners after it had been misappropriated by officials from the Office of the Prime Minister and the officials responsible had not refunded the amount to government. He has also cited in his reports the failure by government to properly account for funds, payments for works not executed, payments to individual personal bank accounts, shoddy government works, poor budget formulation and the lack of budget discipline and many other irregularities as reported in financial, value for money and special audit reports [32]. The World Bank, according to its Group Statement on recent corruption cases in Uganda (November, 14, 2012)[33], has condemned all acts of corruption, which it said are responsible for retarding development efforts and as a result it has sought a review of its development assistance as the country strengthens its fiduciary environment and pursues its national policy of *'Zero tolerance to corruption'*

2.5 The Petroleum subsector in Uganda

Uganda discovered oil in 2006[34] in the Albertine Graben, in the western part of the country. The country's proven oil reserves stand at 2.5 billion barrels as at January 1, 2014 (Oil and Gas Journal, and EIA). The country is also endowed with natural gas with proven reserves of 500 billion cubic feet[35]. The country hopes to start commercial production in 2018 and the initial

30http://www.oag.go.ug/index.php?option=com_phocadownload&view=category&id=32:2012-2013&Itemid=15

31Uganda Shs.49,816,466,501 exchanged at Bank of Uganda rate as at July 24, 2014; https://www.bou.or.ug/bou/collateral/interbank_forms/2014/Jul/Major_24Jul14.html

32 http://www.oag.go.ug/index.php?option=com_phocadownload&view=sections&Itemid=10S

33http://www.worldbank.org/en/news/press-release/2012/11/14/world-bank-group-statement-on-recent-corruption-cases-in-uganda

34 http://www.eia.gov/countries/country-data.cfm?fips=ug AND By Lawrence Bategeka, Julius Kiiza & Sarah Ssewanyana, Economic Policy Research Centre and Makerere University, 2009 A

35 http://www.eia.gov/countries/country-data.cfm?fips=ug

oil flows will be used to fuel a 50-megawatt crude-fired electricity plant (Oil and Gas Journal, and EIA) and ministry press release[36].

2.5.1 Legal and Operational Framework

The Country has extensively consulted and prepared a legal and operational framework, which includes laws and policies, which specify the establishment of various institutions and their roles and responsibilities. This gives hope that the framework will help the country successfully exploit its oil resources, when fully adhered to, thus avoiding the oil curse syndrome. Table: 1 shows a summary of the legal frame work and more details are attached in **Appendix A.**

Table 1: Summary of Legal and Operational Framework in the Petroleum Subsector

Legal/Operational Instrument	Purpose/objective
Petroleum (Exploration, Development and Production) Act, 2013	Governs exploration, and development and production activities (upstream), including: licensing, drilling, decommissioning of projects.
Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act, 2013	Governs the midstream activities, including refining and pipeline construction and power plants.
Petroleum Supply Act, 2003	Governs petroleum activities in the downstream (construction and operation of petroleum Stations, Transportation, trading of commodities, etc.).
Public Finance Bill, 2012 (Proposed)	When passed into law, it will provide for the general public financial management in Uganda, including the legal and regulatory framework for the collection, allocation and management of the petroleum revenue.
Oil and Gas policy, 2008	Basically gives guidance to the development of the emerging oil and gas sector.
Oil Revenue Management Policy, 2012	Gives direction on: the fiscal regime necessary for collection and administration of oil and gas revenue; microeconomic management framework; oil and gas revenue sharing; etc.
Energy Policy, 2002	gives guidance on energy matters in the country, including: the generation, distribution and supply of power

Source Author's summary from legal and operational instruments

[36] http://www.petroleum.go.ug/ Press Reviews (Interview with Permanent Secretary, MEMD

2.5.2 Roles and Responsibilities of Key Institutions in Oil Revenue Management in Uganda

The legal and operational framework has bestowed roles and responsibilities upon various key government institutions to ensure that oil revenues collected are properly managed and utilized for sustainable development of the country as follows[37]. Table: 2 shows a brief summary of the roles and responsibilities, and more details are attached in **Appendix B.**

Table 2: Key Institutions and their roles and responsibilities in the Petroleum Subsector

Key Institution	Roles/Responsibilities
Ministry of Energy & Mineral Development and its technical department, PEPD	Responsible for policy formulation and implementation, regulation of the subsector and managing the commercial aspects, and coordinating national oil capacity building, including: licensing; industrial promotion; issuing policy and regulations.
Ministry of Finance	Responsible for management of the Petroleum Fund, including: overseeing the transfer into and disbursements from the Fund.
Uganda Revenue Authority	Responsible for collection and receipt of petroleum revenue; assisting in monitoring and assessing the impact of oil and gas revenue on the economy.
Office of the Auditor General	Required to provide an independent oversight of the government petroleum operations by conducting financial audit and other management audits.
The Parliament	Responsible for enacting regulations for the petroleum subsector and generally overseeing the performance of the Petroleum Fund.
Bank of Uganda	Generally in charge of operational management of the Holding Account and Petroleum Revenue Investment Reserve.
Investment Advisory Committee	Responsible for advising the minister on general petroleum fund investment activities.
The Petroleum Authority of Uganda	Responsible for the regulation of the subsector.
National Oil Company	Taking charge of state commercial interests in the subsector

Source Author's summarization from legal and operational instruments

[37] Public Finance Bill, 2012; Oil Revenue Management Policy, 2012; and Oil and Gas Policy, 2008

2.5.3 Petroleum Subsector Performance and Monetization

The country is progressively increasing its activities in the petroleum subsector, especially in the upstream and midstream divisions. According to the Ministry of Energy and Mineral Development (MEMD), by end of 2013, 115 exploratory wells had been drilled of which 101 wells had hydrocarbons, registering 85 percent success rate[38]. During 2012, one production licence for the Kingfisher field was granted to CNOOC and nine production licences submitted by Tullow (8) and Total (1) are being evaluated by Government[39]. Total company investment in the subsector is approximately $ 2.3 billion, which is expected to grow to $ 3.0 billion by the end of 2014[40]. In order to address the challenges of local content, Government has established a Uganda Petroleum College at Kigumba, running certificate and diploma courses, and the Public University at Makerere is offering degree courses in petroleum engineering, and a number of staff from government ministries, agencies and departments have been sent abroad to train and boost government understanding of oil related issues[41].

In the bid to monetize its oil reserves, government has signed a memorandum of understanding (MOU) with IOCs to construct a refinery, build a pipeline to Lamu, Kenya, and construct a crude oil fired-power plant. The initial refinery capacity of 30,000 bbd will be gradually increased to 60,000 bbd by 2020, and the refinery shall have priority call on the IOCs estimated combined production of 200,000 bbd. The proposed plant is expected to reduce on the country's energy deficit (only 9% of the population has access to installed power- World Bank report, 2011) and increase its security of energy supply, by also reducing on overreliance on hydroelectricity, which is vulnerable to weather vanguards[42].

[38] Public Finance Bill, 2012; Oil Revenue Management Policy, 2012; and Oil and Gas Policy, 2008
[39] Ibid
[40] http://www.petroleum.go.ug/ Press Reviews (Interview with Permanent Secretary, MEMD
[41] Ibid
[42] http://www.eia.gov/countries/country-data.cfm?fips=ug

CHAPTER THREE

3.0 METHODOLOGY

3.1 Data collection and Analysis

In the preceding chapter, literature from selected text books and articles, and research works was reviewed to gain a better theoretical understanding of the oil curse syndrome, its causes and how it can be avoided. Various mechanisms used by different countries for oil revenue management were reviewed. In furtherance of these, the role of national audit institutions in managing oil revenue in this project were identified, and economic data on key performance indicators on both international and national levels was collected and analysed to obtain empirical evidence on selected Sub-Sahara African countries. Following on from that, some government micro and macro-economic policies and strategies towards the prevention of the oil curse syndrome were reviewed, specifically, as observed in their oil revenue management mechanisms and in their legal and operational frameworks, as well as the proposed mechanisms for Uganda, with an objective of mapping out key audit issues therein that supreme auditing institutions should interest themselves with when conducting audits of oil revenues.

Finally, the preparedness of the audit institutions, taking a case study of the OAG, Uganda, has been evaluated in this project using the ISSAI standards as developed by INTOSAI, and in particular, ISSAI 1[43], which requires the establishment of an independent government auditing institution, with powers to conduct independent audits, and reporting objectively, while maintaining a cordial working relationship with Parliament, Government and the implementing administrations. ISSAI 1 also requires SAIs to develop proper auditing methodology, recruit competent staff and maintain international exchange of experience. The evaluation, in

[43] http://www.issai.org/media/12901/issai_1_e.pdf

accordance with ISSAI 1, was simplified by applying AFROSAI-E (Regional body of INTOSAI) Institutional Capacity Building Framework (ICBF)[44]. ICBF measures SAI institutional capacity using five parameters: (1) independence and legal framework, which assesses if SAIs operate in a favourable environment that allows objective reporting; (2) Organization and Management, which assesses SAIs' internal processes that enable them exercise their mandates; (3) Human resource, which assesses SAI capacity to recruit, retain, train and develop its staff and also share this capacity with others SAIS; (4) Auditing Standards and methodology, this assesses the SAIs technical capacity to conduct audits including audit plans, tools, quality control, expertise procedures and reporting of audit results; and (5) Communication of results and stakeholders management, which assesses SAI's capacity to communicate its results and purpose, both internally and externally, including its interactions with Parliament, the media and the public, including academic institutions and the international community. The ICBF was used to ascertain how prepared SAIs were in conducting oil revenue audits, a case study of OAG, Uganda.

3.2 Limitations

The initial research design included plans to obtain stakeholders' views on the oil curse syndrome, a perspective of Uganda, using a simple electronic questionnaire. The questionnaire was designed in accordance with the University of Dundee research guidelines (**Appendix C**) and sent to 108 respondents from key government institutions in charge of oil revenue management. At the time of concluding this research, no single respondent had answered the questionnaire. However, this challenge was overcome by obtaining and analysing additional information from source documents and websites of institutions.

[44] http://afrosai-e.org.za/institutional-capacity-building-framework

CHAPTER FOUR

4.0 PREPAREDNESS OF THE NATIONAL AUDIT INSTITUTIONS

Building strong institutions is a critical function and key to controlling corruption and SAIs can play a key role in promoting sound financial management systems and holding governments accountable (Kenneth M et al., 1998). Kenneth M et al. (1998) identifies four key factors that lead to the success of a SAI: (1) Clear mandate (2) independence (3) adequate funding and staff, and (4) sharing of knowledge and experience.

The preparedness of the National Audit Institutions, commonly referred to as, Supreme Audit Institutions (SAIs), can be evaluated using the ISSAI standards as developed by INTOSAI, and in particular, ISSAI 1[45], which requires the establishment of an independent government auditing institution. Accordingly, This Project simplifies the evaluation using the Institutional Capacity Building Framework (ICBF)[46] as developed by AFROSAI-E, of which most of the Sub Sahara African SAIs are members. The Framework is based on ISSAI 1 and looks at the capacity of a SAI from five parameters: (1) Independence and legal framework; (2) Organization and management; (3) Human resource; (4) Auditing standards and audit methodology; and (5) communication of results and stakeholder management, which are discussed below:

4.1 Independence and Legal framework

ICBF requires SAIs to be independent in both operational and financial functionalities and deriving their mandates from the constitution and/or legal framework and directly submitting their reports to Parliament[47]. The OAG is a very independent SAI established by an Act of

[45] http://www.issai.org/media/12901/issai_1_e.pdf
[46] http://afrosai-e.org.za/institutional-capacity-building-framework
47 Ibid

Parliament (Article 163 of the Constitution of the Republic of Uganda, 1995 (as amended) and directly reports to Parliament. The NAA, 2008, further gives the SAI more mandate and responsibilities to carry out various audits (as discussed in 2.4 of this project). All the laws and policies on the petroleum subsector and specifically on oil revenue management, in Uganda (as discussed in 2.5.1 of this project) have bestowed upon the AG the mandate and responsibilities (as discussed in 2.5.2 of this project) to conduct financial and any other management audits to ensure transparency and accountability in oil revenue management. Using the backing of the legal and operational framework in the subsector, the OAG is in a better position to carry out audits in oil revenue management. However, the OAG has not fully achieved financial independence as his operational budgets also face underfunding like any other government institutions (AG annual performance reports, 2010/11; 2011/12 and 2012/13)[48], thus affecting his area of audit coverage and this might also apply to the petroleum audits.

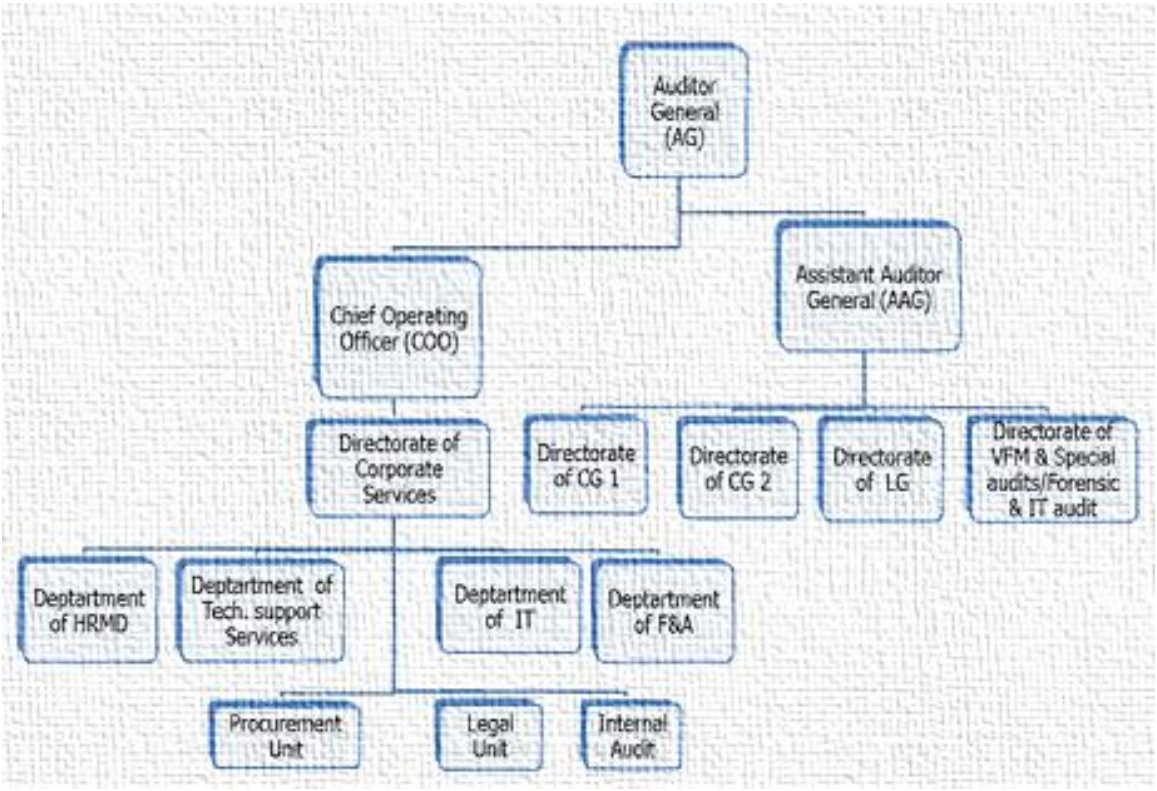
4.2 Organization and Management

ICBF requires SAIs to have a clear leadership and direction thereby preparing strategic and operational plans, organizing themselves, including setting up a performance audit, Information System audit, and IT support functions. The Framework also requires SAIs to establish an internal control system; properly manage their resources, such as introducing MIS and staff time recording system, and also setting up a code of ethics, which should be monitored for compliance[49]. The OAG is headed by the AG, who is assisted by the Assistant AG (in charge of auditing function) and the Chief Operating officer (in charge of corporate functions and who also doubles as the Accounting Officer). There are six Directors, five of them in charge of various audits (Financial audits-CG1, CG2 & LG; Value for money audits; and Forensics, Investigations and Special audits) and one Director in charge of Corporate Division. There are

[48]http://www.oag.go.ug ; Annual Performance Reports
49 http://afrosai-e.org.za/institutional-capacity-building-framework

four departments under the corporate division (HR management and development, Technical support services-for Quality Control and Assurance, IT and Finance and Administration). Under the departments, there are three specialized units (Procurement. Legal and Internal audit)[50]. The OAG has also a top management team, comprising AG, AAG, Directors and Assistant Directors, which is responsible for policy direction[51].

Figure 8: Organizational Structure, OAG, Uganda



Source: Office of the Auditor General, Uganda

N.B: The Directorate of VFM& Special audits/Forensic& IT has been split to form two directorates: Directorate of Value for Money and Directorate of Forensics, Investigations and IT audits[52].

[50] http://www.oag.go.ug/index.php?option=com_content&view=article&id=27&Itemid=25
51 http://www.oag.go.ug/index.php?option=com_content&view=article&id=8&Itemid=9
52 http://www.oag.go.ug ; Annual Performance Report 12/13

The OAG prepares five-year strategic plans. Its current corporate plan covers a period from 2011 to 2016[53]. The OAG during its corporate plan period aims at achieving four objectives: (1) to improve the quality and impact of audit work to promote increased accountability, probity and transparency in the management of public funds; (2) to improve the efficiency and effectiveness of internal and external communications to raise the corporate image of the OAG among the key stakeholders; (3) to strengthen the financial and operational independence of the Office of the Auditor General; and (4) to attain higher organisational performance[54]. The corporate plan forms the basis for preparation of both the OAG annual plans/ budgets and directorate annual audit plans.

The above level of organization and management is in line with the ISSAI and ICBF requirements and puts the OAG in a strong position to carry out the audit of oil revenues in the country. However, the current lean 'Energy Sector', under the Directorate of CG2, may not be in position to effectively conduct appropriate petroleum audits, thus the OAG may be required to make some structural adjustments that will best fit the operations of the audit of petroleum subsector.

4.3 Human Resources

ICBF also obliges SAIs to have a human resource and professional development policy clearly indicating procedures for staff; recruitment, remuneration, performance measurement, training, career development, welfare, professional development, retaining, rotation, and exit, which should be reflected in the strategic plan and aligned to annual operational plans. The SAI should also have capacity to train its staff, as well as promoting knowledge sharing with other SAIs. The OAG has undertaken staff training and professional development, for example, during FY

53 http://www.oag.go.ug/index.php?option=com_docman&Itemid=80
54 http://www.oag.go.ug/index.php?option=com_content&view=article&id=8&Itemid=9

2012/13, a total of 504 staff were trained in different areas: 30 staff trained in professional courses (ACCA, CPAU, CISA and CFE), 17 staff attained career development courses (4 for Master's Degree-Petroleum disciplines and one staff had completed his masters in petroleum accounting, 3 staff obtained Post Graduate Diploma and 9 staff attained Bachelor's degree) and 457 staff trained in skills enhancement trainings - disciplines, such as: Engineering audits, IT audits, VFM audits, financial audit, use of electronic audit working papers, use of forensic audit manual, communication for top managers, SAI professionalism, strategic human resource management and Oil and Gas audit; and the OAG has the highest number (106) of certified accountants in the country from a single institution[55].

The AG, under the NAA, 2008, Section, 9 has powers to determine his staff requirements, appoint, disappoint and remunerate. The office has also developed a HR manual and policy which guide the recruitment, remuneration, training, performance appraisal, rotation, welfare, and career development of staff. OAG has a pool of skilled staff from which it can draw, using the inter-directorate synergies, to conduct the audit petroleum subsector including the audit of oil revenues.

4.4 Auditing Standards and Audit Methodology

ICBF further requires SAIs to apply auditing standards and design proper methodology when conducting their audit work. This entails: the development of annual audit plans, which clearly indicate risks assessed, current issues and stakeholder expectations, audit scope, activity plans for regularity and performance audits, and designing measures to address backlogs; development of audit manuals, which are aligned to international standards on auditing and which should regularly be updated and staff trained on their use; establishing quality control and assurance measures, including external reviews by other SAIs; promoting the use audit

[55] http://www.oag.go.ug ; Annual Performance Report 12/13

techniques such as electronic working papers and computer assisted audit techniques (CAATS); communicating the audit process to the auditees; use of experts, including relationships with professional bodies, relevant journals, and other SAIs; and development of standard report structures, which are user friendly and with materiality considerations with a follow up mechanism of previous recommendations.

OAG bases its audits on ISA and has currently rolled out the use of ISSAIs; it has revised its Regularity and VFM audit manuals to ensure that they are aligned with auditing standards. Staff have been re-trained on the use of both manuals. The OAG has an established quality control and development unit, which conducts hot reviews, coordinates the development audit methodologies, reviews teammate libraries (CAATS) for the regularity audits (CG and LG) and VFM audits. Both audit manuals prescribe the audit procedures of how auditors should conduct entry and exit meetings during commencement and completion of audits, respectively. The office produces standard reports and abridged reports for easy reading, and outstanding matters in the previous reports are brought to the attention of Parliament in the current reports. All audit reports are uploaded on OAG website and compact disks (CD) distributed to stakeholders. The SAI participates in AFROSAI activities both as a participant and a facilitator. It has 17 trainers in performance auditors and currently over 5 trainers are facilitating regional trainings and one facilitator in SAI-PAC communication training. All of these details have been obtained from the Auditor General's performance reports[56].

However, the challenge ahead of the OAG is that the audit of extractive industries, including oil and gas activities presents peculiar and complex circumstances[57], which require a clear understanding by the SAIs in order to identify and assess associated material risks in

[56] http://www.oag.go.ug ; Annual Performance Report 12/13

[57] http://www.iasplus.com/en-gb/news/2010/April/news5494

accordance with ISA315[58] and ISSAI 200 para. 86-95[59]. Areas of contention have been; (1) How to estimate and classify the quantities of minerals or oil and gas discovered; (2) how to account for minerals or oil and gas properties; (3) how minerals or oil and gas should be measured; and (4) what information about extractive industries should be disclosed.

IFRS are increasingly becoming significant as the need for reliable, transparent and comparable financial reports progressively become central to decision making in the petroleum sector (Zaif and Karapinar, 2012). However, IFRS 6: Exploration for and evaluation of mineral resources, has given companies a lot of room to determine their own accounting policies (Zaif and Karapinar, 2012), even including those used before the coming into force of IFRS 6, as well as giving exceptional treatment under IAS 8: Accounting policies, changes in accounting estimates and errors, IAS 16: Property Plant and Equipment, IAS 36: Impairment of Assets and IAS 38: Intangible Assets[60]. This creates a problem of comparability of results and also increases the 'Audit Risk', especially, where proper audit guidance has not been given in form of; Statement of Recommended Practices (SORP), Audit guidelines and procedures. For example, different cost methods, such as: Full Cost Method (FCM) or Successful Effort Method (SEM), and amortization methods, such as: Straight line Method (SLM) or Unit of Production (UOP), are used in extractive industries depending on which costs are to be capitalized, and the motives of the oil company to either delay or bring nearer recoveries to its advantage (Zaif and Karapinar, 2012).

The gap in the IFRS and the discretionary use of accounting policies by oil companies; the peculiar characteristics of oil revenue- discussed in 2.2.1 of this project (which make it massive, unstable, opaque (Ross, 2012 and Morrison, 2013); the complex oil revenue management

[58] http://www.ifac.org/auditing-assurance/clarity-center/clarified-standards
[59] http://www.issai.org/media/69910/issai-200-english.pdf
[60] http://www.iasplus.com/en-gb/standards/ifrs-en-gb/ifrs6

mechanisms (discussed in 2.2.2 of this project); the complex oil revenue management environment (discussed in 2.2.3 of this project); the complexity of oil revenue sharing arrangement- shown in figure1; and the bad examples of misappropriation of oil revenues already reported in some African countries (Kopinski et al., 2013, Ploeg, 2011a and Ploeg, 2011b), all increase the 'Audit Risk', thus requiring Standard setting bodies to review reporting standards, and SAIs also to rigorously review their audit methodologies.

Like any other SAIs, SAI-Uganda, has not yet developed an appropriate audit methodology, including guidelines and procedures for comprehensive audit of the petroleum subsector. However, the OAG has been conducting petroleum cost recovery audits and has completed an environmental audit in the subsector[61].

4.5 Communication of Results and Stakeholder management

Lastly, the ICBF require SAIs to develop a communication policy and strategy covering both internal and external communication based on: a legal framework; clear vision, mission, values and an analysis of stakeholders; identified communication channels between the SAI Parliament, PAC, Judiciary, staff, ministry responsible for finance and other oversight bodies; communication arrangement with the media, public, academic institutions, international community, using effective information sharing practices; and SAI annual performance reports clearly indicating audit coverage, number of signed and issued reports, coverage of IS audit, time of submission of audit reports to parliament, and stakeholders' view on the benefits of the audit.

OAG has a communication policy and has effectively used it to communicate to both staff and other stakeholders, especially Parliament. The office has a parliamentary liaison department,

[61]http://www.oag.go.ug/index.php?option=com_phocadownload&view=category&id=31:2012-2013&Itemid=86

headed by an Audit Manager who coordinates SAI-Parliament activities, including scheduling PAC meetings and the department assists Parliament in the drafting of parliamentary recommendations. The SAI has a well-established website[62] on which all published AG's reports are uploaded and other public information, including its vision, mission and core values. The AG, also prepares his annual performance reports, which are also published on OAG website[63]. The website also has links to other government ministries, departments and agencies and the international professional bodies and organizations to which the SAI is a member[64].

The OAG is in a better position to communicate its revenue audit results using the existing communication and stakeholder management strategy, which complies with ICBF standard.

Generally, according to AFROSAI-E Activity report on SAIs, 2010[65] resulting from a self-assessment of all the 23 member SAIs using ICBF, it was found that majority of SAIs were on level 2-development level (The Framework grades SAIs from levels 1, 2, 3, 4, 5), which indicates that majority SAIs, although had developed some tools and audit practices, and plans to enable them function properly in accordance with international standards and best practices, they had not implemented them. This impairs their preparedness to audit extractive industries, including audit of oil revenues. However, AFROSAI noted that the audit coverage and the time SAIs were taking to report their results to parliament had improved.

On another positive note, AFROSAI noted the accelerating growth of the petroleum sector in Africa and issued audit guidelines on the regularity audit of the extractive industries-Audit Considerations for Extractive Industries[66].

[62] http://www.oag.go.ug/index.php?option=com_content&view=frontpage&Itemid=1
[63] Ibid
[64]http://www.oag.go.ug/index.php?option=com_weblinks&view=category&id=24%3Ainternational-links&Itemid=12
[65] http://afrosai-e.org.za/sites/afrosai-e.org.za/files/consolidated_version.pdf
[66]http://afrosai-e.org.za/regularity-audit/publications/afrosai-e/audit-considerations-extractive-industries

Based on the evaluation by this project, SAI-Uganda has developed and implemented the necessary audit tools, audit practices and plans, what it requires now is to incorporate the emerging developments of the extractive industries, and specifically those of oil and gas sector in its audit methodology, as well as leveraging on the synergies from its independence and legal framework, organization and management, human resources, and communication of results and stakeholder management. This will enable the office get fully prepared to conduct oil revenue audits and other related audits in the sub sector.

CHAPTER FIVE

5.0 CONCLUSION

Uganda, like any other Sub Sahara African countries, is a developing economy, with high hopes that the discovery of oil will change its economic path and improve the standards of living of its citizenry (National Oil and Gas Policy, 2008, Sections, 4.3 and 4.8). However, research and surveys have shown that possession of natural resources can offer both negative effects and benefits (Frankel, 2010). It is imperative that African countries develop strong institutions, including the SAIs in order to manage their oil resources effectively (Grynspan, 2012) and avoid the resource curse syndrome (Morrison, 2013, Ross, 2012, Enisan , 2012 and Mitchell, 2009). The Oil curse has been attributed to many factors, such as: corruption, rent seeking, inequality, inadequate policies, and weak institutions (Ross, 2012 and Adeniyi and Ushie, 2013); and lack of rule of law, corruption, presidential democracies, and underdeveloped financial systems (Ploeg, 2011b), thus making oil producing countries susceptible to resource curse syndrome (Kopinski et al., 2013). A number of oil revenue management mechanisms have been suggested, which Uganda and other African oil- producing countries can adopt. They include: Restrained government spending; Establishment of special oil funds; Economic diversification; Good governance and rule of law; building strong institutions, including supreme audit institutions, and learning from one another.

Uganda appears to have widely consulted and prepared herself against the oil curse as observed from its existing and proposed legal and operational framework, and governance and accountability system, which highly entrench the role of the office of the Auditor General in ensuring efficient and effective use of oil resources.

Building strong institutions is a critical function and key to controlling corruption, and SAIs can play a key role in promoting sound financial management systems and holding Governments accountable (Kenneth M et al., 1998). SAIs need to possess: (1) Clear mandate (2) independence (3) adequate funding and staff, and (4) sharing of knowledge and experience (Kenneth M et al., 1998) and should constantly strive to improve on their independence and legal framework, organization and management; human resources, Audit standards and audit methodology, and communication of results and stakeholder management (AFROSAI-E).

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APPENDICES

Appendix A: Detailed *Summary of Legal and Operational Framework in the Petroleum Subsector*

Key Institution	Roles/Responsibilities
Ministry of Energy & Mineral Development and its technical department, PEPD	Generally responsible for policy formulation and implementation, regulation of the subsector and managing the commercial aspects, and coordinating national oil capacity building, including: licensing; industrial promotion; issuing policy and regulations; legislation drafting; Negotiating, endorsing and managing PSAs; Approval of field development plans; participation in formulation of oil revenue management laws; promotion of transparency; approving data management systems; Recommend for options for state participation; and dissemination of information
Ministry of Finance	Management of the Petroleum Fund, including: overseeing the transfer into and disbursements from the Fund; maintaining proper records and books of account of the Fund; Preparing and submission of semi-annual and annual financial statements to the Minster, ST and AG; present to Parliament estimated petroleum revenue for the financial year by 30th September, and semi-annual and annual reports by 1st April and 31st December, respectively; issuing of the petroleum investment policy; Tabling to Parliament annual petroleum reserve investment plan; Drawing up management contracts of the fund management;
Uganda Revenue Authority (URA)	Collection and receipt of petroleum revenue; Assisting in monitoring and assessing the impact of oil and gas revenue on the economy; and participate in formulation of tax measures to regulate collection of the right revenues from oil and gas.
Office of the Auditor General	Generally provide and independent oversight of government petroleum operations through conducting financial audit and other management audits in accordance with the constitution and any other relevant legislation. The OAG should ensure adherence to national and international accounting standards in oil and gas sector, including; Auditing of the Petroleum Fund; Receipt of copies of the receipt of the Petroleum received in kind; Issuing audit warrants for withdraws from the Holding Fund to the Consolidated Fund and Petroleum Revenue Investment Reserve; receipt for review and audit of semi-annual and annual financial statements of

	the Fund prepared by Accountant General; Audit the financial statements of the PRIR
Parliament	Enacting regulations for the petroleum subsector and generally overseeing the performance of the Fund including: Appropriating funds in the holding account to the consolidated Fund and Petroleum Revenue Investment Reserve;
Bank of Uganda (BoU)	Operational management of the Holding account and Petroleum Revenue Investment Reserve in accordance with the Ministry of Finance investment strategic funds plan, including: Preparation of annual plans; Appointment of the external manager to manage the PRIR; maintain proper books of account for the PRIR and prepare and submit semi-annual and annual financial statements to the minister and copy the same to AG, ST and Accountant General by 15th February and 31st August, respectively; preparing monthly performance reports; prepare annual report of the PRIR and submit to the Minister of finance and AG; and report to the Investment Advisory committee on the performance of the Fund.
Investment Advisory Committee	Advise the minister on general petroleum fund investment activities, including; formulation of the petroleum fund investment policy; setting reporting requirements to the fund manager; and setting ethical codes and standards for funds management
The Petroleum Authority of Uganda (PAU)	Generally its role is to regulate the subsector, including: Reserve estimation and measuring oil and gas produced; Assisting in negotiation and administering of PSAs; Assessing field development plans; Assisting in measurement, estimation, and assessment of royalties and cost oil due to State; Ascertaining Cost oil due to Licensees; ensure optimal level of resource exploitation; cost efficient operations, optimal utilization of existing and planned infrastructure; Provision of information for tax collection and other fees;
National Oil Company (NATOIL)	Generally handling state commercial interests in the subsector, including: Marketing government share of oil and gas received in kind

Appendix B: ***Detailed roles and responsibilities of Key Institutions in the Petroleum Subsector***

Regulation/Policy	**Key objective/Purpose**
Petroleum (Exploration, Development and Production) Act, 2013	Governing exploration, development and production activities, including: licensing, drilling, decommissioning of projects, domestic supply obligation, pricing of oil, local content, pollution, Health and safety, information and data, payments, and offences. It also provides for the establishment of the Petroleum Authority of Uganda and the National Oil Company.
Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act, 2013	It also provides for the establishment of Petroleum Authority and the National Oil Company; licensing of midstream operations (refining, pipeline, etc.); Venting and flaring of gas; pricing of petroleum commodities and products; domestic supply obligations; decommissioning of projects; local content; pollution; Health and safety, information and data, payments, and offences.
Petroleum Supply Act, 2003	This is the law primarily managing petroleum activities in the downstream (Petroleum Stations, Transportation, Etc.); issuing operating licenses; Market competition; security of supply; Public safety and environment; National strategic stocks; offences; and mediation and reviews.
Public Finance Bill, 2012*	Basically, when passed, the bill will provide for public financial management in Uganda, including the legal and regulatory framework for the collection, allocation and management of the petroleum revenue; Give guidance on: the development of fiscal policies & National Budget; creation of contingency fund; management of the Consolidated Fund; management of government bank accounts; Borrowing & management of public debt; management of grants; Assets management; and Accounting and Audit.
Oil and Gas policy, 2008	Basically gives guidance to the development of the emerging oil and gas sector. It supersedes the Energy Policy, 2002 in matters of exploration, development, production and utilization of oil and gas resources. It also provides for a framework for efficient management of oil

	and gas resources including the revenues accruing therefrom.
Oil revenue Management policy, 2012	This is the policy that gives direction on: the fiscal regime necessary for collection and administration of oil and gas revenue; microeconomic management framework; oil and gas revenue sharing; Banking, accounting and auditing of oil and gas revenue; and on governance, transparency, investment, oversight and control, and encumbrance issues of the Petroleum Fund.
Energy Policy, 2002	Gives guidance on energy matters in the country including the generation, distribution and supply of power; Petroleum use; Renewables; Atomic energy and conservation of the environment and climate change.

Appendix C: Research Questionnaire

RESEARCH QUESTIONNAIRE

Building Strong Institutions: a prerequisite for preventing the Oil curse syndrome

I am a Ugandan student currently pursuing a MSc Degree in Oil and Gas management at the University of Dundee, Scotland, UK. I am finalising the Programme and am subsequently required to carry out a research work as one of the requirements for the successful completion of the Programme. The research is being supervised by **Dr. Ayodele Asekomeh** from the Centre for Energy, Petroleum and Mineral Law and Policy (CEPMLP), University of Dundee.

The purpose of this research questionnaire is to kindly seek your views, as one of the key stakeholders, on the above stated subject matter, which I briefly introduce to you in the next paragraph.

The Oil curse syndrome, also referred to as the "Paradox of plenty" is a phrase that brings into context the fact that despite the country's endowment with natural resources, the resources' revenues are not properly utilized to foster economic growth that can lead to a positive change in the well-being of its citizenry. The recent discovery of oil in Uganda in 2006, and the Government's ambitions of starting early production in the next 5 years raise hopes amongst many Ugandans that the oil revenues will turn around the economic path of the country, thus improving their welfare significantly through government's provision of better services, such as: Education, Health and roads infrastructure, etc. However, empirical evidence, through research, has shown that this has not been always a straight case in some countries, especially in developing economies. The challenge has been attributed to poorly or inadequately prepared or established institutions among other factors. Building strong institutions has been viewed as a prerequisite for preventing the oil curse syndrome.

I once again kindly seek your views on the matter by briefly responding to the attached questionnaire. Any information/responses given shall strictly be used for academic purposes and shall be treated with utmost confidence and in accordance with the University of Dundee's research ethics guidelines. If you want to find out about the final results of the research, you should contact the CEPMLP, through **Dr. Ayodele Asekomeh** on e-mail address: a.asekomeh@dundee.ac.uk

Thank you for taking your invaluable time on responding to this questionnaire.

Yours Sincerely,

Godwin Bob Monday

University of Dundee

RESEARCH QUESTIONNAIRE

QN.1 Please, kindly indicate:

a) Name of your institution/Organization Click here to enter text.

b) Your Title: Click here to enter text.(Name not necessary)

c) Your Role/ Management level (Please click in the option circle appropriately)

○ Subordinate staff ○ Middle manager ○ Senior Manager

○ Executive/Head of Organization

QN.2 (a) Briefly state what role /responsibilities your institution or organization plays or will play in the Petroleum sub-sector:

Click here to enter text.

(b) There are specific activities attached to the above roles/responsibilities. (Please click in the option circle appropriately)

○ Strongly Agree ○ Agree ○ Neither Agree nor Disagree

○ Disagree ○ Strongly Disagree

(c) If you agree, could you please briefly state those activities below?

Click here to enter text.

QN.3 Are the roles/responsibilities and activities clearly specified in any legal or administrative instrument? If yes, please, state below the instrument(s):

Click here to enter text.

QN.4 (a) The above stated instrument(s) **adequately** provide for the conduct of your roles/responsibilities and activities in the petroleum sub sector. (Please click in the option circle appropriately)

○ Strongly Agree ○ Agree ○ Neither Agree nor Disagree

○ Disagree ○ Strongly Disagree

(b) Please briefly state those roles/responsibilities and activities which are **not** adequately provided for.

Click here to enter text.

(c) Are there any other roles/responsibilities or activities which have not been specified that you feel your institution/organization should be involved in? If yes, kindly state below:

Click here to enter text.

QN.5 (a) At what level of organizational set up are the activities of the petroleum sub sector in your institution/organization coordinated? (Please click in the option circle appropriately)

○ Unit/Section ○ Department ○ Directorate

○ Others (please specify)

(b) Would you suggest any other level that would enable you operate appropriately and for what reasons? Please briefly state below:

Click here to enter text.

QN.7 (a) There is **adequate capacity** (personnel- numbers & skill competences; equipment; and logistic support) in your organization/institution to undertake your roles/responsibilities and activities in the petroleum sub sector. (Please click in the option circle appropriately)

○ Strongly Agree ○ Agree ○ Neither Agree nor Disagree

○ Disagree ○ Strongly Disagree

(b) Please state briefly below how your organization/institution can be strengthened to carry out its roles/responsibilities and activities in the petroleum sub sector:

Click here to enter text.

QN. 8 (a) Transparency and accountability are key institutional principles that strengthen organizational performance and reputation. (Please click in the option circle appropriately)

○ Strongly Agree ○ Agree ○ Neither Agree nor Disagree

○ Disagree ○ Strongly Disagree

(b) What mechanisms or activities are available at your organisation/institution that ensure/will ensure transparent and accountable conduct of your business in the petroleum sub sector? Please, briefly state below:

Click here to enter text.

QN.9 (a) The Office of the Auditor General will complement your organization/institution's efforts in improving transparency and accountability in the petroleum sub sector. (Please click in the option circle appropriately)

○ Strongly Agree ○ Agree ○ Neither Agree nor Disagree

○ Disagree ○ Strongly Disagree

(b) How would you like the Office of the Auditor General to complement your efforts in improving transparency and accountability in the petroleum sub sector? Please, briefly state below:

Click here to enter text.

(c) The Office of the Auditor General conducts several audits. Which audit(s) would you suggest for the improvement of transparency and accountability in the petroleum sub sector? (Please click in the option circle(s) appropriately)

- ○ Financial Audits
- ○ Value for Money/Performance Audits
- ○ Fraud/Investigations Audits
- ○ Special Audits
- ○ Envoronmental Audits
- ○ Gender Audits
- ○ Procurement Audits
- ○ Petroleum Cost Recovery Audits
- ○ Any other, Please specify below

Click here to enter text.

QN.10 (a) Proper utilization of petroleum revenues will foster the county's economic growth, thus leading to a positive change in the well-being of its citizens. (Please click in the option circle appropriately)

- ○ Strongly Agree
- ○ Agree
- ○ Neither Agree nor Disagree
- ○ Disagree
- ○ Strongly Disagree

(b) Please, briefly suggest below, the ways how you would like Government to properly utilize the petroleum revenues for the benefit of its citizens.

Click here to enter text.

(c) In your opinion, what are the likely practices that may lead to the misuse of the petroleum revenue? Please, briefly state below:

Click here to enter text.

(d) Basing on the likely practices mentioned above, what measures would you suggest to government that will minimise their likelihood? Please, briefly state below:

Click here to enter text.

Q.N 11 Is there any other information you would like to share in relation to this subject matter? Please, briefly state below:

Click here to enter text.

Please, kindly save file as: "Responses", reply e-mail and send as attachment to g.monday@dundee.ac.uk

THANK YOU ONCE AGAIN FOR TAKING YOUR INVALUABLE TIME ON RESPONDING TO THIS QUESTIONNAIRE.