

# OIL EXTRACTION IN LAKE ALBERT

## Briefing booklet

### Action for Better Governance Programme



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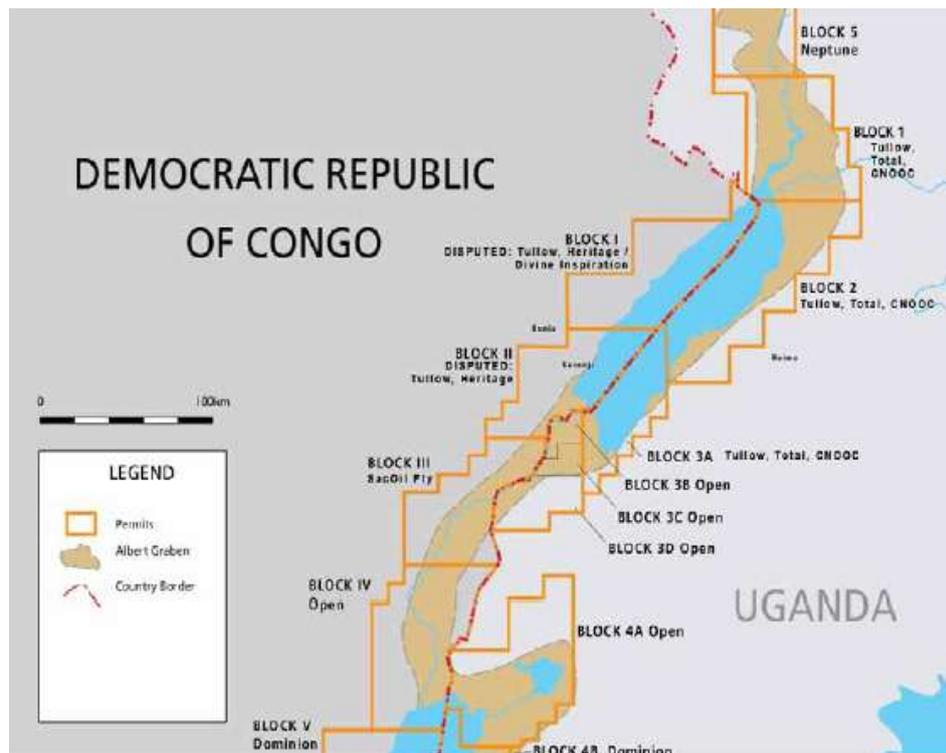
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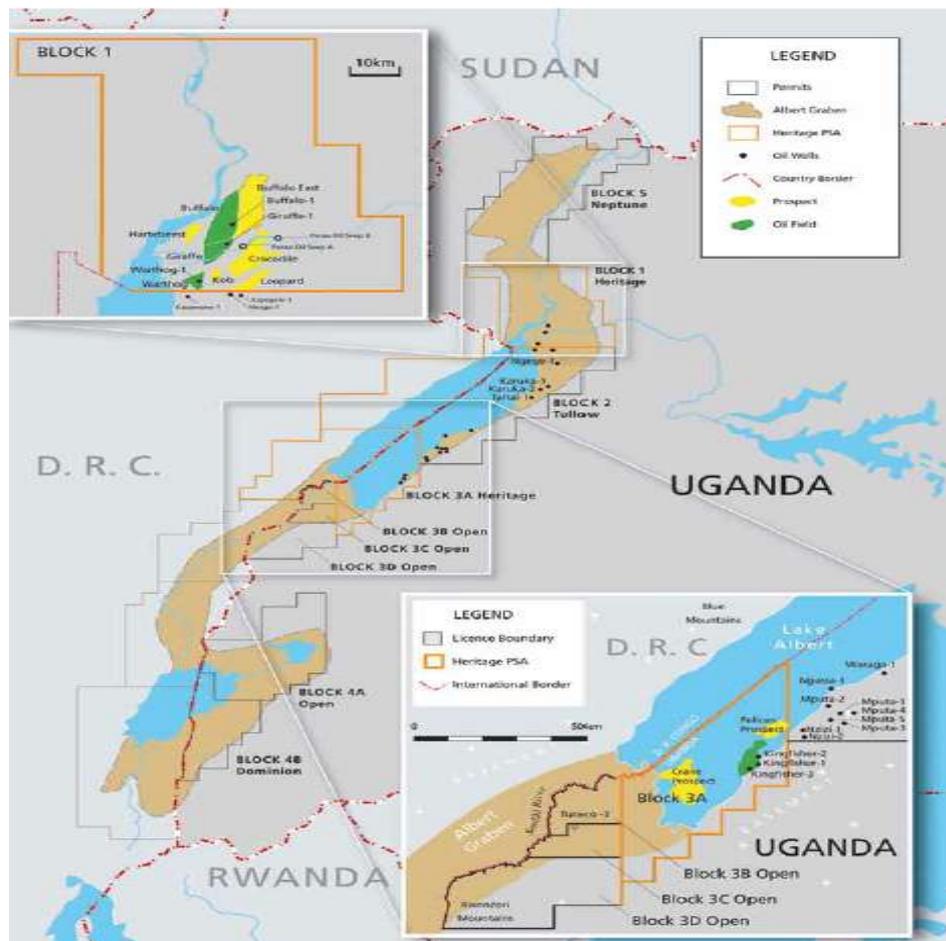
Every possible effort has been made to ensure that facts and figures are stated accurately in this booklet. However, not all the available sources are equally up to date, and the situation in both countries is subject to change and in many aspects subject to secrecy. Therefore no guarantees can be given that the booklet is entirely accurate and up to date in every detail.

# Oil blocks around Lake Albert, 2010

**DRC**



**Uganda**



Note: 'Open' blocks are those not yet allocated to a company or consortium when these maps were originally published in 2010

## **Background and developments to date**

Lake Albert, 160 km long and averaging 32 km wide, is Africa's seventh largest lake. It forms part of the Uganda–Democratic Republic of Congo (DRC) border, with the two countries sharing the lake. The land surrounding Lake Albert is rich in biodiversity and on the Ugandan side partly a designated protected area. Much of the land is used for agriculture (crops and livestock) and human settlements, while the lake provides fish for the surrounding communities and beyond.

Ituri on the DRC side and Nebbi, Amuru, Buliisa, Hoima, Kibaale and Bundibugyo on the Uganda side surround the lake. Population growth is expected to increase pressure on natural resources and access to land. Future oil extraction and processing will pose major additional risks to the environment, with effects on Uganda's important tourist industry likely.

Ituri in the eastern DRC is one of the country's poorest and least stable regions, experiencing a brutal war in 1998–2003 and still conflict-prone, despite the presence of United Nations troops. Uganda was militarily involved in the DRC in the 1990s, with links to some Congolese militia, and there is evidence that Ugandan officers were involved in trafficking DRC minerals. Agreements between the DRC and Uganda under the Arusha Pact have not yet fully been implemented, although relations have improved.

### ***Oil discovery***

Current oil exploration began in Uganda's part of the Lake Albert basin in the late 1990s, increasing in 2003–4, and major finds were confirmed in 2006 and 2007, both offshore (under the lake bed) and onshore.

The Ugandan government has negotiated and renegotiated production sharing agreements (PSAs) with international oil companies for more than 10 years. The world economic downturn and other factors have however slowed development. Among the first international exploration companies involved were Tullow and Heritage. Tullow is developing partnerships with larger international production companies Total and CNOOC (China). Tower and Dominion are also present in Uganda. The government has allocated five of its current nine exploration blocks to companies.

Uganda enacted an Oil and Gas Policy in 2008, but its new guidelines have not yet been implemented. The Ministry of Energy and Mineral Development is drafting a new oil law to regulate the sector. Final revision was due by end-2011 but has been delayed. A key question for Uganda is whether to develop a refinery, a pipeline or railway to transport the crude oil. Production is expected to start in 2013.

On the DRC side oil exploration is developing more slowly than in Uganda, although the DRC has been a minor oil producer from other parts of the country since the mid-1970s. The DRC government has said that it will open up 16 exploration licences and has signed PSAs with at least two sets of companies: in 2006 with Tullow and Heritage, and in 2008 with Divine Inspiration Consortium, H-Oil, Sud, and Congo Petroleum & Gas. Oil exploration was expected to begin in 2010–11, but disputes and controversy have surrounded the PSAs, and plans are affected by Ituri's instability. CNOOC, Eni and Total are also interested in entering the DRC sector. The DRC is said to lack a policy framework for developing its oil industry, although work is under way on a new Oil Code.

In 2010 a reportedly secret deal was revealed relating to Blocks 1 and 2 on the DRC side of Lake Albert. Two previously unknown oil companies, Caprikat and Foxwhelp, were granted rights to the two blocks by presidential decree. This was 'despite the government already awarding the blocks multiple times to other companies', according to investigative NGO Global Witness.

### **Issues of concern**

Lack of information about development of the oil sector on both sides of the border, including contract secrecy and strong rumours of corruption, has led to much mistrust.

Ugandan civil society has campaigned about the secrecy surrounding the first PSAs (only part of which have been made public), the government's apparent lack of a strategy for the use of oil revenues, legislative delays and allegations of corruption. Ituri civil society has strongly criticised the way the DRC has developed its sector to date, and some critics argue that oil extraction in Ituri poses a direct threat to food security and employment. Concerns particularly surround the potential environmental hazards in both countries. There is much uncertainty about how the DRC and Ugandan governments and companies will manage these risks during and after production.

Full exploitation of the offshore oil will require political and technical cooperation between the DRC and Uganda and could lead to conflict if the countries do not honour agreements. The DRC is said to fear that Uganda may 'steal' part of its share of the oil. Congolese and Ugandan rebel groups operating in the area add to conflict risks.

International oil companies, especially early entrants Tullow and Heritage, are thought likely make huge profits at Lake Albert. Civil society critics widely accuse both governments of making agreements that are far too generous to the oil companies and leave the countries themselves with an unfair burden of risk.

#### **The 'resource curse'**

Over 50 countries worldwide are defined as natural-resource-rich. In sub-Saharan Africa nearly half the population lives in oil- and mineral-rich countries, yet most of such countries have poor levels of human development. The phrase 'resource curse' describes how many resource-rich developing countries experience negative economic, social and environmental consequences from oil and minerals exploration and production.

Natural-resource-dependent economies tend to be vulnerable to 'boom and bust' cycles – large sudden inflows of revenue from selling oil and minerals at high prices, followed by declines in revenue when the resource prices or demand levels fall rapidly, or when production slows or reserves are depleted. Volatile prices and unstable revenues make budget forecasting difficult.

Other factors in the 'resource curse' include: companies using transfer mispricing to move profits out of host countries to tax havens and secrecy jurisdictions, depriving the host government of a fair share of the revenue; government financial mismanagement and corruption; unplanned public spending sprees on socially useless or divisive projects; high inflation that distorts and weakens other sectors of the economy, especially exports; strengthening of patronage systems that undermine accountability and stability; mistrust when contracts are kept secret; negative social and environmental impacts on local communities, with poor levels of compensation; a loss of governance transparency as 'easy' (unearned) money renders governments less reliant on earned income such as taxation; rising economic inequality; political instability; and in the worst cases violent conflict over who controls and who benefits from extracting the resources.

Counties that lack public sector capacity to develop the oil are also likely to have poor capacity in terms of negotiating, monitoring and managing contracts, managing revenue and expenditure flows, and mitigating negative social and environmental impacts.

## The companies involved

<b>Company</b>	<b>Where registered or listed</b>	<b>Where active</b>	<b>Remarks</b>
Caprikat	Virgin Islands (tax haven)	DRC	Possibly owned by nephew of South African President Zuma
China National Offshore Oil Corporation (CNOOC)	China	Uganda, interested in DRC	Very large, state-owned; partnering with Tullow
COHYDRO	DRC	DRC	State-owned
Congo Petroleum & Gas	DRC	DRC	Private
Divine Inspiration Consortium	South Africa	DRC	Private; close links to Encha Group (South Africa) and financiers Investec (UK/South Africa); links to Kabila family
Dominion	Uganda?	DRC, Uganda	
ENI	Italy	Interested in DRC & Uganda	Publicly listed
Exxon	US	Interested in Uganda	World's largest oil multinational; publicly listed
Foxwhelp	Virgin Islands (tax haven)	DRC	Possibly owned by nephew of South African President Zuma
Global Petroleum	Australia, UK	?	Upstream exploration
Heritage	UK listed, Jersey (tax haven) registered, previously Canada	DRC, Uganda	Owned by former mercenary; history of military involvement, eg in Angola; nominally partnering with Tullow in DRC
H-Oil	Cyprus, also Spain?	DRC	Private; links with Repsol (Spain)
Neptune	UK?	DRC	
SacOil	South Africa?	DRC	Joint venture between Divine and Encha Group
Soco	UK	DRC	
Sud Oil	DRC	DRC	Private; oil trader? Links to Kabila family
Total	France	Uganda, interested in DRC	Publicly listed; one of world's largest oil multinationals; partnering with Tullow
Tower Resources	UK	DRC, Uganda	Upstream exploration
Tullow Oil	UK, Ireland	DRC, Uganda	Publicly listed; mainly upstream exploration; partnering in Uganda with CNOOC and Total; nominally partnering in DRC with Heritage; likely to remain operating in Uganda

## What CAFOD and Trócaire can contribute

International faith-based NGOs CAFOD (UK) and Trócaire (Ireland) combine international advocacy on human-centred rights-based development, good governance and revenue transparency in the extractive industries (oil, gas and mining) with support for partner organisations working at grassroots level. They have both worked for many years on business and human rights issues.

CAFOD ([www.cafod.org.uk](http://www.cafod.org.uk)) is a leading UK member of the global Publish What You Pay civil society coalition. It is active in dialogue with politicians and officials in the UK and in the European Union concerning current European proposals for extractive industry revenue transparency legislation.

Trócaire ([www.trocaire.org](http://www.trocaire.org)) supports the Publish What You Pay agenda, maintains a dialogue with the Irish government and has recently published a *Business and Human Rights Advocacy Manual*.<sup>1</sup>

## Legal process related to oil extraction in the DRC and Uganda

### **Uganda**

Under Uganda's 2005 Constitution, 'All minerals and petroleum in, on or under any land or waters in Uganda are vested in the Government on behalf of the Republic of Uganda.' No person can lawfully carry out oil exploration or development operations without a licence. Other applicable laws are from before large-scale oil exploration began and include the Petroleum (Exploration and Production) Act 1985, Petroleum Act 1957 and Petroleum Supply Act 2003, as well as such laws as the Land Act 1998, Access to Information Act 2005, National Environment Act 1995 and Investment Code Act 1991.

Uganda has a legal requirement for companies developing oil and mineral resources to conduct an environmental impact assessment (EIA). In addition, the right to a clean and healthy environment is recognised in Ugandan law.

The 2008 National Oil and Gas Policy (NOGP)<sup>2</sup> assigns to the Ugandan parliament the role of passing oil industry legislation including for the management of oil revenues, and monitoring performance in the oil sector through policy statements and annual budgets. The NOGP highlights the need for a long-term national strategy to maximise benefits from oil exploitation to Ugandans and recognises the importance of transparency and accountability in handling all aspects of natural resource management, including towards affected individuals and communities.

Uganda is developing new legislation to implement the NOGP. A Petroleum (Exploration, Development, Production and Value Addition) Bill was approved by cabinet in 2010 and expected to be tabled before parliament during 2011, but progress appears to have slowed. The new law includes provisions to establish a Petroleum Authority to monitor developments in the oil sector, plus NATOIL to manage Uganda's commercial participation in the sector. There will be two national Commissioners. The Bill also addresses basic legal requirements on revenue sharing – such as licence fees, bonuses, tax payments, land rents, and royalty sharing among different government levels – environmental protection, health and safety, local content (such as job creation for Ugandans) and compensation for affected communities where applicable.

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<sup>1</sup> [www.trocaire.org/sites/trocaire/files/pdfs/policy/BusinessHumanRightsManualFinal.pdf](http://www.trocaire.org/sites/trocaire/files/pdfs/policy/BusinessHumanRightsManualFinal.pdf)

<sup>2</sup> [conserveuganda.files.wordpress.com/2010/06/national-oil-and-gas-policy-for-uganda.pdf](http://conserveuganda.files.wordpress.com/2010/06/national-oil-and-gas-policy-for-uganda.pdf)

## **Production sharing agreements (PSAs) and concessions**

**Production sharing agreements (PSAs)** are legal contracts that host country governments sign with foreign companies (or with consortiums of companies) allowing the company to explore for and/or produce oil, gas or minerals. The country retains ownership of the resource.

Oil PSAs require the company to provide capital investment for exploration, drilling, construction of infrastructure and production. The first oil extracted is often termed 'cost oil' and allocated to the company to sell to recoup its initial costs. Once the company has recovered its costs, the remaining 'profit oil' is divided between the host country and the company in agreed proportions. The company usually pays licence fees and taxes on its profit oil, and often royalties on all oil produced. Signature bonuses (initial payments to the host country for the right to develop a particular field or block) and production bonuses (when production begins) are also common.

Some PSAs involve the state, through a state-owned company, participating as a commercial partner in a joint venture or consortium with one or more foreign companies. In this case the state usually provides a percentage share of development investment and receives the same share of profits.

Under a **concession**, unlike a PSA, the government grants ownership of the resource in the ground to the company in return for royalties and taxes. PSAs have come to replace concessions because they appear to give governments more ownership and control, but in practice this may not result in more favourable terms for the host country.

PSAs are usually very complex documents, sometimes kept secret between the government (or a small number of politicians) and the company concerned. Because international oil companies often have better technical and legal capacity than developing country governments, or as a result of governments being impatient to turn natural resources into cash, or because of corruption, PSAs often grant excessively favourable terms to companies with regard to costs and payments due (including tax), human rights and environmental responsibilities, and business risk.

## **DRC**

The legal framework for the DRC oil sector is less well documented – at least in English-language publications – than for Uganda. In the DRC the state is empowered to grant large-scale commercial licences for oil development, but permits are sometimes granted outside the formal legal framework. Commentators mention the government's currently limited capacity to negotiate satisfactory extractive industry agreements or to enforce compliance.

Since 2000 the DRC government has enacted new legal codes for forestry and mining and a new Environment Law (2011), and a new Oil Code released in 2010 by the Ministry of Energy has been under discussion. The Oil Code has reportedly been passed by the Senate and is currently with the National Assembly. It contains revisions to the regulatory regime and recommends changes to future PSAs to avoiding weaknesses of deals already signed. Under the new code, disputes between the DRC government and foreign oil companies will be resolved not in DRC courts but by an international investment tribunal in Paris.

Further facts are available (in English) mainly from limited published details of specific PSAs signed prior to 2010. The DRC made its current PSAs with oil companies through the Ministry for Energy and Ministry for Finance. The agreements commit the companies to a preliminary environmental audit and mitigation plan for the exploration period, but environment impact assessments and management plans are not required until oil fields have been located and assessed and operations are shifting to production. And these provisions are said not to be integrated into a coherent legislative and regulatory framework.

Commentators have criticised the DRC's PSAs for an absence of enforceable environmental safeguards and of applicable fines for environmental damage to land and water resources. (Internationally, fines are widely recognised as crucial to preventing regular large oil spills.) 'Stabilisation clauses' in current PSAs with oil companies mean that when new legislation or regulations are introduced they will not apply to these earlier agreements.

The DRC is a candidate country for the Extractive Industries Transparency Initiative (EITI; see below). If the DRC government wishes to be accepted as compliant with the EITI's voluntary code it will be obliged to publish the revenues it receives from companies for oil production.

Under the existing PSAs, the oil companies must spend relatively small amounts of money each year during exploration and production on 'education, public health and culture' projects designed by the DRC Ministry of Energy.

### **Relevant international laws, standards and initiatives**

Among the main international laws, standards and initiatives applicable to the extraction of oil and other natural resources are these:

***Extractive Industries Transparency Initiative*** (EITI, <http://eiti.org>): a multistakeholder voluntary initiative involving governments, companies and civil society; companies and governments commit to disclose payments and revenues for oil, gas and mining and agree to independent verification.

***US Dodd-Frank Act 2010*** (Dodd-Frank Wall Street Reform and Consumer Protection Act, [www.sec.gov/about/laws/wallstreetreform-cpa.pdf](http://www.sec.gov/about/laws/wallstreetreform-cpa.pdf)): a US law, not yet in force, requiring all oil, gas and mining companies listed on US stock exchanges to disclose payments to governments of countries where they operate on a country-by-country basis; implementation is expected in 2011.

***European Union Accounting and Transparency Directives*** ([http://ec.europa.eu/internal\\_market/accounting/other\\_en.htm](http://ec.europa.eu/internal_market/accounting/other_en.htm)): proposed new EU laws, not yet in force, requiring all oil, gas, mining and forestry companies listed on EU stock exchanges or registered in the EU to disclose payments to governments of countries where they operate on a country-by-country basis; implementation is expected in 2011–12.

***UN 'Protect, Respect and Remedy' Framework and Guiding Principles on Business and Human Rights*** ([www.ohchr.org/documents/issues/business/A.HRC.17.31.pdf](http://www.ohchr.org/documents/issues/business/A.HRC.17.31.pdf)): a legal framework based on the state duty to protect against human rights abuses by third parties, including companies; companies' responsibility to respect human rights and avoid causing harm; and access by victims to effective remedy.

***Global Reporting Initiative*** (GRI, [www.globalreporting.org](http://www.globalreporting.org)): an international initiative that provides companies with a sustainability reporting framework, with specific reporting guidelines for the oil, gas and mining sectors.

***Natural Resource Charter*** ([www.naturalresourcecharter.org](http://www.naturalresourcecharter.org)): an independent set of principles for governments and civil society on how to best harness the opportunities created by natural resources for development.

***Equator Principles*** ([www.equator-principles.com](http://www.equator-principles.com)): a voluntary set of principles that recognise the responsibilities of the banking industry for the social and environmental impacts of large scale projects that banks and investors finance.

***Publish What You Pay*** ([www.publishwhatyoupay.org](http://www.publishwhatyoupay.org)): a global civil society coalition and campaign to hold governments and companies accountable for oil, gas and mining revenues and payments.

***Voluntary Principles on Security and Human Rights*** ([www.voluntaryprinciples.org](http://www.voluntaryprinciples.org)): a non-binding multistakeholder initiative to assist extractive industries in developing and implementing security and safety standards that ensure proper respect for human rights.

***United Nations Global Compact*** ([www.unglobalcompact.org](http://www.unglobalcompact.org)): an initiative bringing together UN agencies, companies, labour organisations and civil society to work towards businesses aligning operations and strategies with universally accepted principles of human rights, labour, environment and anti-corruption.

### **Actual and projected oil revenues**

Uganda's share of the oil around Lake Albert has been called Sub-Saharan Africa's largest onshore discovery in 20 years and estimated at 2 billion barrels or more of confirmed reserves. How much of the oil is realistically recoverable is estimated at between a low of about 1 bn barrels and a high of several billion. Uganda is expected to start production at a relatively low rate of 4,000 to 5,000 barrels per day (bpd) in 2013, rising to 125,000 bpd or more after five years.

Ugandan government revenue to date consists mainly of signature bonuses paid by oil companies when signing PSAs. These payments typically average about \$300,000 for each agreement. Once the oil starts to flow, the operating companies will pay production bonuses, such as the \$5 million that Dominion Petroleum is contracted to pay the government on the first day of oil production in its block.

As to future revenue, oil price volatility – ranging in recent years from about \$30 to \$140 per barrel – makes projections difficult. Current estimates are that oil exports could generate between \$2 bn and \$5 bn in annual revenue for Uganda for more than 20 years, doubling its current export earnings. (To put these figure in context, Nigeria, with about 30 bn barrels of proven reserves, has generated an average of about \$8.5 billion per year from oil production since 1970.) In Uganda this could mean about \$60 to \$150 per capita in annual revenue.

In many respects actual and projected oil revenues in the DRC are similar to those in Uganda. Estimates suggest there may be 2 bn barrels of oil reserves in the DRC's Lake Albert blocks, yielding 150,000 bpd or more per year at peak production levels and generating annual revenues in the low billions of dollars. (Currently the DRC earns several hundred million dollars per year from exporting oil from other parts of the country.)

Current revenues from the DRC's Lake Albert oil fields are mainly from signature bonuses paid by companies. These range from \$300,000 up to \$2 bn for single agreements (higher than in Uganda, apparently because the DRC deliberately renegotiated some contracts to secure more money up-front), with production bonus payments of up to \$5 million due per PSA when production begins.

Other factors besides the oil price will determine both countries' income from the oil. These include the development costs that the oil companies claim against income before each state can apply corporate tax to profits, and whether the DRC or Uganda participates in production via joint venture agreements, which will gain them a greater share of the revenue.

If the concerns of some NGOs are correct – that both countries’ current PSAs are over-generous in allowing the companies to make huge returns on capital invested and depriving the DRC and Uganda of a fair share of the revenue – neither country is likely to gain significant economic benefits from oil production, while environmental and social harms may be very considerable.

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### **Sources of maps**

Page 1: Initiative for Peacebuilding, 2010

Page 2: Platform, 2010