

## AFRICA RISK CONSULTING

### Uganda Monthly Briefing February 2017

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#### Uganda Summary 1 February 2017

**President Yoweri Museveni (1986-present) appoints his son Muhoozi Kainerugaba Museveni as senior presidential adviser. The appointment suggests President Museveni is looking to ensure family succession. United Kingdom (UK)-based Tullow Oil Plc agrees a \$900m farm down agreement with France-based Total E&P for Lake Albert Development Project. Parliament launches an investigation into government payments to officials linked to a tax dispute involving international oil companies. Members of the Democratic Republic of the Congo (DRC) anti-government Mouvement du 23-Mars (M23) group leave their camps in Uganda, amid increased insecurity in DRC.**

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#### Museveni appoints son as senior presidential adviser

President **Yoweri Museveni** (1986-present) on 9 January appointed his son **Muhoozi Kainerugaba Museveni** as senior presidential adviser for special operations.<sup>1</sup> The appointment of Muhoozi Museveni, currently a military officer, to a political office increases the possibility that Museveni is preparing for his son to eventually succeed him. Muhoozi Museveni is currently a major general in the **Uganda People's Defence Force (UPDF)**.<sup>2</sup> Muhoozi Museveni headed the **Special Forces Group (SFG)** that guards strategic infrastructure including **Uganda's** oil fields. Muhoozi Museveni's successor as head of the SFG is his deputy, **Don Nabaasa**, who was promoted to commander.<sup>3</sup>

Muhoozi Museveni's military advancement was meteoric and was driven by his father's position as commander-in-chief rather than his own capabilities.

*"He has little talent for military matters, having flunked courses at staff colleges in various countries, but was given passes to avoid embarrassment."*<sup>4</sup>

Alongside his military role, Muhoozi Museveni has reportedly used his political influence to build up sizeable hidden business interests.

*"Muhoozi Museveni is increasingly using businessmen as proxies. He holds hidden stakes in a significant number of **Kampala** real estate developments. He fears public scrutiny, but in reality the companies are his."*<sup>5</sup>

Ruling **National Resistance Movement (NRM)** sources have said that Muhoozi Museveni must first develop a civilian political and regional (**East African**) profile before he can become a credible candidate to succeed his father.<sup>6</sup> It was previously thought that President Museveni had put succession plans on the backburner to prioritise the ongoing constitutional review to remove the age limits that currently prevent him standing in 2021, However, Muhoozi Museveni's appointment suggests that he wants both processes to run in tandem.

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<sup>1</sup> New Vision, 9 Jan 2017.

<sup>2</sup> New Vision, 18 May 2016.

<sup>3</sup> New Vision, 18 May 2016.

<sup>4</sup> Source, former military attaché, Kampala

<sup>5</sup> Source, journalist, Kampala

<sup>6</sup> Source, former western diplomat, East Africa

*“One indication that Museveni is accelerating succession plans will be when Muhoozi Museveni swaps his military uniform for a suit.”<sup>7</sup>*

A move to usher in Muhoozi Museveni may cause political instability. President Museveni seemed to have abandoned ‘Project Muhoozi’, the planned removal or assassination of senior security and military figures opposed to a family succession, after controversy in 2013. The UPDF described the appointment as a normal change in command, but it appears part of a broader reshuffle to demote possible opponents to Muhoozi Museveni.<sup>8</sup> Notably, chief of defence forces general **Edward Katumba Wamala** became junior works and transport minister, in an apparent demotion.<sup>9</sup> His successor as chief of defence forces is former land forces commander **David Muhoozi**. However, even with the reshuffle, Muhoozi Museveni will still face significant challenges from the NRM ‘historicals’ who fought in the Bush War in the 1980s.

*“If Museveni were to move too early, he might trigger high-level defections from the ruling NRM as unsuccessful potential successors sought to further their careers with the opposition. In addition, the sources added that the promotion of younger NRM members – i.e. the same age as Muhoozi Museveni – to senior political roles, would be a part of the succession plan.”<sup>10</sup>*

President Museveni is placing family members in key positions, increasing the likelihood of a family succession, even if he decided that a Muhoozi succession would face too much opposition. Museveni’s half-brother, UPDF general **Caleb Akandwanaho** (a.k.a **Salim Saleh**) is an increasingly influential presidential adviser,<sup>11</sup> and first lady **Janet Museveni** is education minister. Observers have also noted the rise up the NRM ranks of presidential son-in-law **Odrek Rwabwogo**, a special presidential adviser on research and information.<sup>12</sup> Rwabwogo is married to **Patience Kokundeka Museveni Rwabwogo**, who is popular with Uganda’s politically influential conservative constituency through her role as a pastor in the **Covenant Nations Church**, a born-again Pentecostal denomination.<sup>13</sup> Observers have warned that a family succession will destabilise Uganda:

*“Not even the boy [Muhoozi Museveni] with his links to the military could ensure stability. Any Museveni family member would create chaos.”<sup>14</sup>*

Uganda and the NRM now enter a period of increased political uncertainty. For Museveni, amending the constitution and ushering in his chosen successor will both require the backing of senior NRM officials who will demand concessions if they are to defer their own political ambitions and support Museveni remaining in office until his succession by a family member.

## **Tullow reaches farm down agreement with Total**

**United Kingdom (UK)-based Tullow Oil Plc** announced on 9 January that it had agreed a \$900m farm down agreement with **France-based Total E&P** subsidiary **Total E&P Uganda BV** effective 1 January.<sup>15</sup> Despite concerns about infrastructure delays and commercial viability amid the low oil price environment, Total’s purchase is indicative of investor confidence in the Ugandan oil sector. Under the agreement, Tullow will transfer 21.6% of its 33.3% interests in **Exploration Areas (EA) 1, 1A, 2 and 3A of the Lake Albert Development Project**.<sup>16</sup> Total is already operator of EA1 and EA1A and will now assume operatorship of EA2. Tullow has ceded its operatorships in Uganda, but will

<sup>7</sup> Source, former western diplomat, East Africa

<sup>8</sup> New Vision, 9 Jan 2017.

<sup>9</sup> New Vision, 9 Jan 2017.

<sup>10</sup> Source, former western diplomat, East Africa

<sup>11</sup> Source, journalist, Kampala

<sup>12</sup> Africa Confidential, 20 Jan 2017.

<sup>13</sup> Africa Confidential, 20 Jan 2017.

<sup>14</sup> Source, journalist, Kampala

<sup>15</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

<sup>16</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

retain an 11.8% interest in the exploration areas and export pipeline.<sup>17</sup> This will decrease to 10% when the government exercises its right to back-in.<sup>18</sup> Some observers have warned that having fewer oil companies with larger stakes in the Lake Albert Development Project will prove detrimental to the government:

*“The sale of the assets of Tullow Oil to Total is going to impact on Uganda negatively by slowing down the development in the oil industry. Uganda is going to lose out on revenue because as a country it has been collecting taxes from Tullow in excess of \$100m annually. In the oil industry there’s what we call vertical integration where companies use each other as a proxy company in order to strengthen their bargaining power with governments. These are effective cartels that deprive local governments a chance of striking a good deal in their oil agreements. The sale of Tullow to Total is also going to cause unemployment as several local workers are bound to be sacked by the new managers. Generally speaking, the more the participants, the more vibrant the industry so this transaction is bad news for Uganda.”<sup>19</sup>*

Tullow, which has faced cash-flow issues due to the low price environment, will welcome the cash-injection. The structure of the transaction is: \$200m in cash consisting of \$100m on completion of the transaction and \$50m at both final investment decision and first oil; and \$700m in deferred consideration which Tullow will use to fund its share of the cost of upstream development and the export pipeline.<sup>20</sup> Tullow said it expects to record a pre-tax write-off of \$400m in 2016 as a result of the deal.<sup>21</sup> Tullow has, since the start of 2016, “quietly”<sup>22</sup> retrenched its Ugandan workforce and this, alongside the farm down, may presage a complete withdrawal from Uganda.

*“I think Tullow will eventually pull out of Uganda. Remember, they get money from the farm down and already have lots of money in recoverable costs, meaning as things are they will still walk away with profits; meanwhile Total will eventually take over much of the Lake Albert Development because it makes business sense for it, being among the **Big Five** oil companies; remember at current global prices of about \$50 per barrel it is only Total which would make profits from the oil.”<sup>23</sup>*

This resulted in some political opposition to the farm down agreement, which the government still needs to approve.

*“It’s going to bring monopoly and this will leave us at the mercy of Total. When the companies are many, the government has a better bargaining power but when it’s only one, then it gets a bad deal. It may only be good for the purpose of centralising resources since our oil reserves are not that much but politically it’s not good at all. Dealing with one company will not be easy as they are likely to have a high bargaining power over government since they will now be monopolists in the oil industry.”<sup>24</sup>*

The Lake Albert Development Project will produce approximately 230,000 barrels per day (bpd) at its peak. Tullow said it expects production of the first 1.2 billion barrels of oil to require \$5.2 billion of upstream capital expenditure, with \$3 billion required to reach first oil approximately three years after a final investment decision, expected in 2017.<sup>25</sup>

<sup>17</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

<sup>18</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

<sup>19</sup> Source, oil and gas sector expert, Kampala

<sup>20</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

<sup>21</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

<sup>22</sup> Source, oil sector analyst, Kampala

<sup>23</sup> Source, policy analyst, Kampala

<sup>24</sup> Source, member of parliament, Kampala

<sup>25</sup> London Stock Exchange Aggregated Regulatory News Service, 9 Jan 2017.

The farm down comes amid scrutiny of government payments to officials linked to a tax dispute involving Tullow. While the issue is not related to the deal and will not threaten to derail it, it highlights the political challenges that international oil companies continue to face in Uganda. Parliament on 18 January agreed to investigate 6 billion Ugandan shillings (US\$) (\$1.6m) payments that Museveni made to government officials.<sup>26</sup> The payments highlight Museveni's direct role in oil sector decision making, often circumventing energy minister **Irene Muloni**. Museveni reportedly approved the payments in a meeting with **Uganda Revenue Authority (URA)** commissioner general **Doris Akol** in May 2015.<sup>27</sup> The recipients were officials involved in the government's case against UK-based **Heritage Oil Ltd** in front of the **United Nations Commission on International Trade Law (UNCITRAL)** in **London (UK)** (see below).<sup>28</sup> The recipients were reportedly from the URA, the attorney general's office, and the justice, finance and energy ministries.<sup>29</sup> The recipients reportedly include:<sup>30</sup>

- **Allen Kagina**, former URA commissioner general;
- Doris Akol;
- **Kampala Capital City Authority (KCCA)** executive director **Jennifer Musisi**;
- **Peter Nyombi**, former attorney general;
- **Fred Ruhindi**, former deputy attorney general;
- **Keith Muhakanizi**, secretary to the treasury.

The government has defended the payments as bonuses that constitutionally the president has the prerogative to award.<sup>31</sup> Critics, however, allege that the payments breach the **Public Finance Management Act 2015**.<sup>32</sup>

The parliamentary committee will investigate the circumstances of the payment, the beneficiaries, and the use of funds the government received from court cases against international oil companies.<sup>33</sup> On 10 January, deputy chief justice **Steven Kavuma** ruled that parliament could not investigate the payments.<sup>34</sup> However, parliamentary speaker **Rebecca Kadaga** suspended parliamentary activity – including discussions of the 2017/2018 budget and the planned capitalisation of the **Uganda Development Bank** – until the government appealed the ruling.<sup>35</sup> Museveni's appearance before parliament suggests that Kadaga's strategy worked.

The government claimed before domestic tribunals and courts, and eventually UK courts, that Heritage Oil owed it capital gains tax from the \$1.5 billion sale of Blocks 1 and 3A to UK-based Tullow Oil Plc in July 2010.<sup>36</sup> The government demanded Tullow settle the disputed capital gains tax bill or face non-renewal of its exploration licence. In April 2011, Tullow opted to pay the government \$121m, before paying the \$313m outstanding balance. Tullow sued Heritage and, in June 2013, the courts awarded it the remaining \$313m.<sup>37</sup> In February 2015, the UNCITRAL ruled against Heritage Oil, and that the URA was right to demand capital gains tax on the sale of the assets.<sup>38</sup>

The deal will increase momentum behind the development of Lake Albert. Tullow is now in a position to finance its outstanding capital contributions. Total, an increasingly important upstream and

<sup>26</sup> The Independent, 19 Jan 2017.

<sup>27</sup> Daily Monitor, 17 Jan 2017.

<sup>28</sup> Daily Monitor, 17 Jan 2017.

<sup>29</sup> Daily Monitor, 17 Jan 2017.

<sup>30</sup> The Independent, 19 Jan 2017.

<sup>31</sup> East African, 11 Jan 2017.

<sup>32</sup> East African, 11 Jan 2017.

<sup>33</sup> Daily Monitor, 17 Jan 2017.

<sup>34</sup> Daily Monitor, 10 Jan 2017.

<sup>35</sup> Daily Monitor, 10 Jan 2017.

<sup>36</sup> Daily Monitor, 17 Jan 2017.

<sup>37</sup> www.telegraph.co.uk

<sup>38</sup> Daily Monitor, 26 Feb 2015.

downstream player in Uganda, has the financial and political clout to drive the project towards commercial development. The deal therefore increases the likelihood of a final investment decision before the end of the year. Nevertheless, hurdles remain. Securing \$5 billion in a low oil price environment may prove challenging. Tullow, Total and upstream partner **China National Offshore Oil Corp** still need to agree on an investment strategy and complete the requisite land acquisitions.

### **M23 former combatants leave Uganda camps**

The government on 19 January acknowledged that members of the **Democratic Republic of the Congo (DRC)** anti-government **Mouvement du 23-Mars (M23)** group have departed from their camps in Uganda.<sup>39</sup> Increased M23 activity will lead to a deterioration in the security situation in the DRC increasing the risk of spillover into western Uganda. The Ugandan government has hosted approximately 400 M23 rebels at the **Bihanga** military camp (**Ibanda District**) since their military defeat in the DRC in 2014. The DRC government on 15 January alleged that 200 former M23 combatants had crossed the border and occupied a village in **North Kivu Province**, and blamed Uganda for allowing the attack to take place.<sup>40</sup> The Ugandan government originally denied that any former M23 combatants were missing.<sup>41</sup> However, it eventually admitted that it did not know the location of 40 former M23 combatants, while security forces had detained another 100 in **Mbarara District** attempting to cross the border.<sup>42</sup> It is unclear if M23 leader **Sultani Makenga** is missing. The mainly ethnic **Tutsi** M23 emerged from a 2012 military mutiny and held territory, including North Kivu capital **Goma**, in eastern DRC. During the M23 insurrection, the DRC government accused both Uganda and **Rwanda** of backing the group.<sup>43</sup> Following their military defeat in 2013, the Ugandan government agreed with the DRC government to host the former combatants until agreement is reached on an amnesty and eventual repatriation.<sup>44</sup> The accord has, however, stalled with few of its provisions implemented.<sup>45</sup>

The security situation in the eastern DRC is likely to remain poor amid wider political uncertainty as president **Joseph Kabila** (2001-present) looks to remain in office ahead of elections before the end of the year. The DRC government will probably continue to blame Uganda for M23 activity to detract blame from its own failings. While this will increase bilateral tensions, conflict is unlikely, with both governments having more pressing domestic concerns.

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<sup>39</sup> Daily Monitor, 19 Jan 2017.

<sup>40</sup> Daily Monitor, 19 Jan 2017.

<sup>41</sup> Daily Monitor, 19 Jan 2017.

<sup>42</sup> Daily Monitor, 19 Jan 2017.

<sup>43</sup> Daily Monitor, 19 Jan 2017.

<sup>44</sup> Daily Monitor, 19 Jan 2017.

<sup>45</sup> Daily Monitor, 19 Jan 2017.

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