

## THE REGULATION OF THE OIL AND GAS UPSTREAM SECTOR IN TANZANIA: A THEMATIC REVIEW OF THE PETROLEUM ACT 2015

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### Abstract

*This article reviews the regulation of upstream sector in the Tanzanian petroleum industry in the wake of the regulatory changes. For the first time, Tanzania has enacted a comprehensive piece of legislation, the Petroleum Act, 2015, to cater for its oil and gas sector in a comprehensive manner. The new law repeals two previous legislations relating to petroleum, viz; The Petroleum (Exploration and Production) Act, and the Petroleum Act. This article reviews some aspects of the upstream industry as enacted in the new law. The main argument advanced is that with the new law, the petroleum industry in Tanzania is no more business as usual as the rules of the game have substantially been modified. This is virtually in most crucial aspects from ownership of resources; government's participation; the fiscal regime and local content. In all the reviewed aspects the author concludes that the Petroleum Act, 2015 is expected to impact substantially future engagement of oil companies investing in Tanzania.*

**Key Words:** Regulation, Fiscal regime, Ring fencing

### 1.0 Introduction

This article looks at some of rules relating to upstream activities in the Tanzanian petroleum sector. The rules discussed in this paper are those contained in the Tanzania Petroleum Act, 2015. This is a major piece of legislation providing for a comprehensive regulatory framework for the Tanzanian petroleum sector. It is intended in this paper to thematically look at some provisions governing the upstream activities with specific discussion on petroleum rights and conditions; surrender, cancellation and transfer of licenses; the petroleum fiscal regime; ring fencing; the Government participation, local content, corporate social responsibility and the question of integrity pledge. It is anticipated that the midstream and downstream activities will form a subject of a separate paper, and, the question of environmental standards and decommissioning deserves a complete treatise. The major argument espoused in this paper is that the coming into operation of the new law greatly changes the rules of the game which substantially impacts the investment climate in the Tanzania's oil and gas sector.

### 2.0 Petroleum Rights and Conditions

The power to grant petroleum rights is vested with the Minister responsible for Energy and Minerals, in whose exercise, the Minister is duty bound to take into consideration the advice of the Petroleum Upstream Regulatory Authority, known by its abbreviation as PURA.<sup>44</sup> The exclusive rights in respect of petroleum operations are to be granted only to the National Oil Company, the NOC, in this case, the Tanzania Petroleum Development Corporation (TPDC), which shall have exclusive rights granted under the

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<sup>44</sup> The Petroleum Act, 2015, Act No. 21 of 2015, section 44 (1) and (2).

new law, and such licence shall not be transferrable to any other person.<sup>45</sup> However, the NOC may, subject to the Minister's consent and on advice by PURA enter into partnership with a Tanzanian or a foreign entity through an open tendering process or a direct award of a block.<sup>46</sup> The licence granted shall require the NOC to maintain a participating interest of not less 25%.<sup>47</sup> A company wishing to carry out petroleum operations in Tanzania outside the scope of a reconnaissance permit is required to do so together with the NOC.<sup>48</sup>

The above paragraph informs the International Oil Companies (IOCs) that with the operationalization of the new law, petroleum operations in Tanzania are no longer business as usual. The author's understanding of the provisions referred to in the previous immediate paragraph, is that all petroleum rights shall be granted to the NOC; and IOCs or Tanzanian entities wishing to engage in petroleum operations, besides reconnaissance operations, will have to do that in partnership or through the NOC. It is also clear that, in any arrangement, the licence will require the NOC to maintain at least 25% participating interest. The minimum 25% participating interest substantially departs from the previous regime where participation interest was subject to negotiations, and in most cases, TPDC's participation interest in the actual PSAs is limited to 15%, except in one PSA where the participation interest hits 20%.<sup>49</sup> Therefore, ownership of blocks will rest with the NOC as licensee, and other stakeholders may undertake petroleum operations only together with the NOC. These may be in the form of a PSA where the NOC besides the production share, will have to maintain not less than 25% participating interest;<sup>50</sup> it may also be through joint venture agreements in which the NOC should maintain a participating interest of not less than 25%; or it may be through partnership.<sup>51</sup>

The arrangement, it could be argued is reflective of nationalistic tendency of ownership of petroleum resources and the need to improve transparency. This is because the ownership of petroleum rights rests with the NOC and the Minister shall not enter into an agreement without prior approval of the Cabinet. Here, one should note that the Cabinet will benefit dearly from the Oil and Gas Advisory Bureau established under section 7. Thus, in addition to the production share, the NOC will be entitled under the arrangement, to a participating interest of not less than 25%, and these together, in addition to other taxes and royalties payable, is what is known as the government take in the petroleum industry. That is a great achievement from a theoretical point of view. However, the author is inclined to note that, that is not the end of the story. The question would be; does the TPDC, the Tanzanian NOC has enough resources and capital necessary to maintain a participating interest of not less than 25%?

45 *Ibid*, section 44 (1), (2) (3).

46 *Ibid*, section 44 (4).

47 *Ibid*, section 44 (5).

48 *Ibid*, section 44 (6).

49 The author is aware of the terms in the signed PSAs, however, is not in a position to provide the details of the PSAs and the participation interest in each due to the perceived confidentiality requirements.

50 It is the responsibility of PURA to develop and submit to the Minister a Model of PSA or any other Model agreement to be approved by Cabinet under section 47 (3).

51 The Petroleum Act, 2015, Act No. 21 of 2015, section 45 provides for persons who may partner with the NOC.

At this juncture, it may be useful that some few things be briefly clarified. The new law takes the approach that no foreign proprietorship of the petroleum resource, IOCs may act as a contractor to the NOC. This has been the practice in Libya, Indonesia, Egypt and Algeria to mention a few. But also, the new law provides for NOC's participation interest of not less than 25%. This implies that the NOC is required by law to directly participate in all the petroleum contracts as a co-contractor.<sup>52</sup> That would mean that, the NOC is to co-invest in exploration, development and production activities together with the IOC. Here, the NOC will have two capacities; one as the owner of the oil and gas resources and two, as an investor. Three questions arise with respect to State participation interest in the upstream industry; First, the percentage of participation by the NOC; Second, when does the NOC begin to participate; and third, what costs of the project will the NOC bear?

It is noted here with respect to the first question that, the law puts 25% as the minimum NOC participating interest. Therefore, it appears that the actual NOC participation interest will be agreed by the contractor. Of course some countries have a participating interest of as high as 50% (Brunei and Tunisia) or 60% (Abu Dhabi). Thus the minimum 25% should not be seen as on the high side if one compares with that of Belize of 5% or Indonesia of 10%. The question of when does the NOC begin to participate is also expected to be agreed in the agreement. It may be from the start of the contract. The challenge here will be the NOC's ability to pay its share of costs, and the willingness to assume the exploration risks that the activity may not be successful. It should be appreciated that, it is not a good idea for a State to take such exploratory risks, particularly for a developing country like Tanzania. This challenge may be addressed by providing for an option to participate in the project, and triggering that option at a point when some or all exploration risks are eliminated; such as upon declaration of commerciality or upon approval of the development plan.

The question of the NOC's ability to pay for its share is answered by the third question and there are three alternatives that can be provided. One, 'fully paid equity' participation as in Norway, in which the NOC bears its share of all costs in full; two, 'partial carried interest' in which, the IOC bears/carries all of the costs incurred prior to the NOC election to participate, but following election to participate there is a repayment of some or all the NOC's share of the costs incurred before the election to participate, as in Indonesia; and three, 'full carried interest' in which the IOC bears/carries all of the costs incurred prior to NOC election to participate and there is no repayment of the NOC's share of the costs incurred before election to participate, as in Cameron, Chad, and Uganda which has recently moved from a 'partial carried interest' to 'full carried interest'. The last alternative has been also referred to as a "hard" or sometimes "free" carry. In virtually all existing Production Sharing Agreements (PSAs) in Tanzania, the NOC's participation interest is full carried interest, in which case, TPDC bears costs only subsequent to the exercise of

<sup>52</sup> Under the previous regime where participation interest was a subject of negotiation, the NOC had the option to either participate or not.

the option to participate. This aspect will have great bearing on other terms of the agreement depending on, at what time the NOC elects to participate. For example a full carried interest may motivate IOC/contractor to demand a higher percentage of cost oil, or even a production share.

It would be concluded on this aspect that much as the law appears to favour the interests of the country, the same may not work in practice. Some provisions of the agreements will inevitably be aligned to take care of the legislated conditions or else the country is doomed to be less competitive. IOCs do not have idle money to invest in a less profitable venture, yet mostly risky. These observations, however, should not be understood to encourage negotiators to blindly let the negotiable terms defeat the spirit of the new law.

## 2.1 Surrender, Cancellation and Suspension of Licences, Transfers and Registration of Records

The aspects listed under this heading are also relevant when looking at changes in the rules of the game as their provisioning imply the notion of no business as usual. It is proposed to start with surrender of licence, which the licence holder is entitled to. The Minister will issue a certificate of surrender; however, the application must be made not less than ninety days before the date on which the contractor wishes to surrender.<sup>53</sup> It is noted that the Minister shall not issue a certificate of surrender to an applicant who is, *inter alia*, in default or where decommissioning is not complete.<sup>54</sup> Surrender may be in respect of all blocks or part of the blocks.<sup>55</sup> In order to ensure transparency and efficiency, the Minister will exercise the powers of issuance of certificate of surrender only upon the advice of PURA.<sup>56</sup>

Suspension or cancellation of licence is another critical area addressed by the new law. The Minister is empowered, upon consultation with PURA and by notice in writing served upon the licence holder to suspend or cancel the licence if the licence holder is in default. The provisions of section 83 (2) seeks to take care of the rules of natural justice before the licence is cancelled or suspended. Of interest here are the events triggering cancellation or suspension. One of such event is where the licence holder enters into any agreement or scheme of composition with his creditors or takes advantage of any law for the benefit of the debtors.<sup>57</sup> It appears the saying '*once beaten, twice shy*' has impacted the drafting of the provision. It is thought here that the experiences in *Standard Chartered Bank (Hong Kong) Limited v. Tanzania Electric Supply Company Limited*<sup>58</sup> (herein after referred to as "*SCB (Hong Kong) Limited*") has an influence in this. It may be recalled that in the *SCB (Hong Kong) Limited*, there was a debt restructuring arrangement entered into between Mechmar, purporting to act in Independent Power Tanzania Limited (IPTL) behalf, according to which SCB Hong Kong held all of IPTL's right, title and interest in and to the assigned

<sup>53</sup> The Petroleum Act, 2015, Act No. 21 of 2015, section 81 (1).

<sup>54</sup> *Ibid*, see also section 81 (5) for the reasons for which the Minister shall not issue a certificate of surrender.

<sup>55</sup> *Ibid*, See section 82 on the effects of certificate of surrender.

<sup>56</sup> *Ibid*, see section 81 (4).

<sup>57</sup> *Ibid*, section 83 (4) (a).

<sup>58</sup> ICSID Case No. ARB/10/20.

Power Purchase Agreement (PPA), including all moneys which would at any time be or become payable to the borrower. Such an arrangement, in my opinion, if entered under the new law, would entitle the Minister to cancel the licence.

The second triggering event is where an order is made or a resolution is passed of winding up the affairs of the company or corporation unless the winding up is for purpose of amalgamation and the Minister has consented to the amalgamation, or is for the reconstruction and the Minister has been given notice of the reconstruction.<sup>59</sup> Again, the IPTL saga might have some contribution in this. The legal battles both in Courts of Tanzania, the International Centre for the Settlement of Investment Disputes (ICSID) arbitrations and others involving IPTL are well documented.<sup>60</sup> In Tanzania, there had been a series of winding up petitions relating to IPTL as far back as from 2002, and at one point the High Court of Tanzania issued a winding up order, which, due to procedural irregularities the Court of Appeal reversed the decision. Nevertheless, it suffices to say that a winding up order or a resolution for winding up the affairs of the company is a perfect event for cancellation of a licence under the new law.

Transfer and registration of records is another important aspect the new law addresses. The law requires PURA to establish and maintain a registry of petroleum agreements, licences, permit authorizations and any change in interests of an existing petroleum agreement, permit or licence.<sup>61</sup> Of interest is that the petroleum registry should contain a record of any court decision including arbitration, award, deeds or instruments related to the licence, and these shall be public except as otherwise provided by law.<sup>62</sup> This is a new dimension towards transparency in the petroleum industry. In this regard, it is expected that even PSAs, licences and permits will henceforth be public records. The long held notion of confidentiality in petroleum agreements will not survive the operationalization of the new law. It is not taken that section 91 is a provision prohibiting a person's access to such agreements, but rather deals with making them available to the public. The rules of the game have changed, it is a movement towards transparency in the extractive industry and this is a good move for Tanzania to implement the Extractive Industries Transparency Initiatives (EITI).

All above stated is not the end of the story as far as transfer of interests is concerned. The law requires any legal or equitable interest in, or affecting a licence to be by way instrument in writing for it to be capable of being created, transferred, assigned, effected or dealt with.<sup>63</sup> Such a transfer must be approved by the Minister, in which case, lack of Minister's approval

<sup>59</sup> *Ibid*, section 83 (4) (b).

<sup>60</sup> See the award in *Standard Chartered Bank (Hong Kong) Limited v. Tanzania Electric Supply Company Limited*, ICSID Case No. ARB/10/20; where the Tribunal makes a brief historical review to cases involving IPTL both in Tanzania and outside Tanzania.

<sup>61</sup> The Petroleum Act, 2015, Act No. 21 of 2015, section 84 (1).

<sup>62</sup> *Ibid*, section 84 (5) & (6).

<sup>63</sup> *Ibid*, section 85 (1).

renders such transfer of interest of no effect.<sup>64</sup> An application for approval is required to be accompanied with, *inter alia*, transfer agreement; certificate of incorporation or compliance by the transferee; certificate of tax clearance from the Tanzania Revenue Authority; and an integrity pledge by the transferee.<sup>65</sup> These requirements are going to hit hard IOCs that had been engaging in an unethical transfer of interests prejudicial to the interests of Tanzania. A range of such practices have been applied for quite sometimes like offshore acquisitions in the name of tax planning. With the new law, IOCs will have to think twice before entering into such arrangements. Such arrangements necessitated the amendment of section 90 of the Income Tax Act, 2004. That notwithstanding, multinationals would always find novel ways to transfer interests. With the new law in the petroleum sector, which requires the contractors to sign an integrity pledge breach of which is the breach of the agreement, coupled with restrictions on transfer of interests, have changed the rules of the game where ethical business practices will guarantee smooth investment in the country. Investors should be keen to seek professional advice prior to engaging into practices that might be interpreted as prejudicial to the interests of Tanzania. A legal and tax audit for IOCs into their affairs would be a welcome move under the changed regulatory regime.

It should be noted that the Minister will exercise the powers to approve such a transfer after consulting PURA. And also the NOC has the right of first refusal to acquire the participating interest that a member of contractor part intends to assign to a non-affiliate.<sup>66</sup> Of interest is also section 86 (8) which provides that for the purposes of subsection (1) (a) "transfer of an interest in a licence" includes a transfer of an interest in a licence by operation of law. This is because, it is thought here, that the drafters might had in mind the novel arguments raised by the claimants in *Standard Chartered Bank (Hong Kong) Limited v. Tanzania Electric Supply Company Limited*<sup>67</sup> with respect to statutory assignments which were held to require the joining of the assignor as a claimant. The issue arose as TANESCO queried the propriety of SCB Hong Kong suing in its capacity as assignee of rights. The points raised in that case, are suggested to have been taken care of by section 85 (1), 86 (1) and the interpretation provided for under section 86 (8). It would be submitted that the combined effects of section 90 of the Income Tax Act, 2004 and the new law, will be helpful in protecting the Government's revenues lost through transfer of interests in the petroleum sector. This involves protected capital gains tax and stamp duties that will arise from transfer of interests in licences irrespective of where the transfer takes place.

## 2.2 Petroleum Fiscal Regime

It is noted on the outset that a number of provisions that used to be provided for in the PSA are now legislated conditions, giving no room for uncalled variations. The question of royalty is now legislated and does no longer fall within the realm of negotiable provisions. Section 113 is clear on payment of

64 *Ibid*, section 86 (1).

65 *Ibid*, section 86 (2).

66 *Ibid*, section 86 (4) & (7).

67 *Supra*.

royalty and the rate is stipulated in the second schedule to the Act as being 12.5% for onshore/shelf areas and 7.55 for offshore areas.<sup>68</sup> It is important to note here that royalty is payable by both the licence holder and the contractor in respect of the gross volume on petroleum recovered at the delivery point of total crude oil/natural gas production prior to cost oil and or cost gas recovery at such royalty.<sup>69</sup> This provision is commendable from the Government's point of view as the 12.5% or 7.5% is calculated before a reduction of the cost oil. However, from an investor perspective, the provision does not address the concerns of investors. In this regard, Tanzania is likely to lose its competitive edge in terms of attracting potential investors in the oil and gas sector.

A brief clarification on cost oil/cost gas is to be made at this juncture that would shade some light specifically on cost recovery and production share mechanisms that are included in a PSA. Cost oil or cost gas is simply the share of production that the contractor will receive for recovery of the costs it has incurred, which in most cases is subject to a maximum amount (the cost oil/gas limit). The Tanzanian Model PSA of 2013 puts the cost oil limit at 50%. Demonstratively, if for instance, the annual quantity of oil production is 100,000 barrels; 50,000 barrels will go to the contractor as cost oil for recovery of costs incurred. The remaining 50,000 barrels will be shared by the contractor and the NOC depending on the agreed production share. If the share is 70% for the NOC and 30% for the IOC, then the NOC will get 35,000 barrels whereas the contractor will get the remaining 15,000 barrels. Both the NOC and IOC will be required to pay royalty from their share not after the deduction of cost oil/gas, but prior to. That means, assuming the 70% to 30% share, the NOC will pay for onshore production 12.5% of 70,000 barrels and the IOC will pay 12.5 of 30,000 barrel in royalty.

Besides royalty, the contractor shall be required to pay the NOC annual fees in respect of a licence. The amount shall be prescribed in the regulations which shall include the acreage rental, training and research fees.<sup>70</sup> In addition, the contractor is required to make bonus payments.<sup>71</sup> However, bonus payment that the contractor shall be required to pay is of two types; one is signature bonus payable by the contractor to the Government upon signing of the agreement. This is a single non-recoverable lump sum payment; and two, is production bonuses which according to the new law is bonus payable on the commencement of production.<sup>72</sup> It is noted that the definition of a production bonus reflects what is stipulated in the Model PSA, 2013.<sup>73</sup>

It would be argued that a non-restrictive definition of production bonus would be ideal, so as to provide production bonuses upon achieving a certain quantity of cumulative production. A good example is the Libyan Exploration and Production Sharing Agreement where an amount of US \$ 1mil is paid

<sup>68</sup> *Ibid*, section 113 (1) read together with the Second Schedule.

<sup>69</sup> *Ibid*.

<sup>70</sup> *Ibid*, section 114 (1) & (2).

<sup>71</sup> *Ibid*, section 115 (1) & (2).

<sup>72</sup> *Ibid*, see section 115.

<sup>73</sup> See Article 11 of the 2013 Model PSA.

in respect of each commercial discovery as production bonus within 30 days after commercial production start date; and an amount of US \$ 5mil is payable as production bonus upon achieving cumulative production of one hundred million Barrels of oil equivalent from each commercial discovery and thereafter an amount of US \$ 3mil upon achieving each additional thirty million barrels of oil equivalent. It is my humble view that the definition of production bonus need be reconsidered. It would be proposed here that a production bonus to be a payment made at a certain point in time during the life of the petroleum contract which may occur at the time a commercial discovery is declared, at the time that petroleum production begins, at a defined production rate or quantity of cumulative production. The quantity, or rate or time would be left to be provided for in the Model PSA and subject to negotiations.

The other fiscal issues is the payment of taxes whereby all the licence holder, contractor and subcontractor are required to pay taxes including corporate tax, capital gain tax and other taxes applicable in Tanzania under the relevant laws.<sup>74</sup> The profits resulting from any direct or indirect assignment transfer or any other disposal of rights under the petroleum agreement regardless of the beneficiary type of transaction shall be subject to taxes at rates prescribed in the relevant laws.<sup>75</sup> This issue has been addressed when discussing transfer of rights. Of interest here is that the petroleum agreement should provide for financing of the petroleum activities with a loan from a third party that shall be considered as a subcontractor and be subject to withholding tax on the interest payment on loans.<sup>76</sup> The percentage of the loan shall be approved by PURA and any cost of any unapproved loans shall not be treated as allowable or deductible for tax purposes, and the interest rate for loans shall not exceed the lowest market interest rate available for such loans.<sup>77</sup>

A quick observation here; while it is appreciated that the intention of the provisions on loans aim at controlling thin capitalization on financing the petroleum activities as well as transfer pricing with respect to interest rates, it is not understood by the author as to why is it mandatory that the agreement should provide for financing of the petroleum activities by a third party. Is it assumed that the contractor will always not have cash at hand to finance the petroleum activities? If that is the assumption, then, it would be disagreeable if that is always the case. It is thought, it would be enough to provide such a requirement when the contractor intends to borrow from a third party not necessarily every agreement should provide for financing with a loan from a third party. The author understands the issues that arose in *Standard Chartered Bank (Hong Kong) Limited v. Tanzania Electric Supply Company Limited*<sup>78</sup> with respect to IPTL's loan restructuring and the question of default by IPTL to inject the 30% equity contribution. Besides this requirement, this paper notes the new law though fairly attuned, may be rendered ineffective by the Tanzanian

74 *Ibid*, see section 116 (1).

75 *Ibid*, section 116 (2).

76 *Ibid*, section 116 (3) & (4).

77 *Ibid*, section 116 (5), (6) & (7).

78 *Supra*.

ineffective tax system. One should not read the new law and start celebrating without having a broader view of the tax system. This is so because the new law clearly states that such taxes will be paid as provided for under relevant laws.

### **2.3 Ring Fencing**

Ring fencing allows the tax regime to look at the activities within the ring fenced area as a separate and independent tax unit, so that other gains, losses or costs outside the ring fenced area are excluded. This is well addressed under the provisions of section 117 of the new law. This is not new in Tanzania as the same is applicable to mining sector as introduced in the Income Tax Act, 2004 by the Finance Act 2010.<sup>79</sup> However, one should note that the Finance Act 2016<sup>80</sup> introduces substantial changes in relation to a ring-fencing regime in the petroleum and mining sector. The changes include providing for ring-fencing at a well level; licence level, upstream, midstream and downstream level. Investors are thus called upon to seek in advance a professional advice on how the new ring-fencing will impact their existing PSAs.

Investors have always raised concerns over ring fencing, in that, ring-fencing discourages re-investment into exploration activities. However, the current author fully supports ring fencing in natural resources. The basis of ring fencing is the fact that oil and gas are finite resources, and thus for a country to benefit from such resources, it makes sense to limit production in one area, not be used to finance exploration in another area. Similarly, if ring-fencing is not provided for, investors should be ready to accept low rate of return, as in case, an exploration risk in one block will be compensated by a discovery in another block. In the absence of ring-fencing provisions, the contribution of natural resources in the national economy may not match with what has been discovered. However, notwithstanding the fact the author supports ring-fencing in natural resources, the ring-fencing regime as introduced by the Finance Act 2016 is extremely stringent and there is a dire need to be revisited before potential investors divert their capital to other countries.

## **2.4 Government Participation, Local Content, Corporate Social Responsibility and Integrity Pledge**

### **2.4.1 Government Participation**

According to section 218 (1), the Government 'may' through the NOC participate in petroleum operations through a specified participating interest of a licence or contract granted under the Act and in a joint venture established by a joint venture operating agreement. It is the responsibility of the Minister to specify the maximum Government shares when announcing areas for granting of petroleum exploration licences and development licences.<sup>81</sup> The revenue resulting from participation interest belongs to the Government and

<sup>79</sup> *Ibid*, section 13.

<sup>80</sup> The Finance Act 2016, Act No. 2 of 2016.

<sup>81</sup> *Op cit*, section 218 (2).

the expenses incurred in relation to management of the participating interests shall be recovered by appropriation from the Government.<sup>82</sup>

It is important to make some observations here. While section 218 (1) provides that the Government may participate in petroleum operations, it was noted elsewhere that section 44 (5) is categorical in that the licence under the Act shall require the NOC to maintain a participating interest of not less than 25%. That notwithstanding, the proper interpretation would be that maintaining a participation interest is not an option and the Minister cannot grant a licence without providing for the maximum Government's participating interest.<sup>83</sup> Also the question of operating expenses, investments and other expenditure incurred in relation to the management of the participation interests to be covered by appropriation from the Government, may pose challenges. It was noted earlier that for a poor country like Tanzania, it is not wise to participate in the exploration stages. And it was suggested that the NOC should be given an option to participate upon declaration of commercial discovery and wherever possible the exploration expenses should be full carried over interest. It is undisputable that the Government does not have the financial muscles to invest in risky explorations. However, as far as contractors are concerned, they should note that under the new law, there must be a Government participation interest of not less than 25%. This requirement may serve as a weapon for IOCs to demand favourable terms in other negotiable aspects of the agreement especially if things turn out that the Government does not have the financial resources to participate during the exploratory stages.

#### **2.4.2 Local Content**

The local content requirements under the new law display a significant change of the rules of the game. To the country and its people, it should be a cause for celebration as the requirements sufficiently address the people's concerns. One of such requirements is that a licence holder, contractor or subcontractor is required to give preference to goods which are produced or available in Tanzania and services which are rendered by Tanzanian citizens and or local companies.<sup>84</sup> And where goods or services required by the contractor or licence holder are not available in Tanzania, such goods shall be provided by a company which has entered into a joint venture with a local company, and the local company here must own share of at least 25% in the joint venture or as shall be provided in the regulations.<sup>85</sup> In ensuring that the requirements are observed the licence holder, contractors and subcontractors are required to prepare and submit to PURA a procurement plan for a duration of at least five years indicating among others, use of local services in insurance, financial, legal accounts and health matters and goods produced in Tanzania.

The other requirement is that requiring the licence holder, its contractors and subcontractors to ensure that the local entities notify PURA of quality, health, safety and environmental standards required by licence holder and

<sup>82</sup> *Ibid*, section 218 (3) & (4).

<sup>83</sup> *Ibid*, section 218 (2) which is couched in mandatory terms and section 44 (5).

<sup>84</sup> *Ibid*, section 219 (1).

<sup>85</sup> *Ibid*, section 219 (2) & (3).

contractor; upcoming contracts as early as practicable; and compliance with the approved local content plans.<sup>86</sup> Section 219 (7) requires further that within sixty days after the end of each calendar year, the licence holder to submit to PURA a report of its achievements and its contractors and subcontractors' achievement in utilizing Tanzanian goods and services during that calendar year. To ensure that 'local companies' are local companies in the real sense, the new law defines 'local companies' meaning a company or subsidiary company incorporated under the Companies Act, which is 100% owned by a Tanzanian citizen or a company that is in a joint venture partnership with a Tanzanian citizen or citizens whose participating share is not less than 15%. It is argued here that multinationals are likely to take refuge of the last part of the definition of entering into a joint venture as the 15% participating share is likely to operate to their favour.

The local content requirement also touches the aspect of training and employment of Tanzanians where a licence holder and a contractor are required within twelve months after the grant of each licence and on each subsequent anniversary of that grant to submit to PURA for approval, a detailed programme for recruitment and training of Tanzanians in accordance with an approved local content plan.<sup>87</sup> The program should provide training and recruitment of Tanzanians in all phases of petroleum operations and gas activities and take into account gender, equity, persons with disabilities, host communities and succession plan in accordance with the Employment and Labour Relation Act.<sup>88</sup> Where a programme or a scholarship proposed to be awarded is approved by PURA, it cannot be varied without permission of PURA.<sup>89</sup> It is the responsibility of the licence holder and a contractor to submit to PURA annually, a report on the execution of the programme under section 220. The section defines host communities to mean inhabitants of the local area in which petroleum operations or gas activities take place.<sup>90</sup> The question of whether the host communities are accorded the benefits they would deserve under the principle of permanent sovereignty over natural resources and the Inter-American Court on Human Rights articulation in the case of *Twelve Saramaka Clans against the Republic of Suriname*.<sup>91</sup> is outside the scope of this article.

Training and technology transfer for the Tanzanian employees of the licensee is another local content requirement. Such training may be carried out within or outside Tanzania and may include scholarships and other financial support for education and a commitment by licence holder and contractor to maximize knowledge transfer to Tanzanians and establish management and technical capabilities and any necessary facilities for technical work, including interpretation of data.<sup>92</sup>

86 *Ibid*, section 219 (5).

87 *Ibid*, section 220 (1).

88 *Ibid*, section 220 (2).

89 *Ibid*, section 220 (3).

90 *Ibid*, section 220 (5).

91 Case No. 12.338 (June 23, 2006).

92 *Ibid*, section 221 (1).

### 2.4.3 Corporate Social Responsibility and Integrity Pledge

On the aspect of a corporate social responsibility a licence holder and a contractor is required to prepare a credible corporate social responsibility plan jointly agreed upon by the relevant local government authority or local government authorities.<sup>93</sup> Essentially, the plan is required to take into account environmental, social, economic and cultural activities based on the local government priorities of host community.<sup>94</sup>

The question of integrity pledge is a novel one that has been legislated in the new law. A licence holder and the contractor who undertakes petroleum or gas activities is required to comply with the integrity pledge which implies the conduct of regulated activities with utmost integrity; desist to engage in any arrangement that undermines or is in any manner prejudicial to the country's financial and monetary systems, in particular, all earnings, payments or receivables derived from or in respect of regulated activities shall be received in, and accounted for in Tanzania; desist to engage in any arrangement that undermines or is otherwise prejudicial to the Tanzanian tax system; disengage in arrangement that is inconsistent with the country's economic objectives, policies and strategies; disengage in arrangement that undermines or is otherwise prejudicial to Tanzanian's national security; and maintenance of satisfactory insurance coverage against losses, injuries or damage to environment, community etc.<sup>95</sup> The consequences of failure to comply with the integrity pledge is a breach of the conditions of the licence or permission to engage in regulated activity and such licence or permission shall be deemed to have been withdrawn or cancelled and that the Government shall exercise the right to takeover facilities provided for under the Act.<sup>96</sup> It is unfortunate that the integrity pledge appears to apply only to midstream and downstream activities and not upstream activities. This is because the sanctions provided for its failure to comply relates to regulated activities, and by definition regulated activities do not include upstream activities.<sup>97</sup>

### 3.0 Conclusion

The purpose of this article is to shade light on the regulation of the Tanzanian petroleum upstream sector under the Tanzania Petroleum Act, 2015. The idea was to thematically discuss some aspects of the upstream sector. It has been demonstrated that the new law has changed some aspects, like the fiscal regime as well as issues of transfer of interests, which under the new law is subject to strict conditions. The question of Government participation through the NOC and exclusive rights being granted to the NOC is another aspect that has called the author's attention. Efforts were taken to, not only state what the law provides but also make, albeit in brief, an assessment regarding its

<sup>93</sup> Read The Petroleum Act, 2015, Act No. 21 of 2015, section 222 for requirements of corporate social responsibility.

<sup>94</sup> *Ibid*, section 223 (2).

<sup>95</sup> *Ibid*, section 223 (1) & (2).

<sup>96</sup> *Ibid*, section 223 (4).

<sup>97</sup> See the definition of regulated activity in The Petroleum Act, 2015, Act No. 21 of 2015, section 3.

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achievements and possible challenges to the country as well as the contractors. It is generally concluded that while the new law is likely to increase efficiency and accountability on one hand, on the other there have been concerns from investors that the new regime is not investor friendly.