

Localizing Tanzania’s Gas Sector: Determining Optimal Policies for an Emerging Producer

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SUMMARY

Tanzania’s gas sector is at a crucial juncture. Game-changing ventures such as a liquefied natural gas (LNG) project point to the sector’s considerable potential. However, this project is by no means guaranteed to happen and it remains unclear how much Tanzanians will actually benefit from the country’s natural gas reserves.

Whether the sector’s potential is realized will in large part depend on Tanzania’s ability to design good policies and implement them effectively. One important component of that policy framework is a local content strategy the government is in the process of developing. The Petroleum (Local Content) Regulations 2017 were published in early May 2017 and will come into full effect in early November 2017. In this brief, we analyze Tanzania’s evolving local content strategy and discuss how effectively it can meet the government’s objective of maximizing the country’s benefits from potential and existing gas projects.

Considerations

Strategic direction. Tanzania’s policy and legal framework appears to prioritize maximizing local participation in the gas sector—including in highly specialized operational areas—over developing linkages with other sectors. However, it is uncertain whether Tanzania has gas reserves that justify investing in the development of highly technical skills or the production of specialized goods and services of use only to gas operations.

Definition of “local.” The definition of a “local company” differs across policy and legislation, but the legally binding definition allows an 85 percent foreign-controlled joint venture to qualify as a local company and receive preference for providing goods and services to operators in the gas sector. The implicit definition of local goods or services includes those that are “locally available,” which, if interpreted literally, could describe goods imported into Tanzania by a foreign-owned company.

Baseline information and alignment of requirements with local capacity.

A comprehensive quantitative baseline study of the existing and potential capacity of Tanzania’s workforce and companies to participate in the gas sector has yet to take place. Without such information, there is a risk of setting unrealistic requirements that could significantly increase the cost of gas projects and, consequently, lower government revenues, deter investment and encourage non-compliance.

ABOUT THE SERIES

This brief is one of a series analyzing the Tanzanian government’s approach to managing the offshore natural gas sector. Forthcoming briefs in the series include “Negotiating Tanzania’s Gas Future” and “Managing Tanzania’s Potential Gas Revenues.”

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Institutional capacity and interagency coordination. It is not clear how the different government institutions involved in developing and implementing the strategy will coordinate and delineate roles and responsibilities. The regulations do not make reference to the role of the National Economic Empowerment Council (NEEC), which provides a crucial mechanism for coordination. Capacitation of these institutions is also important, but the government will need to make difficult decisions to ensure that it utilizes scarce resources efficiently and in areas that will have the greatest benefit.

Public access to information. The policy and legal framework has few explicit transparency provisions. The public can request information the government has designated as publicly available, but it is unclear what kinds of information the public is entitled to access—for example, whether local content plans and reports are included. As the regulations allow for local content obligations to be varied and provide limited criteria for exemptions, this dearth of information prevents the public from knowing what requirements have been imposed on companies, prevents it from understanding whether companies are meeting those requirements, and also prevents it from supporting government monitoring of company compliance with those requirements.

Recommendations for the government

Review the regulations. Use the period before the regulations come into full effect to refine them and ensure they are based on two key elements: impact and feasibility.

Align local content with the national agenda. Align the local content strategy with the broader national development agenda. Also consider initially narrowing the scope of obligations to a few strategic areas and transferable skills, goods and services.

Improve the definitions of “local.” Harmonize and strengthen definitions of “local” companies, goods and services to ensure that requirements maximize participation and in-country value addition. This may require amendments to the definitions included in the Petroleum Act 2015.

Prioritize baseline information. Prioritize the collection of baseline information on existing and potential local capacity and the prospects for long-term demand. Use this information to inform the revisiting of mandatory targets.

Improve interagency coordination. Further develop mechanisms for interagency coordination. In particular, establish a clearer role for NEEC. In the course of doing this, take into account the institutional capacity that is necessary for monitoring local content requirements. The scope of these requirements should be determined by a careful consideration of how to best allocate the government's scarce resources.

Improve public access to information and benchmarking. Improve provisions for making information and benchmarking available to the public. This should include establishing the conditions in which exemptions to requirements will be granted in a public document and publishing local content plans and reports online.

INTRODUCTION

The discovery of natural gas off the coast of Tanzania from 2010 onward has led to expectations that the sector can help transform the lives of its citizens, including 12 million Tanzanians who live in poverty.¹ The large gas deposits could accelerate the industrialization of the economy and drive human development through three key mechanisms: government revenues, energy and local content. While the most important benefit of these discoveries is likely to be the generation of government revenues through the export of liquefied natural gas (LNG), the government also envisions the sector playing a large role in improving the country's power generation capacity via some of the natural gas being sent to the domestic market. The government is also in the process of developing an ambitious strategy to maximize local content as part of a larger set of policies and laws that it will use to manage the sector.

The government began articulating a vision for its local content strategy through the Natural Gas Policy of 2013 ("Natural Gas Policy") and has just published the Petroleum (Local Content) Regulations 2017 ("regulations"). Stakeholders in the sector agree that local content is an important mechanism through which Tanzania can benefit from its gas reserves. However, it is also a source of significant contention, with divergent views on the best approach.² Establishing an optimal strategy is particularly crucial at this juncture given the uncertainty surrounding investment in the LNG project. A poor global price outlook—with the price forecasts falling by more than 50 percent since early 2015³—makes for a high hurdle to be jumped before the project is commercially viable.

This brief looks at the evolving local content strategy and to what extent it is effectively designed to meet the government's objective of maximizing the country's benefits from potential and existing gas projects.⁴ We set out both the strengths and weaknesses of the current strategy and highlight areas for reform. We recommend that adjustments are needed to better respond to the specific risks and trade-offs inherent in the government's strategy. By doing so, we hope to inform any review of the recently published regulations before they come into full effect in early November 2017.

Context: opportunities and challenges

Local content is an important component of the government's strategy to ensure that the extractive sector substantially contributes to long-term sustainable development. Many analysts argue that the generation of government revenues alone is unlikely to maximize the benefits that citizens gain from natural resource wealth. In order to create an additional source of public benefits, countries have encouraged or required local participation in the sector beyond what would occur in the absence of government intervention. Greater local participation is pursued through the employment of local labor, the procurement of local goods and services, and the development of local capacity. Some of the skills, goods and services required by extractive companies may have wider applications in the economy. Local content policies can therefore also support economic diversification and growth in other sectors, and ultimately drive the structural transformation of the wider economy.

Establishing an optimal local content strategy is particularly crucial at this juncture given the uncertainty surrounding investment in the LNG project.

1 World Bank, *Tanzania Mainland Poverty Assessment: Executive Summary* (2015), 12.

2 Abel Kinyondo and Espen Villanger. *Local content requirements in the petroleum sector in Tanzania: A thorny road from inception to implementation?* (CMI/REPOA, 2016), 15-18.

3 "World Economic Outlook Database," IMF, last modified April, 2017, <http://www.imf.org/external/pubs/ft/weo/2017/01/weodata/index.aspx>.

4 We focus on the participation of the local workforce and local suppliers of goods and services in this brief, and do not consider the role of state-owned companies in any great detail. The Natural Resource Governance Institute will be producing a separate brief on the national oil company, Tanzania Petroleum Development Corporation, in the coming months.

While local content policies are developed and implemented in resource-rich countries with the objective of capturing more benefits from the sector, there are significant trade-offs, at least in the short term, that need to be taken into account. A key trade-off occurs with local content and government revenues. In countries with a low industrial base, like Tanzania, local suppliers may initially be unable to provide goods and services at a comparable price, quality and scale to foreign providers. In this scenario, the required use of more expensive local goods and services would increase project costs. At the very least, this would result in lower profit-based government revenues from the sector (revenues that could have been invested in developing and expanding the industrial base). If the impact on costs is expected to be significant, it could actually discourage investment.

Another potential opportunity cost is reduced economic diversification. While greater diversification is a primary objective of many local content policies, these policies can actually make diversification more difficult. Increased local participation in extractives can increase the share of a country's assets that are dependent on a sector that is finite in nature and inherently volatile (this dependence is even greater if the policy focus is on specialized operational areas that require skills, goods and services not demanded elsewhere in the economy). For example, if a country's manufacturing companies sell a large part of their output to the gas sector, a fall in the gas price resulting in cost-cutting by the gas sector would significantly reduce the income of these manufacturing companies—increasing the impact of lower gas prices on the economy beyond the direct effect on government revenues. Other productive sectors could also be harmed if local suppliers are unable to meet the increased demand caused by greater use of local content in the extractives sector. The resulting cost inflation would reduce the competitiveness of these sectors and the economy as a whole.

With these general opportunities, challenges and trade-offs in mind, we now provide an overview of Tanzania's local content strategy for its emerging natural gas sector. Following this overview, we assess the policy and legal instruments that will be used to implement the strategy.

POLICY, LEGAL AND INSTITUTIONAL FRAMEWORK

Policy and legal framework

Local content strategies are established through policies, laws, regulations or contracts between the state and investors. The policy and legal framework for governing local content in Tanzania's gas sector is becoming increasingly comprehensive. The Petroleum Act 1980 (for the upstream) merely required an application for a development license to be accompanied by a proposal for training and employing Tanzanians, while the Petroleum Act 2008 (for the midstream and downstream) did not make reference to local content. Similarly, the National Energy Policy of 2003 only made reference to the need for human resource development.⁵ The large offshore discoveries commencing in 2010 resulted in the gradual replacement of the policy and legal framework for the sector, and, with it, a greater focus on local content. This process began with the Natural Gas Policy— which dedicates a section to local content⁶—and continued with the development of a local content policy for the sector. However, the latter was not finalized, and some of its contents were subsumed in the National Energy Policy of 2015 (“National Energy Policy”),⁷ which is now the prevailing policy document guiding the government's approach to local content in the sector.

The large offshore discoveries resulted in the gradual replacement of the sector's policy and legal framework and a greater focus on local content.

5 Section 5.7.2 of the National Energy Policy 2003.

6 Section 3.1.7 of the Natural Gas Policy 2013.

7 Section 3.3. of the National Energy Policy 2015.

A few months before the National Energy Policy was finalized, the government passed the Petroleum Act of 2015 (“Petroleum Act”). This act is the central pillar of the legislation governing the sector; it applies to the up-, mid- and downstream, and addresses a number of local content issues.⁸ The government’s Ministry of Energy and Minerals (MEM) published local content regulations under this act in early May 2017. Stakeholders (including NREGI) provided comments on the first and second drafts earlier this year.

Two other notable pieces of legislation that impact local content in the gas sector are the Non-Citizens Act 2014 (“Non-Citizens Act”) and the Public Procurement Act 2011 (“Public Procurement Act,” which was amended in 2016). The Non-Citizens Act was the first law to start imposing limits on foreign participation in economic activities in Tanzania, placing limits on work permits for foreigners and requiring that a plan for their replacement with Tanzanians be developed.⁹ The Public Procurement Act encourages the unbundling of contracts to increase local participation.¹⁰ Given that the Public Procurement Act does not state that any government entities are exempt, this provision is currently expected to apply to the national oil company, Tanzania Petroleum Development Cooperation (TPDC). The government passed three pieces of legislation on the extractives sector in early July 2017. One of these, the Written Laws (Miscellaneous Amendments) Act 2017, outlines a revised local content strategy for the mining sector through amendments to the Mining Act 2010 (“Mining Act”).¹¹ However, it does not amend the existing strategy for the gas sector.

Local content requirements applicable to specific gas projects are set out in contracts between the government and companies. Production sharing agreements (PSAs) set out these requirements for upstream activities. Requirements for the LNG plant and supporting midstream infrastructure will be established in the host government agreement, negotiations around which are at an early stage. The Petroleum Act includes a “grandfather” clause, which means provisions in the Petroleum Act or its regulations do not affect existing licenses or agreements.¹² The legislation passed in early July 2017 also does not amend existing agreements, but it does allow the government to renegotiate them if they are deemed to contain “unconscionable terms.”¹³ Unless existing PSAs are renegotiated, the requirements that they contain are likely to differ from those set out in general legislation. However, it is unclear what these requirements are because the government and companies have not disclosed the PSAs, with the exception of one PSA for an onshore project.¹⁴ All current PSAs were signed before the model PSA of 2013, which requires companies to comply with the prevailing local content policy.¹⁵ Local content provisions in the earlier model PSAs of 2004 and 2008 focus on preference being given to local labor, goods and services. This earlier approach is reflected in the one disclosed PSA, which was signed in 2001.¹⁶

The government published local content regulations under the Petroleum Act in early May 2017.

8 Section 219-220 of the the Petroleum Act 2015.

9 Section 4(8) of the Non-Citizens (Employment Regulation) Act 2015.

10 Section 49(1)(c) of the Public Procurement Act 2011.

11 Section 28 of the Written Laws (Miscellaneous Amendments) Act 2017, which adds a new Part VIII Local Content, Corporate Social Responsibility and Integrity Pledge to the Mining Act 2010.

12 Section 260(3) of the Petroleum Act 2015.

13 Section 5(3) of the Natural Wealth and Resources Contracts (Review and Renegotiation of Unconscionable Terms) Act 2017.

14 The Tanzania Extractive Industries Transparency Act of 2015 requires that all new concessions, contracts and licenses should be made public, but it is unclear whether this requirement applies to contracts signed prior to 2015. From: Don Hubert and Rob Pitman. *Past the Tipping Point? Contract disclosure within EITI* (Natural Resource Governance Institute, 2017), 16.

15 Article 20(a) of the model PSA of 2013.

16 Article XV-XVI of the Songo Songo Gas Field PSA of 2001.

Institutional framework

An increasing focus on local content by the government—not only in the gas sector but also across the wider economy—is reflected in the recent establishment of a local content department in the National Economic Empowerment Council (NEEC), which is located within the prime minister’s office. Established in 2015, this department has responsibility for the government’s local content strategy and leads the development, coordination and monitoring of local content in the economy. However, MEM, as the ministry responsible for the gas sector, has taken the lead thus far in the development of that sector’s local content policy and legislation.

The Petroleum Upstream Regulatory Authority (PURA), established by the Petroleum Act, is responsible for regulation of the upstream, while the existing Energy and Water Utilities Regulatory Authority (EWURA) is responsible for regulation of the mid- and downstream. The regulations indicate that these responsibilities include advising MEM on local content requirements and monitoring compliance with them.¹⁷ TPDC not only has a direct role in the government’s local content strategy through its participation in gas operations, but the Petroleum Act also provides it with responsibility to promote local content.¹⁸

NEEC has requested that other government entities appoint a local content coordinator to work with it and oversee local content operations in their area of responsibility. However, it is not yet clear how the different institutions will coordinate and share responsibility for development and implementation of local content initiatives going forward.

Government institution	Acronym
Ministry of Energy and Minerals	MEM
National Economic Empowerment Council	NEEC
Petroleum Upstream Regulatory Authority	PURA
Energy and Water Utilities Regulatory Authority	EWURA
Tanzania Petroleum Development Corporation	TPDC

Table 1. Main government institutions responsible for local content strategy

OBJECTIVES OF TANZANIA’S LOCAL CONTENT STRATEGY

We see one primary objective for local content in the gas sector set out in the government’s first statement on local content in the Natural Gas Policy, and in the series of subsequent policy documents culminating in the National Energy Policy: maximization of benefits to Tanzanians through participation in the gas value chain. The draft local content policy describes this objective as the “maximum engagement of local content and local participation in the development of the oil and gas industry,” while the National Energy Policy articulates it as “a progressive and comprehensive integration of Tanzanian citizens into all aspects of the petroleum industry to ensure maximization of benefits.”¹⁹

The primary objective of the local content strategy appears to be local participation in the gas value chain.

These policies then set out more specific objectives that indicate how this main objective will be reached. Reference is made to both directly increasing the participation of the local workforce and suppliers and developing their capacity to participate. Human capacity, technological skills and financing are all identified as significant challenges to local participation (but also essential to the promotion of local content) and form the basis for a number of specific objectives. Fabrication,

17 E.g., Regulation 29(2-3).

18 Section 9(2)(l) of the Petroleum Act 2015.

19 Section 2.4.1 of the draft local content policy; Section 3.3. of the National Energy Policy 2015.

manufacturing and maintenance services are identified as areas in which the development of capacity and participation should be prioritized.

Another objective set out in the Natural Gas Policy and the National Energy Policy is the development of linkages between the gas sector and other sectors of the economy. This objective is listed in a different section than the local content provisions; it is therefore unclear whether the government views this as one of its explicit objectives for its local content strategy. Indeed, the description of this objective in these documents does not make it clear what “linkages” are envisaged. The National Energy Policy states that the government shall: (i) ensure that growth of the petroleum industry supports strategic investment in other sectors of the economy; and (ii) facilitate the establishment of an integrated plan for strategic sectors of the economy.²⁰ These linkages could therefore refer to the investment of gas revenues in other sectors or relate to the earmarking of gas supply, for example. However, they could also encompass the leveraging of local participation in the gas sector to generate spillover benefits for the rest of the economy.

KEY CONSIDERATIONS FOR OPTIMIZING TANZANIA'S INSTRUMENTS FOR INCREASED LOCAL CONTENT

Hints at which instruments the Tanzanian government envisages using to achieve its local content objectives in the gas sector are provided in its policies. However, these instruments are predominantly set out in the Petroleum Act and its regulations.

Local content instruments generally fall within two broad categories. “Hard” strategies contain legally binding requirements for domestic employment, local ownership, in-country goods, services provision and capacity development. “Soft” strategies only encourage such actions (sometimes through the use of incentives) and set targets that are aspirational rather than mandatory. Country context—including political, economic and sectoral factors—has a significant influence on which approach is more likely to maximize the benefits and minimize the costs of pursuing increased local participation. Differences in country context therefore often result in countries with the same objectives using different instruments to pursue them.

The Tanzanian government appears to be taking a “hard” approach to local content in the gas sector. This is in contrast to the local content strategies that other emerging African producers have developed recently. Legislation recently passed in Mozambique, Kenya and Liberia have indicated a “soft” approach to local content in their emerging oil and gas sectors.²¹ For example, the law governing Mozambique’s nascent large-scale operations does not require preference to be shown to local content for contracts worth more than USD 25 million, while a public tender is not required for goods that need to be compatible with goods already in use.²²

The regulations for Tanzania’s gas sector set out a large number of minimum local content levels for both the employment of labor and the use of goods and services across the value chain, with relatively significant penalties for non-compliance. However, these strict requirements stand in contrast to undemanding definitions for a local company and local goods and services, and the allowance for exemptions for areas in which local participation is not possible.

The Tanzanian government appears to be taking a “hard” approach to local content in the gas sector.

20 Section 3.2.1.6 of the National Energy Policy 2015.

21 Jesse Salah Ovidia. “Local Content Policies and Petro-development in Sub-Saharan Africa: A Comparative Analysis”, *Resources Policy* 49 (2016): 26-28, doi:10.1016/j.resourpol.2016.04.003.

22 Shearman and Sterling. *Mozambique’s Decree Law: Worth the Wait* (2015), 2. As of early 2017, the government of Mozambique was in the process of developing a new National Content Act, the draft of which has been reported to provide harder targets than the existing rules. However, the act is not expected to modify the provisions in the Decree Law.

In this section, we look at these instruments in more detail and set out some of the key factors that could ensure that the evolving strategy is optimal for Tanzania. The selection of these instruments will need to be informed by Tanzania's specific political, economic and sector contexts, as well as a weighing of the typical trade-offs and challenges that arise from the pursuit of increased local content.

We do not attempt to identify the specific design of the instruments that Tanzania should consider incorporating into its local content strategy. For example, we do not provide recommendations on the specific sectors that should be prioritized; make projections of potential demand or value capture; or recommend specific targets. Our considerations are limited to the broad approach that is likely to be optimal for Tanzania.

Strategic direction

An optimal local content strategy for Tanzania would be based on the government's long-term national development objectives. This strategy would be informed by a "big picture" approach, which systematically considers the objectives set out in the government's Tanzania Development Vision 2025 ("Vision 2025") and national five-year development plans, how those objectives can be supported by the gas sector, and then how local content can help the sector support these objectives.

Vision 2025 sets out the objectives of semi-industrialization and reaching middle income status; these objectives are reinforced in the current national development plan, the National Five Year Development Plan of 2016/17-2021.²³ We believe that using local content in the gas sector to further these objectives requires prioritizing developing linkages with other sectors over maximizing local participation in the gas sector *per se*.

Tanzania's natural gas reserves are significant but small compared to other current and potential gas producers. Gas currently in place in Tanzania is now estimated to be 57 trillion cubic feet (tcf), but there are currently only development plans for 28 tcf.²⁴ In contrast, Nigeria has proven reserves of around 180 tcf and Mozambique is estimated to have 100-180 tcf. It is questionable whether Tanzania has or is even likely to have reserves that justify investing in the development of highly technical skills or the production of specialized goods and services of use only to gas operations. Given that these capabilities are likely to take a considerable amount of time to develop, there is a risk that they will become obsolete before they generate significant benefits for the country.

It is questionable whether Tanzania has reserves that justify investing in the development of skills or the production of goods and services of use only to gas operations.

Focus on transferable skills

Instead of aiming for local participation in highly specialized operational areas, it would be more advantageous to focus on developing skills, goods and services that are also of use to the non-gas economy. It would therefore be advisable for the regulations to make the fulfillment of the National Energy Policy's objective of developing linkages with other sectors the basis for any requirements it sets out. A particular focus could be on developing capacity in higher value-adding sectors that will drive the industrial transformation envisaged in both Vision 2025 and the current national development plan. Selection of the areas in which the government pursues local participation needs to also take into consideration the potential demand from the sector and Tanzania's existing and potential capacity to meet that demand.

23 United Republic of Tanzania, *The Tanzania Development Vision 2025* (1998), 2; United Republic of Tanzania, *National Five Year Development Plan 2016/17-2020/21* (2016), i.

24 Ministry of Energy and Minerals, *Energy Sector Quarterly Review, Ed. No. 4* (2016), 18; Wood Mackenzie, *Tanzania Upstream Summary September 2016* (2016), 17.

A recent World Bank study on the local content opportunities in Tanzania's LNG project identifies construction (specifically clearing and developing the site for the LNG plant, including constructing the buildings) and metal and steel fabrication as meeting these criteria.²⁵ This will ensure that capacity developed through participation in the gas sector has a broader and longer-term impact on economic development, and acts as a catalyst for a more rather than less diversified economy. The achievement of this objective, with the resulting expansion of the tax base, could justify any initial trade-off between government revenues and use of local content.

Prioritize select key areas

There are also benefits to focusing on only a limited number of key strategic areas. A more focused approach should improve the willingness of gas companies to work toward meeting more ambitious requirements in these areas. It enables the government to better target its interventions in capacity development, and ensures priority areas receive adequate funding and institutional support. This approach would also prevent the government's limited resources from being spread too thin—government can focus on ensuring that the requirements in these areas are adhered to, rather than having to monitor compliance with requirements in other more peripheral areas.

There are benefits to focusing on only a limited number of key strategic areas.

While the policy documents identify fabrication, manufacturing and maintenance services as priorities, NEEC identifies eight priority sectors and the regulations provide requirements for a wide range of sectors.²⁶ The government could consider moving toward a more focused approach—one that makes it likelier that local content in the gas sector will significantly contribute to the achievement of the national development objectives.

Analysis of potential demand and local capacity

A key stage in developing an effective local content strategy is determining the potential demand for labor, goods and services in the sector and establishing the local capacity to meet it. Without this information, three crucial components of the strategy are likely to have failings: identification of areas of focus; expectations around realistic local content levels; and the design of interventions to build local capacity over time.

Establishing this baseline information is all the more important given that there appear to be differences in opinion on these areas among stakeholders. The African Development Bank's (AfDB) forthcoming situation analysis for NEEC sets out estimates of labor demand for the LNG project from BG Group (which has since been taken over by Shell) and from a recent World Bank study, with the latter's estimate under the "success scenario" around 60 percent higher.²⁷ While there is widespread acknowledgement that current local capacity to participate is relatively low, recent discussions between the government and industry actors have focused on how much capacity can realistically be increased. For example, the regulations require the procurement of local inputs that industry officials say even an advanced producer (such as Indonesia) does not have sufficient capacity to produce.²⁸ It is unlikely that Tanzania will be able to develop this capacity before its gas reserves are exhausted.

25 World Bank, *Leveraging a Large Capital Investment to Develop Local Value Chains* (2016), 32-52.

26 African Development Bank (AfDB), *Local Content Situation Analysis in Tanzania in the Mining and Gas Sectors* (2017), 27.

27 AfDB, *Local Content Situation Analysis in Tanzania*, 45.

28 Indonesia is said to import many of the inputs that the first schedule of the Tanzanian regulations (part 2.3) would require to be domestically sourced.

Prioritize the collection of baseline information

The collection of baseline information on current local capacity and capabilities is envisaged in the draft local content policy and by Regulation 4(2)(a). However, a comprehensive quantitative study that could gather that information has yet to take place. Undertaking this study will need to be an immediate priority for government, especially as the regulations are due to come into effect in early November 2017. Indeed, the government could consider postponing this date until the baseline study has been completed, or at least exclude specific mandatory targets (see below) until after the study has been carried out. Given that this information would form the basis for large components of the local content strategy, it is crucial that it enjoys strong buy-in from all stakeholders. We therefore think it would be beneficial for the study to be a collaborative exercise among the government (led by NEEC), local companies and labor organizations (represented by the Tanzania Private Sector Foundation and Trade Union Congress of Tanzania), and the gas industry (represented by the Oil and Gas Association of Tanzania).

The collection of baseline information on local capacity will need to be an immediate priority for government.

Definitions of “local”

Definitions of “local content,” “local companies” and “local goods and services” are of particular importance to determining the extent of local participation and in-country value addition that local content requirements are likely to achieve.

Local content. Across the policy and legal documents related to the gas sector, there is a consistent focus on value added in the definition of local content. The National Energy Policy, the Petroleum Act and the regulations all define local content as “the quantum of composite value added to, or created in, the economy of Tanzania through deliberate utilization of Tanzanian human and material resources and services in the petroleum operations.”²⁹ However, there are slight differences in the overall definition used.

Local company. The National Energy Policy defines local business as an entity “which is incorporated under the applicable laws of Tanzania and is wholly owned by Tanzanians or with at least 51 percent of shares owned by Tanzanian Nationals.”³⁰ However, the Petroleum Act and the regulations define a local company as “a company or subsidiary company incorporated under the Companies Act, which is 100 percent 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 percent.”³¹ Notably, the less demanding definition is legally binding and stands in contrast to recent amendments to the Mining Act, which more closely adhere to the National Energy Policy and define a local company as being an entity either 100 percent owned by a Tanzanian citizen or a joint venture at least 50 percent owned by Tanzanian citizens.³² While the reason for the change from the definition in the National Energy Policy to that in the Petroleum Act is unclear, it remains a fundamental loophole that may undermine local participation.

Local goods and services. A definition of local goods and services is not strictly provided in any legally binding document, but it can be inferred. The Petroleum Act and Regulations 8(b) and 15 state that preference must be given to goods and services “provided, manufactured or locally available in Tanzania.” The draft local content policy definition of local goods refers to goods “obtained, produced or manufactured and hav[ing] after-sales services in Tanzania Mainland.”³³ It later states that operators

29 For example, see Section 3 of the Petroleum Act 2015.

30 Page xiii of the National Energy Policy 2015.

31 Section 219(9) of the Petroleum Act 2015.

32 Section 28 of the Written Laws (Miscellaneous Amendments) Act 2017.

33 Page iii of the draft local content policy.

shall “as far as practicable use goods and services produced by or provided in Tanzania by Tanzanian-owned businesses for their operations in preference to foreign goods and services provided in Tanzania by foreign registered businesses in Tanzania or foreign businesses not registered in Tanzania.”³⁴ The National Energy Policy also focuses on the use of goods and services “produced” in Tanzania.³⁵

Strengthen and harmonize definitions

Reassessing the definition of a local company would be beneficial. By allowing for an 85 percent foreign-controlled joint venture to qualify as a local company and receive preference for providing goods and services to operators in the gas sector, this definition limits the extent to which Tanzanians will benefit from local content provisions. The definition set out in the National Energy Policy (which refers to majority Tanzanian ownership) is more likely to have the desired impact on local participation in the gas sector. Even this could be improved on by making it so that only companies with “majority Tanzanian ownership, management and employees” are classed as local companies to prevent fronting and/or elite capture and provide benefits to a broader base of Tanzanian citizens.³⁶

Allowing for an 85 percent foreign-controlled joint venture to qualify as a local company limits the extent to which Tanzanians will benefit from local content provisions.

The implicit definition of local goods or services in the Petroleum Act and its regulations, and its inclusion of those that are “locally available,” could also be reconsidered. Taking a literal interpretation, goods imported into Tanzania by a foreign-owned company are “locally available” in Tanzania, yet they would provide no value-addition in the country, supply chain participation or similar benefits to Tanzanians. Limiting the definition to goods and services that are “produced in Tanzania” or “provided by Tanzanian-owned businesses” in line with the draft local content policy and National Energy Policy would better capture the goal of having the gas sector stimulate local supply chain development.

Aside from strengthening these definitions of key terms to ensure that local content provisions actually benefit Tanzanians, harmonizing these terms would avoid confusion across the policy and legal framework. While it is only the definitions set out in the Petroleum Act and its regulations that are legally binding—and while there is consistency across these documents—the difference between these definitions and those in the National Energy Policy makes the government’s underlying approach less clear, gives rise to an unnecessary risk of misinterpretation and provides a non-uniform basis for monitoring and enforcement.

Mandatory targets

The policy and legal framework sets out provisions requiring preferential treatment to be given to local labor, goods and services and requiring minimum local content levels in these areas. These are most comprehensively set out in the regulations.

In line with most local content strategies elsewhere, Section 3.3.3 of the National Energy Policy and the Regulation 8(a) require gas companies to give preference to Tanzanians across all employment opportunities, and Regulation 14 indicates that

34 Page 20 of the draft local content policy.

35 For example, see Section 3.3.1 of the National Energy Policy 2015.

36 For example, Regulation 49 of Ghana’s Petroleum (Local Content and Local Participation) Regulations, 2013, defines an “indigenous Ghanaian company” as “a company...that has at least fifty-one percent of its equity owned by a citizen of Ghana; and ... that has Ghanaian citizens holding at least eighty percent of executive and senior management positions and one hundred percent of non-managerial and other positions ...”.

both “unskilled” and “semi-skilled” positions can only be filled by Tanzanians.^{37,38} However, in contrast to more recent policies in the region, Regulation 29(1) also establishes minimum levels of local employment in more skilled positions. Set out in the first schedule, these requirements are measured in terms of man hours.

Similarly, Section 219(1) of the Petroleum Act and Regulation 8(b) indicate that preference should be given to local goods and services (though, as noted above, this includes goods and services that are simply “locally available”). Minimum levels of local content in the procurement of goods and services (measured in terms of spending) are established by Regulation 29(1). This regulation does not make the requirement to reach these levels contingent on local inputs being of comparable price, quality and scale to foreign inputs.

Section 219(2) of the Petroleum Act and Regulation 15(2) require that any goods and services not available in Tanzania be provided by a company that has entered into a joint venture with a local company. The regulations allow for more flexibility than the Petroleum Act. Regulation 15(4) permits other “business arrangements” to be formed if a joint venture is not possible. However, these arrangements still represent a blanket requirement for local equity ownership. Section 3.1 of the draft local content policy suggests that the primary objective of this requirement is as a mechanism for capacity development and technology transfer.

The regulations allow for exemptions from these different requirements. For example, Regulation 14(3) permits PURA or EWURA to approve the employment of a non-Tanzanian in a semi-skilled position if a qualified Tanzanian cannot be identified. Similarly, these entities can also exempt a foreign supplier from entering into an arrangement with a local company to supply non-local goods and services (Regulation 15(5)). Regulation 29(2) allows the Minister of Energy and Minerals some flexibility to adjust the minimum levels of local content. However, there is a lack of clarity on what basis such exemptions or changes to requirements will be approved.

As noted above, local content requirements could lower government revenues from the sector—at least until the quality and price of local inputs become competitive—and could ultimately discourage investment. However, some note that without a binding requirement, extractive companies generally have little regard for local content.³⁹ Given established international supply networks, companies may fail to be proactive in sourcing local labor or suppliers even if the necessary capacity exists in-country. Indeed, a World Bank report that sets out lessons learned on local content for Tanzania cites the experience of Trinidad and Tobago and suggests that specified minimum levels may be necessary for local content policy to be sufficiently enforceable to be effective.⁴⁰

However, even among those who advocate for mandatory local content use, there is a consensus that setting requirements at levels that are too far out of sync with existing or potential capacity in the country is detrimental to local content objectives. Attempts to attain these levels have a significant impact on costs, and therefore are rarely effectively complied with (the cost of adhering to the requirements can be significantly greater than any penalty for non-compliance). This can have a damaging,

The requirement to reach minimum levels of local content is not contingent on local inputs being of comparable price, quality and scale to foreign inputs.

37 Though the latter is inconsistent with the first schedule, which only requires 80 percent of semi-skilled labor in the upstream to be local in 10 years.

38 Unskilled positions are defined as “jobs which do not require special training or skills” and semi-skilled positions are defined as “jobs which require basic knowledge in the area of professional”.

39 For example, Simon White. “Regulating for Local Content: Limitations of Legal and Regulatory Instruments in Promoting Small Scale Suppliers in Extractive Industries in Developing Economies,” *The Extractive Industries and Society* 4(2) (2016): 266, accessed 15 May 2017, doi:10.1016/j.exis.2016.08.003.

40 World Bank, *Maximizing Domestic Value Added in the Oil and Gas Industry* (2016), 10.

secondary effect on compliance with more realistic local content requirements and with the rest of the wider legal framework for the sector. Kinyondo and Villanger highlight the risk that unrealistic requirements lead to fronting, as they encourage companies to “play the game of numbers rather than strive to build local capacities.”⁴¹ Finally, they can force the government to provide broad exemptions on an *ad hoc* basis, as has been the case in a number of countries (including Ghana).⁴² This undermines the credibility of the legal framework and limits its usefulness as guidance to companies on which areas they will have to plan for local participation. It may also introduce an unhelpful element of discretion on exemptions, which increases the risk of corruption.

Set fewer, more strategic targets

Tanzania's current approach risks many of these weaknesses, diluting the effectiveness of its local content strategy. The regulations specify required levels of local content across the value chain (including 126 categories of goods or services) and, among other requirements on legal and financial services, require companies to be fully insured by a local provider. This brief does not attempt to definitively establish the current or potential capacity of the local workforce and suppliers to meet these requirements, and whether these requirements are realistic. However, the problem of setting these requirements without baseline information on local capacity is apparent in a number of areas. For example, the requirement to procure all insurance from a local provider could represent a systemic risk to the economy, given the size of potential insurance claims relative to the limited financial capacity of Tanzania's providers. Indeed, the limited number of small- and medium-sized enterprises in Tanzania has made it a challenge for local suppliers to adequately supply the needs of contractors in the mining sector (even in non-technical areas such as catering).⁴³ Given the detrimental impact of imposing unrealistic requirements on industry, as aforementioned, the government could consider postponing the date at which the regulations come into full effect, or at least the imposition of these specific requirements, until baseline information has been collected.

Tanzania's current approach to setting mandatory targets risks diluting the effectiveness of its local content strategy.

As discussed in relation to strategic direction, the government could also consider reducing the number of requirements or at least aligning the majority of them with existing capacity. As part of this more focused approach, strengthening the definition of local companies and local goods and services would ensure that intervention in these key areas has the intended impact on local capture of value added. However, it is important to consider that even fewer targets may initially increase costs for companies and therefore reduce government revenues, and that overly ambitious/unrealistic targets that significantly increase costs may have an impact on the decision to invest in Tanzania's offshore deposits.

Align business arrangement requirements with existing capacity and demand prospects

The cautious approach we believe the government should consider taking when setting wide-ranging requirements is also relevant for the requirement that goods and services not available in Tanzania be provided by a company that has entered into an arrangement with a local company. As noted in the forthcoming AfDB situation analysis, this blanket requirement is unusually demanding (especially in a

41 Kinyondo and Villanger, *Local content requirements in the petroleum sector in Tanzania*, 18.

42 Presentation by Dr. Juliette Twumasi-Anokye, Consultant on Local Content to Petroleum Commission, Ghana at World National Oil Companies Local Content Congress, 2015.

43 Siri Lange and Abel Kinyondo. “Resource nationalism and local content in Tanzania: Experiences from mining and consequences for the petroleum sector,” *The Extractive Industries and Society* 3(4) (2016): 1100, accessed 15 May, 2017, doi:10.1016/j.exis.2016.09.006.

context where the commercial drivers for such an arrangement, such as the sharing of technical expertise or expansion of output capacity, are limited).⁴⁴ The primary objective of this arrangement is capacity building, but given that some of these arrangements will have an extremely short duration—as some goods and services are likely to be required only once by the sector in Tanzania—achieving it will be difficult. Moreover, the global market for many of these goods and services is limited. Therefore, even if the local partner were to become sufficiently capacitated, the sustainability of its business model would be uncertain. Indeed, the draft local content policy and Regulation 4(2)(c) acknowledges that Tanzanian participation in some areas would have limited value. Aligning requirements for foreign companies to enter into business arrangements with local companies with areas where capacity currently exists (or where future demand can sustain profitable business in the long-term) would be beneficial.

Prescribe parameters for granting exemptions

The regulations do allow for exemptions from requirements, and the Ministry of Energy and Minerals is able to adjust the minimum levels of local content. This provides important flexibility. However, granting broad exemptions reduces the credibility of the wider local content strategy and therefore risks the achievement of its main objectives. Thus, the availability of exemptions does not diminish the importance of initially setting realistic and targeted requirements. For example, if the host government agreement for the LNG plant were to provide exemptions on a multitude of legislated requirements, it would make exemptions for other activities more likely, and yet imposing the proposed regime could result in investment in the LNG project not happening.

Well-defined criteria for the granting of exemptions are also necessary to reduce the discretionary power of individuals or institutions and ensure that the regulations provide useful forward guidance to stakeholders. However, there are limited criteria for exemptions and no indication of whether flexibility in minimum local content levels applies generally or to a specific entity on a case-by-case basis. For example, if the requirements for business arrangements with local companies for the provision of non-local goods and services is retained, the regulations could set out criteria for the identification of goods and services for which local participation is not expected (such as goods and services for which local or regional demand would be unable to sustain a profitable enterprise in the long term), and state that providers of these goods and services would not be required to enter into an arrangement with a local company.

Capacity development

There are various instruments proposed in the policy and legal framework that are aimed at improving the capacity of local labor and suppliers to operate in the sector.

With regard to the development of the local workforce, Regulation 12 and Regulation 13 require the submission of training and succession plans for approval by PURA or EWURA. Regulation 12(6) sets out a rather open-ended requirement: when a lack of capacity prevents the employment of Tanzanians, “reasonable effort [is] made to provide training to [them] in that field.” This training requirement is in addition to the requirement in the model PSAs for contractors to provide an annual training grant to TPDC.

Regulation 18 also requires the submission of a technology transfer plan. While this plan requires approval from PURA or EWURA, there does not appear to be a stipulated amount of technology transfer that gas companies are required to undertake.

The availability of exemptions does not diminish the importance of initially setting realistic and targeted requirements.

44 AfDB, *Local Content Situation Analysis in Tanzania*, 20.

While the law and regulations seem to place significant responsibility on gas companies to develop local capacity, there are also a number of government-led initiatives in this area that are not explicitly defined in policy or law. As noted in the forthcoming AfDB situation analysis, the Human Capital Development Programme led by MEM aims to build the capacity of local training institutions and ultimately establish the “Centre of Excellence in Oil and Gas” as envisaged in the draft local content policy. The National Skills Development Strategy led by the Ministry of Education and the Ministry of Labour has a wider focus, directed at a number of sectors with high growth potential.⁴⁵ There are also government initiatives in supplier development. The National Energy Policy notes that the government will develop a strategy for ensuring local suppliers access to financing, and NEEC now has financing facilities for that purpose.⁴⁶

Align capacity development priorities with strategic direction

It may not be optimal for the local content strategy to focus on capacity development in highly specialized operational areas of the gas sector when that capacity only has short-term or one-time applicability. This is particularly important given the dilemma of needing to start developing capacity now if there is going to be significant local participation in the LNG project while there is still uncertainty around whether the project will go ahead at all. Instead, it would be beneficial for capacity development efforts to be aligned with local content that emphasizes skills transferable to non-gas, high-growth sectors.

For the development of the local workforce, this requires initiatives such as MEM’s Human Capital Development Programme to be complemented by a broader push to improve basic skills (as well as vocational and technical capabilities) that are demanded by the wider economy. It also means that it might be beneficial to reconsider the requirement that gas companies provide training in every operational area. Not only will some skills be useful for a short period, but this approach is likely to reduce training efforts in more important areas.

Similarly, supplier development initiatives could be better focused on capabilities that extend beyond merely supplying the gas sector. They could also address some of the barriers to growth for small- and medium-sized enterprises. While Tanzania has become an easier place to do business in, businesses continue to face challenges in a number of areas (for example, paying taxes, power supply and starting a business).⁴⁷ Improvements to Tanzania’s business climate would have benefits for both local content in the gas sector and the wider economy (and would also reduce costs for gas companies, making investment more likely). While the World Bank’s *Doing Business 2017* assessment suggests that accessing credit has been getting easier, government policies and independent reports indicate that it continues to be a major challenge. Prioritizing a strategy for tackling this, as envisaged in the National Energy Policy, would therefore be important.

There are significant capacity development coordination problems both within the government and between the government and other stakeholders.

Ensure a coordinated government approach to capacity development

The forthcoming AfDB situation analysis highlights the significant capacity development coordination problems both within the government and between the government and other stakeholders, namely industry and donors.⁴⁸ Again, NEEC provides a crucial mechanism for coordination that should be fully utilized in the months (and years) ahead.

45 Ibid., 51-52.

46 Page 38 of the National Energy Policy 2015.

47 World Bank, *Doing Business 2017: Tanzania* (2017), 6.

48 AfDB, *Local Content Situation Analysis in Tanzania*, 46.

Fiscal incentives

Fiscal incentives can be offered as part of a local content strategy in combination with, or in place of, enforceable requirements. Unlike neighboring Uganda, such incentives are limited in Tanzania's policy and legal framework. Regulation 19(2) provides the Minister of Energy and Minerals the option of using fiscal incentives to encourage gas companies to develop local capacity and to encourage local companies to establish productive activities. The regulations do not specify what incentives may be provided; but they could, for example, entail a reduction in, or exemption from, specific taxes or fees for a gas company if it implements a supplier development program.

Take a cautious approach to fiscal incentives

Before any incentives are offered, a comprehensive cost-benefit analysis would need to be conducted. This analysis could take into account the government's objectives (for example, whether it prioritizes revenue generation or local content) and the potential risk of companies exploiting this policy to reduce their tax liabilities without necessarily increasing local capabilities. Given that there is already likely to be a trade-off between local content and government revenues, at least in the short term, and given that the benefits of local content are less certain, we think it would be advisable for the government to be cautious about any further prioritization of local content over government revenues. Any incentives that are granted could be time-bound.

It would be advisable for the government to be cautious about any further prioritization of local content over government revenues.

Supplier database

Regulation 35 provides for the establishment of a "Common Qualification System," a database containing the details of local suppliers that have been approved by the government. As stated in Regulation 36, its objective is "to serve as the sole system for the registration and pre-qualification of service providers in the petroleum industry."

Ensure a timely and transparent registration process

Government officials have indicated that only local companies that have been registered in this system can be awarded contracts (though this is not explicitly stated in the regulations). Such a requirement could be beneficial. It could make the contracting process more efficient by providing contracting companies with a comprehensive database of local providers of goods and services that have already been approved by regulatory agencies. It would also enable PURA and EWURA to focus their compliance-monitoring activities on a defined list of companies. However, requiring contracts to be awarded only to local companies on the Common Qualification System would necessitate PURA and EWURA to have sufficient capacity to evaluate and register companies in the system in a timely manner. Delays could have significant repercussions for the performance of the sector, preventing goods and services from being procured when needed.

Well-defined and transparent registration criteria applied via a transparent process will also be important given the influential role it gives to system operators and the resulting risk of corruption. Developing this criteria in collaboration with industry would ensure it is aligned to industry's own standards.

Fronting and elite capture

The draft local content policy acknowledges the risk of fronting, and Regulation 42(2) provides PURA and EWURA with the authority to investigate potential instances of it. However, the regulations contain few other preventative measures.

The minimum levels of local content established in the regulations will actually increase the risk of fronting if they are too far out of sync with existing or potential capacity in the country. If using local companies to supply goods and services is not feasible, gas companies will be incentivized to meet the requirements through other means.

Consider additional measures to reduce the risk of fronting and elite capture

There are few preventative measures against fronting in Tanzania's current policy and legal framework. For example, the definition of a local company only refers to equity ownership, which opens the door for the creation of shell companies; to eliminate this possibility, an enterprise that wishes to be categorized as a local company could be required to own at least some of its capital equipment. (The Nigerian government introduced a requirement of this nature to combat fronting.⁴⁹) Further, while Regulation 31 establishes a number of information requirements for a company to be awarded a procurement contract or order, it does not explicitly require the disclosure of beneficial ownership—to require such disclosures could facilitate the detection of fronting. Finally, local content requirements that require, or provide preference for, companies with majority Tanzanian management and employment will ensure that companies providing benefits to as many Tanzanians as possible are prioritized.

Minimum levels of local content will increase the risk of fronting if they are too far out of sync with existing or potential local capacity.

Monitoring and enforcement

The draft local content policy and National Energy Policy envisage a monitoring and evaluation plan that is developed via a consultative process involving a range of stakeholders. This plan includes establishing the indicators by which local content performance by industry will be assessed. While Regulation 4(2)(d) charges PURA and EWURA with developing a monitoring and evaluation framework, it does not repeat the intention, set out in the policies, for multi-stakeholder consultations. The regulations also provide little additional detail on the framework itself.

However, a number of reporting requirements are set out in the regulations that will provide important information for monitoring and evaluation. Regulation 9 requires a licensee or contractor engaged in the sector to submit a local content plan for approval (and to submit additional such plans on an annual basis thereafter). This plan should cover employment and training, procurement of goods and services, technology transfer, and research and development for both licensees/contractors and their subcontractors. Regulations 31 and 33 require additional reporting on procurement. Companies are required to provide PURA or EWURA with details of their procurement process before procuring any good or service. (However, in contrast to the draft regulations, this requirement does not apply to “emergency procurement”). There are also requirements around reporting the actual use of local content: Regulation 34 requires the submission of an annual performance report covering all activities (which specifies, for example, actual employment of local labor and spending on local goods and services). In addition, a semi-annual report on employment and training activities that have been undertaken is required, as is a separate annual report on technology transfer.

Regulation 47 provides for fines or imprisonment for any person submitting false or misleading information, wrongly representing a local company, or involvement in tendering irregularities. Financial penalties are also given for non-compliance with the requirements set out in the regulations.

49 Jean Balouga. “Nigerian Local Content: Challenges and Prospects,” *International Association for Energy Economics* 4 (2012): 24, accessed 15 May, 2017, <https://www.iaee.org/en/publications/newsletterdl.aspx?id=176>; Section 3(2) of the Nigerian Oil and Gas Content Development Act 2010.

Develop a monitoring and evaluation plan

Robust monitoring and evaluation systems and processes are crucial for the effective implementation of a local content strategy—and are often a weakness in local content frameworks. Now that the regulations have been published, the development of the envisioned monitoring and evaluation plan is an important next step. Developing this plan in consultation with industry would ensure it is aligned with industry's own reporting mechanisms. Performance indicators will need to be unambiguously defined and aligned with the reporting metrics used in local content plans. This requires a standardized template for the local content plan to be set out in subsequent guidelines. We believe these plans should be published. Designing the template in a manner that is comprehensible to the public would make their publication even more useful.

Developing the monitoring and evaluation plan in consultation with industry would ensure it is aligned with industry's own reporting mechanisms.

Streamline reporting and approval requirements

The comprehensive reporting requirements set out in the regulations should facilitate effective monitoring and enforcement. However, while the government has rightly scaled back some reporting requirements since the draft regulations, a cost-benefit analysis may still be necessary to ensure that neither the compliance cost for industry nor the administrative burden for government outweigh the likely benefits.

Government approval of the procurement process for every contract represents a significant burden on government and industry and could have a considerable impact on operations. It takes 14 days for approval to be provided—sufficient time to disrupt operations and cause lost revenues for both the operator and government. Given these risks, there are benefits to only requiring approval for individual procurement processes if these processes differ from those provided for in the annual plan.⁵⁰

These comprehensive reporting requirements—in particular the need for approval from PURA or EWURA before some activities are undertaken—highlight the importance of these agencies having sufficient capacity to ensure operations are unaffected by delays. However, as noted below, capacitation of these agencies has to take into consideration the opportunity cost of using government's limited resources. Focusing on just a few key areas of local content would reduce resourcing requirements.

Institutional framework

While NEEC has responsibility over the government's local content strategy and leads the development, coordination and monitoring of local content in the economy, MEM has taken the lead thus far in the development of local content policy and legislation that specifically pertains to the gas sector. This was expected, as MEM is responsible for the gas sector; and yet it has resulted in the regulations only referring to the roles of MEM, PURA and EWURA, with no mention of a role for NEEC.

Ensure inter-agency coordination

The institutional framework will be a key determinant of the success of Tanzania's local content strategy. For the strategy to benefit the wider economy, its development and implementation needs to be coordinated across the government. As noted by Kinyondo and Villanger, MEM's strong ownership of local content may have resulted in excessive focus on technical areas specific to the gas sector that are likely to result in fewer linkages to other sectors.⁵¹ It is also not yet clear how the different institutions will coordinate and delineate roles and responsibilities.

⁵⁰ Paul, Tony. Interview by Thomas Scurfield. Phone interview. Tanzania, 22 April 2017.

⁵¹ Kinyondo and Villanger, *Local content requirements in the petroleum sector in Tanzania*, 6.

NEEC provides a crucial mechanism for coordination, but there is currently some ambiguity in its role in the current policy and legal framework. For example, Regulation 29 gives the Minister of Energy and Minerals the authority to change minimum local content levels with input from PURA and EWURA. The lack of involvement of NEEC in this process would risk that changes are made that do not align with the economy's wider local content strategy. It is important to clarify how these different institutions—and others that will be responsible for leading sector-specific programs (such as the ministries responsible for education, labor, agriculture, and industry and trade)—will coordinate and share responsibility for the development and implementation of local content initiatives.

NEEC provides a crucial coordination mechanism, but there is currently some ambiguity in its role.

Optimize administrative resources

Capacitating these institutions to implement an effective local content strategy is also important. However, as noted above, this needs to be informed by the need to utilize government's scarce resources efficiently and in areas that will have the greatest benefit. Resource rents are generally significantly larger than the economic value of any local content generated.⁵² Therefore we do not think it would be advisable for the capacitation of these institutions to come at the cost of less support to improving the capacity of, for example, the Tanzania Revenue Authority. Such trade-offs and the administrative capacity of these institutions to effectively monitor local content obligations will be key determinants of the optimal scope of the local content strategy.

Involvement of other stakeholders

Many stakeholders note that there has been insufficient consultation on gas legislation—and on local content strategy in particular—in recent years. Members of parliament were only given four days to review the Petroleum Act, the sector's central pillar of legislation. The consultation process for the regulations was more comprehensive, but, again, despite a range of stakeholders having significant concerns about its contents, stakeholders had only four days to review the “final” version before it was submitted to the minister.

Ensure a more inclusive, consultative approach

Multi-stakeholder consultations on policy and legislation that involve government, industry, non-governmental organizations and members of the public are crucial for improving knowledge and an understanding of conflicting positions. They also increase the opportunity for compromise and alignment of interests, which results in stronger buy-in and more effective implementation. Given that the local content strategy is a source of significant contention (with divergent views on the best approach), a more inclusive and consultative approach is all the more important.

One mechanism for improved dialogue and collaboration among stakeholders is the development of a national local content committee envisaged in the draft local content policy. This would be an independent body comprised of government, industry and nongovernmental organizations that is mandated to oversee the implementation of local content policies and laws. Collaborative exercises (such as the collection of baseline information) could also be overseen by this body. However, the body has yet to be established and has not even been mentioned in subsequent policies or legislation.

52 Silvana Tordo, Michael Warner, Osmel E. Manzano and Yahya Anouti. *Local Content Studies in the Oil and Gas Sector* (Washington D.C.: World Bank, 2013), xiii, accessed 15 May, 2017, <http://documents.worldbank.org/curated/en/549241468326687019/pdf/789940REVISED000Box377371B00PUBLIC0.pdf>.

Transparency

Following questions around the local content figures reported by mining companies, the Tanzania Extractive Industries Transparency Initiative began to collect local content data in 2013. The Tanzania Extractive Industries (Transparency and Accountability) Act 2015 requires companies to submit annual reports on local content and corporate social responsibility to an independent government entity established by the same act.⁵³ However, the act does not explicitly provide for the publication of these reports. Regulation 38—which allows the public to request information “designated as public records” they are “entitled to access”—is the only explicit transparency provision in the regulations.

Improve public access to information

Given the significant expectations of the benefits the gas sector will generate for citizens, transparency is not only crucial for accountability reasons but also for the management of expectations. Regulation 6(2) requires companies to make available “the local content procedures and obligations” on their websites. However, the regulations do not specify whether this means local content plans must be published in full, nor is the publication of local content reports mentioned. Regulation 38 neither specifies what information will be designated as “public records” nor what information a member of the public might be “entitled to access.” Therefore, the regulations do not provide full clarity on what kinds of information will be made publicly available.

As the regulations allow for local content obligations to be varied under Regulation 29 (and do not provide details on criteria for exemptions), a failure to publish these plans prevents the public from knowing what requirements have been imposed on companies; prevents the public from understanding whether companies are meeting the requirements; and prevents the public from knowing when to push for the monitoring of company compliance. We believe local content plans and reports should therefore be published online in publicly available, free formats. Publishing the database of suppliers (including their ownership details) online would also be useful. The government might also consider developing a communication strategy (as envisaged in the draft local content policy) for keeping the public updated on local content implementation, achievements and challenges.

The regulations do not provide clarity on what information will be made publicly available.

International trade agreements

World Trade Organization (WTO) agreements and bilateral investment treaties (BIT) often contain restrictions on local content requirements. However, the WTO General Agreement on Trade in Services currently only applies to the tourism and hotel sector in Tanzania. Similarly, as a Least Developed Country, Tanzania currently has some flexibility in how it complies with the WTO Agreement on Trade-Related Investment Measures which restricts the requirements that governments can impose around the use of local goods. This agreement will have a greater impact when Tanzania achieves middle-income status. Tanzania currently has 11 BITs in force, and eight others that have been signed but are not in force.⁵⁴ In an initial study of 11 of these agreements conducted by the Columbia Center on Sustainable Investment, only one—Canada’s—explicitly prohibits local content requirements.^{55,56}

53 Section 15 of the Tanzania Extractive Industries (Transparency and Accountability) Act 2015.

54 “International Investment Agreements Navigator,” UNCTAD, accessed 15 May, 2017, <http://investmentpolicyhub.unctad.org/IIA/CountryBits/222#iialnnerMenu>.

55 The BIT with Canada is very restrictive, prohibiting local content requirements from being imposed on any investor, not just Canadian ones.

56 CCSI, *Local Content: Tanzania* (2015), 18.

Align trade agreements with local content rules

The government could benefit from undertaking a comprehensive review of Tanzania's trade agreements, which would establish their impact on Tanzania's local content strategy. The Columbia study can provide a good starting point for this review, and the government or its advisors can review the outstanding eight agreements. Going forward, the government will also need to be cognizant of the potential impact of new agreements. Coordination between NEEC, MEM, the Ministry of Trade and Ministry of Foreign Affairs will therefore be crucial.

Conclusion and recommendations

Local content is an important component of a government's strategy for maximizing the benefits of a country's oil and gas sector. However, there are risks and trade-offs that any strategy should address. In our analysis of Tanzania's local content strategy for its emerging gas sector, we have indicated that adjustments are needed in a number of areas.

The government was sensible in setting out a comprehensive strategy while the sector is still at a nascent stage. This leaves time for further fine-tuning, as well as gives the government, gas companies and their contractors, and potential local providers of goods, services and labor sufficient time to plan. However, even at this early stage, it is still important to establish a strategy that is accepted by all stakeholders. Investment in the LNG project is still very uncertain and a poor global price outlook means that there will be significant obstacles to the project becoming commercially viable. Given that government revenue from the project is likely to be significantly larger than the economic value of any local content generated, it is important that this strategy does not distract from what we believe should be the government's main objective: securing investment while getting a fair share of revenues and then using them effectively. The government could use the period before the regulations come into full effect to review and refine them, ensuring that they are based on two key elements: impact and feasibility. This could include:

- *Reviewing the strategic direction for the local content strategy.* This would involve ensuring the strategy is aligned with the broader national development agenda and considering (initially) narrowing the scope of local content obligations to focus on a few strategic areas and transferable skills, goods and services.
- *Harmonizing and strengthening definitions of "local" companies, goods and services.* This would ensure that local content requirements maximize participation and in-country value addition. This may require considering amendments to the definitions included in the Petroleum Act 2015.
- *Prioritizing the collection of baseline information.* This information includes existing and potential local capacity and prospects for long-term demand. It could be used as a basis to revisit mandatory targets.
- *Prescribing the conditions upon which exemptions to requirements will be granted.* This would reduce the discretionary power of individuals or institutions, facilitate oversight and ensure that the regulations provide useful guidance to stakeholders.
- *Considering additional measures to reduce the risk of fronting and local elite capture.* These could include requiring local companies to own at least some of their capital; requiring beneficial ownership disclosure of suppliers registered on the supplier database; and prioritizing companies with majority Tanzanian management and employees, in addition to Tanzanian ownership.

- *Streamlining reporting and approval requirements.* This process would aim to establish requirements that facilitate effective monitoring but do not involve a compliance cost for industry or an administrative burden for government that will outweigh the likely benefits.
- *Further developing mechanisms for interagency coordination.* This could include a clearer role for NEEC and would take into account institutional capacity needs and the allocation of the government's scarce resources when determining the optimal scope of the local content requirements.
- *Ensuring an inclusive, consultative approach to local content strategy development and implementation.* E.g., through establishing a multi-stakeholder national local content committee.
- *Improving provisions for public access to information and benchmarking.* This could include setting out the conditions upon which exemptions to requirements will be granted and publishing local content plans and reports online.

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