CHATHAM HOUSE
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National Seminar for Tanzania

An event of the New Petroleum Producers Discussion Group

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Introduction

The New Petroleum Producers Discussion Group[1] facilitated a discussion between the main stakeholders of Tanzania's petroleum sector at a roundtable with representatives of 10 emerging producer countries. The seminar, which took place in Dar es Salaam on 2 July 2015, was co-organized by the Tanzania Petroleum Development Corporation (TPDC) and the Uongozi Institute.[2] Discussions were under the Chatham House Rule, which allows participants to use the information learned at the meeting but does not permit attribution to speakers or their organizations.

The national seminar was held against a backdrop of intense debate in the parliament, which at the time was reviewing three bills affecting the petroleum sector: the Petroleum Act, the Oil and Gas Revenue Management Act and the Tanzania Extractive Industries Act. All three were enacted shortly thereafter, but the outcome of this legislative process was unclear at the time the seminar was held. Overseas participants in the seminar did not challenge the content or purpose of these bills, but focused instead on potential implementation challenges. All participants drew from the experiences of other emerging producers around the table, which allowed these challenges to be put into a broader context.

The morning session of the seminar was an intra-governmental discussion focusing on how the reform of governance if the petroleum sector would change TPDC's role and sources of finance, as well as on what the prospects were for the establishment of an independent regulator. The discussions did not go into the details of the reform being debated in the parliament or the specific roles that TPDC will be expected to play. Rather, the participants discussed the common challenges that face emerging producers in defining the role of the national oil company (NOC), in financing that role and in establishing a new regulator in countries where the NOC has plays a lead part in overseeing the sector.

The role of the NOC

The research carried out by the New Petroleum Producers Discussion Group project on the basis of the experience of NOCs in emerging producer countries shows that their roles evolve with the geology:[3]

i) Stage 1: Pre-commercial discovery
ii) Stage 2: Post-discovery, pre-production
iii) Stage 3: Early production or small resource base
iv) Stage 4: Large or long-term production

As countries progress from exploration in Stage 1 to discoveries in Stage 2 and, especially, to production in Stage 3, the NOC commonly relinquishes, or is forced to relinquish, its regulatory responsibilities (that is, its governance role). A key learning point that emerged from the analysis of how NOC roles and finances evolve through these stages was that **an NOC with a governance role carries a much heavier workload** than an NOC without such a role.[4] In several cases cited, including those of Liberia

[1] This project is a collaborative effort between Chatham House, the Natural Resource Governance Institute, the Commonwealth Secretariat, the Africa Governance Initiative and the World Bank with the support of the UK Foreign & Commonwealth Office's Africa Prosperity Fund and Shell. These summary notes were edited by Valérie Marcel, a Chatham House associate fellow and the project lead on the New Petroleum Producers Discussion Group, based on notes taken by several participants at the seminar.
[2] Further details about the Uongozi Institute: Institute of African Leadership for Sustainable Development can be found online at http://uongozi.or.tz/.
[3] A paper detailing this research will be published on the project website: http://www.chathamhouse.org/about/structure/eer-department/new-petroleum-producers-discussion-group-project. The editor has also published an interim paper for the KPMG Energy Institute, available at http://www.kpmg.com/global/en/issuesandinsights/articlespublications/africa-nocs/pages/unlocking-potential-africas-nocs.aspx.
[4] This is not always the case. Suriname's NOC, Staatsolie, has a workforce of 960, while the team responsible for its governance role is composed of just eight people. Limiting the size of this department was a deliberate company strategy.

and Ghana, the budget and workforce of an NOC moving from a governance to a commercial role were both cut by three-quarters. Sometimes, NOCs retain only part of the governance role in the wake of reform. For example, some will continue to play an advisory role vis-à-vis government. Similarly, the responsibility for collecting, managing and promoting geological data is a governance duty that some NOCs retain despite ceding their broader governance role.

Responsibility for data management is often fought over by the ministry/new regulator and the NOC because it offers:

- Better opportunities for capacity-building in geosciences;
- An intimate understanding of the national natural-resource base, which is crucial for subsequent power relations;
- The chance to become the early-stage interlocutor of oil-company partners; and
- The possibility of earning substantial revenues through the promotion of data (together with upstream payments from operators, such income often accounts for two-thirds of the revenues of emerging producer NOCs in Stages 1 and 2).

A participant acknowledged that it was difficult for TPDC to relinquish responsibility for data management. As another official conceded, a general lesson is that, 'You go until someone stops you.' Part of the reason why NOCs with a governance role seek to continue in that capacity is concern that no other agency is as capable as they are. Indeed, one participant worried that the new Tanzanian regulator would not have the expertise to 'know the quality of the acreage' it will be licensing.

Some emerging producers highlighted the obstacles that obstruct the transfer of regulatory responsibilities from the NOC to a newly established regulator. For example, an NOC that has been responsible for some time for both the licensing and monitoring of operators foresaw a growing risk of conflict of interests as it monitors activities in which has a vested interest. Although it was (almost) ready to transfer those responsibilities to the state, the main obstacle was lack of capacity: '[We have] weak institutions, weak analysis, weak staffing and funding, weak control and a weak sense of direction.' At the same time, there was a sense, echoed by other countries, that **political control over the licensing and monitoring functions posed a threat to technical expertise**.

In Kenya – much like in Ghana before the 2012 reform – the NOC has been responsible for overseeing operations and work programmes as well as for marketing the country's acreage. But the Ministry of Energy has never explicitly defined its role, as a result of which there has been some conflict between the NOC and the ministry. The former has since decided to abandon those responsibilities but is fighting to keep the data; currently, it is investing in the country's seismic centre to add value to the data.

A participant from an emerging producer (in which the regulator/ministry has always been responsible for data management and other governance roles) said it is important for Tanzania to clarify whether oil companies are to report to TPDC or the new regulator.

Finance

Another key learning point from the New Petroleum Producers Discussion Group project's comparison of cases was that **in both Stages 1 and 2, NOCs struggle to secure reliable and sufficient sources of finance** because the country is not yet producing oil or gas. NOCs usually rely on government funding, revenues from a fuel import mandate or a levy on product sales, as well as data sales and payments from operators. NOCAL, the NOC in Liberia, has succeeded in generating relatively large revenues from signature bonuses, but most other NOCs have not. Such payments fluctuate with exploration activity and are particularly difficult to secure in a low-price environment. Most NOC revenues in the pre-production stage are unreliable, which not only keeps company ambitions in check but also limits the ability to forward plan. Post-discovery, NOCs are better able to raise money on the open market, which empowers them but puts the government at risk through the debt raised.

TPDC's access to finance was cause for concern among some Tanzanian participants, who explained that the NOC had relied on budget allocations and relatively insignificant operator fees. Generally, it has received less than it has requested and the timing of the allocations has been a challenge for operational expenditure. While the recent legislative reform provides for essentially the same financial model, it does stipulate that funds equivalent to 0.1 per cent of GDP be ring-fenced annually into a revenue savings account of a new oil and gas fund for TPDC's strategic investments.[5] One Tanzanian participant commented: 'When this is passed, we hope TPDC will have a new face. It will be allowed access to blocks and to partner with strategic partners.'

There was interest around the table in the various financial models adopted by NOCs and their pros and cons. For countries in Stage 3 (that is, with early production or a small resource base), the basic models are:

- All revenues go into a consolidated fund;
- The NOC retains a predetermined part of the revenues; and
- The NOC retains all revenues but pays taxes and dividends to the state

Staastolie from Suriname, for example, pays taxes and dividend and acts like a normal company borrowing funds on the international market. This is generally the financial model preferred by NOCs because it allows 'greater predictability and autonomy', as one participant from a new NOC put it.

Ghana's model is a cross between the first and second basic models. All revenues go to a petroleum holding fund. The government pays GNPC's costs and (at its discretion) allocates to the company a share of the revenues of between 30 per cent and 50 per cent. GNPC's finances have been hard hit by low oil prices and a smaller share of transfers from the petroleum fund. In addition, the low oil prices have reduced the NOC's capacity to borrow money to meet its strategic plans to develop into an operator and to fund its national gas aggregation programme.

Capacity

Another strong theme of the discussions was the commercial focus of NOCs and understanding what that focus entails. A participant from an NOC that had recently lost its governance role said: 'We are looking to be something different. [Our company] is not the burial ground for former political figures!' The participant went on to describe what was evidently a bloated company: 'It took the fall in oil prices to awaken us to the fact that we need to be better planners.' An austerity plan is now in place to keep costs in check.

Kenya's NOC has well-established downstream activities but is quite new to the upstream. In order to build technical skills, it has developed a training programme and relies on the transfer of skills from oil-company partners and opportunities to 'learn by doing'.

5 The bill that has since been approved introduces conditions that make it more difficult both to grow the revenue savings account and to access it. The final version of the draft law was not available at the time of writing.

One adviser cautioned against focusing too much on the training budget, suggesting a **strategic approach to the development of skills** was more important. The following can guide the skills development, in line with the NOC/regulator's strategic plan:

- Determine the skills already acquired and the skills still required at the current stage of development of the resource;
- Identify training and secondment programmes with international oil companies that teach the required skills; and
- Focus on how to apply the newly acquired skills.

There was a great deal of interest around the table about how to build both the 'commercial capacity' of the NOC and the technical capacity of the regulatory agency. The discussions focused on the **salary structure that is required to attract and retain talent** – especially at a newly established regulator. One adviser said producers should be weary of the Norwegian example – the regulator spent much of its resources on training to ensure excellent staff, only to have them poached by competitors: 'You don't want to become a training ground for international oil companies.' For that not to happen, regulators need to be exempt from the rules that govern salaries in the civil service.

When it was establishing a new regulator, Kenya took into account three important factors:

- *Regulatory*: To promote the independence of the board of the regulatory agency, competitive recruitment was introduced, clear rules established and procedures for nominating and removing its members drawn up.
- *Financial independence*: The regulator is to have independent sources of finance, notably from levies (there was some discussion about the benefits and risks of regulators being paid by the companies regulated by them).
- *Accountability*: The regulator is to be subject to auditor scrutiny (a point that was deemed important by one participant who felt that some countries, including Trinidad and Tobago, had lacked the commitment to holding regulators to account for their performance). Moreover, a code of conduct has been introduced for staff and board members whereby they are prohibited from being employed by any company regulated by them for at least 18 months after they leave regulator.

Tanzania's conclusions about roles, capacity and finance

The Tanzanian participants concluded the morning discussion by highlighting the following:

- Institutional frameworks for managing the petroleum sector evolve with the resource base: 'Mistakes will be made but we have to learn to adapt'. To navigate this change, clear roles and responsibilities are required for all players in the sector, in particular the NOC, the regulator and the government.
- The case of Ghana –where the NOC is pursuing an accelerated growth strategy – is interesting and points to the need to empower the NOC to allow it to develop. For optimal growth, sufficient capitalization is required. By contrast, another participant noted that if financing NOCs in emerging producer countries is a challenge, especially at a time of low oil prices, those companies should consider adjusting their expectations.
- The discussion about financial and professional independence gave one participant new hope that an independent regulator can be established: 'That independence would give

> comfort to staff in taking decisions which might not have favourable impacts for government but which are the right decisions none the less.'

Opening up the discussion

The afternoon session was opened up to include oil and gas companies active in Tanzania and a broader civil society representation, including research centres. The purpose of the discussion was to expose various stakeholders in Tanzania to current thinking about the outlook for the oil and gas industry with the aim of ensuring that discussions about the Tanzania National Gas Utilization Master Plan were based on a realistic view of the broader industry and market environment. At the same time, the intention was to help give a focus to public relations efforts related to the future of gas in Tanzania.

Prospects for investment

At (and on the sidelines of) the meeting, Tanzanian officials, TPDC and representatives of the gas companies explained what each expected the other to do to move the liquefied natural gas (LNG) project forward. However, it seemed that more trust was required for those messages to be heard. On the Tanzanian side, there was an expectation that the companies should push ahead with making their final investment decision (FID). The companies noted that they require various fiscal, legislative and regulatory guarantees in order to increase the predictability of the terms and conditions of investment. One participant noted that the 'FID would be in four years … if we start to do things today [to prepare for that decision]. We have the concept. We still lack progress on the negotiation side and on the market.'

With regard to the market environment, an oil and gas company highlighted the fact that there are numerous LNG projects competing for LNG demand post-2020: 'Cost competitiveness and the pace of development will determine which projects proceed.'

Current market conditions are not very favourable for investment. An independent analyst foresaw **multiple drivers for a lower oil price environment for quite some time** (US$70 per barrel and volatility). Companies will be more cautious over a relatively long time horizon and will look for low-risk prospects offering good geology, good terms and good governance. Another important factor is the robustness of the project.

One participant from an African emerging producer country argued that **public support of government policy was an important draw for investors**. In the run-up to its most recent licensing round, this country 'had 162 national consultations just to write one policy. Demonstrating that you have citizen consensus is very important to how you attract world-class players.' The same participant noted that the combination of favourable geology and good marketing had helped make the country attractive in a context of low oil prices.

Managing expectations

Investor caution and market conditions mean that the FID is being delayed on many projects throughout the world. **Managing both public and political expectations** in this context is critical. The discussion focused on the tendency of politicians to promise the perhaps unattainable. Civil servants noted that they were concerned about communicating with communities in a timely manner – i.e. before politicians had a chance to do so. But one Tanzanian academic pointed out that one reason why politicians give out wrong information is that they are not in possession of the right information. Efforts were needed to ensure that they are better informed.

- Experts in community engagement from Tanzania and another African emerging producer explained what communities (and politicians) need to know:
- How a certain development will affect them;
- What the positive and negative impacts over the course of the project will be – and what mitigation measures are in place;
- At what stage of development the resource is;
- What the difference is between resources and reserves ('Tanzania may have a resource base of 58bcf but this doesn't tell us anything about the commerciality of the reserve – this should be simplified in a way citizens can understand');
- What the important dates are (for the FID, starting production, etc.);
- That revenues to government and project windfalls will take a long time to be forthcoming – even after production starts, companies will need to recoup their investment;
- That local content in the petroleum sector is not like that in the mining sector – far fewer low-skilled jobs will be available (thus potential producers need be specific about what the provision for local content is); and
- What the industry standards for goods and services are (local companies are missing opportunities to supply industry because they are not well informed about industry requirements).

All this information should be provided in a clear and timely manner with a view to moderating expectations, not inflating them. One participant noted that there is more information available now than at any time previously and yet people are still dissatisfied about the quality of information, especially that from government. He went on to ask whether 'this was about more than communicating?'

Tanzania's concluding remarks on the gas debate

At the end of the discussion, each Tanzanian participant had the opportunity to state what learning was gained. An important point made by one Tanzanian participant was that the development of offshore gas resources cannot be guaranteed, especially in current market conditions. Many steps are required to make the FID and then to effectively leverage the development of gas resources to increase industrial and economic activity. **A strategic approach is required to bring the pieces of the puzzle together**.

For some participants, the meeting had improved their understanding of some key issues and revealed some misperceptions. While the Ministry of Labour had hoped that gas development would result in a lot of new jobs, it became clear that would not be the case because 'there are differences between the mining and gas sector.' Another participant commented that 'we still have a long way to go' to have gas onshore or LNG exports. In fact, one participant expressed mock depressive thoughts after presentations highlighting the obstacles that the country faces in developing its gas resources.

'We were ready to reap the fruits of gas but discovered through this seminar that it is very expensive,' another participant commented. Indeed, the meeting highlighted how expensive offshore dry gas (non-associated gas) is compared with associated gas. With regard to that point, an independent expert on gas and local content emphasized that it is up to the government and the nation to determine what the value of their resource is. They need to **evaluate the trade-offs of allocating gas for domestic use and export**.

Another government participant highlighted that Tanzanians must realize that 'you can't have a gas economy without exporting gas'. In other words, LNG exports are the only way to incentivize gas companies to develop the reserves found offshore. The companies are in agreement that a share must go to the domestic market, but the sale of that share is not profitable enough to warrant the development of the gas discovered. For Tanzania, the value of the domestic use of gas is that it supports economic development. The profits generated through LNG exports can underwrite some of the costs of developing infrastructure and education as well as the provision of gas as a low-cost feedstock to industry and consumers. But **revenues from export sales will not pay for everything and political commitment is required to fund large-scale development projects and education.**

A national strategic vision

There appeared to be a sense among participants that **time and space are needed for Tanzania to work towards developing a long-term strategic vision** for the petroleum sector. A participant from an established producer country that had elaborated a national strategic vision pointed out that the strategy should be determined by informed analysis of the resource base, the current national industrial base and the country situation. That process involves both consultation and coordination.

Representatives of a large number of state institutions admitted there is insufficient communication between the various bodies and recognized the importance of improved information flows and better policymaking coordination. One participant noted that, ‘We still have challenges in reaching out to colleagues in other institutions’ and suggested there would be **benefits from a government retreat or similar gathering at which participants could learn from one another and develop a coordinated strategy**. Another participant suggested that ‘the government needs to work hard to build links between stakeholders’ that would be supported by a strategy for intra-governmental communication.

Some participants pointed to the benefits of a **collaborative approach between environmental agencies and TPDC**. One noted that the National Environment Management Council had a programme to communicate with the public about the national impact of the country’s gas resources and that it would benefit from TPDC’s input about the technical and commercial details of the LNG project.

A civil society representative argued that beyond government coordination and communication, Tanzania needed a vision – something that it could communicate to the public. It should consider and debate how the benefits of the resource will be distributed: ‘Someone has to start articulating this and telling the citizens.’ From there, it should proceed to build consensus around this vision. ‘But stating the vision is not enough – you have to implement it.’

Conclusion

The national seminar exposed Tanzanian stakeholders to a broad range of other emerging producers’ international experience. It offered neither solutions nor clear policy advice nor specific policy direction. Rather, it provided wide-ranging examples of how practice has been applied and tested in other emerging producer countries. It is now up to Tanzanians to reflect on what policy direction is appropriate in their own national context.