

## WHY IS THE PETROLEUM INDUSTRY SO BAD AT SUPPORTING AFRICAN DEVELOPMENT

### A Case Study of Oil and Gas Extraction in Tanzania

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#### SYNOPSIS

Over the past decade, petroleum resources have become a crucial area for mobilizing domestic resources. Tanzania, for example, has put in place strategies on natural gas so that its derivatives can become key drivers in the nation's objectives to becoming a middle-income nation, as iterated in Tanzania Vision 2025. This study evaluates some of the issues of petroleum exploration and production and trade in Africa, more specifically: gas industry reform in Tanzania, good governance, and the current capacities of institutions and technical experts to handle the arriving behemoth.

**Key findings.** Studies found that the majority of people felt uncomfortable about how natural resources are managed in Tanzania and were concerned about access to reliable information on governance and policies related to extraction. The public does not have, in fact, access to information on the magnitude of and revenues from the nation's natural resources: the mining companies have been and are the only gatekeepers of such information and there is no mechanism to verify the veracity of the information provided to the country. Further, the insufficient capacity of national institutions to address the challenges related to the oil and gas industry has contributed to the ineffectiveness of the government in supervising the operations and foreign direct investments in the industry.

**Key lessons.** By virtue of its size and enormous resources for investment, extractives industry can easily overwhelm a developing country that has not previously built its own internal capacity. This requires foresight, investment, and political will – and the determination to do everything possible to eliminate corruption in the whole extraction sector. It is also important for any country to diversify its economy to avoid an imbalanced reliance on any single extractive industry, especially one that can be as volatile as oil and gas.

**Key recommendations.** The government should give consideration to hiring its own foreign expertise to help develop the capacity needed through a comprehensive approach that includes advising; helping negotiate with the major industry players; and designing a full package of regulatory and control mechanisms that will help Tanzania operate on a level playing field in order to build a strong industry to serve the nation. African Capacity Building Foundation should develop programs to enhance the capacity of nationals, so that within a prescribed, reasonable time-frame African people can manage and fully control the exploitation of their natural resources.

#### Introduction

It is Tanzania's hope that natural gas will be a key contributor to the drive toward becoming a middle-income nation, as stated in the Tanzania Vision 2025

and Five-year Plan, 2013–18 (URT 2014). The potential benefits of a strong gas industry to socioeconomic development are well integrated into the gas policy (URT 2013). Further, oil and gas

development is one of the key resource mobilization areas in Big Results Now! (BRN). Now, BRN intends to eliminate implementation bottlenecks and install a new working culture to realize the nation's development goals (URT 2015). With estimated gas reserves of more than 55 trillion cubic feet, Tanzania is expected to join the regional and global gas economy (Katunzi and Siebert 2015). Unsurprisingly, multinational oil companies are engaged with the government in exploring natural gas and oil, off- and onshore (Katunzi and Siebert 2015).

But large questions remain. For example, to what extent is the government ready to engage with citizens and key stakeholders in the petroleum industry to ensure that the livelihoods of people and the national economy are placed first in the development of what may be an enormous resource? How many of the data on these resources are available and shared with the government to ensure that the resources can be used in the interest of the nation? How are local experts and specialized institutions used by, and serve the interests of, the government rather than multinational companies?

These are critical questions, for the oil industry has vast resources on which it can draw to challenge much less well financed governments. The playing field is far from level, so the government should plan well in advance and draw on all national domestic resources it can muster to try to adjust the imbalance. This is not to suggest a confrontational stance (though that should not be backed away from if it is necessary) but there should be an enhanced sense of awareness of the significant challenges.

Starting with a systematic review of reports and studies, this study evaluates some of the issues of petroleum exploration and production and trade in Africa, more specifically: gas industry reform in Tanzania, stakeholder and public engagement there, good governance, and the current capacities of institutions and technical experts to handle the arriving behemoth.

### Too little stakeholder involvement

Already the discovery of gas and oil in Tanzania has sparked conflict between lawmakers and the community members they purport to serve. Although the Mnazi Bay gas extraction site in Mtwara was discovered in 1982, it only went commercial in the 2000s (Kibendela 2013). The 2013 announcement that the Chinese government would construct a 532 km gas pipeline from Mnazi Bay to Dar es Salaam raised concerns among local stakeholders, including the public, over the link between gas extraction and the locals' improved livelihoods. National stakeholders were unclear how the Mtwara extraction would contribute to the economy (Kamndaya and Mugarula 2013). According to Hamis (2013), there was also external pressure with growing concern in western countries about growing Chinese investments in the gas-rich countries in Africa.

The government's initial response to a riot that broke out in Mtwara on May 22, 2013 was not to initiate dialogue but to order the police to break it up. The army was deployed to patrol the streets and the Tanzania People's Defense Force had to return the city to normality (Katunzi and Siebert 2015).

One of the major underlying factors in the chaos in Mtwara was political rivalry between the ruling and opposition parties (Katunzi and Siebert 2015). However, Domasa (2013) indicated that Members of Parliament from both sides of the political divide supported the actions taken by the citizens of Mtwara. The National Assembly even formed a bipartisan committee to investigate the matter, and came up with short- and long-term solutions (Bakari and Kamndaya 2013). This committee pointed out that the agitation at the grassroots level and the concern from other stakeholders was not a matter of opposition to the project—rather, citizens were raising their voices to take responsibility and demand information, transparency, their rights as citizens, and accountability from government officials.

Domasa (2013) also suggested that stakeholders' feelings were magnified because the government

had failed to engage with local people over land and gas issues, or to educate them in the impacts and benefits the industry could bring. Further, Domasa (2013) emphasized that the Mtwara conflict could have been mitigated if the government had properly engaged with leaders of political parties, development partners, and civic organizations on their roles as key stakeholders, and if it had involved them in developing mechanisms to safeguard accountability and transparency to ensure that gas extraction would be in the public interest.

Conflict over gas and mining resources is not a challenge for Tanzania alone. The lack of public engagement has been a major obstacle to effective use of oil and gas resources and has been at the root of political turmoil throughout Africa. In the Niger Delta for example, the discovery of oil was a contributing factor to the Nigerian civil war (6 July 1967 – 15 January 1970). A secessionist movement flourished in Angola over the oil-rich area of the Cabinda region. Recently, an oil resource was a main source of conflict in the Khartoum-Juba conflict, and this led to the border line between South and Northern Sudan (Katunzi and Siebert 2015). Darby (2010), studying the transparency index on natural resources in various countries in Africa showed that corruption and mismanagement of natural resources have led to slower economic growth in countries more dependent on natural resources than in those that rely less on them. In fact, this “resource curse” in countries with a wealth of natural resources often widens the gap between the majority poor and the few rich, and often intensifies political rivalries.

### Challenges of good governance and transparency

In their analysis of how the public views natural resources such as oil, gas, and mining, Katunzi and Siebert (2015) found that the majority of people surveyed in telephone interviews felt uncomfortable about how natural resources are managed in Tanzania. Respondents also remained pessimistic that the opening up of a petroleum industry would improve the quality of daily life for most citizens. What most respondents were concerned about was

access to reliable information on governance and policies related to extraction, what profits were being taken and by whom, accountability, and how the government was using such benefits for socioeconomic development to improve the lives of the majority (rather than once more simply lining the pockets of the few).

Previous studies correlate with this more recent survey of the public’s view, which is not surprising, as mismanagement of natural resources is not unknown in Tanzania. Since the 1980s, the public has experienced opacity, mediocrity, impunity, and corruption of mineral resources at the hands of senior government executives (Darby 2010). There is a very good reason that the public does not have access to information on the magnitude of and revenues from the nation’s natural resources: the mining companies have been and are the only gatekeepers of such information and there is no mechanism to verify the veracity of the information they pass on (Tanzania Minerals Audit Agency 2014).

In 2009, Tanzania joined the Extractive Industries Transparency Initiatives (EITI) and in 2011 the Open Government Partnership (OGP). Both organizations require that all members commit to freedom of information, open data, and transparency in regard to the budget, lands, and extractive industries. EITI and OGP members are also required to disclose and reconcile all revenues from their extractive sectors and be open, accountable, and responsive to citizens. Although Tanzania has ratified EITI requirements on transparency, the major challenge is to integrate those undertakings into national policies so that they can be properly implemented (Hardoon 2012). How well this is going may be measured by a study conducted by the Global Corruption Barometer, which indicated that 56 percent of respondents from the mine and gas extraction sectors in Tanzania admitted that they had given a bribe to one or more “public servants,” including officials, political parties, religious leaders, leaders of civil society organizations, and the media (Katunzi and Siebert 2015: 179).

In 2010 Tanzania joined Publish What You Pay, a civil society organization global network that demands that each member country maintain a high level of transparency and accountability for its extractive industries. Tanzania's membership was suspended in 2015 following its failure to comply with governance and membership conditions (PWYP 2015).

### Limited institutional and human capacities

A 2014 International Monetary Fund report projected that if physical infrastructure was enhanced and regulatory frameworks adequately implemented and managed, Tanzania could reap \$3 billion to \$6 billion from gas production (Katunzi and Siebert 2015: 179). This estimate corresponds with a recent projection by the Dubai-based Dodsal Energy Group of an onshore gas discovery in Ruu Basin. Their report projects the value of that gas at \$11 billion when the project is completed in 2018. However, there is insufficient human and institutional capacity for such a leap from the current status to a fully-fledged successful gas business.

For the latest gas extraction project, profits are divided between the company and the government, 50–50. But according to Boma (2013), the legal instruments, such as production-sharing agreements and the licensing regime provide blanket cover to foreign companies preventing the government from accessing the true operational costs.

As most local experts have not yet developed the skills to track the performance of foreign energy companies, for the most part the government relies on information provided by foreign experts or employees of the operating companies. Hellevik et al. (2014: 39) mapped the skill sets required for the petroleum industry, focusing on gas extraction at Mtwara. His finding that Tanzania has only a few professional and technical experts with a good understanding of the petroleum industry was no surprise.

Katunzi and Siebert (2015), while agreeing that human capacity at the technical and professional levels is inadequate, argue that the main problem is

low pay and low morale on the part of most local experts; this is the same problem faced in other public sectors. Katunzi and Siebert further assert that experts and professionals in the petroleum industry are infected by the culture of corruption that tarnishes the image of the entire natural resources sector in Tanzania.

With foreign companies bringing into the country the most highly experienced technical and institutional experts, as well as the most sophisticated technology, there is a serious mismatch between them and the locals. A gap of such size inevitably creates a capacity vacuum that makes it extremely difficult, if not impossible, for nationals to take ownership of the process of gas production. Further, the insufficient capacity of national institutions to address the challenges related to the oil and gas industry has contributed to the government becoming ineffective in supervising the operations and foreign direct investment in the industry (Warner 2012).

According to Warner (2012), established national policies and operational procedures do not match the country's capacity. For example, the local private sector cannot meet the requirements of the 2004 Public Procurement Act and its 2005 supplement and implementing regulations. He further argues that current law offers little guidance on rules for sourcing from domestic suppliers, developing the industrial skills base, building local supplier capacity, or investing in infrastructure and research and development. "The low-level of domestic capability in Tanzania means that very few suppliers would pass the technical requirements in a tender and thus be eligible for a price advantage. Additionally . . . domestic-only restricted tender lists would be unlikely to emerge for services or equipment that were unavailable in Tanzania" (Warner 2012: 3). If this is an accurate assessment, it is likely that the government will continue to count on foreign expertise and institutions rather than on its own experts.

## Observations

The oil and gas industry can be alluring, especially for developing nations with major “visions” and few other resources. But as recent events in Tanzania and worldwide have shown, it can turn volatile almost without notice, with disastrous results for any economy that has tied itself to the industry.

Even when things are going well, because of its size and enormous resources for investment, the industry can overwhelm a developing country that has not built its own internal capacity. This requires foresight, investment, and political will—and the determination to do everything possible to eliminate corruption in the whole extraction sector. Incentives must be brought to levels commensurate with the skills of those being given the responsibility of exercising control over the nation’s natural resources to ensure they are used to the benefit of all citizens. This does not mean adoption of socialist policies or of confrontation with the industry, but will only be possible if the essential capacities are developed.

## Lessons learned

- It is important for any country to diversify its economy to avoid an imbalanced reliance on any single extractive industry, especially one that can be as volatile as oil and gas.
- It is critical to engage citizens (stakeholders) at national and subnational levels to ensure that all socioeconomic development initiatives related to resource extraction will be positive and effective. People no longer appreciate being told what to do; increasingly the public wants to be involved in meaningful dialogue about new initiatives, especially if these may incur risks. They also want to know about potential problems in advance and to be able to participate in decision making and responsibility.
- For the petroleum industry to become a real contributor to the economic and social development of Tanzania, there must be skilled and committed African experts dedicated to implementing policies and regulatory systems

crafted to this end. Capacity development must be mainstreamed throughout the education system, and delivered through every means, including apprenticeship programs and on-the-job training.

- Because national capacity is starting from a point of weakness, the government should give consideration to hiring its own foreign expertise to help develop the capacity needed through a comprehensive approach that includes advising; helping negotiate with the major industry players; and designing a full package of regulatory and control mechanisms that will help Tanzania operate on a level playing field to build a strong industry to serve the nation and its partners in extraction. The centerpiece of any such initiative must be a program to develop the capacity of nationals, so that within a prescribed, reasonable time-frame the Tanzanian industry will begin to be managed and fully controlled by Tanzanians dedicated to ensuring that it is run free of corruption.
- With so much money rolling around the extractive industries it is a major challenge to reduce corruption to a manageable level and push as much of the money generated as possible into supporting true national growth objectives. To this end, the government’s primary role should be to set up proper regulatory and control mechanisms to mainstream oil and gas revenue into national budget systems and to empower key public and private national stakeholders to participate as fully as their capacity allows.
- Information sharing on policies and benefits related to natural resource development is essential. Effective communications strategies must be developed.
- Also critical is the availability of financial capacity for the local private sector to participate and invest in the local infrastructure required to support new extraction.

- The government should build its reputation and develop goodwill with—and forestall hostility from—the public by involving and educating people living near any proposed gas plant or any other extractive facility on what the impact will be. It is vital that locals fully understand the changes that may affect their lives.
- It is equally important to educate policymakers to recognize how local-content policies may affect other petroleum policies and directives, so that they understand the regulatory boundaries between the upstream and downstream sides of the industry and that they recognize the potential trade-offs between local content, commercial interests, inward investment, and national revenues.

### **Policy messages**

- Think long-term, recognizing that while the oil and gas industry can bring significant financial benefits it can also be destabilizing. Witness, for example, the highly disruptive impact on developed and developing nations by the fall of oil prices in 2015–16. Wisdom should dictate that a “rainy day” stabilization fund be established from the moment revenues start to flow to help the country benefit from windfall revenues and guard against disastrous volatility. Many governments promise to do this, but very few follow through; it would greatly benefit Tanzania and other African countries to resist the temptation to spend the windfall recklessly and to save a reasonable proportion of the revenues from extractive industries to use when volatility strikes, as it surely will.
- Make explicit in every extractive policy or in the production-sharing agreement that those living close to oil/gas or any other mineral extraction site are prioritized for preferential employment opportunities, training, and the right to supply goods and services.

- Establish a knowledge-transfer policy to ensure that experts from abroad leave their knowledge of the petroleum industry in the country.
- Emphasize national ownership of supplier firms, requiring all suppliers to be tax registered in Tanzania and to demonstrate that they are decently employing and advancing the careers of Tanzanian citizens. It is essential to widen the obligations of investors and operators to move from simply using more available national labor and suppliers, to making a long-term contribution to develop the capacity of the national labor force, domestic suppliers, and (where appropriate) public institutions.
- The commission for higher education should provide guidance to support academia to develop new curricula that will help meet the emerging needs of the petroleum industry.

### **Conclusions**

Oil and gas extraction has the capacity to support the national development vision. However, in Tanzania the level of industrial capacity required to service the petroleum exploration industry is extremely low. In addition, the exploitation of these domestic resources is held back by accountability and transparency issues and by inadequate public and stakeholder engagement. Foreign investment in mining is effectively an enclave of human, institutional, and technological capacity that generates few backward linkages, and leaves less than optimal capacity to develop a national labor force or a supplier industry capable of participating in investment.

To take full advantage of the potential of the oil and gas industry, it is critical that a strategy be put in place to develop a full range of new capacity—technical experts, policymakers, key stakeholders including citizens, the private sector, labor, and academia. The strategy will require heavy investment, which in turn will require commitment

and political will. But the choice is clear: either act to create an environment under government control or leave it to the industry to set the terms and operate as extractive industries in the past have done. The preference should be to create an enabling environment that attracts investment in oil and gas, and fosters and serves the public interest.

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