

25 September 2026



No Depreciation Allowed for Exploration Companies

- Court requires assets to be owned and actually used in the production of income
- Depreciation allowance not deductible for exploration capital expenditure
- Pre-production capital expenditure not eligible for depreciation allowance
- Court's decision inconsistent with global treatment of depreciation allowance in the extractives
- Decision prompts critical questions on the timing of capital recovery in the extractive sector

Background

The Court of Appeal of Tanzania (the Court) has delivered its judgment in Civil Appeal No. 08A of 2025, concerning the deductibility of depreciation on petroleum exploration expenditure incurred during the pre-production stage. The Taxpayer was engaged in petroleum exploration under a Production Sharing Agreement and had incurred substantial expenditure on exploration and development activities. Following an audit, the Tanzania Revenue Authority (TRA) disallowed depreciation claimed on the expenditure on the basis that the project remained at the pre-production stage and the relevant assets had not been employed in the production of income.

Both the Tax Revenue Appeals Board (the Board) and the Tax Revenue Appeals Tribunal (the Tribunal) held in favour of the Taxpayer. They considered paragraph 1(3) of the Third Schedule to the Income Tax Act (the ITA) to specifically treat expenditure incurred on natural resource prospecting, exploration and development as expenditure incurred in acquiring an asset used in the production of income. The TRA appealed to the Court of Appeal.

Decision of the Court

In its decision, the Court allowed TRA's appeal, holding that section 17 of the ITA requires a depreciable asset to be both owned and employed wholly and exclusively in the production of income before depreciation may be claimed. According to the Court, paragraph 1(3) of the Third Schedule does not dispense with that requirement. Importantly, the Court observed that expenditure of a capital nature relating to natural resource prospecting, exploration and development does not qualify for deduction of depreciation allowance. Paragraph 1(3) instead treats such expenditure "as if it were incurred in securing the acquisition of an asset." However, the Court held that this deeming treatment does not itself establish that the asset has been used in producing income. The taxpayer must still satisfy the use requirement under section 17.

The Court relied on its earlier decision in Civil Appeal No. 192 of 2018 (taxpayer in this case was already at production stage) reiterating that depreciation requires both ownership and actual employment of the asset in the production of income. It consequently held that the taxpayer whose project remained at the pre-production stage, was not entitled to the depreciation claimed.

Implications of the decision

The decision creates a significant dilemma for exploration investors. Although the law deems qualifying exploration expenditure to have been incurred in acquiring an asset used in the production of income, the Court held that depreciation still requires proof of actual income-producing use. The practical difficulty is that exploration is undertaken precisely to determine whether commercially recoverable resources exist. If exploration is unsuccessful and no income-producing use ever arises, the depreciation allowance may never become available despite substantial exploration expenditure having been incurred. This outcome raises important questions on capital recovery and the attractiveness of Tanzania's petroleum fiscal regime, particularly given that other petroleum-producing jurisdictions provide clear mechanisms for recognising or preserving unsuccessful exploration costs.

To read the Judgment [click here](#)

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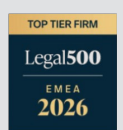
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