



Submission No 66

## **Inquiry into Australia's Relationship with Timor-Leste**

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Organisation: ConocoPhillips Australia Pty Ltd

Joint Standing Committee on Foreign Affairs, Defence and Trade  
*Foreign Affairs Sub-Committee*

12 April 2013

Mr John Carter  
Committee Secretary  
Joint Standing Committee on Foreign Affairs, Defence and Trade  
Foreign Affairs Sub-Committee  
Department of House of Representatives  
PO Box 6021  
Parliament House  
CANBERRA ACT 2600

Submission email to: [jscfadt@aph.gov.au](mailto:jscfadt@aph.gov.au)

Dear Mr Carter

**Inquiry into Australia's relationship with Timor-Leste**

ConocoPhillips is pleased to make a submission to the Joint Standing Committee on Foreign Affairs, Defence and Trade, on the inquiry into Australia's relationship with Timor-Leste.

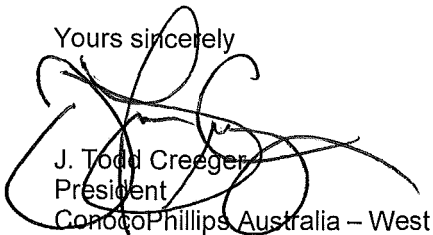
As operator of the Bayu-Undan joint venture inside the Joint Petroleum Development Area, ConocoPhillips has worked closely with the governments of both Australia and Timor-Leste since before Timor-Leste achieved the restoration of its independence. Last year we celebrated the joint tenth anniversaries of both that event and Bayu-Undan operations.

Taxes, royalties and revenues from Bayu-Undan have accrued to both governments and income from Bayu-Undan has provided the greater part of Timor-Leste's national income since 2004, contributing over \$12 billion to the nation's sovereign petroleum fund.

This submission summarises the history, structure and economic benefits of the Bayu-Undan field development. In addition, it describes support for capacity-building, local content and community investment programs. It also raises some concerns with the approach of the Timor-Leste government to contract sanctity and the rule of law, which we believe are hindering progress towards achieving a sustainable positive investment climate.

ConocoPhillips considers a strong relationship between Australia and Timor-Leste to be critical in helping to alleviate these concerns and we are committed to continuing to work diligently with the Timor-Leste and Australian governments to promote the sustainable good governance necessary to ensure investor confidence, thereby allowing Timor-Leste to continue on its path of nation-building.

Yours sincerely



J. Todd Creger  
President  
ConocoPhillips Australia – West



# Inquiry into Australia's relationship with Timor-Leste

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Perspectives from ConocoPhillips Australia

**April 2013**

# **Inquiry into Australia's relationship with Timor-Leste**

## **Perspectives from ConocoPhillips Australia**

### **1. Executive summary**

- Through the development and production of the Bayu-Undan gas-condensate field, the continued progression of the Sunrise field development and participation in multiple capacity-building community initiatives, ConocoPhillips has enjoyed a strong association with the nation of Timor-Leste since the restoration of independence in 2002. Royalties, taxes and revenues from Bayu-Undan, at the halfway point of the project's life, have generated US \$12 billion to Timor-Leste, accounting for most of the state income over this period.
- However, as senior Timor-Leste government minister Alfredo Pires recently noted, "In the next 10 years we should continue to develop together (with the Bayu-Undan joint venture) but with diversification in mind as we approach the depletion stages of Bayu-Undan". ConocoPhillips supports this view. The Timor-Leste government, with the support of industry partners, development agencies and the Australian government must continue to broaden the base of its economy (and consequently the tax base) to ensure sustained economic growth over the coming decades. Such an approach will also encourage greater representation from the population and greater accountability from government institutions.
- Unfortunately, ConocoPhillips is currently encountering challenges associated with the approach of the Timor-Leste government to contract sanctity and the rule of law, which we believe are hindering progress towards achieving a sustainable positive investment climate. Continued support and encouragement from the Australian government is essential and, in its absence, Timor-Leste may become vulnerable to a reputation of poor governance, with consequent erosion of investor confidence and economic and political instability.
- ConocoPhillips remains committed to working diligently with the governments of Timor-Leste and Australia to reassert the fiscal stability and good governance necessary to ensure investor confidence, thereby allowing Timor-Leste to continue on its path of nation building.

### **2. History, structure and economic benefits of the Bayu-Undan field development**

- The Bayu-Undan gas condensate field, located within the Timor Sea Joint Petroleum Development Area (JPDA), was discovered in 1995. Production commenced in 2004. Produced natural gas is transported from the field by pipeline (Darwin Pipeline) to the Darwin natural gas liquefaction facility (DLNG). ConocoPhillips is the operator of these three constituent parts of the project. The Bayu-Undan joint venture is a global initiative comprising six partners from four different countries (INPEX, Santos, ENI, Tokyo Electric Power Company and Tokyo Gas), as well as ConocoPhillips (the Joint Venture).
- The multi-billion dollar investment by the joint venture in Bayu-Undan was made in reliance of the fiscal and regulatory framework for the JPDA and the project. The basis of this framework is the Timor Sea Treaty (TST) made between Timor-Leste and Australia, which underpins the Production Sharing Contracts (PSCs) for the Bayu-Undan field between the Joint Venture and the Designated Authority acting for Timor-Leste and Australia. This is further supported by the Bayu-Undan project tax law and tax stability guarantees provided by Timor-Leste to the Joint Venture. This comprehensive fiscal and regulatory framework gave the Joint Venture the confidence to proceed with the substantial investment in the Bayu-Undan project.

- The fiscal regime set out in this framework provides Timor-Leste with a favourable “government take” from the project, as evidenced by a 2012 study of international petroleum regimes by the International Monetary Fund<sup>1</sup>. This study showed the effective taxation, or “government take”, that Timor-Leste receives benchmarks favourably on an international basis, exceeding the percentage take of Australia, Nigeria, Mozambique, Vietnam, Liberia, Malaysia and others.
- Under this fiscal regime, the Bayu-Undan project was originally anticipated to contribute US \$3 billion to Timor-Leste, over full project life. However, due to increased world oil and gas prices and successful project execution, this contribution has substantially increased. Due to the agreed value allocation between the constituent parts of the project under the fiscal and regulatory framework, this increased value has been realised at the Bayu-Undan field (in the JPDA), not by the Darwin Pipeline and DLNG (in Australia).
- The revenue stream from the Bayu-Undan field is shared between Timor-Leste (90%) and Australia (10%). In total, approximately 70% of the increased value has gone to the two governments. Royalties, taxes and revenues from Bayu-Undan at the halfway point of the project’s life have generated US \$12 billion to Timor-Leste which has been paid into its sovereign petroleum fund.

### **3. History, structure and economic benefit of the proposed Sunrise field development**

- In addition to its interest in Bayu-Undan, ConocoPhillips also holds a 30% interest in the Greater Sunrise field, located on the boundary between the JPDA and the Australian continental shelf. The Sunrise Joint Venture is operated by Woodside, with Shell and Osaka Gas the other JV participants.
- The Greater Sunrise International Unitisation Agreement (IUA) was signed by Australia and Timor-Leste on 6 March 2003 and unifies the Greater Sunrise fields under the two jurisdictions for production and revenue apportionment purposes. The Treaty on Certain Maritime Arrangements in the Timor Sea (CMATS) was signed on 12 January 2006 by Australia and Timor-Leste. Both CMATS and the IUA were ratified in 2007. The TST, the IUA and CMATS provide a regulatory regime under which the Sunrise development can be progressed.
- The development of the Greater Sunrise fields could enable stable and significant revenues over a period of 30 years to both Timor-Leste and Australia. In relation to Timor-Leste, development of the Greater Sunrise fields could continue on from the Bayu-Undan project in providing substantial revenues to the Government of Timor-Leste for its development of the national economy. The development would also deliver a significant social return to Timor-Leste through associated local content, capacity-building and education and training initiatives.

### **4. Support for capacity-building, local content and community investment programs**

- Both the Bayu-Undan joint venture and the Sunrise joint venture are committed to building capacity and developing sustainable economic and community initiatives in Timor-Leste. This includes training and employment opportunities for Timorese nationals, the purchase of local goods and services wherever possible, and supporting local programs through community investment. The commitment of ConocoPhillips and the other joint venture partners to Timor-Leste extends beyond any contractual and statutory obligations.
- Up to the end of 2012 the Bayu-Undan joint venture had directed in excess of US \$36 million to training and employment programs, purchase of local goods and services and community projects.

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<sup>1</sup> International Monetary Fund (Fiscal Affairs Department) “Fiscal Regimes for Extractive Industries: Design and Implementation”, August 15 2012.

- There are now more than 250 Timor-Leste nationals training or employed on the Bayu-Undan project as ConocoPhillips employees and contractors, both on and offshore. We hope to see this number grow. We work closely with our major contractors to develop local training and employment opportunities. These contractors, including Clough AMEC joint venture, WorleyParsons, ESS Services, CHC, M.O.S, Svitzer, SDV, Caltech, Maubere, Cape East and Geographe Energy, share our commitment to create more of these opportunities.
- ConocoPhillips sees these opportunities as a springboard for local capacity-building that will facilitate increased employment of Timor Leste nationals. Our investment in training and development not only provides a pathway to employment through the Bayu-Undan project, but also employment opportunities in the broader petroleum sector and financially secure career paths worldwide.
- Training and development opportunities are also created in our onshore projects such as our transit and heliport facility located at the Nicolau Lobato International Airport in Dili. Heliport operations conduct crew transfers to the offshore platforms, with up to 500 crew members transferring each month. The heliport currently employs 30 Timor-Leste nationals.
- As the Bayu-Undan project has developed and the petroleum sector in Timor-Leste has grown, we have seen a multiplier effect in income and employment from Timor-Leste supporting the offshore project. Over time, the increased presence of our contractors and service providers has led to growth in employment opportunities in supporting industries. This multiplier effect continues to build a solid platform for future economic development.
- Community investments through the Bayu-Undan joint venture have a specific focus on education, health and capacity-building programs in Timor-Leste and have benefited several thousand people. Bayu-Undan joint venture, or ConocoPhillips stand-alone supported programs, include the Fulbright-SERN Scholarship Program; Alola Foundation - Education and Literacy Program; USAID horticultural projects with 500 farmers; St John of God Outreach – Nursing Development Program; Alola Foundation – Maternal and Child Health Program; Santalum NGO – Reforestation Program; World Vision – Village water pump program; Rotary Oceania Medical Aid for Children; Community Education Centre for the Franciscan Sisters at Maubisse; field trips, books and equipment for the Dili Institute of Technology; renovation of the Bidau Primary School; and computers and books for children’s education from the Canossian Sisters in Balide. Sponsorships have included the Tour de Timor cycle race, First Lady Fun Run, Timor Sea Cup soccer tournament and others.
- We are proud of our role in forging relationships that are not limited to our performance as an oil and gas producer, and will ensure that ConocoPhillips, with our joint venture partners, makes a lasting contribution in Timor-Leste.

*More information on these programs and a video report on them may be found on ConocoPhillips Australia’s website at:*

<http://www.conocophillips.com.au/EN/responsibilities/TimorLeste/Pages/index.aspx>

*A pdf version of a commemorative book produced by ConocoPhillips, entitled “Developing Together”, which celebrates the joint tenth anniversaries of Bayu-Undan operations and the restoration of Timor-Leste’s independence was provided with this submission.*

## 5. Capacity-building of the ANP under the Timor Sea Treaty (TST)

- The Joint Commission (established under the TST) oversees the work of the Designated Authority, which is the regulator of petroleum operations in the JDPA on behalf of both Australia and Timor-Leste). The Joint Commission is comprised of representatives from both countries.
- The Designated Authority was initially the Timor Sea Designated Authority (TSDA), which was a body jointly staffed by Timor-Leste and Australia, but since 2008 it has been the Autoridade Nacional do Petróleo (ANP), a Timor-Leste staffed organisation.
- It has been ConocoPhillips' experience that the Joint Commission between Australia and Timor-Leste relationship has brought a healthy balance of views to the regulation of the project. The Commission has supported capacity-building within the ANP, resulting in a relatively smooth transition of the Designated Authority role to the ANP from the TSDA. However, it is fair to observe that, more recently, there has been divergence of opinion on a greater number of issues, which have therefore escalated to the Joint Commission process.

## 6. Concerns with certain governance practices and consequent loss of investor confidence

- The commitment to tax stability by Timor-Leste a decade ago gave the Joint Venture the confidence necessary to invest in the Bayu-Undan project, even though oil prices were at an all-time low and Timor-Leste was the world's newest nation with a comparatively high "government take". This framework has served the project and Timor-Leste well.
- However, ConocoPhillips and the other Bayu-Undan joint venture partners have recently received multiple tax assessments that breach the fiscal framework committed to by Timor-Leste. In addition, two of the assessments impose a double taxation cost on the Joint Venture that directly impacts the relationship between Timor-Leste and Australia and impinges upon Australia's sovereignty. They also represent a change in the interpretation and application of Timor-Leste tax laws.
- Additionally, the TLRS has imposed penalties on all assessments that greatly exceed the underlying amounts of tax in a manner that we see as inconsistent with Timor Leste tax laws. Repeated attempts over several years to resolve these matters through direct negotiation with the Timor-Leste government have been unsuccessful and, consequently, the Joint venture partners are now seeking recourse both in the Timor-Leste District Court and through international arbitration, pursuant to the tax stability guarantees provided by Timor-Leste.
- In sum, these tax assessments have resulted in an unfortunate erosion of the confidence and trust necessary for investment in any nation, especially one that is still early in its development. We sincerely hope these matters can be resolved in a manner that will restore the stable framework that prevailed prior to these assessments.
- The restoration of investor confidence is also essential to support further progression of the Sunrise project. The Sunrise Joint Venture submission to this panel notes the following requirements and concerns:
  - Before proceeding with any large capital investment, investors require confidence and certainty in the investment framework.
  - The treaties, titles and associated project agreements provide the legal framework and the honouring of these agreements provides the essential certainty to investors of a regime that will be stable and predictable over the life of the investment and therefore enable the necessary final investment decision.

- To date differences in interpretation of the treaties have resulted in the project being unable to secure government approvals of a common development concept. The Sunrise Joint Venture understands differences of interpretation, but long periods of time without resolution can cast doubt on not only the large initial investment of capital, but also the stability of the investment regime in future years.
- The Sunrise Joint Venture believes it is now time to focus on building a stronger understanding of all parties' key requirements. This will allow solutions to be identified which include a common development concept, associated support infrastructure and agreed interpretation of existing agreements.
- Another important factor in ensuring investor confidence is maintaining independence between the ANP as regulator and Timor-Leste development and commercial aspirations, so the ANP does not deviate from its defined regulatory role.

## 7. Conclusion

- The Bayu-Undan joint venture project is contributing directly and indirectly to economic development in Timor-Leste and has been a remarkable success story that, 10 years on, still has potential to endure. As minister Alfredo Pires recently noted, "the Bayu-Undan project changed the fate and destination of Timor-Leste. The economic and social implications of Bayu-Undan in Timor-Leste cannot be underestimated". ConocoPhillips is proud of this achievement and hopes the Sunrise project can become the next chapter in this success story.
- As noted above, the Bayu-Undan project has helped Timor-Leste make significant progress in a relatively short period since the restoration of independence in 2002. However, the capacity of the key institutions necessary to ensure good governance requires further development. Unless resolved, the current tax disputes could become a significant concern for existing and potential investors that will hinder progress towards economic diversification and future nation-building capital projects such as the Sunrise development.
- We consider a strong relationship between Australia and Timor-Leste to be critical in helping to alleviate these concerns. Minister Alfredo Pires also recently noted, "In a few years' time I would like to look back at our current tax disputes (with the Bayu-Undan venture partners) as an event that tested our relationship but also provided an opportunity for us to understand each other better". The minister further noted, "the next 10 years will be a better decade. I will go further to say if we handle it right this developing together relationship should spill into the Greater Sunrise for the next 30 to 40 years".
- We share Minister Pires' sentiment. ConocoPhillips will continue to work diligently with the governments of Timor-Leste and Australia to promote sustainable good governance necessary to ensure investor confidence, thereby allowing Timor-Leste to continue on its path of nation-building.