



## RESUMED MARITIME TALKS BETWEEN TIMOR-LESTE AND AUSTRALIA IMPACT TIMOR SEA OIL AND GAS PROSPECTS

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### Resumed maritime talks between Timor-Leste and Australia impact Timor Sea oil and gas prospects

The decision by East Timor to freeze international arbitration for six months and resume bilateral negotiations with Australia could resolve the disputed maritime border and the contested ownership of more than USD 55 bn worth of proven oil and gas resources in the Timor Sea. Any resolution is expected to give East Timor greater control over disputed fields, casting uncertainty over the future of regulations governing already delayed projects in East Timor's immature oil and gas sector. The impact for existing operators and prospects for future exploration will be influenced by whether the dispute is resolved bilaterally or through arbitration. Recent tax disputes with international oil companies suggest that greater control by East Timor over the resources in the Timor Sea could have a negative impact on the regulatory environment.

### Dispute background

East Timor is seeking to nullify the Certain Maritime Arrangements in the Timor Sea Treaty (CMATS) agreement signed with Australia in January 2006, which obliges it to postpone legal claims for maritime boundaries until 2056. Under the 1982 UN Convention on the Law of the Sea, East Timor has a strong case to change the Australia-Indonesia Maritime Boundary Agreement signed in 1972, which places much of the resources in the Timor Sea under Australian jurisdiction, even though they are geographically closer to East Timor. East Timor claims that Australia spied on its parliament's cabinet rooms during the CMATS negotiations, creating legal grounds for disputing the treaty.

### Operational and regulatory impact

The dispute has already prevented the development of resources at the Greater Sunrise field, delaying original plans to bring the USD 40 bn project online in 2018. East Timor has repeatedly rejected Australian licence holder Woodside Petroleum's plans to connect the field with a pipeline to Darwin in northern Australia or build a floating liquefied natural gas (LNG) plant to process fuel. East Timor instead insists on building a pipeline to an onshore processing facility in its territory to start production, a decision seen as uneconomical by industry experts and a sign of the government's intent to increase its share of revenue from the current even split dictated by the CMATS.

The dispute casts significant uncertainty over the future of exploration in the area due to expected worsening terms for operators. Were current bilateral negotiations to fail and East Timor to win the case through a legal challenge, Australia could lose access to the Laminara-Coralina field, which has generated more than USD 2 bn of revenue exclusively for Australia since 1999. Australia's share of revenues from the Bayu-Undan gas pipeline could also be placed in jeopardy. Exclusive East Timorese jurisdiction over the Greater Sunrise field would also threaten Woodside Petroleum's rights to development.

East Timor has taken an aggressive stance on resolving tax disputes with extractives companies in recent years, and greater jurisdiction over the Timor Sea oil fields could result in an overhaul of the tax regime for current operators. The government has already claimed the right to tax the natural gas pipeline from the Bayu-Undan gas-condensate fields to a Darwin-based liquefied natural gas plant operated ConocoPhillips, but its attempts have been rejected by Canberra and disputed by the company. Canberra says the pipeline runs within its exclusive jurisdiction and therefore cannot be taxed by Dili.

The government has also reshuffled the judiciary, which it says was corrupted by foreign influence and produced biased decisions in tax disputes in favour of foreign operators. East Timor's legislature ruled on 24 October to fire all foreign nationals working in its judicial system, including judges, advisers to the prosecutor-general as well as secondees to its anti-corruption commission, heralding a review of past tax cases involving resource companies. Operators claim the move severely undermines the independence of the country's judicial system and is damaging to the business environment, and cases handled by the fired and allegedly corrupt judges could now also be revived.

## Outlook for negotiations

Although bilateral talks could yet resolve the dispute, the ongoing negotiations uphold regulatory uncertainty around the investment climate in the disputed waters. The prospect of increased East Timorese jurisdiction over resource-rich waters and online projects could result in changing contract terms and potential tax disputes with existing operators, slowing investment.

Encouragingly, the two countries' pursuit of bilateral negotiations suggests a willingness to speed up resolution of the dispute, something that could help counter the long-term regulatory uncertainty of investment in the area, which international arbitration proceedings would prolong. Australia's weak position in the face of international law means it will favour bilateral talks. A bilateral resolution could provide more continuity for operators currently active in the area under Australian jurisdiction—which include the Laminara-Coralina field, the Bayu-Undan gas pipeline, and around 80 percent of the Greater Sunrise field—reducing the likelihood of licence revocation or contract reviews. However, East Timor is likely to demand increased revenues in any scenario and any changing terms could impact operators' profit margins, compliance and government relations requirements.

Should negotiations fail and arbitration proceedings resume in six months, East Timor holds a stronger legal position than Australia. The UN Convention on the Law of the Sea favours East Timor in the delineation of an Exclusive Economic Zone based on the median boundary line—a border equidistant between the two countries' shorelines—providing it with a way to define clear national boundaries in line with international law, placing the majority of the resources in its exclusive jurisdiction. Australia holds a weak position in any international arbitration and its claims are based on an outdated legal understanding of its continental shelf, which extends to the current Australia-Indonesia maritime boundary and allows it greater territory than the median line. Canberra rejected adherence to the International Court of Justice's (ICJ) jurisdiction over maritime boundary disputes in March 2002—just two months before East Timor's declaration of independence—in a likely attempt to prevent losing access to the Timor Sea fields. However, only two years later it adhered to the median line boundary when resolving a maritime dispute with New Zealand. The spying scandal has also undermined its position and prompted the ICJ to order Canberra to stop using national security as an excuse to conduct commercial espionage.

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