

Attachment 1: Comments on Draft PSC

Article	Text/ Details	Comments	Recommendation
Definitions			
1.1	"Commercial Discovery".	Definition is unclear.	Change to: "A discovery which the contractor declares commercial pursuant to clause 4.10".
1.1	"Commercial Production".	Linkage to shipping complicates definition.	Change to: "start of regular production for the purpose of sale of the products to a buyer".
1.1	"Crude Oil", Crude Oil Field, "Associated Gas".	These definitions together results in gas reservoirs with a tiny oil/condensate rim to be classified as oil fields.	Introduce a "Condensate" definition and a cut-off size for oil field gas caps.
1.1	"Development".	The inclusion of production is inconsistent with the definition of production (which excludes development).	Delete the words: "and subsequent production".
1.1	"Exploration".	"... for the purpose of making a Discovery" presupposes successful outcome.	Replace with "for the purpose of exploring for hydrocarbons".
1.1	"Natural Gas".	Definition is unclear.	Definition should explicitly include inerts.
1.1	"Reservoir".	Definition is flawed with respect to compartmentalisation.	Use definition in the PMC.
Government Take			
2.2	Security. Contractor is to provide "Security" for its obligations under the PSC, which may include a letter of credit, bank guarantee or corporate guarantee.	This is a new requirement which creates an additional cost for the contractor that is not cost recoverable. The requirement for the Security to cover the minimum work obligations for 5 years (3.1(f)) is out of line with international practice.	Delete requirement for security since Contractors are vetted as part of initial award.
6.2 (d)	Uplift on outstanding recoverable costs.	The uplift on recoverable costs only applies for 7 years prior to development. This is a short period for a gas development which will require an appropriate market to be secured before development proceeds.	Extend to full term of current and previous PSCs.
7	Sharing of Petroleum.	Modelling of oil and gas projects over a range of sizes and water depths indicates that the State Take would be higher than under the old ZOCA terms and compares unfavourably with many other competing fiscal regions around the world. The ring fencing of each PSC for Timor-Leste tax adds to this disadvantage by making exploration very expensive on an after tax basis.	State Take could be reduced by reducing the initial 5% royalty, increasing the uplift rate for outstanding Recoverable Costs or reducing the DA share of profits (given its receipt of the 5% royalty) or a combination of these.
9.1	Fees.	The reference to PMC 23 is incorrect. Fees should be based on the costs of administration as in the old PSC Article 47 and be increased only as a result of	Refer to PMC 22.1(b) (xix). Insert a proviso that fees and other payments shall not exceed the costs of administration.

Article	Text/ Details	Comments	Recommendation
		increases in administration costs.	
Annex C	Accounting Procedure Ineligible Costs (2.8).	<p>The list of Ineligible Costs (i.e. costs which do not qualify for cost-recovery) is considerably longer than the list in the interim PSC. Amongst other additions the list of Ineligible Costs now includes:</p> <ul style="list-style-type: none"> • interest on finance. Previously the consent of the DA could be sought (see old PSC 6.9(a)). • except with the consent of the DA, “any expenditure in respect of the hiring or leasing of structures, facilities, installations, equipment or other property, or of other works”. • costs associated with local offices and local administration, including staff benefits, which are excessive. • except with the consent of the DA, but subject to Article 4.7, costs not included in a Budget for the relevant Year (recoverable costs should be based on actual expenditure (approved in accordance with the PSC) not on budget). • Costs stated elsewhere as not recoverable and costs incurred without the approval of the DA. 	<p>Remove (a) from list of Ineligible Costs in 2.8.</p> <p>Remove (q) from list of Ineligible Costs in 2.8.</p> <p>Remove (s) from list of Ineligible Costs in 2.8.</p> <p>Remove (u) from list of Ineligible Costs in 2.8.</p> <p>Remove 2.8 (v) since it merely duplicates provision elsewhere governing eligible costs and DA approvals.</p>
Omission 1	Missing tax stability clause.	Tax Stability clauses are an important element of typical PSCs but have not been included.	Include clause that confirms tax rate for life of PSC.
Omission 2	Other levies, duties, fees, excise, VAT, WHT, training, welfare.	These do not appear to be covered by the PSC which again negates one of the main benefits of a PSC.	Amend PSC to explicitly cover all taxes and charges.
Omission 3	Past Expenditures.	The new PSC does not appear to recognise past expenditures, even expenditures incurred under the Interim PSCs.	Explicitly include past expenditures as recoverable.
DA Control			
1.6 (e) & (f)	Approval for change in Operator / competency of operator.	<ul style="list-style-type: none"> • Approval should not be able to be unreasonably withheld. • 1.6 (f) gives no guidance as to how the DA would assess whether an operator is no longer competent to be an Operator. 	<ul style="list-style-type: none"> • Insert a subclause that “the approval of the Operator or of a change of Operator will not be unreasonably withheld”. • Delete 1.6 (f).

Article	Text/ Details	Comments	Recommendation
3.5	Gas Retention Area.	Commerciality within 5 years is too short given that the Contractor has to demonstrate activity during that period anyway and commerciality is dependant on market capture.	Extend the commerciality criteria to 15 years as applies in Australian Retention Leases.
5.1 (vii)	Prevent escape of any mixture of water or drilling fluid with Petroleum or any other matter.	Definition is too stringent to be practical. Would include produced water with a few ppm of oil.	Replace with "Prevent escape of petroleum or drilling fluids in amounts which are damaging to the environment".
5.1 (ix)	Obligation to keep each reservoir separate.	It may be necessary to co-mingle production in order to achieve sufficient well production rate or optimise reservoir performance (gas re-injection using gas from a separate reservoir).	Make provision for exceptions by adding "except with the consent of the DA".
10 10.1	Provision of Goods and Services. Notice.	Some of the requirements in Clause 10 are impractical and not consistent with international practice. They would place an enormous administrative burden on the contractor and would lead to project delays and increased project costs. In Clause 10.1 they are considered to be: <ul style="list-style-type: none"> • requirement to advise all suppliers in Timor-Leste of all opportunities; • requirement to obtain approval of each award but without any requirement on the DA to make a decision within a specified time (previously a 30 day period applied) • requirement to provide the DA with full financial details of all contracts, irrespective of the amount of expenditure. 	<ul style="list-style-type: none"> • Apply a minimum threshold of \$US0.5m for advising all suppliers with advice to suppliers coordinated by the TSDA. • Specify 30 day period for DA approval of awards. Non response to be consent. • Delete 10.1(c) since details of all Recoverable Costs are provided to meet cost recovery requirements.
10.2	Contracts not Requiring DA's Approval.	In 10.2(b) the level of non-approved contracts has been reduced from US\$10m to US\$5m (even though financial details need to be provided and budgets must be approved).	Raise the thresholds for contracts not requiring DA approval to \$US5m and \$US10m.
10.3 (a)	Tender Invitations Requiring DA Approval.	In Clause 10.3 (a) there are two major concerns: <ul style="list-style-type: none"> • The DA's consent would be required before tendering (the old PSC required approval only of the award of the tender, no approval was required prior to tendering). • Regardless of value, all goods and services must be procured through arms length tenders except with the consent of the DA. Low value purchases should be excluded from this. 	<ul style="list-style-type: none"> • Delete clause 10.3. • Amend 10.3 (b) to include a \$US5m tendering threshold.
10.5	Other Information to be Provided.	Making the information requirements in Clause 10.5 mandatory	Delete (a), (b) and (c) and retain only 10.5 (d).

Article	Text/ Details	Comments	Recommendation
		<p>would be administratively excessive for both the TSDA and contractors. For example all awards require approval by the DA under 10.1 (b). Requirements to provide copies of all contracts and a report on each award duplicate the information provided when seeking contract approval.</p> <p>The requirement to provide a detailed report of selected contracts is also onerous but in any case could be requested by the DA under clause 10.5 (d) as it is currently worded.</p>	
19.	Assignment.	The new PSC has introduced more detailed and stringent restrictions on assignment. An assignment or dealing is of no force unless approved by the DA.	Include an entitlement to assign to affiliates (old PSC 5.3(b))e. Delete 19 b(ii).
19.2	Change in control.	The new PSC has introduced a "change in control" provision whereby the DA may terminate the PSC in the event of an unauthorised change in control or such further change in control occurs as it specifies in a notice. The only exception is where the change in control is the direct result of an acquisition of shares listed on authorised stock exchange. A breach by one JV could lead to loss of title by everyone. These provisions are highly interventionist in corporate transactions and are unusual in a PSC.	Delete 19.2 or terminate PSC only in relation to defaulting corporate entity, and give the contractor companies not in default an opportunity to ratify and confirm compliance with the PSC.
AP 2.9 (c)	General and Administration cost subject to approval by DA.	Requirement for general and administration costs to be determined by a "detailed study" and subject to approval by the DA adds to administrative costs and uncertainty. It is unnecessary given the DA's audit rights.	Remove clause 2.9 (c).
Administrative Burden			
1.1	"petroleum operations".	The definition is narrower than and inconsistent with the equivalent definition "Petroleum activities" in the Treaty (see TST Art 1(k)). The TST definition included activities "contemplated" by the PSC, the new PSC requires DA "authorisation". Operations must also be "in the contract area" – the previous definition included all activities "undertaken to produce petroleum...under a contract". It is likely that some developments would require work to be carried out outside the contract area and this work should be covered by the PSC.	Adopt TST definition.
1.6 (d)	Operations to be conducted from	Flexibility to conduct operations from most efficient location is	Change to: "the Operator shall operate an

Article	Text/ Details	Comments	Recommendation
	an office located in Timor-Leste.	important.	office in Timor-Leste".
4.7	Limit on budget overspend.	<ul style="list-style-type: none"> • \$50,000 limit for individual line items is unnecessary. • 5% limit on total annual expenditure is too low (eg could be exceeded by one extra day of drilling). 	<ul style="list-style-type: none"> • Remove dollar cap for line items (but retain 10%). • Change Work Programme limit to 10% and remove dollar limit.
4.11	Development Plan.	<ul style="list-style-type: none"> • A 12 month period after the declaration of a Development Area is an appropriate timeframe to prepare a Field Development Plan. However, the qualification of "and as the DA requires" in 4.11 (a) suggests that this period may be shortened which could adversely affect the quality of the Development Plan. • A typical Field Development Plan focuses on the efficient development and recovery of hydrocarbons. Copies of gas sales contracts and contracts downstream of the Field Export Point (4.11 (d) (xi)) are inappropriate. 	<ul style="list-style-type: none"> • Delete "and as the DA requires" in 4.11(a). • Delete 4.11 (d) (xi).
4.13	Approved Contracts.	<p>The new PSC has introduced the notion of an "Approved Contract", i.e. approved by the DA. The Contractor is not entitled to sell natural gas from the Contract Area other than pursuant to an Approved Contract or as otherwise provided in the Development Plan. The Contractor may not use facilities downstream of the Field Export Point for transporting, processing, liquefying, storing, handling or delivering Petroleum other than under the terms of an Approved Contract.</p> <p>For a gas project with onshore processing, this would potentially extend the reach of the DA well outside the JPDA. The implication is that the DA would have the right to approve, for example, a contract for liquefaction of the gas in Australia. This creates a conflict of jurisdictions, is excessive and unacceptable.</p> <p>Moreover there is considerable overlap and excessive control imposed by a range of sections concerning approval of contracts and access to contract information – compare 4.13 with 4.11, and see PSC13.2(b), and PMC4.1, 4.4 and 4.7.</p>	<p>Delete 4.13.</p> <p>Limit approvals and access to information to activities upstream of the Field Export Point, and make the variety of approvals/access provisions consistent and reasonable.</p>
5.3	Most stringent HSE/welfare obligation.	This is an evergreen obligation which gets tighter for all contractors in the JPDA (supersedes old HSE plans) every time any contractor in the JPDA, T-L or Australia or any of the	Rethink HSE clause to effect high HSE standards in a practical manner that offers reduced uncertainty for contractors.

Article	Text/ Details	Comments	Recommendation
		affiliates of contractors in the JPDA makes an improvement.	
7.5	1/12 payment to DA for each month.	<ul style="list-style-type: none"> This pays no regard to the actual lifting dates and may lead to significant payments before any sales have actually occurred and also ignores customary payment periods. It is not clear whether the DA is obliged to repay an overpayment. 	<ul style="list-style-type: none"> Bring payment to DA in line with receipt of sales proceeds. Clarify treatment of overpayments.
13.1	Financial and Technical Data, Records and Reports. Ownership	<ul style="list-style-type: none"> These provisions give the DA title to all technical data and conclusions derived from it. 	<ul style="list-style-type: none"> The DA should not have title to processed information and conclusions.
13.2	Records, Storage, Retrieval and Submission.	<ul style="list-style-type: none"> The Contractor's obligations with regard to the keeping of records and the provision of information to the DA and its access to all of the Contractors records are extremely onerous. The requirement to have all data, information and records available in Timor Leste "at <u>all</u> reasonable times" is impractical. The cost of having all data, information and records available in Timor Leste could be significant so should be explicitly listed as recoverable in Clause 3 of Annex C. 13.2 (b) currently suggests that an Electronic Receipting System is not to be used in Timor-Leste (ie paper based transactions only) which increase the administrative burden for the accounts payable team. The timeframe for delivery of data is also not specified. 	<ul style="list-style-type: none"> An exclusion should apply to information which is self incriminatory or subject to legal privilege (see old PSC29/3). Delete "all". Include costs of complying with 13.2 as Recoverable in Clause 3 of Annex C. Specify delivery within 14 days and that copies may be produced in electronic format.
13.4	Export of Data and Information.	Impractical and an unreasonable administrative burden.	Delete 13.4.
13.5	Restrictions on Use of Data.	This restricts the ability to use data for data trades or regional studies that would assist exploration of the JPDA	Delete 13.5 (b).
13.7	Trade Secrets.	Impractical and an unreasonable administrative burden (see also PMC14.3 (b)).	Delete 13.7 (b).
16.1	Audit to start 24 months after end of year.	No mention about the period of the audit.	Audit once commenced should conclude within 12 months.
16.1/16.2	Independent Audit/ DA Audit.	Potential for 2 DA audits in a given year.– independent audit at contractors cost, DA audit at its cost.	Amend so DA can only exercise right of audit under one clause for any contract year.
16.5	Audit of affiliates.	It is inappropriate for the DA to have the right to audit the books	Delete 16.5.

Article	Text/ Details	Comments	Recommendation
		of a Contractor's affiliate or parent companies.	
AP1.3	Language and Units of Account.	Costs and revenues in a currency other than \$US are to be translated at the exchange rate of the day incurred or received at a time and bank designated by the DA. This will require maintenance of an additional set of exchange rates within the Contractors accounting system.	Amend so that translation occurs on the exchange rate of the day as quoted by a major bank selected by the Contractor and approved by the DA.
AP 2.9 (d)	Inventory recoverable at time of use.	A stock of inventory/spares is required for ongoing operations; this provision would de facto exclude the long-term amount of spares from being recoverable cost.	Amend such that inventory is recoverable at time of purchase; terminal value gets adjusted at time of decommissioning.
AP 7.2	Cost Recovery Statement.	Requires submission of a Provisional Cost Recovery Statement on last day of quarter and final version within 30 days. This is duplication as no financial information for the last month of the quarter is available by the last day of the quarter.	Delete requirement for a Provisional Cost Recovery Statement by the last day of the quarter.
Lack of Certainty			
1.1	Definitions of Initially Processed and Field Export Point.	The definition of Initially Processed makes sense for an oil development that is located within the JPDA, but it is unclear insofar as it applies to natural gas, or oil developments where the processing facility is located outside of the JPDA. It is unclear at what point natural gas would be "Initially Processed". Under the new PMC the Contractor does not acquire title to Petroleum until it has been Initially Processed (PMC4.2). However, the PSC suggests that title and risk passes at the Field Export Point (PSC7.4) with no cost recovery for costs incurred after the Field Export Point.	Clarify the definitions of Initially Processed and Field Export Point.
2.1 b(i)	Exclusivity.	Exclusive right is inconsistent with restrictions on exclusivity defined in the PMC with respect to hydrocarbon type.	Remove restrictions on exclusivity in PMC 7.1(c).
2.1	No authorization to process petroleum beyond point where Initially Processed.	May work for oil, but definitely complicates matters for gas (compression, transportation, separation, inhibition, pigging, ...).	Delete and cover matter under Field Development Plan approval.
4.5	Non-performance of exploration work programme.	<ul style="list-style-type: none"> Art 4.5 entitles the DA to require liquidated damages to be paid for non-performed work. This is an onerous requirement as this expenditure is not actually loss suffered by the DA – they would never have "received" these funds or the benefit of them. (Note the old PMC provided for a fixed penalty related to the contract fees, not the work 	<ul style="list-style-type: none"> Make fulfilment of work program a condition for entering into next phase.

Article	Text/ Details	Comments	Recommendation
		<p>program and budget – PMC 45).</p> <ul style="list-style-type: none"> Termination is too harsh since non-performance may be due to factors beyond the Contractor's control. 	<ul style="list-style-type: none"> Delete ability for DA to terminate PSC if delay is due to factors outside Contractor's control.
4.10	DA ability to vary Field definition.	After a discovery has been declared the DA should not have the right to remove sub-blocks or vary the depth of the Contract Area unless requested by the Contractor.	Delete the words: "whether of its own volition or".
5.1	Managing resources.	<p>There is a new requirement that resources be managed in a way which has "long-term benefits to Timor-Leste, Australia and the contractor". What effect this will have on the Contractor's "petroleum operations" is unclear.</p> <p>This also links to the DA's exercise of its powers to "promote the economic development of Timor-Leste" (see PMC 1.4) which could have an adverse effect on petroleum operations.</p>	<p>Delete 5.1 (b) (iii).</p> <p>Delete PMC 1.4 (a) (i).</p>
5.4	Goods, Services, Training and Employment.	Reference to Article 6 of the Code should be Article 5.4	Amend "Article 6" to "Article 5.4"
5.4 (b)	Preference for local employment.	As well as meeting occupational health and safety requirements, all employees (including nationals and permanent residents of Timor-Leste) must have the skills necessary to operate the facilities safely and efficiently according to good oil field practice.	Should be subject to availability of necessary skills, and subject to contractor's requirements for safe and efficient activities and to good oilfield practice.
7.2	Option of DA re sales.	The DA on a calendar year basis may choose to sell its own petroleum. This would be impossible to manage for long term gas contracts, and difficult for any term oil contracts.	Amend 7.2 so that DA has option to elect to market its share of petroleum and that option can only be exercised within a specified period following the declaration of a Development Area.
8.3	Valuation of Petroleum.	<p>The new PSC does not appear to cater for the possibility of natural gas being sold at a point which is later than the Field Export Point. 8.1 and 8.3 (a) are conflicting. The price received needs to be adjusted to reflect the assessed value at the Field Export Point.</p> <p>For natural gas the "fair and reasonable market price" should be established by an objective and independent way, such as a netback or cost plus pricing methodology. The concern otherwise is that a price will be imposed by the DA, which could have significant value repercussions for a gas project.</p> <p>The combination of 4.11, 4.13 and 8.3 creates circularity and</p>	Objective criteria for valuation of Petroleum is required.

Article	Text/ Details	Comments	Recommendation
		inter-meshing of approvals and determinations, leading to a high degree of uncertainty. A contractor cannot assess the economic viability of a development until the valuation is known. Valuation is not determined until the Development Plan is approved and Approved Contract in place. This obliges the Contractor to negotiate sales contracts and progress development of the field in the absence of an understanding or appreciation of the economics and therefore the viability of the development.	
15.	Third Party Access.	The new PSC has introduced provisions requiring the Contractor to allow for third party access to structures and facilities within the Contract Area. These are an elaboration of the old PMC 18/2 which applied to pipelines only. The Contractor is to use reasonable endeavors to negotiate a satisfactory agreement for third party access and in default of agreement the DA can set the terms of third party access in accordance with internationally accepted principles. This adds to risk and uncertainty. Third party access should be in accordance with good oilfield practice and subject to operational requirements and standards.	There should be consultation with the contractor (and agreement not to be unreasonably withheld) if the DA sets the third party access regime.
Omission 1	Minimum contract term.	There is no provision about minimum contract term.	Contractor may terminate PSC after the end of the 3 rd contract year.
Increased Risks for Contractors			
2.2	Drafting Error.	Reference to Art 16 in 2.2 (a) (iv) is incorrect.	Replace "Article 16" with "Article 17" in 2.2 (a) (iv).
2.3	Inconsistency in Effective Date. Term.	2.3(a) envisages the possibility of the effective date being later than the 7 th day after the date of the Agreement if the conditions are not met until a later date but 2.2(b) says that if the conditions are not met within 7 days the Agreement is terminated. To secure marketing arrangements of a natural gas project, the PSC term should be automatically extended to the end of the term of the natural gas sales contract (Old PSC 2.5).	The effective date should be when all of the conditions have been met. Add similar provision to old PSC 2.5, 2 nd sentence.
2.3 b(iv)	Automatic PSC termination if Treaty lapses.	Puts title at risk through no fault of contractor.	Include provision for equivalent terms to be maintained.
2.4	DA termination rights of whole PSC if any of the contractors is in	Puts title at risk through no fault of contractor who is not in	Termination rights should be limited to that contractor who is in financial distress or should

Article	Text/ Details	Comments	Recommendation
	financial distress.	financial distress.	allow other contractors to remedy breach by defaulter. PMC 21.2 attempts to do this but needs reworking (see PMC comments below).
3.1/3.2	Relinquishment.	Relinquishment after 7 years is earlier than for old PSCs and reduces the attractiveness of taking up acreage in the JPDA.	Revert to old PSC terms of 3, 6 and 10 years.
3.3	Relinquishment of Development Area.	<p>Relinquishment due to force majeure breaks with principle of force majeure. Relinquishment should not apply where “good faith” efforts have been made to recover from force majeure.</p> <p>Relinquishment on the 25th anniversary of approval of the Development Plan, which in the case of gas projects could be several years before the end of production, is not sufficient. Standard industry contracts of 20 or 25 years could well extend beyond the 25th anniversary of approval of the Development Plan.</p>	<p>Delete mandatory relinquishment due to force majeure in 3.3 (a) (i) and have a process of consultation/ agreement with contractor.</p> <p>Delete 3.3 (a) (ii).</p>
7.4	<p>Risk in Petroleum.</p> <p>Title transfer at field export point, but risk transfer at wellhead.</p>	<p>The new PSC seeks to impose on the Contractor all risk associated with loss of petroleum after wellhead, such that any loss of petroleum after wellhead is deducted from Contractor's Recoverable Costs. This is onerous and unusual. It also appears to be inconsistent with the PMC which provides that the Contractor does not acquire title to Petroleum until it has been Initially Processed. Petroleum will not necessarily be Initially Processed at the Field Export Point.</p> <p>In addition the expression “lost” is open to interpretation and may be interpreted to include part of what is used or discharged in normal operations (eg fuel oil and gas).</p>	<p>Loss-of-product risk should be shared between parties simply via accepting a reduction in available petroleum resource.</p> <p>Delete subclause (a) and modify subclause (d).</p>
9.3	Late payment penalty.	LIBOR + 5% is excessive.	Reduce to LIBOR + 2%.
18.5	Extension of time due to Force Majeure.	A break with what is commonly the consequence of Force Majeure, i.e. the clock stops and obligations are excused to the extent prevented due to Force Majeure.	The PSC should be extended for the period of the Force Majeure.
Omission 1	Repatriation of Funds.	PSC should include a provision that explicitly provides contractors with the right to expatriate funds without being subject to banking or exchange rate controls.	Include a clause that confirms contractors' right to repatriate funds.