



global witness

Revenue Transparency in Timor Leste

Global Witness submission on the draft petroleum legislation, September 2004

Summary:

- Timor Leste's commitment to revenue transparency is exemplary. We would like to see that commitment secured at the earliest possible stage in its petroleum legislation, so as to ensure that this legislation does not introduce any unintended prohibitions on disclosure of revenues.
- The legal framework under review should have a stronger presumption in favour of public disclosure of information, with commercial confidentiality applied only to proprietary data and never to payments to the state.
- The concept of disclosing industry agreements via a Public Register is excellent and could be extended to include company payments to the state, and receipts by the state.
- After publication, an independent third party needs to audit all payments and receipts to reconcile or, if necessary, investigate any discrepancies. Audits should be published.
- The proposed Oil Fund law could be widened, with little difficulty or delay, into a revenue management law that ensures the transparency of all revenue flows from oil companies to the state, not just of revenues in the Fund itself.
- There should be future legislation to provide legal recourse for citizens in the event that revenues go missing, as part of a wider anti-corruption strategy.

Introduction

Global Witness (www.globalwitness.org) is a London-based NGO that works for good governance and transparency in the natural resource sector. We were nominated for the Nobel Peace Prize last year for our work highlighting the role of conflict diamonds in funding civil wars across Africa, and we helped to start the Publish What You Pay campaign (www.publishwhatyoupay.org) to improve the transparency of oil revenues worldwide. We are active participants in the Extractive Industries Transparency Initiative, which was launched by British Prime Minister Tony Blair in June 2003.

Transparent and accountable management of oil revenues, which will comprise a majority of Timor's income in the near future, is essential to ensure that such money is used effectively to promote national development. It will greatly increase the hope that Timor Leste will escape the 'resource curse' of weak growth, corruption, authoritarian government and instability that has afflicted so many oil-rich developing countries.

Revenue transparency means that:

- Each company that extracts natural resources publishes its payments to the state, its agencies and representatives;
- The state publishes what it receives from the companies;
- Revenue data are audited by an independent body so that any discrepancies can be reconciled or, if necessary, investigated.

This means that citizens can track the flow of revenues from the oil industry into the national budget. If citizens do not know how much money their government is receiving, they have no way of knowing whether the money is being properly used or not. Trust in the government is weakened and the risk of corruption is greater.

We were very impressed by the speech of His Excellency Mari Alkatiri, the Prime Minister of Timor Leste, to the EITI launch in 2003 stating his government's intention to adopt best practice in transparency and good governance in the management of his country's oil revenues. In this spirit, we would like to offer some comments on the draft legislation on the petroleum industry, which we hope will be a useful contribution to the discussion.

The draft legislation, in its current form, has many positive elements; however, there is no overriding and explicit commitment to the public disclosure of revenue flows. Certain provisions in the legislation could even enable companies to restrict such disclosure on the grounds of commercial confidentiality, which may hinder future attempts to promote transparency.

We think an explicit commitment to revenue transparency should be embodied in national law at the earliest possible stage rather than being left to later legislation or regulation.

The draft Petroleum Act (PA) and its model Production Sharing Agreement (PA-PSA) and the Petroleum Mining Code (PMC) and its model Production Sharing Agreement (PMC-PSA) will establish a legal foundation for the oil industry in Timor Leste from now on, so it is important that they create an enabling environment for the public disclosure of revenues and that they do not clash with any subsequent legislation by placing unintended prohibitions on such disclosure.

There may be something of this intention already in the Preamble to the Petroleum Act, which states that the Act "...aims to ensure stability and transparency". Currently there is little in the language of the Act that explain how this will be achieved. We have attached a series of suggestions below.

We note that there are plans for forthcoming legislation to establish an Oil Fund and to provide for its governance and oversight. This would be a very positive development to help ensure that oil revenues are saved for future generations in Timor Leste. However, our understanding is that the Oil Fund legislation, as currently envisaged, would not make provision for the disclosure of revenue flows from industry to government, until after the transfer of such revenues into the Fund. Our experience of other countries is that much oil-industry corruption involves 'side payments' by companies to officials, or the illicit diversion of revenues, before they even reach the public treasury. Such payments would not be curbed by transparency provisions applied only to money that is already in the Fund.

This is another reason why all Timor Leste's legislation covering the oil industry, not just a specific law for the Oil Fund, should promote the public disclosure of company payments and government receipts, and their audit and reconciliation by independent third parties.

The draft Petroleum Act and the draft Petroleum Mining Code, 2004

As the two Acts and the two PSAs are designed to be very similar, we put our comments on the twin pieces of legislation side-by-side, to make discussion easier.

Preamble

We suggest the Preamble to the Act, which states its intention to ensure ‘stability and transparency’, should include an explicit reference to the right of the citizens of Timor Leste to access to full information from the state and from oil companies, about the sources, management and uses of oil revenues, in order to ensure stability and transparency.

We recognise that the detailed mechanisms for implementing this right might be set out in separate laws later on, for example in an oil revenue management law or a freedom of information law, but since the Act is setting out the operating framework for the oil industry, we believe it needs include a presumption in favour of transparency.

Putting such an explicit commitment into the Act would be a safeguard against any attempt by future governments, which may not be as enlightened as the present government, to undermine the transparency and accountability of revenue management.

The Petroleum Mining Code currently has no such commitment to stability or transparency in its preamble. Something akin to what we are suggesting for the Act could also be inserted here.

Data and information (PA §21, PMC§13,14)

Article 21 of the Petroleum Act states that all data obtained pursuant to any Authorisation for the petroleum industry is the property of Timor Leste. We presume that such information would include data on revenue payments by companies. Article 21.2 states that terms and conditions for the exercise of rights in respect of data ‘shall be established in the respective contracts and in regulation’.

Revenue transparency is such an important principle that it should be defined by law, rather than through specific contract negotiations or regulation. Public disclosure of data on revenue flows could be made a legal obligation for oil companies in a separate clause of the records and reporting’ part of the Act (ie. PA §21, after 21.2) and the ‘use of data and information’ part of the Code (ie. PMC§14, after 14.1).

The provisions of the Code on data and information (PMC§14.2 onwards) contain a more complex series of items on confidentiality and trade secrets. It may be necessary to insert a waiver here clarifying that revenue payments to the state (not bids) are not covered by commercial confidentiality.

Public Information (PA§25,26; PMC§19,20)

These Articles reflect very well on the government’s commitment to transparency as they provide for the publication of a summary of the terms of all Authorisations, and for the public inspection of entire Authorisation documents at a Public Register, on payment of a fee.

We believe they could be strengthened, by making clear that production-sharing contracts (PSC) and all their annexes and supporting documents (without redactions or alterations) will be disclosed in full to the public, within a specified time period of their coming into force, in a form

which a reasonably educated citizen is able to understand (ie. in Portuguese and Tetum as well as English). It would be reasonable to ask oil companies to bear the costs of translation, given that the industry has an interest in ensuring public support for its activities in Timor Leste.

We note, however, that PSCs are highly complex documents that are difficult for non-specialists to evaluate, meaning that citizens will find it hard to determine how much revenue is actually being paid by each company to the state. The public information provisions should therefore also include a requirement for the publication of disclosure of the revenues paid by oil companies to the state and the state's receipts thereof on a regular basis (for example, quarterly) after auditing of the data.¹ The EITI templates provide a possible model for the form that such summary disclosures for could take.

The Public Register should also contain full records of all payments over US\$1,000 made to the state or its agencies relating to oil extraction in Timor Leste, stating the amount of the payment, the identity of the payer and payee and the purpose of the payment.

Paying a fee to obtain such information might be a strain for poorer citizens, so we suggest that the fee be waived (less a nominal charge for photocopying), or that the fee be subsidised by the oil companies operating in Timor Leste, in the interests of good public relations.

Audits and Inspection (PA§22; PMC15,16)

The Act and the Code state that an Inspector, whose powers are to be defined by regulation, can be appointed and that Authorised Persons must make their books and records available for auditing. This could be a very important tool for ensuring that the oil industry is working in the best interests of Timor Leste.

Summaries of audits should be published and full copies of the audits should be made available for inspection at the Public Register under PA§26 and PMC§20.

We suggest that the appointment of an Inspector should be mandatory, and that the Inspector and their staff should be chosen through a transparent process, possibly with the involvement of Parliament and the Council of Ministers, rather than left to the Ministry itself. This would avoid any possible conflicts of interest.

We also suggest the purpose, powers and reporting obligations of the Inspector should be made more explicit in the Act and the Code. For example, they might stipulate that the purpose of the Inspector is to ensure, by means of regular inspection, that Authorised Persons are in full compliance at all times with the letter and spirit of all the laws and regulations of Timor Leste, and acting in the public interest. In particular, we suggest that the office of the Inspector have the authority and the technical support to carry out cost audits of oil companies. We are aware of cases in other countries where international oil companies have unreasonably inflated their costs in order to increase their own income and deprive the state of revenues: in one particular country, this under-payment cost a government nearly US\$100 million from revenues of US\$500 million. We urge the government to ensure the Act gives the Inspector the means to prevent such problems in Timor Leste.

The Act and the Code could also spell out the powers of the Inspector to require the delivery of documents and the attendance of witnesses for questioning, within a set time period. We are not

¹ Perhaps in the government gazette and on the internet in appropriate languages, as well as in local newspapers.

aware of the laws that will govern the role of the Ombudsman (Provedor), but the Inspector could perhaps be given the right to refer any cases to the Provedor or the courts. To ensure public accountability, Parliament should have the power to question the Inspector on any matter, and the Inspector should make regular public reports on the compliance of Authorised Persons with the laws and regulations.

Summaries of investigations could be published in the government gazette and full reports made available in the Public Register.

Regulations and directions (PA§27,28; PMC§22,)

Given the central importance of transparency and accountability for Timor Leste's future prospects, we suggest that the Ministry responsible for managing the oil industry should not be solely responsible for drawing up regulations for the governance of the industry. This will avoid the possibility of conflicts of interest between the public need for disclosure and the need of the Ministry to maintain good relations with oil companies.

We are also concerned by several provisions in the draft legislation that could potentially give a power of veto over legislation to a single government agency. Article 28 of the Act gives the Minister the power to issue a Direction without executive or judicial oversight, which nonetheless has the power to override an existing Regulation. Article 22.2 of the Code gives the same power to the Designated Authority. We fear that these Articles could put great power into the hands a Minister or a Joint Authority which, in future administrations, may not be as enlightened or as protective of the public interest as the current authorities. We strongly urge that safeguards be inserted into these two clauses to prevent liens and encumbrances being placed on the intent and purpose of the existing Act and the Code.

Public competitive tender for Authorisations and petroleum contracts

We suggest that there should be additional provisions in the Act and the Code to require competitive public tender for Authorisation applications and extraction licences.

Production sharing contracts

We suggest that the same principles noted above in respect of the Act and the Code should also be embodied in the Act and the Code's model Production Sharing Contracts.

Payments (PA-PSC§9; PMC-PSC§9)

We would like to see additional provision at the end of Article 9 in both PSCs highlighting that information on payments to the state (outside a bidding round) is not commercially confidential, and providing for the disclosure of all payments over US\$1,000 to the state or its agencies relating to oil extraction in Timor Leste to the Public Register established under the Act or Code.

Audit (PA-PSC§16; PMC-PSC§16)

These Articles could also provide for a regular audit by a credible and independent institution to reconcile all payments to and receipts by the state relating to oil extraction in Timor Leste. Audits should be publicly available at the Public Register.

Financial and Technical Data, Records and Reports (PA-PSC§14; PMC-PSC§13)

The right of companies to commercial confidentiality should never include data about payments to the state. The definition of such information covered by the confidentiality provision in Article 14.6 of the PA-PSC and in Article 13.6 of the PMC-PSA would seem to currently cover such revenues. Therefore, there is an implied prohibition over public release of such information in Article 14.6 (a) of PA-Act's PSC and in Article 13.6(a) Code's PSA. This should be amended to avoid an inadvertent clash with requirements for revenue transparency.

Forthcoming oil fund legislation

The government may also want to consider turning the forthcoming Oil Fund law into a wider revenue management law, which would cover both the management of an Oil Fund and the disclosure of revenue flows from companies into the government's accounts.

We do not see this as adding any substantial addition burden or time delay the drafting of such controls. Indeed, there is already excellent model legislation for revenue management, drawn up by New York's Columbia University for Sao Tome and Principe, that the government and its advisors may find helpful to this end.²

Thank you.

² The legislation in English and Portuguese can be viewed at www.earth.columbia.edu/cgsd.