

Timor Sea Joint Petroleum Development Area: Production Sharing Contracts Atop a Fragile Maritime Boundary

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Disclaimer

The information provided in this presentation is in summary form and is designed to alert parties to various issues and developments of general interest. The information is not comprehensive, is not offered as legal advice, and should not be used to formulate business or other fiscal decisions.



Why Re-hash the Topic?

- Persistent uncertainty as to the applicable law and enforcement
- Who owns the resources?
- What law applies to the exploration, extraction of the resources?
- Can structuring impact the applicable law?



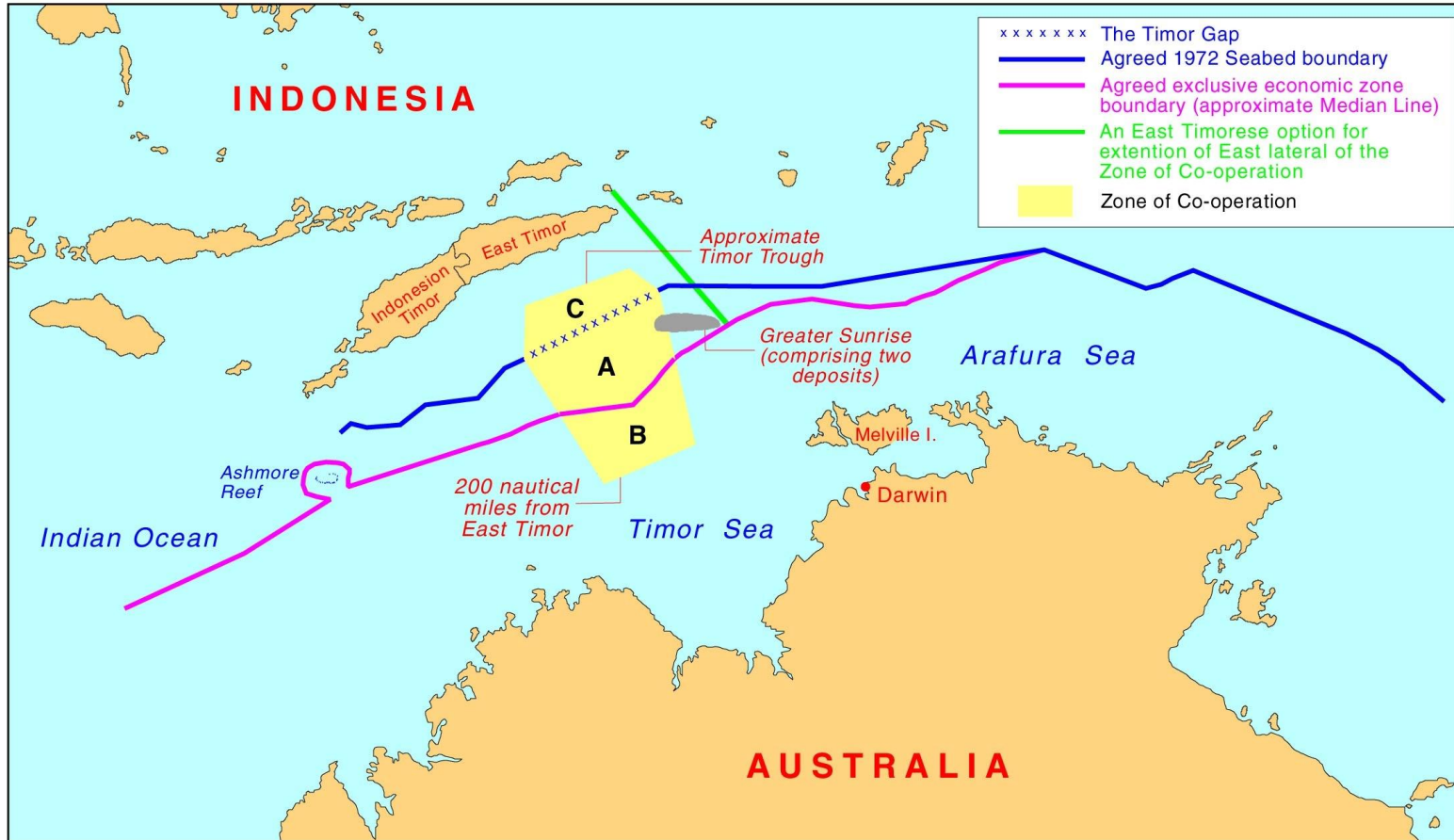
Why Re-hash the Topic?

- Significant recent developments:
 - Timor Leste arbitration to the Hague to invalidate CMATS following espionage claims.
 - Whistleblower investigation by Fed Police re espionage tip-off and impact on the Hague arbitration
 - Timor Leste proceedings in ICJ concerning raid on their lawyers' office and seizure of material
 - Change in governments of Australia, Timor Leste and Indonesia

Why Re-hash the Topic?

- Oilex Limited seeking mutual termination of its PSC
- Conocophillips embroiled in tax proceedings
- Woodside announcing that Sunrise Project to be frozen pending certain developments
- Timor Leste entering talks with Indonesia in August 2015;
- China investing heavily in Timor Leste
- Has fuelled doubts of Operators: Can they carry on under their PSCs?

1972 “Seabed Boundaries in the Area of the Timor and Arafura Seas” Agreement between Australia and Indonesia



Source: <http://www.atns.net.au/agreement.asp?EntityID=711>

Historical Agreements and Treaties

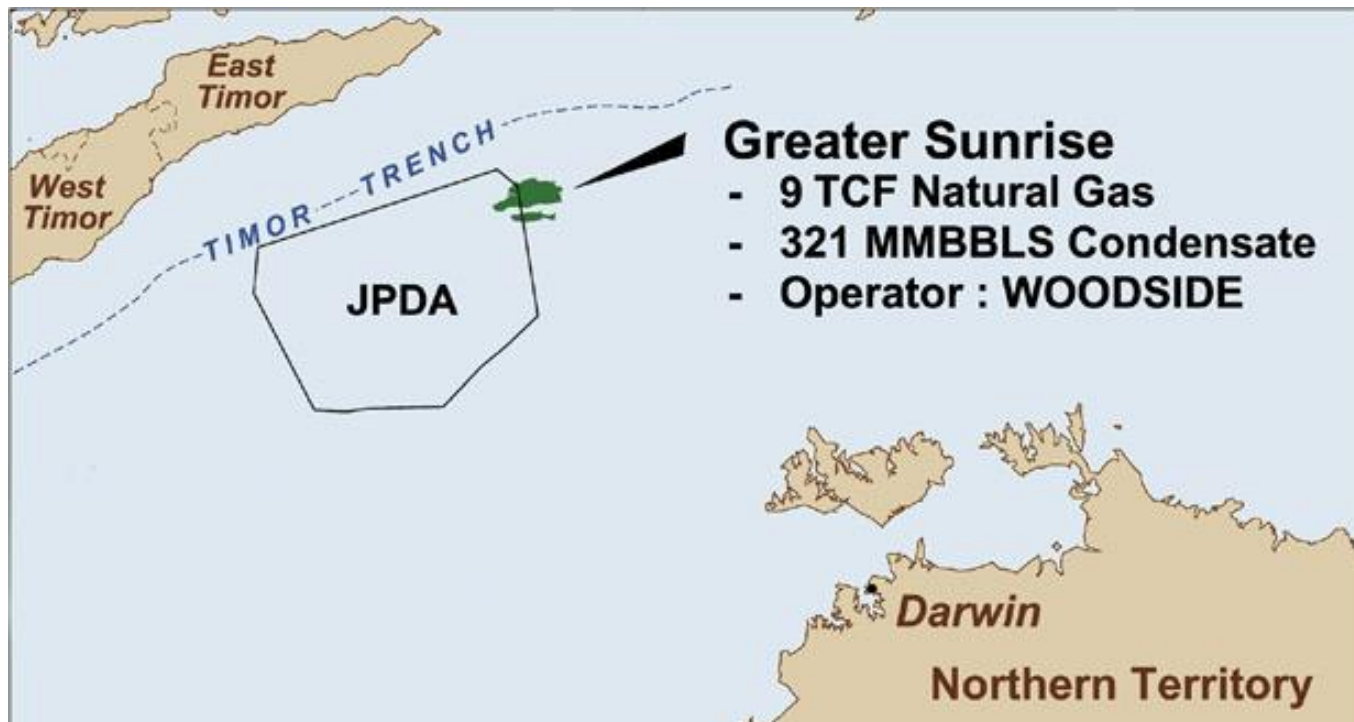
- 1972 “Seabed Boundaries in the Area of the Timor and Arafura Seas” Agreement between Australia and Indonesia
- In force 8 November 1973
- Australia have sovereign rights over seabed to limit of the continental shelf (closer to Indonesia than Australia)
- Agreement left a “gap” in Timor Sea:- “Timor Gap”
- Portugal key to its closure.

Historical Agreements and Treaties

- 1989: Previous 1972 “Seabed Boundaries” agreement superseded by the “Timor Gap Treaty”
- Recognised the Australian claim to the continental shelf up to the Timor Trough
- 1999 Timor-Leste separated from Indonesia
- Independence 2002
- 20 May 2002 “Timor Gap Treaty” then superseded by the “Timor Sea Treaty”
- In force 2 April 2003
- Covered JPDA and part of Greater Sunrise Gas Field

The Greater Sunrise Gas Field

- Gas field lies 20% inside the JPDA and 80% on the Australia side of the JPDA



Source: <http://www.hydrocarbons-technology.com/projects/sunrise-gas-field/sunrise-gas-field4.html>

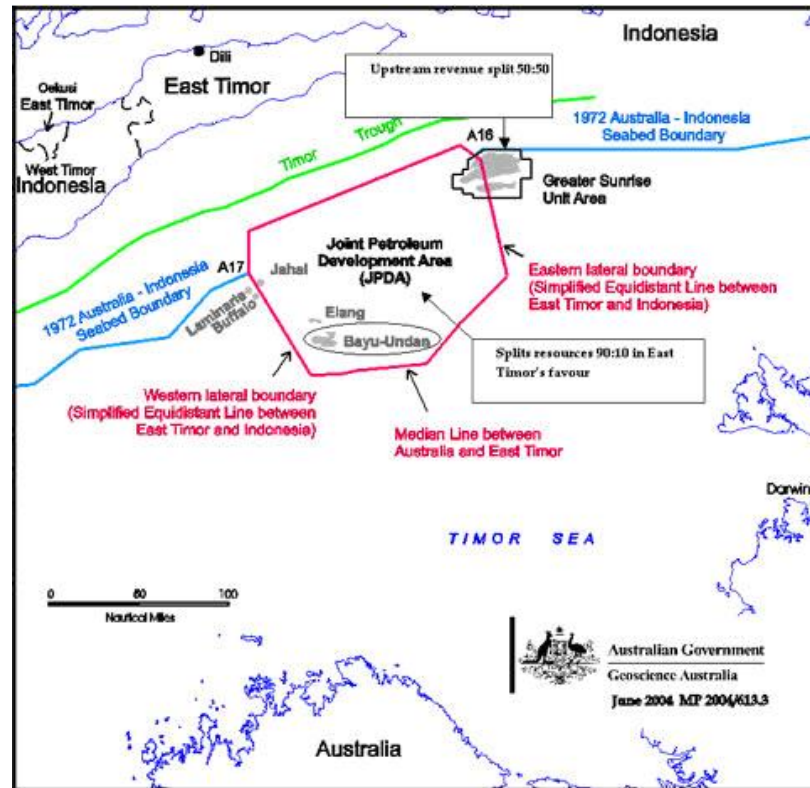
Further development of the laws in the JPDA

- 23 February 2007: “Treaty on Certain Maritime Arrangements in the Timor Sea”
- Article 6 “Timor Sea Treaty” established three-tiered administrative structure: Designated Authority; Joint Commission and the Ministerial Council.
- 2 April 2003: the Joint Commission enacted the “Interim Petroleum Mining Code” (the “IPMC”)
- 16 June 2003: the Designated Authority enacted the “Interim Regulations” under Article 37 of the IPMC (the “IPRs”)
- IPRs supplemented on 16 June 2003 by “Interim Directions” under Article 37 of the IPMC (the “IDs”)

Further development of the laws in the JPDA

- 2005: “Petroleum Mining Code” (the “PMC”) was enacted which repealed the IPMC but not the IPRs or IDs
- Early 2006: attempt to consolidate and update produced the draft “Technical Regulations for the Exploration and Exploitation of Petroleum in the JPDA” (the “TRs”)
- May 2008: Designated Authority called for public comment on the TRs.
- 30 June 2008: Article 6(b)(ii) of the Timor Sea Treaty, old Designated Authority ceased to exist.
- Replaced with Timor Leste “Autoridade Nacional do Petrllleo” (or National Petroleum Authority) (the “ANP”)
- What of the TRs?

Current agreed Boundaries in the JPDA?



Source: <http://www.industry.gov.au/resource/UpstreamPetroleum/>

The ANP's 2014 Annual Report

- The President stated:

“In 2014 ANP continue to review the upstream legal framework aiming for better governance of the Petroleum resources exploration and exploitation... This legal framework review includes the JPDA technical regulation and PSC model contract. A suite of documents in preparation for 2015 acreage release ... have been prepared for further consideration of the board.”

Production Sharing Contracts in the JPDA

- Interesting to note the terms of the standard Production Sharing Contracts entered into between the ANP and Operators of Projects:
 - Clause 12: Disputes relating to the interpretation and performance of the PSC **and** relevant provisions of the Timor Sea Treaty and the PMC to ICC Arbitration in Singapore
 - Clause 20: The contracts are governed and construed in accordance with English Law.

Increased concerns as to the legal framework in the JPDA and Sunrise Field

- Escalation of concern on part of key stakeholders as to the stability of the laws applicable in the JPDA and Greater Sunrise Area

Oilex

- Encountering difficulties in drilling the required wells under its PSC
- Various extensions by Timor Leste
- April 2013, Timor Leste referred dispute with Australia over validity of the CMATS to the Hague
- July 2013, Oilex sought Timor Leste agreement to the mutual termination of its PSC citing concerns over the unilateral rights of Australia and Timor Leste to terminate CMATS and impact rights in the JPDA.
- Rejected:- self-serving
- July 2015, Timor Leste terminates PSC: holds Oilex liable for damages

Increased concerns as to the legal framework in the JPDA and Sunrise Field

ConocoPhillips

- Challenges to tax assessments made on behalf of Timor Leste regarding Bayu Udan revenues
- Complicated for both, by fraud perpetrated by a petroleum tax adviser engaged by Norway and offered to Timor Leste as part of an aid program
- Inadequate (if any at all) HR due diligence
- Actually convicted fraudster: 3 years in USA jail
- Stole \$3.5M from Timor Leste
- Compromised tax clawbacks of \$236M from ConocoPhillips
- Arrested by FBI
- Charged US Wire Fraud and multiple others
- Pleaded guilty
- Sentenced October 2015

Increased concerns as to the legal framework in the JPDA and Sunrise Field

Woodside

- Conflict over where to build a new processing facility for refinement and liquefaction of the raw product extracted from the Sunrise Project.
 - Timor Leste wants plant onshore Timor Leste and pipeline
 - Woodside preference is FLNG or plant onshore Australia with pipeline
- The legal implications depending on where this facility is built are vast:
 - If constructed onshore Timor Leste with a pipeline connecting to the field:- subject to the Timor Leste jurisdiction
 - If the facility was built in Australia with the necessary pipeline:- Australian law would have precedence
 - FLNG? Multiple jurisdictional issues

Increased concerns as to the legal framework in the JPDA and Sunrise Field

- February 2015:- Timor Leste new Prime Minister declares:
 - Rejects Woodside preference;
 - Timor Leste will forge ahead with the CMATS Arbitration and then draw new boundary
- Woodside responds to declare that it will not proceed with Sunrise Project until there is some stability
- March 2015, Timor Leste state that it would be happy to buy out any disenchanted party in Sunrise
- No one jumps at the offer

Force Majeure clause in the relevant PSCs

Force Majeure clause in the relevant PSC:

- Force Majeure is not a common law concept, such that parties can agree to whatever scope they wish
- Clause 18.1(a) of the PSCs provides:

“... a Party shall not be liable for any failure to perform an obligation under this Agreement to the extent such performance is prevented, hindered or delayed by events or circumstances which are beyond its reasonable control and the effects of which could not (including by reasonable anticipation) and cannot reasonably be avoided or overcome by it (“Force Majeure”)”

Force Majeure clause in the relevant PSCs

- Clause 18.1(b)(ii) of the PSCs provides:

“... In the case of a Contractor, the law, or any action or inaction of the government, of a place other than Timor-Leste or Australia ...”

- Clause 18.1(b)(iii) of the PSCs provides:

“...In the case of a Designated Authority, the law, or any action or inaction of the government of Timor Leste or Australia”

Force Majeure clause in the relevant PSCs

- Appears to leave it open to argue that the action taken by the Timor Leste government to seek to have CMATS declared *void ab initio* entitles the Operator to claim force majeure
- On the basis that its obligations are “hindered” or “delayed” by such action which is “beyond its reasonable control”
- The clause also makes no express reference to the implications of any particular duration of a force majeure event.
- Significant, as where the event has radically changed the nature of the contract so that it would be inequitable to hold either party to the contract, it could be argued that the contract is “frustrated”.

THANK YOU

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