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AND ADVICE FOR THE PARLIAMENT

INFORMATION AND RESEARCH SERVICES

Bills Digest  
No. 6 2003–04

## **Petroleum (Timor Sea Treaty) Bill 2003**

ISSN 1328-8091

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Petroleum (Timor Sea Treaty) Bill 2003

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28 July 2003

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# Petroleum (Timor Sea Treaty) Bill 2003

**Date Introduced:** 5 March 2003

**House:** Representatives

**Portfolio:** Industry, Tourism and Resources

**Commencement:** On the day of Royal Assent but, where relevant, various provisions in the Bill are made retrospective in operation to coincide with the date of the signing of the Timor Sea Treaty between Australia and East Timor (20 May 2002).

## Purpose

This Bill is part of a package of Bills to give effect to the Timor Sea Treaty signed by Australia and the newly independent nation of East Timor on 20 May 2002.

## Background

[This Bill was the subject of urgent passage and passed both Houses on 6 March 2003. This Bills Digest has been prepared after the debate.]

### The Timor Gap Treaty between Australia and Indonesia

As a courtesy, it is noted that the nation of East Timor prefers the name Timor L'Este.<sup>1</sup> For convenience, references in this Digest will be to East Timor, consistent with the name used in the legislation and in the Timor Sea Treaty.

In 1975, East Timor was incorporated into Indonesia and was annexed the following year. The United Nations did not recognise Indonesia's annexation and continued to regard East Timor as under the administration of Portugal. Australia was the only country to recognise Indonesia's annexation. In 1989, Indonesia and Australia concluded negotiations over a treaty for joint exploration and production of oil and gas under the Timor Gap Treaty. The Timor Gap Treaty was signed on 11 December 1989.

Australia gave effect to the Timor Gap Treaty by enacting the *Petroleum (Timor Gap Zone of Cooperation) Act 1990*. The Timor Gap Treaty provided a provisional settlement of a

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dispute over the seabed boundary line and it established a ministerial council and joint authority involving Australia and the Republic of Indonesia to jointly develop the rich reserves of oil and gas in the Timor Sea area. The Timor Gap Treaty included annexes dealing with a Petroleum Mining Code and a taxation code.<sup>2</sup>

The use of the word 'gap' reflected a long-standing delimitation issue involving Portugal, Australia and Indonesia concerning the seabed boundary line of the Timor Sea. Portugal maintained that the boundary line was the median distance between East Timor and Australia. Australia maintained that the boundary was delimited by the Timor Trench, a deep seabed depression closer to East Timor and which Australia asserted was the edge of its continental shelf. Indonesia recognised the Australian position.

The boundary issue is significant because the disputed area contains the major Bayu-Undan oil and gas field. Another field, the Greater Sunrise Field, straddles the boundary with 79.9% of the field within Australian jurisdiction.<sup>3</sup> Where a resource field straddles an international boundary an International Unitisation Agreement (IUA) can be negotiated to define the scope of the resource and to provide terms for the administrative and regulatory regimes that will apply. The field is then treated as a single unit.

## The Separation of East Timor from Indonesia

East Timor separated from Indonesia on 26 October 1999 and after a period of civil unrest, which was brought under control by United Nations peacekeepers, became an independent nation on 20 May 2002. On separation, Indonesia no longer had jurisdiction over East Timor. Between separation and independence the continuation of exploration and development of the oil and gas resources was the subject of an agreement between Australia and the United Nations Transitional Administration in East Timor (UNTAET).

## The Timor Sea Treaty between Australia and East Timor

Australia signed the Timor Sea Treaty with East Timor on 20 May 2002. The treaty was tabled in Parliament on 25 June 2002.

At the time that the treaty was signed it was envisaged that the negotiations for the IUA for the Greater Sunrise field would be concluded by December 2002. The Joint Standing Committee on Treaties recommended (at Recommendation 2) that:

[T]he Government of Australia use its best endeavours in accordance with the Memorandum of Understanding signed in Dili on 20 May 2002 to conclude the International Unitisation Agreement for the Greater Sunrise fields on or before the date on which the Timor Sea Treaty is ratified and in any event before 31 December 2002 as this would serve the best interests of both nations.<sup>4</sup>

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The ratification of the Timor Sea Treaty is a fundamental condition precedent to the exploitation of the gas and oil resources. Contractual obligations of the commercial venture partners for the Bayu-Undan field were premised on ratification of the treaty, preferably by the end of 2002, to enable sufficient lead-time for infrastructure, such as on-shore facilities, to start construction. This Bill, to enable the ratification of the Timor Sea Treaty, required urgent consideration on 5 and 6 March 2003 because the deadline for the Bayu-Undan commercial contract was the 11 March 2003. At the time the Bill was debated in the House of Representatives on 5 March 2003, the IUA for the Greater Sunrise field remained unsigned. It was signed on 6 March 2003.

The deep Timor Trench precludes pipeline delivery for on-shore processing in East Timor. Instead, on-shore infrastructure will be constructed in and around Darwin. The likely investment in the Northern Territory by the developers associated with the Bayu-Undan field is estimated at \$3 billion for a pipeline to Darwin and a liquid natural gas (LNG) plant at Wickham Point, near Darwin.<sup>5</sup>

The former Timor gap area was referred to as the Zone of Cooperation. Under this legislation that area will be known as the Joint Petroleum Development Area (JPDA). The Timor Sea Treaty provides that the title to all petroleum in the JPDA belongs to both East Timor and Australia on the basis of 90% of the petroleum attributed to East Timor and 10% to Australia. In the case of the Greater Sunrise Field, which straddles the JPDA boundary line, East Timor is likely to be entitled to 90% of the 20% of the field that falls within the JPDA i.e. 18% of the total field. The expected revenue stream to East Timor from its share of the oil and gas resources is likely to be significant and critical for this emerging nation.

Unless there is a permanent delimitation of the Timor Sea seabed, the Timor Sea Treaty will remain in force for 30 years.<sup>6</sup> The treaty does not prejudice territorial claims. To that extent, the treaty is regarded as a practical provisional arrangement under international law (see Article 2 of the Timor Sea Treaty).

## Main Provisions

### Part 1—Preliminary

**Clause 4** authorises specified regulatory bodies to exercise the rights and responsibilities of Australia in relation to activities covered by the Timor Sea Treaty. These bodies are the 'Ministerial Council' (the Australia-East Timor Ministerial Council) and the 'Joint Commission' (the Australia-East Timor Joint Commission). The Joint Commission in turn designates the 'Designated Authority' under Article 6 of the Timor Sea Treaty. The Designated Authority has the power to contract and to be party to legal proceedings. It is responsible for the day-today regulation and management of petroleum activities under the Timor Sea Treaty.

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## Part 2—General Provisions

**Clause 6** and **Clause 7** prohibit prospecting or production, respectively, within the JDPDA without the approval of the Designated Authority. **Clause 7** recognises that approval extends to parties to a production sharing contract concluded with the Designated Authority.

**Clause 8** confers and specifies the powers of inspectors who are certified and appointed to ascertain whether 'petroleum activities' in the JDPDA comply with the Petroleum Mining Code and with relevant contract terms and conditions.

**Clause 9** confers federal jurisdiction on appropriate State and Territory courts to hear civil litigation by Australians (including a permanent resident) for damages or expenses relevant to JPDA activities.

**Clause 10** applies the civil laws of the Northern Territory for litigation referred to in Clause 9.

## Part 3—Tax provisions

**Clause 12** applies the Timor Sea Treaty and its Taxation Code to Australian tax laws that deal with fringe benefits, income tax and the superannuation guarantee. The Medicare levies are treated as income tax (**Clause 13**). The *Alert Digest* (No. 3 of 2003) of the Senate Standing Committee for the Scrutiny of Bills has noted, in the context of any likely retrospective effect to **Part 3—Tax provisions** in the Bill, that there:

...is no assurance in the Explanatory Memorandum that the commencement of that Part on 20 May 2002 will not adversely affect taxpayers.<sup>7</sup>

**Clause 15** provides a formula to determine the gross tax payable for a person who is not a resident of Australia but who derives income from the JPDA. That person is entitled to a 90% rebate on the gross tax payable.

## Division 2—Application and other provisions

This Division applies the Taxation Code contained at Annex G of the Timor Sea Treaty as a 'new taxation code' and it continues the operation of the 'old taxation code' that was included in the now redundant Timor Gap Treaty (the Zone of Cooperation established by Australia and Indonesia in 1989) up to 20 May 2002 when the 'new' Timor Sea Treaty was signed with East Timor. This Division is necessary because the key date of 20 May 2002 falls within a financial year for income tax purposes.

**Clause 19** provides a short-term taxation exemption to an individual who is a resident of East Timor. East Timorese are not liable to pay tax on income derived from the JPDA until 1 July 2003. This concession recognises that the resident should not be taxed where

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they had no prior awareness of an obligation to pay the specific taxes imposed by the Timor Gap Treaty.

#### Part 4—Transitional provisions

This Part contains provisions that allow the validation (retrospectively, where necessary) of approvals, contracts and actions taken under the authority of the Timor Gap Zone of Cooperation legislation including the former Petroleum Mining Code.

**Clause 23** allows the Joint Commission to adopt an Interim Petroleum Mining Code, if necessary, pending final agreement to any new Petroleum Mining Code.

#### Schedule 1—Timor Sea Treaty and its Annexes

The Schedule contains the Timor Sea Treaty and its Annexes. The Timor Sea Treaty is comprised of a series of Articles agreed to by Australia and East Timor.

**Article 3** establishes the Joint Development Petroleum Area (JDPA) by reference to the coordinates specified in Annex A to the Treaty.

**Article 6** establishes the regulatory bodies consisting of a Designated Authority, a Joint Commission and a Ministerial Council. The Ministerial Council will have an equal number of Australian and East Timorese Ministers. If the Council is deadlocked, either country may invoke the dispute resolution procedure in Annex B. The Joint Commission has Commissioners appointed by Australia and East Timor but East Timor shall have one more Commissioner than Australia. The Joint Commission is responsible for policies and regulations and it oversees the work of the Designated Authority. The powers and functions of the Designated Authority are specified at Annex C and include:

- day-to-day management of petroleum activities
- lines of communication for security, air traffic and search and rescue activities
- controlling movements within the development area
- pollution prevention measures, and
- reporting requirements.

The specific powers and functions of the Joint Commission are set out in Annex D.

**Article 9** requires Australia and East Timor to work 'expeditiously and in good faith' to reach agreement on a joint IUA to cover a petroleum area that straddles the boundary of the JDPA. The resource is then managed as a single unit.

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**Article 10** requires Australia and East Timor to use best means to protect the marine environment from the harmful consequences of petroleum activities.

**Article 11** encourages measures that give preference to the employment of nationals or permanent residents of East Timor.

**Article 13** applies the Taxation Code set out in Annex G. A detailed explanation of the Taxation Code is provided in the Explanatory Memorandum to the Bill. As mentioned above, the *Alert Digest* (No. 3 of 2003) of the Senate Standing Committee for the Scrutiny of Bills has noted, in the context of any likely retrospective effect to **Part 3—Tax provisions** in the Bill, that there:

...is no assurance in the Explanatory Memorandum that the commencement of that Part on 20 May 2002 will not adversely affect taxpayers.<sup>8</sup>

**Article 14** applies the criminal law of Australia or East Timor, respectively, to its nationals (or permanent residents). A third country national is subject to the criminal laws of both countries, except that only one country's criminal law can be applied (Australia and East Timor may consult as to which country will enforce their criminal law). A flag State retains the right to apply its criminal law for unlawful actions taken on board a vessel or aircraft in the development area.

**Article 18** allows surveillance by Australia or East Timor in the development area. Both countries will cooperate on and exchange information derived from surveillance activities.

**Article 22** provides that the duration of the Timor Sea Treaty is 30 years from the date of its entry into force, unless there is an earlier permanent delimitation of the national seabed boundary between Australia and East Timor.

## Concluding Comments

East Timor's long-term economic survival depends on the development of the oil and gas reserves in the Timor Sea. UNTAET estimates that the Bayu-Undan field will deliver \$3 billion in revenue to East Timor over 17 years.<sup>9</sup> Without this revenue stream, East Timor would be heavily dependent on foreign aid. The economy of East Timor has a likely future potential in tourism, fisheries and agriculture (including coffee).

The reports of the discussions leading up to the Timor Sea Treaty indicate that the negotiations were robust. Formal negotiations began in October 2000. In January 2001, it was reported that Australia may have underestimated how well prepared the East Timorese negotiators were when entering the negotiations. In an article by Hamish McDonald with the title 'Oil is more important to us than to Australia, says Gusmao' in the *Sydney Morning Herald* of 15 January 2001, the following statement was reported:

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The Australian side never expected the Timorese side would have prepared their position and would make the claims we did. And from the East Timorese side we never expected that the Australians would come with such a conservative position. It was a real shock to both sides.<sup>10</sup> (Dr Mari Alkatiri, now Prime Minister of East Timor)

The article states that the initial Australia position was a 60:40 split in favour of East Timor. The Timor Sea Treaty eventually established a 90:10 split in favour of East Timor.

A further issue that appears to have caused concern during the negotiation period was Australia's withdrawal in March 2002 from the International Court of Justice's jurisdiction to determine disputes on maritime boundaries. That move was reported to have 'astonished the international community'.<sup>11</sup>

The brief but intense debate on the package of Bills in the Australian Parliament focused largely on the delays encountered in settling the IUA relating to the Greater Sunrise field and the obvious urgency of the ratification legislation. In the Senate, the Australian Democrats and the Australian Greens specifically recorded that they voted against the legislation.<sup>12</sup>

The legislation passed the Senate without amendment on 6 March 2003.

## Endnotes

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- 1 See the comments of Mr K. W. Wilkie MP, 'Second Reading speech', in the House of Representatives, *Debates*, 5 March 2003, p. 12299.
- 2 The Hon Alan Griffiths MP, Minister for Resources, 'Second Reading speech', Petroleum (Australia-Indonesia Zone of Cooperation) Bill 1990, House of Representatives, *Debates*, 8 May 1990, pp. 68.–70.
- 3 For more detail, see *The Timor Sea Treaty – Report 49*, Joint Standing Committee on Treaties, Parliament of the Commonwealth of Australia, November 2002.
- 4 *ibid.*
- 5 Office of Territory Development, Department of the Chief Minister for the Northern Territory, internet website information on Bayu-Undan, [www.otd.nt.gov.au](http://www.otd.nt.gov.au), updated on 1 April 2003.
- 6 *The Timor Sea Treaty – Report 49*, Joint Standing Committee on Treaties, Parliament of the Commonwealth of Australia, November 2002, p. 5.
- 7 *Alert Digest*, No. 3 of 2003, Senate Standing Committee for the Scrutiny of Bills, 19 March 2003, p.11.
- 8 *ibid.*
- 9 Geoff Hiscock, 'Oil the fuel for East Timor', *CNN.com/business*, 17 May 2002.

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- 10 Hamish McDonald, 'Oil is more important to us than to Australia, says Gusmao', *Sydney Morning Herald*, 15 January 2001.
- 11 Kalinga Seneviratne, 'Canberra slammed for "bullying" Timor', *Asia Times*, 11 March 2003.
- 12 Senate, *Debates*, 6 March 2003, p. 9399.

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