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Committee Secretary  
Joint Standing Committee on Treaties  
PO Box 6021  
Parliament House  
Canberra ACT 2600

**Joint Standing Committee on Treaties inquiry examining the Treaty between Australia and the Democratic Republic of Timor-Leste establishing their Maritime Boundaries in the Timor Sea ("Timor Treaty") (New York, 6 March 2018)**

Further to the Joint Standing Committee on Treaties' (JSCOT) invitation for interested organisations to make submissions on the above-referenced inquiry, ConocoPhillips (03-12) Pty Ltd (COPA) as operator of the Bayu-Undan Joint Venture thanks JSCOT for the opportunity to contribute to this process.

COPA as operator of the Bayu-Undan Joint Venture is undertaking petroleum activities in the Timor Sea, which activities have created and will continue to create direct and indirect benefit for Australia, Timor-Leste and for many other stakeholders. Both the existing Timor Sea Treaty and the Timor Treaty confirm that such petroleum activities will continue under "conditions equivalent". If there is any change to the fiscal, regulatory or contractual conditions that apply to those petroleum activities upon the Timor Treaty coming into effect, then there is potential for those petroleum activities to be immediately and materially impacted, and for the Bayu-Undan Joint Venture and other stakeholders to be significantly disadvantaged.

COPA therefore greatly appreciates the efforts that have been made by the Governments of Australia and Timor-Leste to set out specific transitional arrangements for Bayu-Undan within the Timor Treaty. COPA also looks forward to engaging with the Australia and Timor-Leste representatives in building-out the detail of the transitional arrangements that, when implemented, will provide equivalent fiscal, regulatory and contractual conditions to those that currently exist today.

Given the longstanding and complex nature of current fiscal, regulatory and contractual conditions, the detailed implementation of the transitional arrangements will be a significant and complex undertaking. The implementation process will also need to be completed prior to the Timor Treaty coming into effect so that the requisite stability and certainty exists for ongoing and future petroleum activities.

COPA provides the following written submission to JSCOT, which it hopes will be of assistance to Australia and Timor-Leste as the detail of the transitional arrangements is built-out and the plan for implementation is developed.

## Background

The Bayu-Undan field is a large gas-condensate field. The field is located in the Timor Sea, currently within the Joint Petroleum Development Area (JPDA), and will be within exclusive Timor-Leste waters upon ratification of the Timor Treaty. It is located offshore 500 km north-west of Darwin, NT, Australia and 250 km southeast of Suai, Timor-Leste. A 26-inch, 500 km subsea export gas pipeline connects Bayu-Undan to the Darwin LNG plant where gas from Bayu-Undan is processed into LNG. The investment in the facilities was underpinned by the Bayu-Undan Joint Venture through committing sales of LNG under long-term contracts to major Japanese LNG buyers, which arrangements remain in force today. The Bayu-Undan field began production in 2004 pursuant to two productions sharing contracts (PSC 03-12 and PSC 03-13). Throughout its' life to date the Bayu-Undan project has provided more than US\$20 Billion in taxation and royalty revenues to the governments of Timor-Leste and Australia.

In accordance with the existing fiscal regime, PSC revenues are currently distributed 90% to Timor-Leste (with Timor-Leste taxes generally applicable to 90% of business profits and activity) and 10% to Australia (with Australian taxes applicable to 10% of business profits and activity). When the Timor Treaty comes into force, PSC revenues will be distributed 100% to Timor-Leste, and Timor-Leste taxes will apply to 100% of business profits and activity.

## Timor Treaty Transitional Arrangements

The existing Timor Sea Treaty (TST), Article 22, states that if the TST is no longer in force, Bayu-Undan petroleum activities shall continue under "conditions equivalent" to those in place today under the TST. The Timor Treaty acknowledges and reiterates this obligation in Annex D, Article 1.1.

Further Annex D, Article 2.2, sets out that Australia and Timor-Leste agree to maintain the fiscal regime relating to both the upstream and downstream components of the exploitation of the Bayu-Undan Gas Field. Para. 49 of the National Interest Analysis acknowledges that, in addition to the general obligation to maintain conditions equivalent, Australia and Timor-Leste have agreed to grandfather existing arrangements.

The existing Bayu-Undan regulatory and contractual regime was the subject of extensive negotiation between the stakeholders and was the basis upon which investment decisions were made. As detailed in the attached schedule, it is substantial and very complex in nature and has been in operation for many years.

To provide the requisite stability and certainty for petroleum companies with continued operations in the Timor Sea, the detailed implementing arrangements will need to respect and ensure continuity of:

- Security of title: it is expected that the replacement PSCs will preserve the existing terms of the current PSCs with regards to ownership rights, security of title and entitlement to petroleum produced. As such, the calculations of entitlement to share of petroleum under the PSCs for the Bayu-Undan Joint Venture and the Government entity PSC counterparty should remain the same.
- Contractual position: it is expected that the sanctity of existing contracts will be preserved, including all actions, commitments and decisions already taken under them (e.g. the Development Plan, the Decommissioning Plan, audits previously completed and concluded and existing commercial arrangements). As such, the obligations and duties of the Bayu-Undan Joint Venture should not increase, nor will their rights, powers, authorities and discretions decrease.
- Operational activities: it is not expected that there will be any change to the way in which petroleum activities are undertaken compared to the way in which they are undertaken at

present. As such, the Timor Treaty should not result in any disruption to ongoing petroleum activities, nor jeopardise the safety, efficiency and cost of ongoing operations in the Timor Sea.

- **Fiscal regime:** it is expected that the existing fiscal regime will be fully maintained or grandfathered, including the preservation of the rights and obligations of the Bayu-Undan Joint Venture under the existing PSCs and the taxation code. As such, there should be no increase to costs or taxes incurred by the Bayu-Undan Joint Venture, nor any reduction to their revenue entitlements. Rights to use existing or future tax benefits should also be preserved. Maintaining the existing fiscal regime will be a particularly complex aspect to the 'grandfathering process'. To illustrate this complexity with a couple of examples:
  - i. under existing arrangements, Bayu-Undan joint venture companies have substantial costs that are allowable as future tax deductions under the Australian tax regime. These future tax deductions are not available under the existing Timor-Leste tax regime, where such costs have already been deducted. Notwithstanding that Timor-Leste taxes will apply to 100% of business profits and activity, it is expected that the new fiscal regime will take account of the existing or future tax deductions that would have been available to each Bayu-Undan Joint Venture participant under the Australian tax regime;
  - ii. with respect to Australian employees, arrangements are currently in place to prevent double taxation by ensuring that Australian employees obtain a full tax credit/offset for all Timor-Leste wages tax. It is expected that this special provision will be replicated in the Australian provisions implementing the Timor Treaty.
- **Regulatory regime:** it is expected that the existing regulatory regime, as set out in the attached schedule, will be appropriately translated into Timor-Leste domestic law, as contemplated by the Timor Treaty.

To ensure that the Bayu-Undan Joint Venture and other stakeholders are not disadvantaged by the Timor Treaty coming into force, the existing fiscal, regulatory and legal regime will need to be effectively grandfathered, such that relevant matters (such as those mentioned above) are comprehensively addressed prior to the Timor Treaty coming into effect.

#### Detailed Engagement

Ensuring that the transitional arrangements, including drafting detailed implementing provisions, effectively satisfies the Timor Treaty's obligations on Australia and Timor-Leste to provide equivalent conditions to the Bayu-Undan Joint Venturers as those existing today will require significant input and collaboration between Timor-Leste, Australia and the Bayu-Undan Joint Venture. COPA appreciates the significance of this effort and has the required resources ready to engage and work with the Governments.

We welcome the opportunity to provide any further information that JSCOT requires with respect to this submission and look forward to future engagement with Australia on the transitional arrangements.

Yours sincerely,



**Chris Wilson**  
President, Australia West

### Schedule - Existing Bayu-Undan Fiscal, Regulatory and Contractual regime

The fiscal and regulatory framework currently applicable to Bayu-Undan includes:

- Timor Sea Treaty, including
  - Establishing the rights and obligations of Contractors
  - An allocation of taxing and revenue rights 90% to Timor-Leste and 10% to Australia
  - Provisions for application of immigration, customs and criminal jurisdiction and employment taxes
  - Exclusion of customs duties and excise in relation to Bayu-Undan activities in the Timor Sea
- The Timor Sea Treaty Taxation Code which provides for the avoidance of double taxation and includes limitations and rules on the application of taxes by Australia and Timor-Leste such as:
  - An allocation of tax on business profits being 90% Timor-Leste and 10% Australia;
  - Caps on certain tax rates; and
  - Rules on determination and calculation of income that is subject to tax under the laws of Australia and Timor-Leste respectively for all persons including sub-contractors and employees
- Interim Petroleum Mining Code for the Joint Petroleum Development Area ("JPDA")
- Interim Regulations for the JPDA
- Interim Directions for the JPDA
- Interim Administrative Guidelines for the JPDA
- Memorandum of Understanding relating to the regulation of a pipeline from Bayu-Undan field in the JPDA to a landing near Darwin, Northern Territory
- Timor taxation law, subject to the existing TST, including:
  - Tax Stability Act, 2003
  - Taxation of Bayu-Undan Contractors Act, 2003
  - Taxes and Duties Act, 2008
  - Law on Income Tax applicable in Timor-Leste under UNTAET Regulation No.1999/1
  - Law on Value Added Tax and the Law on Luxury Goods Tax, applicable in Timor-Leste under UNTAET Regulation No. 1999/1
  - Law on General Tax Provisions and Procedures applicable in Timor-Leste under UNTAET Regulation No. 1999/1 as modified by UNTAET Regulation 2000/18 (as amended) and other related regulations and tax rulings
- Australian taxation laws which are integrated with the existing TST, including:
  - Income tax assessment laws and tax rulings
  - The following entitlements which are of particular relevance to the determination of existing and future Australian taxation liabilities for Bayu-Undan Contractors:
    - i. Access to a consolidated taxation regime where Bayu-Undan Contractors may be able to offset taxable income from Bayu-Undan against costs incurred in other Australian operations; and
    - ii. Entitlement to future income tax deductions for Bayu-Undan costs, which can be offset against income from other Australian operations.

The contracts to which the Bayu-Undan PSC Contractors are a party either with the governments or Designated Authority (as established by the TST) or as agents on behalf of the Designated Authority, or under approval from the Designated Authority include:

- PSC's 03-12 and 03-13 which include" ... the rights accorded to it under the Treaty, including the Petroleum Mining Code and the taxation code";
- Gas Transportation Agreement - Bayu-Undan to Darwin Pipeline;

- Feed Gas Sale and Purchase Agreement between Darwin LNG Pty Ltd and the Bayu-Undan Contractors.
- Bayu-Undan LPG and Condensate sales and marketing agreements
- Various taxation arrangements made with the government of Timor-Leste, including:
  - Tax Stability Agreement which effectively guarantees that there will be no change to the Timor-Leste tax obligations of the Bayu-Undan Contractors; and
  - Various other agreements made pursuant to the Tax Stability Agreement relating to application of taxation laws and tax dispute resolution.