



**A STUDY OF THE  
OFFSHORE PETROLEUM NEGOTIATIONS  
BETWEEN AUSTRALIA, THE U.N. AND EAST TIMOR**

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I declare that this thesis is the result of my original work and all sources have been acknowledged.

Alexander J. Munton  
14 June 2006





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## **ACRONYMS**

APODETI – Timorese Popular Democratic Association (Associação Popular Democrática Timorense)

AUD – Australian Dollars

CMATS – Treaty on Certain Maritime Arrangements in the Timor Sea

CNRT – National Council of Timorese Resistance (Conselho Nacional de Resistência Timorense)

DFAT – Department of Foreign Affairs and Trade

DISR – Department of Industry, Science and Resources

DPKO – United Nations Department of Peacekeeping Operations

EEZ – Exclusive Economic Zone

FRETILIN – Revolutionary Front for an Independent East Timor (Frente Revolucionária de Timor Leste Independente)

GDP – Gross Domestic Product

ICJ – International Court of Justice

INTERFET – International Force in East Timor

IUA – International Unitisation Agreement

JPDA – Joint Petroleum Development Area

LNG – Liquefied Natural Gas

LOI – Letter of Intent

LPG – Liquid Petroleum Gas

MoU – Memorandum of Understanding

OLA – United Nations Office of Legal Affairs

PRRT – Petroleum Resource Rent Tax

PSA – Production Sharing Area

PSC – Production Sharing Contract

UDT – Timorese Democratic Union (União Democrática Timorese)

UNTAET – United Nations Transitional Administration for East Timor

ZOC – Zone of Cooperation

ZOCA – Zone of Cooperation, Area ‘A’



## PROLOGUE

According to analysts of contemporary international conflict, the struggle for control of valuable natural resources has become an increasingly prominent feature of the global landscape.<sup>1</sup> In the wake of East Timor's transition to independence, in 1999, the Timor Sea became the location of one of the world's major international territorial disputes in areas containing oil and natural gas.<sup>2</sup> Prior to the dramatic political changes and devastation that took place in East Timor that year, the resources at stake were being managed by Indonesia and Australia under a bilateral treaty of joint petroleum development. During the 1990s, exploration and investment in the Timor Sea had flourished to such an extent that by the end of the decade the region was rapidly emerging as a key commercial centre of offshore oil and gas production. East Timor's transition changed the political future of this resource-rich area. The massive energy reserves of the Timor Sea were considered by the East Timorese to be an important element within their struggle for independence, *viz.*, an intrinsic part of self-determination.<sup>3</sup> Over a period of five years, from 2000 to 2005, Australia's and East Timor's conflicting claims to these petroleum resources would come to totally dominate the governments' bilateral relations.

In this thesis, I undertake a detailed investigation of the negotiations to resolve the dispute. The purpose of the research is to answer the basic analytical question of how negotiated outcomes have been determined. Part of the funding for this research has been provided by the Arafura Timor Research Facility (ATRF). This organization, based in Darwin, was established in 2002 as a joint venture between the Australian National University and the Australian Institute of Marine Sciences. The ATRF's mission is to conduct world class scientific research into the coastal and marine ecology of the Arafura and Timor Seas as well as the management of living and non-living resources.<sup>4</sup> My study was initially intended as an analysis of the problems relating to marine resource management and regional cooperation that naturally arise in enclosed, or semi-enclosed, seas. However, the focus of the research gravitated towards the territorial dispute between Australia and East Timor, which

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<sup>1</sup> Klare, M. T. 2001. *Resource Wars; the new landscape of global conflict*, Henry Holt and Co., New York.

<sup>2</sup> *Ibid.*, p.227-31.

<sup>3</sup> In a speech made to the South East Asia Australia Offshore Conference, in Darwin, 8 June 2004, East Timor's Prime Minister, Mari Alkatiri, stated that East Timor's legal and sovereign rights to the resources of the Timor Sea were "an integral part of rights to self-determination".

<sup>4</sup> See Arafura Timor Research Facility website at <http://www.atrf.org.au>

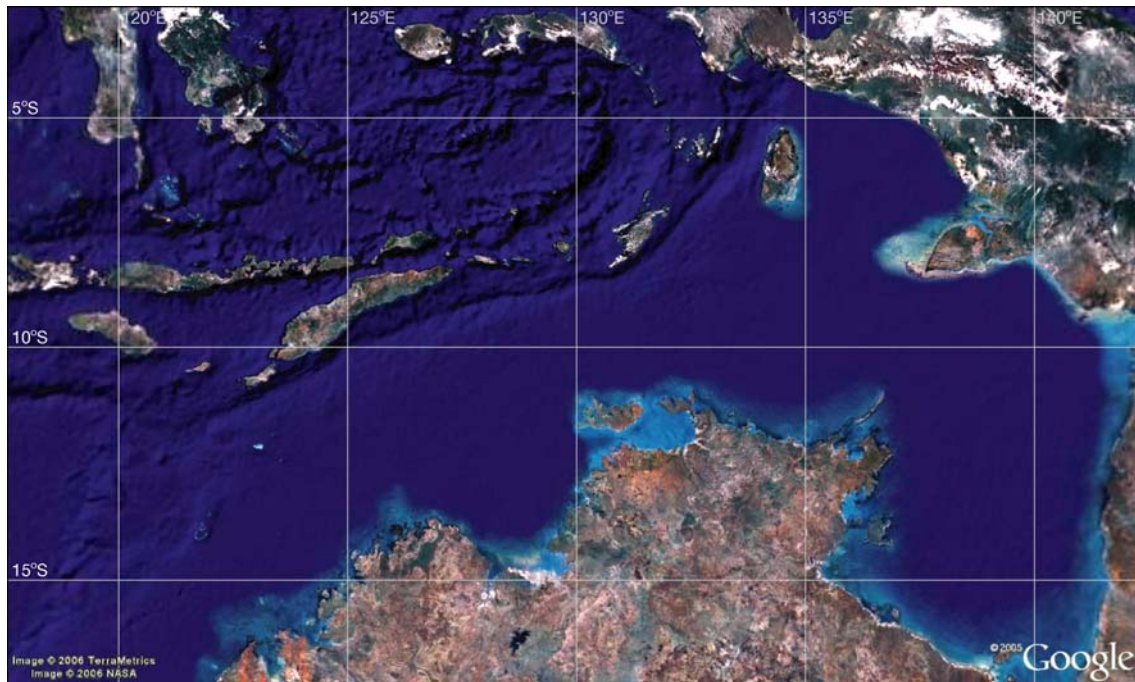
had the effect of almost obliterating everything else actually on the regional agenda.<sup>5</sup> As a result, this thesis is a study of an acute conflict over offshore oil and gas and the efforts to resolve that conflict through diplomacy.

The story of the negotiations is a remarkable one for the unusually complex range of factors that converged into the core of the bargaining dilemma. These factors are to be found within the unique history to the dispute, the extraordinary political circumstances surrounding the negotiations, the commercial evolution of the Timor Sea, as well as a complex range of legal and commercial issues that the talks encompassed. In 2003, I completed a short internship at the United Nations Division of Ocean Affairs and Law of the Sea (DOALOS), in the Office of Legal Affairs, New York. In spite of the key role played by a small group of UN representatives in the negotiations between Australia and East Timor during the period of transitional administration, there was little awareness outside of this group of how the bargaining process had actually unfolded. The curiosity I encountered during my time in DOALOS, amongst some UN staff, to know what had happened and why certain outcomes had been reached, had a large influence upon my own approach to the research. Confidential records of the negotiations existed, yet no-one had analysed this material and nothing had been written or published that documented the important events which had taken place. In this thesis, I have undertaken to fill that gap – to ensure that the process is not consigned to the ‘shadows of history’. Whilst the emphasis is on the particular story of these negotiations, both the theoretical and empirical content of this thesis contains important insights that are of wider relevance to the study of international negotiation and dispute settlement more broadly. Thus, in seeking to understand and explain the reasons for outcomes within the specific context, the conclusions that are drawn inevitably lead to a broader set of questions concerning conflict and cooperation in the international realm.

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<sup>5</sup> The tendency for disputes over offshore hydrocarbon resources to overshadow other issues on the regional agenda is not uncommon, as noted in Townsend-Gault, I., 1997. *International Boundaries and Environmental Security: frameworks for regional cooperation*, in G. Blake, C. Lia Sien, C. Grundy-Warr, M. Pratt and C. Schofield (eds), Kluwer Law International, London.

## THE TIMOR AND ARAFURA SEAS



*The Timor and Arafura Seas are enclosed by the maritime jurisdictions of three states: Australia, Indonesia and East Timor. This satellite image shows the landmass that surrounds these waters, with the northern coast of Australia, in the south, and the eastern arc of the Lesser Sunda islands running across the centre to the north. The island of Timor is the centrally positioned and largest of this island chain. The landmass to the east is the Indonesian territory of West Papua on the island of New Guinea. The complex and unusual seabed bathymetry of this region is also visible. The shallow and expansive Sahul shelf that extends off the north coast of Australia is contrasted against the series of deep ocean troughs and submarine depressions which encircle the Lesser Sunda group.*

# 1. THE PETROLEUM POLITICS OF THE TIMOR SEA

## 1.1 Introduction

In this study, I investigate the negotiations between Australia and East Timor over the gas and oil resources of the Timor Sea. The negotiations, which had been initiated in March 2000 by the United Nations Director of Political Affairs in East Timor, Peter Galbraith, arose within the context of Indonesia's de-annexation of East Timor in 1999, and that territory's subsequent moves towards becoming an independent country. The negotiations extended throughout the period of United Nations transitional administration and continued for several years past the date of East Timor's independence, in a process that has been both legally complex and politically contentious. A conclusion was reached with the signing of the Treaty on Certain Maritime Arrangements in the Timor Sea (CMATS) on 12 January 2006. This was the last of three separate, yet interlinked, agreements between Australia and East Timor which collectively provide a legal framework for the development of the largest of the region's gas reserves – totaling about 12 trillion cubic feet of gas.<sup>1</sup> The high level of inter-governmental cooperation that will be required to successfully manage resources under the implementation of these negotiated arrangements means that the potential for disagreement is likely to remain a feature of bilateral relations for some time to come. Yet, in resolving the critical issues concerning revenue allocation and regulatory control, the two sides have managed to overcome one of the most divisive and troubling problems to have emerged within that relationship thus far.

Disputes over maritime boundaries are a widespread source of friction between neighbouring coastal states and, in many ways, the Timor Sea exemplifies the problems of maritime delimitation that arise within the context of geographically enclosed seas, where energy resources are either believed or known to exist.<sup>2</sup> When oil and gas resources are at stake, governments are predisposed to adopting positions that maximize areas of national control and are generally resistant to any forms of compromise. In respect of the dispute

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<sup>1</sup> This figure is based on estimates for the Bayu-Undan and Greater Sunrise accumulations, which contain about three and eight to ten trillion cubic feet (tcf) of gas, respectively.

<sup>2</sup> A review of the regions widely affected around the world is given in Blake, G. H. and Swarbrick, R. E., 1998. 'Hydrocarbons and international boundaries: a global overview', in G. Blake, M. Pratt, C. Schofield and J. Allison Brown (eds), *Boundaries and Energy: problems and prospects*, Kluwer Law International, London.



between Australia and East Timor, the process of negotiation has been more intricate than is generally the case because of the exceptional circumstances surrounding East Timor's political transition and the enormous commercial pressures that have accompanied the negotiations every step of the way. Yet in its barest form, the problem, fundamentally, which the two countries have had to deal with, is one that underlies all negotiations: namely, a conflict of interest between primarily two opposing sides, each of whom want different things but must ultimately settle upon a common position.

Questions of bargaining power are an intrinsic element within negotiation and they figure prominently within the dispute between Australia and East Timor. A constant theme throughout has been the notion of power asymmetry. The material disparity between the two states could hardly be more extreme: Australia – a huge country, wealthy and with vast petroleum reserves; and East Timor – a poor and fragile state, dependent on oil and gas revenues for its very economic survival. East Timor has been portrayed and perceived, in the public eye, as being at a distinct bargaining disadvantage due to “the tremendous economic, political, size and other disparities” in what has been characterized as “an inherently unequal negotiation process”.<sup>3</sup> Yet the terms of the deal that has finally been reached, on the surface at least, seem to paint a very different picture. The extent to which the Australian government has been moved beyond its preferred position is striking. The transition from the pre-1999 legal framework to the present one has resulted in a decline in Australia's share of production revenues that equates to the loss of more than five trillion cubic feet of natural gas and several hundred million barrels of natural gas liquids. Concessions of such a magnitude are difficult to reconcile with the view that negotiations were conducted from a position of greatly unequal bargaining power.

I am not making the claim that East Timor was the outright winner in these negotiations – far from it; compromises have been made on both sides, as would be expected in the resolution of this type of dispute. Nonetheless, it is puzzling how the supposedly weaker party in this case, quite the opposite from being overwhelmed or submissive, has been able to acquire such large concessions – more than perhaps might have been expected prior to negotiations taking place. This raises an interesting question concerning why the Australian government was prepared to yield to the extent that it did and what this, in turn, tells us about each side's capacity to influence behaviour – which is generally how the concept of power in

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<sup>3</sup> ETAN Statement on Timor-Leste/Australian Maritime Arrangement, 15 January 2006, <http://etan.org/news/2006/01timsea.htm> <Accessed 28 January 2006>

negotiation is understood.<sup>4</sup> This question lies at the centre of my examination of the negotiation process and investigation into how outcomes have been determined. Prior to setting out the objectives of this research in more detail and the central argument of the thesis, this chapter proceeds by describing the context for these negotiations, focusing initially upon the events that led to East Timor's emergence in 1999, and the implications this posed for the future of Timor Sea oil and gas development.

## ***1.2 Political and Commercial Context***

### THE EMERGENCE OF EAST TIMOR

East Timor's existence as a sovereign state is a legacy of more than three centuries of Portuguese colonization. The island of Timor is the farthest east of the Sunda island chain that arcs southwards through the Indonesian archipelago. The largest of the Lesser Sunda group and the nearest to Australia, it measures 470 kilometers along a southwest-northeast axis, with a maximum width of 100 kilometers. Portugal discovered Timor in the sixteenth century and commenced a process of settlement, claiming the island as a colony in 1701.<sup>5</sup> During the mid-seventeenth century, Portugal lost control of the western part to the Netherlands. Timor was later divided into two distinct political entities under Portuguese and Dutch authority during the eighteenth century. A colonial boundary treaty delimiting the bulk of the land frontier, down the middle of the island, between East and West Timor, was concluded in 1859.<sup>6</sup> However, diplomatic efforts aimed at establishing a clearer and more exact definition of the boundary in all areas failed, and the dispute that eventuated was finally resolved by a decision of the Permanent Court of Arbitration in 1914.<sup>7</sup>

The 1914 legal determination of the international boundary between the Netherlands and Portugal on the island of Timor became "a critical reference point for the political future of East Timor".<sup>8</sup> In the struggle for Indonesian independence after World War Two, the territorial claims made by the independence movement were based upon the colonial

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<sup>4</sup> Zartman, I. W. and Rubin, J. Z., 2000. *Power and Negotiation*, University of Michigan Press, Ann Arbor, p.7.

<sup>5</sup> Krieger, H. (ed.), 1997. *East Timor and the International Community: basic documents*, Cambridge University Press, Cambridge, p.xix.

<sup>6</sup> *Ibid.*, p.1-17.

<sup>7</sup> *Traité de Lisbonne du 20 Avril 1859; Ibid.*, p.1.

<sup>8</sup> *Chega!*, Final Report of the Commission for Truth, Reception and Reconciliation in East Timor, October 2005, Part 3, p.8

boundaries of the Dutch East Indies. Thus, in 1949, West Timor became part of the Republic of Indonesia, whilst the eastern half of the island remained a Portuguese colony. In 1960, East Timor was listed as a Non-Self Governing Territory with the United Nations decolonization committee, which affirmed its people's right to self-determination.<sup>9</sup> As with its other colonial possessions, Portugal initially tried to deny this right to East Timor, by claiming that the territory was not a colony but constituted an "overseas province" of its metropolitan territory.<sup>10</sup> This argument was rejected by the United Nations in a series of annual General Assembly resolutions from 1960 onwards. Following the military coup in Lisbon in 1974, however, the new government of Portugal moved rapidly to enact constitutional amendments that allowed for the process of decolonization. During 1974 and 1975, Portugal handed power to armed independence movements in each of its African colonies – Guinea, Cape Verde, Guinea-Bissau, Mozambique and Angola.

In late 1974, the Portuguese attempted to establish an advisory government council for the processing of self-determination in Timor, which according to a former Australian Consul in Dili, James Dunn, was to be "worked out step by step in an evolutionary process encompassing a period of several years".<sup>11</sup> However, the council was unable to properly function, as two of the three major indigenous political parties refused to participate.<sup>12</sup> Over the course of 1975, political conditions deteriorated substantially. In August, the Portuguese Foreign Minister informed the UN Secretary General that armed conflicts between rival factions had created a situation of near civil war, which made it impossible to exercise political control.<sup>13</sup> Shortly afterwards, Portuguese authorities withdrew from the mainland territory to a small island just north of Timor. The de-colonization process was unfinished when the forces of the Republic of Indonesia launched a full-scale military invasion of East Timor, in the early hours of 7 December 1975. The action was defended by the Indonesian government as a response to requests from within the territory to restore peace and stability there.<sup>14</sup>

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<sup>9</sup> General Assembly Resolution 1542 (15 December 1960) defined Portuguese colonies, including Timor, as non-self governing territories within the meaning of the UN Charter and recognised that independence "is the rightful aspiration of peoples under colonial subjugation..."

<sup>10</sup> Kreiger, 1997, *op. cit.*, p.18.

<sup>11</sup> Dunn, J. 2003. *East Timor: a rough passage to independence*, 3<sup>rd</sup> Ed., Longueville Books, New South Wales, p.68.

<sup>12</sup> The two groups were: APODETI and FRETILIN. The former refused to participate because it preferred to deal directly with Indonesia. The latter declined to participate on grounds that certain members of the twelve-member council were too closely connected to the former regime. See Krieger, 1997, *op. cit.*, p.18.

<sup>13</sup> *Ibid.*, p.38.

<sup>14</sup> Leifer, M., 1976. 'Indonesia and the incorporation of East Timor', *The World Today*, vol.32(9), p.353.

After the invasion, the UN Security Council adopted resolutions calling upon Indonesia to withdraw its forces.<sup>15</sup> The Indonesian government ignored these resolutions and proceeded to formally annex the territory once military control over a large part of it had been achieved.<sup>16</sup> Yet East Timor continued to remain a ‘question’ on the UN’s annual agenda. In 1982, the General Assembly asked the Secretary General to initiate consultations between Portugal and Indonesia with the aim of resolving the ongoing conflict.<sup>17</sup> The talks continued on a fairly regular basis but made little progress until 1998, when a political and economic crisis in Indonesia brought an end to the thirty-year rule of President Soeharto and forced a review of the government’s Timor policy.<sup>18</sup> From the point of view of Indonesia’s new President, Jusuf Habibie, East Timor had become a costly economic and political burden.<sup>19</sup> The country’s international standing had been seriously damaged by the impact of the invasion and counter-insurgency, which in 1996 the Norwegian Nobel Committee estimated had killed one-third of the population of East Timor “due to starvation, epidemics, war and terror”.<sup>20</sup> In January 1999, Habibie made the surprise decision, in the face of considerable political opposition, that East Timor could become an independent country if that was what its people wanted.<sup>21</sup>

On 5 May 1999, Portugal and Indonesia announced the agreement that would govern the political process by which the long-drawn question concerning decolonization in East Timor was to be finally resolved.<sup>22</sup> The United Nations was entrusted with conducting a referendum in which the people would be given two options: either to accept, or to reject, continued integration with Indonesia under a constitutional framework that allowed for special autonomy. If a majority voted to reject the proposal, the agreement stipulated that the Indonesian government would then take the necessary steps to terminate its links with East

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<sup>15</sup> UN Security Resolution 384, 22 December 1975; and, Resolution 389, 22 April 1976.

<sup>16</sup> Indonesia made constitutional amendments to incorporate East Timor within the Republic on 7 June 1976. See Kreiger, 1997, *op. cit.*, p.44-9.

<sup>17</sup> General Assembly Resolution 37/30, ‘Question of East Timor’, 23 November 1982.

<sup>18</sup> Dunn, 2002, *op. cit.*, p.340.

<sup>19</sup> Budiardjo, C., ‘A Global Failure on Human Rights in East Timor’, paper presented at *East Timor in Transition, Sovereignty, Self-Determination and Human Rights*, Nottingham University, May 1999, [http://tapol.gn.apc.org/news/files/sp\\_etimor9905.htm](http://tapol.gn.apc.org/news/files/sp_etimor9905.htm) <Accessed 20 May 2005>

<sup>20</sup> The Norwegian Nobel Committee, Nobel Peace Prize, 1996, *Press Release*, <http://nobelprize.org/peace/laureates/1996/press.html> <Accessed 16 February 2006>

<sup>21</sup> Habibie first raised the possibility of making political compromises in East Timor within a month of assuming the Presidency, during June 1998. However, his announcement on 27 January 1999 went considerably further, raising for the first time the possibility of full independence from Indonesia. See ‘Habibie speaks on East Timor’, *Financial Times*, 10 June 1998; and, ‘Indonesia might discuss possible independence for East Timor’, *Associated Press Newswires*, 27 January 1999.

<sup>22</sup> A copy of the agreement is included in the Report of the Secretary General, UN doc., A/53/951; S/1999/513, 5 May 1999.

Timor and authority would be transferred to the United Nations, which in turn would initiate a process of transition towards political independence. The results of the ballot were announced in New York, on 3 September 1999. Nearly 80 percent of votes cast rejected special autonomy – thereby triggering East Timor’s transition to full independence.<sup>23</sup> In accordance with the terms of the 5 May Agreement, the United Nations established a transitional administration for East Timor, mandated to administer the territory until it had achieved the capacity for self-government.<sup>24</sup> The duration of the UN transitional administration lasted almost two and a half years – from November 1999 until 20 May 2002 – upon which date East Timor officially joined the ranks of the world’s sovereign states.

#### IMPACT OF EAST TIMOR’S EMERGENCE ON THE OFFSHORE LEGAL FRAMEWORK

The political struggle associated with the process of East Timor’s decolonization is closely intertwined with the question of ocean boundary-making in the Timor Sea. The commercial evolution of the Timor Sea and the conflict in East Timor are, in a sense, two separate story lines, which have intersected at different points in time. The hydrocarbon resources of the Timor Sea have been the focus of exploration activities since the middle of the 1960s. The first discovery of hydrocarbons was made in 1969.<sup>25</sup> The following year, Australia and Indonesia commenced negotiations on a continental shelf boundary to settle questions of seabed jurisdiction. Those negotiations culminated in two delimitation agreements, signed in 1971 and 1972, which created a maritime boundary that extended from the land frontier between Indonesia and Papua New Guinea on the island of New Guinea westwards across the Arafura and Timor Seas, to a point between the Indonesian island of Roti and Australia’s Ashmore reef. However, due to the fact that Portugal had not been a party to those negotiations, the 1972 boundary was drawn in two sections so that a gap was created in the area between East Timor and Australia.

Less than three years after the 1975 invasion, Indonesia and Australia began controversial negotiations on the delimitation of the area off East Timor’s coast. The Australian government had initially hoped that a settlement could be swiftly reached based on the formula that had been used in the 1972 agreement. This proved to be wishful thinking, as

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<sup>23</sup> Press Release, UN doc. SC/6721, 3 September 1999.

<sup>24</sup> UN Security Council Resolution 1272, 25 October 1999.

<sup>25</sup> The first exploration well in the Timor Sea was drilled by the joint venture between the Atlantic Richfield Company and Aquitaine, in 1969, resulting in the Petrel gas discovery.

Indonesia adopted a much firmer stance than it had previously, which caused the negotiations to drag for almost a decade. The agreement that was eventually arrived at in 1989, embodied an elaborate compromise: the two sides set aside the question of permanent boundaries and agreed, instead, to the establishment of a zone of joint jurisdiction. The zone covered nearly 61,000 square kilometres and was subdivided into three discrete jurisdictional areas. The central and largest of these – designated “Area A” – covered 34,970 kilometres and was governed under a comprehensive range of joint arrangements for the exploration and exploitation of petroleum. The government share of any petroleum produced within Area A was to be divided between Australia and Indonesia on a 50/50 basis. This agreement came to be referred to as the “Timor Gap Treaty” because the zone filled the ‘gap’ in the Australian/Indonesian seabed boundary.<sup>26</sup>

Thus, not only was there a complex legal framework covering East Timor’s maritime zones at the time of the 1999 transition but there was also a considerable amount of exploration activity being conducted through the operation of the Timor Gap Treaty. Between 1992 and 1999, company investments in Area A totaled around US\$700 million and had yielded the discovery of a number of oil and gas fields.<sup>27</sup> Investment decisions pending on projects associated with the development of those discoveries amounted to US\$2 billion.<sup>28</sup> The Timor Sea was rapidly emerging as an important new centre of commercial oil and gas production and thus the circumstances surrounding East Timor’s emergence could hardly be more dramatically poised. If the outcome of the referendum had have been in support of the special autonomy proposal, the Timor Gap Treaty would have remained in force and the legal regime would have continued to operate unaffected.<sup>29</sup> Questions concerning the distribution of Indonesia’s royalties or share of petroleum production, which may have arisen as a consequence of the shift to greater autonomy in East Timor, would have been solely an internal matter for Indonesia and would have not have required any amendments being made to the treaty. With the complete transition of power, however, Indonesia lost all authority to

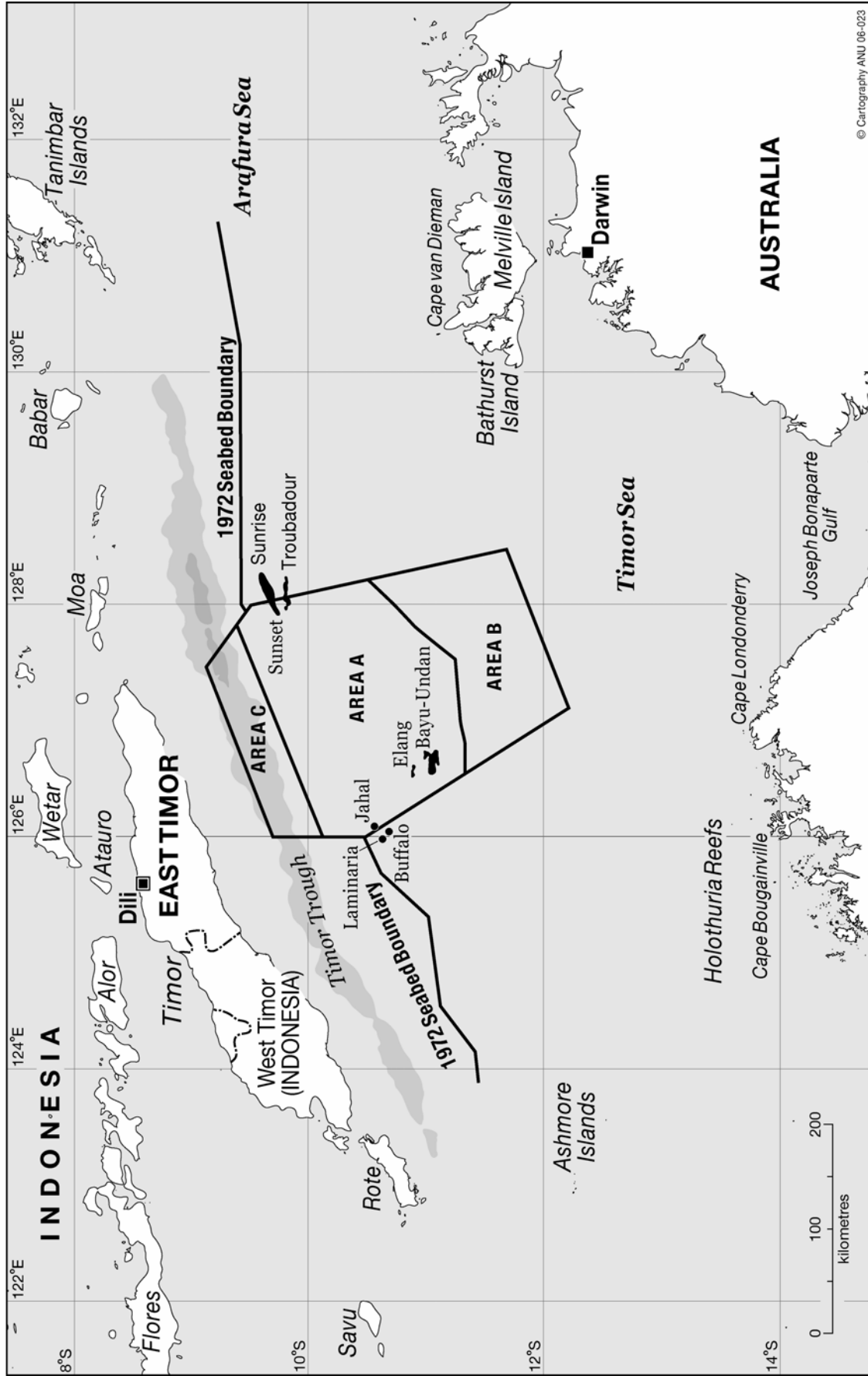
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<sup>26</sup> The official title of the ‘Timor Gap Treaty’ was: *Treaty between Australia and the Republic of Indonesia on the Zone of Cooperation in an Area between the Indonesian Province of East Timor and Northern Australia*, signed over the Timor Sea, 11<sup>th</sup> December 1989; entered into force, 9 February 1991. The Treaty was to remain in force for an initial period of forty years and, thereafter, for successive terms of twenty years, pending an agreement on a permanent shelf delimitation (*Article 33, paragraphs 1 and 2*).

<sup>27</sup> Department of Industry, Science and Resources, Submission #63, Senate Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*, 1999.

<sup>28</sup> UN Aide Memoire, Timor Gap Treaty, 29 November 1999.

<sup>29</sup> Attorney-General’s Department, Submission #62, Parliament of Australia, Senate Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*, 1999.



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MAP 1

The Offshore Legal Framework and Major Oil and Gas Discoveries

exercise jurisdiction off East Timor's coast and, therefore, had no capacity to continue to participate in the treaty.

The future viability of the joint development regime was thus thrown into uncertainty as, indeed, were the contractual arrangements governing resource exploitation – a situation that created enormous risk for those companies that had spent heavily on exploration and development in accordance with the terms of the treaty.<sup>30</sup> The major companies involved were predominantly US and Australian based. They included: Phillips, Woodside and Shell and, to a lesser extent, Santos and the Japanese company, Inpex.<sup>31</sup> The Australian government recognised that an independent East Timor would have the legal authority to seek changes to the Timor Gap Treaty, or even to reject it entirely.<sup>32</sup> However, the government's paramount interest was in maintaining the existing legal framework, by replacing Indonesia with East Timor as the country's treaty partner, thereby maintaining the status quo. Any disruption to commercial development in the area of the so-called Timor Gap caused by the political transition would impact upon Australia in a variety of ways.

Whilst the economic ramifications of a disruption in the current levels of production would be slight, the losses associated with a delay in the major natural gas developments in the region would be much greater. A second Australian liquefied natural gas (LNG) industry proposed for Darwin offered the potential for a substantial increase in gas exports as well as additional economic growth and investment associated with the construction of downstream gas processing facilities on the country's northern shore.<sup>33</sup> For the Northern Territory of Australia – home to less than one percent of the country's population – the impact from losing these investment opportunities would be acute. For several decades, capital investment associated with the mineral and energy resources of the region had been seen as a development catalyst, “the magic key”, to unlocking the door to the Territory's future economic prosperity.<sup>34</sup> The petroleum industry's willingness to invest further in the Timor Sea region, however, and the level of business confidence in Australia, more generally, would

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<sup>30</sup> Ward, C. and Wilder, M., 2000. ‘An independent East Timor: ramifications for the Timor Gap Treaty’, *International Trade and Business Law*, vol.1(1):4-5; Also, ‘Oil companies get jittery about East Timor referendum’, *The Australian*, 9 August 1999.

<sup>31</sup> By 1999, 13 production sharing areas within Area A were being actively explored, involving 37 separate companies established for the sole purpose of participating in a single production sharing contract. Shell owned seven of these companies as did Phillips. Woodside owned four. See Department of Industry, Science and Resources, 1999, *op. cit.*

<sup>32</sup> Attorney-General's Department, 1999, *op. cit.*

<sup>33</sup> Australia's first LNG development was in Western Australia (The Northwest Shelf Project). Completed in 1989 at a cost of AUD\$12 billion, it was the largest private commercial investment in the country's history.

<sup>34</sup> Australian Institute of Political Science, 1954. *Northern Australia: task for a nation*, Angus and Robertson, Sydney, p.233.



be based on the successful political management of the Timor Gap Treaty and the elimination of politically related threats to the companies' security of tenure as well as the terms of their production sharing contracts.<sup>35</sup>

#### EMERGENCE OF A BARGAINING DILEMMA

In the period following the referendum, the Australian government informed the United Nations that the Timor Gap Treaty should continue to operate, thus providing a stable framework for the exploitation of petroleum resources in the area covered by the treaty. The UN considered that an interim arrangement providing for the continuation of the Timor Gap Treaty could be entered into between Australia and the United Nations Transitional Administration in East Timor (UNTAET), under the powers granted to it through Security Council Resolution 1272. Those powers were extremely far-reaching and included the authority to “conclude such international agreements with States and organizations as may be necessary for the carrying out of the functions of UNTAET in East Timor”.<sup>36</sup> However, it was decided by the UN that such action would be taken only if accepted by broadly representative Timorese opinion and on the grounds that it would be completely without prejudice to any action (succession or otherwise) that the East Timorese themselves may wish to take upon independence.<sup>37</sup> Under international law, East Timor was not a successor state to Indonesia and therefore was not bound by any treaty arrangements entered into by Indonesia on East Timor's behalf.<sup>38</sup> However, this did not preclude East Timor from succeeding to the Timor

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<sup>35</sup> The issue of sovereign risk is of overriding importance for extractive industry investors, whether these are petroleum or minerals/mining projects, because of the long time period between initial investment and payback. LNG projects are amongst the most expensive energy projects in the world, costing anywhere from US\$3 to 10 billion. See, Bray, J., 2003. ‘Attracting reputable companies to risky environments: petroleum and mining companies’, in I. Bannon and P. Collier (eds), *Natural Resources and Violent Conflict: options and actions*, The World Bank, Washington, D.C.

<sup>36</sup> UN doc. S/1999/1024, Report of the Secretary-General on the Situation in East Timor (*paragraph 35*), 4 October 1999.

<sup>37</sup> UN Aide Memoire, Timor Gap Treaty, 29 November 1999.

<sup>38</sup> The international law of state succession reinforces the principle that a new State enters the international community with a ‘clean slate’ insofar as it will not be bound by the treaty arrangements of the predecessor state. As noted by Dixon and McCorquodale, however, “this principle has some significant limitations – for example, a boundary treaty must be accepted – which are necessary for international peace and security”. In this context, it is relevant to note that the Timor Gap Treaty was not a boundary treaty but an interim arrangement pending the delimitation of an international boundary. Thus, as far as the continuation of this treaty was concerned, East Timor was starting with a clean slate. See Dixon, M. and McCorquodale, R., 2003. *Cases and Materials on International Law*, 4<sup>th</sup> Ed., Oxford University Press, Oxford, p.73.

Gap Treaty if that was what the future government wanted. The unlawful annexation of East Timor did not necessarily invalidate the Treaty.<sup>39</sup>

The Australian government wanted East Timor to succeed to the Timor Gap Treaty and, initially, there were signs that this objective could be achieved.<sup>40</sup> In a public statement issued on 20 October 1999, leading East Timorese figures indicated their desire for the legal framework to remain in operation by affirming that, “working with the United Nations, Australia and Portugal it is our intent to negotiate appropriate transition arrangements and consequent changes in the current Treaty that maintain its legal authority over petroleum resource development”.<sup>41</sup>

Between October 1999 and January 2000, a series of meetings involving UN and Australian officials as well as East Timorese representatives were held to discuss transitional legal arrangements.<sup>42</sup> These discussions culminated in an agreement signed on 10 February 2000, in the form of an Exchange of Notes between Australia and UNTAET, which constituted the legal basis for the continued implementation of the Timor Gap Treaty. UNTAET’s decision to enter into this agreement was taken solely in the interests of preserving investor confidence in the region and to enable major investment decisions in gas projects to move forward.<sup>43</sup> The agreement expressly stated, however, that only the *terms* of the treaty – the legal regime – had been continued but *not* the treaty itself. From the point of view of both UNTAET officials and East Timorese leaders, the Indonesian occupation of East Timor had been illegal and, therefore, Indonesia was seen as having no legal authority to enter into a treaty affecting East Timor’s resources. Hence, the actual treaty was not continued because UNTAET did not want to “retroactively legitimize” what many in East Timor essentially considered to have been an illegal arrangement between Australia and East Timor’s former occupier.<sup>44</sup>

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<sup>39</sup> In a correspondence between Hans Corell (Under Secretary General for Legal Affairs) and Bernard Miyet (Under Secretary General for Peacekeeping) in November 1999, Corell noted that “the UN secretariat had accepted the Timor Gap Treaty for registration and publication in accordance with Article 102 of the UN Charter (Reg. No. 28462). The UN or any of its organs is not well placed to argue the invalidity of a treaty considered valid at the time of registration”.

<sup>40</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 11 November 1999, p.879-82.

<sup>41</sup> CNRT Press Release, “On the Timor Gap Treaty”, Darwin, 20 October 1999.

<sup>42</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 9 December 1999, p.1009-11.

<sup>43</sup> UNTAET, Daily Briefing, 19 January 2000, <http://www.un.org/peace/etimor/DB/sbr1901.htm> <Accessed 9 October 2004>

<sup>44</sup> *Ibid.*; Mari Alkatiri was quoted as referring to the Timor Gap Treaty as an “illegal treaty”, in late 1999. See ‘Future of Timor Gap Treaty thrown into doubt’, *Australian Associated Press*, 29 November 1999.

The Exchange of Notes was an interim arrangement, which would terminate upon the date of East Timor's independence. It therefore provided no commercial or legal certainty beyond this point but merely served a practical purpose of ensuring a stable legal framework during the transitional phase. An independent East Timor would be starting with a clean slate. As a result, a question automatically arose concerning the legal situation after independence. The Australian position was that the current arrangements could simply be continued under a similar agreement between Australia and East Timor until a more permanent legal framework had been agreed. This is precisely what commercial operators wanted, *viz.* a "binding devolution" of treaty arrangements.<sup>45</sup> However, this position was not supported in East Timor. On 20 March 2000, Australia's Foreign Minister, Alexander Downer, was informed by the UN's Director of Political Affairs in East Timor, Peter Galbraith, that the Timor Gap Treaty was effectively dead and that an independent East Timor would not continue its terms. The Foreign Minister was informed that negotiations must therefore be held so that a new regime could be implemented by the date of independence or there would be no regime at all. This was the crucial decision that precipitated the negotiation process. Downer protested UNTAET's action by lodging a formal complaint with the UN Secretary General.<sup>46</sup> From the standpoint of the Australian government, UNTAET was overstepping its mandate and, in demanding that negotiations be opened, was interfering in a bilateral issue that concerned only Australia and East Timor. Yet, such was the level of concern within Canberra to prevent the Timor Gap Treaty from unraveling that the government reluctantly agreed to negotiate.

#### THE RESOURCES AT STAKE

Between 1993 and 1999, a total of 42 wells had been drilled in Area A and the hydrocarbons which had been discovered in all but six of these wells amounted to more than five trillion cubic feet of gas and about half a billion barrels of oil and natural gas liquids. These resources had been discovered in some medium to small oil fields, including Elang, Kakatua and Jahal, although much of the commercial interest was presently focused on the development of the large gas fields at Bayu-Undan and Sunrise/Troubadour. Bayu-Undan had been discovered in 1995 and was the largest gas discovery to have been made anywhere in the world that year. It was initially expected to produce about 400 million barrels of liquids and

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<sup>45</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 8 September 1999, p.418.

<sup>46</sup> Pers. Comm., Senior UN Official, August 2004.

three trillion cubic feet of gas.<sup>47</sup> Phillips, the operator, planned to develop the resource as two projects. The first, involving production of the liquids component (condensate, butane and propane), entailed a process of gas-recycling, to ‘strip’ off the liquids and then re-inject the ‘dry’ gas into the same reservoir. The liquids would be loaded onto tankers and shipped to world markets. The second project would involve the transport of the dry gas by means of a 500 kilometer sub-sea pipeline to Darwin for domestic use in Australia and/or input into an LNG processing facility for export to foreign markets.<sup>48</sup> In October 1999, Phillips announced that the joint venture partners would be proceeding with a US\$1.4 billion investment in the first stage of the development of the Bayu-Undan field.<sup>49</sup>

A second major gas project was also planned for the Sunrise/Troubadour fields – known collectively as Greater Sunrise. The Greater Sunrise structure has been described as “a complex of large, elongated east-west fault blocks”, which contain the largest accumulation of natural gas in the Timor Sea, estimated to be around nine-and-a-half trillion cubic feet.<sup>50</sup> Though discovered during the mid-1970s, the development of these fields had been hampered by their remoteness from gas markets and by the long-standing controversy surrounding the issue of sovereign jurisdiction in the area of the Timor Sea where they are located. However, in May 1997, a project had been conceived by Woodside and Shell to develop Greater Sunrise as an LNG export and domestic gas supply project at a cost of about AUD\$10 billion.<sup>51</sup> The drilling of the Sunset, Sunset West and Bard wells between 1997 and 1998 confirmed the extension of the Sunrise/Troubadour fields into Area A, across the eastern lateral boundary of the Zone of Cooperation – therefore straddling two different jurisdictions – of which about 10 to 20 percent lay inside the zone.<sup>52</sup> Australia and Indonesia had been engaged in discussions on a suitable framework for the unitisation of straddling resource deposits, but these discussions had not been concluded at the time of the transition.<sup>53</sup> Hence, this was an issue that would have to be resolved in the negotiations between Australia and East Timor.

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<sup>47</sup> Department of Industry, Science and Resources, 1999, *op. cit.*

<sup>48</sup> *Ibid.*

<sup>49</sup> ‘Majority of Co-Venturers Approve Development of Bayu-Undan Liquids Project’, *Business Wire*, 27 October 1999.

<sup>50</sup> Cadman, S.J. and Temple, P.R., 2004. *Bonaparte Basin, NT, WA, AC & JPDA*, Australian Petroleum Accumulations Report 5, 2nd Edition, Geoscience Australia, Canberra, [http://www.ga.gov.au/image\\_cache/GA3861.pdf](http://www.ga.gov.au/image_cache/GA3861.pdf) <Accessed 18 February 2006>

<sup>51</sup> Department of Industry, Science and Resources, 1999, *op. cit.*

<sup>52</sup> *Ibid.*

<sup>53</sup> *Ibid.*

## POSITIONS OF THE PARTIES

Australia's position ahead of the negotiations was well known to all concerned. The government had publicly stated that its approach would be one of trying to "ensure that the Timor Gap Treaty continues".<sup>54</sup> The position of the joint UN and East Timor team was diametrically opposed. During the consultations that had taken place in March, Peter Galbraith and Mari Alkatiri had notified Australia that the new regime must constitute either a mid-point maritime boundary or a major reallocation of revenues in East Timor's favour.<sup>55</sup> UNTAET considered that a fair maritime boundary was the mid-point, or median line, between the Australian coast and the coast of East Timor, as this would divide the intervening space between the two countries equally between them. A boundary drawn according to this line would have the effect of placing the entirety of Area A under the exclusive control of East Timor.

However, during pre-negotiation discussions that took place in Canberra in June 2000, it was agreed that the basis of negotiations would be to devise a new interim regime, pending the determination of a maritime boundary between Australia and East Timor subsequent to East Timor's date of independence. The UNTAET position was to obtain for East Timor the same economic benefits as if it had exclusive sovereign rights north of the median line, albeit within the continued framework of joint development.<sup>56</sup> There were several substantive and interrelated issues that needed to be resolved in negotiating this new regime. These included:

- The revenue split, in terms of the percentage share of government royalties and taxes from petroleum activities allocated to Australia and East Timor;
- The legal framework governing petroleum activities within the zone;
- The fiscal regime to apply to petroleum developments, especially in regard to the exploitation of the region's gas;
- The institutional architecture for the zone, in terms of the political institutions for governing petroleum activities;
- The geographical definition of the area subject to joint development;
- The question of pipeline jurisdiction; and,

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<sup>54</sup> Senate Estimates Committee, Foreign Affairs, Defence and Trade, Committee Hansard, 23 November 2000, p.165-6.

<sup>55</sup> Joint Cabinet Submission, P. Galbraith and M. Alkatiri, 16 September 2000.

<sup>56</sup> *Ibid.*

- The unitisation of hydrocarbons that straddled the boundaries of the zone (in particular the Greater Sunrise fields).

All of these issues clustered around the question of economic and political control and, therefore, they had the characteristics of being highly distributive, or re-distributive, in nature. Gains made by East Timor in any area would automatically register as a loss for Australia. Australia wanted to maintain the “sovereignty neutral” focus of the pre-existing regime, which had been carefully designed in such a way that neither Indonesia nor Australia had greater jurisdiction or control of the joint development zone.<sup>57</sup> In contrast, the UN transitional administration wanted East Timor to have ultimate power over all petroleum activities, including exploration, production, pipeline management, transportation and all related activities, as well as a share of the royalties and taxes commensurate with having – or, as if it had – sovereign rights north of the median line: in other words, close to 100 percent.<sup>58</sup>

The nature of the commercial pressures in the negotiations was similar for both sides. The companies involved, in particular Phillips and Woodside, were concerned solely with protecting their commercial interests in the region: they wanted the petroleum sharing contracts which had been entered into under the Timor Gap Treaty to be ‘grandfathered’ under a new regime between East Timor and Australia; they wanted the fiscal terms to be ‘no more onerous’ than those currently in existence and for the tax terms to be locked-in for the life of the contracts.<sup>59</sup> They wanted a swift resolution of the gas fiscal issues, including an acceptable method for gas valuation; they also wanted a ‘technical’ unitisation of Greater Sunrise based on the fields’ geographic distribution across the eastern boundary of Area A. The companies had no particular interest in how much of the governments’ overall take went to East Timor or to Australia, as long as their own tax burden was no more onerous than if the Timor Gap Treaty had remained in place.<sup>60</sup>

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<sup>57</sup> Burmester, H. 1990. ‘Timor Gap’, *Australian Mining and Petroleum Law Association Yearbook*, p.236.

<sup>58</sup> Cable sent by S. V. de Mello to B. Miyet, ‘Timor Gap – first round of formal negotiations’ (Dili, 9-12 October 2000), 12 October 2000.

<sup>59</sup> The ‘no more onerous’ requirement had been enshrined within the Timor Gap Treaty under *Article 33, paragraph b*, which stipulated that, in the event the treaty ceased to be in force due to the conclusion of an agreement on permanent continental shelf delimitation, both Indonesia and Australia would apply “within its territorial jurisdiction a regime no more onerous than that set out in under this Treaty and the relevant production sharing contract.” East Timor was not legally bound by this provision but, on 20 October 1999, Xanana Gusmao, Mari Alkatiri and Jose Ramos Horta signed a statement assuring contractors that “their legal rights will continue through the full term of those contracts and that the fiscal policies applicable to production sharing and taxation will be no more onerous than current policies as they relate to the contractors share”, see footnote 41.

<sup>60</sup> Godlove, J. ‘Practical implications of East Timor’s transition to the Timor Gap Treaty’, *Australian Mining and Petroleum Law Association Yearbook*, 2000, p.138-50. See, also, testimonies given by representatives of

### ***1.3 Outcomes Reached***

The entire process unfolded during a five year period and over the course of several distinct phases. The negotiations between UNTAET and Australia during 2000 and 2001 – arguably the most crucial phase – culminated in the Timor Sea Arrangement, signed in Dili on 5 July 2001. This provided for a new regime of joint petroleum development, which was then included within a formal bilateral treaty between Australia and East Timor, signed on the date of East Timor’s independence, 20 May 2002. The Timor Sea Treaty, as it was titled, subsequently entered into force on 2 April 2003. Though certain elements of the Australian/Indonesian regime were retained, a number of important changes were made. The most visible of these was the change from a 50-50 split of production to a 90-10 split in favour of East Timor, under the new arrangements for the Joint Petroleum Development Area (JPDA).<sup>61</sup> In addition, a number of quite substantial modifications were made to the institutional and administrative structure, in order to provide East Timor with a greater level of political control. The previous regime had been meticulously designed to ensure that neither state had greater jurisdiction or control. Indeed, whilst the concept of joint development had been continued, the roles of the two states would be dramatically different. Australia’s status in the administration of the JPDA had become vague and nebulous to the point where joint development is, in fact, virtually unilateral. Melbourne University Professor of International Law, Gillian Triggs, has argued that the agreement “sails as close to recognition of East Timor’s sovereignty over the disputed seabed as it is possible to maneuver without conceding the point entirely”.<sup>62</sup>

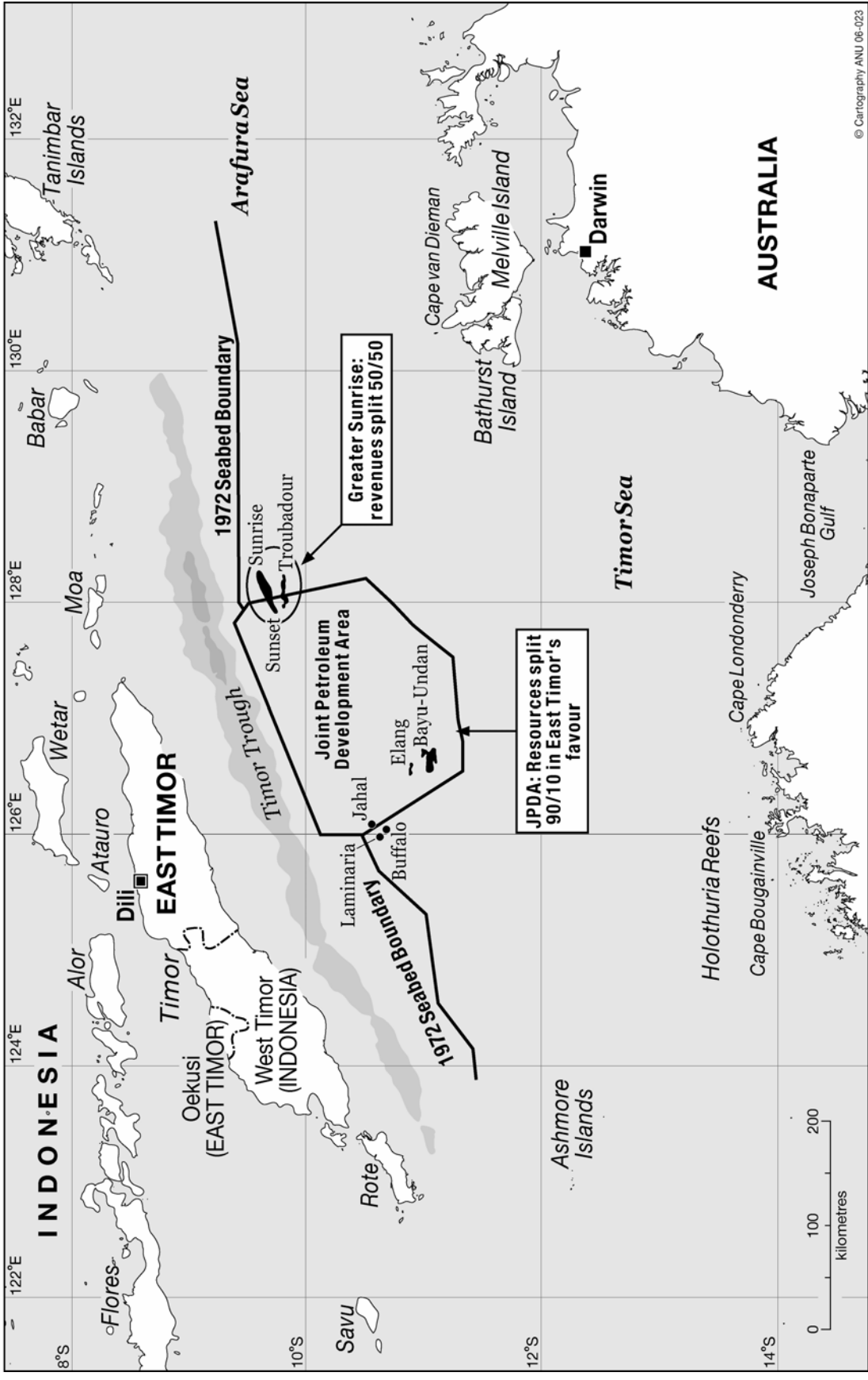
In March 2003, the two sides agreed on a separate international unitisation agreement (IUA) governing production of the Greater Sunrise fields. Yet despite the conclusion and

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Woodside and Phillips to the Senate Committee on Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*, on 20 July 1999 and 8 September 1999, respectively.

<sup>61</sup> Timor Sea Treaty, *Article 4, paragraph a*.

<sup>62</sup> Triggs, G. and Bialek, D., 2002. ‘The New Timor Sea Treaty and Interim Arrangements for the Joint Development of Petroleum Resources of the Timor Gap’, *Melbourne Journal of International Law*, vol.3(2), p.333.



MAP 2



formal signature of the IUA, Greater Sunrise continued to be a source of controversy. East Timor refused to ratify the IUA, claiming that the terms of the agreement were unfair. This led to a further period of negotiation, over the course of 2004 and 2005, to break the impasse. In December 2005, the Australian government announced that agreement had been reached on a resolution of the issues in dispute. The terms of the deal were specified within a separate bilateral treaty, signed by the Foreign Ministers of both countries, in Sydney, on 12 January 2006. The breakthrough was achieved with Australia's decision to accept a complete revision of the actual percentage distribution of Greater Sunrise, so that revenues would be divided on a 50-50 basis. Previously the split had been roughly 80-20 in Australia's favour.

The entry into force of the Timor Sea Treaty had been essential for the commercialisation of Bayu-Undan hydrocarbons. The first stage of the development was brought on stream in February 2004 and production rates of more than 100,000 barrels of condensate and LPG's per day were reached later that year.<sup>68</sup> The second stage construction of the gas pipeline, LNG processing plant and export terminal at Wickham Point, near Darwin, was completed in January 2006. The LNG will be sold under a seventeen-year sales contract to two Japanese utility companies. As Bayu-Undan lies wholly within the JPDA, the governments' share of production is divided 90-10 in favour of East Timor. The Australian government has estimated that, under these revenue sharing arrangements, East Timor will receive US\$15 billion over the field's lifetime at current (2006) oil prices.<sup>69</sup> A project for Greater Sunrise has not yet been finalised.

#### ***1.4 Aims of the Research***

The purpose of this research is to investigate this process of negotiation, with the aim of understanding and explaining how outcomes have been determined. The primary focus is on the particular story of how the Timor Sea negotiations unfolded. These were complicated negotiations that took place within an unusual political context and in which a number of commercial and legal issues were tied up together. The stakes in the negotiations were extraordinarily high. The resources of the Timor Sea are East Timor's greatest natural resource and most important economic asset. As Hill and Saldanha have commented, if

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<sup>68</sup> Santos, Bayu-Undan LNG, <http://www.santos.com/Content.aspx?p=206> < Accessed 25 February 2006 >

<sup>69</sup> Department of Foreign Affairs and Trade, Australia-East Timor Maritime Arrangements, *Fact Sheet*, [http://www.dfat.gov.au/geo/east\\_timor/fs\\_maritime\\_arrangements.html](http://www.dfat.gov.au/geo/east_timor/fs_maritime_arrangements.html) <Accessed 22 February 2006 >

appropriately managed, “[East] Timor could derive undreamed-of wealth from its off-shore reserves of oil and gas”.<sup>70</sup> The issue was of national concern from the Australian perspective, also, and profoundly important to the future economic development of the Northern Territory as well. As a consequence, the division of these resources has been a hotly contested affair and the difficult exchanges between the parties have put a considerable strain on the governments’ bilateral relations.

In conducting this research, I wanted to examine the dynamics of the bargaining process: how the various stakeholders – predominantly, the UN, East Timor, Australia and the major companies involved – responded to the bargaining situation they faced; the strategies they adopted for achieving their goals; and the attempts to reconcile their conflicting interests. However, I am especially interested in investigating what seems to me to be the most remarkable aspect of these negotiations: namely, the question of how a country the size of East Timor could take on its powerful neighbour and emerge with better than expected results. One should be under no illusion as to how far Australia has been moved in these negotiations. Some five to six trillion cubic feet of natural gas that was considered to be federal property, prior to the commencement of negotiations in March 2000, now, in effect, belongs to the Democratic Republic of East Timor.<sup>71</sup>

Future discoveries and production in the Joint Petroleum Development Area could mean that the total amount of resources conceded by Australia, in the transition from the 1989 Timor Gap Treaty to the post-2006 set of arrangements, will be much higher.<sup>72</sup> Some would still argue that Australia has not moved far enough and that the government’s approach throughout has been quite unethical, if not “morally repugnant”.<sup>73</sup> Yet, it is because Australia has tried hard to avoid granting any significant concessions to East Timor in these negotiations that makes the end result that much harder to explain.

A wide convergence of factors means that outcomes are not reducible to a single explanatory variable, however. A variety of elements have simultaneously been at play, both in the negotiations and the context in which that process has been situated. These factors are to be found within the unique history to the dispute; the extraordinary political circumstances

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<sup>70</sup> Hill, H. and Saldanha, J. M., 2001. ‘The key issues’, in H. Hill and J. M. Saldanha (eds) *East Timor: development challenges for the world’s newest nation*, Asia Pacific Press, Australian National University.

<sup>71</sup> It should be noted, however, that the CMATS treaty provides for the sharing of revenues and not resources, although the net effect is no different.

<sup>72</sup> Additional undeveloped discoveries in the JPDA include the Jahal and Kuda Tasi oil fields, with approximately 15-20 million barrels of crude oil, and the Chudditch gas field, estimated to hold 0.7-1 tcf of gas.

<sup>73</sup> Khamsi, K., 2005. ‘A settlement to the Timor Sea dispute’, *Harvard Asia Quarterly*, vol.IX(4), <http://www.asiaquarterly.com> <Accessed 25 February 2006>

surrounding the negotiations; the commercial evolution of the Timor Sea; and the complex range of legal issues the negotiations covered. However, my point of reference in thinking about the issue of causation in this study is the comments made by one of Australia's chief negotiators, Geoff Raby, to the Joint Standing Committee on Treaties, in 2002. Consistent with Australia's treaty ratification processes, the Timor Sea Treaty had been submitted for parliamentary review by the Minister for Foreign Affairs in June that year. One of the issues of interest concerned the distribution of revenues within the joint petroleum development area. The committee was aware that the previous arrangement with Indonesia had been based upon an equal division of resources, and that this had now been changed to a ratio of 90% to 10% in favour of East Timor. The committee wanted to know how the 90-10 was arrived at. Raby explained:

The [original] 50-50 split was, if you like the starting position. From an Australian point of view that seemed a fair and reasonable split, but it was evident within the context of the negotiations that we were unable to maintain the position of a 50-50 split and we had to work to a compromise. We would see 90-10 as quite a substantial concession by Australia, which also underscores the point that the negotiations involved a partner that had influence and weight in the negotiations. So it is a compromise that emerged out of the negotiations...It is one that came out of the negotiations through a period of hard and difficult bargaining, but one that at the end of the day we think we can justify in terms of Australia's national interest...in terms of providing a revenue stream to East Timor which will underpin its viability, and that is very important for Australia's own security.<sup>74</sup>

The government's 'official' position was that for both strategic and altruistic reasons, Australia *intended* East Timor to have a greater share of the revenues.<sup>75</sup> The reality was

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<sup>74</sup> Joint Standing Committee on Treaties, Committee Hansard, *Timor Sea Treaties*, 8 October 2002, p.235. Raby essentially makes two separate points here: firstly that East Timor used its weight and influence in the negotiations to obtain quite significant concessions from Australia; and, secondly, that those outcomes could be adequately justified on the grounds that Australia has a broader strategic interest in the long term economic viability of East Timor. The justification, therefore, is merely a rhetorical one, unconnected to the underlying reasons for political decision-making.

<sup>75</sup> Minister for Foreign Affairs, Minister for Industry, Science and Resources and the Attorney-General, *Joint Media Release*, 'Australia, East Timor and the United Nations agree on a new resource deal for the Timor Sea', 3 July 2001.

distinctly less edifying. Raby disclosed: “At the end of the day, that was the best we could get for ourselves in terms of revenue sharing...But it was not our opening position; it was not our preferred position”.<sup>76</sup> He chose not to elaborate any further on what might have given East Timor “influence and weight” in the negotiations, although an oblique reference was made to the skill of UN negotiators. I would submit that the different bargaining skills and strategies of the key personalities involved have, indeed, played a crucially important role. Yet, to understand more fully the reasons behind the particular distribution of gains reflected within the final terms of the agreement, I would argue that one must take into consideration more than that of skilful diplomacy. I would contend that the key to understanding bargaining outcomes is to be found within the relationship between bargaining strategy and tactics on the one hand, and the legal context within which the dispute is situated on the other. In this thesis, I shall argue that negotiated outcomes are causally related to the interaction between legal norms and bargaining behaviour. I am not making the claim that everything can be reduced to this particular set of dynamics but I am saying that, more than anything else, the relationship between diplomacy and law needs to be properly understood if outcomes are to be adequately explained.

### ***1.5 The Pivotal Role of International Law***

“...the strength of East Timor, being a small country, is international law”.<sup>77</sup>

From a general standpoint, the means by which international law exerts influence in negotiation can be understood from the perspective of both rational choice and sociological theories of decision-making. From the perspective of rational choice, international law affects behaviour through negotiators’ perceptions of the strategic context.<sup>78</sup> If litigation is seen to be a credible alternative to negotiation, behaviour will be shaped decisively by perceptions of what the result would be if the case went to court. Beliefs about how a court might decide the case will feed into negotiators’ evaluations of alternatives and, thus, their decision-making.

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<sup>76</sup> Joint Standing Committee on Treaties, Committee Hansard, *Timor Sea Treaties*, 8 October 2002, p.236.

<sup>77</sup> Mari Alkatiri, 12 April 2001 (UNTAET Daily Press Briefing)

<sup>78</sup> Mnookin, R. H. and Kornhauser, L., 1979. ‘Bargaining in the shadow of the law: the case of divorce’, *Yale Law Journal*, vol.88, p.950-996; Stone Sweet, A., 2000. *Governing with Judges: constitutional politics in Europe*, Oxford University Press, Oxford; Sandholtz, W. and Stone Sweet, A., 2004. ‘Law, politics and international governance’, in C. Reus-Smit (ed.), *The Politics of International Law*, Cambridge University Press, Cambridge.

The more convinced a party is of the strengths of its case, the greater will be the incentive to stand its ground. Conversely, the side that is less confident of its case will see the risks of arbitration, or adjudication, as being higher and, therefore, is likely to be more flexible in negotiations. Disputes over maritime jurisdiction and boundaries are rarely clear cut; yet, experienced diplomats have an intuitive grasp of the legal pressures involved. David Anderson has remarked that negotiators will “form a view on the true ‘worth’ of the claim, rather in the way that financial claims are negotiated and compromised...The question to ask is: what line would an international tribunal award were the issue to come before it for decision?”<sup>79</sup> Governments will rely primarily on the precedents which have been established by the International Court of Justice (ICJ) and other *ad hoc* courts of arbitration in previous maritime boundary cases to develop and argue their position.

An understanding of the way argumentation is used and exerts influence in negotiation constitutes an important theoretical axis that divides rational choice theory from social constructivism. From the standpoint of rational choice, the power of normative argumentation, whereby each side argues the merits of its case, operates according to a strategic rationality. Negotiators argue with the aim of influencing the opponent’s perceptions of the options they face, not necessarily his or her views. It affects choices by influencing expectations of reciprocal behaviour, by feeding into the perceptions that each side has of the other’s willingness to concede, in the sense that, ‘we are convinced of our position and will not back down, so you must.’ Arguing is intended to put pressure on an opponent in negotiations by demonstrating resolve and commitment.

Yet arguing can be understood differently and, indeed, may function differently under certain circumstances. For there is a normative component in the legal arguments negotiators use to justify, explain, rationalize or legitimize their positions.<sup>80</sup> Albin has observed that diplomats sometimes draw on normative ideas and concepts to “overcome conflicting interests and claims, and to build consensus on the nature of an acceptable outcome”.<sup>81</sup> From the perspective of social constructivism, it is assumed that the use and effect of normative argumentation operates according to a distinctively different type of logic than that which underpins the use of other influence techniques, such as those intended to modify the

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<sup>79</sup> Anderson, D. H., 2002. ‘The Negotiation of maritime boundaries’, in C. Schofield, D. Newman, A. Drysdale and J. A. Brown (eds), *The Razors Edge: international boundaries and political geography*, Kluwer Press, London.

<sup>80</sup> Bacharach, S. B. and Lawler, E. J., 1981. *Bargaining: power, tactics, and outcomes*, Jossey-Bass Publishers, San Francisco.

<sup>81</sup> Albin, C., 2001. *Justice and Fairness in International Negotiation*, Cambridge University Press, Cambridge, p.15.

opponent's cost/benefit calculations. According to Thomas Risse, when negotiators use norm-based arguments to support their claims, it implies that they are "open to being persuaded by the better argument".<sup>82</sup> From this standpoint, behaviour is partly governed by the "logic of reason"; or, by what Risse refers to as, an "argumentative rationality", on which basis "actors do not seek to maximize or to satisfy their given interests and preferences, but to challenge and to justify the validity claims inherent in them – and they are prepared to change their views of the world or even their interests in light of the better argument".<sup>83</sup> Here, diplomatic negotiation is portrayed almost in terms of a positional debate, oriented towards the attainment of a mutual understanding of the problem and its appropriate solution. Each side attempts to convert the other to accepting the legitimacy, or validity, of their own particular position.

From this standpoint, acts of choice are deeply informed by concepts of legitimacy and are not determined purely by the instrumental calculation of expected utility. In a Habermasian sense, the law exerts influence because it enables parties to assert the validity of their claims.<sup>84</sup> This view differs in subtle but distinct ways from that of Thomas Franck, who emphasises the law's psychological pull on behaviour, in the sense that, 'this is the rule, it must be followed.' Interestingly, Franck has noted that the rules on continental shelf delimitation that are laid down within the 1982 UN Convention on the Law of the Sea invites disputes due to their lack of determinacy and "textual elasticity".<sup>85</sup> Yet, he asserts that "this has been redressed effectively in a series of interpretations by the International Court of Justice".<sup>86</sup> The implication is that governments' claims will be pulled into line with court decisions because of the authoritativeness of those decisions and the influence this exerts upon conceptions of an "equitable solution".<sup>87</sup> Communication in negotiation becomes the medium through which that process occurs.

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<sup>82</sup> Risse, T., 2000. "Let's Argue!": communicative action in world politics', *International Organization*, vol.54(1), p.7.

<sup>83</sup> *Ibid.*

<sup>84</sup> Outhwaite, W. (ed.), 1996. *The Habermas Reader*, Polity Press, Cambridge, 160-9.

<sup>85</sup> Franck, T. M., 1988. 'Legitimacy in the international system', *American Journal of International Law*, vol.82(4), p.724.

<sup>86</sup> *Ibid.*

<sup>87</sup> The 1982 UN Convention on the Law of the Sea, *Article 83, paragraph 1* stipulates that continental shelf delimitation "shall be effected by agreement...in order to achieve an equitable solution".

### *1.6 The Central Argument of this Thesis*

Because these different influence mechanisms are internal to the decision-maker, explanations cannot be automatically inferred from observed behaviour. For example, whilst it may be possible for one party to convince the other of the merits of his or her government's position so that the other concedes, it would be erroneous for the outside observer to infer that this had happened as a result of a shift in either side's position. When negotiators are deadlocked in an argument, it might still be in the economic or political interests of one side to eventually concede to enable the dispute to be brought to an end. Powerfully articulated arguments grounded in international law may appear to an opponent as a difficult obstacle to be overcome. What this means is that it may not always be necessary for an opponent to be convinced by, or believe in, the validity of these legal claims; only to believe that the first party attaches legitimacy to such claims and, for this reason, is unlikely to back down. The legitimacy of international law not only makes offers more acceptable, it also makes threats more credible.<sup>88</sup> Thus, for the outside observer that wishes to understand the reasons for the particular choices and actions of negotiators, it may not be possible to discern whether their viewpoints and beliefs have been altered solely on the basis of the decisions they make and the outcomes that are reached. Changes that occur on the surface may reflect a deeper shift in attitude that has come about through persuasion and an openness to reason; but such changes could equally be the result of a utility maximizing choice based upon the consideration of the courses of action that are available and, in particular, expectations, of the other party's motivations and intentions.

Empirical accounts of maritime boundary negotiations tend to support the rationalist perspective. Alex Oude Elferink has noted that, "in the negotiating process the law seems to have a static character. States in general do not adjust their legal positions in the course of negotiations and do not aim to come to a common interpretation of the law of maritime delimitation".<sup>89</sup> The prevailing view, it would seem, is that the legal rules governing maritime delimitation exert influence primarily by shaping perceptions of the strategic context; that is, by giving to each state certain claims based on what they would get if the dispute went to third party dispute settlement and the threat of litigation that automatically goes with it. In this

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<sup>88</sup> Fisher, R., Schneider, A. K., Borgwardt, E. and B. Ganson, 1997. *Coping with Conflict: a systematic approach to influence in international negotiation*, Prentice-Hall Inc., New Jersey, p.247.

<sup>89</sup> Oude Elferink, A., 1994. *The Law of Maritime Boundary Delimitation: a case study of the Russian Federation*, Martinus Nijhoff Publishers, Dordrecht, the Netherlands, p.371.

thesis, I shall argue that the negotiations between Australia and East Timor provide further evidence of these forces at work. For East Timor, conceptions of legal entitlement have been an extremely powerful motivating force, which has exerted influence *through* the dynamics of the parties' interaction. The decisions of international courts have substantially undermined the legal strength of Australia's long-held claims in the Timor Sea whilst bolstering those of East Timor at the same time. These decisions have granted East Timor's negotiating position a special prominence over Australia's and this gave the threats of ICJ litigation made by UNTAET's negotiators a high level of credibility.

The main difficulty that Australia has encountered in these negotiations stems from the fact that the government has been confronted by an opponent that was deeply convinced of the legitimacy of its position and which was prepared to have the dispute settled by a higher, legal authority if negotiations failed. The choice that Australia ultimately faced – and one that was brilliantly engineered, it must be said, by the UN's Director of Political Affairs in East Timor, Peter Galbraith – was either to accept a diminished share of Timor Sea resources, or risk not having an agreement at all. The government did not necessarily need to be convinced of East Timor's claims and was even prepared to take fairly extreme measures to prevent the case from going to court. Yet, because of its paramount interest in maintaining a functioning legal framework for the Timor Sea, coupled with a fear of what the outcome might be from a third-party settlement procedure, the government has been compelled to negotiate a resolution that accommodates, to a significant extent, East Timor's maritime claims.

### ***1.7 Overview of the Thesis***

This thesis is organized as follows: in Chapter Two, I examine how the regime of the continental shelf has evolved, focusing particularly on the rules governing continental shelf delimitation. The purpose of this chapter is to provide an understanding of the legal context of the negotiations between Australia and East Timor and to show why the Australian government was so averse to the idea of third-party settlement of the dispute. In the third chapter, I provide a concise history of ocean boundary-making in the Timor Sea. The analysis focuses on the negotiations between Australia and Indonesia that took place over a twenty-odd year period and which led to the conclusion of the two seabed agreements, in 1971 and



1972, as well as the Timor Gap Treaty, in 1989. The purpose of this chapter is to provide a more comprehensive understanding of that history and an explanation, also, of why negotiations evolved in the manner that they did as well as certain salient aspects of the outcomes reached.

This provides the crucial backdrop to the main focus of the research concerning the Australia/East Timor negotiations, in the period 1999 to 2005. The analysis of this process is undertaken over three successive chapters. Chapter Four concentrates on the period after the referendum in East Timor, in late 1999, until the formal commencement of treaty negotiations between Australia and the UN transitional administration, in October 2000. I examine how the principal actors with a stake in the Timor Sea's oil and gas resources responded to the political changes in East Timor and, in particular, the strategic reasoning behind UNTAET's decision to initiate the negotiations on a new petroleum regime prior to East Timor's independence. In Chapter Five, I investigate the process that led to the signing of the Timor Sea Arrangement, on 5 July 2001. This is, in many ways, the centerpiece of the research. I carry out a detailed analysis of the negotiation interaction: the parties' starting positions; the pattern of concessions, modification and change that led to agreement; and, the key events and turning points during that process. In Chapter Six, I study the process of stakeholder interactions and negotiations in the period after the signing of the 5 July Arrangement and the various factors that led to a final settlement being reached, in 2005. I analyse the problems that were encountered during this period and their resolution. In the conclusion, I return to the central argument of this thesis and discuss, within that context, the relevance of this research for the study of international negotiation, dispute resolution and the politics of ocean governance, more broadly.

#### A NOTE ON METHODOLOGY

On a methodological level, it is relevant to note from the outset that in analysing these negotiations, two important challenges have emerged that are common to the study of international negotiation.<sup>90</sup> The first is descriptive and essentially involves finding out what happened. This is obviously fundamental to the analysis, yet quite problematic given that the negotiations, at all times, were highly confidential. The second challenge is explanatory and

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<sup>90</sup> Cottam, R., 1986. 'Understanding negotiation: the academic contribution', Institute for the Study of Diplomacy, School of Foreign Service, Georgetown University, Washington, D.C.

relates to the basic analytical problem of understanding the causal forces behind the dynamics observed: that is, the specific reasons behind the parties' moves and concessions that ultimately led to agreement. The epistemological problems concerning the latter are profound. Information *about* the negotiations cannot, of itself, *tell* the analyst why the parties acted in the way that they did. Therefore, conclusions must be reasoned in light of the available evidence. As Druckman has pointed out, negotiation analysis involves "weaving together diverse data sources into a mosaic of influences that contribute to an understanding of the phenomenon".<sup>91</sup> Since the events under investigation are unique historical occurrences, they cannot be subjected to the kind of experimental or survey techniques that are widely used in the social sciences.<sup>92</sup> Whilst the comparative analysis of multiple cases of international negotiation may provide, at best, a *post-hoc* means of testing the salience of particular variables, Raymond Cohen has argued that:

In the final analysis...there can be no substitute for the skill and discrimination of the researcher. He or she must piece together a conventional narrative of what actually occurred and also attempt to provide a psychological reconstruction of what lay behind the outward train of events. In other words, he or she must open up the black box and peer into the inner world of the negotiators' perceptions, assessments, and anticipations. To do this, one can rely on the personal testimony of participants, whether in the form of contemporary records (memoranda or protocols of the negotiation), written autobiographical accounts, or solicited interview material. On occasion, existing secondary sources can supplement the picture.<sup>93</sup>

In writing this thesis, I have drawn extensively on primary source material, including official UN correspondences, records of high-level meetings and detailed transcripts of the crucial period of negotiations between the UN and Australia, between October 2000 and June 2001. Interviews were conducted with many of the people who played a direct role in the negotiations, as well as other key stakeholders. A list containing the names of these

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<sup>91</sup> Druckman, D., 1977. 'Introduction and overview', in D. Druckman (ed.), *Negotiations: social-psychological perspectives*, Sage Publications, California, p.42.

<sup>92</sup> Blaxter, L., Hughes, C. and M. Tight, 1996. *How to Research*, Open University Press, Buckingham, UK, p.63-80.

<sup>93</sup> Cohen, R., 1990. 'Deadlock: Israel and Egypt negotiate', in F. Korzeny and S. Ting-Toomey (eds), *Communicating for Peace: diplomacy and negotiation*, Sage Publications, California, p.138.

individuals has been included at the end of the thesis. Most of the fieldwork for this research was undertaken between June and August 2004 and during July 2005. Two trips were made to Darwin, Washington, D.C. and New York and one trip was made to Dili, the capital of East Timor.

## 2. THE INTERNATIONAL LEGAL CONTEXT OF THE DISPUTE

The international politics of maritime governance rests on foundations that are legal in nature. International law is constitutive of the sovereign rights which generate competing national claims and, hence, bring coastal states into conflict with one another. Although the negotiations between Australia and East Timor dealt mainly with the issues of petroleum distribution and governance, the underlying reason for the dispute is, essentially, one of divergent, or overlapping, claims to jurisdiction north of the putative median line between Timor and Australia. All of the resources that were in contention lie to the north of this point, on the Indonesia/East Timor side, including the entirety of Area A of the Zone of Cooperation, as designated within the 1989 Timor Gap Treaty. Senior members of the UN transitional administration in East Timor, including the Transitional Administrator, Sergio Vieira de Mello and the Director of Political Affairs, Peter Galbraith, as well as prominent East Timorese political leaders, such as Mari Alkatiri, Xanana Gusmão and José Ramos Horta, considered that international law supported the use of a median line, at least in terms of setting the frontal boundary dividing the Timor Sea into northern and southern parts.<sup>1</sup> It was their view therefore, that under a new interim petroleum regime, an independent East Timor should be entitled to 100 percent, or close to that amount, of the revenues from Area A, as opposed to the 50-50 revenue sharing arrangements that had existed between Indonesia and Australia.

In this chapter, I examine the historical and legal basis of the Australian claim to jurisdiction in the Timor Sea – a claim that extends well north of the median line to within a relatively short distance from the shores of Timor. This is crucial to understanding important aspects of the legal context for the negotiations. Australia's claims to jurisdiction in the Timor Sea are well established, having first taken shape during the early 1960s. They are based upon concepts of seabed geomorphology. In reviewing the international jurisprudence in respect of continental shelf delimitation, it will be shown that seabed geomorphology was at one stage considered by the International Court of Justice to be a fairly intrinsic aspect of the regime of continental shelf delimitation. Yet, over time, the law has evolved and such concepts have, for a number of years now, been treated as a completely irrelevant factor to delimitations where the distance between the coasts of opposite states is less than 400 nautical miles. This occurs

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<sup>1</sup> A different view was taken with regard to the lateral lines dividing the eastern and western parts of the Timor Sea, as opposed to the north/south boundary, which will be examined in more detail in Chapter Five.

in the Timor Sea where the distance between Australia and East Timor is around 250 nautical miles. After reviewing the legal basis of Australia's claims, as well as the current status of international law, I return, in the last part of this chapter, to the central theme concerning the relationship between international law and the diplomacy of maritime delimitation.

### ***2.1 Australia's Claims in the Timor Sea.***

Australia's approach towards the issue of seabed boundary delimitation in the Timor Sea crystallized in the mid-1960s against the background of increasing commercial interest in the region's petroleum potential.<sup>2</sup> Although the federal government had proclaimed jurisdiction over the continental shelf in 1953, no legislation was subsequently passed to give it authority over the allocation of the earliest permits for the exploration of petroleum.<sup>3</sup> These had initially been issued at the sub-national level, under the pre-existing legislation of the adjacent states.<sup>4</sup> Exploration permits which had been granted to two major investment consortia, between 1963 and 1965, indicate the extent of the area that was claimed to be within Australia's offshore jurisdiction.<sup>5</sup> Off the country's remote north coast, these permits covered almost all of the offshore Bonaparte and Browse basins, including the Timor Sea area, and extended to the slope of a deep, underwater, topographical feature, known as the Timor trough.

The morphological structure of the area, including the Timor trough and the surrounding seabed, is thus the critical element to Australia's long-standing jurisdictional claims in this region. The Timor trough has been described as "an elongated basin oriented along a northwest-southwest axis", roughly parallel to the island of Timor and which lies at depths of between 1,500 and 3,200 meters.<sup>6</sup> It is one of a chain of submarine depressions forming a giant horseshoe which underlie the Arafura and Seram seas to the east, and

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<sup>2</sup> Haward, M., 1989. 'The Australian offshore constitutional settlement', *Marine Policy*, vol.13(4):334-48; Crommelin, M., 1988, 'The Legal Regime Applicable to Petroleum', *Petroleum in Australia – the First Century*, Australian Petroleum Association Exploration Limited, Canberra.

<sup>3</sup> "Continental Shelf: Proclamation", *Commonwealth of Australia Gazette*, 11 September 1953, No.56.

<sup>4</sup> The 1901 Australian Constitution established the Commonwealth of Australia, comprised of six States – New South Wales, Queensland, South Australia, Tasmania, Victoria and Western Australia. The Northern Territory was originally governed by South Australia at the time of federation.

<sup>5</sup> One of these consortia comprised, Burmah Oil Company Australia Limited, Woodside (Lakes Entrance) Oil Company, Mid-Eastern Oil Company and Shell Development Australia. The second involved Arco Limited and Australian Aquitaine Petroleum Proprietary Limited.

<sup>6</sup> US Department of State, Bureau of Intelligence and Research, *Limits in the Seas*, No.87, Territorial and Continental Shelf Boundaries, Australia and Papua New Guinea – Indonesia, August 20 1979.

westwards to the Java Trench in the Indian Ocean. Unlike the much deeper Java Trench, which forms a subduction zone between two tectonic plates, the Timor trough is now widely understood to have formed as a result of “downwarping” caused by tectonic forces and plate movement further to the north of the island.<sup>7</sup> Timor itself is a product of the tectonic evolution of the region. The island is a “ridge” of oceanic and continental crust caused by the collision of Australian continental material with the oceanic plate of the Banda Sea in eastern Indonesia.<sup>8</sup> To the south and east of the trough, the Timor Sea is underlain by a shallow platform of the ocean floor, known as the Sahul Shelf, which extends from the north coast of Australia to the island of New Guinea. Hence, a bathymetric cross-section from Darwin to Timor establishes a wide and shallow shelf extending from Australia, a southern slope into the trough, an undulating trough floor and a comparatively steep slope rising northwards to the coast of Timor.

Australia’s claims to jurisdiction in the Timor Sea were based on the contention that the trough marked the physical edge of the Australian continental shelf.<sup>9</sup> From this standpoint, a maritime boundary could already be said to exist between Australia and the island of Timor, *viz.*, one that was created by nature. As the trough lies at a distance of between 25 and 50 nautical miles south of Timor but more than 200 nautical miles north of the Australian mainland, a line drawn along its axis would divide the Timor Sea into two areas of jurisdictional control enormously disproportionate in size: a narrow Timor shelf north of the trough and a massive Australian shelf to its south.<sup>10</sup> Between 1963 and 1965, Australia’s assertion of authority north of the median line did not receive any challenge from either the Indonesian or Portuguese governments; and, despite the concerns of some ministers over the possibility of future ‘confrontation’ with Indonesia, the government decided that its approach should be to confirm jurisdiction over all areas covered by exploration permits, which had been previously been granted, in national legislation.<sup>11</sup>

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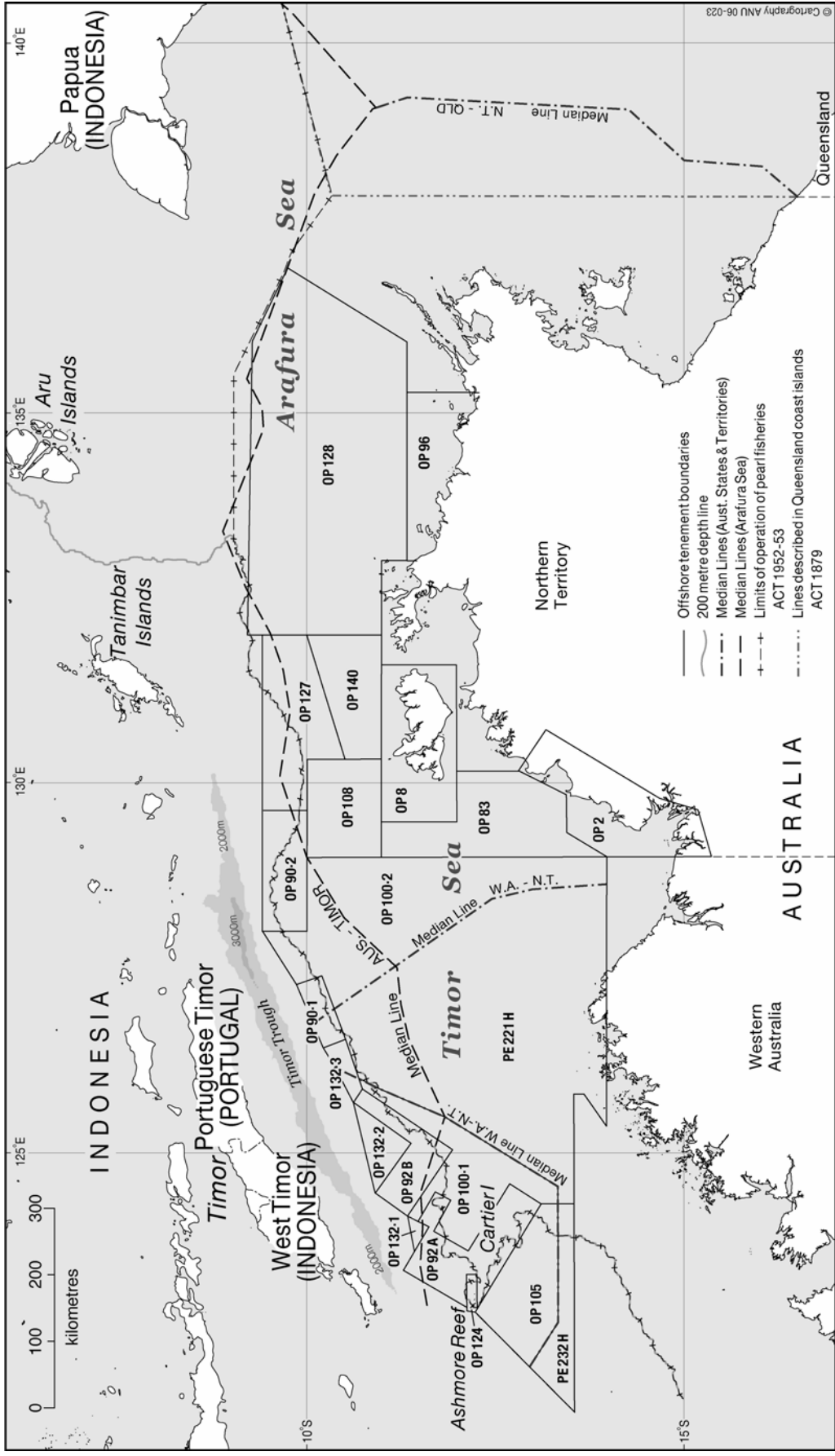
<sup>7</sup> Baillie, P., Fraser, T, Hall, R. and K. Myers, 2003. ‘Geological development of eastern Indonesia and the northern Australia collision zone: a review’, Timor Sea Petroleum Geoscience, Proceedings of the Timor Sea Symposium Darwin, Northern Territory, 19-20 June 2003.

<sup>8</sup> Richardson, A. N. and Blundell, D. J., 1996. ‘Continental collision in the Banda Arc’, in R. Hall and D. J. Blundell (eds), *Tectonic Evolution of Southeast Asia*, Geological Society Special Publication, No.106, The Geological Society, London, p.47.

<sup>9</sup> Statement in the House of Rep. by the Minister for External Affairs, William McMahon, 30 October 1970.

<sup>10</sup> Prescott, J. R. V., 1972. ‘The Australian-Indonesian Continental Shelf Agreements’, *Australia’s Neighbours*, No.82:1-2.

<sup>11</sup> In a Cabinet submission made in late 1965, Minister for National Development, David Fairbairn, advised “falling back” to the safety of the median line until international boundaries had been agreed to in the Timor Sea. This, he recommended, to avoid provoking a sharp reaction in Indonesia, whose foreign policy at this time was perceived within Australia to be volatile and unpredictable. After lengthy Cabinet debate, Fairbairn’s advice was



MAP 3

**Adjacent Area Boundary of the Petroleum (Submerged Lands) Act, 1967 and Offshore Petroleum Exploration Permits, c.1965\***

\*The Adjacent Area Boundary coincided with the outer edges of the petroleum permits. The map provides a vivid illustration of how extensive Australia's claims in the Timor Sea were. They extended well beyond both the notional median line and the 200 metres depth-line to within a short distance of Indonesian and Portuguese territory.

On 20 December 1965, *The Australian* newspaper reported that Australia could be inviting a territorial challenge from Indonesia if the cabinet's decision was put into effect.<sup>12</sup> The government reacted with a strong affirmation that the position which had been adopted was fully consistent with international law (explored below). Legislation giving effect to the decision was subsequently passed in October 1967, under the Petroleum (Submerged Lands) Act. The legislation was to apply over offshore areas within 'adjacent area boundary lines'. In the area of the Timor Sea, this line was drawn so as to validate the existing petroleum titles given by the Northern Territory and Western Australia governments prior to federal legislation being implemented, as indicated on the map, on the preceding page. The government estimated that in the period between 1962 and 1965, companies holding permits in the Timor Sea had spent £750,000 on exploration. Of this amount, approximately £150,000 related to areas beyond the median line.<sup>13</sup> Whilst recognising the risk that Indonesia and Portugal could assert conflicting claims in this region, the Attorney-General's Department advised that there was "no reason to be bashful...maps have been circulating for some time and we must not keep this problem in the cupboard".<sup>14</sup>

## ***2.2 Legal Analysis of Australia's Claims***

A close relationship between the morphological character of the continental shelf and notions of sovereign entitlement is, indeed, a deeply rooted part of legal doctrine. It can be traced to customary principles first to have been expressed within the proclamation issued by the government of the United States on 28 September 1945 ("Truman Proclamation"). According to the International Court of Justice (ICJ), the Truman Proclamation is to be regarded as the starting point of the positive law concerning the continental shelf – "and the chief doctrine it enunciated, namely that of the coastal state as having an original, natural and exclusive (in short a vested) right to the continental shelf off its shores".<sup>15</sup> In this instrument, the US declared that it regarded "the natural resources of the sub-soil and sea-bed of the

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rejected. See NAA: A5827, vol.37/Agendum 1165.

<sup>12</sup> 'Australia risks oil challenge by Indonesia', *The Australian*, 20 December 1965.

<sup>13</sup> NAA: A5827, vol.37/Agendum 1165.

<sup>14</sup> NAA: A1838, 1733/5 Part 1 - Law of the sea - Oil mining on the Australian continental shelf.

<sup>15</sup> *North Sea cases*, 1969, p.32-3, para.47.



continental shelf beneath the high seas but contiguous to the coasts of the United States as appertaining to the United States, subject to its jurisdiction and control”.<sup>16</sup>

The Truman Proclamation did not specify how the outer limits to US jurisdiction were to be measured but, in an accompanying press release, the government defined the continental shelf as “that area adjacent to the continent covered by no more than 100 fathoms [184.6 metres] of water”.<sup>17</sup> The 100 fathom line was not a totally arbitrary bathymetric point, as typically the shelf extends outward and slopes gently downward from the coast to depths of between 100 and 200 metres before ending, in most instances, at a more abrupt drop along the seaward edge, called the shelf break. Below this lies the continental slope – a much steeper zone that merges with a section of the ocean floor, known as the continental rise.<sup>18</sup> A similar definition was subsequently incorporated within the Convention on the Continental Shelf, which was adopted at the First UN Conference on the Law of the Sea in 1958. The Convention provided that the rights of the coastal state extended “to a depth of 200 metres or, beyond that limit, to where the depth of the superjacent waters admits of the exploitation of the natural resources of the said areas”.<sup>19</sup>

Since its inception, therefore, the geophysical framework for the application of the regime was that the continental shelf was a physical extension of the land-mass of the coastal state.<sup>20</sup> This was subsequently reinforced by the ICJ in its judgment in the *North Sea* cases, in 1969, through the principle of “natural prolongation”. Namely, the idea that “what confers the *ipso jure* title which international law attributes to the coastal State in respect of its continental shelf is the fact that the sub-marine areas concerned may be deemed to be actually part of the territory over which the coastal State already has dominion, – in the sense that, although covered with water, they are a prolongation or continuation of that territory, an extension of it under the sea”.<sup>21</sup> The ICJ stated that the principle of natural prolongation was not only fundamental to determining validity of title but was also an intrinsic part of the rules binding upon states in the matter of delimitation.<sup>22</sup>

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<sup>16</sup> White House Press Release, 28 September 1945. Also published in *The American Journal of International Law*, vol.40(1):45- 48.

<sup>17</sup> Young, R., 1948. ‘Recent developments with respect to the continental shelf’, *American Journal of International Law*, vol.42(4):849-57.

<sup>18</sup> “Continental Shelf”, *Encyclopædia Britannica*, <http://www.britannica.com> <Accessed 27 April 2005>

<sup>19</sup> 1958 Convention on the Continental Shelf, *Article 1*.

<sup>20</sup> Dundas, C. W. n.d. *Practical Steps in Negotiating Maritime Boundary Agreements: a guide for small states*, Technical Assistance Group, Commonwealth Fund for Technical Cooperation, London, p.35.

<sup>21</sup> *North Sea* cases, 1969, p.31, para.43.

<sup>22</sup> *Ibid.*, p.47, para.85.

At the First UN Conference on the Law of the Sea, delegates had considered a number of possible methods of delimitation. The International Law Commission of the United Nations (ILC) had adopted, as a general rule, the system of the median line, in the draft articles that were prepared for the Conference.<sup>23</sup> A median line boundary, by definition, is a line every point of which is equidistant from the nearest points on the baselines of the states in question. It has an objective geometric precision and an inherent, or *prima facie*, degree of fairness that derives from the fact that it results in an equal division of any areas of overlap. The ILC felt that the rule should be “fairly elastic”, however, as it was recognized that certain geographical configurations of the coast would render a line drawn strictly on this basis inequitable.<sup>24</sup> Thus, the Commission recommended that provision must be made for the median line to be modified, or an alternative method used, in cases where this was justified “by any exceptional configurations of the coast, as well as the presence of islands or of navigable channels”.<sup>25</sup> Under this formula, therefore, the median line, whilst considered paramount, could be overridden when its rigid application resulted in an outcome that was felt to be unfair or disproportionate.

The treaty articles on delimitation drafted by the ILC were adopted within the 1958 Convention, under Article 6. The regime consisted of two components, or procedural steps. In the first instance, Article 6 specified that delimitation was to be effected through mutual agreement, thereby prohibiting one country from unilaterally determining boundaries shared with another country. Unilateral delimitations would have no validity under international law. In the event that states were unable to reach an agreement, however, the Convention stipulated that the line was to be based upon the principle of equidistance, unless special circumstances justified otherwise. The special circumstances provision provided a means of striking a balance between predictability and objectivity, on the one hand and flexibility and discretion, on the other. This formula was to apply ostensibly in situations “where the *same* continental shelf is adjacent to the territories of two or more states whose coasts are opposite each other”.<sup>26</sup>

However, in the 1969 *North Sea* cases, the ICJ asserted that equity was the core juridical construct governing delimitation. The rule of equidistance was found *not* to constitute customary international law according to which the delimitation of continental shelf

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<sup>23</sup> See International Law Commission, *Yearbook of the International Law Commission*, Vol.II, 1956.

<sup>24</sup> *Ibid.*, p.300.

<sup>25</sup> *Ibid.*

<sup>26</sup> 1958 Convention on the Continental Shelf, *Article 6, paragraphs 1 and 2*. My emphasis.

areas must be carried out; rather, the fundamental requirement was that, “delimitation must be the object of agreement between the states concerned, and that such agreement must be arrived at in accordance with equitable principles”.<sup>27</sup> However, although a close association was drawn between the concept of natural prolongation and equity, the juridical link between the two was left ambiguous. The principal equitable criteria that were identified by the ICJ were intrinsically geographical concepts. The Court’s primary concern, in that case, was with achieving a reasonable degree of proportionality between the length of the parties’ coastlines and the division of the area in dispute. From this standpoint, the binding rule of equity was “not a question of totally refashioning geography whatever the facts of the situation but, given a geographical situation of quasi-equality as between a number of states, of abating the effects of an incidental special feature from which an unjustifiable difference of treatment could result”.<sup>28</sup>

How this related to the geological shape and extension of the seabed was somewhat unclear. Yet the Court’s use of the term “natural prolongation” conveyed a sense that natural underwater frontiers could be discovered, seemingly analogous to the way in which natural geographical features, such as rivers or mountain ranges, have often formed the basis of terrestrial political boundaries. This was not actually the intention, but the Court contributed to this misreading by affirming that certain configurational features of the seafloor could influence delimitation because, “in certain localities, they point-up the whole notion of the appurtenance of the continental shelf to the state whose territory it does in fact prolong”.<sup>29</sup> By creating a nexus between underwater geology and delimitation, the Court introduced a critical scientific role into the law, which merely served to invite further controversy. As a result, the tendency in several subsequent cases that went to international adjudication was for the states involved to examine the morphology and geophysical characteristics of the seabed, in some cases commissioning detailed and extensive scientific surveys, to ascertain whether the existence of a naturally forming boundary could be deduced from the shelf’s physical properties.<sup>30</sup>

Notwithstanding the confusion surrounding the ICJ’s use of the term “natural prolongation”, the 1969 judgment can be read as providing cogent support for Australia’s

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<sup>27</sup> *North Sea cases*, p.46, para.85.

<sup>28</sup> *Ibid.*

<sup>29</sup> *Ibid.*, p.51, para.95.

<sup>30</sup> The cases in which the parties relied upon geological and/or morphological evidence to support their claims include: the *UK/France* (1977), *Tunisia/Libya* (1982), *Gulf of Maine* (1984); and, *Libya/Malta* (1985).

claims. Certain paragraphs of the judgment resonate powerfully with the circumstances of the Timor Sea. In particular, the Court stated that:

Whenever a given submarine area does not constitute a natural – or the most natural – extension of the land territory of a coastal state, even though that area may be closer to it than it is to the territory of any other state, it cannot be regarded as appertaining to that state; or at least it cannot be so regarded in the face of a competing claim by a state of whose land territory the submarine area concerned is to be regarded as a natural extension, even if it is less close to it.<sup>31</sup>

The Court's view of the Norwegian trough in relation to the North Sea context confirmed, both in a legal and physical sense, the view held by Australia that the Timor trough could not be treated as a mere depression in a common continental shelf but as a natural divide between two separate shelves. The Court noted that “the shelf areas in the North Sea separated from the Norwegian coast by the 80-100 kilometres of the Trough cannot in any physical sense be said to be adjacent to it, nor to be its natural prolongation”.<sup>32</sup>

The ICJ's judgment in the *North Sea* cases is extremely important for understanding the grounds upon which Australia staked its claim in the Timor Sea, as this was the first occasion when the customary rules of international law in the area of maritime delimitation had been subjected to authoritative interpretation. In October 1970, an article in the *Australian Financial Review* questioning the validity of Australia's expansive continental shelf claim prompted Foreign Minister McMahon to make a statement on Australia's position in the House of Representatives.<sup>33</sup> The speech is an important one, as it contains the most explicit public statement of the government's policy and its underlying legal rationale that exists on record. McMahon stated that:

Australia based its 1967 legislation for regulating the exploration and exploitation of the petroleum resources on the continental shelf squarely on the international Geneva Convention of 1958, to which Australia is a party [...]

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<sup>31</sup> *North Sea* cases, p.31, para.44.

<sup>32</sup> *Ibid*, p.32, para.45.

<sup>33</sup> 'Aust's 'expanding rim' offshore minerals doctrine in question', *Australian Financial Review*, 16 October 1970.

the 1958 Convention embodies the two conceptions on which the law of the continental shelf is founded. It expressly states what has been called the 'expanding rim' doctrine – that is, that the shelf extends to the 200-metres depth-line, and beyond it to the limit of exploitability. From this, it is crystal clear that there is nothing in the law as it stands to restrict exploration permits to the 200-metres depth-line

...But the International Court of Justice has emphasized in a recent North Sea case that what is known as the morphological concept is also inherent in the Convention: indeed it is the foundation of the doctrine which the lawyers later took over and developed. The morphological concept is that the continental shelf is the natural prolongation under the sea of the land mass of the coastal state, out to the lower edge of the 'margin', where it slopes down to, and merges in, the deep ocean-floor or abyssal plain. These two concepts are in no way inconsistent. They both point to the outer edge of the 'margin' as the limit of the coastal state's rights

...the rights claimed by Australia in the Timor Sea are based unmistakably on the morphological structure of the seabed. The essential feature of the seabed beneath the Timor Sea is a huge steep cleft or declivity called the Timor trough, extending in an east-west direction, considerably nearer to the coast of Timor than to the northern coast of Australia. It is more than 550 nautical miles long and on the average 40 miles wide, and the seabed slopes down on opposite sides to a depth of over 10,000 feet. The Timor trough thus breaks the continental shelf between Australia and Timor, so that there are two distinct shelves, and not one and the same shelf, separating the two opposite coasts. The fall-back median line between the coasts, provided for in the Convention in the absence of agreement, would not apply, for there is no common area to delimit.<sup>34</sup>

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<sup>34</sup> Statement in the House of Representatives by the Minister for External Affairs, William McMahon, 30 October 1970.

The speech indicates the significance attached by the government to the ICJ's judgment in the *North Sea* cases regarding its own claims in the Timor Sea. Yet, the government's position was by no means impervious to legal critique or challenge. This was because the 'exploitability criterion' contained within Article 1 of the 1958 Convention had introduced an element of uncertainty and indeterminacy into the legal regime.

The Convention had stipulated that the rights of the coastal state extended to where the depth of the water "admits of the exploitation of the natural resources". As technology advanced the shelf boundary and, therefore, the coastal state's authority could be extended further out into the ocean, potentially indefinitely – hence being referred to in McMahon's statement as the "expanding rim doctrine". Yet, contrary to the Foreign Minister's claim, it did not, *prima facie*, 'point to the outer edge of the margin as the limit of the coastal state's rights'; actually, it pointed to well beyond that limit. Louis Henkin has described the inclusion of the exploitability criterion within the Convention as being highly controversial – the product of political bargaining and pressure from a group of countries with narrow shelves that wanted to enshrine within the treaty the potential to expand the geographical scope of their jurisdiction as offshore technology developed.<sup>35</sup> For this reason, it could be argued that Article 1 was "open-ended", which showed that whilst the legal regime derived from the natural phenomenon, it had "pursued its own development";<sup>36</sup> and as the law continued to evolve during the 1970s, this important distinction would become even more pronounced.

In 1973, the Third United Nations Conference on the Law of the Sea was convened to comprehensively deal with all issues of ocean governance. Amongst other things, the conference had the specific task of fixing the outer limits of national jurisdiction over the continental shelf, to replace the open-ended definition of the 1958 Convention. In December 1970, the General Assembly had adopted the Declaration of Principles Governing the Seabed and the Ocean Floor, which designated the seabed beyond the limits of national jurisdiction to be the common heritage of mankind; and "shall not be subject to appropriation by any means by states or persons, natural or juridical, and no state shall claim or exercise sovereignty or sovereign rights over any part thereof".<sup>37</sup> The Declaration was intended to protect the interests of developing countries but particularly newly independent developing countries, both coastal and landlocked. It was intended to stop technologically advanced coastal states from

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<sup>35</sup> Henkin, L. 1969. 'International law and "the interests": the law of the seabed', *American Journal of International Law*, vol.63(3), p.505.

<sup>36</sup> *Tunisia/Libya*, 1982, p.46, para.42.

<sup>37</sup> General Assembly Declaration 2749, 17 December 1970.

unilaterally appropriating unlimited areas of the deep ocean at the expense of the rest of the world.

The Conference extended over a period of almost a decade, involving more than 90 weeks of deliberations, in what has been described as the “most ambitious lawmaking endeavour ever undertaken by the international community”.<sup>38</sup> The treaty that emerged from this process – the 1982 UN Convention on the Law of the Sea – was a complex and multifaceted constitutional arrangement designed to govern all aspects of ocean space. The major innovation within the Convention was the institution of the exclusive economic zone (EEZ). This was a single, unitary 200 nautical mile zone wherein the coastal state has sovereign rights for the purpose of exploring and exploiting natural resources.<sup>39</sup> Entirely artificial and man-made, the concept was developed primarily in response to problems of water column jurisdiction and fisheries management and concerns about the depletion of various fish stocks in international waters.<sup>40</sup> It bears no relation to the natural features of the continental shelf and margin and, yet, because the regime of the EEZ grants states exclusive rights to the seabed and subsoil within the 200 nautical mile limit, its effect has been to totally transform the *legal* character of the continental shelf, as originally conceived and defined within the 1958 Convention, such that the jurisdiction of the coastal state extends “to a distance of 200 nautical miles from the baselines from which the breadth of the territorial sea is measured where the outer edge of the continental margin does not extend up to that distance”.<sup>41</sup>

With the materialization of the institution of the 200-mile zone, the relevance of seabed geomorphology as embodied within the juridical concept of natural prolongation would come to be seen by the ICJ in a completely different way. This became apparent, initially, within the context of the case between Tunisia and Libya in 1982. In the proceedings of that case, both states devoted a great deal of attention to the concept of natural prolongation, which they regarded, in light of the *North Sea* cases, as “not only pertaining to the essence of the continental shelf but also a major criteria for its delimitation”.<sup>42</sup> In arguing support for their respective positions, the parties made extensive use of the geophysical and oceanographic sciences, including the theory of plate tectonics, to demonstrate how the areas

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<sup>38</sup> Jacobson, J. L. and Rieser, A., 1998. ‘The Evolution of Ocean Law’, *Scientific American*, vol.9(3):104.

<sup>39</sup> The rights, jurisdiction and duties of the coastal state in the exclusive economic zone are set out under Part V of the UN Convention on the Law of the Sea, *Articles 55-75*.

<sup>40</sup> Evans, M. D., 1989. *Relevant Circumstances and Maritime Delimitation*, Clarendon Press, Oxford, p.4-5.

<sup>41</sup> 1982 UN Convention on the Law of the Sea, *Article 76, paragraph 1*.

<sup>42</sup> *Tunisia/Libya*, 1982, p.43, para.36.

in dispute formed the ‘most natural’ extension of their land territory.<sup>43</sup> *Tunisia/Libya* thus became something of a test case for the role of geological and morphological criteria in maritime delimitation. Yet the ICJ took a dim view of the parties’ scientific arguments and dismissed the idea that delimitation was a matter of simply “complying with the dictates of nature”.<sup>44</sup>

Because the legal regime of the continental shelf was disconnected from the physical phenomenon, the Court adopted the view in *Tunisia/Libya* that the principle of natural prolongation would “not necessarily be sufficient, or even appropriate, in itself to determine the precise extent of the rights of one state in relation to those of a neighbouring state”.<sup>45</sup> This fairly tentative rejection of the litigants’ geological arguments was dealt with more severely in the separate opinion of Judge Jimenez de Aréchaga. Aréchaga concurred with the ICJ’s decision but he argued that the new definition in Article 76, paragraph 1, of the 1982 Convention had, “even more than did Article 1 of the 1958 Convention, done away with the requirement of a geological or geomorphological continental shelf, thus destroying the conception of ‘natural prolongation’ advocated by both parties in this case”.<sup>46</sup> He continued: “this new method of defining the continental shelf by laying down an agreed distance from the baselines definitively severs any relationship it might have with geological or geomorphological facts. The continental shelf extends, regardless of the existence of troughs, depressions or other accidental features, and whatever its geological structure, to a distance of 200 miles from the baselines, unless the outer edge of the continental margin is to be found beyond that distance”.<sup>47</sup>

Aréchaga’s views were not only subsequently endorsed by the ICJ but found fuller expression in the Court’s judgment in the dispute between Libya and Malta in 1985. In that case, the ICJ did not simply abandon the principle of natural prolongation, as it had done in 1982, but sought to totally destroy it. The legal circumstances in *Libya/Malta* strikingly resemble those surrounding the dispute between Australia and East Timor and it is therefore worth setting them out in more detail. Malta claimed that the continental shelf boundary between the two countries should simply be the median line, as this would divide the area of overlap on a perfectly equal basis. Libya, by contrast, argued that the principle of natural prolongation made it incumbent upon both states to actually prove that their land territory

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<sup>43</sup> *Ibid.*, p.49-58, para.51-68.

<sup>44</sup> *Ibid.*, p.46, para.44

<sup>45</sup> *Ibid.*, p.46, para.44.

<sup>46</sup> *Ibid.*, p.114, para.51.

<sup>47</sup> *Ibid.*



physically extended, under the surface of the water, into the middle of the ocean between them. It asserted that, where there was a fundamental discontinuity between the natural prolongations of both countries, the boundary should be drawn “along the general line of that fundamental discontinuity”.<sup>48</sup> Libya argued that there were in fact two distinct continental shelves off the coasts of Libya and Malta separated from one another by a series of deep underwater troughs, more than 1,000 metres in depth, within an area described as a “rift zone”.<sup>49</sup> As the troughs were located much closer to Malta, a line drawn through this area would divide the space between the two countries disproportionately in favour of Libya.

Libya’s ‘rift zone’ argument was practically identical to Australia’s arguments vis-à-vis the Timor trough. It was comprehensively rejected by the Court for the reason that:

Since the development of the law enables a state to claim that the continental shelf extends up to as far as 200 miles from its coast, whatever the geological characteristics of the corresponding seabed and sub-soil, there is no reason to ascribe any role to geological or geophysical characteristics within that distance either in verifying the legal title of the states concerned or in proceeding to a delimitation as between their claims. This is especially clear where verification of the validity of title is concerned, since, insofar as those areas are situated at a distance of under 200 miles from the coasts in question, title depends solely on the distance from the coasts of the claimant state of any areas of sea-bed claimed by way of continental shelf, and the geological or geomorphological characteristics of those areas are completely immaterial.<sup>50</sup>

The Court concluded that there was therefore “no reason why a factor which has no part to play in the establishment of title should be taken into account for the purposes of delimitation”.<sup>51</sup>

There were two reasons, it should be noted, behind the ICJ’s dismantling of the principle of natural prolongation: the first had to do with the emergence of the 200 nautical mile zone. As a purely spatial concept, the zone rendered facts of geology totally irrelevant to the issue of delimitation within that distance. Secondly, because arguments based on natural

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<sup>48</sup> *Libya/Malta*, 1985, p.34, para.36.

<sup>49</sup> *Ibid.*, p.34, para.36-37.

<sup>50</sup> *Ibid.*, p.35, para.39.

<sup>51</sup> *Ibid.*, p.35, para.40

prolongation accorded a prominent role to scientific analysis, which the ICJ soon recognised militated against the normative development of the law. In *Libya/Malta*, the Court resented being placed once again in the unhappy position, whereby in order to decide a case it first had to make a “determination...as to the more plausibly correct interpretation of apparently incomplete scientific data”.<sup>52</sup> In response to the obvious problems this posed, it was noted that, “a criterion that depends upon such a judgment or estimate having to be made by a court, or perhaps also by negotiating governments, is clearly inapt to a general legal rule of delimitation”.<sup>53</sup> In terms of its relevance to the problem of delimitation, the concept of natural prolongation had, it seems, been consigned to history. According to Keith Highet, the 1985 decision was conclusive: “there was no more room for any further elaboration of the concept of a ‘natural prolongation boundary’” within international law.<sup>54</sup>

The morphological basis of Australia’s claim, in light of the ICJ’s 1985 decision therefore appears to have been substantially undermined. The legal significance of the trough, both in terms of establishing the validity of title and as a criterion relevant for the purposes of delimitation, had been reduced to nothing. The *Libya/Malta* ruling drove a stake right through the heart of Australia’s legal case. The precedent was firmly established that, with regard to maritime delimitations between facing coasts that are less than 400 nautical miles apart, geological or morphological factors are not to be taken into account. This is of tremendous significance within the context of the Timor Sea, where the distance between Australia and Timor is about 250 nautical miles. It is virtually inconceivable that an international court tasked with deciding the boundary between Australia and East Timor, today, would place any weight upon Australia’s argument concerning the significance of the Timor trough. For to do so would run counter to both the development of the jurisprudence and the whole tendency of state practice on the continental shelf in the last thirty years.<sup>55</sup> On this point, there is near

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<sup>52</sup> *Ibid.*, p.36, para.41.

<sup>53</sup> *Ibid.*, p.36-7, para.41.

<sup>54</sup> Highet, K. 1989. ‘Whatever became of natural prolongation’, in D. G. Dallmeyer and L. DeVorse, Jr. (eds), *Rights to Oceanic Resources: deciding and drawing maritime boundaries*, Martinus Nijhoff Publishers, Dordrecht, The Netherlands.

<sup>55</sup> As Dolliver Nelson has pointed out, there are a number of bilateral agreements which ignore features of far greater significance than the Timor trough. He notes that:

The agreement between France and Spain disregards the Cape Breton Trench. The agreement between Cuba and Haiti establishes an equidistance line without taking notice of the Caymen Trench (which is 2,900 metres deep, 1,700 kilometres in length and 100 kilometres wide). The India-Thailand delimitation takes no account of the Andaman Basin. The agreements between the Dominican Republic and Colombia and the Dominican Republic and Venezuela ignore the Aruba Gap (4,600 metres deep). The delimitation between the United States and Venezuela does not give any weight to the Venezuela Basin.

universal consensus within academic discussion of the question of the East Timor/Australia maritime boundary.<sup>56</sup>

### ***2.3 The Current Status of International Law: the norms applicable to courts***

Despite the ICJ's somewhat dismissive treatment of the equidistance/special circumstances rule in its 1969 decision, courts have since rescued it from obsolescence. It has now been fully reconciled with the equity norm, such that this rule is presently considered to have the character of customary international law.<sup>57</sup> Particularly in regard to delimitation between opposite coasts, the ICJ has stated that the "tracing of a median line...by way of a provisional step in a process to be continued by other operations, is the most judicious manner of proceeding with a view to the eventual delimitation of an equitable result".<sup>58</sup> This is something that courts have reiterated in a significant number of subsequent decisions.<sup>59</sup> For example, in the 2006 arbitration of the maritime dispute between Barbados and Trinidad and Tobago, the Permanent Court affirmed:

The determination of the line of delimitation thus normally follows a two-step approach. First, a provisional line of equidistance is posited as a hypothesis and a practical starting point. While a convenient starting point, equidistance alone will in many circumstances not ensure an equitable result in the light of the peculiarities of each specific case. The second step accordingly requires

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See Nelson, L.D.M., 1990. 'The Roles of Equity in the Delimitation of Maritime Boundaries', *American Journal of International Law*, vol.84(4), p.847-8.

<sup>56</sup> The works consulted include, *inter alia*, Cook, C., 1987. 'Filling the Gap – Delimiting the Australia-Indonesia Maritime Boundary', *Australian Yearbook of International Law*, p.131-75; Auburn, F. M., Ong, D. and V. L. Forbes, 1994. 'Dispute resolution and the Timor Gap Treaty', *Indian Ocean Centre for Peace Studies*, Occasional Paper No. 35; Prescott, J. R. V., 1999-2000. 'The Question of East Timor's Maritime Boundaries', *IBRU Boundary and Security Bulletin*, vol.7(4):72-82; Lowe, V., Carleton, C. and Ward, C., 2002. *In the Matter of East Timor's Maritime Boundaries: opinion*, unpublished; Ong, D. M., 2002. 'The New Timor Sea Arrangement 2001: is joint development of common offshore oil and gas deposits mandated under international law?' *The International Journal of Marine and Coastal Law*, vol.17(1): 79-105; Triggs, G. and Bialek, D., 2002. 'The New Timor Sea Treaty and Interim Arrangements for the Joint Development of Petroleum Resources of the Timor Gap', *Melbourne Journal of International Law*, vol.3(2):322-362; Antunes, N. M., 2004. *Towards the Conceptualisation of Maritime Delimitation: legal and technical aspects of a political process*, Brill Academic Publishers, Leiden, The Netherlands.

<sup>57</sup> *Qatar/Bahrain*, 2001, para.176.

<sup>58</sup> *Libya/Malta*, 1985, p.47, para.62.

<sup>59</sup> For example, in the *Eritrea/Yemen Arbitration*, the Tribunal took, as its "starting point, as its fundamental point of departure, that, as between opposite coasts, a median line obtains", *Award of the Arbitral Tribunal in the Second Stage of Proceedings (Maritime Delimitation)*, 1999, p.27, para.83.

the examination of this provisional line in the light of relevant circumstances, which are case specific, so as to determine whether it is necessary to adjust the provisional equidistance line in order to achieve an equitable result (*Cameroon v. Nigeria*, I.C.J. Reports 2002, p.303; Prosper Weil, *Perspectives du droit de la delimitation maritime*, p.223 (1988)). This approach is usually referred to as the “equidistance/relevant circumstances” principle (*Qatar v. Bahrain*, I.C.J. Reports 2201, p.40; *Cameroon v. Nigeria*, I.C.J. Reports 2002, p.303). Certainty is thus combined with the need for an equitable result.<sup>60</sup>

Notwithstanding the fact that courts have intentionally avoided any attempt “to identify, in the abstract, all the circumstances theoretically relevant to delimitation”, both the range and scope of criteria that fall within the category of ‘relevant circumstances’ have, over time, been steadily refined through the adjudicative process.<sup>61</sup> Churchill and Lowe have noted that they now “can be identified with some confidence as there has been a degree of consistency in the case law”.<sup>62</sup> These factors tend overwhelmingly to be geographic or cartographic in character, in terms of the geography of the surrounding area of seabed and/or the body of water concerned.<sup>63</sup> The fundamental equitable principle which underlies and unites all of these criteria is “a reasonable proportionality factor”.<sup>64</sup> This generally manifests itself in two types of geographical circumstances. The first is when minor geographic features, such as islands, or unusual and irregular features of the coastline, result in a disproportionate division of the area in dispute, even though the actual coastlines of the states concerned are roughly comparable in length.<sup>65</sup> The second situation is a mirror image of the first: it occurs when the relevant lengths of the coastlines of the respective states are dramatically different in length but the result of the equidistance line is a roughly equal division of the area in question.<sup>66</sup>

When either of these two scenarios obtains, the requirement for a reasonable degree of proportionality places a responsibility upon the dispute resolver to make a qualitative

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<sup>60</sup> *Barbados/Trinidad and Tobago*, 2006, p.73-4, p.242.

<sup>61</sup> *Gulf of Maine*, 1984, p.313, para.158.

<sup>62</sup> Churchill, R. R and Lowe, A. V., 1999. *The Law of the Sea*, 3<sup>rd</sup> Ed., Juris Publishing, Manchester University Press, Manchester, p.188-9.

<sup>63</sup> *Gulf of Maine*, 1984, p.278, para.59.

<sup>64</sup> Kozyris, P. J., 1998. ‘Lifting the veils of equity in maritime entitlements: equidistance with proportionality around the islands’, *Denver Journal of International Law and Policy*, vol.26:319-88.

<sup>65</sup> This principle underlies the decision taken by courts in *UK/France* (1977) and *Guinea/Guinea-Bissau* (1985).

<sup>66</sup> This principle underlies the decision taken in *Libya/Malta* (1985) and *Jan Mayen* (1993).

assessment of equity that determines whether a modification of, or departure from, the equidistance line can be justified. In both cases, it is “disproportion rather than any general principle of proportionality, which is the relevant criterion or factor”.<sup>67</sup> However, as the extent to which such disproportion is to be abated as well as the precise means by which it is to be remedied remains largely at the discretion of the tribunal seised, it has to be accepted that the law governing maritime delimitations is still affected with a degree of indeterminacy and will continue to remain so. Judges have resigned themselves to the fact that some measure of judicial discretion is an inescapable feature, “perhaps an irreducible core” of a rule of equity.<sup>68</sup> As was pointed out by the Permanent Court in *Barbados/Trinidad and Tobago*:

There will rarely, if ever, be a single line that is uniquely equitable. The Tribunal must exercise its judgement in order to decide upon a line that is, in its view, both equitable and as practically satisfactory as possible, while at the same time in keeping with the requirement of achieving a stable legal outcome. Certainty, equity, and stability are thus integral parts of the process of delimitation.<sup>69</sup>

#### ***2.4 Assessing the Role of International Law in the Negotiations***

The foregoing analysis provides an indication of why the Australian government might look upon the possibility of ICJ litigation in respect of maritime delimitation with considerable unease and offers an insight also into the opposing East Timorese viewpoint. The full scope of East Timor’s jurisdictional claims in the Timor Sea, it should be noted, are somewhat more complex than that of a mid-point boundary but as these claims evolved within the context of the negotiations they are best examined within that context (a task which is taken up in Chapters Five and Six). The remainder of this chapter is concerned with the theme introduced in Chapter One regarding the possible role that the jurisprudence played in the negotiations. This is an issue that, from the outset, is struck by a significant degree of ambiguity. Despite the argument I made in the previous chapter that international law has been a pivotal factor in these negotiations, there are reasons to assert that it has in fact had a

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<sup>67</sup> *UK/France*, p.58, para.101.

<sup>68</sup> *Libya/Malta*, 1985, Separate Opinion of Judges Ruda, Bedjaoui and de Aréchaga, p.90, para.37.

<sup>69</sup> *Barbados/Trinidad and Tobago*, 2006, p.74, p.244.

very marginal influence – far less perhaps than, as McLean has argued, “the commercial and governmental imperatives for the development of Timor Sea petroleum resources”.<sup>70</sup>

The first of these reasons is of a purely juridical nature. It has been shown that with regard to Australia and East Timor’s competing claims to jurisdiction north of the median line, the jurisprudence weighs heavily in favour of East Timor.<sup>71</sup> Yet, the jurisprudence is not binding upon Australia in any way. Australia is not bound by the ICJ’s judgment in the 1985 *Libya/Malta* case any more than East Timor would be bound by the ICJ’s decision in the 1969 *North Sea* cases. The decisions of previous cases provide a residual framework of legal norms which are totally subordinate to a bilateral or multilateral agreement reached on the basis of mutual consent. To be sure, the Australian government is bound only by the rules on delimitation enshrined within Article 83, paragraph 1, of the 1982 UN Convention on the Law of the Sea, to which Australia is a signatory.<sup>72</sup> Article 83, paragraph 1, simply states that:

The delimitation of the continental shelf between States with opposite or adjacent coasts shall be effected by agreement on the basis of international law, as referred to in Article 38 of the Statute of the International Court of Justice, in order to achieve an equitable solution.

Superficially, this provision contains a number of separate elements but, in practice, only one of them counts: namely, that delimitation is to be effected by agreement. The additional requirement that the boundary solution must be “equitable” is an almost entirely vacuous provision.<sup>73</sup> In the absence of any further provisions stipulating the means or method by which equity is to be achieved, other than by agreement, it is virtually meaningless. Further, the reference to “international law” provides little, if any, practical or normative guidance to parties in a dispute. In the absence of any indication as to which principles and

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<sup>70</sup> McLean, D., ‘Timor Sea Arrangement after East Timor independence’, *Australian Mining and Petroleum Law Association Yearbook*, 2002, p.622.

<sup>71</sup> There is, potentially, one mitigating factor for Australia, which is sometimes mentioned in academic discussions of the potential legal boundaries of East Timor; and that concerns the disparity in the lengths of the Australian and East Timorese coastline in the relevant area. According to David Ong, it is “eminently possible” that any tribunal tasked with adjudicating the matter could consider this to be a relevant factor, perhaps culminating in the northward movement of the putative median line. See Ong, D. M., 2002. ‘The New Timor Sea Arrangement 2001: is joint development of common offshore oil and gas deposits mandated under international law?’ *The International Journal of Marine and Coastal Law*, vol.17(1), p.89.

<sup>72</sup> Australia was an original signatory to the UN Convention on the Law of the Sea, on 10 December 1982. The official date of Australia’s ratification of the Convention is 5 October 1994.

<sup>73</sup> Evans, M. D., 1994. ‘Delimitation and the Common Maritime Boundary’, *British Yearbook of International Law*, vol.64, p.294.

rules from out of the whole spectrum of customary, general, positive and conventional international law are of particular significance, it is questionable whether any normative constraints upon the contractual freedom of states in this area actually exist.<sup>74</sup> Shigeru Oda has argued that the delimitation provisions of the 1982 Convention contain no such constraints. States may freely negotiate and can reach an agreement on whatever they wish; and they may utilize any bargaining strategy or leverage at their disposal for achieving political objectives.

Thus, the norms binding upon states are very different from the norms binding on courts. In the case of litigation, courts are required to apply the rule of equity. “The Court whose task is by definition to administer justice is bound to apply it”, the ICJ has declared.<sup>75</sup> Political discretion or any other non-legal factors must, in principle, play no role in judicially decided delimitations.<sup>76</sup> Diplomatic negotiations, on the other hand, are first and foremost a political exercise in which the objective of the governments concerned is not to administer justice but, in most instances, to attain agreement on the most favourable terms possible. As long as outcomes are arrived at through mutual consent and such arrangements do not affect the enjoyment by other states of their rights, the legitimacy that emanates from the independent sovereignty of states to conclude and enter into agreements of their own volition overrides all other legal considerations. States are free to establish maritime boundaries in areas subject to their jurisdiction on whatever basis they see fit and there is, therefore, “no compelling principle of delimitation which must be respected by the terms of such agreement as may be reached”.<sup>77</sup> A maritime boundary negotiated and freely entered into by the legitimate representatives of sovereign states is *a priori* an equitable one.

There is a profound difference therefore between settling maritime boundaries on a negotiated, as opposed to a judicial, basis. International law does not require any particular solution to the settlement of offshore areas, whether by way of a single, or combination, of boundary lines or by some other type of functional regime. International law grants states the freedom to agree on any arrangement they regard as satisfactory and can base their agreement

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<sup>74</sup> Weil, P., 1993. ‘Geographic considerations in maritime delimitation’, in J. L. Charney and L. M. Alexander (eds), *International Maritime Boundaries*, Vol.II, Martinus Nijhoff Publishers, Dordrecht, the Netherlands, p.121.

<sup>75</sup> *Tunisia/Libya*, 1982, p.60, para.71.

<sup>76</sup> Although, as has been pointed out by Robinson, Colson and Rashkow, “in a court such as the ICJ where only sovereign states can be parties, the judges in a given case may feel pressure to arrive at a decision that is acceptable to all”, in Robinson, D. R., Colson, D. A. and B. C. Rashkow, 1985. ‘Some perspectives on adjudicating before the world court: the Gulf of Maine case’, *American Journal of International Law*, vol.79(3), p.590.

<sup>77</sup> *Tunisia/Libya*, 1982, Separate Opinion of Judge Shigeru Oda, p.190, para.55.

on any consideration they regard as pertinent;<sup>78</sup> and negotiation provides governments with the flexibility to consider a wide range of political factors and economic interests which may or may not be related to their claims as of right. As Weil has noted, “governments certainly can, and often do, take into account legal precedents or rules when negotiating a delimitation agreement, but they can quite as well set aside legal considerations and draw a line according to whatever considerations they deem relevant (i.e. politically relevant) such as geography, economics, military, or convenience”.<sup>79</sup>

The implications of all of this is that legal norms do exist that are binding upon states in the area of maritime delimitation but not, it seems, in any way that is particular to the problem of maritime delimitation. They rest on a foundation of very general precepts of justice that are basic to the whole structure of international society.<sup>80</sup> The rule of agreement is, effectively, nothing more than a duty to negotiate in good faith. It has the character of *jus cogens*, which flows from the principle of the equality of the sovereignty of states and the obligation for states to settle their disputes by peaceful means – both of which are enshrined within the UN Charter. Beyond this most basic set of principles, however, nothing else is binding. As a result, one could argue that the extent to which the jurisprudence may impact upon diplomatic negotiations is a question whose answer depends entirely upon how far legal arguments are invoked in support of offshore claims and the extent to which the settlement takes account of them.<sup>81</sup>

Yet, in the case of the negotiations between Australia and East Timor, here again, it seems that opportunities for this kind of influence did not exist. The negotiations did not really touch upon the issue of maritime delimitation and, as will be shown later, the parties did not engage in any meaningful discussions of the jurisprudence relating to their claims as of right. The focus in the negotiations on issues of revenue distribution, pipeline jurisdiction, and the institutional architecture of the joint zone, were one step removed from the case law concerning disputes over maritime boundaries. The absence of any normative argumentation in the negotiations thus forecloses the possibility that the Australian government made concessions because of the ‘power of the better argument’. Indeed, the Australian government has consistently maintained that, at no point during the entire process, have concessions been

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<sup>78</sup> Weil, 1993. *op. cit.*

<sup>79</sup> *Ibid.*

<sup>80</sup> *North Sea cases*, 1969, p.46, para.85.

<sup>81</sup> Bowett, D., 1983. ‘Contemporary developments in legal techniques in the settlement of disputes’, *Receuil des Cours*, 1983, Vol.II, p.177.



made in acknowledgement of East Timor's legal or moral claims.<sup>82</sup> Regardless of what has been agreed, the government continues to assert the validity of its claim to the full extent of the continental shelf, northward to the deepest part of the Timor trough.<sup>83</sup>

Thus, despite the prominence of East Timor's legal claim, there are good reasons why it might not be possible to draw a *direct* causal connection between the jurisprudence and the pattern of concessions made over the course of negotiations. Yet, if one is to start with the proposition that the law did have a decisive impact upon the negotiation process, the question is how? My argument, as explained in the previous chapter, adopts a view of negotiation as, essentially, a problem of strategic choice. The process of negotiation is a pattern of interaction that takes the form of a linked series of choices.<sup>84</sup> These choices are frequently strategic in the sense that each party's ability to further its own ends depends on how the other behaves, and therefore the opponent's intentions must be taken into account.<sup>85</sup> At a very minimum, each side will confront the choice of whether to accept or reject the terms on offer. Agreement is in fact a fusion of two unilateral decisions to accept the terms as they stand rather than pursue an alternative course of action, whether this entails further attempts at influence, on the one hand or breaking off negotiations completely, on the other. From this standpoint, the basic objective in the bargaining process is to make the opponent prefer to choose agreement on your terms more than choosing either of these other alternatives. Negotiators will use tactics in an ongoing effort to make the terms on offer seem more attractive to the opponent and thus to dissuade him or her from further bargaining. This is where the use of threats and warnings normally come into play, as tactics intended to reduce the opponent's incentives for maintaining a non-compliant position.

According to Fred Iklé, the best way to dissuade an opponent from using such tactics is to convince him or her that no agreement will always look better to you than an agreement for which you would have to reduce your terms.<sup>86</sup> My contention is that case law and precedent provides a compelling means with which negotiators can achieve that objective. It enables negotiators to hold to a position consistent with the precedent and say to the other party that it would be better to have no agreement than one which is less favourable than that

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<sup>82</sup> Interview with member of Australia's negotiating team, November 2005.

<sup>83</sup> Department of Foreign Affairs and Trade Factsheet, *Australia-East Timor Maritime Boundaries*, July 2004, [http://www.dfat.gov.au/geo/east\\_timor/index.html](http://www.dfat.gov.au/geo/east_timor/index.html) <at 20 September 2004>

<sup>84</sup> Gross Stein, J., 2002. 'Psychological explanations of conflict', in W. Carlsnaes, T. Risse and B. A. Simmons (eds), *Handbook of International Relations*, Sage Publications, London, p.292.

<sup>85</sup> Lake, D. A. and Powell, R., 1999. 'International relations: a strategic-choice approach', in D. A. Lake and R. Powell (eds), *Strategic Choice and International Relations*, Princeton University Press, Princeton, p.1.

<sup>86</sup> Iklé, F. C., 1964. *How Nations Negotiate*, Praeger Press, New York, p.71.

position. To the extent that the other party still values having an agreement on those terms, such a commitment is likely to have a powerful effect on that party, as it will shape their perceptions of what is achievable. In this thesis, I shall show that the role played by international law within the negotiations between Australia and East Timor can be understood largely in these terms. The Australian government came to accept a position that was consistent with the case law, not through being convinced of the legal merits of East Timor's claims, but because Australia's negotiators became convinced that those terms had to be accepted if the dispute was to be brought to an end.

## CONCLUSION

The focus of this chapter has been on the legal issues that are of special relevance to this study. The emergence of the concept of the political maritime boundary is a distinctly post-World War Two phenomenon and one that is inextricably connected to the question of national ownership of marine resources, particularly offshore petroleum. During the second half of the twentieth century, particularly in the wake of the 1945 Truman Proclamation, the legal framework governing the oceans underwent a profound transition, from one based largely upon unrestricted freedom of access to a regime of increasing complexity that exhibits a far greater degree of coastal state control. International law, today, recognises coastal state rights to exclusive control over the resources of their continental shelves and economic activities within 200 nautical miles off their shores. As a consequence, coastal states now attach a high level of importance to the delimitation of maritime boundaries, for the purpose of clearly defining where their sovereignty over offshore areas lies.

Rules governing maritime delimitation have crystallised since the middle of the twentieth century through a process of international legal and political deliberation. The relevant legal provisions are to be found in the 1958 Geneva Conventions (Territorial Sea and Contiguous Zone; Continental Shelf) and the 1982 UN Convention on the Law of the Sea. These treaties do not provide a detailed framework of rules but, rather, are constitutive of states' rights and basic obligations. In determining how maritime areas subject to their jurisdiction are to be divided, states have considerable scope for crafting solutions to the problems they might encounter. Over time, however, the legal framework established by these treaties has evolved through third-party adjudication. Indeed, the judgments of the International Court of Justice and other *ad hoc* tribunals have played a crucial role in shaping

the law's development over the past forty-odd years. This 'normative framework' provides an indispensable basis for the agreements that states make.

The dispute between Australia and East Timor is situated wholly within this legal context. The purpose of this chapter has therefore been to explore that context, with particular focus on the aspects that are of special relevance to the Timor Sea dispute. When one considers the jurisprudence within the context of the parties' conflicting legal claims, it automatically becomes apparent why there was a motivation within East Timor following the 1999 referendum, both amongst United Nations officials and Timorese political leaders, to push for a larger share of the region's petroleum resources. Whilst being entirely legitimate in the eyes of the law, Australia's claims to jurisdiction on East Timor's side of the putative median line have lost the support of the evolving body of jurisprudence, as indicated in the precedent established by the ICJ's decision in the 1985 *Libya/Malta* case. The natural boundary concepts upon which Australia's claims are based were "laid to rest" by the ICJ in *Libya/Malta*, "probably for all time".<sup>87</sup>

Yet, negotiations between states, either for the purposes of delimitation or, for that matter, the establishment of a joint development regime in the absence of fixed boundaries, is an intrinsically political process, in which the states concerned have no obligation to take into account legal factors. As Oxman has pointed out:

The law of maritime delimitation may require the parties to negotiate in good faith. But it places few if any limitations on the location of an agreed boundary or related arrangements. Provided they agree, the parties are largely free to divide as they wish control over activities subject to their jurisdiction under international law. They may be guided principally, in some measure or not at all by legal principles and legally relevant factors a court might examine, and by a host of other factors a tribunal might well ignore such as relative power and wealth, the state of their relations, security and foreign policy objectives, convenience, and concessions unrelated to the boundary or even to maritime jurisdiction as such.<sup>88</sup>

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<sup>87</sup> Legault, L. and Hankey, B., 1993. 'Method, oppositeness, adjacency, and proportionality', in J. L. Charney and L. M. Alexander (eds), *International Maritime Boundaries*, Vol.I, Martinus Nijhoff Publishers, Dordrecht, the Netherlands, p.206.

<sup>88</sup> Oxman, B. H., 1993. 'Political, strategic and historical considerations', in J. L. Charney and L. M. Alexander (eds), *International Maritime Boundaries*, Vol.I, Martinus Nijhoff Publishers, Dordrecht, the Netherlands, p.11.

This chapter has attempted to highlight the problems that arise, when looking at the legal facts of the Timor Sea dispute, in understanding the precise nature of the relationship between the normative framework of international law and the dynamics of the bargaining process. The causal mechanism by which international law exerts influence is by no means straightforward. In the previous chapter, I reviewed the theoretical literature that relates to this question and in this chapter I have further elaborated on the central argument that was made. My contention is that international law exerted influence in these negotiations primarily through the dynamics of strategic interaction and processes of rational choice. International law was not the sole factor involved and it did not directly exert influence; but it had a decisive impact upon the motivations and behaviour of key players, which, in turn, determined bargaining outcomes.

### **3. THE POLITICAL HISTORY OF THE DISPUTE**

The dispute between Australia and East Timor has a long and intricate history that has been shaped predominantly by two separate, yet closely intertwined, processes: namely, the politics of decolonization in East Timor and the process of ocean boundary-making in the Timor Sea. Both of these were touched on briefly in Chapter One. The purpose of this chapter is to extend that discussion and, thus, to build upon the legal analysis of the previous chapter in developing a more detailed understanding of the context within which the negotiations between Australia and East Timor over offshore petroleum resources took place. The issues at stake in the negotiations are inextricably tied to past events. The chapter is organised around the successive phases of the seabed boundary negotiations between Australia and Indonesia that extended over a period of two decades, from 1970 to 1990. These negotiations culminated in the conclusion of two delimitation agreements, in 1971 and 1972 respectively, as well as the Timor Gap “Zone of Cooperation” Treaty, which was signed in 1989. Collectively, these arrangements laid down the international jurisdictional framework for the exploration and development of Timor Sea energy resources that existed at the start of East Timor’s transition to independence in 1999. The central task of this chapter is to understand how this framework was put in place. The analysis is based on both primary and secondary sources. Primary sources include the actual minutes of the seabed negotiations between Australia and Indonesia in March 1970 and February 1971, and a summary record of the talks in Jakarta, in October 1972. These official records of the Australian government have been made available through the Australian National Archive (NAA), Canberra.

#### ***3.1 Australia/Indonesia Seabed Negotiations***

The three original states with claims to a continental shelf in the Timor Sea comprised Australia, Indonesia and Portugal; the latter by virtue of its colonial position in East Timor. Australia was the first one of these to unilaterally claim jurisdiction in this region: firstly, through the Pearl Fisheries Act (1953) and then through the Petroleum (Submerged Lands) Act (1967). The Pearl Fisheries Act had adopted the 200 metre depth-line for the purposes of defining areas subject to Australia’s sovereignty over the resources of the continental shelf.

The ‘adjacent area’ line that was drawn up under the 1967 legislation, and which defined the seaward limits for the licensing of petroleum exploration, went considerably beyond this point. As was shown in the previous chapter, this line extended in the Timor Sea to the southern slopes of the feature known as the Timor trough, out to depths of between 1,000 and 1,500 metres, just a short distance from the island of Timor.

The drawing of this line was a bold move on the part of the federal government that had been strongly advocated by Australia’s Solicitor General, Sir Kenneth Bailey. Bailey held the view that “Australia and Timor do not, and would not at any time in the future, have ‘the same continental shelf’ within the meaning of the 1958 Convention (i.e. a common shelf which is subject to division on median line principles)”.<sup>1</sup> His advice was that the federal government should “assert jurisdiction publicly to the full extent of the existing grants”.<sup>2</sup> The areas of the Sahul Shelf, in the Timor Sea, which were covered by the 1967 legislation, were considered to be highly prospective and the government had encouraged and supported early exploration efforts through the use of federal expenditures in the form of subsidies.<sup>3</sup> The first significant discovery of hydrocarbons in the Timor Sea was made at the Petrel gas field by a joint venture involving the Atlantic Richfield Company, Aquitaine and Esso. The well was located 160 kilometres from the nearest Australian landfall in water depths of about 100 metres.<sup>4</sup>

Later that year, the Indonesian Minister of Mines, Soemantri Brodjonegoro, raised with Australian officials the possibility of discussing the issue of sea-bed boundaries between their respective territories, in areas of the Arafura and Timor Seas to the south of the island of New Guinea and north of Australia.<sup>5</sup> The Indonesian government had proclaimed sovereign rights to the resources of the continental shelf under a Presidential Decree in February 1969 but, unlike Australia, had not unilaterally drawn lines mapping the outer limits of jurisdiction. Soemantri had initially suggested that the parties’ discussions should take place in two stages, commencing with a preliminary technical exchange of views and information.<sup>6</sup> The Australian government agreed to this proposal and the first informal meeting was held in Canberra, from 19 to 24 March, 1970. The leader of the Indonesian delegation was Mochtar Kusumaatmadja, a Dean of the Faculty of Law, Bandung, who also acted as a legal adviser to

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<sup>1</sup> NAA: A5827, vol.37/Agendum 1165.

<sup>2</sup> *Ibid.*

<sup>3</sup> *Ibid.*

<sup>4</sup> Lee, R. J. and Gunn, P. J., 1989. ‘Bonaparte Basin’, in *Petroleum in Australia – the First Century*, Australian Petroleum Exploration Association Limited, Canberra, p.257-8.

<sup>5</sup> ‘Indo-Aust. Talks on who owns the offshore oil’, *Australian Financial Review*, 4 November 1969.

<sup>6</sup> NAA: A1838, 3034/7/8/1, Part 1.

the Department of Foreign Affairs. The Australian party was led by Sir Laurence McIntyre, Ambassador and Permanent Representative of the Australian Mission to the United Nations.

The approach suggested by the Australian side for dealing with the delimitation issue was to “break down the region into specific parts, or areas, so as to reduce to manageable proportions discussion on any particular area, and to avoid confusion”.<sup>7</sup> McIntyre proposed that four main areas called for particular consideration. These included:

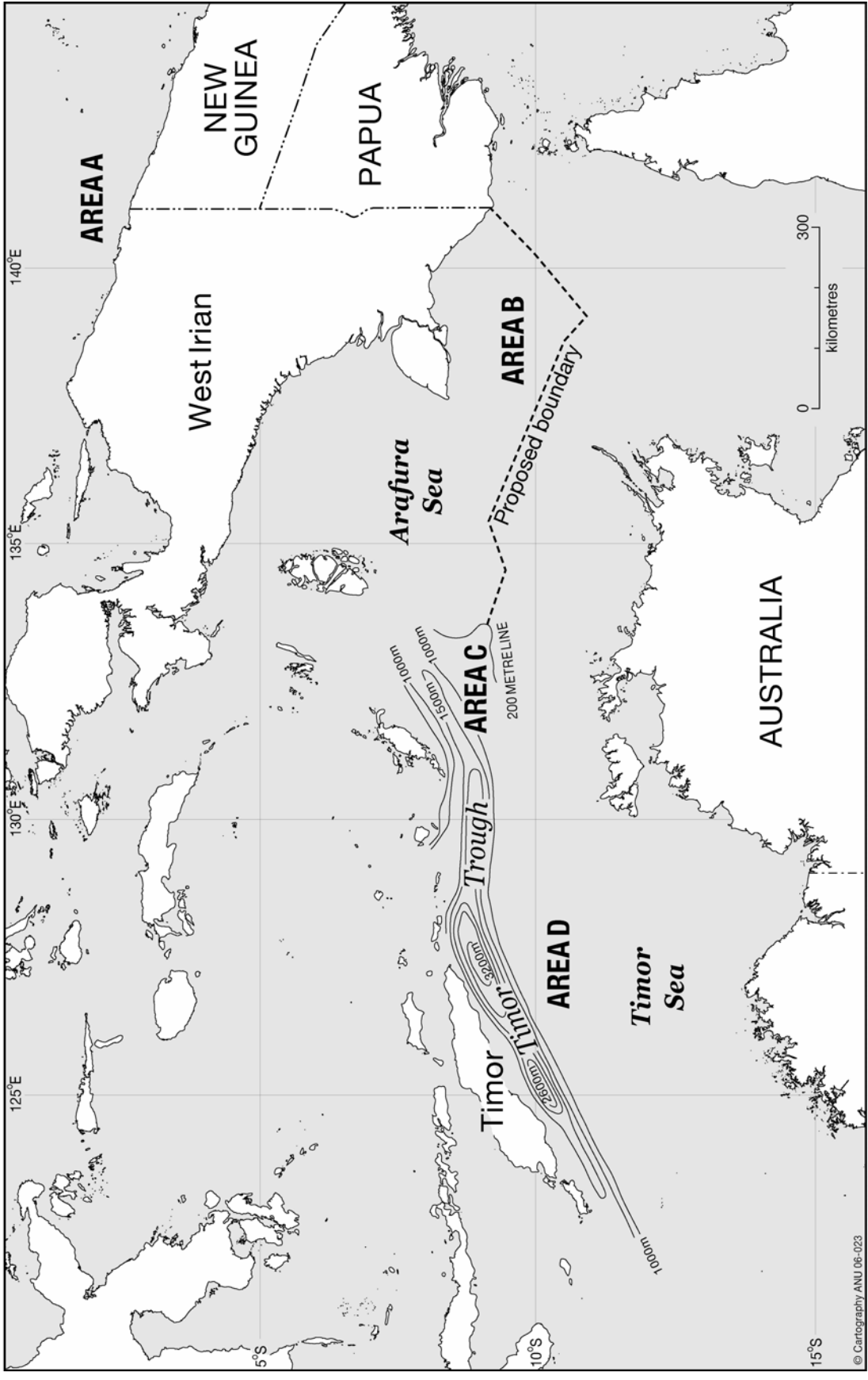
- A) the area in the Pacific Ocean off the north coast of New Guinea, adjacent to the northern end of the boundary between West Irian and the Trust Territory of New Guinea<sup>8</sup>
- B) the area in the Arafura Sea, extending southwards and westwards from the southern end of the land boundary between Papua and West Irian, out to a point on the 200 metre contour on the seabed
- C) the area between the 200 metre contour in the Arafura Sea and the eastern end of the Timor trough; and,
- D) the Timor Sea area between Indonesian Timor and Australia, including the Timor trough (see map below).

The breaking down of the region in this manner seems as much to have been a practical measure as it was a tactical move on the part of the Australian delegation to emphasise the importance of the topographical, or bathymetric, peculiarities of the areas concerned. Yet, it reflected a consideration given to purely legal factors, also. Reference to the 200 metre contour, in particular, stemmed from the significance attached to this point within the definition of the continental shelf under the 1958 Convention.

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<sup>7</sup> NAA: A4359, 201/2/3, Part 2.

<sup>8</sup> West Irian is, today, more widely known as West Papua. It refers to the western half of the island of New Guinea, which since 1969, has been recognised as part of the Republic of Indonesia. In Indonesia, the province is known by the name Irian Jaya.



MAP 4

Sketch Map Indicating Areas Subject to Negotiation in the Discussions between Australia and Indonesia, c.1970\*

\*The 'Proposed Boundary' indicated on the map was a median line between northern Australia and West Irian/Aru Islands. The line terminated at the eastern edge of the Timor trough where the depth of water reached 200 metres. West of this point, Australia and Indonesia's claims completely diverged.



Indonesia did not raise any objections to proceeding on this basis and the first of these areas that was opened for discussion concerned the region to the south of New Guinea (Area B). Here, there appeared to be no major differences in principle between the parties and the boundary lines that were initially proposed by the Australian and Indonesian delegations largely coincided. Both sides considered that the continental shelf in this area constituted a single and continuous shelf, common to each of the littoral states, on which basis a boundary delimited on median line principles was deemed appropriate. The area north of New Guinea (Area A) also posed little difficulty, although this was something that the Indonesian delegation had not envisaged being included because of the territory's political status under the trusteeship of Australia.<sup>9</sup>

However, it emerged that there was a considerable divergence of position with respect to Areas C and D where Australia claimed the existence of two separate continental shelves divided by the Timor trough. In contrast, Indonesia based its claim upon the principle of exploitability, which had been enshrined within Article 1 of the 1958 Convention. Mochtar made the argument that as the whole of the Timor Sea was capable of being exploited, at least potentially, there was, in a legal sense, a single continental shelf between Timor and Australia. Therefore, he contended that the whole area should be divided by a median line in accordance with established international practice.<sup>10</sup> Mochtar drew attention to the fact that the 'adjacent area' lines included within Australia's domestic legislation extended, in places, to where the depth of the seabed reached 5,000 metres (mainly off the south and east of the country). As Australia had endorsed the principle of exploitability for the purposes of its domestic legislation, Mochtar was critical of the fact Australia sought to assert that the international boundary in the Timor Sea should be based upon a different principle – that of seabed geomorphology.

The Indonesian position posed a major set-back for the Australian delegation, as one of the main objectives for the negotiations had been "to get the Indonesians to accept the Australian view that there were two shelves in the Timor Sea".<sup>11</sup> On 20 March, McIntyre suggested that the parties should work to a permanent agreement in areas that were not fundamentally in dispute (i.e. Areas A and B) but, with regard to the areas surrounding the

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<sup>9</sup> Australia had been the administering power of the Territory of Papua and New Guinea since 1902. Papua New Guinea gained its independence from Australia in 1975.

<sup>10</sup> NAA: A4359, 201/2/3, Part 2. State practice on continental shelf boundary delimitation at this point in time was limited. However, many of the international agreements that had been concluded, particularly those delimiting areas of the North Sea, had been settled on the basis of equidistance, irrespective of underwater geological features.

<sup>11</sup> NAA: A1838, 3034/7/8/1, Part 1.

Timor trough could “think about a line of administrative convenience, omitting of course the area opposite Portuguese Timor”.<sup>12</sup> The Indonesian delegation responded positively to this suggestion and the talks were adjourned for three days to allow for both sides to consult privately on the matter. When, the parties reconvened, on 24 March, Mochtar stated that the most appropriate form of compromise would be to accept a line half-way between the Indonesian median line and the “adjacent boundary” line, as indicated within Australia’s domestic legislation.<sup>13</sup> The counter-proposal suggested by McIntyre was to simply adopt the “adjacent area” boundary as the interim solution, which he explained could be viewed as a concession as it would represent an opportunity for Indonesia to exploit part of the southern slope of the trough, which from the Australian perspective “is strictly part of” Australia’s continental shelf.<sup>14</sup> Mochtar replied that McIntyre’s proposal was “not of much help to the Indonesian delegation” and, as a result, the problem of delimitation in the area of the trough was left open.<sup>15</sup>

Shortly after the conclusion of these preliminary discussions, both the Australian and the Indonesian governments were approached by Portugal on the same subject. The responses to Portugal’s approaches were negative. During a meeting with officials from Australia’s Department of External Affairs, in Canberra on 24 April 1970, the Portuguese Ambassador, Carlos Wemans, was told of the Australian contention that there were two continental shelves in the area between Portuguese Timor and northern Australia and, as a result, delimitation was not called for.<sup>16</sup> Wemans explained that Portugal took a different view, similar to that of Indonesia, and considered that the boundary between Timor and Australia should be the median line. He also mentioned that his government was contemplating issuing exploration permits in the region. This was confirmed in October 1970, when the Portuguese government published the co-ordinates of a draft exploration concession in response to an application made by a little-known US company, Oceanic Exploration.<sup>17</sup>

The draft concession consisted of three contiguous zones, the exterior limits of which extended beyond the equidistance lines between Portuguese Timor and Indonesia (to the east

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<sup>12</sup> NAA: A4359, 201/2/3, Part 2.

<sup>13</sup> *Ibid.* The position of the ‘adjacent area’ boundary is indicated on the map on p.36.

<sup>14</sup> *Ibid.*

<sup>15</sup> *Ibid.*

<sup>16</sup> NAA: A1838, 723/1/23 Part 2.

<sup>17</sup> The application had been made on 31 December 1968 and the coordinates of the draft concession were notified within the Official Bulletin of Timor, a government publication, on 24 October 1970.

and west) and Australia (to the south).<sup>18</sup> Shortly afterwards, Foreign Minister McMahon delivered his statement to the House of Representatives affirming the uncompromising basis and extent of the rights claimed by Australia in the Timor Sea. It is possible that McMahon's speech was, in part, a reaction to the publication of the draft concession, which appears to have provoked a response, in turn, from Portugal. On 2 November 1970, the Australian government became disturbed by a note received at its Embassy in Lisbon that was not only intended as a request for negotiations but as a formal reservation of Portugal's position with respect to what it regarded as "the unilateral appropriation by Australia of areas over which the island of Timor has rights".<sup>19</sup>

The negotiations between Australia and Indonesia subsequently resumed in Canberra, from the 15 to 21 February, 1971 and were confined mainly to the task of confirming the basic line, which had been provisionally adopted during the March 1970 talks, running roughly east-west in the eastern part of the Arafura Sea. This was a median line dividing the continental shelf between West Irian in the north and the Northern Territory in the south. The agreed line started from a point (B1) about 22 miles seawards from the West Irian coast and was drawn by reference to a series of twelve turning points (A1 – A12), ending at a point with the co-ordinates 8° 53' south and 133° 23' east, roughly southeast of the Tanimbar Islands in the Arafura Sea. This point marked the edge of the 200 metre contour at the eastern end of the trough.<sup>20</sup> There was an exchange of views with respect to the boundary beyond this point but the Australian delegation had not been given a mandate "to discuss a compromise line or agree to any line" in this region, thus preventing any further progress being made.<sup>21</sup>

The partial seabed boundary agreement was signed in Canberra, on 18 May 1971, by the Australian Minister for Foreign Affairs, Leslie Bury, and the Indonesian Minister for Mines, Soemantri Brodjonegoro. Because it affected the seabed boundaries of Papua New Guinea, the agreement was also submitted for consideration by the Administrator's Executive Council in Papua and New Guinea prior to signature to ensure the Council's support, which it received. Both prior to and after the signing ceremony, Ambassador Wemans approached Australia, this time with a formal request from the Portuguese government to commence delimitation negotiations. Australian officials reiterated the government position that there

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<sup>18</sup> A map of these concession zones has been reproduced in Antunes, N. M., 2004. *Towards the Conceptualisation of Maritime Delimitation: legal and technical aspects of a political process*, Brill Academic Publishers, Leiden, The Netherlands, p.546.

<sup>19</sup> NAA: 756/2/4/1.

<sup>20</sup> *Agreement between the Government of the Commonwealth of Indonesia and the Government of the Republic of Indonesia establishing Certain Seabed Boundaries*, signed 18 May 1971; entered into force 8 November 1973.

<sup>21</sup> NAA: A1209, 1970/6400, Part 2.

was no scope for negotiations and handed Wemans a copy of the ‘McMahon Statement’. This negative response reflected Australia’s assessment of both the bilateral and wider international dynamics of the situation. There was a concern that opening discussions with Portugal could hamper cooperation with Indonesia, which itself had been very unwilling to have talks with Portugal because it implied endorsement of the colonial regime.

With regard to the broader international situation, particular consideration was given to the preparations being made in the UN Seabed Committee for a comprehensive international conference on the Law of the Sea, expected to commence in the following year. The Australian government informed Portugal that if negotiations were to be held between the two countries at some point in the future, it would agree to do so only once the conference had reached its conclusion. In 1970, the UN General Assembly had endorsed the “common heritage of mankind” concept, which implied the need to impose fixed limits upon the extent of coastal states’ ocean jurisdiction and for international machinery to be established for the management and development of the mineral resources of the deep seabed, in areas beyond. In May 1970, President Nixon had proposed that all nations adopt a new treaty under which they would renounce all national claims over the natural resources of the seabed beyond the 200 metre isobath and to regard these resources as the common heritage of mankind.<sup>22</sup> Any changes made to the regime of the continental shelf along these, or similar, lines carried obvious implications for questions of jurisdiction in areas such as the Timor trough, which reached depths of more than 3,000 metres.

In a submission made to the Australian Cabinet, on 25 November 1970, McMahon had stated that “it seems probable that an area of deep seabed in the Timor Sea will eventually become subject to an international regime”.<sup>23</sup> The government’s position, therefore, was to leave the question of delimitation in the area of the Timor trough, vis-à-vis both Portugal and Indonesia, completely to one side, until the uncertainties regarding the legal limits of coastal state jurisdiction had been internationally agreed. However, Indonesia was determined to press the boundary issue with Australia and, in spite of the latter’s concerns about possible adverse reactions at the UN, it was agreed, in February 1972, that “all outstanding sea bed boundary questions should be negotiated at an early date”.<sup>24</sup> A Joint Communiqué issued at the conclusion of McMahon’s visit to Indonesia, now as Prime Minister, on 8 June 1972,

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<sup>22</sup> White House Press Release, May 23, 1970, 62 Dept. of State Bulletin 737 (1970).

<sup>23</sup> NAA: A1838, 752/1/23, Part 3.

<sup>24</sup> The joint communiqué was issued on 7 February at the conclusion of President Soeharto’s visit to Australia; See NAA: A1838, 1733/5 Part 1.

confirmed that negotiations would be resumed on the seabed boundaries still unsettled.<sup>25</sup> The re-commencement of formal talks was subsequently scheduled for Jakarta, from 2 to 10 October 1972.

Australia's decision to proceed with these negotiations was shaped, primarily, by its overriding interest in maintaining good relations with Jakarta. Foreign Minister Bowen advised that a continuation of the boundary dispute could be "a fundamental and lasting obstacle to the development of a relationship of trust and influence with Indonesia".<sup>26</sup> Furthermore, the government was conscious that Indonesia was willing to make concessions in the interests of reaching an early settlement. In private bilateral discussions following the February talks the Indonesians had hinted that they were anxious to secure agreement and would not insist on their maximum position.<sup>27</sup> In an interview given with the *Sydney Morning Herald* in July 1972, Mochtar was quoted as saying that Indonesia would "not seek to take an all-or-nothing stand but would look for a settlement based on an equitable balance between the Indonesian and Australian positions".<sup>28</sup> The situation facing Australia with regard to the claims of Portugal, on the other hand, was very different. Relations with Lisbon were considered to be of "relatively little importance" and, thus, it was easier for Australia to adopt a more intransigent approach.<sup>29</sup>

The leader of the Australian delegation to Jakarta at the October talks was Robert Ellicott, the Solicitor-General. On this occasion, the Indonesian delegation was led by R. B. (Didi) Djajadiningrat, Head of the Political Affairs Directorate in the Department of Foreign Affairs, with Mochtar acting as Deputy Chairman. When the negotiations opened on 2 October, both sides again re-iterated their original positions, which had been established at the first round of informal talks, in Canberra, March 1970. The Indonesia delegation re-stated their argument for a median line and, in reply, the Australian team argued that the proper outer limit of Australian jurisdiction was the bottom of the slope in the Timor trough. In the next session, Indonesia rejected Australia's notion of a naturally forming boundary but indicated that they wanted a settlement now and were prepared to compromise. Australia then offered to take as a starting point the principle that the continental shelf extended out at least to a depth of 200 metres, and proposed a line mid-way between the 200 metres contours of

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<sup>25</sup> 'The Australian-Indonesian Seabed Agreement', *Current Notes on International Affairs*, 1972, vol.43(10), p. 511.

<sup>26</sup> NAA: A1838, 752/1/23, Part 14.

<sup>27</sup> NAA: A1838, 752/1/23, Part 8.

<sup>28</sup> NAA: A1838, 752/1/23, Part 14.

<sup>29</sup> Way, W. (ed.), 2000. *Australia and the Indonesian Incorporation of Portuguese Timor, 1974-1976*, Melbourne University Press, Melbourne, p.52.

Australia and of Timor and Tanimbar. This was also rejected by the Indonesia delegation, as it would have resulted in a line running along the trough.

On 3 October, Indonesia made a counter proposal. Djajadiningrat suggested a line mid-way between the median line and the ‘adjacent area’ line of Australia’s offshore legislation. The Australian delegation agreed to consider this proposal but argued that the ‘adjacent area’ boundary seemed reasonable in principle to Australia, “since it would divide the disputed area approximately equally, would take into account what Australia had done in the area, and would take into account the 200 metres line”.<sup>30</sup> At the following session, Indonesia explained that, “after considerable debate among themselves and in a spirit of compromise”, they would accept the ‘adjacent area’ boundary in the area south of the Tanimbar islands but not in the western part south of Timor.<sup>31</sup> They then presented a further compromise proposal, namely, a line in the area south of Timor halfway between the compromise line, which had been initially proposed, and the ‘adjacent area’ boundary. However, the Australian delegation continued to pursue the ‘adjacent area’ boundary as a whole, which the Indonesian delegation finally accepted, in large part, after Australia agreed to give some minor face saving concessions.<sup>32</sup>

The line was drawn in two sections, with a gap in between of approximately 130 nautical miles south of Portuguese Timor, which subsequently came to be referred to within Australia as the ‘Timor Gap’. The first section extended the 1971 boundary across the western Arafura Sea by reference to four turning points (A13 – A16); the second section through a further eight turning points (A17 – A25).<sup>33</sup> Points A16 and A17 were intended to be equidistant between Portuguese Timor and Indonesia and thus as close to the coast of Portuguese Timor as was legally permissible.<sup>34</sup>

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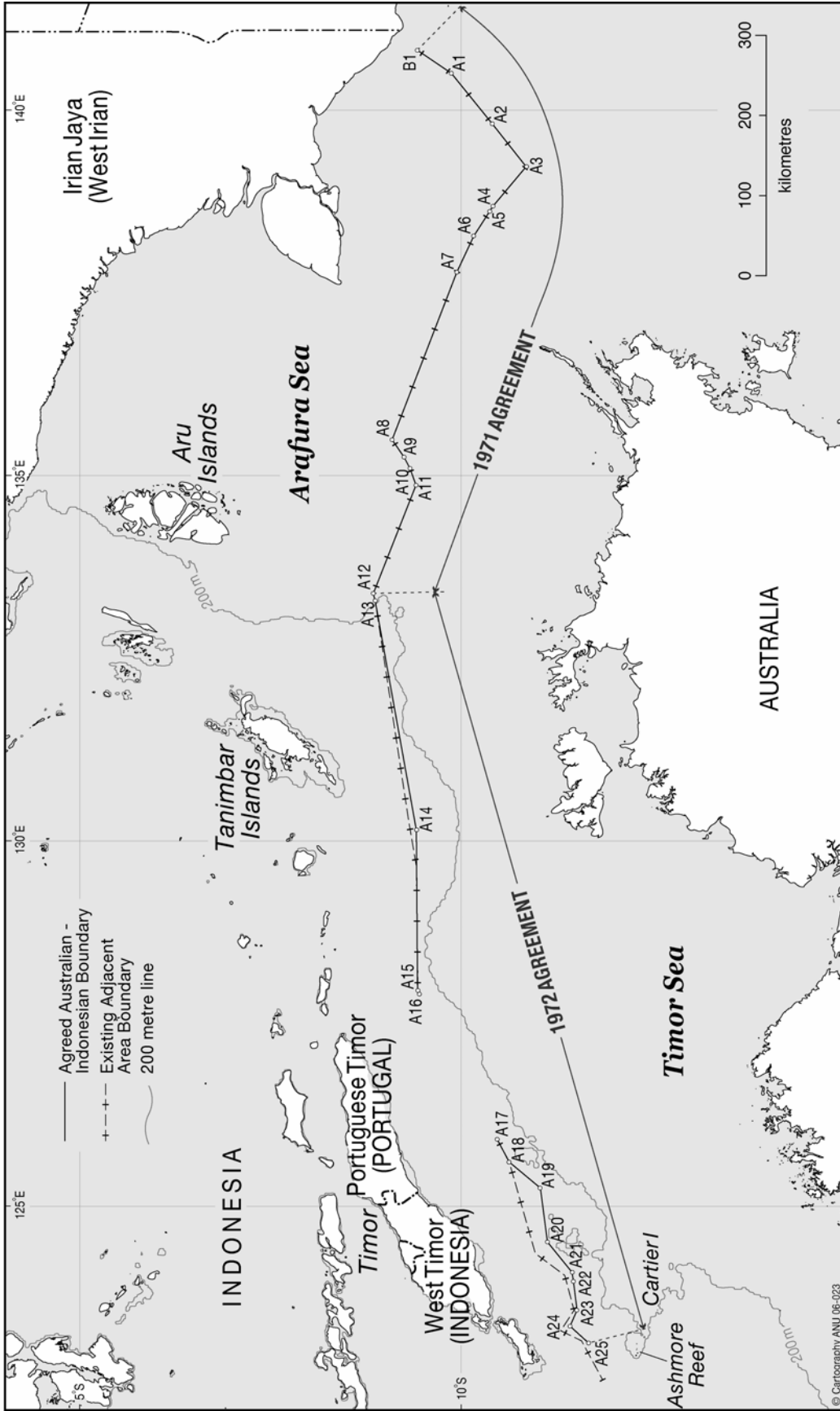
<sup>30</sup> NAA: A1838, 752/1/23, Part 14.

<sup>31</sup> *Ibid.*

<sup>32</sup> *Ibid.*

<sup>33</sup> *Agreement between the Government of the Commonwealth of Australia and the Government of the Republic of Indonesia establishing certain seabed boundaries in the Area of the Timor and Arafura Seas, supplementary to the Agreement of 18 May 1971*, signed 9 October 1972; entered into force, 8 November 1973.

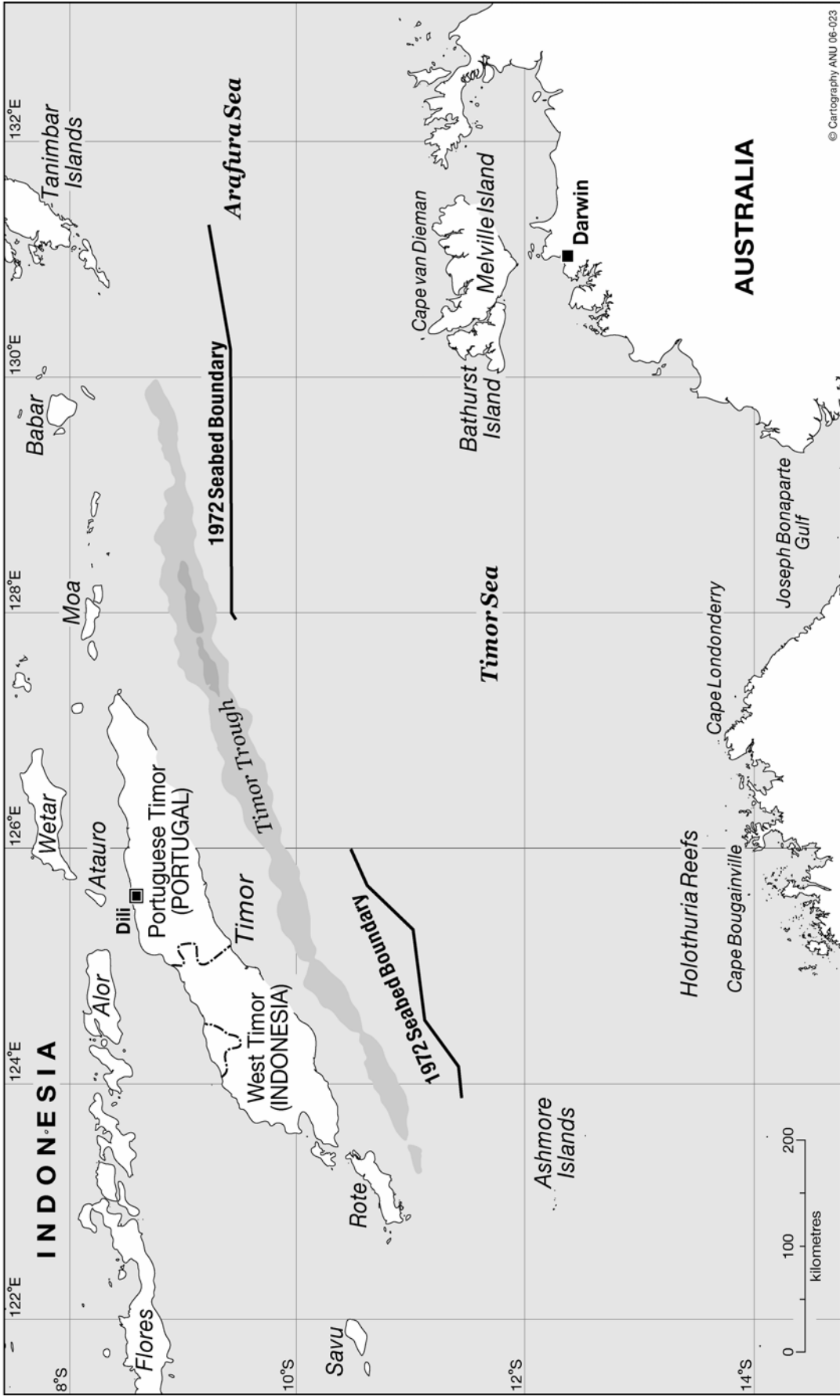
<sup>34</sup> Prescott has noted that these points are not precisely equidistant between East Timor and Indonesia. Point A16 apparently lies slightly closer to East Timor, whereas point A17 lies slightly closer to Indonesia. See Prescott, V., 2002. ‘East Timor’s Possible Boundaries with Indonesia and Australia in the Timor Sea’, a paper presented at the *JPDA 2002 Joint Petroleum Development Area Summit*, September 26-7, 2002.



MAP 5

**The 1971 and 1972 Australian/Indonesian Seabed Agreements\***

\*This map shows how close Australia came to achieving an outcome consistent with the boundary unilaterally claimed in 1967 (Adjacent Area Boundary). Australia conceded a sliver of the adjacent area line between A13 and A14 and a larger piece between A18 and A25. Of a total of 22,000 square miles in dispute, in the area between the median line and the adjacent area line, Indonesia gained only 1806 square miles.



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MAP 6

The “Timor Gap”



It was recognised, however, that these two points were not binding upon Portugal. In legal terms, they were not ‘opposable’ to Portugal. Thus, a special provision was included within the treaty so that these two points could be adjusted to accommodate a potential delimitation around Portuguese Timor.<sup>35</sup> A Joint Communiqué issued at the signing ceremony of the agreement, on 9 October 1972, stated that the boundary had been drawn “on the southern slopes of the Timor trough...dividing the area...in a fair and equitable manner”.<sup>36</sup> According to the post-conference report of the Australian delegation, the line had been structured on the basis of two main principles: equitable sharing of the disputed area and, secondly, respect for the significance of the 200 metre contour in the development of the international law of the continental shelf.<sup>37</sup>

The boundary gave Australia some 20,000 square miles of continental shelf more than a median line would; it preserved Australian jurisdiction over the whole of the shelf out to the 200 metre contour; and secured for Australia almost the entirety of the seabed area in which exploration permits had already been granted prior to the 1967 legislation. What surprised Australia’s negotiators was the relative effortlessness with which they were able to achieve such a favourable outcome. Patrick Brazil, who participated on the side of Australia, has described the agreement as being “pretty close to a world record” in terms of “the amount of time between when we began those negotiations and when we had a treaty that was signed off by the respective ministers and then, in due course, ratified”.<sup>38</sup> Because of the speed and ease with which a settlement was reached, the Australian side wanted the agreement to be officially signed as quickly as possible in case the Indonesian government suddenly realized how much had been given away and changed their mind. Brazil explained: “Normally, once a delegation has established an agreement in principle, it would have initialed the treaty to say that it was the authentic text...and then that would have had to come back to the respective governments, and the next step would have been the signing of the treaty by the respective ministers for foreign affairs...But...we moved so quickly that the leader of our delegation, Robert Ellicott...got on the phone to the foreign minister and said, ‘I think you ought to hop on a plane and come up here to sign this treaty straight away’”.<sup>39</sup>

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<sup>35</sup> This provision was included under *Article 3* of the 1972 Agreement.

<sup>36</sup> ‘The Australian-Indonesian Seabed Agreement’, *Current Notes on International Affairs*, 1972, vol.43(10), p. 510.

<sup>37</sup> NAA: A1838, 752/1/23, Part 8.

<sup>38</sup> Joint Standing Committee on Treaties, Committee Hansard, *Timor Sea Treaties*, 26 August 2002, p.1.

<sup>39</sup> *Ibid*, p.2

To understand why Indonesia was so eager to conclude this agreement with Australia one needs to understand something of the evolution of Indonesia's law of the sea diplomacy during the decade or so prior to negotiations. In Indonesia, the issue of offshore jurisdiction, historically, has been seen primarily through the prism of national security and the political cohesion of the state. Indonesia encompasses the most extensive archipelago in the world, comprising more than 13,000 islands that span a distance equivalent to an eighth of the Earth's total circumference. Maintaining the territorial integrity of such a geographically fragmented and ethnically diverse region has been an enduring political challenge. When the Republic of Indonesia was formed out of the Netherlands East Indies after the Second World War, the central government struggled to maintain control of the country in the face of recurring political crises, involving regional rebellion from a variety of religious and political groups vying for greater autonomy, or even separate provincial status.<sup>40</sup> Support given to rebel movements by external powers heightened the government's sense of vulnerability;<sup>41</sup> and, these fears were exacerbated by the fact that international law prevented the government from being able to exercise full control over the movement of foreign vessels and warships in areas of 'high seas' between the islands.

In December 1957, the Indonesian government moved to substantially alter this situation by issuing a declaration unilaterally extending the breadth of the country's territorial waters from three to twelve nautical miles. Concurrently, the government asserted rights to establish a system of linked straight baselines around the archipelago connecting the outermost points of the outermost islands. All waters within these straight baselines were claimed to be national waters subject to the absolute sovereignty of the state. This legal innovation, which came to be known as the archipelago principle, or doctrine, treated the islands and seas as a single entity, a notion which is itself embodied in the Indonesian word for fatherland or country – *tanah air* – literally meaning, the land (island) and water (the sea).<sup>42</sup> The concept was designed to increase the government's powers of authority over the country's fragmented territorial frame whilst also establishing a unifying symbol of national integration at a time of acute instability.<sup>43</sup>

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<sup>40</sup> Kroef, J. M. van der, 1957. 'Instability in Indonesia', *Far Eastern Survey*, vol.26(4):49-62.

<sup>41</sup> Leifer, M., 1978. *Malacca, Singapore and Indonesia*, Sijthoff and Noordhoff, the Netherlands, p.16.

<sup>42</sup> Djalal, H., 1995. *Indonesia and the Law of the Sea*, Centre for Strategic and International Studies, Jakarta, p.336.

<sup>43</sup> Leifer, 1978, *op. cit.*; Djalal, D. P., 1996. *The Geopolitics of Indonesia's Maritime Territorial Policy*, Centre for Strategic and International Studies, Jakarta, p.32.

Indonesia's attempts to have its maritime/territorial regime recognised within international law met with firm resistance by the world's maritime powers out of concern that their right of innocent passage and submerged navigation through the archipelago would be subjected to unilateral forms of control.<sup>44</sup> Indonesia occupies a highly strategic position, lying across all the main passages from the Pacific to the Indian Ocean north of Australia. For the US navy, in particular, free and unimpeded access through these navigational straits constituted an important component of maritime strategy and doctrine. At both the First and Second UN Conferences on the Law of the Sea, Indonesia was unable to build sufficient support amongst delegates to have the 'archipelagic regime' included on the conferences' agenda. In the face of such strong international opposition, the government looked towards alternative political methods of gaining support – one of which included maritime delimitation.<sup>45</sup> By invoking the straight baselines used to draw the territorial limits of the archipelago as the base-points for delimitation with neighbouring countries, the government hoped that international recognition for the archipelagic regime concept could be built through state practice and local precedent.

After proclaiming jurisdiction over the continental shelf in 1969, Indonesia embarked upon a process of delimiting its international maritime boundaries at an unusually high pace. Negotiations first commenced with Malaysia to settle seabed boundaries in the Malacca Straits and South China Sea, in 1969, and an agreement was concluded the same year. In addition to the agreements with Australia, Indonesia successfully negotiated a complex delimitation with Malaysia and Thailand in the northern Malacca Strait and with Thailand in the Andaman Sea, in December 1971. In early 1972, Indonesia also opened negotiations with South Vietnam. Indeed, between 1969 and 1975, Indonesia concluded a total of twelve bi- and tri-lateral maritime boundary agreements with neighbouring countries, including Malaysia, Thailand, Singapore, Burma and India as well as Australia.<sup>46</sup> Delimitation served a dual purpose. For it not only allowed President Soeharto to demonstrate his 'good neighbour' credentials by cooperating over the management of sensitive territorial matters but it also

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<sup>44</sup> Dean, A. H., 1960. 'The second Geneva conference on the law of the sea: the fight for the freedom of the seas', *American Journal of International Law*, vol.54(4), p.765-6.

<sup>45</sup> Kusumaatmadja, M., 1982. 'The Concept of the Indonesian Archipelago', *Indonesian Quarterly*, vol.X(4)12-26.

<sup>46</sup> At no time during this period did Indonesia indicate any interest in negotiating maritime boundaries with Portugal, in the area around Portuguese Timor. This was likely to have been for two reasons: firstly, because the Indonesian government had taken a strong stand against European colonial policy in Southeast Asia and thus would not have wanted to act in any way that legitimated Portugal's role in East Timor; and, secondly, because Portuguese Timor presented a special problem for Indonesia given that maritime boundaries around the territory would have created an enclave inside Indonesia's archipelagic baselines.

provided a means of bolstering support for Indonesia's controversial 'archipelagic doctrine'. In effect, maritime delimitation agreements were designed to provide a vehicle through which Indonesia sought acceptance of its archipelagic baselines through state practice and acquiescence.<sup>47</sup>

This brief history of the evolution of Indonesia's law of the sea diplomacy provides some insight into the attitude, or the political mind-set, that helps explain the accommodative stance shown not just towards Australia but most of the countries Indonesia shared a maritime boundary with. However, other factors related to the particular context of bilateral relations at this time seem also to have been very important. It has been argued elsewhere that Indonesia's willingness to concede in the 1972 negotiations can be understood as a specific reciprocity push in return for the economic and political 'goodwill' Australia had shown Indonesia over preceding years.<sup>48</sup> The status of bilateral relations at the time of the 1972 negotiations was highly uneven. Australia had warmed to Soeharto's pro-Western outlook and was at the forefront of those countries willing to commit economic and defence aid to support his grip on power and suppress communist activities within Indonesia. Since the rise of the 'New Order', Australian economic aid and technical assistance had been steadily increasing year by year. Between 1970 and 1973, for example, Australia provided Indonesia with AUD\$54 million in foreign aid and had also assisted Indonesia secure funding through the International Monetary Fund and the World Bank. This was in addition to other forms of defence and military assistance.<sup>49</sup> In July 1972, Australia initiated a defence co-operation programme with Indonesia worth AUD\$20m, which included provision of fighter aircraft, training and intelligence cooperation.<sup>50</sup> Thus, the broader context of Indonesia's foreign policy and relations with Australia at this time pointed to a situation in which Soeharto would have been reluctant to take a hard line against an Australian side that was reasonably confident of the legal basis of its negotiating position.

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<sup>47</sup> Hamzah, B. A., 1984. 'Indonesia's Archipelagic Regime: implications for Malaysia', *Marine Policy*, vol.8(1), p.30.

<sup>48</sup> Mills, A., 1990. 'The Timor Gap Treaty: more paper for the cracks or a foundation for the wall?' *Inside Indonesia*, March 1990, p.6.

<sup>49</sup> NAA: A1209, 1970/6400 Part 2 - Discussions between Indonesia and Australia regarding continental shelf boundary; Chalk, P., 2001. *Australian Foreign and Defense Policy in the Wake of the 1999/2000 East Timor Intervention*, RAND Publications, <http://www.rand.org/publications/MR/MR1409/> <Accessed 27 September 2005>, p.23-4.

<sup>50</sup> *Chega!*, Final Report of the Commission for Truth, Reception and Reconciliation in East Timor, October 2005, Part 7, p.29.

Andrew Mills has argued that concessions over seabed jurisdiction may have been one of the few means Soeharto had available to reciprocate Australian bilateral support.<sup>51</sup> Whilst unlikely to have been the product of an explicit *quid pro quo*, there was a distinct awareness within the Australian government of there being an opportunity to take advantage of the present circumstances. Robert Furlonger, Australia's Ambassador to Indonesia during this period, and a member of the Australian team at the Jakarta negotiations, has stated that Soeharto's interest in developing closer strategic, political and economic ties with Australia made it a propitious time to negotiate.<sup>52</sup> In effect, Indonesia was prepared to accommodate the bulk of Australia's claim in order to secure other political objectives.<sup>53</sup>

Soeharto's decision to have Djajadiningrat chair the discussions, as opposed to Mochtar, is indicative of the political content Indonesia attached to them. Mochtar would have been more mindful of the legal issues involved, particularly with respect to the negotiations taking place in the UN Seabed Committee and the changes to the law of the sea that were expected to be made in the near future.<sup>54</sup> He would have been acutely aware of the growing support, particularly amongst Asian and African states, for national jurisdiction over the seabed to be limited by a fixed distance factor, with the trend increasingly towards the concept of the 200 nautical mile zone. The obvious fact that a 200 mile limit would place greater emphasis on a median line in the Timor Sea was something that Hasjim Djalal, of the Indonesian delegation to the UN Seabed Committee, had conveyed to members of the Australian delegation, as early as July 1971.<sup>55</sup> For Indonesia to have made concessions at a time when the law was entering a period of such profound and rapid change may, in retrospect, have been a bad decision, yet one that was obviously considered to be of wider political value at the time it was taken.

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<sup>51</sup> Mills, *op. cit.*

<sup>52</sup> Pers. Comm. Robert Furlonger, August 2004.

<sup>53</sup> *Ibid.*

<sup>54</sup> The Seabed Committee had been set up in 1967 and, from 1971 to 1973, it worked as a preparatory body for the Third UN Conference on the Law of the Sea. Both Australia and Indonesia were members of the Seabed Committee.

<sup>55</sup> NAA: A1838, 752/1/23, Part 8. Indeed, the Australian delegation had noted "the growth of support among the developing states over the resources beyond the territorial sea, both of the sea (fish) and of the seabed (minerals) and over pollution and scientific research". Following the 1971 session of the conference's preparatory committee, the Australian delegation reported that "the Latin American claim of a 200-miles resources zone seems to be gaining favour".

### *3.2 The Seabed Dispute between Australia and Portugal and the Conflict in East Timor*

From the perspective of Portugal, the 1972 seabed boundary agreement between Australia and Indonesia was strategically unhelpful, given the earlier symmetry of the Portuguese and Indonesian claims to a boundary at the mid-point. The agreement made it practically impossible to conceive of Australia now accepting the Portuguese position. Australia, however, was understandably keen to reach a similar agreement with Portugal, yet found that it lacked the leverage to obtain such an outcome. When the government formally approached Lisbon, on 5 March 1973, with a request to open negotiations on the delimitation of the continental shelf, it found that the tables had been completely reversed: it was Portugal that now explained that it would rather wait for the conclusion of the UN Conference of the Law of the Sea, before entering into such bilateral discussions. The impending changes to international law, which would place greater emphasis on distance based as opposed to morphologically oriented entitlement criteria, meant that it was to Portugal's advantage to await these changes.

Subsequently, and in an apparent effort to unilaterally deny the validity of Australia's seabed claims, the Portuguese government announced, on 31 January 1974, that its Minister for Overseas Territories had been authorized to sign an agreement with Oceanic Exploration, under which the company would be permitted to explore for oil in the Timor Sea.<sup>56</sup> Australia made an oral protest to Ambassador Wemans in response to the announcement on 25 March, which itself produced a written reply from the Embassy on 18 April 1974. The Embassy's note gave details about the Portuguese concession and also stated that "Portugal recognises only one continental shelf between Australia and Portuguese Timor and regards the median line between the respective coasts as the boundary".<sup>57</sup>

The concession covered an area of more than 60,000 square kilometers, extending to the median line and cut across seven permits which had been granted under Australian legislation. This created a clear conflict of interest, which was particularly concerning to Australia in view of the fact that drilling operations in the area of the Troubadour Shoals, not far from the eastern edge of the Oceanic concession, were currently being undertaken. The

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<sup>56</sup> Negotiations between the Portuguese government and Oceanic had taken place throughout the period since the first draft terms of the Timor Sea concession had been offered in 1970. In 1972, Oceanic created a subsidiary to administer the concession, *Petrotimor Companhia de Petroleos S.A.R.L* ("Petrotimor"). The concession was signed by the Portuguese Minister for Overseas Territories on 11 December 1974.

<sup>57</sup> NAA: 756/2/4/1.

Department of Minerals and Energy, with support from the Foreign Affairs and Attorney-General's Departments, had encouraged the drilling of this area "mainly to assert [Australia's] sovereignty and also keeping in mind that the Troubadour structure is very large and therefore very prospective".<sup>58</sup> The government felt that if the area could be developed it would be difficult for anyone "to take it away".<sup>59</sup> The Australian government felt that a formal written protest should be made in response to the Embassy's note but this was not immediately done on account of the fact that, just one week after the note was received, the Portuguese capital was gripped by a sudden revolution.

On 25 April, a coalition of battle-weary and disenfranchised Portuguese soldiers led by General Antonio Spínola, known as the Armed Forces Movement, seized political control in Lisbon, seeking radical changes in both domestic and foreign policy.<sup>60</sup> With respect to the latter, the new regime immediately sought to implement a programme of decolonization by "abrogating the former territorial definition of the Republic of Portugal and acknowledging the right of self-determination, including independence, for territories under Portuguese administration".<sup>61</sup> In Portuguese Timor, the Lisbon coup galvanized political interest in the future of the territory and, within just a few weeks, several political parties had been formed, each advocating competing goals in the process of self-determination.<sup>62</sup>

As early as 1963, Australia's Cabinet had expressed the view that "no practical alternative to eventual Indonesian sovereignty over Portuguese Timor presented itself".<sup>63</sup> This was re-affirmed in a policy planning document prepared, on 3 May 1974, in response to the revolution in Portugal. The government considered that in view of the territory's perceived economic non-viability, the "logical long-term development is that it should become part of Indonesia".<sup>64</sup> Furthermore, it was noted that there would be certain advantages to pursuing this outcome for Australia in that, "the Indonesians would probably be prepared to accept the same compromise as they did in the negotiations already completed on the seabed boundary".<sup>65</sup> Portuguese Timor was of little intrinsic interest to Australia. The volume of bilateral trade between the two, at this time, was fairly negligible and the only issue of

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<sup>58</sup> NAA: A1838, 1733/5 Part 1 - Law of the sea - Oil mining on the Australian continental shelf.

<sup>59</sup> *Ibid.*

<sup>60</sup> Way, 2000, *op. cit.*, p.3.

<sup>61</sup> Krieger, H. (ed.), 1997. *East Timor and the International Community: basic documents*, Cambridge University Press, Cambridge, p.34.

<sup>62</sup> *Chega!*, Final Report of the Commission for Truth, Reception and Reconciliation in East Timor, October 2005, Part 3, p.15.

<sup>63</sup> Way, 2000, *op. cit.*, p.26.

<sup>64</sup> *Ibid.*, p.51.

<sup>65</sup> *Ibid.*, p.52.

substantial concern was the delineation of the continental shelf.<sup>66</sup> Of “special interest”, however, were the ramifications of Timor’s decolonization for Australia’s relations with Indonesia. In order to maintain the co-operative relationship which had developed between the two countries over recent years, the government placed a premium on avoiding taking any stance regarding the colony’s political future that would put Australia at variance with Indonesia. And the basic “thrust” of Indonesian thinking following the Lisbon coup was for the territory to be fully absorbed into Indonesia.<sup>67</sup>

Indonesia held “strategic anxieties” about the territory’s possible emergence into independence, which stemmed from a paranoiac fear of Timor becoming a future base of communist subversion throughout the archipelago.<sup>68</sup> At a meeting between President Soeharto and the Australian Prime Minister, Gough Whitlam, on 6 September 1974, Soeharto explained that, as an independent state, Portuguese Timor would need to rely on foreign economic assistance to remain politically viable and this would pose a “big danger” of communist countries, such as China or the Soviet Union, gaining “an opportunity to intervene”.<sup>69</sup> Whitlam was sympathetic to these fears and informed the President that he believed Portuguese Timor should become part of Indonesia, although he indicated that this outcome would be more agreeable to Australia if it happened “in accordance with the properly expressed wishes of the people of that territory”.<sup>70</sup> In light of this policy, the Australian government decided that to continue to pursue negotiations with Portugal on seabed delimitation would be counter-productive. Instead, Whitlam approved a note being sent to the Portuguese Embassy, in Canberra, on 29 November 1974, requesting Portugal to cancel the 31 January concession and not to allow exploration in any of the areas covered by established Australian permits. Two letters were subsequently sent to Oceanic warning of “substantial penalties” if the company conducted any exploration activities in areas covered by Australia’s offshore legislation.<sup>71</sup>

There were three main political associations in Timor which had been formed in response to the April 25 coup. The UDT (Democratic Union of East Timor) supported independence after a period of continued association with Portugal. FRETILIN (Revolutionary Front for an Independent East Timor), which had the largest following,

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<sup>66</sup> *Ibid.*, p.108; Reece, R., 1974. ‘Portuguese Timor: 1974’, *Australia’s Neighbours*, No.90, p.5.

<sup>67</sup> Way, 2000, *op. cit.*, p.88-90.

<sup>68</sup> *Ibid.*, p.91.

<sup>69</sup> *Ibid.*, p.97.

<sup>70</sup> *Ibid.*, p.95

<sup>71</sup> The two letters to Oceanic were sent on 28 July and 28 August, 1975.



favoured immediate independence. APODETI (Timorese Democratic People's Union), which was little more than a front for Indonesian interests and the smallest of the three, advocated integration with Indonesia. Between May and June 1975, negotiations were held between the Portuguese government and representatives of these political associations leading to an agreement on the process of self-determination in Timor, which was incorporated into Portuguese constitutional law.

The programme established by the new law set a timetable for "direct, secret and universal" elections to be taken in October 1976 and for an end to Portuguese sovereignty two years later. It also provided for a transitional government, composed of both elected East Timorese and appointed Portuguese members, and a government consultative council, which would have the responsibility of administering the territory until the termination of Portuguese sovereignty, in 1978.<sup>72</sup> However, Portugal was ill-equipped – both financially and militarily – to manage the implementation of the agreement and, during August 1975, rising tensions between the Timorese factions led to the outbreak of armed conflict in Dili, which quickly spread to other parts of the territory. On 27 August, the Portuguese authorities evacuated Timor, initially to the island of Atauro, thirteen miles from Dili. The deterioration of political conditions in East Timor and Portugal's incapacity to control the situation in some ways assisted Indonesia as it provided a basis upon which armed intervention could be justified, *viz.*, in the name of restoring peace and security to allow for the processing of self-determination.

At this point, it had already been decided in Jakarta that the territory would be integrated into Indonesia, by force if necessary. In February 1975, Malcolm Dan of the Australian Embassy in Jakarta reported of a meeting with a key figure in Soeharto's inner circle, Harry Tjan, at which Tjan had explained that a unanimous decision had been made by all the leading Indonesian personalities involved, including the President, "that sooner or later Portuguese Timor must form part of Indonesia".<sup>73</sup> Apparently, "all that remained to be decided was when, and how, this should be brought about". Tjan stated that the Indonesian government would first try every conceivable means of achieving a peaceful integration before turning to the "ultimate act" of a military solution.<sup>74</sup> Two of the key actors responsible for formulating Australia's policy on Timor – Prime Minister Whitlam and Australia's Ambassador to Jakarta, Richard Woolcott – firmly believed that if, in the worst case scenario,

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<sup>72</sup> Kreiger, 1997, *op. cit.*, p.34-5.

<sup>73</sup> Way, 2000, *op. cit.*, p.198.

<sup>74</sup> *Ibid.*

Indonesia invaded and forcibly annexed East Timor without a proper act of self-determination, this should not be opposed by Australia. They made a key judgment: that the risks to Australia of intervening on behalf of Timor were potentially so great that it should be avoided.<sup>75</sup>

In June 1975, Woolcott advised that in the event of the use of force by Indonesia, Australia's interests would best be served if the government were to "modify Australian opposition as far as possible and to minimise the impact on the long term need for a close and secure relationship with Indonesia".<sup>76</sup> To gain broader support for this approach from officials within the Department of Defence who were less sanguine about the prospect of an Indonesian take-over, Woolcott encouraged Defence officials to consult with the Department of Minerals and Energy, which he noted "might well have an interest in closing the gap in the agreed sea border", – an issue he calculated "could be much more readily negotiated with Indonesia...than with Portugal or an independent Portuguese Timor".<sup>77</sup> To be sure, the petroleum prospects of the disputed region were continuously improving throughout this period. During 1975, the Woodside/Burmah consortium had followed up its success at Troubadour with the drilling of the Sunrise well, which resulted in the discovery of another gas/condensate field on the edge of the Portuguese concession. The discovery of the two fields raised industry expectation of a high likelihood of additional hydrocarbons in the surrounding region.

Indonesia began covert military operations on the Indonesian/Portuguese Timor border, during September 1975, and attacked Fretilin strongholds in the districts of Bobanaro and Ermera, during October and November 1975.<sup>78</sup> A full-scale military invasion, using naval, air and land forces, was launched in the early hours of 7 December, concentrated mainly on the capital, Dili. The Indonesian government claimed that its intervention had been taken in response to the progressively deteriorating situation in East Timor and in the interests of "helping to ensure that the democratically expressed will of the majority of the people not be overruled by the unilateral imposition of a ruthless minority".<sup>79</sup> Nine days prior to the invasion, on 28 November 1975, FRETILIN had unilaterally declared East Timor's independence – an action which was immediately rejected by Portugal, as well as the other

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<sup>75</sup> *Ibid.*, p.309

<sup>76</sup> *Ibid.*, p.268

<sup>77</sup> *Ibid.*, p.314.

<sup>78</sup> Smith, M. G., 2003. *Peacekeeping in East Timor: the path to independence*, Lynne Reiner Publishers, Boulder, p.38; *Chegal*, 2005, *op. cit.*, p.51.

<sup>79</sup> Kreiger, 1997, *op. cit.*, p.277.

Timorese factions. Following the Indonesian invasion, Portugal referred the crisis to the UN Security Council, which, on 22 December, unanimously adopted a resolution calling upon Indonesia to withdraw its forces. Indonesia's representative to the UN, Anwar Sani, reiterated that Indonesia had no claim on the territory and that the intervention had been necessary to restore conditions of peace and order, to enable the people to exercise their right to self-determination.<sup>80</sup>

The General Assembly also rejected Indonesia's justifications for military action and, on 22 December 1975, adopted Resolution 3485, which deplored the intervention and called upon Indonesia to desist from further violation of the territorial integrity of Portuguese Timor. Many in Australia had been fundamentally opposed to the Indonesian invasion, which largely accounted for why the Australian government decided to support Resolution 3485. The government of Malcolm Fraser, which had defeated Whitlam in a general election, on 13 December 1975, felt compelled to adopt an international stance that was in line with domestic public sentiment.<sup>81</sup> This condemnatory stance was not maintained, however. In 1976, Australia abstained from voting on General Assembly Resolution 31/53, rejecting the Indonesian claim of annexation and abstained again in 1977.<sup>82</sup> The attitude of many senior bureaucrats was that the "longer term inevitabilities of the situation" made it in Australia's national interest to recognise Indonesian sovereignty in East Timor to ensure that the bilateral relationship did not suffer.<sup>83</sup>

The main problem for the government, however, was in finding a way of accepting Indonesia's *fait accompli* without causing a domestic political backlash. By 1978, the issue of seabed delimitation had been identified as a politically expedient means of achieving this objective. As one senior official from the Department of Foreign Affairs described the plan: "the Government could explain its position by arguing that it was necessary to acknowledge Indonesia's claim to East Timor for the purpose of negotiating an international agreement which is very much in Australia's interest, but that the Government remains critical of the

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<sup>80</sup> *Ibid*, p.63. UN Security Council Resolution 384 (1975) of 22 December 1975.

<sup>81</sup> Salla, M. E., 1999. 'Australian Foreign Policy and East Timor', in J. Cotton (ed.), *East Timor and Australia: AIA contributions to the policy debate*, Australian Defence Studies Centre, Canberra, p.167.

<sup>82</sup> In order to legitimate the occupation of East Timor, Indonesia set up a Popular Representative Assembly, which, on 31 May 1976, unanimously adopted a petition calling for the territory's integration with Indonesia. The Indonesian Parliament approved a bill of integration on 15 July 1976. As a final step, the statute of integration was signed into law and formally promulgated by President Soeharto on 17 July 1976. UN General Assembly Resolution 31/53, of 1 December 1976, rejected the claim that a valid act of self-determination had taken place. This was repeated in Resolution 32/34, of 28 November 1977.

<sup>83</sup> Way, 2000, *op. cit.*, p.657.

means by which integration was brought about”.<sup>84</sup> In December 1978, the Minister of Foreign Affairs, Andrew Peacock, announced that Australia would give *de jure* recognition of Indonesia’s sovereignty in East Timor so that negotiations to settle the boundary in the area south of the territory could commence.<sup>85</sup> Peacock explained that Australia had to face the “realities of international law” in negotiating the seabed boundaries but that the government remained critical of the means by which East Timor’s integration into Indonesia had been brought about.<sup>86</sup>

### ***3.3 Australia/Indonesia Negotiations on the Timor Gap***

The Australian government viewed the issue of seabed delimitation as one area, in particular, in which its interests would be well served by East Timor’s integration into Indonesia. This was based on the assumption that Indonesia would be willing to accept an Australia/East Timor boundary that was no less advantageous to Australia than the 1972 boundary. Indeed, as noted earlier, this belief had actually informed government thinking in the formulation of foreign policy on Timor. In retrospect, this assumption appears to have been ill-conceived. Prior to the start of talks, Mochtar Kusumaatmadja, now foreign minister, indicated that Indonesia intended to “take the Portuguese position in seeking to have the boundary put at the line of equidistance”.<sup>87</sup> This was not a reversal of policy but actually the continuation of one that had been established under Indonesia’s 1969 Ordinance on the Continental Shelf, which stated that, “in the absence of any delimitation agreement, the boundary shall be a median line measured between the outermost Indonesian islands and the outermost points of the territory of the neighbouring State”.<sup>88</sup> Mochtar explained that the adjustments which had been made to the median line in the 1972 negotiations with Australia had been excessive, owing to Indonesia’s “hurry” in trying to conclude the agreement.<sup>89</sup>

Whilst Mochtar’s comments serve to reinforce the contention, as discussed earlier, that political reasons, unrelated to the delimitation as such, lay behind Indonesia’s willingness to make concessions in those negotiations, they also reveal that such considerations were of little

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<sup>84</sup> NAA: A9737, 92/012409, vii; in, Way, 2000, *op. cit.*, p.840.

<sup>85</sup> Krieger, 1997, *op. cit.*, p. 335.

<sup>86</sup> *Ibid.*, p.335.

<sup>87</sup> Richardson, M., ‘Tying Up Timor’s Loose Ends’, *Far Eastern economic Review*, 5 January 1979, p.45.

<sup>88</sup> Agoes, E. R., 1991. ‘Indonesia and the LOS Convention: recent developments in ocean law, policy and management’, *Marine Policy*, vol.15(2), p.125.

<sup>89</sup> Richardson, 1979, *op. cit.*

relevance within the current circumstances. Indonesia's goal of achieving international acceptance of its 'archipelagic doctrine' was no longer an issue, as by this time, both the Australian government and the Third UN Conference on the Law of the Sea had largely endorsed the concept;<sup>90</sup> and, furthermore, the major political objective of securing Australia's *de jure* recognition for Indonesia's incorporation of East Timor had already been achieved by the act of commencing negotiations itself. The Indonesian government was thus willing to take its time with the hope possibly that Australia's comparatively greater interest in gaining access to the resources of the disputed region might induce it to make certain compromises.<sup>91</sup> The Indonesian position was naturally viewed from within Canberra as a considerable setback. Yet, the government was not willing to give ground on its now well-established claim based on concepts of geomorphology and the significance of the Timor trough. Thus, during the initial rounds of discussions, it became evident to both sides that an early resolution to the dispute would not be possible.

The political impasse was to last for several years until, during negotiations held in Jakarta in November 1984, the two sides agreed to shift the focus of their talks towards the idea of a provisional joint development zone to operate in the area of overlapping maritime claims.<sup>92</sup> The idea of joint development had recently materialized in several international agreements, between Japan and Korea, in 1974, as well as Thailand and Malaysia in 1979. Growing and widespread interest in the potential advantages of the joint zone concept as a means of resolving jurisdictional disputes had also culminated in a series of international workshops, held during the early 1980s at the East-West Centre, Honolulu, Hawaii. Amongst the sponsors of the workshops had been the ASEAN Council on Petroleum as well as the UN Economic and Social Commission for Asia and the Pacific.<sup>93</sup> The Australian government was open to the idea of joint development and had recently taken a 'functional' approach in negotiations with Papua New Guinea, in respect of the countries' maritime boundary in the area of the Torres Strait. Negotiations between Australia and Papua New Guinea commenced in 1973 and had been at a deadlock for several years, until the parties' decided to abandon the

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<sup>90</sup> On a visit to Indonesia, in April 1975, Foreign Minister Peacock publicly announced that Australia would support Indonesia's archipelago principle at the Law of the Sea Conference, subject to certain safeguards of free navigation through designated navigation routes. Leifer, M., 1978. *Malacca, Singapore and Indonesia*, Sijthoff and Noordhoff, the Netherlands, p.177.

<sup>91</sup> Stepan, S., 1990. 'Credibility Gap: Australia and the Timor Gap Treaty', Australian Council for Overseas Aid, Canberra, p.3.

<sup>92</sup> King, R., Submission #43, Joint Standing Committee on Treaties, *Timor Sea Treaties*, 2002, p. 20.

<sup>93</sup> Miyoshi, M., 1988. 'The basic concept of joint development of hydrocarbon resources on the continental shelf', *International Journal of Estuarine and Coastal Law*, vol.3(1), p.3-4.

idea of a single maritime boundary in favour of “an imaginative, broadly focused approach.”<sup>94</sup> The negotiations between Australia and Indonesia in respect of the so-called ‘Timor Gap’ followed a similar pattern, although, eventually, these would take more than a decade to complete.

The decision to leave aside the question of permanent delimitation in favour of a resource sharing regime for the Timor Gap required a strong political commitment from both sides. This commitment appears only to have been forthcoming, however, once the Australian Labor Party, which regained power in federal elections held in 1983, affirmed its recognition of Indonesia’s sovereign authority in East Timor.<sup>95</sup> During its years of opposition to the Fraser government (1975-83), the ALP had regularly passed resolutions calling for a withdrawal of Indonesian forces and for a genuine act of self-determination in East Timor to take place.<sup>96</sup> On assuming office, however, Prime Minister Hawke and his senior ministers, including Foreign Minister Hayden, showed an interest in developing close ties with Indonesia; and, “were determined not to let the issue of East Timor harm bilateral relations”.<sup>97</sup> The need for resolution of the boundary dispute had also taken on greater urgency in light of recent commercial discoveries elsewhere in the region. In 1983, BHP drilled the Jabiru-1 well in the area of Ashmore Reef to the west of the Timor Gap, which produced flow rates of up to 7,300 barrels of crude oil per day – among the highest ever from a wildcat well in Australia.<sup>98</sup> The discovery resulted in world-wide oil industry interest in vacant acreage in the surrounding area and an acceleration of exploration activity. The Jabiru discovery also sparked renewed interest in the Timor Gap, wherein exploration permits had been frozen since 1978 pending settlement of the boundary negotiations. Earlier seismic surveys of this area had revealed the presence of a large, dome-shaped structure of potentially oil-bearing reservoir rock, covering approximately 7000 square kilometres (which came to be known as the ‘Kelp’ structure).<sup>99</sup> Australian oil companies as well as the governments of Western Australia and the Northern

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<sup>94</sup> Burmester, H., 1982. ‘The Torres Strait: ocean boundary by agreement’, *American Journal of International Law*, vol.76(2), p.328.

<sup>95</sup> King, 2002, *op. cit.*, p.18-9.

<sup>96</sup> Salla, M. E., 1999. ‘Australian Foreign Policy and East Timor’, in J. Cotton (ed.), *East Timor and Australia: AIAA contributions to the policy debate*, Australian Defence Studies Centre, Canberra, p.167.

<sup>97</sup> *Ibid*, p.168.

<sup>98</sup> Northern Territory Government, Department of Mines and Energy, 1983, *Annual Report*, p.27.

<sup>99</sup> Williamson, P. E. and Lavering, I. H. 1989, *Preliminary Assessment of the Hydrocarbon Prospectivity of Area A of the Zone of Cooperation*, Bureau of Minerals and Resources, Canberra.

Territory wanted a swift resolution of the dispute so that the search for oil could be resumed.<sup>100</sup>

The first and most difficult step in the negotiations proved to be that of determining the boundaries of the area which would be subject to joint development.<sup>101</sup> When this issue was settled in 1988, negotiations progressed expeditiously on the details of the regime providing for the joint exploration and exploitation of petroleum.<sup>102</sup> On 27 October 1989, officials initialled the text of the treaty, which was eventually signed on 11 December 1989.<sup>103</sup> The regime of the “Timor Gap Zone of Cooperation” was given an elaborate structure, consisting of three contiguous, jurisdictional sub-zones.<sup>104</sup> The largest of these, at approximately 35,000 square kilometers – Zone of Cooperation ‘A’ (Area A) – encompassed the entire continental shelf north of the median line between Australia and East Timor roughly up to the 1,500 metre isobath along the southern slope of the Timor Trough. Area B, the most southerly of the three zones, was closed on the south by a line 200 nautical miles from the coast of East Timor, which reflected the maximum limits of Indonesia’s EEZ and continental shelf claim. Area C, a smaller zone to the north of Zone A, was closed on the north by a line marking the bathymetric axis of the Timor Trough, therefore reflecting the maximum limit of Australia’s continental shelf claim.

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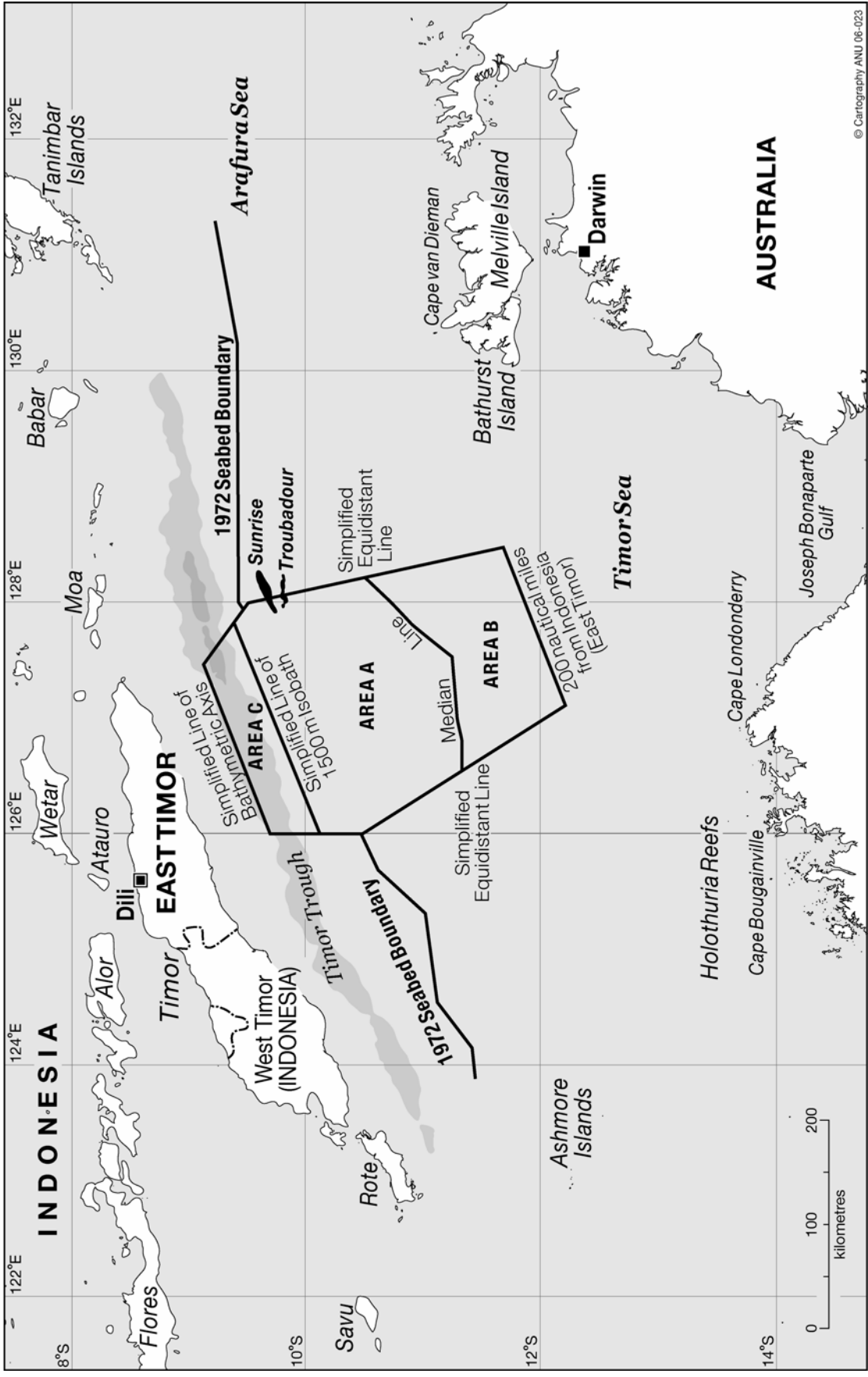
<sup>100</sup> Bergin, A., ‘The Australian-Indonesian Timor Gap Maritime Boundary Agreement’, *International Journal of Estuarine and Coastal Law*, vol.5(4):384; also, Richardson, M., ‘Timor Gap rift remains’, *Far Eastern Economic Review*, 19 April 1984, p.40.

<sup>101</sup> Burmester, H., 1990. ‘Timor Gap Treaty’, *Australian Mining and Petroleum Law Association Yearbook*, p.233.

<sup>102</sup> *Ibid.*

<sup>103</sup> *Treaty between Australia and the Republic of Indonesia on the Zone of Cooperation in an Area between the Indonesian Province of East Timor and Northern Australia [Timor Gap Treaty]*, signed 11 December 1989, entered into force 9 February 1991.

<sup>104</sup> Prescott, V., 1993. ‘Australia-Indonesia (Timor Gap)’, in J. L. Charney and L. M. Alexander (eds), *International Maritime Boundaries*, Vol.II, Martinus Nijhoff Publishers, Dordrecht, the Netherlands, p.1246.



MAP 7

Area Lines of the Australian/Indonesian Timor Gap Zone of Cooperation Treaty



The eastern and western lateral lines of the Zone of Cooperation had two segments that converged in opposite directions. South of the 1972 boundary, these lines had been drawn as simplified equidistance lines between the territorial land and sea border between East Timor and surrounding Indonesian territory. The image of the three-area Zone of Cooperation was of a coffin-shaped box, wedged in the gap created by the 1972 seabed agreement. The actual regime of joint development applied only to Area A, where government revenues from petroleum production were to be split on a 50-50 basis. Areas B and C came within the jurisdiction of Australia and Indonesia respectively, subject to a limited degree of taxation revenue sharing. According to Onorato and Valencia, the Treaty created the most “sophisticated and complex” joint development regime known at that time. They described the Treaty as one that:

...goes far beyond any previous arrangements in that it also creates a detailed and comprehensive interlocking legislative, contractual and fiscal regime. Other arrangements have selectively extended the applicable laws, suitably adapted, of one or both interested States to a joint development area, but never before have contracting States purposefully negotiated in advance a complete and area-specific regime solely for the purpose of setting the total parameters of their intended joint endeavor.<sup>105</sup>

The regime applicable to Area A embodied the principle of “sovereign neutrality”.<sup>106</sup> In addition to the equal division of resources, Indonesia and Australia were to share equal control over the governance institutions, which comprised a Joint Authority and Ministerial Council. Petroleum activities in Area A were subject to a composite taxation rate, whereby 50 percent of income was to be taxed at the Indonesian rate and 50 percent at the Australian rate. Whilst the financial headquarters of the Joint Authority was to be based in Jakarta, its technical directorate would be located in Darwin. The finely balanced nature of all of these arrangements was intended to ensure that the positions of each country as to their sovereignty claims in the area covered by the treaty were not prejudiced in any way. A formal ‘without prejudice’ clause was included within its provisions to underscore this point. Indeed, the concept of sovereign neutrality was even considered with respect to the official signing of

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<sup>105</sup> Onorato, W. T. and Valencia, M. J., 2000. ‘The new Timor Gap Treaty: legal and political implications’, *ICSID Review Foreign Investment Law*, vol.15(1), p.59, 64.

<sup>106</sup> Burmester, 1990, *op. cit.*

treaty, which was done on board a Royal Australian Air Force VIP 707 plane flying at 10,000 metres over the Timor Gap and thus on neither Indonesian nor Australian ‘territory’. Official photographs taken of Foreign Ministers Alex Alatas and Gareth Evans toasting the signature of the treaty with glasses of champagne on board the plane would be an enduring and somewhat disturbing image, which became synonymous with the treaty and symbolic also of the Indonesian and Australian governments’ collusion at the expense of the people of East Timor.

### ***3.4 Political and Commercial Impact of the Timor Gap Treaty***

The conclusion of the Timor Gap Treaty provoked a highly cynical reaction from sections of the public in Australia as well as condemnation from East Timorese, in whose opinion the treaty represented the division of stolen property between Australia and Indonesia.<sup>107</sup> It exposed and, in many respects, epitomised the contradictory nature of Australia’s rhetorical commitment to self-determination in East Timor. The *de jure* recognition of Indonesia’s incorporation of East Timor embodied within the treaty implied Australia’s non-recognition of East Timor’s status as a non-self governing territory.<sup>108</sup> Public criticism of the treaty, often expressed in ‘blood for oil’ terms, gained greater resonance when the first contracts between commercial operators and the Zone of Cooperation Joint Authority were announced shortly after the notorious massacre at the Santa Cruz cemetery in Dili, in November 1991.

The Australian government was forced to defend the legality of the treaty, both at home and abroad. In 1991, Portugal commenced a case against Australia in the International Court of Justice, claiming that, in negotiating and concluding the Timor Gap Treaty, Australia had acted unlawfully.<sup>109</sup> The Australian government argued that it was being sued as a surrogate for Indonesia – the party with whom Portugal was actually in dispute. The Court decided that there was a dispute between Australia and Portugal but considered that it could not decide the case on its merits because in so doing, “it would have to rule, as a pre-requisite, on the lawfulness of Indonesia’s conduct in the absence of that State’s consent”.<sup>110</sup> The

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<sup>107</sup> ‘Are we going to profit from the East Timor holocaust?’, an open letter to the Prime Minister, *The Australian*, reprinted in East Timor Relief Association, *Timor Gap Dossier*, p.69.

<sup>108</sup> *Portugal/Australia*, 1995, First Round of Oral Pleadings (Portugal). See Krieger, 1997, *op. cit.*, p.378.

<sup>109</sup> *Portugal/Australia*, 1995, p.93-95, para.10.

<sup>110</sup> The Court determined that:

consensual nature of international jurisdiction prohibits the ICJ from adjudicating on the legal interests of a state which has not clearly expressed its consent to jurisdiction; and, it was the fact of Indonesia's non-consent which ultimately proved decisive. Despite Portugal's 'technical' defeat, the East Timor independence movement took some solace from the Court's affirmation of East Timor's status as a non-self governing territory whose people had the right to self-determination.<sup>111</sup> A separate legal challenge was made through the courts in Australia by a group of East Timorese residents, but this also failed when, in August 1994, the High Court upheld the validity of Australia's domestic legislation that gave effect to the Timor Gap Treaty.

The treaty represented the most explicit recognition of Indonesia's annexation of East Timor by any third state and it was apparent that the foreign policy benefits of this recognition were not lost on Indonesia. East Timor had been described as a province of Indonesia in the very title of the treaty and this had more than once been repeated in the text. Foreign Minister Alatas believed that the treaty would help Indonesia in its ongoing diplomatic efforts to "have the question of East Timor settled at the UN".<sup>112</sup> The UN Special Committee on Decolonization continued to treat the former Portuguese colony as a non-self governing territory and, in 1983, the UN Secretary General had been requested by the General Assembly to initiate consultations with Indonesia and Portugal to find a comprehensive settlement of the conflict. The Australian government also attached wider political value to the treaty. For in as much as it symbolized Australia's "total betrayal of the Timorese people", it provided, by the

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...the effects of the judgment requested by Portugal would amount to a determination that Indonesia's entry into and continued presence in East Timor are unlawful and that, as a consequence, it does not have the treaty-making power in matters relating to the continental shelf resources of East Timor. Indonesia's rights and obligations would thus constitute the very subject matter of such a judgment made in the absence of a State's consent. Such a judgment would run counter to the well-established principle of international law embodied in the Court's Statute, namely that the Court can only exercise jurisdiction over a State with its consent.

(*Portugal/Australia*, 1995, p.105, para.34)

Drew has argued that East Timor case exposed the prejudicial nature of the international legal system, whereby "the rights of an absent *state* (Indonesia) were upheld while those of the absent *people* (East Timorese) remained *per force* beyond the jurisdictional reach of the Court". Under UN law, the people of East Timor had a potential entitlement to the whole of the area covered by the Timor Gap Treaty but, when confronted with a demand to protect that entitlement, to say nothing of the opportunity to promote the values of justice and morality, the International Court of Justice ultimately decided that a greater respect was owed to political power and the institution of state sovereignty. See Drew, C., 2001. 'The East Timor story: international law on trial', *European Journal of International Law*, vol.12(4), p.668.

<sup>111</sup> *Ibid.*, p.106, para.37.

<sup>112</sup> 'Timor Gap deal will have political impact', *Jakarta Post*, 6 December 1989.

same token, a powerful demonstration of Australia's commitment to the goal of maintaining good relations with Indonesia.<sup>113</sup>

Foreign Minister Evans described the Timor Gap Treaty as “the most significant agreement concluded in the forty year history of Australia's relations with Indonesia”;<sup>114</sup> and one that “would lead to new areas of cooperation between the two countries”. The Treaty was to be a fundamental cornerstone of the bilateral relationship and fitted neatly into Australia's foreign policy of “comprehensive engagement”, described by Evans as aimed at “building a more diverse and substantive array of linkages with the countries of Southeast Asia, so that they have an important national interest in the maintenance of a positive relationship with Australia”.<sup>115</sup> Others viewed Australia's Timor policy simply as the appeasement of, or acquiescence in, the interests of a violent, totalitarian regime.<sup>116</sup> Following its entry into force, on 9 February 1991, Australia and Indonesia instituted arrangements for joint surveillance and security operations in the zone. This, in turn, acted as a catalyst for more extensive defence cooperation, including occasional joint exercises between Australian and Indonesian surveillance units, as well as the establishment of routine communications links between ships, aircraft and shore authorities.<sup>117</sup>

Invitations to tender for exploration acreage in the joint development zone were sent to prospective bidders worldwide, on 24 June 1991. In December that year, production sharing contracts for eleven of the fourteen areas were approved. Contracts were awarded to a total of nine different consortia, made up of both local and international companies and the total level of risk investment for the initial six-year programme of exploration was US\$362 million.<sup>118</sup> The highly publicized proceedings that had been instituted by Portugal at the ICJ and the continuing public controversy overhanging the treaty appeared to provide these companies with little cause for concern.<sup>119</sup> However, the first set of drilling results was disappointing.

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<sup>113</sup> ‘Oil treaty to bring “era of cooperation”’, *Canberra Times*, 11 February 1991.

<sup>114</sup> Evans, G. and Grant, B., 1995. *Australia's Foreign Relations: in the world of the 1990s*, Melbourne University Press, Melbourne.

<sup>115</sup> *Ibid.*, p.195.

<sup>116</sup> Roff, S. R., 1992. *Timor's Anschluss: Indonesia and Australia Policy in East Timor 1974-1976*, Edwin Mellen Press, New York, p.x-xii.

<sup>117</sup> Ball, D., 1995. ‘Indonesia and Australia: strange neighbours or partners in regional resilience’, in Soesastro, H. and McDonald, T. (eds), *Indonesia-Australia Relations: diverse cultures, converging interests*, Centre for Strategic and International Studies, Jakarta.

<sup>118</sup> Kyranis, N. and Aryawijaja, R., 1993. ‘The Implementation and Progress of the Exploration Regime in the Timor Gap Zone of Cooperation – Area ‘A’’, *Proceedings of the Indonesian Petroleum Association*, Twenty Second Annual Convention.

<sup>119</sup> The signing ceremony for the first production sharing contracts actually had to be carried out at a secret location in Jakarta to avoid any possibility of East Timor campaigners staging a public protest; See ‘Timor oil deal signed’, *Australian Financial Review*, 12 December 1991.

Three wells drilled by the US firm, Marathon, encountered oil that had seeped through the faulting and had dissipated. Yet, a sequence of oil and gas discoveries during 1994 and 1995 soon confirmed industry expectations of the hydrocarbon-bearing potential of the Timor Gap region. These included the Elang and Kakatua oil fields drilled by BHP, in permit 91-12, on the western flank of the joint development zone and the Laminaria oil discovery drilled by Woodside, just outside the western perimeter of the zone in waters administered by the Northern Territory government. In February 1995, Phillips Petroleum announced the discovery of a gas-condensate field, Bayu, within Area A. Later that year, BHP drilled the Undan well, ten kilometers north of Bayu and observed that the two separate discoveries formed one huge field straddling the 91-12 and 91-13 Production Sharing Areas of the joint development zone. The practice was to give the wells Indonesian names, particularly those of birds: Elang is the Indonesian for eagle, Kakatua, cockatoo; Bayu means breeze, or wind and Undan, pelican.

The region's proven reserves of petroleum continued to increase over the course of the 1990s. Between September 1997 and September 1998, a Woodside/Shell joint venture drilled three wells on the eastern flank of the joint development zone, which confirmed the massive Sunrise and Troubadour fields' lateral extension across the eastern perimeter of the zone. These discoveries, in addition to a number of other successful drilling operations elsewhere in the greater Timor Sea area generated substantial commercial interest and a sense of excitement in northern Australia over the potential for economic development based on the offshore petroleum industry. The Elang and Kakatua fields commenced production in 1998, quickly reaching peak rates of roughly 40,000 barrels of crude oil per day. During the same year, the Northern Territory government reported that oil companies holding Timor Sea permits had committed to drilling around 165 wells over the next six year interval, with associated expenditures expected to exceed AUD\$1.4 billion.<sup>120</sup> In terms of its impact on the commercial development of the region, the Timor Gap Treaty was a proven success.

Over the same period of time, the Australian and Indonesian governments continued negotiations on the settlement of a number of outstanding maritime boundary issues. Eight rounds of formal negotiations, held between 1993 and 1996, culminated in the signing of the Maritime Delimitation Treaty, signed in Perth, March 1997. The treaty established an EEZ boundary between Australia and Indonesia in the Arafura and Timor Seas, as well as in the

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<sup>120</sup> Department of Mines and Energy Annual Report, Northern Territory Government, 1997/8, p.10.

Indian Ocean, between Australia's Christmas Island territory and Java.<sup>121</sup> The treaty also extended the 1972 seabed boundary for some distance further to the west of Timor. The EEZ boundary replaced the Provisional Fisheries Surveillance and Enforcement Line, which had been agreed by the two countries in 1981. As this was a median line, lying well to the south of the pre-existing seabed boundaries, it reflected Australia's recognition that, "since 1972, international law has moved to encompass a distance-based criterion".<sup>122</sup>

The EEZ boundary was to apply only to the water column, which meant that the treaty created a complex situation of overlapping jurisdiction. In the area of overlap, Indonesia had rights over the water column, whilst Australia would retain continental shelf sovereign rights.<sup>123</sup> As long as the political foundation for jurisdiction in the Timor Sea remained one of bilateral control, Australia and Indonesia, it seems, were prepared to accept any of the political difficulties that operating within such a complex legal and jurisdictional environment was likely to bring. Yet, towards the end of the decade, the chances of the Timor Sea remaining a province of exclusively Australian and Indonesian control looked increasingly unlikely. When the thirty-year rule of Soeharto came to an abrupt end in May 1998, an opening was created for much broader political change in Indonesia as well as a revision of the government's policy on East Timor. Within months of Soeharto's departure, the prospect of an independent East Timor would become a reality and the continuing viability of the offshore legal arrangements – painstakingly negotiated by Australia and Indonesia over a twenty-five year period – would instantly be thrown into doubt.

## CONCLUSION

Since its original formulation during the mid-1960s, the policy of the Australian government with regard to issues of continental shelf jurisdiction has been driven by a very simple idea: namely, that the further from the shore Australia's international boundaries are, the better. In respect of questions of seabed jurisdiction in the Timor Sea, this objective found its clearest expression within the "McMahon Statement", of 30 October 1970, which claimed, on grounds of morphology alone, that the Timor trough formed a natural division between

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<sup>121</sup> *Treaty between the Government of Australia and the Government of the Republic of Indonesia establishing an Exclusive Economic Zone Boundary and Certain Seabed Boundaries*, signed 14 March 1997 (not in force).

<sup>122</sup> Joint Standing Committee on Treaties, *Australia-Indonesia Maritime Delimitation Treaty*, 12<sup>th</sup> Report, November 1997, p.9.

<sup>123</sup> Herriman, M. and Tsamenyi, M., 1998. 'The 1997 Australia-Indonesia Maritime Boundary Treaty: a secure legal regime for offshore resource development?', *Ocean Development and International Law*, vol.29, p.362.

two separate continental shelves. The political implications of the natural boundary concept in this region are best summarised by the fact that the trough is about 200 miles from Australia but just 25 to 50 miles off the coast of Timor. The rejection of that concept by the governments of both Indonesia and Portugal provided the context within which a dispute over seabed jurisdiction in the Timor Sea arose. This chapter has examined the diplomatic efforts to resolve that dispute and the outcomes that were reached. Indonesia and Australia were able to reach an acceptable compromise between their competing claims with relative ease. However, the dispute between Portugal and Australia remained at a complete deadlock for several years, until a *coup d'état* in Lisbon precipitated a period of turbulent political change that would lead inexorably to the end of Portuguese rule in Timor. Subsequently, and in the process of accommodating East Timor's illegal annexation, Australia and Indonesia negotiated a bilateral regime of joint petroleum development to apply in the area of the Timor Gap.

The events described in this chapter not only cover critical factual elements of the situation confronted by East Timor at the time of its emergence but also provide valuable insights into the process of bargaining for control of the Timor Sea. The close interaction between legal norms and political considerations in the negotiations between Australia and Indonesia is, for the purposes of this research, the most important conclusion to be drawn. The 1972 and 1989 agreements each embody distinctive aspects of international law that existed when the negotiations which led to those agreements took place. To the extent that the boundary lines of the 'Zone of Cooperation' are, in part, derived from legal principles, which had not yet fully crystallized in law at the time of the 1972 treaty, the law's influence can clearly be discerned. Yet, in each case, political conditions and considerations have had a decisive influence upon the outcomes reached. The broader context of Australia and Indonesia's bilateral relations emerges as a pivotal factor; and, it is the dynamic interaction between legal norms and the shifting pattern of that relationship which accounts for the variance in bargaining outcomes reached.

## **4. EAST TIMOR'S EMERGENCE AND THE RE-AWAKENING OF THE DISPUTE**

The thirty years of history covered in the previous chapter provide the backdrop to the situation at the time of the vote on self-determination in East Timor. The aim of this chapter is to investigate the parties' oil diplomacy in the initial phase of the post-referendum period. The analysis covers the interactions of the Australian and Indonesian governments, the United Nations, the National Council of Timorese Resistance, as well as the major oil companies, but particularly the US firm, Phillips Petroleum, over a period of about two years, from January 1999 to October 2000. This is the time from when the Indonesian government announced that a vote on self-determination would be held to determine East Timor's future until the point when negotiations formally commenced between Australia and the UN transitional administration on a new regime of offshore petroleum development. It also marks a turning point in the commercial evolution of the Timor Sea: a period in which a number of billion-dollar oil and gas projects were coming to fruition. The emergence of East Timor created a new situation, one that was evolving and uncertain. In this chapter, I examine how these parties approached the Timor Gap issue in the lead up to, and immediately after, the August 30 referendum in East Timor; their key interests and concerns; the way in which their interests came into conflict with one another; and, the parties' attempts to protect and promote their own interests.

Shortly after the Indonesia-to-UNTAET transition of power in East Timor, the UN/East Timor side staked a claim to a mid-point maritime boundary, thus assuming the position which had previously been adopted by Portugal some thirty years earlier. This implied a claim of exclusive East Timorese sovereign rights to the entirety of the resources within Area A of the Zone of Cooperation. At this point in time, the area was known to contain hydrocarbon reserves of more than 400 million barrels of condensate and liquid petroleum gas (LPG) and three trillion cubic feet of gas and was the site of a proposed multi-billion dollar development of the "world class" Bayu-Undan field, operated by Phillips.<sup>1</sup> The UN/East Timor claim was a threat to the Australian strategy "aimed at ensuring the smooth

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<sup>1</sup> Department of Industry, Science and Resources, 1999. Submission #63, Senate Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*, p.8.



transition” of the Timor Gap Treaty.<sup>2</sup> In this chapter, I examine the way in which UNTAET’s Director of Political Affairs, Peter Galbraith, used influence to induce the Australian government to the negotiating table as well as the strategy adopted by Phillips to protect its interests in the Bayu-Undan development. The analysis draws on both primary and secondary sources. Primary sources include some highly confidential UN records of meetings between UN officials and Australian government officials, during November 1999, and the two rounds of “pre-negotiations” between UNTAET and Australia, in March and June 2000. The records of the pre-negotiations were contained in two cables sent by Sergio Vieira de Mello to Under Secretary General for Peacekeeping, Bernard Miyet, in New York, on 1 April and 19 June 2000, respectively. Information was also acquired through research conversations with representatives of all the key parties.

#### ***4.1 The End of Indonesia’s Occupation of East Timor***

The resignation of President Soeharto, on 21 May 1998, was a watershed in Indonesian politics. Soeharto had held power in Indonesia for over three decades by way of an autocratic and repressive system of rule; and his departure, in the midst of the country’s worst ever financial crisis, brought opportunities for broad political and social change. According to Ricklefs, when B. J. (Bacharuddin Jusuf) Habibie assumed the Presidency, there were five main issues before him: the political reform process; the role of the military in Indonesian society; the future of dissident territories which sought to break away from the nation; the future of Soeharto, his family, their wealth and their cronies; and, the future of the economy and people’s welfare.<sup>3</sup> With respect to the question of East Timor, Soeharto’s downfall catalysed ongoing diplomatic initiatives at the United Nations focused on achieving a settlement of the conflict. In June 1998, Foreign Minister Alatas travelled to New York with a proposal, endorsed by Habibie, for achieving a comprehensive “end-solution”.<sup>4</sup> The government offered to grant a special status to East Timor with wide-ranging autonomy, the

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<sup>2</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 11 November 1999, p.871.

<sup>3</sup> Ricklefs, M. C., 2001. *A History of Modern Indonesia*, 3<sup>rd</sup> Ed., Palgrave, Hampshire, United Kingdom, p.408.

<sup>4</sup> Marker, J., 2003. *East Timor: a memoir of the negotiations for independence*, McFarland and Company, Jefferson, North Carolina, p.87.

scope of which, it was proposed, could be negotiated within the framework of the ongoing tripartite talks between Indonesia, Portugal and the UN.<sup>5</sup>

By the end of 1998, the parties had negotiated a draft document specifying the constitutive elements of the autonomy plan but they remained in complete deadlock on the question of East Timor's status. For Indonesia, the granting of autonomy was to be conditional on Portugal's recognition of Indonesian sovereignty in East Timor. In contrast, Portugal saw autonomy as being a necessary step in providing the conditions under which self-determination could ultimately be exercised. This was the position also shared by the National Council of Timorese Resistance (CNRT), which had formed in April 1998 to bring together nearly all of the East Timorese resistance factions under a common political and military umbrella.<sup>6</sup> During the first few weeks of 1999, however, Indonesian policy underwent a radical rethinking. On 27 January, the Indonesian government announced that it would offer the special autonomy proposal to East Timor but, if this was not accepted, the government would "suggest to the new membership of the Peoples Consultative Assembly, formed as a result of the next elections, to release East Timor".<sup>7</sup>

According to Jamsheed Marker, who was the UN Secretary General's representative in the tripartite talks, the Indonesian initiative "seems to have emanated almost entirely from Habibie".<sup>8</sup> However, many analysts have acknowledged that an important precursor to this announcement was a letter Habibie received from Australian Prime Minister, John Howard, in December 1998.<sup>9</sup> In the letter, Howard suggested that a lasting and peaceful resolution of the conflict in East Timor could best be achieved by an act of self-determination by the East Timorese at some time in the future, following a substantial period of autonomy. Whilst Howard also affirmed that Australia's interests would best be served by East Timor remaining part of Indonesia, the suggestion of holding a referendum on self-determination reflected a major shift in government policy.<sup>10</sup> Habibie reacted negatively to this idea, as it implied that Indonesia would still continue to bear a financial burden in East Timor during the transitional period but without any guarantee of achieving permanent sovereignty over the territory.

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<sup>5</sup> *Ibid.*, p.86-7.

<sup>6</sup> Ball, D., 2002. 'The Defence of East Timor: A recipe for disaster?', paper presented to the Faculty of Asian Studies, Australian National University, Canberra.

<sup>7</sup> Marker, 2003, *op. cit.*, p.121.

<sup>8</sup> *Ibid.*, p.129.

<sup>9</sup> *Ibid.*; Cotton, J., 2004. *East Timor, Australia and Regional Order: intervention and its aftermath in Southeast Asia*, RoutledgeCurzon, London, p.114; Fernandes, C. 2004. *Reluctant Saviour: Australia, Indonesia and the independence of East Timor*, Scribe Publications, Melbourne, p.38-45.

<sup>10</sup> Department of Foreign Affairs and Trade, 1999. Submission #52, Senate Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*.

Subsequent negotiations between Indonesia, Portugal and the UN took place on the understanding that there would not be a long transition period before the question of East Timor's final status was decided. Therefore, the choice offered to the East Timorese would be immediate and final.

On 5 May 1999, Portugal and Indonesia signed a set of agreements on the implementation of the ballot. The Main Agreement stipulated that a referendum would be held in which the East Timorese people would be given the choice between either accepting special autonomy within Indonesia or rejecting it, leading to full independence.<sup>11</sup> Under the special autonomy proposal, the Indonesian government would retain control over foreign policy and defence, monetary and fiscal policies, as well as "strategic or vital" natural resources.<sup>12</sup> However, responsibility for legislation in all other areas would rest with the East Timorese, "who would set up a Regional Council, elect the Governor, and nominate members of the Advisory Board of the Government of the Special Autonomous Region of East Timor".<sup>13</sup> The ballot was originally scheduled to take place on Sunday, 8 August 1999 but this later had to be delayed until 30 August on account of a marked increase in militia activities which disrupted the UN voter registration process.<sup>14</sup>

These political developments carried enormous implications for the future of the Timor Gap Treaty. In the event of the autonomy proposal being rejected, Indonesia would automatically lose the ability to exercise jurisdiction within East Timor's maritime zones and would therefore have no capacity to participate in the joint development regime. Indonesia's Foreign Minister, Alex Alatas, confirmed that if the East Timorese voted for independence the treaty would need to be renegotiated.<sup>15</sup> However, following meetings between Australia's Minister for Foreign Affairs, Alexander Downer, and East Timorese leaders Jose Alexandre ('Xanana') Gusmão and José Ramos Horta, during February 1999, the initial indications were that the Timor Gap Treaty would be accepted by an independent East Timor. Gusmão had been appointed as the "Lider Maximo" (supreme leader) and President of CNRT, with Ramos Horta as Vice President, in 1998. Although captured and imprisoned by the Indonesian military, in 1992, Gusmão had been transferred to house arrest on 10 February 1999. After meeting with Gusmão on 26 February, Downer remarked: "Mr Gusmão told me they would

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<sup>11</sup> UN doc. A/53/951, S/1999/513, 5 May 1999.

<sup>12</sup> *Ibid.*

<sup>13</sup> Marker, 2003, *op. cit.*, p.122.

<sup>14</sup> *Ibid.*, p.167.

<sup>15</sup> 'Independent Timor can renegotiate Gap deal' *Indonesian Observer*, 18 February 1999.

honour the Timor Gap Treaty and that they were happy to share on an equitable basis with Australia resources that were between East Timor and Australia".<sup>16</sup>

The CNRT knew that if they attained independence Timor Sea revenues would be incredibly important to the future of the territory. The Timor Gap Treaty arrangements were expected to yield over US\$4 billion in government revenues over the next twenty-five years.<sup>17</sup> To place this figure in context, East Timor's allocation from Indonesia's national budget, in 1999/2000, was estimated to be US\$122 million.<sup>18</sup> As a large proportion of this was needed for the heavy military presence in East Timor, which would not be required following independence, the implication was that Timor Gap revenues would be adequate to fund the public administration of the territory over the medium term. The CNRT wanted to instill confidence within both the Australian government and commercial operators that an independent East Timor would maintain a stable investment regime for the Timor Sea. On 22 July 1998, the organisation released a communiqué in support of the "rights of the existing Timor Gap contractors and those of the Australian Government to jointly develop East Timor's offshore oil reserves in cooperation with the people of East Timor".<sup>19</sup> The statement had an overtly strategic purpose. It was not only intended to assuage investor concerns over the impact of political change but also to deny pro-Jakarta elements within the Australian establishment of one of the possible reasons for arguing that East Timor's independence would be damaging to Australia's national interests.<sup>20</sup> José Ramos Horta, one of East Timor's most internationally recognized independence campaigners, publicly confirmed his support for the Timor Gap Treaty in a speech to the National Press Club, in Canberra, on 13 July 1999.<sup>21</sup>

Political interest and concern for the treaty was underscored by the rapid progress made by the Bayu-Undan joint venture in finalizing a development project. The Bayu-Undan field fell wholly within the boundaries of Area A of the Zone of Cooperation and the project was therefore exposed to risks associated with any impact to the Treaty regime caused by a possible change in political circumstances. For several years, the two largest equity holders,

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<sup>16</sup> 'Gusmao assures Gap treaty is safe', *Australian Financial Review*, 27 February 1999.

<sup>17</sup> 'New state will want a slice of gap', *Sydney Morning Herald*, 27 February 1999.

<sup>18</sup> Department of Foreign Affairs and Trade, 1999, *op. cit.*

<sup>19</sup> CNRT statement on Timor Gap oil, 21 July 1998, <http://www.etan.org/et/1998/july/july14-21/21CNRoil.htm>  
<Accessed 10 October 2005>

<sup>20</sup> McKee, G. A., 2000. 'The new Timor Gap: will Australia now break with the past?', in L. Taudevin and J. Lee (eds), *East Timor: making amends?: analysing Australia's role in reconstructing East Timor*, Australia East Timor Association, Otford Press, Sydney.

<sup>21</sup> 'East Timor leader backs Timor Gap pact, eyes econ future', *DowJones Newswires*, 13 July 1999.

Phillips and BHP had been unable to reach agreement on fundamental aspects of project design, which had been one of the principal factors hindering early field development.<sup>22</sup> A key turning point came in April 1999, when BHP decided to sell a number of Timor Sea assets, including the company's stake in the Bayu-Undan, Elang/Kakatua and Greater Sunrise fields to Phillips. Once the latter had taken full control over Bayu-Undan, project planning moved forward expeditiously. A unitization agreement between joint venture partners was executed in July 1999, which nominated Phillips as the project operator. Preliminary engineering for the initial phase of development had already been completed in late 1998 and a second, detailed engineering contract was awarded in July 1999.<sup>23</sup> Although BHP indicated that the reasons for the sale were purely economic, apprehensions over the "escalating political uncertainty" in the region seem also to have been an important factor.<sup>24</sup> In August 1998, a secret meeting between BHP's senior representative in Jakarta, Peter Cockroft, and Xanana Gusmão had been leaked to the press.<sup>25</sup> Gusmão was incarcerated at the high security Cipinang Prison at the time, yet such was the level of political uncertainty that Cockroft wanted to know what would happen to the Timor Gap Treaty under an independent East Timor.<sup>26</sup>

#### ***4.2 Post-Referendum Stakeholder Interactions***

The result of the referendum in East Timor was announced on 3 September 1999. The special autonomy proposal was rejected by a significant margin of voters: East Timor would become an independent country.<sup>27</sup> Under the terms of the 5 May Agreement, it had been agreed that if the result of the ballot was in favour of independence, power in East Timor would be transferred from Indonesia to the United Nations for an interim period until there was sufficient capacity for self-government. However, immediately after the results had been announced, pro-integration militia, in concert with Indonesian forces, embarked upon a

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<sup>22</sup> 'Petroleum rivalries flare up over Timor Gap gas field', *Australian Financial Review*, 29 November 1996.

<sup>23</sup> 'Tiga stays top of Bayu food chain', *Upstream*, 16 July 1999; 'Australia – Timor Sea gas fields project – opp'ties', *International Market Insight Trade Inquiries*, 30 July 1999.

<sup>24</sup> 'BHP sells interest in Timor Sea oil and gas', *The Age*, 14 April 1999.

<sup>25</sup> 'BHP in Timor', *Sydney Morning Herald*, 7 September 1998.

<sup>26</sup> Sword Gusmao, K., 2003. *A Woman of Independence: a story of love and the birth of a new nation*, Macmillan, Sydney, p.201.

<sup>27</sup> The results of the ballot indicated that 94,388, or 21.5 per cent, of East Timorese had voted in favour of the special autonomy proposal and 344,580, or 78.5 per cent, had voted against it. Press Release, U.N. doc. SC/6721, 3 September 1999.

scorched earth campaign to destroy as much of the territory's physical infrastructure as possible. The militia targeted and executed CNRT leaders and their families as well as people seeking refuge in churches, including clergy and nuns, in what the UN described as "a deliberate, vicious and systematic campaign of gross violations of human rights".<sup>28</sup> At least 900 people were killed and many more attacked as the catastrophe unfolded.<sup>29</sup> Much of Dili's infrastructure and buildings were destroyed and 750,000 people out of a total population of 880,000 were either displaced from their homes or became refugees in Indonesian West Timor.<sup>30</sup>

Images of the violence and bloodletting shocked the world and massive international pressure was brought to bear upon the Indonesian government to authorize a military intervention to restore peace and security.<sup>31</sup> A multinational UN peacekeeping force, named INTERFET, which was placed under Australian command, began deployment in the territory on 20 September. Dili was the first area to be pacified, with other regional centres of population being secured in a step-by-step process. The Oecussi enclave in the western part of the island was the final district to be occupied, on 22 October 1999.<sup>32</sup> A Brazilian UN official, Sergio Vieira de Mello, was appointed by the UN Secretary General to be the Transitional Administrator, with plenary powers during the period of transitional administration. De Mello arrived in Dili on 16 November. Contact was immediately established with Xanana Gusmão, as well as other prominent East Timorese personalities, to coordinate their involvement in the subsequent administration of the territory.<sup>33</sup> A National Consultative Council (NCC) was established composed of fifteen members; seven from the CNRT; four from UNTAET; one

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<sup>28</sup> Security Council Resolution 1264 of 15 September 1999; also, UN High Commission for Human Rights, Report of the High Commissioner, E/CN.4/2000/44, 24 March 2000.

<sup>29</sup> *Chega!*, Final Report of the Commission for Truth, Reception and Reconciliation in East Timor, October 2005, Part 3, p.145; also, Report of the International Commission of Inquiry on East Timor, UN doc., A/54/726; S/2000/59, 31 January 2000.

<sup>30</sup> Jean Christian Cady, Assistant to the Special Representative of the Secretary General of the United Nations Transitional Administration in East Timor, 'Building the new state of East Timor', paper presented at the Centre for International and Public Law, Faculty of Law, Australian National University (18 May 2000), quoted in Charlesworth, H., 2003. 'The Constitution of East Timor, May 20, 2002', *International Journal of Constitutional Law*, vol.1(2), p.326.

<sup>31</sup> As part of the 5 May Agreement, it was agreed that Indonesia would have full responsibility for ensuring security in East Timor. The Australian-led military intervention in the violent aftermath of the referendum became possible once the Security Council had mandated the operation and it had received the consent of Indonesia. See Cotton, J., 2004. *East Timor and Regional Order: intervention and its aftermath in Southeast Asia*, RoutledgeCurzon, London, p.95; also, Wheeler, N. J. and Dunne, T., 2001. 'East Timor and the new humanitarian interventionism', *International Affairs*, vol.77(4), p.807.

<sup>32</sup> Smith, M. G., 2003. *Peacekeeping in East Timor: the path to independence*, Lynne Reiner Publishers, Boulder, Colorado.

<sup>33</sup> UN doc. S/2000/53, 'Report of the Secretary General on the United Nations Transitional Administration in East Timor', 26 January 2000.

from the Catholic Church; and, three from political groups outside CNRT, which had supported integration with Indonesia.

Once the results of the referendum had been made known and it was apparent that Indonesia would no longer play a role in East Timor, the question automatically arose concerning the future of the Timor Gap Treaty. The termination of Indonesia's participation in the treaty was not an issue. Rather, the problem concerned that of maintaining a functioning legal framework for Timor Sea petroleum development when political events had rendered the Treaty null and void.

Australia's response was to develop and then implement a "strategy aimed at ensuring the smooth transition of the treaty".<sup>34</sup> The government stated that "it regarded a prompt and smooth transition as very important for investor confidence, for continuing petroleum exploration and development in the zone of cooperation".<sup>35</sup> During October and November, several meetings were held between Australian and UN officials in both New York and Canberra to discuss transitional arrangements. Representing East Timor during these initial meetings was Mari Alkatiri. Alkatiri was a founding member of FRETILIN and had been an active player in the independence movement, despite having spent much of the period of Indonesian occupation in exile in another of Portugal's ex-colonies, Mozambique. In August 1999, he had been appointed by Gusmão to take charge of Timor Sea issues on behalf of the CNRT.

The approach adopted by both Alkatiri and Ramos Horta appeared to inspire great confidence in the Australian government. On 12 October 1999, Foreign Minister Downer told parliament, in response to a question on the Timor Gap Treaty, that "we are happy with the way discussions are proceeding...all the signs are very positive".<sup>36</sup> On 11 September, a senior official from the Department of Foreign Affairs and Trade stated that, "as matters stand, we can be confident that the East Timorese would like the treaty to continue and to bind them once they become a state and that, in the interim before they are a state, they would like the United Nations to exercise their role in waiting until they achieve independence".<sup>37</sup> The United Nations shared a similar understanding of the situation. On 29 November, the UN reported that:

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<sup>34</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 11 November 1999, p.871.

<sup>35</sup> *Ibid*, 9 December 1999, p.1009.

<sup>36</sup> House of Representatives, Official Hansard, 12 October 1999.

<sup>37</sup> Senate Foreign Affairs, Defence and Trade References Committee, *Committee Hansard*, 11 November 1999, p.884.

Senior representatives of the National Council for Timorese Resistance (CNRT) have expressed their desire for the Timor Gap Treaty to remain in force. At meetings held on 7 and 27 October between Australian and East Timorese officials, Mr Mari Alkatiri...confirmed that East Timorese leaders wished to take the steps necessary for the continued operation of the Timor Gap Treaty at the earliest possible time. He was of the view that an appropriately worded United Nations/Australia agreement would be an acceptable mechanism. Mr Alkatiri also specified that the East Timorese may wish to revisit unspecified aspects of the Timor Gap Treaty at a later time. We acknowledged that this would, in any case, fall within the legitimate rights of a successor state. Following a meeting between the Australian Prime Minister, John Howard, and Xanana Gusmão in Canberra earlier this month, Xanana publicly confirmed that the East Timorese would “respect the terms of the treaty”. José Ramos Horta also reconfirmed publicly on 19 October that the East Timorese were eager to see the Timor Gap Treaty remain in force...We therefore expect that formal confirmation of the will of the East Timorese representatives for the Timor Gap Treaty to remain in force, in the form of a letter from the CNRT to the United Nations, will be conveyed to the United Nations in the very near future.<sup>38</sup>

For Phillips, the overriding concern was simply to keep the momentum of the Bayu-Undan project going. The company considered that it could not simply wait for political events to take their course but had to be actively involved in shaping outcomes so that the company’s commercial interests would not be harmed and that development would proceed unaffected. Phillips acquisition of BHP’s assets, at a cost reputed to be in the order of AUD\$300 million, was a major strategic commitment to the Timor Sea.<sup>39</sup> On 8 September, the company’s Darwin area manager, Jim Godlove, made a statement to Australia’s Foreign Affairs, Defence and Trade References Committee outlining the company’s position in view of the “material change” in East Timor’s political status following the referendum. Godlove

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<sup>38</sup> UN Aide Memoire, ‘Timor Gap Treaty’, 29 November 1999.

<sup>39</sup> ‘BHP sells interest in Timor Sea oil and gas’, *The Age*, 14 April 1999.



stated that there were three outcomes that Australia had “an obligation to pursue” on the company’s behalf:

First, to preserve the near-term confidence of investors such as Phillips within the Zone of Cooperation, clear and unequivocal statements in support of the current treaty need to be issued immediately by any council created to represent the East Timorese and by any interim administrative authority established to assist during the transition. To sustain development over the long term, however, there must be a binding devolution agreement among the parties in which East Timor agrees to adhere to the current terms of the treaty. Second, the present commercial and fiscal terms of the treaty must be maintained. These include provisions relating to production sharing and cost recovery of capital and operating expenses. Furthermore, any tax regime established in East Timor should be no more onerous than the Indonesian regime being replaced. These provisions establish the basis for petroleum development in the Zone of Cooperation and any adverse change in these provisions could have a profound effect on our project economics. Third, the treaty establishes a Ministerial Council and a Joint Authority to administer activities within Area A. It is critical that both organisations remain viable during any transition process to ensure necessary oversight and approvals are provided to ongoing projects such as ours. East Timor representatives should be identified without delay to observe and to contribute, where appropriate, to the deliberations of these groups. Likewise, it is important that uncontested administrative decisions that have been issued or agreed among the parties remain effective. Any disruption of this process or repeal of these important decisions could again undermine investments made in Area A.<sup>40</sup>

These demands in effect amounted to state succession - not only of treaty arrangements but of the company’s petroleum sharing contracts (PSC) also. The Australian government was not being asked; it was being instructed. At the end of October 1999, Godlove arranged to meet with Gusmão, Alkatiri and Ramos Horta, with the aim of obtaining

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<sup>40</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 8 September 1999, p.418.

some form of raw commitment from these leaders that they would honour the existing terms of the PSCs which covered the development of the Bayu-Undan field. The meeting was arranged informally through Juan Federer of the East Timor Relief Association. At this time, Gusmão was still being kept at a secure location by the Australian army in the vicinity of Darwin to ensure his protection until East Timor had been pacified. Despite not having any detailed knowledge of the precise terms of the Timor Gap Treaty PSCs, the three leaders were willing to accommodate Godlove's request. A public statement issued by the CNRT subsequent to the meeting, on 20 October 1999, stipulated:

With regard to the current Timor Gap Treaty and the so-called Zone of Cooperation, CNRT wishes to assure all ZOC contractors of our support for continued development of the petroleum resources within this area. Working with the United Nations, Australia and Portugal it is our intent to negotiate appropriate transition arrangements and consequent changes in the current Treaty that maintain its legal authority over petroleum resource development. Without limiting our rights and interests in the Zone of Cooperation, we wish to ensure all ZOC contractors operating under current Production Sharing Contracts that their legal rights will continue through the full term of those contracts and that the fiscal policies applicable to production sharing and taxation will be no more onerous than current policies as they relate to the contractors share. In exchange for these assurances, we would expect that petroleum exploration and development within the Zone of Cooperation would continue in both the near and long term.<sup>41</sup>

Although signed by the three FRETILIN leaders, Gusmão, Alkatiri and Ramos Horta, the similarities between this and Phillips' 8 September statement (quoted above), particularly with respect to the use of the "no more onerous" term, suggest that Godlove had a hand in drafting its crucial elements. Whilst not being a legally binding document, this was a tremendous commitment on the part of these leaders, at a time when military operations to secure East Timor were ongoing and political arrangements for the territory's transition to full independence had not yet been established. Almost immediately afterwards, Phillips

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<sup>41</sup> CNRT Press Release, "On the Timor Gap Treaty", Darwin, 20 October 1999.

announced that the joint venture partners would be proceeding with the first phase of the Bayu-Undan development. This would require an expenditure of about US\$1.4 billion.<sup>42</sup>

The investment decision was a strong show of faith at a time of profound political uncertainty. The fate of the project and the gains that would ultimately accrue to the company and its joint venture partners would depend, to an important extent, on how the future of the Timor Gap Treaty would be resolved. For a company of Phillips' size, a billion dollar investment was a substantial undertaking. Success or failure in the Timor Sea would inextricably be tied to political decisions that were outside of the company's direct control. However, whilst the letter of comfort signed by the three independence leaders was a critical prerequisite, Godlove predicted that the project would essentially "drive the political process", in so far as it would shape the context for political decision-making.<sup>43</sup> A strong financial commitment to developing the resource at this stage, guaranteeing the early production of the field's natural gas liquids and associated fiscal and taxation revenues, would make it impossible for political leaders to act in any way that would jeopardize the project's future. Godlove calculated that Bayu-Undan was simply too valuable for any of the stakeholders to risk losing, particularly East Timor. The massive destruction of the territory's physical infrastructure that occurred in the wake of the referendum had served cruelly to increase the new state's dependence upon the success of the project and the revenues that would be generated from it.<sup>44</sup>

The situation was thus extremely fluid and events were moving fast, with simultaneous and separate interactions between four sets of actors: Australia, the UN, the East Timorese leadership, and the major corporate stakeholder, Phillips Petroleum. On 12 November 1999, an official of the Australian Mission to the UN, David Steward, met with Hans Corell, UN Under-Secretary General for Legal Affairs, in New York to discuss the political management of the Timor Gap Treaty. Steward had come to the meeting armed with two documents which embodied the Australian government's policy for handling the Timor Gap situation. These were: a draft note verbale that would constitute the basis for an agreement in the form of an Exchange of Notes between the UN and Australia; and, a draft Memorandum of Understanding between the same parties on practical arrangements relating

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<sup>42</sup> 'Majority of Co-Venturers Approve Development of Bayu-Undan Liquids Project: Companies to Continue Development Work, Monitor Timor Gap Treaty Process', *Business Wire*, 27 October 1999.

<sup>43</sup> Pers. Comm. James Godlove, August 2004.

<sup>44</sup> The violence following the referendum resulted in damage or destruction to between 60 and 80 percent of the country's physical infrastructure; World Bank, 2002. *East Timor: policy challenges for a new nation*, Washington, D.C.

to the Treaty.<sup>45</sup> Both documents were designed to provide the legal framework under which the implementation of the Timor Gap Treaty could be continued during the UN's administration of East Timor. Effectively, these arrangements would allow UNTAET to assume the rights and obligations previously exercised by Indonesia in the operation of the joint development zone. Correll considered that Security Council Resolution 1272, when read in conjunction with the Secretary General's Report of 4 October 1999, provided a sufficient basis for UNTAET to assume such a role. The Secretary General's Report had in effect been incorporated into Resolution 1272 through its operative paragraph 1, which authorized the establishment of UNTAET in accordance with the Report of the Secretary General and endowed UNTAET with "overall responsibility to exercise all legislative and executive authority". Paragraph 35 of the Report had stipulated, under the heading "Powers of the Transitional Administration", that, "the United Nations will conclude such international agreements with States and international organizations as may be necessary for the carrying out of the functions of UNTAET in East Timor".<sup>46</sup>

Yet, the UN was mindful that entering into such an arrangement could have legal implications for an independent East Timor. During the meeting, Steward emphasised the importance for Australia of the continuation of the treaty and stressed that the parties which were to decide on this matter were Australia and the UN. He also made the point that the Timorese themselves might want to renegotiate the treaty when becoming independent. "That is their right but no participation of the UN should be envisaged".<sup>47</sup> Steward informed Correll "that Australia expected the UN to participate in the transitional period, including through representation in joint bodies, but it did not correspond to the UN to renegotiate the treaty".<sup>48</sup> This point needs to be underlined. The United Nations was expressly told not to get involved in any renegotiation of the Timor Gap Treaty. At this stage, however, the UN's chief concern was to ensure that any decision regarding the continuation of the Timor Gap Treaty during the transitional phase was taken in accordance with the will of the East Timorese people and without prejudicing any actions that they may wish to take vis-à-vis the treaty after independence. This was important as, over the course of November and December 1999, there

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<sup>45</sup> Record of Meeting with David Steward of the Australian Mission to the United Nations, Office of Legal Affairs, 12 November 1999.

<sup>46</sup> UN doc. S/1999/1024, <http://www.un.org/peace/etimor/docs/sg1024.htm> <Accessed 10 October 2005>

<sup>47</sup> Record of Meeting between David Steward of the Australian Mission to the United Nations and the United Nations Office of Legal Affairs, 11 November 1999.

<sup>48</sup> *Ibid.*

was a discernible shift in the tone and rhetoric used by some of East Timor's leaders, particularly Mari Alkatiri.

Whilst, in the immediate aftermath of the referendum, the approach taken by Alkatiri had been very supportive of keeping the treaty, this changed fairly rapidly towards the end of the year as he began to consolidate his position within the emerging political order in East Timor. During this period, the main source of Alkatiri's legal advice was Miguel Galvão-Teles, a widely experienced and highly qualified Portuguese lawyer, who had represented Portugal in the Security Council debates on East Timor, in 1975, as well as the case against Australia at the International Court of Justice in 1995. Galvão-Teles had argued that the Timor Gap Treaty was not just illegal but prejudicial to the rights of East Timor. Citing the precedent of the *Libya/Malta* case, Galvão-Teles had made a powerful statement of East Timor's claims to the entirety of Area A of the Zone of Cooperation. The similarities between the circumstances in the *Libya/Malta* case and the Timor Gap dispute, he had argued, were "so striking – facing coasts, distance of less than 400 miles, geomorphological accident – that the words uttered by the Court in 1985 can quite simply be echoed in determining the validity of the titles of East Timor and Australia with regard to the continental shelf in the Timor Gap area".<sup>49</sup>

In an interview reported on 29 November 1999, Alkatiri was quoted in connection with the Timor Gap Treaty as saying "we are not going to be a successor to an illegal treaty".<sup>50</sup> The positive outlook which had hitherto marked Foreign Minister Downer's comments on the issue a month earlier instantly evaporated. On 30 November, he warned: "to start to unravel the whole of the Timor Gap Treaty would in turn unravel all of the investment in the Timor Gap and that wouldn't be in anybody's interests, particularly East Timor's."<sup>51</sup> This was precisely Alkatiri's dilemma: he wanted the oil and gas revenues but not the Treaty. The Treaty was viewed from within the CNRT as both a product and a symbol of the occupation. It was seen as Australia's reward for acquiescing in the Indonesian occupation.<sup>52</sup> The idea of state succession was anathema. Yet, for investment in the joint development zone to continue, political institutions governing the area needed to remain operational and, in light of Indonesia's disengagement, the Joint Authority could not function in its present state. At

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<sup>49</sup> *Portugal/Australia*, 1995, First Round of Oral Pleadings (Portugal), in Krieger, H. (ed.), 1997. *East Timor and the International Community: basic documents*, Cambridge University Press, Cambridge, p.379.

<sup>50</sup> 'Future of Timor Gap Treaty thrown into doubt', *Australian Associated Press*, 29 November 1999.

<sup>51</sup> 'Australia promises East Timor full benefits of Timor Gap oil treaty', *Agence France Press*, 30 November 1999.

<sup>52</sup> Australian Broadcasting Corporation, *Four Corners: rich man, poor man*, 10 May 2004.

this time, a 5.8 million dollar added investment was pending on the Elang/Kakatua project to enhance production rates and the multi-billion dollar Bayu-Undan development plan, which had been submitted to the Joint Authority at the end of November 1999, also required formal regulatory approval.

Thus, in the interests of enabling these investment decisions to move forward, UNTAET agreed, with the assent of the CNRT, to a continuation of the terms of the Timor Gap Treaty throughout the period of transitional administration.<sup>53</sup> In the absence of such an agreement, the treaty framework would cease to apply, which would create a riskier investment environment. On 19 January, Hansjoerg Strohmeier, the Principal Legal Adviser to Sergio Vieira de Mello, explained that the decision to continue the terms of the treaty was not a case of treaty succession but an interim measure that would cover the period of UNTAET's mandate in East Timor. Strohmeier stressed that although the regime would remain completely unchanged this was a "new legal instrument...as we do not want to retroactively legitimize, or give any legitimacy to the conclusion of the treaty, that was done by Indonesia over what is part of the territory of East Timor".<sup>54</sup> The Exchange of Notes between UNTAET and Australia was signed on 10 February 2000.<sup>55</sup> On the same day, Foreign Minister Downer and the Minister for Industry, Science and Resources, Nicholas Minchin, issued a joint media release, stating that Indonesia "had agreed that...the area covered by the Treaty was now outside Indonesia's jurisdiction and that the Treaty ceased to be in force as between Australia and Indonesia".<sup>56</sup>

Shortly after the conclusion of the Exchange of Notes, de Mello and Minchin announced that the Timor Gap Joint Authority, now under Australian and UN control, had approved the development plan for the Bayu-Undan project.<sup>57</sup> The decision represented the final governmental authorization required by the joint venture partners before proceeding with the construction of the drilling platforms and production facilities. Bayu-Undan would be

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<sup>53</sup> Daily Briefing, United Nations Transitional Administration in East Timor, 19 January 2000. <http://www.un.org/peace/etimor/DB/sbr1901.htm> <Accessed 9 September 2004>

<sup>54</sup> *Ibid.*

<sup>55</sup> The title of this agreement was: *Exchange of Notes constituting an Agreement between the Government of Australia and the United Nations Transitional Administration in East Timor (UNTAET) concerning the continued Operation of the Treaty between Australia and the Republic of Indonesia on the Zone of Cooperation in an Area between the Indonesian Province of East Timor and Northern Australia of 11 December 1989*, signed 10 February 2000.

<sup>56</sup> Minister for Foreign Affairs and Minister for Industry, Science and Resources, Commonwealth of Australia, *Timor Gap Agreement reached with UNTAET*, Joint Media Release, 10 February 2000, [http://www.dfat.gov.au/media/releases/foreign/2000/fa010\\_2000.html](http://www.dfat.gov.au/media/releases/foreign/2000/fa010_2000.html) <Accessed 11 October 2005> The disengagement was made formal in an exchange of letters between the Indonesian Minister of Foreign Affairs, Dr Alwi Shihab, and Foreign Minister Downer, on 25 May 2000.

<sup>57</sup> 'World scale petroleum project for Timor Sea', *M2 Presswire*, 28 February 2000.

developed in two phases. The first phase would involve production and processing of the field's 'wet' gas, which amounted to about 400 million barrels of condensate, propane and butane. The second stage would involve the transport of the 'dry' gas by pipeline for use at locations near Darwin and/or for input to a Liquefied Natural Gas (LNG) processing facility and export to foreign markets.<sup>58</sup> Design production rates for the facility were for approximately 115,000 barrels per day. This would be a technologically complex operation. Until sales contracts for the dry gas had been concluded, the facility would strip out the liquids and re-cycle 950 million cubic feet of gas, per day, back into the reservoir.<sup>59</sup> The enormous cost of phase one – at around US\$1.4 billion – was attributable, in large part, to the massive compression equipment required to recycle such a large volume of gas on a continual basis.

#### ***4.3 UNTAET Demands a New Treaty***

The conclusion of the 10 February Exchange of Notes constituted an unprecedented undertaking for the UN: it was the first time in history that the organisation had taken on the role of partnering a state in the operation of a bilateral regime of this nature. Whilst conscious of the need to act in a manner consistent with broadly representative East Timorese opinion, it was nonetheless considered by the UN Secretariat to be a necessary decision for the carrying out of UNTAET's Security Council mandate in East Timor. The continued exploitation of Timor Sea gas and oil resources would be critical to a range of fundamental political, economic and social objectives, including: supporting capacity-building for self-government; assisting in the creation of conditions for sustainable development; and, promoting economic and social recovery and development – all of which had been set out comprehensively in paragraph 2 of Security Council Resolution 1272 as well as paragraphs 28 and 29 of the Report of the Secretary General, of 4 October 1999.<sup>60</sup> However, the Exchange of Notes was an interim agreement only and would expire on the date of East Timor's independence. The CNRT had supported it as a "temporary expedient" but indicated that, after independence,

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<sup>58</sup> Department of Industry, Science and Resources, Submission #63, Senate Foreign Affairs, Defence and Trade References Committee, *Inquiry into East Timor*, 1999.

<sup>59</sup> 'Bayu-Undan gas recycle project development plan approved by Timor Gap Joint Authority', *Business Wire*, 29 February 2000; 'Australia – Timor Sea gas field project', *International Market Insight Trade Inquiries*, 30 July 1999.

<sup>60</sup> UN doc. S/1999/1024, 4 October 1999.

they would be looking into “ways to adjust the treaty to East Timor’s interest”.<sup>61</sup> Yet, up until this point, there had been little consideration of exactly what would happen after independence. All the attention had been focused solely on the transitional period. Australia’s plan was to extend the Timor Gap Treaty in two stages, firstly with the UN and then with an independent East Timor – otherwise referred to as the “two-step strategy”.<sup>62</sup> Once the period of UN administration came to an end, it seems the government presumed that East Timor could easily be persuaded to agree to its further continuation because of the new state’s dependence on petroleum revenues. In order for revenues to be generated, a functioning legal framework would have to remain in place. By exploiting this dependence, Australia aimed to ensure that the existing treaty arrangements continued indefinitely. This was the reality of the Australian strategy and, whilst not officially expressed in such terms, was nonetheless the way in which it was read by Peter Galbraith shortly after his arrival in Dili, at the end of January 2000. Galbraith, of the US State Department, was appointed the Director of Political Affairs within the UN Transitional Administration. With executive powers that covered UNTAET’s dealings with foreign powers, his role in Timor Sea politics would have a major influence on the future course of events.

Galbraith brought a considerable amount of diplomatic know how to his assigned position. Previously the US Ambassador to Croatia, from 1993 to 1997, he had experienced one of the bloodiest periods in Balkans history and had played a major role in a number of complex peace negotiations to bring an end to the conflict. These included the Croatia and Bosnia peace process, the negotiations that brought an end to the 1993-4 Muslim-Croat war and also the 1994 Washington Agreement establishing the Federation of Bosnia-Herzegovina. He had also been a co-sponsor of the peace process in Croatia that produced several agreements between the Croatian government and the Krajina Serbs and, with Thorvald Stoltenberg, had been the co-mediator of the Eastern Slovenia negotiations.<sup>63</sup>

#### INTERESTS COLLIDE

De Mello had wanted an experienced diplomat in the role of Political Affairs Director chiefly because of the difficulties and potential conflict that was expected to arise between

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<sup>61</sup> ‘East Timor to renegotiate oil and gas treaty’, *Reuters News*, 31 January 2000.

<sup>62</sup> Senate Foreign Affairs, Defence and Trade References Committee, Committee Hansard, *Inquiry into East Timor*, 11 November 1999, p.868-86; and, 9 December p.1009-14.

<sup>63</sup> Galbraith, P., 1997. ‘Washington, Erdut and Dayton: negotiating and implementing peace in Croatia and Bosnia-Herzegovina’, *Cornell International Law Journal*, vol.30, p.643.



UNTAET and Indonesia over the terms of the latter's withdrawal from East Timor. Galbraith's toughest negotiation, however, would prove to be with Australia, not Indonesia. Within just a few weeks of taking up the position, he had formed the view that the Timor Gap Treaty was a bad deal for East Timor and that an attempt should be made during the period of UN administration to negotiate a new regime. After obtaining a political mandate from both the CNRT and the NCC, an issue which had apparently been the cause of "lengthy debate" within the Cabinet, Galbraith led a small delegation to Australia, in March 2000, to request opening formal treaty negotiations with Australia on a new regime for the Timor Gap.<sup>64</sup>

The first meeting was with Foreign Minister Downer, in Adelaide, on 20 March, and subsequent meetings were held with senior government officials in Canberra. The message conveyed to the government was brief and to the point. Downer was informed:

UNTAET has continued the terms of the Timor Gap Treaty between Australia and Indonesia for the duration of the transition period. We have not continued the treaty because both we and the East Timorese consider the Indonesian occupation of East Timor to have been illegal and therefore Indonesia had no legal authority to enter into a treaty affecting East Timor's resources. UNTAET's action was a temporary measure designed to permit certain investments to go forward. As of the date of East Timor's independence, there will be no regime governing the resources of the Timor Gap.<sup>65</sup>

The situation therefore demanded that Australia and UNTAET commence negotiations so that a new treaty instrument would be ready to take effect from the date of independence, otherwise, the transitional arrangements would lapse and there would be a legal vacuum.

The decision to request opening negotiations was taken for purely strategic reasons and it is critically important to understand what these reasons were. Basically, Galbraith saw the Timor Gap Treaty as a product of the unique political circumstances under which it had been negotiated – circumstances that were fundamentally different than those presently facing East Timor. He considered that Indonesia had entered into negotiations with Australia to settle the sovereignty dispute in the Timor Sea in the late 1970s, recognizing that the country's options were extremely limited. Irrespective of the strength of Indonesia's claims to exclusive

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<sup>64</sup> Morrow, J. and White, R., 2001. 'The United Nations in Transitional East Timor: international standards and the reality of governance', *Australian Yearbook of International Law*, vol.22, p.25.

<sup>65</sup> Diplomatic note given to Foreign Minister Downer, 20 March 2000

jurisdiction within the contested area, the case could not have been taken to the ICJ, or any of the other dispute settlement mechanisms provided for under Part XV of the United Nations Convention on the Law of the Sea, as this would automatically have raised the whole question of the legality of Indonesia's occupation of East Timor and the very basis upon which the country's claims to continental shelf jurisdiction off East Timor's coast were founded. At the same time, however, the actual resource potential of the disputed area was not especially important for Indonesia. The resources of the Timor Gap amounted to only a small fraction of the country's endowment of petroleum resources as a whole.<sup>66</sup>

In stark contrast, an independent East Timor would have recourse to the full range of international conflict settlement mechanisms but this course of action carried substantial, political, legal and commercial risks. It was precisely as a consequence of the protracted boundary dispute between Australia and Portugal, followed by Indonesia, which had brought about a suspension in petroleum activities in the Timor Gap for more than a decade, between 1978 and 1991. A long drawn-out legal battle could have the same effect. Thus, if East Timor wanted a share of Gap resources commensurate with the strength of its claim under international law, whilst avoiding any delays to development at the same time, negotiation was the only option. Yet, as an independent country, it was obvious to Galbraith that East Timor would be extremely vulnerable to political pressure and manipulation by the Australian government. Any future negotiation would be a contest between two sides of dramatically unequal bargaining power. East Timor would be overwhelmingly dependent upon Australia for political and economic aid, as well as for maintaining security within its borders.

To be sure, Australia's dominance in the bilateral relationship could hardly be greater. Australian troops formed the largest contingent of the multinational force that would be stationed in the territory for several years until the UN's peacekeeping activities had come to an end there. East Timor would be heavily reliant upon Australian expertise and money in support of government administration and capacity building. Within this context, an independent East Timor would have virtually no sources of leverage in negotiations with Australia and, moreover, would have only limited financial resources to pay for the expert legal and commercial advice that complex treaty negotiations of this nature would necessarily

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<sup>66</sup> On this point it is worth noting that whilst the collective level of risk investment in the first round of bidding for exploration acreage in the joint development zone in 1992 totaled about US\$360 million, total expenditure on exploration and development in Indonesian onshore and offshore areas that year amounted to US\$1.3 billion; the resources of the Timor Gap may have been important but were by no means fundamental to the economic well-being of the country. See Barnes, P., 1995. *Indonesia: the political economy of energy*, Oxford University Press, Oxford.

require. The asymmetry within the bilateral relationship meant that Australia, by contrast, would have extremely wide ranging and powerful bargaining levers at its disposal if demands made by East Timor's leaders were considered to be detrimental to Australian national interests.

Galbraith considered that the balance of power between Australia and the UN, on the other hand, would be somewhat more equal. UN negotiators would be less sensitive to possible conditional commitments made by Australia, such as threats of political retaliation, for any actions that UNTAET might decide to take. Moreover, they would have more freedom to take an aggressive stance in the negotiations than East Timor's leaders, as the quality of their personal relationships with the Australian government was comparatively unimportant.<sup>67</sup> Finally, it was also recognised that from a legal standpoint the continuation of the Timor Gap Treaty could have a negative impact upon East Timor's claim under a potential future litigation as it could imply East Timor's acceptance of a particular 'modus vivendi', in a manner which international courts have, in the past, been prone to treat as a relevant factor.<sup>68</sup> The decision to seek an immediate commencement of negotiations was therefore also taken for the purposes of denying any legitimacy to a treaty that East Timor considered illegal and void.

Galbraith calculated that Australia would have no choice but to negotiate with the UN – not only because of its obligations to safeguard the interests of corporate investors but also because of the broader political stakes involved. 'Unraveling' the Timor Gap Treaty, as Downer had put it, would be extremely costly for Australia, also. It would reflect badly on the enormous diplomatic resources Australia had expended in negotiating that agreement over a period of more than a decade as well as the political effort and financial cost of defending it against both domestic and foreign legal challenge. The fragmentation of the Treaty would have very important legal, political and economic ramifications not just for Australia but for the wider region also and its possible collapse would, in some respects, bear out the failure of Australia's policy in East Timor. Australia had a deep seated political attachment to the Timor Gap Treaty, which at one point had been hailed as a "trail blazing agreement" and "the most

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<sup>67</sup> See, on this point, Chesterman, S., 2001. *East Timor in Transition: from conflict prevention to state-building*, International Peace Academy, Washington, D.C., p.24.

<sup>68</sup> The precedent was set in *Tunisia/Libya* (1982), when the ICJ treated as a relevant circumstance, the existence of a modus vivendi expressed within the parties' de facto respect for a line that had been drawn during the colonial era. As neither country had since contested the line, the ICJ found that the modus vivendi "could warrant its historical justification for the choice of the method for the delimitation of the continental shelf..." (*Tunisia/Libya*, 1982, p.70-71, para.95).

significant agreement concluded in the 40 year history of Australia's relations with Indonesia".<sup>69</sup>

In an attempt to set the context for negotiations, Galbraith's main objective at this stage was to impress upon the Australian government the strength of UNTAET's determination.<sup>70</sup> His goals for the meeting with Downer were three-fold: to convince the Foreign Minister that the Timor Gap Treaty was effectively dead and that an independent East Timor would not continue its terms past the date of independence; to demonstrate UNTAET's firm belief in the legality of East Timor's claim for a mid-point continental shelf delimitation; and to shift perceptions of Australia's national interests in the issue. In terms of the latter, Galbraith essentially made the argument that it would be in Australia's interests for East Timor to receive all the Timor Gap revenues because this would support the new nation's future viability and lessen its economic and political dependence upon Australia. "With the Timor Gap revenues, East Timor could build a sustainable economy that meets the basic needs of the East Timorese people. Without the full benefit of this income, East Timor is less likely to be stable, more likely to require sustained foreign assistance, and more likely to be an exporter of refugees and economic migrants".<sup>71</sup>

To appreciate Downer's reaction, it must be borne in mind that his Department had instructed the Australian Mission to the UN to inform Under-Secretary General for Legal Affairs, Hans Correll, in November 1999, that the UN must not become involved in any treaty negotiation. From the Australian viewpoint, this was a bilateral matter between Australia and East Timor. But as Galbraith had decided to ignore that warning, the Australian government faced an uncomfortable strategic choice. If it chose to negotiate with UNTAET, the timetable for the negotiations would be dictated by the transitional process and, therefore, not at a pace, or in a manner, that Australia could easily control. Yet if it refused to negotiate, the treaty arrangements would collapse; petroleum activities would be suspended and the government would be exposed to substantial claims of compensation. Downer was extremely unhappy but apparently "alerted" to the situation and said that UNTAET's request had "added a new dimension".<sup>72</sup> He conveyed a veiled warning that re-negotiating the treaty could have a

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<sup>69</sup> Statement by Foreign Minister Evans to the Timor Gap Forum, Darwin, 3 November 1990.

<sup>70</sup> Pers. Comm. Peter Galbraith, August 2004.

<sup>71</sup> Diplomatic note given to Foreign Minister Downer, 20 March 2000.

<sup>72</sup> Pers. Comm., Senior UN Official, August 2004.

destabilising impact on continued investment in the region. After the meeting he lodged an official complaint with the UN Secretary-General.<sup>73</sup>

Following the Galbraith/Downer discussions in Adelaide on 20 March, further meetings were held in Canberra from 21 to 23 March 2000. During these discussions, the Australian delegation was led by Michael Potts, the Director for International Organizations in the Department of Foreign Affairs and Trade, and John Hartwell, the Director of Petroleum and Mines Division in the Department for Industry, Science and Resources. All the major sectors of government were represented at the meeting: the Department of Prime Minister and Cabinet, the Attorney-General's Department, the Australian Taxation Office, the Australian Agency for International Development, the Treasury as well as the Timor Gap Joint Authority. Galbraith re-iterated the key points which had been made to Downer the previous day: namely, that UNTAET had resolved to negotiate a new petroleum regime by independence or there would be no regime at all; that East Timor had a very strong legal case for a mid-point continental shelf delimitation and would be prepared to have this matter settled by the ICJ if necessary; and, that the CNRT and the NCC fully supported the proposed negotiations and would be fully involved in the process.<sup>74</sup> The Australian side replied that it preferred to negotiate with an independent East Timor and that, in the interim, the current treaty arrangements could be extended until a new treaty had been agreed. Galbraith perceived that "behind this approach lay a hope that Australia could stonewall the process" so that the old regime continued indefinitely.<sup>75</sup>

On 1 April 2000, de Mello reported back to UN headquarters on the outcome of the discussions. He noted that:

The exchanges were spirited but productive in that the Australians were able clearly to understand the UNTAET/East Timor position. Whilst insisting they had to take the matter to ministers in order to move forward – a process which could take many months – Potts privately mentioned to Galbraith that Australia would not refuse to negotiate a new regime for the Timor Gap. Over the course of the three days in Canberra, the true nature of the Australian position came into sharper focus. Namely, it became clear that the Australians were anxious to avoid taking this matter before the ICJ, and that the real issue

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<sup>73</sup> *Ibid.*

<sup>74</sup> Cable sent by S. V. de Mello to B. Miyet, 'Timor Gap talks with Australia' (20-23 March 2000), 1 April 2000.

<sup>75</sup> *Ibid.*

for Australia is not the revenue but rather protecting their political claim to a seabed boundary at the outerpoint of their physical continental shelf. In return, Galbraith indicated that a line on the ocean floor was of little interest to East Timor. Rather, East Timor's governing concern was in securing as much (or nearly as much) revenue from the Timor Gap petroleum as it would under a fair maritime delimitation. We also added that it was in East Timor's interest, economically and politically, that Australia remains involved in the Timor Gap. Accordingly, we put forward the proposal of continuing a sharing system based on the existing model but with a 90/10 East Timor/Australia division of the resources north of the mid-point (which would incorporate all of what is the most productive area of the Zone of Cooperation) and a reverse split south of the mid-point.<sup>76</sup>

De Mello's cable was addressed to Bernard Miyet, who was the head of the UN Department of Peacekeeping Operations (DPKO). Technically, East Timor was a peacekeeping operation for the UN and, therefore, de Mello reported directly to Miyet, although the cable was also copied to Under-Secretary General for Political Affairs, Sir Kieran Prendergast and Under-Secretary General for Legal Affairs, Hans Correll. Maintaining the support of these senior UN officials would be critical in the negotiations. De Mello concluded his letter on an encouraging note:

These talks mark a breakthrough. Australia now knows our position, understands we are serious, and realises that the status quo will not continue. We have also established constructive and friendly working relations. This is as much as one can hope for at this stage as we have now started a process to secure for East Timor that to which it is legally entitled. Obviously, there is no guarantee that a deal can be concluded, but the very initial signs are positive.<sup>77</sup>

Yet, over the following months, the atmosphere became increasingly confrontational. In an interview with the Australian Broadcasting Corporation, on 7 May 2000, Ramos Horta

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<sup>76</sup> *Ibid.*

<sup>77</sup> *Ibid.*

was openly critical of the revenue sharing arrangements of the Timor Gap Treaty and stated that East Timor would be seeking 90 percent of revenues from the jointly managed area.<sup>78</sup> Use of the media formed an important part of UNTAET's strategy of building commitment and leverage through public exposure of its negotiating position. During a FRETILIN Conference in East Timor, in May, Galbraith disclosed that the CNRT had informed the Australian government that East Timor would not continue the terms of the Timor Gap Treaty past independence and that a new regime would need to be put in place. He commented that the East Timorese view was that the revenues from oil and gas north of the mid-point should go to East Timor, and that achieving an outcome close to this allocation was UNTAET's goal in the negotiations.

The substance of Galbraith's comments got reported back to the Australian government and both the DPKO and Office of Legal Affairs (OLA) were subsequently warned about the effects that discussion of East Timor's and Australia's conflicting negotiating positions in public forums could have. The UN was told that publicizing the issues could undermine investor confidence, "killing the goose that lays the golden eggs".<sup>79</sup> Galbraith was criticized for creating "over inflated expectations" which could have a "destabilizing effect" in the region.<sup>80</sup> The pressure on the UN Secretariat was creating tensions within the organization. UNTAET was undoubtedly skirting at the very edge of its political mandate. The attitude of the Australian government was that Peter Galbraith had arrogated to himself the authority of the East Timorese. Yet both de Mello and Correll were prepared to stand firmly behind him. Assisting East Timor against the interests of Australia, it seems, was seen, from a moral standpoint at least, as being the right thing to do.<sup>81</sup>

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<sup>78</sup> 'Timor call to review oil treaty', *Sydney Morning Herald*, 8 May 2000.

<sup>79</sup> Office of Legal Affairs, record of meeting, 'Re: Conversation with Jonathan Thwaites, 26 May 2000'.

<sup>80</sup> *Ibid.*

<sup>81</sup> It seems, however, that there were conflicting impressions of what Peter Galbraith had actually discussed at the FRETILIN Conference. On 1 June 2000, de Mello cabled Miyet, noting that "for Australia, Galbraith's comments caused angst". De Mello explained that:

Peter Galbraith...did not say that Australia recognized the need 'to draw a new line in the sea'. On the contrary, the point was made that the important thing for East Timor was not the line at the bottom of the sea but rather the allocation of the money. At the conference, Galbraith noted the East Timor view that the revenues from oil and gas north of the mid-point should go to East Timor and that coming close to this allocation was our goal in the negotiations. Comments did not go beyond public comments on this issue made in Australia by CNRT leaders Xanana Gusmão and José Ramos Horta.

The note continued:

[I] agree with Hans Correll that UNTAET's negotiating goal should be a reallocation of revenues and not a boundary delimitation, which *per se* is of little relevance to East Timor. Should we fail to achieve an acceptable reallocation of revenues, an independent East Timor

During the middle of June 2000, UNTAET and Australia held another round of Timor Gap discussions. As before, the Australian delegation was comprised of senior officials from Foreign Affairs (led by Michael Potts) and Industry, Science and Resources (led by John Hartwell), together with representatives from the Attorney-General's Department and the Treasury. The purpose of the discussions, which were described by Australia as "pre-negotiations", was to organize the timing for the first round of formal negotiations and to determine the basis upon which the negotiations would take place. The Australian delegation confirmed that it was Australia's understanding that negotiations would be held to establish the terms of a new joint petroleum development agreement prior to East Timor's independence.<sup>82</sup> On 19 June, de Mello updated Bernard Miyet on the outcome of these discussions. The cable was copied to Hans Corell and Kieran Prendergast, also. De Mello stated:

Australia's recent discussions with OLA have confirmed in their minds that the UN – whether in New York or Dili – is united in its approach to the Timor Gap. Your support in this regard is greatly appreciated...On the substance of East Timor's claim, Galbraith explained that while East Timor had an excellent claim in law to a maritime boundary with Australia at the mid-point of the Timor Sea, it was more concerned with increasing its share of the revenue from petroleum in the Timor Gap than in seeking a delimitation. Further, if the revenue share was revised then this would need to be reflected in some way in the structure of the Joint Authority as it would not be tenable for Australia to be in a position to veto future petroleum exploitation in the Gap from which East Timor would be the prime beneficiary. Finally, Galbraith mentioned – but without taking a position – that both parties might wish to use the opportunity of negotiating a new treaty to tailor it more for gas exploitation (the old treaty envisaged primarily an oil province) and also to revisit the system, demanded by Indonesia, of Production Sharing Contracts.

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has all options for pursuing a boundary delimitation. The possibility that it might do so is one incentive for Australia to come to an agreement before the end of the transitional period.

Cable from S. V. de Mello to B. Miyet, 'Re: Conversation with Jonathan Thwaites, 26 May 200', 1 June 2000.

<sup>82</sup> Cable from S. V. de Mello to B. Miyet, 'Timor Gap Talks' (14-15 June), 19 June 2000.



...Potts responded that he would be “astonished” if Australian ministers would agree to a fundamental restructuring of the Joint Authority. He suggested that any move away from a consensus approach in the Joint Authority would “completely subvert the philosophical rationale behind the Timor Gap Treaty”, which was to put aside competing sovereignty claims. Galbraith reformulated our position that there would need to be a independent dispute settlement mechanism, should Australia ever seek to veto developments that would primarily be in East Timor’s interest and which might compete with operations that were solely within Australian sovereign waters. Galbraith suggested that perhaps a third party should be designated to resolve such questions should they occur, thus allowing for the retention of the Joint Authority. It was agreed that a formula to resolve the problem should be sought along these lines...In conclusion, it was agreed that the first negotiating round will in all likelihood take place in the second half of September in Dili. Alkatiri mentioned that the new agreement should continue to leave open the question of sovereignty of waters in the Timor Gap. Nonetheless, it was agreed that the new deal could last for a “very long time” provided it broadly reflected the economics of a hypothetical mid-point maritime boundary.<sup>83</sup>

The idea of having a political imbalance in the governance institutions was a new factor which had not been discussed during the first set of discussions, in March. It is an indication of how UNTAET’s approach to the problem and their understanding of the issues were continuously evolving. Both Alkatiri and Galbraith had had no previous experience in dealing with this type of negotiation. The legal and commercial aspects of offshore petroleum governance were foreign territory. This lack of expertise would have placed them at a disadvantage, one would think.<sup>84</sup> Thus, whilst seeking to demonstrate the strength of UNTAET’s interests, Galbraith seems also to have been probing the Australian delegation and testing their own resistance levels.

De Mello considered these pre-negotiation sessions to have been “extremely fruitful”. He ended his cable on a note of cautious optimism:

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<sup>83</sup> *Ibid.*

<sup>84</sup> In March 2000, Galbraith was quoted in an oil industry newspaper as saying “I don’t claim any great experience in oil and gas matters, but I’ve dealt with the Persian Gulf while working for the US Senate Committee on Foreign Relations”. See ‘American takes Timor Gap reins’, *Upstream*, 3 March 2000.

The latest round of talks built significantly on the March round. Australia now seems clearly committed to negotiating a new regime for the Timor Gap – prior to independence – on terms that will be significantly more favourable to East Timor than the current arrangement. It was indicated in an aside to Galbraith that somewhere between a 70/30 and 90/10 split in favour of East Timor was on the cards. While the devil may still prove to be in the details, remarkable progress has so far been made on this matter which could down the road potentially benefit East Timor to the tune of tens of millions of additional dollars per annum.<sup>85</sup>

In spite of this apparent progress, relations between the parties continued to be quite tense. A petty confrontation briefly arose over UNTAET's attempts to access the funds of the Zone of Cooperation Joint Authority. Galbraith had identified this account, which was roughly US\$4 million in credit, as a possible means of supporting the costs of negotiations. In an effort to deny the UN any additional assistance, however, Australia claimed that this money belonged to the old Australian/Indonesian entity and not the current authority that was now under Australian and UN management. Thus, half of it belonged to Australia and the other half to Indonesia. UNTAET contested this response and went as far as invoking the dispute settlement mechanism under the Timor Gap Treaty. Yet the Australian government, somewhat embarrassingly, had made a mistake; the 10 February Exchange of Notes had in fact specified that the Joint Authority was to close its bank accounts in Jakarta and consolidate all of its funds into its existing bank accounts in Darwin.<sup>86</sup> When this was pointed out, Australia backed down and consented to UNTAET/East Timor being able to use Joint Authority funds for the purposes of securing expert legal and commercial advice on petroleum issues. This money would be extremely valuable to UNTAET in its preparations for the negotiations.

Meanwhile, the process of political transition in East Timor continued to evolve. On 14 July 2000, UNTAET established the East Timor Transitional Authority (ETTA) Cabinet. This was an embryonic governmental structure of East Timor that was intended to be retained

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<sup>85</sup> *Ibid.*

<sup>86</sup> *Article 4, paragraph f*, of the Exchange of Notes of 10 February 2000 provided that, “the Joint Authority will close its bank accounts in Jakarta and consolidate all of its funds into its existing bank accounts in Darwin”.

post-independence.<sup>87</sup> Eight portfolios were created within the cabinet. Four of these were controlled by East Timorese nationals (internal administration, infrastructure, economic affairs, social affairs) and four by UN personnel (finance, justice, police and emergency services, and political affairs). Mari Alkatiri became cabinet member for Economic Affairs, and Peter Galbraith retained the Political Affairs portfolio. In October 2000, José Ramos Horta was sworn in as cabinet member for Foreign Affairs, increasing East Timorese control to five out of a total nine cabinet positions.<sup>88</sup> The 15-member National Consultative Council, which had been established in December 1999, was also replaced by a National Council, expanded to 33 members, to facilitate broader participation in policy-making.<sup>89</sup> At its second meeting, the new Cabinet agreed to appoint Alkatiri and Galbraith to the Ministerial Council for the Zone of Cooperation.<sup>90</sup> With East Timorese now in command of the key economic and foreign affairs portfolios as well as Ministerial representation in the institutional arrangements for the joint development zone, UNTAET could legitimately maintain that the position being adopted on Timor Gap matters was that of a fully unified UNTAET/East Timorese government. This was politically important, as it deprived the Australian government any means of challenging the UN Secretary-General on whether UNTAET had the mandate to negotiate with Australia.

Yet it also demonstrated to Alkatiri's domestic constituents, particularly within FRETILIN, that this hugely important issue was not being totally dominated by the UN. To be sure, Alkatiri was under an immense amount of pressure from his own side to take a hard line with Australia. The resources involved were not only the new nation's major economic asset but were a powerful symbol of East Timor's impending sovereignty. Unsurprisingly, the issue was beginning to generate a great deal of nationalistic sentiment. During a CNRT congress, held in August 2000, the suggestion was made that all international oil companies which had operated in the Timor Gap during the period of Indonesian occupation should be barred from exploring there in the future.<sup>91</sup> The situation was extremely awkward for Alkatiri, who basically wanted to attract foreign investment and to signal to industry that East Timor was a safe and business friendly environment. He told the CNRT congress that "we have to respect

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<sup>87</sup> Morrow and White, 2001, *op. cit.*, p.6.

<sup>88</sup> UN doc. S/2000/738, Report of the Secretary-General on the United Nations Transitional Administration in East Timor, 26 July 2000.

<sup>89</sup> UN doc., S/2000/738, 26 July 2000.

<sup>90</sup> UNTAET Daily Press Briefing, 21 July 2000.

<sup>91</sup> 'E.Timor, Australia to begin sea boundary talks in Oct.', *Kyodo News*, 26 August 2000.

the commitments [the oil companies] have made and give them guarantees that they will not lose everything”.<sup>92</sup>

The issue was also proving to be a source of contention within domestic Australian politics. Cross-party support for the government’s policy was not forthcoming. At its National Conference, held in Hobart, August 2000, the opposition Australian Labor Party (ALP) adopted a new resolution which stated that, “Labor is prepared to support the negotiation and conclusion of a permanent maritime boundary in the Timor Gap based on lines of equidistance between Australia and East Timor...Alternatively, should East Timor prefer to continue or modify the existing regime governing the Timor Gap, Labor supports the negotiation of a new agreement for the joint development of these gas and petroleum resources”.<sup>93</sup> The party’s Shadow Minister for Industry, Science and Resources, Martyn Evans, later confirmed that if the East Timorese wanted to retain the joint development concept, then “the ratio of 90/10, as claimed by East Timor, would not be unreasonable”.<sup>94</sup> The head of DFAT, Ashton Calvert, said afterwards that this was contrary to the government’s position which was to “extend the agreement as it stood”.<sup>95</sup> Foreign Minister Downer was disparaging of the opposition and warned UNTAET not to try and gain any leverage from the apparent shift in the ALP’s policy.<sup>96</sup>

With federal elections due to be held in Australia in 2001, however, the situation was being closely watched by Phillips. Godlove later met with ALP leader, Kim Beazley, to ask what the government’s approach would be in the event of an ALP victory. Beazley confirmed the 90/10 policy but also indicated that he would not change Australia’s established position on the question of permanent boundary delimitation.<sup>97</sup> Indeed, from a commercial standpoint, UNTAET’s decision to initiate negotiations on a new petroleum regime was undesirable as it introduced a significant element of uncertainty. For Phillips the paramount objective was to ensure that the existing legal framework remained in place and unchanged. The strategy for achieving that goal was simply to maintain project momentum. In September 2000, the company announced a Letter of Intent with a large Australian engineering firm, Multiplex,

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<sup>92</sup> *Ibid.*

<sup>93</sup> Laurie Brereton MP, *News Release*, 116/00, 3 August 2000.

<sup>94</sup> Speech by Martyn Evans to the Australian Gas Association Convention, 14 November 2000.

<sup>95</sup> ‘New oil deal for E. Timor’, *Northern Territory News*, 4 August 2000.

<sup>96</sup> ‘Downer hoses down expectation of Timor Gap revenue swing’, *Australian Associated Press*, 31 August 2000.

<sup>97</sup> Pers. Comm. James Godlove, 10 August 2004.

relating to construction of a gas pipeline from Bayu-Undan to a site at Wickham Point in Darwin Harbour.<sup>98</sup>

The pipeline was to form an integral component of the company's region-wide strategy of establishing an onshore site in Australia where gas could be gathered from a variety of fields in the Timor Sea and which could then be processed and distributed to either domestic or export customers.<sup>99</sup> In this regard, discussions had been ongoing between Phillips, Woodside and Shell to explore potential areas of cooperation between the development of Bayu-Undan and the Greater Sunrise fields. Together, these reserves were estimated to contain more than eleven trillion cubic feet of natural gas, which could produce roughly 230 million tons of LNG.<sup>100</sup> As a point of comparison, the North West Shelf venture, Australia's largest and most economically significant natural resource project was at this time exporting 7 to 8 million tons of LNG per annum to Japan. Global demand for LNG currently stood at about 100 million tons per annum.<sup>101</sup>

Securing a market for the gas constituted the main problem, however. A variety of domestic supply options were being mooted to set the project in motion, which included both the supply of Timor Sea gas to a new methanol plant that the Canadian firm Methanex was proposing to build near Darwin as well as to the major markets in the south and southeast of the country.<sup>102</sup> Neither of these proposals were particularly commercially attractive for the oil companies – the latter, for example, could be achieved only by means of constructing an expensive and quite ambitious 2,000 kilometer pipeline to the onshore gas hub at Moomba in

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<sup>98</sup> 'Phillips-Multiplex execute Bayu/Undan pipeline agreement', *Australian Associated Press*, 13 September 2000.

<sup>99</sup> 'Darwin 10 MTPA LNG facility', Public Environmental Report, March 2002, prepared for Phillips Petroleum Company Australia Pty Ltd, by URS.

<sup>100</sup> Natural gas is liquefied to make it easier to transport if pipelines are not feasible, as across large bodies of water. According to the Petroleum Economist:

LNG has been the primary means of monetising remote gas for 40 years through the use of long-term contracts based on large, proven non-associated gas reserves. Prior to liquefaction, natural gas is treated by extreme cooling to -162°C (-256°F) for shipment and storage in specially insulated, pressurised containers. The liquefaction process, normally using non-associated natural gas as feedstock, removes oxygen, carbon dioxide, sulphur compounds and water. Compaction yields a volume reduction of 600 to 1 with a density of about one-half the weight of water. LNG is regasified (or revaporized) at LNG receiving (or import) terminals for final distribution to power stations for generating electricity, or supplied to domestic and industrial users as gas

'LNG Glossary', Petroleum Economist, July 2001.

<sup>101</sup> Petroleum Economist, 2001. *Fundamentals of the Global LNG Industry*, Petroleum Economist Ltd, London, p.10.

<sup>102</sup> 'Shell, Woodside and Methanex Announce Letter of Intent Natural Gas Supply for Proposed Syngas Facility', Woodside Media Release, 6 March 2000.

central Australia.<sup>103</sup> At this stage, however, the actual commercial viability of these schemes was more of a secondary concern – the overriding objective was to pressure the political stakeholders into action. To this end, the Letter of Intent between Phillips and Multiplex set a deadline of 31 July 2001. The implication of this agreement was that if all legal and commercial issues for the Timor Gap were not resolved by this time, the agreement would lapse and the second phase of the Bayu-Undan development would not proceed. The vested interests of the Northern Territory government in securing the downstream economic benefits from production in the Timor Sea meant that it could easily be controlled by the oil companies as an enthusiastic campaigner on their behalf. The landing of gas from the Bayu-Undan and Greater Sunrise fields onshore in Australia was seen by the Northern Territory government as being “the key prerequisite to enabling significant industrial growth in Darwin”.<sup>104</sup>

During September 2000, both the UNTAET Cabinet and the Australian federal Cabinet endorsed detailed mandates for the first round of formal bilateral negotiations, which had been scheduled to commence in Dili on 9 October. In a joint submission made to the UNTAET Cabinet on 16 September 2000, Galbraith and Alkatiri set out the reasons why their negotiating strategy should be endorsed:

Two courses of action are available to East Timor: litigation or negotiation. The purpose of litigation would be to establish a maritime boundary between East Timor and Australia where currently there is the Timor Gap (an area of joint development in which the boundary issue is put to one side). East Timor has a strong claim to a mid-point boundary which would accord it total control, and benefit from, petroleum reserves in the Timor Gap. Litigation would entail taking Australia to the International Court of Justice (ICJ). East Timor’s prospects of winning in the ICJ are excellent. However, the process could be lengthy and legal judgments, however strong the case, involve some risk. Negotiation would seek to gain for East Timor that which a positive court judgment would bring but without the cost and risk of litigation. Further, no agreement will be finalized with Australia that does not first receive the endorsement of the Cabinet. Once approved, such agreement would be signed

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<sup>103</sup> ‘Phillips-Multiplex execute Bayu/Undan pipeline agreement’, *Australian Associated Press*, 13 September 2000.

<sup>104</sup> Northern Territory Department of Mines and Energy, *Annual Report*, 2000/2001.

not by UNTAET but by the first government of an independent East Timor. If such agreement cannot be reached, the litigation option remains available (conversely, there can be no negotiation after litigation should East Timor first opt for the latter yet receive an unsatisfactory judgment).<sup>105</sup>

In their submission, Galbraith and Alkatiri highlighted the “monumental” financial implications of the resources at stake:

The Bayu-Undan gas recycle project in the Timor Gap, approved last February, was projected to bring over US\$600 million for East Timor over the next twenty years (based on US\$18/barrel and a 50/50 split with Australia). If there is a reallocation of the revenue split, then this could bring East Timor well over US\$1 billion. A continuation of current oil prices (US\$35/barrel) would double these projections. If this project progresses, as is probable, to developing the gas field, then this figure would significantly increase. Moreover, this is only one field: the development of a gas pipeline could turn the Timor Gap into a regional hub for gas development with significant benefits to East Timor for many years to come.<sup>106</sup>

To put these figures in some kind of context, the International Monetary Fund estimated the total amount of East Timor’s non-petroleum related public revenue in 2000 to be just US\$19 million, rising to US\$22 million in 2001.<sup>107</sup> Even with a continuation of the existing arrangements, therefore, petroleum revenues were expected to be substantially more than all the other sources of government income combined. Yet the true meaning of these resources to East Timor needs to be seen against the collapse of both the public and private sectors as a consequence of the violence during 1999, in conjunction with the large-scale destruction carried out in the wake of the referendum.<sup>108</sup> The extent of the devastation was immense. It caused a reduction by about a third of the territory’s GDP and an upsurge in urban

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<sup>105</sup> Joint Cabinet Submission, P. W. Galbraith and M. Alkatiri, 16 September 2000.

<sup>106</sup> *Ibid.*

<sup>107</sup> Sunley, E. M., Daniel, P., Mooij, H. and A. Schimmelpfennig, 2001. ‘East Timor: an agenda of petroleum fiscal issues’, International Monetary Fund, Fiscal Affairs Department, Washington, D.C.

<sup>108</sup> Report of the Secretary-General on the United Nations Transitional Administration in East Timor, 26 July 2000; UN doc., S/2000/738.

unemployment.<sup>109</sup> The process of post-conflict reconstruction and state building in East Timor would depend on the functioning of government institutions and the provision of basic public services – all of which would require significant fiscal resources over the long term. The Bayu-Undan project was East Timor’s best and possibly only hope of building state capacity to the level required for the functioning of the state.

The crucial challenge faced by the UN and East Timor would of course be that of overcoming the opposing interests of the Australian government, whose publicly stated approach to the negotiations was to “ensure that the Timor Gap Treaty continues”.<sup>110</sup> Yet in the weeks leading up to the start of negotiations, there was increased speculation as to the extent to which the Australian government might be prepared to make concessions to East Timor. Foreign Minister Downer sought to diminish these expectations, however. He warned that any re-adjustment of the treaty’s revenue sharing terms would have to be considered within the context of Australia’s level of overall aid to the new nation.<sup>111</sup> The linkage between the negotiation process and Australia’s foreign aid commitment to East Timor, alluding to the potential withholding of economic assistance or the threat of doing so, was an obvious bargaining lever that was available to the government. In Dili, the idea was denounced as a “crude, empty threat”.<sup>112</sup> Somewhat more invidiously, however, Australian “government sources” were also quoted as referring to the demands made by East Timor as being indicative of an emerging “cargo cult mentality” there.<sup>113</sup> UN and East Timorese officials were extremely insulted by these comments. Thus, by October 2000, the war of words had already begun and the stage was set for an intense confrontation; Australia’s goal of achieving a ‘smooth transition’ of treaty arrangements was now totally at odds with the desire in UNTAET to radically alter the Treaty’s key distributive components in East Timor’s favour.

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<sup>109</sup> World Bank, 2002. ‘East Timor: policy challenges for a new nation’, Report No.23285.TP, Washington, D.C.; also, Saldanha, J. M., 2000. ‘The transition of a small war-torn economy into a new nation: economic reconstruction of East Timor’, in R. Tanter, M. Selden and S. R. Shalom (eds) *Bitter Flowers, Sweet Flowers: East Timor, Indonesia and the World Community*, Pluto Press, Sydney.

<sup>110</sup> Senate Estimates Committee, Foreign Affairs, Defence and Trade, Committee Hansard, 23 November 2000, p.165-6.

<sup>111</sup> ‘Australia says Timor Gap talks tied to aid’, *Reuters*, 9 October 2000.

<sup>112</sup> ‘East Timor’s petro trouble’, *Business Week International Edition*, 30 October 2000.

<sup>113</sup> ‘Rewrite Gap treaty: opposition’, *Australian Financial Review*, 10 October 2000.



## CONCLUSION

The result of the 30 August referendum on self-determination in East Timor had striking consequences for the Timor Gap Treaty. If the outcome had been in support of the special autonomy proposal, the legal and administrative regime covering the Zone of Cooperation would have remained in force. Questions concerning the distribution of Indonesia's royalties or share of petroleum production, which may have arisen as a consequence of the introduction of special autonomy in East Timor, would have been an internal issue for Indonesia. However, with the complete transition of power in East Timor from Indonesia to UNTAET the situation became unpredictable. Indonesia instantly lost all authority to exercise jurisdiction off East Timor's coast, thereby rendering the Timor Gap Treaty null and void. This created considerable uncertainty regarding the future viability of the joint development regime and the management of existing contractual arrangements. For the many companies that had invested heavily in exploration and development in accordance with the provisions of the Timor Gap Treaty, there were serious concerns about the security of their investments.

This chapter has highlighted the intricate strategic interplay between four sets of actors – Australia, the UN, the East Timorese leadership and Phillips Petroleum – that occurred in response to this situation. Both the Australian government and Phillips considered that their interests would be best served through “a smooth transition” of treaty arrangements, by substituting Indonesia for East Timor in an otherwise unchanged Timor Gap Treaty. Two crucial decisions made by different actors worked both for and against this goal. The first of these was the decision by Phillips to press ahead with the Bayu-Undan project. In August 2004, I discussed this decision with James Godlove at some length. Godlove explained that the uncertain political environment following the referendum in East Timor made the investment an extremely risky proposition. In order to determine whether to proceed or not, he considered a range of “what if” scenarios. Although unwilling to disclose the full details of his analysis, Godlove drew the conclusion that the “project would drive the political process”.<sup>114</sup>

By committing to the project, Godlove reckoned that the firm's actions would increase the costs for all the parties concerned if the project then had to be suspended because of political unrest or legal uncertainties. The costs would be high for the Phillips-led joint

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<sup>114</sup> Pers. Comm. James Godlove, August 2004.

venture but, for East Timor, the consequences would be just as bad if not much worse. In other words, the investment decision raised the stakes, creating a massive economic incentive for both Australia and East Timor to work towards a political accommodation of their competing interests. For extra comfort, Godlove managed to secure a statement from Gusmão, Alkatiri and Ramos Horta of their intention to continue the company's production sharing contracts. The significance of the CNRT statement of 20 October 1999 is indicated by the fact that Godlove referred to it, during our conversation, as the "Magna Carta".<sup>115</sup> Before negotiations between UNTAET and Australia had even commenced, Phillips had made commitments for approximately US\$1 billion of equipment and services for the development of Bayu-Undan.<sup>116</sup> This was a major financial undertaking.

The second critical decision that acted *against* the goal of achieving a smooth transition of treaty arrangements, which was also analysed in some detail in this chapter, was the decision taken by UNTAET to challenge the Australian government to commence negotiations on a new regime. This was a purely strategic move. According to Erving Goffman, "during occasions of strategic interaction, a move consists of a structured course of action which, when taken, objectively alters the situation of the participants".<sup>117</sup> Once the decision had been taken, Australia was faced with a new set of strategic choices – a new reality, almost. This decision would have a major impact on the future course of events. It was the type of major strategic move, or key turning point, which has been described within the theoretical literature as an "action forcing event".<sup>118</sup> According to Michael Watkins, these are "specific breakpoints in the process which force negotiators to consider costs. Prior to the event, the cost of inaction may be low. But permitting the event to pass without taking action results in some or all negotiators incurring substantial costs".<sup>119</sup>

Galbraith presented the Australian government with two options: negotiate now, on UNTAET's terms, or risk a collapse in the offshore legal regime. He induced Australia to the negotiating table under conditions the government was unhappy with by making a commitment to a specific course of action that would have imposed severe costs on Australia if the request to open negotiations was rejected. Australia agreed to negotiate with UNTAET because the option of not doing so was perceived to be too risky, the potential costs too high.

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<sup>115</sup> *Ibid.*

<sup>116</sup> Godlove, J., 2000. 'Practical implications of East Timor's transition to the Timor Gap Treaty', *AMPLA Yearbook*, 2002, p.148.

<sup>117</sup> Goffman, E., 1969. *Strategic Interaction*, University of Pennsylvania Press, Philadelphia, p.145.

<sup>118</sup> Watkins, M. D., 1999. 'Building momentum in negotiations: time-related costs and action forcing events', *Negotiation Journal*, vol.14(3), p.250.

<sup>119</sup> *Ibid.*

Thus, the analysis of the events covered in this chapter present a study of strategic interaction. It shows how key actors used influence to pursue clearly defined objectives. Australia's objective was to encourage East Timor's succession to the Timor Gap Treaty but this clashed with UNTAET's objective of securing a larger share of Gap resources for East Timor. The incompatibility between UNTAET and Australia's objectives created a conflict and hence the need for negotiation. The main aim of this research is to examine how those negotiations unfolded and the reasons for why they unfolded in the way that they did. This is a task to which I shall now turn.

## 5. NEGOTIATIONS BETWEEN AUSTRALIA AND THE UN TRANSITIONAL ADMINISTRATION IN EAST TIMOR: OCTOBER 2000 TO JULY 2001

Negotiation may be conceived of as one of the “primary mechanisms” for managing or resolving conflict between individuals or social groups.<sup>1</sup> It is a constant social phenomenon because conflict itself is an ever-present feature of human society. Conflict arises whenever two actors are committed to pursuing a particular goal and cannot both attain that goal at the same time and to the same degree.<sup>2</sup> The mutual incompatibility of interests and objectives is essentially what characterises the dispute between Australia and East Timor. Australia’s desire for a “prompt and smooth transition” of the Timor Gap Treaty stood in stark contrast with UNTAET’s goal of devising a new regime that deviated substantially from the Timor Gap Treaty, one that reflected the “economics of a hypothetical mid-point maritime boundary”. Australia wanted to stick with the treaty they already had; Galbraith wanted to tear it up and start from scratch. The fundamental incompatibility between these policy objectives created a situation of conflict: negotiation offered a possible means of resolution. Thus, whereas the foregoing chapters of this thesis have laid the groundwork for understanding the circumstances surrounding these negotiations, the purpose of this chapter is to examine how they unfolded.

At the outset of any negotiation, there is no determinate solution but rather an indeterminate range of possibilities.<sup>3</sup> As Bacharach and Lawler have pointed out, “the interplay of potential bargaining power and tactical action transforms the bargaining outcomes into an emergent product of the bargaining process”.<sup>4</sup> Negotiation is very much a process of mutual influence, in which both parties exercise influence to induce the other side to make concessions and accept an agreement that meets their interests and needs.<sup>5</sup> And, as noted by Kelman and Fisher, “third parties also exercise influence in conflict situations by backing one

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<sup>1</sup> Kramer, R. M., 2004. ‘The ‘dark side’ of social context: the role of intergroup paranoia in intergroup negotiations, in M. J. Gelfand and J. M. Brett (eds), *The Handbook of Negotiation and Culture*, Stanford Business Books, Stanford, California, p.219.

<sup>2</sup> Munch, R., 1992. ‘Rational choice theory: a critical assessment of its explanatory power’, in J. S. Coleman and T. J. Fararo (eds), *Rational Choice Theory: advocacy and critique*, Sage Publications, California, p.142.

<sup>3</sup> Schelling, T. C., 1980. *The Strategy of Conflict*, Harvard University, Cambridge, Massachusetts, p.22.

<sup>4</sup> Bacharach, S. B. and Lawler, E. J., 1981, *Bargaining Power, Tactics and Outcomes*, Jossey-Bass, San Francisco.

<sup>5</sup> Kelman, H. C. and Fisher, R. J., 2003. ‘Conflict analysis and resolution’, in D. O. Sears, L. Huddy and R. Jervis (eds), *Oxford Handbook of Political Psychology*, Oxford University Press, Oxford, p.318.

or other party, by mediating between them, or by manoeuvring to protect their own interests.<sup>6</sup> In this chapter, I examine this complex interplay within the negotiations between Australia and the UN/East Timor. The aim is to understand the process by which the two parties moved from a situation of initially divergent positions to a common position. What, in fact, were the opening positions of the parties; and, what was the pattern of moves and concessions which enabled these opposing positions to converge? These are essentially descriptive questions, concerned purely with understanding what happened around the negotiating table. Analysis of the negotiation process involves a different set of questions, however: what were the principal underlying interests of the parties; how did they attempt to exert influence; what tactics did they use; what was the impact of these tactics; what effect did the actions of any third parties, outside of the negotiations, have upon the bargaining process; what were the major events and key turning points?

In investigating these questions, I have drawn extensively upon a variety of primary sources. The most important of these sources are the Minutes of the negotiations recorded by UNTAET. These highly confidential documents provide an extremely valuable resource which offers a rare and penetrating insight into the negotiations. Although not verbatim transcripts, the Minutes contain a comprehensive summary record, including direct quotations, of the verbal exchanges that took place around the negotiating table. Additional documents from the negotiations, including the various Drafts and revisions which the agreement underwent before being finally signed, have also been consulted. The chapter is organised principally around each of the formal and informal rounds that took place over a nine-month period between October 2000 and July 2001. I analyse the important developments that occurred both in and around these meetings. The chapter concludes with an appraisal and exposition of the basic analytical question regarding the causal links between bargaining context, tactics, process and outcomes.

### ***5.1 The Parties' Approach to the Negotiations***

Until the start of negotiations, the percentage distribution of the resources in the joint development zone had been seen as the principal issue in contention between Australia and East Timor. This had been the major aspect of the position hitherto adopted by UNTAET,

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<sup>6</sup> *Ibid.*, p.318-9.

both publicly as well as during the parties' two rounds of pre-negotiation discussions, in March and June, 2000. Indeed, in their submission to the UNTAET Cabinet, on 16 September 2000, Galbraith and Alkatiri had stated that "the basis of the talks will be the retention of the current joint management of all operations in the Timor Gap (currently through the Joint Authority) but with the revenue split between the two parties to greatly favour East Timor".<sup>7</sup> In the process of assembling the UN/East Timor negotiating team, however, Galbraith's own perceptions and understanding of the issues evolved. There were two areas, in particular, in which UNTAET's position underwent a major reformulation. These concerned the question of the lateral lines of the joint development zone and the issue of applicable law.

Initially, Galbraith had assumed that the lateral lines defining the eastern and western edges of the Zone of Cooperation were in about the right place. In Chapter Three, it was mentioned that these lines had originally been determined on the basis of equidistance between the territory of East Timor and Indonesia. It was also noted in Chapter Two that, whilst not being a rule of law, lines of equidistance have an inherent degree of fairness because they result in an equal division of any areas of overlap. Thus there was no immediate reason why anyone in the UN transitional administration should have questioned the validity of these lines. The western lateral of the Zone of Cooperation followed the line of equidistance as it projected seawards of the land frontier East Timor shares with Indonesian West Timor; and the eastern lateral extended seawards of a point midway between East Timor and Indonesia's Leti Island. The lines tapered inwards, or converged, because of the slightly concave shape of East Timor's southern coastline within the broader configuration of Indonesian territory, lying to the east and west. This convergence of lines contributed to the zone's coffin-like appearance. These lines were not legally opposable to an independent East Timor, yet, as things stood, they divided the seabed into separate spheres of joint Australian/UN control (inside the zone) and exclusive Australian jurisdiction (outside the zone).

The first indication that something might be wrong with these lines had occurred in June 2000, during a day-long seminar attended by UNTAET delegates at the Australian Institute of International Affairs in Canberra on the topic of "East Timor and its Maritime Dimensions". One of the presentations was given by Victor Prescott, an eminent political geographer, on "The Question of East Timor's Maritime Boundaries".<sup>8</sup> Following the

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<sup>7</sup> Joint Cabinet Submission, P. W. Galbraith and M. Alkatiri, 16 September 2000.

<sup>8</sup> The collection of papers that were presented at the seminar, including Victor Prescott's, was subsequently compiled within a book publication: Rothwell, D. R. and Tsamenyi, M., 2000. *The Maritime Dimensions of Independent East Timor*, Centre for Maritime Policy, University of Wollongong.

conclusion of the seminar, which had been timed to coincide with the second round of the parties' pre-negotiations, de Mello cabled UN Headquarters with the following report:

The seminar was interesting for the point raised by a political geographer that one part of the ZOCA [Zone of Cooperation Area A] boundary might need to be reassessed. He argued that the fixing of Point 16, marking the basis for the eastern boundary of ZOCA might not have taken into account Jaco Islet off East Timor's easternmost point. If that is the case, then this could push the eastern boundary of ZOCA as much as six miles eastwards and bring into the Zone a significant extra slice of the massive Sunrise-Troubadour gas field.<sup>9</sup>

Prior to the start of negotiations, however, this issue was revisited in meetings Galbraith had with Miguel Galvão-Teles and Nuno Antunes. Antunes had formerly served in the Portuguese navy and was known to Galvão-Teles as someone who specialized in ocean cartography and maritime delimitation law. During their discussions, it was explained to Galbraith that whilst equidistant lines represented one method of constructing the lateral lines, alternative methods of delimitation could be used to expand the seabed claims of an independent East Timor to include areas outside the existing Zone of Cooperation to the east and west. Antunes advocated the method of constructing two parallel lines drawn perpendicular to the general direction of Timor's "wider regional façade" that fronts onto the Timor Sea.<sup>10</sup>

The United Nations *Handbook on the Delimitation of Maritime Boundaries* describes the 'parallel lines' technique as a simplified form of the equidistance method, which is based on considerations of equity.<sup>11</sup> It consists of "two parallel straight lines producing a long narrow band of maritime space in order to avoid the cut-off effect produced by the convergence of equidistant lines in front of the coast of one of the parties".<sup>12</sup> Antunes' thinking on the topic of East Timor's potential maritime boundaries was articulated in a book

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<sup>9</sup> Cable from S. V. de Mello to B. Miyet, 'Timor Gap Talks' (14-15 June), 19 June 2000.

<sup>10</sup> Antunes, N. M., 2004. *Towards the Conceptualisation of Maritime Delimitation: legal and technical aspects of a political process*, Brill Academic Publishers, Leiden, The Netherlands, p.400. See, also, Antunes, N. S. M., 2003. 'Spatial allocation of continental shelf rights in the Timor Sea: reflections on maritime delimitation and joint development', *Centre for Energy, Petroleum and Mineral Law and Policy Internet Journal*, vol.13.

<sup>11</sup> United Nations, Office of Legal Affairs, Division for Ocean Affairs and the Law of the Sea, 2000. *Handbook on the Delimitation of Maritime Boundaries*, United Nations Publications, New York, p.56, 61.

<sup>12</sup> *Ibid.*, p.61.

on the technical and legal aspects of maritime delimitation that he published in 2003.<sup>13</sup> He observed that if this technique was used to delimit the lateral lines, the outcome would be a “rough” 50-50 division of Greater Sunrise between Australia and East Timor and the whole of the Laminaria, Corallina and Buffalo oil fields would be attributed to East Timor.<sup>14</sup> The notion that other techniques and methods of line construction could be used to delimit the lateral limits of the joint development zone was a revelation for Peter Galbraith and one that carried huge significance. The Laminaria and Corallina fields were located just a few miles west of the existing zone. They contained about 200 million barrels of oil and had been brought into production under Australian license in November 1999 at a rate that peaked at between 170,000 and 180,000 barrels per day. By the end of 2000, these fields were producing approximately 25 to 30 per cent of Australia’s total output of crude oil. The idea of ‘opening the laterals’ therefore was one that potentially had enormous strategic and economic consequences.

In addition to the question of the laterals, another new aspect of UNTAET’s position that emerged in the lead up to the negotiations related to questions of legal authority and the political control of the petroleum production regime. This issue came to prominence during a crash course on petroleum law given to UNTAET by the Norwegian Petroleum and Energy Ministry, in the first week of October 2000.<sup>15</sup> The Norwegian government has some of the greatest experience in the world in dealing with the trans-boundary management of oil and gas resources, as the bulk of the country’s North Sea gas reserves are exported to other European countries through a network of sub-sea pipelines. The UN team learnt that in order for East Timor to be able to benefit most from petroleum development, it should ideally have control over the internal fiscal arrangements of the zone (that being, all taxes, royalties, cost recovery provisions, profit oil splits, the contractual and legislative aspects of petroleum operations etc.) as well as jurisdiction over any pipelines built to transport gas from within the zone to areas outside.<sup>16</sup> The issue of pipeline jurisdiction was especially pertinent, given that both the Bayu-Undan and Greater Sunrise projects had been conceived on the basis of piping the gas to Australia.

Yet, to control the production regime would require legal authority, which would have strong connotations of sovereign jurisdiction; and sovereignty was precisely the issue in

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<sup>13</sup> Antunes, 2004, *op.cit.*

<sup>14</sup> *Ibid.*, p.399.

<sup>15</sup> Cable from S. V. de Mello to B. Miyet, ‘Timor Gap – First round of formal negotiations’ (Dili 9-12 October), 12 October 2000.

<sup>16</sup> *Ibid.*



dispute. Under the terms of the 1989 Treaty, the production regime of the joint development zone was controlled by a Petroleum Mining Code, which formed an annex to the treaty. It could be amended only with the approval of the Ministerial Council – a bilateral institution. In this way, Indonesia and Australia each retained legal authority over the zone, consistent with the principle of sovereign neutrality. If the applicable law in the zone were to be made East Timorese law, it would not only mark a radical departure from this principle but would also significantly undermine Australia’s political control of resource developments in the region.

Thus, in the lead up to the first round of formal negotiations in October, UNTAET’s position underwent a major revision. Much more than a percentage re-distribution of Timor Gap resources, it would also include the question of applicable law and concepts of pipeline jurisdiction, as well as the re-definition of the area in question. The Australian government’s basic goal remained that of obtaining an agreement that minimised any changes to the existing regime to the greatest extent possible. There was no expectation that UNTAET would be seeking to achieve anything other than a re-distribution of revenues and it was assumed that, with perhaps some minor changes, the existing regime could be maintained.<sup>17</sup> However, it was also recognised that novel arrangements would be required in respect of the taxation and administration of gas developments in the Zone of Cooperation. The Timor Gap Treaty had, in fact, been designed only to cover production of crude oil. Yet most of the hydrocarbons that had been discovered within the treaty area had been natural gas. The companies that were principally involved, Phillips and Woodside, wanted a swift resolution of the gas fiscal regime to enable their projects to move forward. In June 2000, James Mulva, Chairman and Chief Executive Officer of Phillips Petroleum, stated that: “the current terms of the treaty provide a clear fiscal regime for oil development within the Zone of Cooperation, but not for gas development. To date, there has been no agreement on how or where gas will be valued. This is unsettling to producers and potential customers and could delay gas development”.<sup>18</sup>

The complex nature of these issues was highlighted in a report produced by the Australian-based Centre for International Economics (CIE), released in October 2000, on the *Impact of the Sunrise Gas Development on the Northern Territory and Australian Economies*. The report also stated that in order to most efficiently develop the Sunrise resource, an international unitisation agreement would need to be negotiated by Australia and East Timor. Unitisation was required because “a proportion of Greater Sunrise lies outside Australian

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<sup>17</sup> Pers. Comm. Senior Australian Government Official, November 2005.

<sup>18</sup> Speech given at the South East Asia Australia Offshore Conference 2000, at Darwin, 26 June 2000.

territorial waters in the Zone of Cooperation to be jointly administered by the United Nations Transitional Authority in East Timor (UNTAET) on behalf of East Timor and Australia”.<sup>19</sup> The CIE report underlined the massive sums of money that were potentially at stake. Total direct and indirect tax revenues flowing to the Australian federal government as a result of the proposed Woodside/Shell/Methanex project were calculated to be about \$1.6 billion over the period 2012 to 2025.<sup>20</sup> This was in addition to other economic gains for the Northern Territory from the construction of offshore and onshore facilities valued at US\$4.7 billion. Yet everything hung on the outcome of the political negotiations. In the absence of a treaty providing a stable legal, fiscal, administrative and regulatory framework, neither the Sunrise Project nor Bayu-Undan would be able to progress to the point at which hydrocarbons could be produced.

### ***5.2 The First Round – Dili, 9-12 October, 2000***

The first round of formal negotiations between UNTAET and Australia commenced on 9 October 2000, in Dili. Peter Galbraith led the UN/East Timor side, which included Mari Alkatiri, Mario Carrascalão (Vice President of CNRT), Alexander Nicholas (UNTAET’s Deputy Principal Legal Advisor), Miguel Galvão-Teles and Nuno Antunes. The leader of the Australian delegation was Michael Potts. Other members of the Australian team included John Hartwell, Bill Campbell (Attorney General’s Department), James Batley (Head of the Australian Mission to East Timor) and officials from the Department of Foreign Affairs and Trade, the Department of Industry, Science and Resources, the Australian Surveying and Land Information Group and the Northern Territory government. The negotiations were opened by Xanana Gusmão, who “expressed the desire to see the talks mark the beginning of a new relationship between Australia and East Timor in which the two countries could address each other as equals”.<sup>21</sup> He also gave his full endorsement to the joint UN/East Timor negotiating team.

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<sup>19</sup> Centre for International Economics, ‘Impact of the Sunrise Gas Development on the Northern Territory and Australian economies’, a paper prepared for the Office of Resource and Development (Northern Territory Government), Woodside and Methanex, October 2000, p.12.

<sup>20</sup> *Ibid.*, p.viii.

<sup>21</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 9 October 2000.

Following Gusmão's introductory comments, Galbraith proceeded to explain the basis of UNTAET's negotiating position. He started by referring to the UNTAET Cabinet's support of the proposal, included within the 20 September submission, "to obtain for East Timor the royalty and tax revenues from petroleum north of the mid-point between Australia and East Timor, in lieu of litigating for a mid-point maritime boundary".<sup>22</sup> He also stated that:

A fundamental premise of these negotiations is that the 1989 Timor Gap Treaty, in all its aspects, is invalid and therefore will not be used as a basis for negotiations. These negotiations are starting with a clean slate. The talks do not seek to re-negotiate the previous regime and nothing said should be interpreted within the context of the former Timor Gap Treaty.<sup>23</sup>

On the specific elements of UNTAET's position concerning the revenue split and legal arrangements for petroleum activities, Galbraith stated:

East Timor has a claim to sovereign rights north of the median line. We would be happy to discuss East Timor's overall legal case in this regard, including with reference to the Law of the Sea and recent case law. We are also prepared to present geological research demonstrating that East Timor and Australia sit on the same continental margin. However, following the two previous rounds of pre-negotiations in Australia, East Timor recognises Australia's overriding goal to avoid a maritime delimitation and, in lieu of this, though it is East Timor's clear preference to obtain a maritime delimitation, East Timor is prepared to set aside or freeze its maritime claims and accept a single purpose jurisdiction giving East Timor jurisdiction over petroleum resources and activities north of the median line...East Timor seeks a revenue split to reflect its legal entitlement north of the median line – namely, 100 percent of royalties and 90 percent of taxes. In other words, East Timor should receive royalties and taxes from petroleum activities commensurate with having – or, as if it had – sovereign rights north of the median line. To the extent that Australia

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<sup>22</sup> *Ibid.*

<sup>23</sup> *Ibid.*

remains willing to share taxes south of the median line – what is currently Zone B – East Timor does not seek 100 percent of the taxes to the north.<sup>24</sup>

The Australian team did not initially respond with a counter-proposal. Instead, Potts explained that his side had been given a mandate to “explore” UNTAET/East Timor’s requests, where possible “make reactions” and, “within certain parameters put some concepts on the table”.<sup>25</sup> However, he stated that “Australia was not yet in a position to talk in concrete terms”.<sup>26</sup> Potts reacted strongly to the concept of ‘single purpose jurisdiction’ put forward by Galbraith. He described the offer as “staggering and difficult even to serve as a basis for discussion”; “radical beyond acceptability”; “un-saleable”; “unappetizing”; “another form of sovereign delimitation that is not publicly so but which delivers the same benefits to East Timor”; a “conjuring trick”; and, “nowhere near Australia’s understanding of joint development”.<sup>27</sup> He argued that it departed from the understanding reached during the parties’ earlier meetings that the basis for negotiations would be the continuation of joint development. The UNTAET proposal created uncertainty as to the role, if any, Australia would have in the administration of the zone; and it did not reflect “Australia’s interests in Zone A”. Potts dismissed the need for any discussion of the principles of international law concerning permanent sovereignty. For to do so would be a “pointless digression”, given that Australia’s position was diametrically opposed. He further warned that the “clean slate” approach adopted by UNTAET might mean that agreement was several years away.<sup>28</sup>

Notwithstanding this fairly vigorous response, there were subtle indications that the Australian team had a limited degree of flexibility. Whilst Australia was “satisfied” with the current regime, Potts “realized that this was not a viable position”.<sup>29</sup> Furthermore, he explained that Australia “understood East Timor’s legitimate concerns over the possibility of deadlock in the decision-making process of joint development but believed that there were ways to address these”.<sup>30</sup> Galbraith maintained that central to East Timor’s concerns was the need for “ultimate control of the territory within its legal entitlement” and that he and Mari Alkatiri would “have difficulty in persuading the East Timorese to accept a deal that would be

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<sup>24</sup> *Ibid.*

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*

<sup>27</sup> *Ibid.*

<sup>28</sup> *Ibid.*

<sup>29</sup> *Ibid.*

<sup>30</sup> *Ibid.*

significantly different from that which they could obtain in court”.<sup>31</sup> Galbraith did not directly threaten Australia with litigation but continued to emphasise the fact that if negotiations failed, East Timor had alternative means for achieving what it wanted. Hence, whilst the preference in East Timor was to avoid litigation, “the issue was how much UNTAET/East Timor would be prepared to pay now to avoid going to court”.<sup>32</sup> Potts warned that litigation would be extremely costly for East Timor, as it would delay further exploitation of the region’s hydrocarbon resources.<sup>33</sup>

On 10 October, the discussions centred upon the meaning of UNTAET’s concept of ‘single purpose jurisdiction’. The Australian side wanted clarification of what it implied. UNTAET explained that whilst it allowed for concurrent jurisdiction with regard to certain issues, such as surveillance, customs and immigration, quarantine and so forth, all decisions regarding petroleum activities north of the mid-point would be based on East Timorese law and “ultimate authority in the event of political deadlock over a particular decision would be exercised by East Timor”.<sup>34</sup> The Australian team viewed this as tantamount to sovereignty “under a different name” and argued that “Australia would be reluctant to cede control in an area of overlapping claims”.<sup>35</sup> Galbraith responded that the “core choice for Australia was whether its interest in avoiding a situation which prejudiced its claims to sovereign rights were best served by an agreement which tried its utmost to accommodate Australia or by the outcome of litigation on the question of maritime delimitation”.<sup>36</sup> Potts acknowledged that the status quo was unacceptable for East Timor but that the proposed changes may be too much for the Australian people and Ministers “who might view East Timor as ungrateful and asking for too much”.<sup>37</sup> Talks were adjourned early on 10 October to allow the Australian delegation to consult Canberra on UNTAET’s request to hear Australia’s concrete offer on revenue distribution.

On 11 October, Potts disclosed the terms of Australia’s offer: it amounted to a readjustment of the revenue distribution for Area A, of two-thirds to East Timor and one-third to Australia. He stated that this offer was made “on the basis that the fundamental aspects of

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<sup>31</sup> *Ibid.*

<sup>32</sup> *Ibid.*

<sup>33</sup> *Ibid.*

<sup>34</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 10 October 2000.

<sup>35</sup> *Ibid.*

<sup>36</sup> *Ibid.*

<sup>37</sup> *Ibid.*

the 1989 Treaty should remain unaltered”.<sup>38</sup> In addition, the Australian delegation had prepared a draft proposal for a mechanism for the settlement of disputes between Australia and East Timor. Potts explained that this had been produced in appreciation of the concerns regarding decision-making in the treaty and the “potential adverse impact on the development process in East Timor” as a result of political deadlock over key administrative decisions.<sup>39</sup> Galbraith did not respond directly to the specific content of Australia’s offer but, instead, completely shifted the direction of the negotiations. He stated that UNTAET was approaching the question of the revenue share using East Timor’s legal entitlement as a starting point and that it would be difficult to accept a proposal that was much below that threshold. However, referring to the existing lines of the joint development zone, he explained that East Timor did not accept Australia’s and Indonesia’s views as to what constituted East Timor’s maritime entitlement. At this point, Galbraith invited Nuno Antunes to give a detailed presentation of the legal principles underlying East Timor’s claims to jurisdiction in the Timor Sea, including the different techniques that could be used to define the lateral boundaries. In his presentation, Antunes referred explicitly to the fact that Article 3 of the 1972 Seabed Treaty between Australia and Indonesia acknowledged that the boundary line in the vicinity of points A15/A16 and points A17/A18 might have to be redefined to accommodate the claims of third states.

The Australian team responded to the points of law put forward by Antunes and rejected them all, re-iterating that Australia was convinced that there were two continental shelves and thus did not accept any other argument. Potts stressed that “the introduction of the lateral boundaries involved huge issues that were outside the scope of the mandate of the Australian team which had come prepared only to negotiate on the basis of the conditions of the existing ZOCA arrangements”.<sup>40</sup> He continued: “the cleaner the slate the more complex the negotiations” and he affirmed that from the point of view of the Australian government the question of the lateral boundaries had been “settled”.<sup>41</sup> Galbraith responded that he did not understand how this issue could be settled when the 1972 Treaty entertained the possibility of an alteration to the lateral lines and when it was known that UNTAET and East Timor did not consider the 1989 Treaty to be valid. Potts repeated that “the question of the change in the lateral boundaries would raise the stakes considerably and would seriously put at risk the

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<sup>38</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 11 October 2000.

<sup>39</sup> *Ibid.*

<sup>40</sup> *Ibid.*

<sup>41</sup> *Ibid.*

possibility of concluding a treaty before independence”.<sup>42</sup> He described the UNTAET/East Timor proposal as “extreme” and “advised his counterparts to consider carefully how their position would be perceived in the public domain”.<sup>43</sup>

Galbraith noted these concerns but emphasised that “there were two issues which needed to be looked at from different perspectives. First, there was the issue of what regime to apply to a joint area; this was an economic and jurisdictional matter. Secondly, there was the issue of defining the area in question”.<sup>44</sup> Whilst recognizing that the task of securing a regime by independence posed challenges, he reminded the Australian delegation that the questions under discussion had long term implications for the new state of East Timor. UNTAET, in its role as advisor to the East Timorese leadership, “could not ignore the evidence that the maritime boundaries were wider than those proposed by Australia. The drawing of the lines could have implications involving a billion dollars of revenue”.<sup>45</sup> Galbraith repeated that East Timor was not proposing a change to the boundaries as they did not in fact exist, given the illegality of the 1989 Treaty. Potts quickly responded to what he described as the level of “rigour and ambition” reflected in these demands and immediately requested “a clear expression of the totality of East Timor’s claim”.<sup>46</sup> He warned Galbraith that his “macho attitude” meant that it might be better to take the matter to court as “the issue was now beginning to register on the Geiger counter of sensitivity back in Canberra”.<sup>47</sup>

From the perspective of the Australian team, the situation was getting progressively worse as the scope of UNTAET’s demands expanded. The next agenda item concerned the actual regime of petroleum production. There were a number of technical issues related to the production and export of natural gas from the zone which the companies wanted resolved. These included the regulatory arrangements under which a gas pipeline could be constructed and operated, the fiscal treatment of the gas pipeline and the point of gas valuation. The valuation point was crucial because it controlled the means of determining the value of the gas for the purposes of revenue sharing (between the operator and the government) as well as corporate income tax. There was a huge difference between paying royalties on the value of the gas at the well-head than at the outlet flange at the onshore terminal. The Australian team initially suggested that the existing regime for crude oil production could be used as the model

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<sup>42</sup> *Ibid.*

<sup>43</sup> *Ibid.*

<sup>44</sup> *Ibid.*

<sup>45</sup> *Ibid.*

<sup>46</sup> *Ibid.*

<sup>47</sup> *Ibid.*

and that gas could be valued at the production sharing contract boundary. However, UNTAET adopted a radically different position, which mirrored the Norwegian system. To describe how this worked, Galbraith introduced Bjorn-Erik Leerberg, a private petroleum legal consultant, based in Oslo, whom Galbraith had brought in as an adviser to the UN team.

Leerberg explained that, under the Norwegian model, the government's jurisdiction extended over any pipelines used to transport gas from Norway to an importing state, so that the transfer of title and the point of gas valuation occurred at the outlet flange of the landing terminal. Bilateral treaties between Norway and the importing states had been necessary to achieve this arrangement. It was designed to extend the reach of Norway's taxation rights and jurisdiction to the greatest extent possible. The pipeline would be a critical piece of infrastructure for the development of the Timor Sea, enabling abundant yet geographically remote gas reserves to be gathered at a central hub on Australia's northern shore. The Australian team interpreted the Norwegian model as simply another attempt by UNTAET to claim more of the fiscal revenues at Australia's expense. Hartwell responded that the Norwegian regime would "pose difficulties" for Australia, as it implied "an extension of Joint Authority jurisdiction into its own waters".<sup>48</sup> Galbraith pointed out that, under international law, a pipeline does not enter Australian waters when it leaves the joint development zone but only at the point at which it enters Australia's twelve-mile territorial sea.

The last major issue discussed during the first round related to the question of Sunrise unitisation. Unitisation is a standard procedure that is applied to resource deposits that straddle a jurisdictional boundary. International unitisation means that the revenues from a reservoir are shared proportionate to the geographic distribution of the field, so that neither country has an incentive to increase their share by accelerating production on their side of the line.<sup>49</sup> Such rules govern the extraction from several reservoirs that cross the Norwegian-British boundary in the North Sea. Sunrise was unusual, however, in that it straddled a temporary line between a state and a joint development zone. The issue was therefore quite complex. From UNTAET's perspective, it was contingent upon the determination of the boundary lines of the zone. The Australian team commented that it would be necessary, however, to "establish procedures with which the commercial operators would feel confident".<sup>50</sup> As a result, it was decided that two working groups should be set up to carry

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<sup>48</sup> *Ibid.*

<sup>49</sup> Hanneson, R., 1998. *Petroleum Economics: issues and strategies of oil and natural gas production*, Quorum Books, Westport, Connecticut.

<sup>50</sup> *Ibid.*



work forward on several matters related to petroleum pipelines, gas fiscal arrangements as well as unitisation. Galbraith affirmed that it would be difficult to conclude the unitisation agreement until the boundaries were known of the areas that needed to be unitised. He agreed, however, that one could first establish the basic principles by which unitisation could be carried out.

Following the conclusion of the third day of talks, the UNTAET negotiating team met with Xanana Gusmão at the CNRT Headquarters in Dili, to brief him on the current status of the negotiations. Galbraith confirmed that the offer tabled by the Australian delegation was a two thirds/one third division of revenues in favour of East Timor as against the existing 50-50 split. Whilst this constituted an important early gain for East Timor, he emphasised that a considerable difference still existed on a range of questions between the two sides. Gusmão was advised that “litigation would probably have to at least be initiated to convince the Australians of the determination of the UNTAET negotiating team to press for the full entitlement of East Timor in the petroleum resources of the Timor Sea”.<sup>51</sup> On 12 October, a final session was convened to approve an Aide Memoire, providing a record of what had been discussed and the outcomes reached. Potts requested that details of the parties’ respective offers be omitted given that the document was “bound to end up in the hands of the media”.<sup>52</sup> Galbraith insisted on including UNTAET’s offer within the document, which the Australians accepted. However, Potts asked that with regard to Australia’s offer, reference be made to the fact that “Australia had made an offer which was known to both parties without specifying any details”.<sup>53</sup> The Aide Memoire was signed by the two Heads of Delegation: Michael Potts for Australia and Peter Galbraith for UNTAET. At the conclusion of the meeting, Potts stressed “the problems that he and his delegation would have in presenting to their ministers what he considered to be a proposal [by UNTAET] relating to Australian sovereignty without a clear indication of the areas involved”.<sup>54</sup>

On 19 October 2000, Galbraith and Alkatiri made a joint submission to the UNTAET Cabinet on the outcome of the first formal round of talks. They expressed the view that Australia’s initial offer had been “seriously inadequate”, given that it reflected “significantly less than that which a court would be almost certain to accord East Timor if the matter was resolved through litigation in light of the strength of East Timor’s claim to everything north of

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<sup>51</sup> Meeting with Xanana Gusmão regarding the Timor Gap Negotiations with Australia, 11 October 2000.

<sup>52</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 12 October 2000.

<sup>53</sup> *Ibid.*

<sup>54</sup> *Ibid.*

the mid-point”.<sup>55</sup> It was noted that the offer had three main shortcomings: “East Timor would not receive a sufficiently high proportion of the revenues; the area of Timor Sea in question would be unduly circumscribed; and, the management of that area would give undue control to Australia”.<sup>56</sup> As Galbraith was quite skeptical of being able to resolve all these matters satisfactorily within the time available, Cabinet was advised to make the necessary preparations for instituting legal proceedings immediately following East Timor’s date of independence. This was also recommended as a tactical move, “in order to demonstrate the strength of East Timor’s legal case, as well as its commitment towards insisting on a fair outcome to the negotiations”.<sup>57</sup>

The Australian team faced just as daunting a challenge. Prior to the talks, they had anticipated that negotiations would be conducted on the basis of the original treaty. It was now apparent that the parameters had changed. Galbraith had broadened the scope of East Timor’s demands to such an extent that the chances of achieving a continuation of the Timor Gap Treaty, albeit with minor amendments, appeared highly remote. The Minutes of the discussions convey important elements of the parties’ negotiating strategies and influence tactics. Galbraith had assembled a small group of international experts with whom he was able to develop a well-planned and organised negotiating position. He had intentionally staggered the disclosure of UNTAET’s terms over three days, which ensured that Australia made the first big concession – that being, a shift in the revenue split from 50-50 to two thirds/one third – only to then realise that the gap between the parties’ respective positions was much wider than initially expected. The negotiating style employed by Galbraith served a single purpose: namely, to convince the Australian team of the strength of UNTAET’s determination and thus to diminish their expectations of what could be achieved in the negotiations. In this, he was highly successful. Australia’s negotiators left Dili with a completely different perception of what they believed Australia would ultimately have to given up in order to reach an agreement.<sup>58</sup>

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<sup>55</sup> Joint Cabinet Submission, P. W. Galbraith and M. Alkatiri, 19 October 2000.

<sup>56</sup> *Ibid.*

<sup>57</sup> *Ibid.*

<sup>58</sup> Pers. Comm. Senior Australian Government Official, November 2005.

## Aide Memoire

The first formal round of negotiations between UNTAET, acting on behalf of East Timor, and Australia for an arrangement relating to petroleum activities in the area of the Timor Gap was held in Dili, East Timor, from 9-12 October, 2000. A list of delegations of the parties is attached at Annex A. The parties agreed to work towards a petroleum arrangement relating to the Timor Gap. Both parties agreed on the need to ensure a transparent and secure climate for investors in the area of the Timor Gap. They differed, however, on the approach to be taken in developing such a treaty. Each of the parties identified and explained its major issues in negotiations, namely:

- Revenue split, as to which each party made its own proposal;
- Allocation of jurisdiction;
- Concepts of joint administration;
- Definition of the area or areas in question;
- Gas pipeline regime/gas fiscals;
- Unitisation;
- Development of domestic framework; and,
- Industry and petroleum activities to be undertaken in East Timor.

A working group was established to carry work forward on petroleum pipelines, gas fiscals, unitisation and related matters.

### UNTAET, acting on behalf of East Timor, proposed that:

- The fundamental premise is a clean slate;
- The talks do not seek to re-negotiate on the basis of the 1989 Timor Gap Treaty, because that treaty was entered into with Indonesia, which did not have sovereign authority over East Timor and thus did not have authority to compromise the interests of East Timor;
- The question of sovereign rights be set aside for the purpose of these negotiations;
- A single purpose jurisdiction line be adopted for petroleum resources and production, and petroleum related activities, at the median line between the coastlines of Australia and East Timor, with lateral limits to be negotiated;
- East Timor receives the royalties and 90 percent of the tax revenues north of the median line; and,
- As many elements of jointness as possible be adopted.

### Australia proposed:

- That a new petroleum arrangement should be based upon the agreement between UNTAET, acting on behalf of East Timor, and Australia, signed on 10 February, 2000, with minor changes as necessary to update it. Arrangements under these terms had worked well and provided a stable investment climate irrespective of their origin;
- That the area which is the subject of the negotiations be defined by the limits of the existing Zone of Cooperation;
- That a new dispute resolution mechanism be established according to a specific proposed text. This was to meet East Timor's concerns on potential deadlocks resulting from consensus decision-making; and,
- A revenue split which is known to both parties.

The parties agreed that this formal exchange of views about future arrangements relating to the area of the Timor Gap had clarified respective positions. Both parties acknowledged the importance of this issue for the future benefit of both parties and regarded these talks as helpful and constructive. Further detailed discussions, however, will be required. The timing and venue for the next round of negotiations is to be decided through diplomatic channels and is to take place as soon as practicable. The parties also confirmed the confidentiality of the negotiations.

The Minutes do not, however, adequately communicate the intense, emotional nature of the talks. In the course of this research, I have spoken at length to two members of the Australian delegation, at different times, about their recollections of the crucial first round in Dili. Both referred to Galbraith's highly emotive rhetoric and his aggressive, verbal attacks on the Australian team. Galbraith's technique had the characteristics of psychological warfare. He dispensed with the diplomatic protocol of not allowing personal feelings, attitudes or animosities to intrude upon the talks. Quite the opposite, he openly conveyed his dislike of the Australian government, thus making it uncomfortable and difficult for those on the Australian team. He found it useful to convey a sense of outrage. He wanted to create the impression of a hostile opponent that would not be easily moved. According to Bacharach and Lawler, "a critical task" for bargainers, in any negotiation, "is to translate the environmental resources and constraints into tactical action at the bargaining table".<sup>59</sup> To be sure, Galbraith's ability to take such a hard line in the negotiations stemmed from a firm and widely held belief in Dili that East Timor had an "open and shut case" to a median line boundary coupled with a confidence that, if negotiations failed, legal avenues remained available.<sup>60</sup>

On the question of East Timor's median line claim, there was absolute unity amongst the East Timorese leadership. During the negotiations, Alkatiri had asserted that "UNTAET had made it clear from the beginning that the starting point would be boundaries – not simply some kind of revenue split – and thus the offer of only a jurisdictional line was in fact a concession by East Timor".<sup>61</sup> Gusmão had also notified the Australian team that although they may feel as though they have limited room for manoeuvre, "it would be difficult to explain to his people that it did not have possession of that which was theirs".<sup>62</sup> Peter Galbraith gave a strategic dimension to this unity of purpose. His extensive negotiating experience in some of the toughest regions of the world, including the Balkans and the Middle East, gave him an edge over some of even the most experienced senior bureaucrats within the Australian government. For their part, the Australian side sought to make two points: that Australia had an entirely "legitimate interest" in maximising benefits accruing to it from exploration and exploitation of its "adjacent marine areas";<sup>63</sup> and to warn UNTAET that in attempting to make radical changes, they could risk losing everything. Indeed, the logic and

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<sup>59</sup> Bacharach and Lawler, 1981, *op. cit.*, p.41.

<sup>60</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 10 October 2000.

<sup>61</sup> *Ibid.*

<sup>62</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 9 October 2000.

<sup>63</sup> *Ibid.*

intent behind much of what was actually communicated by both sides during the first round, can largely be understood in terms of mutual attempts to manipulate perceptions and thus to alter the parameters of each side's decision-making. Australia's warnings were deployed to create changes in UNTAET's level of motivation, whilst in demonstrating commitment, UNTAET sought to influence the Australian side's perception of what could be achieved.

### ***5.3 Singapore and Cairns, November-December 2000***

After the first round of negotiations, Australian officials refused to be drawn publicly on the substance of each side's negotiating positions. The secrecy surrounding the content of the discussions led the *Sydney Morning Herald* to report that "the Howard Government is attempting to conceal its bid to minimise East Timor's share of Timor Sea mineral wealth because it would be unpopular domestically where there is strong support for the long suffering East Timorese".<sup>64</sup> Galbraith was somewhat more outspoken, however. On 16 October, he told the media that "East Timor has clear entitlements under international law and I doubt the East Timorese are likely to accept something less than they are entitled to... To be honest, the United Nations could not reconcile and I personally could not reconcile accepting something the East Timorese could not accept, something that was not comparable to that which they are entitled".<sup>65</sup>

The Australian Cabinet was shocked and extremely unhappy with the outcome of the Dili talks and particularly troubled by Galbraith. The government was alarmed at Galbraith's aggressiveness and the scope of his demands and indignant at the tactics he employed. This was conveyed forcefully to Sergio Vieira de Mello. On 22 October, de Mello travelled to Canberra for a round of high-level meetings for the purpose of discussing operational aspects of the ongoing peacekeeping mission in East Timor. However, he found that the "key preoccupation" of the Ministers he spoke with concerned the Timor Gap negotiations. Following his return to Dili, de Mello cabled Bernard Miyet with the following report of what had been expressed:

I was told that Australia was "disconcerted" coming out of the recent negotiations in Dili by the wide ambit of UNTAET and East Timor's position

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<sup>64</sup> 'Timor's oil and gas share 'must be seen to be fair'', *Sydney Morning Herald*, 17 October 2000.

<sup>65</sup> *Ibid.*

as embodied in the “clean slate” approach. While Downer and Dauth<sup>66</sup> repeatedly stated that Australia was committed to an outcome to the negotiations that was “generous” to East Timor, they would not agree to anything that raised the risk of Indonesia seeking to re-open negotiations on its maritime boundary with Australia. They were further agitated by press reports that the matter could be taken to the ICJ if East Timor did not receive a satisfactory settlement.

...I noted that the issue of the Timor Gap was a matter of East Timor’s survival. Further, I stressed that our negotiating team was seeking only to defend and maximise East Timor’s interests and that our stance should in no way be interpreted as hostile (indeed, Downer noted that economically the issue was not crucial to Australia's GDP but was to East Timor’s). Rather, I said that I strongly hoped that the Timor Gap talks could be treated for what they were: namely, a commercial dispute between two friendly neighbours. I suggested, and Downer and Howard agreed, that the next step should comprise an informal round of talks, out of the media glare, in which the two sides could seek to better understand the other's positions and some common ground could be sought. Finally, I noted that comments by UNTAET officials about recourse to the ICJ had been made only in response to media queries and concerned East Timor's, not UNTAET’s right to seek that course of action.

...In short, this issue has elicited a strong – even strident – reaction from Downer and his department. Clearly, this was as much a tactic designed to bring about a softening of our position as it was a genuine response to the stance we are adopting. There will likely be more such vigorous interventions as the months proceed and the negotiations develop and it will be important for us to hold the line. In both law and fact East Timor’s position is a strong one. Furthermore, it is a position that is shared by the East Timorese leadership and which has been the subject of lengthy Cabinet deliberations (and endorsement): it would be difficult for UNTAET to explain retreating significantly from our current position. Needless to say however, it is

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<sup>66</sup> John Dauth, Deputy Secretary of the Department of Foreign Affairs.

important to ensure that we do not alienate Australia's goodwill, in this and other areas, and that negotiations stay on track.<sup>67</sup>

De Mello was receptive to the precariousness of UNTAET's position. The UN remained hugely dependent upon Australian support for the most fundamental needs of East Timor, such as the basic security of the territory. The situation therefore called for extremely careful political management. Following his return to Dili, arrangements were made for a secret meeting of the parties to be held at the Regent Hotel in Singapore from 23 to 24 November 2000. Each delegation comprised just three people: Michael Potts, John Hartwell and Rebecca Irwin (Attorney General's Department) for Australia; and Peter Galbraith, Mari Alkatiri and Jonathan Prentice (UNTAET Political Affairs) for UNTAET. As an informal meeting, Galbraith saw it as an opportunity for an unencumbered discussion of the two countries' key interests; and for both sides "to feel sufficiently comfortable to explore to the full any and all possibilities of bridging the wide gulf evident in the Dili talks, in October".<sup>68</sup> There was a need to restore some confidence in the process. Galbraith was conscious of the personal animosity Downer felt towards him and UNTAET officials had become alarmed at the menacing nature of a comment made by Downer to de Mello during his trip to Canberra that, "Australia could bring meltdown to East Timor if it so chose".<sup>69</sup> Prentice told the Australian delegation in Singapore that, even if not actually meant, such remarks "stuck in the mind and caused needless anxiety".<sup>70</sup>

Potts opened the first session of the meeting by stating that if there was no progress in this round, then the Australian delegation would need to revert to Cabinet which would not be meeting again until February 2001. In those circumstances, a new round of formal negotiations would not be possible until March 2001, which would put pressure on the timelines for the talks, given that the transition of sovereignty in East Timor was expected to be completed by the end of 2001. Potts described the 1989 Timor Gap Treaty as being the product of "a quick and dirty deal" between Indonesia and Australia by which the latter sought a seabed boundary delimitation in return for according the former recognition of its sovereignty over East Timor.<sup>71</sup> However, he pointed out that East Timor's position was

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<sup>67</sup> Cable from S. V. de Mello to B. Miyet, 'Timor Gap negotiations', 27 October 2000.

<sup>68</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 23 November 2000.

<sup>69</sup> *Ibid.*

<sup>70</sup> *Ibid.*

<sup>71</sup> *Ibid.*

similar to the position adopted by Indonesia in 1979, while Australia's also remained the same, insofar as Australia "would show no flexibility on the issue of accepting a permanent median line delimitation".<sup>72</sup> Galbraith explained that it was not a maritime boundary that was being sought but rather a single purpose jurisdiction line, which would put aside the question of permanent sovereignty.

Potts responded that if Australia conceded, Indonesia would see things differently. The Australian government considered that Indonesia would probably react in two ways. Firstly, they would want an immediate explanation as to why Australia had been willing to accommodate East Timor whilst having rejected the same claims made by Indonesia in earlier negotiations. Secondly, they would mount a political campaign demanding that the 1972 seabed boundary to be redrawn on median line principles. Potts described the "Indonesian angle" as "the most dynamic point of the problem for Australia".<sup>73</sup> Galbraith argued that this was more of a political problem than a legal one, as there would be no legal basis upon which Indonesia could force the 1972 boundary to be changed. Potts disagreed, noting that "Jakarta had creative lawyers".<sup>74</sup>

Galbraith attempted to steer the discussions away from this type of confrontational positional bargaining towards a more problem-focused approach. To this end, he suggested that the two teams engage in a role-reversal exercise so that the Australian government negotiators could better understand the situation from UNTAET's perspective. Galbraith was able to draw on a repertoire of negotiating skills and think creatively about ways of breaking the impasse. Role-reversal is a negotiating technique, which is designed to help adversaries identify points of commonality and mutual interest – simply by putting themselves in the other party's shoes. The task involved each side pretending to be the other delegation, which then had to persuade their respective foreign ministers of the benefits of accepting the opponent's offer. Thus, the Australian delegation "crafted three imaginary talking points" for the East Timorese foreign minister explaining the advantages for East Timor of accepting the Australian position, and the UNTAET delegation performed the same exercise in reverse.<sup>75</sup>

The Australian team's three points for East Timor accepting the Australian position were:

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<sup>72</sup> *Ibid.*

<sup>73</sup> *Ibid.*

<sup>74</sup> *Ibid.*

<sup>75</sup> *Ibid.*



- this is an excellent psychological start for a new country, locking Australia in as a long-term strategic partner in a number of cross-over areas while presenting a complete departure from the 1989 Treaty because of the new architecture, nomenclature and decision-making structures in the new arrangement;
- it guarantees a secure revenue flow essential for rational, long-term economic planning; and,
- it ensures investor confidence across the board that would be good for development throughout East Timor in all areas. Avoiding litigation would avoid unnecessary damage to the image of the new country.<sup>76</sup>

UNTAET's three main selling points for Australia accepting East Timor's position were:

- it would be yet another example of Australia's generosity and magnanimity to East Timor;
- it would preserve Australia's sovereign rights to the area in question; and,
- Australia would continue to benefit significantly from the downstream benefits emanating from petroleum activity on the Timor Sea.<sup>77</sup>

The Australian team argued that although the first of the points made by UNTAET was "plausible" and the third "largely true", the second point was "less strong". Potts explained that a lot would depend on the "imagery" of the single purpose jurisdictional line concept: "it must be attractive to Australia but not a turn-on to Indonesia".<sup>78</sup> In this regard, Potts continued that the single line jurisdiction must have "real differentiation" from sovereign rights but that this was not reflected in UNTAET's approach.<sup>79</sup> The Australian team noted that if the net effect of this concept were to be the same as a median line delimitation, it perhaps would be more politically palatable to have the decision imposed by a court. However, Potts affirmed that Australia was very uneasy about the prospect of litigation because of the uncertainty surrounding the outcome. He noted that one of Australia's options would be to "chisel out" of the dispute settlement provisions of the UN Convention on the Law of the Sea, thus preventing East Timor from having the boundary legally decided.<sup>80</sup>

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<sup>76</sup> *Ibid.*

<sup>77</sup> *Ibid.*

<sup>78</sup> *Ibid.*

<sup>79</sup> *Ibid.*

<sup>80</sup> *Ibid.*

Galbraith emphasised that the crucial point was that it was East Timor's fundamental belief that it would win in court and the Australian delegation had to take this into account. Potts argued that while East Timor might get the median line, the court would dismiss the laterals because Indonesia would be an indispensable partner to the proceedings.

During the afternoon session, Galbraith began by reiterating that East Timor's sole concern was to maximize revenues. The single purpose jurisdiction and the shift in the laterals were "geared towards that end".<sup>81</sup> Potts asserted that the two key issues for Australia were "not opening up the issue of the Australian/Indonesian boundary, and not losing major assets, such as Laminaria which produces 180,000 barrels a day or roughly 25 to 30 percent of Australia's oil output".<sup>82</sup> He emphasised the futility of East Timor pursuing the question of the laterals either through negotiation or litigation as "Australia refused to acknowledge the East Timorese case".<sup>83</sup> Galbraith suggested an Advisory Opinion of the ICJ as an alternative to litigation, to which Potts replied that "there was no difference in reality".<sup>84</sup> Whilst the question of the laterals remained a major sticking point, the issue of the administrative arrangements for Area A was less contentious. The Australian team explained that they had not ruled out the possibility of East Timorese law being the applicable law. Galbraith responded that whilst, as a general rule, there would be no problem with Australian criminal, health and safety regulations being adopted, petroleum and tax laws would have to be East Timorese. Hartwell commented that both sides "could probably work something out along those lines".<sup>85</sup> Galbraith stressed that the role of the Joint Authority would therefore have to be circumscribed, as "such a body would not be able to decide on tax and royalty issues". In short, "there was a need to develop a system consistent with East Timorese sovereignty but which would allow for a significant role for Australia".<sup>86</sup>

On 24 November, Potts began by reviewing the salient aspects of the previous day's discussions. He re-emphasised that it would be politically impossible for Australia to accept any changes to the lateral lines, which he portrayed as an "image problem" for Australia: "it would be difficult to sell giving East Timor 100 percent of ZOCA plus a surcharge for Laminaria and Sunrise as this would look like a bribe or extortion".<sup>87</sup> With respect to the possibility of litigation, he cautioned Galbraith not to view this as a natural development

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<sup>81</sup> *Ibid.*

<sup>82</sup> *Ibid.*

<sup>83</sup> *Ibid.*

<sup>84</sup> *Ibid.*

<sup>85</sup> *Ibid.*

<sup>86</sup> *Ibid.*

<sup>87</sup> *Ibid.*

which could be managed. Potts described litigation as “an act of failure and loss of control and would be a bad signal for a new country to send out”.<sup>88</sup> Further, “Australia would not accept any temporary agreement pending litigation and development would thus freeze”.<sup>89</sup> More threateningly, he warned that “East Timor should not expect Australia to be chummy about going to the ICJ – it would not be possible to insulate such a development from overall bilateral relations and consequently there would be no enthusiasm for new generosity or magnanimity by the Australian government towards East Timor”.<sup>90</sup> Further, he repeated the point that Australia could simply opt out of the compulsory jurisdiction of the ICJ, which was described as Australia’s “get out of jail card”.<sup>91</sup> Potts disclosed that the possibility of Australia withdrawing from compulsory third-party dispute resolution had been included in the submission endorsed by Cabinet for the negotiations and no Minister had objected to it. He warned that “the more ambitious East Timor’s claim, the easier it would be for the government to pursue this approach in terms of living down domestic controversy”.<sup>92</sup>

As a possible way of moving forward, it was agreed that the negotiations could be broken down into three separate components: (i) the question of what happens to the area defined as ZOCA by the 1989 Timor Gap Treaty; (ii) the question of the arrangement for gas pipelines; and, (iii) the question of the lateral areas. Galbraith emphasised that discussion of (i) should proceed without prejudice to discussion of (iii). He confirmed that it would be UNTAET/East Timor’s expectation that Australia would enter into talks with East Timor on (iii) in accordance with the rules of the UN Convention on the Law of the Sea. In the interim, Australia and UNTAET could work towards a “cooperation agreement” in regard to (i). Galbraith stressed that there should be no trade-off between (i) and (iii): “rather, the two should be kept entirely separate”. He explained that UNTAET would expect talks on (iii) to begin prior to independence. “In other words, the price for Australia of East Timor agreeing to reach a settlement on (i) would be Australia’s commitment to negotiate on (iii)”.<sup>93</sup> The Australian team was supportive of taking this approach and, furthermore, they offered to accept East Timorese petroleum and fiscal law applying in Area A, though with “certain elements of jointness continuing to apply”.<sup>94</sup> In addition, it was suggested that the new treaty

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<sup>88</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 24 November 2000.

<sup>89</sup> *Ibid.*

<sup>90</sup> *Ibid.*

<sup>91</sup> *Ibid.*

<sup>92</sup> *Ibid.*

<sup>93</sup> *Ibid.*

<sup>94</sup> *Ibid.*

could simply “wipe out” Areas B and C, in providing “new imagery” which might prove useful to East Timor.<sup>95</sup>

Teasing out the issue of applicable law, Galbraith sought to sum up the discussion: “East Timor petroleum and fiscal laws would apply (petroleum, corporate and tax, together with certain environmental laws on greenhouse issues), but that on other issues East Timor would be prepared to discuss which laws should apply. In this context, East Timorese decision-making would be supreme though some consultancy mechanism would be established...Australia would have jointness in administration but not in policy”.<sup>96</sup> Potts noted that this would probably entail a move towards a different management structure from the current model. On the issue of the revenue split, Alkatiri commented that this issue needed to be seen through a “new prism”: namely, “that it was not Australia which was being generous in putting forward a 2:1 proposal, but rather it would be East Timor which was being generous to Australia if it accepted this”.<sup>97</sup> Galbraith added that the starting point should not be the 50-50 split of the original treaty; rather “the question is how much is East Timor willing to pay to avoid litigation? Perhaps 10 percent of both royalties and taxes. It would be very difficult to go much farther than this”.<sup>98</sup>

The talks concluded mid-day on 24 November. Potts described the three-fold characterization of the issue as a “significant breakthrough” and believed that it presented a genuine way forward that could serve as a basis for another round of talks.<sup>99</sup> He felt that de Mello’s suggestion for having an informal round of talks had proven to be a good idea, leading to some “traction” on the matter.<sup>100</sup> Galbraith agreed but emphasised that there would be little flexibility with regard to both the issue of applicable law and revenue sharing. Potts expected that with regard to the latter, there would be some movement by Australia and suggested that the next round of talks should focus on the architecture for the new regime applicable to the joint development zone. It was agreed to continue informal talks on this basis in Cairns, Australia, on 11 and 12 December 2000.

Galbraith’s decision to de-link the issues in the negotiations was the first major shift in UNTAET’s position and a reflection of how firmly the Australian side had resisted any idea of ‘opening’ the laterals. Potts had convincingly shown that Australia would rather have no-

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<sup>95</sup> *Ibid.*

<sup>96</sup> *Ibid.*

<sup>97</sup> *Ibid.*

<sup>98</sup> *Ibid.*

<sup>99</sup> *Ibid.*

<sup>100</sup> *Ibid.*

agreement than one that involved any changes to the current co-ordinates of the zone. Galbraith was not prepared to continue to pursue the laterals if this meant risking not having an agreement, as East Timor could not afford petroleum developments being frozen. It is important therefore to have in mind UNTAET's underlying interests. Galbraith's strategy was to "pocket" as much from Bayu-Undan as possible and then take the dispute to the ICJ.<sup>101</sup> The lateral boundary issue was not critical in this regard, as it could be resolved through litigation at a later time once revenues from Bayu-Undan had been secured. Galbraith did not believe that the Australian government would follow through on the threat to withdraw from the ICJ's compulsory jurisdiction because of the damaging effect such a move would have upon the country's international reputation. He saw this as a tactical attempt by Australia to persuade UNTAET to soften its position.

The discussions held in Cairns two weeks later took place against the background of some important commercial developments. On 30 November 2000, Phillips and Woodside announced that they had reached an in principle agreement on the coordinated development of their Timor Sea gas reserves, thus aggregating more than eleven trillion cubic feet of natural gas.<sup>102</sup> The agreement was the result of negotiations that had taken place over a period of several months. In a joint press statement, Phillips' Chief Executive, James Mulva and John Akehurst, Woodside's Managing Director, stated that "the concept is designed to combine the early gas delivery potential of the Bayu-Undan gas and condensate development with the large reserve base of the Greater Sunrise fields".<sup>103</sup> On the same day of the announcement, the two executives attended a meeting with the Australian Prime Minister, Foreign Minister and Resources Minister in Canberra.<sup>104</sup> Mulva gave a presentation on the companies' business plan for the Timor Sea and discussed Darwin's potential as a region-wide gas gathering hub.

The Ministers were informed by the company representatives that they intended to pool the gas resources of Bayu-Undan and Greater Sunrise for marketing purposes and to develop the fields through integrated infrastructure.<sup>105</sup> They planned to construct a tributary gas pipeline from Greater Sunrise linked to the main 500 kilometer trunk line from Bayu-Undan. The gas would be landed in Darwin and used to supply both Australian-based

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<sup>101</sup> Pers. Comm. Senior UNTAET Official, August 2004.

<sup>102</sup> 'Woodside and Phillips agree to Timor Sea cooperation', *News Release*, Woodside Energy, 30 November 2000.

<sup>103</sup> *Ibid.*

<sup>104</sup> 'Burke in gas talks with PM', *Northern Territory News*, 29 November 2000; 'Woodside, Phillips Timor Sea gas co-operation deal near', *The Australian*, 30 November 2000; 'Pollies quiet on billion-dollar deal', *Northern Territory News*, 30 November 2000.

<sup>105</sup> Pers. Comm. Denis Burke, July 2004.

industries, such as Methanex's proposed methanol production facility, as well as foreign markets.<sup>106</sup> The development was expected to cost US\$4 billion, which would rank as one of the biggest resource projects in Australia's history, second only to the Northwest Shelf development in Western Australia. The Ministers were also told that a key precondition of the companies' decision to proceed with the investment, however, would be the maintenance of the current taxation arrangements for Greater Sunrise, which was based on the formula of 80 percent being subject to Australia's Petroleum Resource Rent Taxation (PRRT) and 20 percent under the Production Sharing Contracts (PSCs) of the Timor Gap Treaty. This percentage distribution reflected the field's extension across the eastern boundary of the Zone of Cooperation, such that 20 percent was inside the zone and 80 percent outside.<sup>107</sup> For the oil companies, there was an advantage to having as much of Sunrise allocated to the Australian taxation regime, because it allows companies to carry losses from unprofitable developments to profitable ones, thereby diminishing their overall tax burden.

When the negotiations between UNTAET and Australia resumed on 11 December, Potts suggested that the initial focus of the discussion should be the administrative arrangements for the existing zone, particularly "the applicable law, jointness and how to realize it, and the revenue split". He pointed to some of the problems for the Australian government in accepting East Timor having legal authority over the zone: "What was East Timorese law? Indonesian law with safeguards on human rights?"<sup>108</sup> He argued that it could be seen as "an ability to modify the law at any subsequent stage and as a blank cheque. The East Timorese would be able to change the law in a form that might prove unhelpful towards Australia and investors".<sup>109</sup> The UNTAET team sought to assure the Australian delegation of East Timor's intention to develop a system that was stable and transparent. Alkatiri referred to the 'no more onerous' commitment made by the CNRT in October 1999. Galbraith tried to assuage Australia's concerns about East Timor taking over the control of the fiscal and legal arrangements for the zone. He explained that "a new country would have to develop a track record and avoid the risks of arbitrary decisions that it would pay a high price for in the future".<sup>110</sup>

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<sup>106</sup> '\$1bn bonanza in Timor Gas', *The Australian*, 1 December 2000; 'Phillips, Woodside to team in Timor Sea', *Platts Oilgram*, 1 December 2000.

<sup>107</sup> Pers. Comm. Denis Burke, July 2004.

<sup>108</sup> *Ibid.*

<sup>109</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 11 December 2000.

<sup>110</sup> *Ibid.*

The Australian delegation explained that “the idea of an East Timorese company law, the registration of companies in East Timor, the establishment of offices in East Timor and potentially the establishment of an East Timorese Oil Production Company would be a hard sell to the Australian government, which would see it as a blank cheque for increasing the East Timorese revenue share”.<sup>111</sup> Galbraith stressed that the core issue was that “East Timor should be able to make the essential decisions about their most important resources”.<sup>112</sup> His vision was for East Timor to have legislative control over the production regime and political control of the governance institutions to reflect the “greater economic interest of East Timor in the area”.<sup>113</sup> The Australian team indicated that it was prepared to accept changes to the institutional architecture of the zone, which Potts saw as existing on three levels:

- The Designated Authority
- The Joint Commission with an East Timorese majority
- The Ministerial Council on a one-to-one basis.

Galbraith agreed with this structure and explained that “the Joint Commission would be like the board of a company...It would have a minimum of staff perhaps supplied by the Designated Authority. The Designated Authority would commence as being a joint East Timorese/Australian body but would be gradually taken over by the future East Timor Ministry of Mines as capacity increased”.<sup>114</sup> From this standpoint, “the Joint Commission would be a policy maker and the Designated Authority would develop a corporate and strategic plan, which would be signed off by the Joint Commission. Licensing would be carried out according to the policy of the Commission, which would approve significant development plans and matters with financial implications above an agreed amount”.<sup>115</sup> Potts considered that the “architecture of the new arrangement had been taken a long way”, although members of the Australian delegation continued to express concerns over “the possibility of Australian interests being harmed” if East Timor was to have total legislative control over the zone.

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<sup>111</sup> *Ibid.*

<sup>112</sup> *Ibid.*

<sup>113</sup> *Ibid.*

<sup>114</sup> *Ibid.*

<sup>115</sup> *Ibid.*

On the question of the revenue split for the zone, Potts acknowledged that “the ball was in the Australian court and the 2:1 offer was not the bottom line”.<sup>116</sup> He disclosed that “cabinet had not yet advanced on this question but it was likely that a 75%/25% division would be looked at, depending on a satisfactory package deal on the treaty and the resolution of the downstream processing question”.<sup>117</sup> However, he cautioned that “the Treasury and the Ministry of Finance were against any further offer and the talk of 90%/10% was frightening a lot of people”.<sup>118</sup> Galbraith responded that there was little scope for flexibility on the East Timor side and that the percentage split was “a potential deal breaker”.<sup>119</sup> He emphasized that the starting point should not be seen as the 50-50 terms of the original treaty but the risks involved for East Timor in going to court.

During the afternoon session, on 11 December, Galbraith asked the Australian delegation to elaborate further on the ‘downstream processing issues’ whose resolution Australia’s offer had been made contingent on. Hartwell explained that these included the fiscal regime for gas production, the gas valuation point, the unitisation of Greater Sunrise as well as the legal, fiscal and regulatory regime for the gas pipeline. Potts described the resolution of these issues as “life and death for the development of the Timor Gap area inasmuch as the gas was the dynamic element and resolution of the unitisation and pipeline issues was vital”.<sup>120</sup> The question of unitisation was a particularly thorny issue as it impacted upon the problem of the lateral boundaries. The Australian team asserted that the Greater Sunrise area would have to be unitised on the basis that 20 percent of the hydrocarbons were inside the zone and 80 percent were on the other side. Galbraith pointed out that, from the East Timorese perspective, no boundaries existed and the question was being approached on the basis of a clean slate. “The East Timorese position was that 100 percent of the resources in the area belonged to East Timor”.<sup>121</sup> The Australian side rejected the view that there were no boundaries in the Timor Sea but conceded that if the lateral lines were to be “pushed out in the future there would have to be a mechanism to change the revenue share”.<sup>122</sup>

Galbraith objected to this idea and remarked that “the implication that ‘it was ours until it becomes yours’ was not acceptable”.<sup>123</sup> He stressed the need to treat the issues under

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<sup>116</sup> *Ibid.*

<sup>117</sup> *Ibid.*

<sup>118</sup> *Ibid.*

<sup>119</sup> *Ibid.*

<sup>120</sup> *Ibid.*

<sup>121</sup> *Ibid.*

<sup>122</sup> *Ibid.*

<sup>123</sup> *Ibid.*



discussion as three separate negotiations: Zone A; the pipeline; and, the areas outside of Zone A. Potts emphatically rejected any claims made by East Timor regarding the third point and stated that there would be “no give and take in the Australian position”.<sup>124</sup> He contended that “the co-ordinates included in the treaty would remain the standard for the Timor Gap and there were no other co-ordinates. There was no readiness to open up at the political level regarding these claims”.<sup>125</sup> Potts asserted that the Australian government would “maintain that the lines were there and there was nothing more to talk about”.<sup>126</sup> In response to a comment made by a member of UNTAET’s delegation regarding the possibility of litigation, his response was “see you in court”.<sup>127</sup> For the Australians, the issue of the lateral lines was a “deal breaker”.<sup>128</sup> Galbraith agreed that the question was a difficult one to resolve but reminded the Australian delegation of what had been pointed out in Dili: “Do not expect to agree with our position or ours with yours. What had been negotiated with Indonesia was not binding with East Timor...the lines proposed by East Timor were as valid as the lines proposed by Australia”.<sup>129</sup>

On 12 December, discussions focused initially on the regime for gas pipelines. The main pipeline was expected to be built from Bayu-Undan to northern Australia, which meant that it would cross several jurisdictions – the joint development zone, an area of high seas, Australia’s twelve mile territorial sea and the Northern Territory’s three mile state waters. Both sides saw an advantage in having a regime of harmonized jurisdiction over the full length of the pipeline, simply because it would provide operational convenience. The UNTAET position was that the applicable legal regime should be the same as the one in the Joint Commission area, which, it was contended, would be subject to East Timorese law and administered by the Commission. Galbraith assured the Australian delegation that this was “not an attempt to gain a beachhead in the Northern Territory, only to maximize revenue”.<sup>130</sup> The Australian delegation did not have a clearly defined position and, whilst not completely opposed to the UNTAET proposal, were reluctant to make a commitment at this stage. The pipeline had important government revenue implications. It was a corporate economic activity

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<sup>124</sup> *Ibid.*

<sup>125</sup> *Ibid.*

<sup>126</sup> *Ibid.*

<sup>127</sup> *Ibid.*

<sup>128</sup> *Ibid.*

<sup>129</sup> *Ibid.*

<sup>130</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 12 December 2000.

for which the pipeline owner would seek a return on his investment. Government revenue from the pipeline would come from corporate taxation of the pipeline operator.

Returning to the question of applicable law, Potts observed that the thinking up until this point had been that company, fiscal and petroleum laws in the zone would be covered by East Timor legislation. In response to concerns that East Timor would have the power to make changes to the PSC regime in ways that were detrimental to Australian interests, Galbraith commented that “there would be a one time cost of revising the system but that the East Timorese would not adopt policies to reduce revenue but rather enhance the collection of revenues through an efficient fiscal system”.<sup>131</sup> He stressed that East Timor would look to Australia for assistance in devising the new regime. Potts reacted positively to this suggestion and described it as a “capacity building programme for the future and...a selling point to ministers”.<sup>132</sup> With respect to the subject of Sunrise unitisation, he remarked that there was a different philosophical approach from each side and it would be necessary to work through the problem: “it took two tango but the dancers were not yet lined up”.<sup>133</sup> The UNTAET team confirmed the need for further discussions but also recognized the difficulties involved. Galbraith pointed out that “there was no recognition that the lateral lines of the zone were Australia”.<sup>134</sup>

The final session of the meeting in Cairns began with a telephone conversation with Leerberg to progress issues relating to the gas pipeline and fiscal arrangements. The three issues that were discussed related to the metering system, the harmonization of jurisdiction and the gas valuation point. In relation to the question of jurisdiction, the Australian side saw the responsibility as belonging to the Joint Commission in the area of co-operation and up to the Australian twelve-mile territorial sea limit. A Northern Territory body would have control over the territorial sea and coastal waters as well as onshore installations in that state. Whilst noting that Australian sovereignty within the twelve-mile territorial sea would need to be recognized, Leerberg recommended having harmonized jurisdiction under Joint Commission control over the entire length to avoid any “problems of discrepancies in the systems, slower decision-making processes and uncertainty for the operators”.<sup>135</sup> Galbraith re-iterated UNTAET’s proposal: namely, “jurisdiction would be East Timor law up to the Australian territorial sea and the Australian and Northern Territory governments would delegate the

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<sup>131</sup> *Ibid.*

<sup>132</sup> *Ibid.*

<sup>133</sup> *Ibid.*

<sup>134</sup> *Ibid.*

<sup>135</sup> *Ibid.*

management of the pipeline over the twelve miles to the Zone of Co-operation on a discretionary basis”.<sup>136</sup> On the question of the gas valuation point, Leerberg suggested that, for a range of technical and legal reasons, it would be sensible to have it at the point at which there was a transfer of ownership to a commercial operator in the commodities market. Under the Norwegian system gas was measured and valued at the outlet flange onshore.

Potts considered that the discussion of these issues had been useful but Australia would need to reflect on these options and “get a sense of the pros and cons” before making a reaction.<sup>137</sup> He explained that the Australian team would have to meet with their Ministers to see what commitments could be made as they were “operating without cover”.<sup>138</sup> He stated that there had been “progress since Singapore and a change of dynamics and a better understanding of shared problems”.<sup>139</sup> He confirmed that in the last week of January or first week of February there would be a submission to Ministers to “outline the likely shape of the offer and obtain a viable basis for more detailed negotiations”.<sup>140</sup> Galbraith also considered that much had been accomplished “in the nick of time” but that there was a lot more work to be done. He agreed with Potts’ proposal for the way forward and explained that he would also seek a report from the UNTAET Cabinet to endorse what had been discussed. With regard to the arrangements for Area A, he stated that the “parties were close to agreement on critical issues with a good idea as to the applicable law, dispute resolution and the consultation process”.<sup>141</sup> Other issues had not been resolved, however, including the oil and gas revenue split. Potts replied that the Australian side was “not fixated by the revenue split and there was some flexibility but not enough to bridge the gap”.<sup>142</sup> The meeting concluded with a discussion of the timetable for the transitional political process in East Timor. Galbraith confirmed that the treaty would need to be concluded before the six-week election campaign for East Timor’s Constituent Assembly, scheduled for 30 August 2001. This would imply a deadline of around 15 July 2001 for concluding the agreement. He felt it might be possible for the Constituent Assembly to ratify the treaty and perhaps incorporate it within the new Constitution for East Timor.

The close convergence of the parties’ positions during the Singapore and Cairns talks had resulted in an important set of gains for UNTAET/East Timor: namely, a shift to a

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<sup>136</sup> *Ibid.*

<sup>137</sup> *Ibid.*

<sup>138</sup> *Ibid.*

<sup>139</sup> *Ibid.*

<sup>140</sup> *Ibid.*

<sup>141</sup> *Ibid.*

<sup>142</sup> *Ibid.*

75%/25% revenue split; legislative control over the joint development zone; and, a new institutional architecture comprising a powerful Joint Commission with greater East Timorese representation. Further, the Australian team had signaled a willingness to accept a new fiscal regime for future developments in the zone as well as possible East Timorese jurisdiction over the proposed pipeline. This was very near to achieving UNTAET's objective of developing a system that gave East Timor control over the Timor Gap. These gains had been achieved through tough bargaining and creative thinking but at the cost of the decision to set aside the question of the lateral boundaries in devising the new regime. The tactical approach adopted by Galbraith in Singapore and Cairns was to assuage, to the greatest extent possible, any concerns that transferring authority to East Timor would be detrimental to Australia's interests. Whilst the de-linking of the laterals would make it difficult for East Timor to gain access to the revenues of the Laminaria/Corallina oil fields, UNTAET's primary strategic objective was the control of Bayu-Undan, which was at least three times the size of Laminaria/Corallina, containing hydrocarbons with an energy equivalent of over one billion barrels of crude oil.

Sunrise posed a different set of problems as well as (and in part a result of) a very different set of commercial opportunities to Bayu-Undan. Although potentially more valuable due to its larger reserve base, Sunrise was a much more expensive operation, because the fields were in deeper water and had a more complex geological structure. The ratio of gas to liquids was also much higher than Bayu-Undan, which meant that it was economically unfeasible to develop the resource as a liquids stripping/gas recycle project. Whilst a potential buyer for Sunrise gas had been found in the Canadian firm, Methanex, the quantities involved were not sufficiently large enough to provide the Woodside/Shell joint venture with the minimum required return on investment. Other customers had to be found if the project was to go ahead. The essential point, therefore, is that whereas Bayu-Undan was an immediate concern, Sunrise could wait. Moreover, Galbraith knew that East Timor would always have a degree of leverage over the terms of production because, as the field straddled the zone, the project could go ahead only with the government's explicit approval, and thus only on terms that East Timor was satisfied with. Galbraith wanted to unitise the field independently of the main treaty, in a manner that was non-prejudicial to East Timor's sovereignty claims in the Sunrise production area, or preferably, after achieving a favourable judicial settlement of the boundary.

#### *5.4 The Second Round – Melbourne, 4-6 April, 2001*

During January 2001, the change in the dynamics of the negotiations started to filter through to the Australian press. On 15 January, the *Sydney Morning Herald* reported that “the Australian Government is retreating from its tough opening stance on the oil revenue split in a new seabed boundary treaty with independent East Timor”.<sup>143</sup> Mari Alkatiri was quoted as saying: “New ideas have been adopted by both sides. We are closer now to a consensus about dealing with the issues”.<sup>144</sup> The next month, Woodside and Phillips finalized the terms of their cooperative effort in Bayu-Undan and Sunrise.<sup>145</sup> Under the terms of the deal, Phillips assumed marketing responsibilities for the Sunrise Project and also increased its equity holding to thirty percent. Shortly afterwards, Phillips announced a Letter of Intent (LOI) for a major gas sales contract with a subsidiary of El Paso Corporation, a North American energy utility. The deal was intended to result in the delivery of 4.8 million tons per annum of LNG, with all the gas being supplied from the Bayu-Undan and Greater Sunrise fields.<sup>146</sup>

In international energy markets, oil and gas are very different. Standard commercial practice in the international LNG trade is for buyers to be contractually engaged under fairly stringent purchase and supply agreements prior to the commencement of production. For any project of this size, long-term contractual relationships are normally needed to underpin the massive upstream, or front-end, infrastructure development costs and shipping investments and to govern commercial activities associated with each of the various links in the LNG chain – from extraction and liquefaction to shipping delivery, and regassification. The El Paso deal would involve construction of an LNG plant in Darwin, with production commencing in 2005. Phillips’ Executive Vice President, Bill Parker, stated that “this LOI with El Paso, combined with the cooperative arrangements with Shell and Woodside, validates Phillips’ vision for Timor Sea gas developments and increases the value to all stakeholders in these resources. With future gas sales to this LNG project – and to domestic customers in Australia’s Northern Territory and elsewhere – the Timor Sea will become a new center of production for Phillips, commercializing significant quantities of oil and natural gas”.<sup>147</sup>

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<sup>143</sup> ‘Oil is more important to us than to Australia, says Gusmao’, *Sydney Morning Herald*, 15 January 2001.

<sup>144</sup> *Ibid.*

<sup>145</sup> ‘Phillips increases interests in Timor Sea’, *News Release*, Phillips Petroleum, 23 February 2001.

<sup>146</sup> ‘Timor Sea gas fields – letter of intent for LNG sales’, *News Release*, Woodside Energy, 9 March 2001.

<sup>147</sup> Phillips News Release, ‘Phillips and El Paso plan to deliver Australian LNG to California and Mexico in 2005’, 9 March 2001.

The LOI was described by the Northern Territory government as the “marketing highlight of the year”.<sup>148</sup> UNTAET also responded positively, stating that the cooperative development of Bayu-Undan and Greater Sunrise “would enhance prospects of higher volumes and early production of the region’s resources”.<sup>149</sup> Shortly after the announcement, the Northern Territory Chief Minister, Denis Burke, traveled to the United States to meet with Phillips executives as well as US Vice President, Dick Cheney, about the possibility of building a receiving terminal for Timor Sea gas on the country’s west coast.<sup>150</sup> The LOI had raised the stakes enormously for all concerned. A potential AUD\$13.7 billion of investment in the Northern Territory now rested on the successful conclusion of the political negotiations.<sup>151</sup> The LOI was a clever tool with which the companies sought to build pressure around the negotiations, by shaping perceptions of the commercial context and concentrating the Australian government’s and the transitional administration’s focus on the need for agreement.

In February 2001, UNTAET received confirmation that the Australian government would not be in a position to resume negotiations as early as had previously been planned. In early March, Peter Galbraith met with John Hartwell, in Canberra, to discuss the timing and venue for the second round of formal negotiations. It was agreed that the next meeting would be held in Melbourne, during the first week of April, 2001. Hartwell revealed that the issue was being reviewed by Cabinet, which wanted further clarification on some of the ideas which had been proposed during the informal discussions, over November and December, 2001. Galbraith sensed the possibility of some backsliding by the Australian government. Yet it was now three months since the last meeting and, during the intervening period, the commercial situation had changed dramatically. The Australian government had been under serious pressure from the oil companies to oppose any changes being made to the legal framework currently in place. The companies wanted the existing PSCs to be locked into the new treaty, the tax regime to be ‘no more onerous’ than that which would have applied under a continuation of the Timor Gap Treaty and for Sunrise to be unitised according to the existing Zone of Cooperation boundaries. These demands were diametrically opposed to UNTAET’s goal of “breaking the old treaty” and devising a new regime which gave East Timor the authority to develop its own fiscal and taxation system.

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<sup>148</sup> Northern Territory, Office of Resource Development, *Annual Report*, 2000/2001.

<sup>149</sup> Yahoo Finance, <http://biz.yahoo.com/rf/001201/syd25642.html> <Accessed 15 July 2004>

<sup>150</sup> ‘Cheney drawn into Timor tangle’, *The Australian*, 8 May 2001.

<sup>151</sup> The AUD\$13.7 billion of investment included a liquefied natural gas plant, a methanol plant and gas pipelines from Darwin to Gove, Moomba, Mt. Isa and Townsville.

However, the weight of corporate pressure had the desired impact. The second round of formal negotiations turned out to be a complete disaster, as Australia went back on everything that had been agreed in Cairns. On 11 April 2001, de Mello cabled Jean-Marie Guéhenno, who had taken over from Bernard Miyet as the Under-Secretary General for Peacekeeping Operations, on what had happened:

The second formal round of negotiations on a new treaty in the Timor Sea was held from 4-6 April 2001 in Melbourne. They were a fiasco. Three of the four Australians who participated in the informal rounds in Singapore and Cairns were not in Melbourne, including the delegation head. As a result, the Australians reopened key issues of applicable law and management, acting as if the Singapore/Cairns ad referendum agreements had never existed. Specifically, the Australian side insisted that issues of pipeline and unitisation of the Greater Sunrise be linked to an overall settlement of ZOCA. At Singapore, our proposal to delink these issues had been warmly embraced by the Australians, as it provided a way round the unitisation issue.

With regard to applicable law (where as Singapore it was agreed that East Timor petroleum fiscal, tax and corporate law would apply), the Australians now insist that both countries' corporate and commercial law apply in the zone. This effectively denies East Timor's jurisdiction over companies, which are all foreign, operating in the area. The Australians now insist that the management structure over the area should be controlled equally by the two countries, a shift from Cairns where East Timor's greater interest had been recognised. On the pipeline, the Australians now insist that it must be under their jurisdiction. We have never had an agreement on this, but at the first formal round we had proposed the Norwegian model which would place it under our jurisdiction. In an otherwise bleak picture there was one bright spot. The Australians said if we reached a package deal on ZOCA, the pipeline and unitisation, they would consider a substantially more generous revenue split than the 75-25% proposal offered in Cairns. We assume they are close to, or at our proposal of 90-10.<sup>152</sup>

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<sup>152</sup> Cable from S. V. de Mello to J. M. Guéhenno, 'Timor Gap Second Round of Formal Talks', 11 April 2001.

Australia's reversal in these key areas had brought the negotiations to a critical point. It also provided the impetus for what would prove to be the single most important and dramatic moment of the negotiation process. Three days after the talks had ended in Melbourne, Alkatiri and Galbraith traveled to Hobart, Tasmania, where they had been invited to deliver a keynote address at the annual conference of the Australian Petroleum Production and Exploration Association (APPEA). Although Galbraith's participation had been arranged some months in advance, the timing of the event provided him with the perfect opportunity to publicly commit to UNTAET's negotiating position. Galbraith delivered his address with Mari Alkatiri standing by his side on the podium. The audience consisted of about 1,000 delegates from industry and government. The most senior government figure present was the Minister for Industry, Science and Resources, Nick Minchin. Galbraith's goal was to "get the audience to see East Timor's view, that without a satisfactory agreement, nothing would go ahead".<sup>153</sup> The message within the speech was intended to convey both resolve and trust. Galbraith wanted the major oil companies involved in the Timor Sea to believe that East Timor was a reliable business partner, yet would make a strong stand to ensure that the country's sovereign rights were respected. Galbraith told the conference:

...East Timor understands that oil and gas investments are made for thirty years. Investors require stability and certainty with regard to government policies. Capricious changes in policies may bring short-term gains, but over the long-term countries pay a high premium for being a political and economic risk. On behalf of the East Timor Cabinet and legislature, I am here to underline our intention to develop and implement a transparent, stable fiscal and regulatory regime that will be amongst the most modern in the world, and which will enable both the companies and the East Timorese to profit from the resources. As to existing developments, East Timor had no part in devising the regulatory and fiscal regime now operating in the so-called Timor Gap. This was imposed by Indonesia and Australia without the slightest reference to the interests or concerns of the Timorese people. Nonetheless, the Timorese leadership recognises that companies should not pay the price of an illegal occupation, therefore the Timorese leadership has made a commitment, which

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<sup>153</sup> Pers. Comm. Peter Galbraith, August 2004.



I am authorized by the Cabinet to repeat here today to you, that with regard to existing developments, the future East Timor regulatory and fiscal framework will be no more onerous than that in place at the time Indonesia pulled out of East Timor. The scale of the resources in the Timor Sea is vast: Bayu-Undan holds 3 TCF [trillion cubic feet] of gas, Greater Sunrise nearly 10 TCF, Laminaria, Buffalo and Elang Kakatua are producing more than 220,000 barrels per day. The UN has continued the pre-existing regulatory and fiscal frameworks during its administration and the East Timorese leadership promise a new framework that will be more modern, stable and more business friendly. Under the circumstances, I would like to stand before you and declare the Timor Sea open for business. Unfortunately at the moment I am unable to do this, I can not say when it will be open for business.<sup>154</sup>

The language used was both vivid and extremely intense. In the speech, Galbraith referred to the torture and slaughter of East Timorese under Indonesian occupation within the context of Australia's recognition of that occupation and the subsequent conclusion of the 1989 Timor Gap Treaty. The use of such emotive language was intended as an influence tactic. Galbraith crafted the speech around three central points: namely, the position that UNTAET had adopted was morally and legally justified; that, if Australia agreed to UNTAET's terms, it would still be gaining far more from development than East Timor, through downstream processing of the resources; and, importantly, that UNTAET had resolved to stand firm on the crucial issue that East Timor should have the power to determine the manner in which petroleum is exploited and the financial terms under which exploitation occurs north of the median line:

...Neither Mari Alkatiri nor I can bring back East Timor a treaty that would give East Timor less economic benefit than that which it is entitled under international law. This does not simply mean a share of the revenue, but also the ability to design and implement a tax and petroleum regime suited to East Timor's particular circumstances. And if there is any doubt about our

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<sup>154</sup> Address by Ambassador Peter Galbraith, Cabinet Member for Political Affairs and Timor Sea, East Timor Transitional Government, to the APPEA Conference and Exhibition, Hobart, Tasmania, 9 April 2001. See Galbraith, P., 2001. 'East Timor's Rights in the Timor Sea', *Maritime Studies*, vol.118 (May-June):1-5.

entitlement, we are prepared to have our position examined, and if necessary decided, in any neutral forum.

...In summary, we see a great opportunity for East Timor and Australia in the Timor Sea. With East Timor the petroleum industry has a partner that promises a reliable, stable and exploitation-friendly future. The uncertainty about East Timor's future is over, and we promise a regulatory regime that is transparent, straightforward, and honest. Only one hurdle remains – the need for a treaty. Without a legal arrangement that resolves the status of the Timor Sea there can be no pipeline to bring gas ashore from Bayu-Undan or Greater Sunrise. While these matters may be capable of being settled independently of an overall treaty, they cannot be settled before there is such a treaty.

...I realize many key investors are looking to have greater clarity by mid year. Mari Alkatiri and I are prepared, as we have been for the last year, to continuously negotiate with the Australian government to resolve these matters. We also recognise, however, we may have to wait and that both Australia and East Timor may lose important markets. Mari Alkatiri has, however, asked me to remind you that the Timorese people are a patient people, and, when it comes to their rights, a very determined people. For 24 years, they fought the world's fourth largest country, matching handmade weapons against the latest weaponry. In the end the Timorese prevailed. And, without a treaty based on international law, the East Timorese are prepared to wait patiently for their rights.<sup>155</sup>

The warning that East Timor (and thus the companies involved) might lose out on “important markets” provoked an extremely hostile reaction. After hearing the speech, Minchin spoke urgently with the Prime Minister and Foreign Minister, whose immediate reaction was to lodge an official complaint with the UN Secretary-General. Combining with Phillips, the government made efforts to use US pressure - through the US Ambassador to Australia, the State Department in Washington, D.C. and the US Mission to the UN – to bring an end to Galbraith's involvement in the negotiations and to terminate his employment within

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<sup>155</sup> *Ibid.*

UNTAET completely.<sup>156</sup> Galbraith was castigated for placing project development in jeopardy. Geoffrey Barker, a leading columnist for the *Australian Financial Review*, wrote an abusive attack, describing Galbraith as a “moral zealot”, whose “hatred of Indonesia and Australia was stronger than his commitment to East Timor”.<sup>157</sup> Attempts to dislodge Galbraith proved futile however, as he was not there to push his own agenda. Though accused of being on a “personal crusade”, it is difficult to see any other rationale underlying his actions than that of simply wanting to negotiate the best possible treaty that could be arranged for East Timor, for which he enjoyed the full support of Gusmão, Alkatiri and de Mello. Galbraith was willing to make an enemy of himself with a major US oil company and one of America’s most important regional allies, to advance the interests of East Timor.

The reaction of the Australian government created tensions between UN Headquarters and UNTAET. On 12 April, de Mello cabled Guéhenno to defend Galbraith’s handling of the issue. He explained:

Given the talk in the media of East Timor ‘playing hard ball’ and ‘dropping bombshells’, it is important to stress that the UNTAET/East Timor position in the negotiation has not changed since March 2000 when the Australians were informed that, as of independence, there would be no arrangements in place to govern the petroleum activities in the Timor Sea. In all the negotiations it was made clear to the Australians that the terms of the 1989 treaty had been extended to cover the period up to independence. The treaty itself has never been considered valid, neither by the UN nor the East Timorese, and would not be renewed in its current form. Our position to date has been entirely consistent with this premise.<sup>158</sup>

Furthermore, de Mello emphasized that:

Whilst it is true that UNTAET, at the request of the East Timorese leadership, has been taking the lead in the negotiations, this has always only ever been in close conjunction with Mari Alkatiri, the cabinet member for economic affairs,

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<sup>156</sup> ‘US backs Australia on Timor Gas’, *Australian Financial Review*, 28 April 2001; ‘UN talks put Timor gas under pressure’, *Australian Financial Review*, 4 May 2001.

<sup>157</sup> ‘Timor led to edge of gap’, *Australian Financial Review*, 23 April 2001.

<sup>158</sup> Cable from S. V. de Mello to J. M. Guéhenno, ‘Timor Gap Second Round Follow-up’, 12 April 2000.

who has been present at all rounds of talks and who has fully endorsed the position adopted. Further, we have maintained a continuous dialogue with the presidency of the CNRT (who selected Alkatiri as the organisation's representative on this issue) on the progress of the negotiations and obtained his imprimatur for the position taken.<sup>159</sup>

After the speech, Galbraith returned briefly to Norway. Alkatiri returned to Dili and informed a UN press briefing that the second round of formal talks had been a “setback”.<sup>160</sup> However, he said that there had been an opportunity to meet informally with Senator Nick Minchin, which had apparently been “the most fruitful of all negotiations”.<sup>161</sup> When Galbraith returned to Dili at the end of April, the political landscape had dramatically changed. Having tried and failed to remove Galbraith from the UN administration, Australia's position underwent a major review. It seems the Hobart speech had sent a powerful charge through the Australian government, which was now prepared to make substantial concessions in order to avert a total collapse in the talks.

### ***5.5 Brisbane and Dili, May 2001***

The Hobart speech was indeed a watershed in the negotiations. When the parties resumed discussions in Brisbane, during the first week of May, they moved swiftly back to the point which had been reached in Cairns in December 2000. The main issues that were discussed covered the institutional architecture, the applicable law, unitisation, the pipeline and the revenue split. Galbraith insisted that a Non-Paper be produced so that both sides had a clear record of what had been discussed. With respect to the institutional architecture, the parties reverted to the three-tiered structure (Designated Authority, Joint Commission, and Ministerial Council) with a system of inequality embedded within the Joint Commission. On the question of royalty and taxes, it was agreed that East Timor would have fiscal control over its share of petroleum and/or revenue, and Australia would have fiscal control over its share. The treaty would contain no specific details on unitisation – only an obligation for both sides

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<sup>159</sup> *Ibid.*

<sup>160</sup> UNTAET Daily Press Briefing, 12 April 2001.

<sup>161</sup> *Ibid.*

to try to reach an agreement, which would be without prejudice to the claims of the two states to the seabed.

With regard to the issue of applicable law, Australia's position was that the 1989 treaty should serve as the model with the applicable law contained in a Petroleum Code that would form part of the treaty, whereas UNTAET wanted East Timor's law to be the applicable law. Galbraith saw the negotiation of a new Mining Code as a possible compromise between these alternatives. The Non Paper also specified that different fiscal regimes for Bayu-Undan and Greater Sunrise would be given consideration. Finally, in relation to the revenue split, it was confirmed that the Australian government was now offering East Timor 85 percent. The leader of the Australian delegation, David Ritchie (Department of Foreign Affairs and Trade) advised that Australia "would start some serious drafting on the architecture and the options on applicable law that would protect East Timor's position".<sup>162</sup>

The UNTAET Cabinet endorsed the substantive elements contained within the Non-Paper and authorized Galbraith and Alkatiri to approve an agreement along those lines. A "Proposed Timor Sea Arrangement" was subsequently drafted by the Australian government and a copy given to UNTAET, on 23 May. This served as the basis for the next round of talks, held in Dili six days later. The two sides proceeded by working through the proposed text and, by the afternoon of 30 May, most of the articles included within the Arrangement had been agreed. The new regime applied only to Zone of Cooperation Area A, which was renamed the Joint Petroleum Development Area (JPDA), and it incorporated all of the key elements of the Brisbane Non-Paper. The only contentious articles that still remained bracketed within the Draft Arrangement related to the revenue split and pipeline jurisdiction. It was agreed that these issues should be determined outside of the negotiations at the political level, between Ministers as opposed to government negotiators. Australia's position was that the resources in the JPDA should be split 85%/15% and that jurisdiction over pipelines from the JPDA should be under the state where the pipeline lands. UNTAET's position was that pipelines should be under the jurisdiction of East Timor and resources should be divided 90%/10%.

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<sup>162</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 3 May 2001.

NON-PAPER:  
**Approaches discussed but not agreed to**  
Brisbane, Australia  
3 May 2001

(1) The Area: (Zone A) without prejudice to a future seabed delimitation or either side's view of boundaries.

(2) Bayu Undan Gas: Investigate the feasibility of a well-head royalty combined with application of a profits royalty system (may be related to profit phase of PSC system).

(3) If East Timor achieves what it regards to be a satisfactory well-head royalty (ET preliminary view of 50 cents (US) per 1000 cubic feet) and profits based royalty, it would agree to a pipeline under Australian jurisdiction and regulation with provisions to ensure that other Area gas is not crowded out.

(4) Architecture: 3 tier system:

(1) A designated authority responsible to the Joint Commission, will handle the management of the day-to-day petroleum operations in the Area. For a defined period of time, the designated authority will be substantially the same as the technical and financial directorates of the current Joint Authority. After the defined period of time, the designated authority will be the appropriate East Timorese government ministry. The defined period of time could be extended by mutual agreement.

(2) A Joint Commission with an East Timorese majority of one shall be responsible for the implementation of the Treaty and the oversight of petroleum activities subject to the Treaty. The Commissioners of either country may refer a matter to the Ministerial Council for resolution.

(3) A Ministerial Council consisting of an equal number of Ministers from Australia and East Timor shall meet to resolve a matter referred to it by the Joint Commission and/or at the request of either government, and normally at least once a year.

(4) In the case of Ministerial deadlock, an agreed dispute resolution (arbitration) mechanism can be invoked.

(5) Applicable Law: East Timor's position is that East Timorese law should be the applicable law (with incorporation of elements of Australian law). Australia's position is that the Petroleum Code should be agreed to between East Timor and Australia and form part of the Treaty. As to the other applicable law, Australia's view is reflected in the paper given to the East Timor side on 4 April 2001. In the interim, existing developments (Bayu Undan liquids and Elang Kaktua) should proceed on the basis of existing law. (However, East Timor believes that a valid PSC contract must be signed after a Treaty comes into force). Australia believes that existing law should apply to future developments until a new Petroleum code is agreed

(6) Unitization: Both sides will try to reach an agreement or arrangement to facilitate the unitization of petroleum reservoirs in part located in the Area and in part located outside the Area. This agreement or arrangements shall be without prejudice to the claims of the two states to the seabed.

(7) Revenue Split: Australia has made a new offer on revenue split, which East Timor is considering

(8) Royalty and Taxes: East Timor law will apply to East Timor's share of petroleum and/or revenue. Australian law will apply to Australia's share.

A large part of the discussion in Dili focused upon the issue of the fiscal arrangements for gas production. UNTAET's preference was for a flat rate well-head royalty, as this would reduce East Timor's exposure to the risk of falling prices and would be an easier system to administer. Australia showed a willingness to consider alternative systems. The companies, on the other hand, had lobbied hard in opposition to any changes to the terms of the existing PSCs, especially those providing for cost recovery and investment credits. The issue of the investment credits was extremely sensitive. Under the terms of the 1989 Treaty, firms were entitled to recover investment credits as a quantity of petroleum production equal in value to 127 percent of their exploration and capital costs incurred. Thus for every dollar invested by the companies, they were entitled to recover a \$1.27 credit, in addition to the original expenditure. Given that capital costs for Bayu-Undan would be about US\$1.4 to 1.5 billion, Galbraith considered that this recovery rate would not only provide the companies with a huge source of bonus income but "would clearly operate at the expense of a poor country, which was set to receive limited downstream benefits from these developments".<sup>163</sup> Under the terms of the Draft Timor Sea Arrangement, East Timor's right to retain the existing PSC arrangements or adopt an alternative system had been preserved. Whilst the companies wanted their existing contracts to be locked into the new treaty, Galbraith wanted maximum flexibility and the ability to design and implement a new fiscal scheme compatible with the particular needs and preferences of the East Timorese.

Notwithstanding these few outstanding issues and problems, however, there was a palpable sense of optimism on both sides.<sup>164</sup> After the conclusion of the two days of negotiations in Dili, Galbraith told reporters that: "Great progress was made and a great number of issues were resolved".<sup>165</sup> The basic framework of the new regime was in place and the gap on the remaining issues was narrow. The increasing pressure on the parties to reach a settlement had generated a momentum towards agreement which, it seemed, both sides now felt lay within their grasp.<sup>166</sup>

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<sup>163</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 30 May 2001.

<sup>164</sup> 'Negotiations make progress', *Reuters*, 30 May 2001; 'Timor treaty near', *The Australian*, 31 May 2001.

<sup>165</sup> UNTAET Daily Press Briefing, 30 May 2001.

<sup>166</sup> 'Aust/Timor officials optimistic on Timor gas, oil talks', *Australian Associated Press*, 28 May 2001.

## 5.6 Canberra, June 2001

In the second week of June, Galbraith led a delegation to Canberra for a further round of discussions. On 12 June they met with officials from the Department of Industry, Science and Resources (DISR) to discuss the merits of three alternative fiscal regimes for Bayu-Undan and Greater Sunrise. On the UNTAET delegation were three independent economic policy consultants, including Philip Daniel who had co-authored an IMF report on *East Timor: an agenda for petroleum fiscal issues*, in January 2001.<sup>167</sup> Daniel specialized in the petroleum and mining industries and had an extensive experience of tax and production sharing regimes for these industries and of fiscal matters in general. The three options given consideration were the existing PSC regime, a flat rate royalty scheme, or an *ad valorem* royalty scheme. Revenue streams had been modeled by DISR using an 85-15 revenue split for the JPDA and a 20:80 unitisation of Greater Sunrise, which generated three broadly comparable sets of figures of about US\$3.5 billion for East Timor over a twenty year period. Revenues for Australia from the JPDA, based on its 15 percent share, amounted to about US\$500 million. When converted into Australian dollars, the total revenues from the JPDA were calculated to be \$7 billion for East Timor and \$1 billion for Australia.<sup>168</sup>

Hartwell informed the meeting that eight representatives from the oil companies – four from Phillips and four from Woodside – would be in Canberra the next day, 13 June, and wanted to meet the UNTAET/East Timor delegation. He explained that the simple signing of a framework agreement without the resolution of the fiscal regime would not give the companies the comfort they required to commit to the LNG project. Galbraith insisted that UNTAET/East Timor was not prepared to be rushed or intimidated by the companies and that all fiscal options were to remain on the table. He pointed out that East Timor and Australia had a shared interest in concluding the Arrangement and that the treaty would have no value if there was to be no development that resulted from it. Whilst recognising that the companies needed a reasonable rate of return, however, he explained that East Timor would have a problem in accepting a continuation of the existing PSCs because of the investment credit uplift. Galbraith wanted the investment credit eliminated. He considered that the oil

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<sup>167</sup> Sunley, E. M., Daniel, P., Mooij, H. and A. Schimmelpfennig, 2001. 'East Timor: an agenda of petroleum fiscal issues', International Monetary Fund, Fiscal Affairs Department, Washington, D.C.

<sup>168</sup> These figures were based on extremely conservative estimates for the long-run price of condensate (\$20/barrel) LPGs (\$15/barrel) and natural gas (\$0.90 cents/gigajoule).



companies had taken a risk by exploring in a “stolen area” and East Timor would not credit them for taking that risk.<sup>169</sup>

On 14 June, the UNTAET delegation met with Foreign Minister Downer and Resources Minister, Nick Minchin, for the first Ministerial-level meeting of the parties. The Australian delegation included four officials from DFAT, one from the Attorney General’s Department and John Hartwell from DISR. The meeting was scheduled to coincide with the fourth international donors’ conference on East Timor, which was being held in Canberra on 14 and 15 June. Referring to the revenue split in the JPDA, Downer opened the discussions by remarking, “we have come a long way from 50-50”.<sup>170</sup> He explained that Australia’s bottom line had been 80%/20% in favour of East Timor, but as UNTAET had insisted on 90%/10%, the Australian Cabinet had agreed to split the difference, resulting in the Australian offer of 85%/15%. He continued that the question of the percentages had become a political issue, as the Australian Opposition had supported East Timor’s 90/10 claim, which he felt was unfortunate. He argued that the current offer would not be a great deal for Australia, as already, under the 85%/15% division, “\$7 billion would go to East Timor and only \$1 billion would go to Australia”.<sup>171</sup> Downer noted that there were two other issues, one of which was pipeline jurisdiction. He said that Australia would be happy to talk to East Timor about the question of the pipeline, “but how exciting can a pipeline be?”<sup>172</sup> He asserted that Australia would not be prepared to cede control of the pipeline if it was in Australian waters. The second issue “where more work needed to be done” was unitisation.<sup>173</sup> Downer emphasised the fact that Australia was being generous to East Timor in terms of foreign aid and “changing [the unitisation] percentages without changing the boundaries would be a problem”.<sup>174</sup>

Minchin referred to the two issues of industry concern: namely, the continuation of the existing PSCs and the question of the fiscal arrangements for future projects. He reminded the UNTAET team of the CNRT’s commitment to honour the companies’ existing contracts and to adopt a tax regime that was no more onerous than that which currently applied. Galbraith explained that the process of creating certainty for the oil companies was a several stage procedure, starting with the conclusion of the state-to-state agreement. He noted how the oil companies had been “stunningly inflexible” on the question of the existing PSCs during their

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<sup>169</sup> Pers. Comm. Peter Galbraith, August 2004.

<sup>170</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 14 June 2001.

<sup>171</sup> *Ibid.*

<sup>172</sup> *Ibid.*

<sup>173</sup> *Ibid.*

<sup>174</sup> *Ibid.*

discussions the previous day. However, the meeting had improved when Australian officials made the point that “this is not Indonesia anymore” and also that the investment credit contained in the PSCs had been “an incentive to invest in disputed territory”.<sup>175</sup> Galbraith reminded the Australian delegation that the two sides were now in substantial agreement on many aspects of the new regime and thus a future East Timorese government would be faced with a relatively simple decision of whether to accept the Arrangement as the text of a treaty or not. However, he repeated that the first step was to conclude the state-to-state agreement and the second step would be to talk to the companies about devising an appropriate fiscal regime.

Galbraith confirmed his understanding that, in relation to the state-to-state agreement, there were basically three outstanding issues: Sunrise unitisation; the overall revenue split for the JPDA; and, the pipeline. On the first issue, he stressed that it was important for Australia to understand that “if unitisation takes place along the 1989 line, and East Timor were to accept that Australia was on the ‘other side’ of the line, then East Timor would be conceding territory: this would be impossible for UNTAET/East Timor to agree to”.<sup>176</sup> He thought that it was necessary for both sides to be creative and from that standpoint welcomed how the question of unitisation had been “finessed” in the current text of the Draft Arrangement.<sup>177</sup> Downer agreed that the issue needed to be given more thought but suggested that UNTAET was pursuing the issue “because you just want more dough”.<sup>178</sup> Galbraith argued that it was not an attempt to get more dough; rather, it was an attempt on the part of UNTAET and East Timor not to concede territory. With regard to the third issue, the pipeline, he explained that there were two ways of addressing this issue: either the Norwegian model or the Australian way. On a practical level, he noted that UNTAET wanted an open access and standard tariff regime, which he believed was Australian policy also. However, the pipeline had tax implications. Galbraith indicated that the UNTAET position was that Australian jurisdiction could be accepted if taxation revenue from the commercial operation of the pipeline was split equally. The only alternative solution was for the pipeline to be tax exempt, or for it to have low tariffs. The latter solution would increase the value of the gas at the well-head, thus being to the benefit of East Timor.

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<sup>175</sup> *Ibid.*

<sup>176</sup> *Ibid.*

<sup>177</sup> *Ibid.*

<sup>178</sup> *Ibid.*

The short answer given by Downer to this proposal was “we are already being generous”.<sup>179</sup> Galbraith told the Foreign Minister that East Timor did not accept that Australia had moved from a position of 50-50 as, under international law, East Timor was entitled to a mid-point boundary. He also considered that the question of pipeline jurisdiction “should be seen as part of the global deal”.<sup>180</sup> As a possible compromise, Galbraith suggested that UNTAET would be able to move on the pipeline if an acceptable deal could be achieved with respect to the problem of unitisation. He argued that “the only real way of solving the question of unitisation of Sunrise is to treat it as 50-50”.<sup>181</sup> The Australian delegation referred to the special tax problems associated with Sunrise and the fact that the companies had insisted upon a ‘technical’ unitisation of Sunrise according to the 20:80 split between the ZOCA PSC tax regime and the Australian Petroleum Resource Rent Tax (PRRT) regime. Downer remarked that he could understand the UNTAET position on Greater Sunrise but that if it was unitised on a 50-50 basis then, “straight away, the Arrangement would be increasing the tax burden”.<sup>182</sup> As a possible solution, he suggested that Australia could collect the revenues based on the 20:80 division and “refund the money owed to East Timor”.<sup>183</sup> Minchin, again, referred to the CNRT’s ‘letter of comfort’ and maintained that “we have to deal with the companies on that basis”.<sup>184</sup> Galbraith informed him that East Timor was prepared to repudiate the ‘no more onerous’ commitment. Downer advised that “repudiating the letter would not be a good idea – the companies will go feral”.<sup>185</sup>

Both sides, at this point, faced a particular kind of strategic decision-making problem that can be conceptualised in terms of the arrangement of the costs and benefits associated with different outcomes. The last stages of any negotiation involve a complex judgment task of trying to settle on a particular course of action after weighing up the possible consequences. For East Timor, the costs of losing agreement were much higher now than they were at the start of negotiations. The terms on offer had drastically improved. The reasons behind the Australian Ministers’ obstinacy and intransigence stemmed from their perception of the asymmetry between the two sides in terms of the relative costs of ‘no agreement’. They

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<sup>179</sup> *Ibid.*

<sup>180</sup> *Ibid.*

<sup>181</sup> *Ibid.*

<sup>182</sup> *Ibid.*

<sup>183</sup> *Ibid.* Downer was essentially offering to make retrospective payments to East Timor if, under a future permanent delimitation, the existing lines were adjusted. But Australia had no intention of making concessions on a permanent boundary and thus it guaranteed East Timor nothing.

<sup>184</sup> *Ibid.*

<sup>185</sup> *Ibid.*

were banking on East Timor moving to bridge the final gap in order to avoid losing everything. The progression of the negotiations towards the final stages would become increasingly stressful. “Decisional conflicts” in the mind of the individual negotiator, Janis and Mann have observed, become more acute as the decision maker becomes aware of the risk of suffering losses from whatever course of action is selected and the difficulties of reversing whatever decision is taken.<sup>186</sup>

After leaving the room momentarily to confer privately on the matter, UNTAET returned with a compromise package offer. Galbraith explained that “in the interests of a speedy resolution to the negotiations, UNTAET and East Timor could agree to the following: (1) the creation of a pool of revenue from Sunrise, based on 80 percent PRRT and 20 percent PSC, subject to satisfactory arrangements being reached in relation to PSC investment credits) which would then be split on a 50-50 basis; (2) the pipeline to be under Australian jurisdiction and Australia to receive all the pipeline revenue; and, (3) an 87.5%/12.5% split on the overall revenue [from the JPDA]”.<sup>187</sup> UNTAET had gauged that an extra 2.5 percent of the JPDA and the loss of pipeline tax revenue would be a small price to pay for securing 50 percent of Greater Sunrise. Galbraith emphasised that time was running out, especially since there would not be a fully functioning government in East Timor from 15 July to 15 September. Downer stated that he would have to refer to his Cabinet colleagues on the substance of the offer but repeated that a “seven billion, one billion split was already bloody generous...I know where you are coming from, but I’m pessimistic”.<sup>188</sup>

Galbraith noted that the negotiations could not really progress at this point and stressed that the East Timorese position remained 90-10 and that the compromise offer was just a proposal. He said that in these sorts of negotiations, “it was often best to lock everyone up until they agreed...it may be necessary to think creatively about the problems”.<sup>189</sup> Downer commented that “the next steps may not be entirely productive, with broader discussions taking place between whole Cabinets”.<sup>190</sup> From UNTAET’s perspective, the meeting had been totally unproductive anyway. It had merely served as an opportunity for Australia to insist on its position. Afterwards, arrangements were made for further talks to be held in Canberra, in the week beginning Monday 25 June 2001.

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<sup>186</sup> Janis, I. R. and Mann, L., 1977. *Decision Making: a psychological analysis of conflict, choice, and commitment*, The Free Press, New York, p.46.

<sup>187</sup> *Ibid.*

<sup>188</sup> *Ibid.*

<sup>189</sup> *Ibid.*

<sup>190</sup> *Ibid.*

When the issue went back to the Australian Cabinet, the decision was taken that the UNTAET compromise proposal should be rejected and no further concessions should be offered. This was conveyed to UNTAET on 19 June. On that day, Stephanie Schwabsky, of the Australian Mission in East Timor, organised an impromptu meeting with the Transitional Administrator, Sergio Vieira de Mello. Minutes of the meeting were recorded by UNTAET staff. Schwabsky told de Mello that she had earlier heard from José Ramos Horta that there was to be a special meeting of the UNTAET Cabinet on the subject of the Timor Sea negotiations later in the day and that she wished to convey the decision of the Australian Cabinet regarding those negotiations before the UNTAET Cabinet met. She confirmed that the decision of the Australian Cabinet was that the offer of an 85%/15% revenue share was final and was part of a package. She stressed that “the Australian government considered the timing was extremely short on these negotiations and that it would not go beyond the terms of the package”.<sup>191</sup> Schwabsky passed de Mello a paper which detailed the Australian offer. The terms included: an 85%/15% revenue split for the JPDA, unconditional jurisdiction for Australia over the pipeline, the unitisation of Greater Sunrise 80:20 in Australia’s favour; and the resolution of gas fiscal arrangements by the time of the conclusion of the agreement. Schwabsky confirmed that all the points set out within the paper represented the final position of the Australian Cabinet.

It seems the Australian government calculated that with an 85/15 offer on the table, it would be impossible for the UN and East Timor to walk away from the deal. This take-it-or-leave-it ploy was risky but geared to obtaining a result that did not expose the government to criticisms of being too soft in the negotiations. To have conceded 90 percent of the JPDA plus 50 percent of Sunrise, as UNTAET had requested, would have been viewed by some in Australia, particularly within the oil industry, as a relinquishment of Australian sovereignty. Yet, it was viewed by UNTAET as an ultimatum – an almost callous bid to extract last minute concessions. Galbraith was particularly angered by Australia’s attempts to link the problem of Sunrise unitisation to the conclusion of the joint development regime. The strength of UNTAET’s ill feeling towards Australia’s ‘bottom-line’ offer was brought to John Howard’s attention through a letter written by Peter Galbraith and signed by the full UNTAET Cabinet. I have quoted the letter at some length to provide an accurate record of the concerns that were raised. It read as follows:

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<sup>191</sup> Minutes from Meeting with Stephanie Schwabsky, Australian Mission, ‘Timor Sea Negotiations’, 20 June 2001.

...Until our negotiating team went to Canberra last week, we had believed Australia and East Timor were close to an agreement. Indeed, our Cabinet had approved a nearly complete draft text negotiated with your side. The only bracketed items were the article on the pipeline and the actual percentages. In this context, we were therefore shocked to learn that you now insist that the Greater Sunrise gas field be unitised 20/80 in your favour as a condition of an agreement. As you know, this issue is one of the most difficult in the negotiations, as it impacts on the question of borders. For this reason, we embraced the proposal Australia put forward just a month ago, in Brisbane, on unitisation. Your negotiator, David Ritchie, put forward a compromise requiring the two sides to negotiate expeditiously on this matter. These negotiations were to take place after the framework agreement had been concluded. At the time he put forward the compromise proposal, Ritchie clearly explained that it was a way to overcome the impasse over Sunrise. We accepted your proposal in good faith and it is now incorporated in Article 9 of the draft Arrangement. Further, we remain willing to carry through the commitment you asked of us.<sup>192</sup>

...Your last minute demand for unitisation will make it difficult, if not impossible, to reach a framework agreement. Nonetheless, we are prepared to negotiate continuously toward that goal. Under no circumstances, however, will we accept a division of oil and gas based on your concept of the correct border. This is particularly important since your officials have publicly tried to link our acceptance of a framework agreement to an acceptance of your view of the boundaries. With regard to your demand that we agree to Australian jurisdiction over the pipeline, we note there are two models for pipelines

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<sup>192</sup> *Article 9* of the Draft Timor Sea Arrangement (15 June 2001) , which had been circulated at the meeting, contained two provisions on unitisation:

- (a) Any reservoir of petroleum that extends across the boundary of the JPDA shall be treated as a single entity for management and development purposes.
- (b) East Timor and Australia shall work expeditiously and in good faith to reach an agreement on the manner in which the deposit will be most effectively exploited and on the equitable sharing of the benefits arising from such exploitation.

Therefore, it contained no specific revenue sharing arrangements for Sunrise, but merely placed an obligation upon both sides to cooperate in resolving the issue.

exporting gas from the seabed of one country to the territory of another. In the most common model, jurisdiction over the pipeline rests with the exporting state, in this case the authority administering the JPDA. It is also possible for the pipeline to be under the jurisdiction of the importing state. In the interests of reaching an agreement, we are prepared to accept Australian jurisdiction over the pipeline as part of an overall deal that we see as fair to East Timor. We see no justification for Australia reaping all the financial benefits of the pipeline, especially since the revenues are inconsequential to Australia but represent nearly 40% of East Timor's annual budget.<sup>193</sup> We think it a reasonable compromise that the two states share the tax revenue generated by the pipeline. We understand that you offered such a sharing arrangement to Indonesia in the 1990s and we cannot fathom why you would propose to treat East Timor less well.

...In May, both Australia and East Timor were stunned to learn that the PSCs entered into pursuant to the Timor Gap Treaty contained terms far out of line with industry standards and any sense of fair play. Comparable Indonesian PSCs (which served as the model for the Timor Gap Treaty PSCs) allow contractors to recover their investment plus 17% before profit sharing with the resource owner begins. This investment credit is intended to compensate for additional burdens placed on the contractor, such as a requirement to supply the domestic market at controlled prices, and to permit state participation. Timor Gap Treaty contracts contain none of the burdens of the Indonesian PSCs. Yet they provide contractors with an incredible 127% investment credit, meaning that investors get back \$2.27 for every dollar spent on capital and exploration. This is paid to the contractor before any profit is shared with the resource owner, and is so extreme that in most PSCs there will be no profit for the resource owner. In the case of Bayu-Undan, this will cost East Timor and Australia \$1.7 billion more than under a standard Indonesian PSC. There are no geographic or geological circumstances that would justify such outsized pay-offs to the contractors. We can only conclude these rewards were provided

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<sup>193</sup> UNTAET were working on the assumption that pipeline revenues would be worth US\$12 – 15 million per annum.

to compensate contractors for the political risk of exploring and developing petroleum in an area that the United Nations repeatedly said did not belong to Indonesia. The determination of the East Timorese people to be free, at great loss of life and treasure, made the Timor Gap politically risky and thus prompted Indonesia and Australia to make the extraordinary offer to contractors.

...We recognise that our differences over the oil and gas resources of the Timor Sea will not be easy to resolve. Commercial and maritime disputes are not uncommon as between neighbours and close friends. For more than 60 years the Australian and East Timorese people have stood shoulder to shoulder. From the Second World War, where East Timorese sacrificed their lives in blocking a Japanese invasion of Australia, to INTERFET, where Australia rescued East Timor, the fates of our two countries have been intertwined. East Timorese will never forget the courage and generosity of Australians who came to our rescue in our moment of need. As political leaders, we would readily reward Australia a generous share of our resources in the Timor Sea. We are, however, not only the leaders of today, but the custodians of tomorrow. Each concession we make deprives a child of education and a family of health care. Nonetheless, assuming the other terms are satisfactory, we will agree to provide Australia with 15% of the revenues of our part of the Timor Sea, as you requested. We are mindful of the July deadline for critical investment decisions. However, it is not our fault that the negotiations are at this stage. After the highly productive informal rounds in Singapore and Cairns last November/December, we were prepared to resume negotiations in January this year. Unfortunately, the Australian Cabinet did not take up the matter until April, and then fielded an almost entirely new negotiating team.

Given the time constraints, ever-shifting negotiating positions make it difficult to meet the deadline. Therefore, at this late stage, we believe the only way forward is to proceed with the nearly complete Timor Sea Arrangement. We realise that the Arrangement does not solve every issue investors want



resolved. However, with the framework in hand, we will work with you to give them the necessary confidence and certainty to move forward.<sup>194</sup>

The letter was a final push on the part of Peter Galbraith to salvage a better deal for East Timor. At this critical stage in the talks, a final meeting was convened in Canberra, on 28 June 2001. Galbraith and Alkatiri were joined by José Ramos Horta and the Australian government was represented by Downer, Minchin, the Treasurer, Peter Costello and the Attorney-General, Daryl Williams. Each of the Ministers had one advisor from their respective departments. Any written record of the last meeting, if it exists, has not been made available for the purposes of this research. It was an extremely tense and heated confrontation. According to one of the officials present, Alkatiri resisted Downer and Costello “bearing down on him” for several hours.<sup>195</sup> An agreement was finally reached through a deal brokered between Ramos Horta and Downer in a one-to-one discussion.<sup>196</sup> East Timor conceded on the issues of the pipeline and unitisation, whilst Australia conceded on the revenue split.

Thus, it was agreed that JPDA resources would be split 90%/10% in favour of East Timor; Sunrise would be unitized on the basis of 80:20 in Australia’s favour; and, Australia would have jurisdiction over the pipeline. In addition, however, the Australian government agreed to give “additional financial support” to East Timor worth AUD\$8 million per annum for each year of the pipeline’s operation. This was in lieu of a share of the taxation revenues that the pipeline was expected to generate. UNTAET also agreed, at Australia’s insistence, to continue the PSC’s for Bayu-Undan and Greater Sunrise. However, they did so on the understanding that East Timor would use its taxation powers under the treaty to re-claim the value of the investment credits. Ramos Horta played a crucial part in pulling the final strands of the agreement together but his pro-Australian tendencies were the source of mistrust by Alkatiri and the UN. Both Galbraith and Alkatiri found Ramos Horta’s actions to be largely self-serving and they bore some resentment for the role he played at the final stages of the negotiations.

The agreement was officially signed in Dili on 5 July – by Galbraith and Alkatiri, for UNTAET/East Timor; and Downer and Minchin, for Australia. The Timor Sea Arrangement was included within a Memorandum of Understanding, which stated that, “the signatories...confirm that the Timor Sea Arrangement forming Attachment ‘A’ to this

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<sup>194</sup> Letter to Prime Minister Howard from the UNTAET Cabinet, 20 June 2001.

<sup>195</sup> Pers. Comm. Senior Australian Government Official, November 2005.

<sup>196</sup> Pers. Comm. Senior Australian Government Official, April 2006.

Understanding is suitable for adoption as an agreement between Australia and East Timor upon East Timor's independence, embodying arrangements for the exploration and exploitation of the Joint Petroleum Development Area pending a final delimitation of the seabed between Australia and East Timor".<sup>197</sup> The same day, UNTAET's Office of Communication and Public Information issued a press statement, outlining the key elements of the treaty (see below). From Galbraith's standpoint, it was extremely important that some statement be made to reflect the fact that, in accepting the 80:20 unitisation of Sunrise, this did not imply any acceptance that the eastern lateral line of the JPDA was an international boundary. The UNTAET press release stipulated that "East Timor has a strong claim under international law to 100% ownership of the seabed in the JPDA and 70% ownership of the seabed where the Greater Sunrise development is located".<sup>198</sup> It also confirmed that East Timor would use its taxation power under Article 5(b) of the treaty to recover all, or part, of the investment credits included within the PSCs for Bayu/Undan and Greater Sunrise, estimated to be worth US\$500 million.

Despite not having been able to achieve all of their negotiating targets, there was a large measure of satisfaction amongst UNTAET staff at the deal which had been reached, particularly with regard to the 90/10 split. On 6 July 2001, Galbraith and Alkatiri penned an opinion piece in the *Sydney Morning Herald*, in which they described the agreement signed in Dili as one that "rights a historic wrong".<sup>199</sup> Their main criticism of the Australian government was directed at the latter's insistence upon locking in the pre-existing PSCs for Bayu-Undan and Greater Sunrise within the new regime.<sup>200</sup> It was not just that these contracts were perceived as being fundamentally unfair to East Timor, which so incensed Peter

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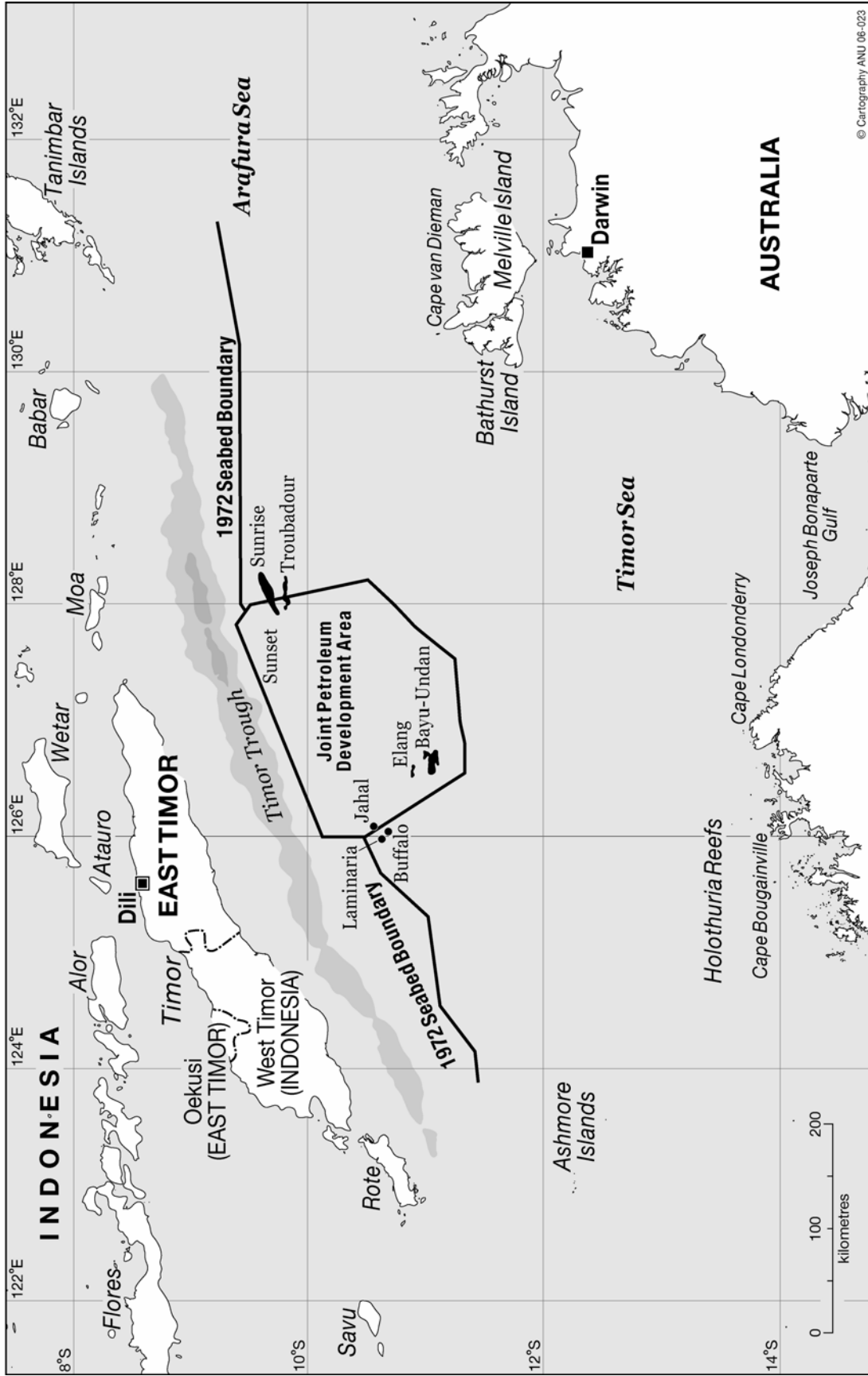
<sup>197</sup> Memorandum of Understanding of Timor Sea Arrangement, Dili, 5 July 2001.

<sup>198</sup> UNTAET media press release, 5 July 2001.

<sup>199</sup> 'Pouring oil on the troubled waters to our north', *Sydney Morning Herald*, 6 July 2001.

<sup>200</sup> *Ibid.*; Galbraith and Alkatiri wrote:

The new Timor Sea treaty is a fair deal for East Timor and an even better deal for Australia and the companies developing oil and gas in the Timor Sea. Yet the negotiations that achieved this were very nearly torpedoed in Canberra last week, when Australia insisted that East Timor continue the terms of contracts that companies had with Indonesia and Australia under the illegal 1989 treaty. This was an enormous problem for the East Timorese because the 1989 treaty had offered companies enormous financial incentives to explore in the Timor Sea. The incentives were not economically justifiable but reflected the political risk of investing in territory that did not rightfully belong to Indonesia. Even though East Timor had not been party to these unfair incentives, Australia expected East Timor to continue to pay these companies their premium...As a party to the 1989 treaty, Australia was concerned that changing the contracts could damage its reputation, as well as incur liability. To accommodate Australia, East Timor ultimately agreed to continue the terms of the contracts.



MAP 8

Timor Sea Arrangement: Joint Petroleum Development Area 'Closing Lines' and Major Oil and Gas Fields

**PRESS RELEASE**

**Information provided by the media by UNTAET OCPI**

Dili, 5 July 2001

Summary of Timor Sea Arrangement

- East Timor receives 90% of the production of oil and gas in the Joint Petroleum Development Area (“JPDA”) estimated to amount to US\$4-5 billion for East Timor over a 20-year period.
- East Timor retains its right to tax current and future developments on the JPDA according to its law.
- East Timor may devise its own fiscal scheme for future developments (e.g. through production sharing contracts, royalties etc.).
- East Timorese will receive preference for employment and training opportunities in the JPDA.
- The East Timorese Ministry responsible for petroleum activities will manage the day-to-day operations in the JPDA after a transitional period. It will be responsible to a Joint Commission where East Timor will be in the majority. A Ministerial Council made up of equal numbers from East Timor and Australia will be the final authority over matters in the JPDA.
- Twenty percent of Greater Sunrise Development falls within the JPDA. East Timor will receive 90% of this share.
- East Timor retains its right to seek a seabed delimitation in the Timor Sea. East Timor has a strong claim under international law to 100% ownership of the seabed in the JPDA and 70% ownership of the seabed where the Greater Sunrise development is located.
- Contracts in the Bayu-Undan and Greater Sunrise fields will continue on the same terms as before. These contracts contain financial incentives, not economically justifiable, to reward the exploration and exploitation of petroleum in a territory illegally occupied by Indonesia. These incentives would cost East Timor US\$500 million. As a party to the 1989 “Timor Gap Treaty”, Australia felt it had to stand behind these contracts. East Timor acceded to Australia’s demand to continue the contracts but will use its taxation power under Article 5(b) of the Arrangement to recover part or all of these unfair incentives.
- The pipeline from the JPDA to Australia will be under Australian jurisdiction. In lieu of taxes, Australia will provide AUD\$8 million in unrestricted assistance to East Timor for every year that the pipeline is in operation.

The Timor Sea Arrangement provides companies with additional certainty for their investments. In particular, the Arrangement avoids the legal vacuum that would otherwise have existed on the date of East Timor’s independence. East Timor remains committed to providing a stable climate for investors that promotes development of the petroleum resources in the Timor Sea.

UNITED NATIONS TRANSITIONAL ADMINISTRATION IN EAST TIMOR (UNTAET)  
OFFICE OF COMMUNICATION AND PUBLIC INFORMATION

Galbraith, but the fact that Australia had caved in to industry pressure. A great deal of time and energy had been spent in the negotiations analysing and discussing alternative fiscal systems for the JPDA on the understanding that there would be no obligation upon East Timor to continue the fiscal regime contained within the original contracts. During June, however, the oil companies had lobbied extremely hard on this issue and “impressed upon the Australian government their legal responsibilities towards contract holders”.<sup>201</sup> Australia eventually yielded to the companies to avoid being sued for breach of contract.

## CONCLUSION

The signing of the Timor Sea Arrangement marked the end-point to an extraordinarily difficult process of negotiation between the Australian government and the UN administration in East Timor. It had extended over a period of almost sixteen months, from March 2000 to July 2001. The agreement which materialized from this process was a world first for the United Nations, as never before had the UN negotiated a bilateral treaty on behalf of another country. “There was”, as de Mello noted, “no precedent for the U.N. sitting as a government across the table from another government”.<sup>202</sup> Challenges made by the Australian government to the legitimacy of UN involvement in these negotiations were prevailed over by the involvement of Mari Alkatiri at every stage in the process as well as the strong support of Xanana Gusmão and a majority-East Timorese Cabinet.<sup>203</sup> From the UN’s perspective, the outcomes reached had seemingly vindicated Galbraith’s decision to force Australia to the negotiating table and to undertake the challenge of renegotiating the old regime during the transitional period. The principle of equality and sovereign-neutrality, which had framed the 1989 treaty, had been comprehensively overhauled and, in all of the new regime’s key distributive dimensions, a clear emphasis in favour of East Timor meant that the situation was far closer to a position of East Timorese sovereignty north of the mid-point than it was to any notion of sovereign neutrality.

The sharing of revenue had moved dramatically in favour of East Timor. Within the zone, East Timor would have 90 percent of the government share of production and the ability to impose taxation on 90 percent of company profits. The concept of joint development had been retained but the roles of the two states would be very different. Australia’s status in the administration of the JPDA had been reduced to the point at which joint development was in

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<sup>201</sup> Pers. Comm. James Godlove, August 2004.

<sup>202</sup> Steele, J., 2002. ‘Nation building in East Timor’, *World Policy Journal*, vol.19(2), p.82.

<sup>203</sup> ‘Pouring oil on the troubled waters to our north’, *Sydney Morning Herald*, 6 July 2001.

fact closer to one of unilateral, rather than joint, control. Australia's claims to exclusive sovereign rights in the area remained valid yet severely undermined. As Triggs has pointed out:

The [1989] Timor Gap Treaty was scrupulous in preserving the respective juridical positions of Australia and Indonesia so that the treaty remained sovereign-neutral in its effect. By contrast, the new Timor Sea Treaty creates a structure that in certain respects distinctly favours control by East Timor through the proposed Joint Commission. While a 'without prejudice' clause technically protects the views of Australia and East Timor on seabed delimitation, future activities under the new agreement may render it increasingly difficult for Australia to insist upon its claim to sovereignty over the continental shelf up to the Timor trough.<sup>204</sup>

With respect to the revenue split, the pattern of concessions tells its own dramatic story in a neatly condensed form. Australia's share of JPDA resources fell from half, to a third, to a quarter and, finally, to just one tenth. This reflected a loss of almost half a billion barrels of oil equivalent in the Bayu-Undan field alone.<sup>205</sup> Australia's preferred position was 50 percent but they ended up with 10 percent. The question that needs to be asked is, why? The answer, as articulated in Chapter One, lies in the relationship between legal norms and strategic interaction. For both the UN transitional administration and the East Timorese leadership, conceptions of legal entitlement proved to be an extremely powerful motivating force that exerted influence through the inner dynamics of the negotiation interaction. As noted in Chapter Two, by privileging geography over geology and equity above all else, the decisions of international courts have given East Timor's negotiating position a special prominence over Australia's. Case law and precedent favours a median line boundary between opposite coastal states and this line became the obvious focal point for UNTAET for revenue sharing within the framework of a new interim petroleum regime. Anything substantially short of the 90-10 division of the JPDA and the UNTAET negotiating team

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<sup>204</sup> Triggs, G. 2002. 'The New Timor Sea Treaty', *Australian Journal of Asian Law*, vol.4(2), p.188.

<sup>205</sup> The proven and probable reserves of Bayu-Undan stand at almost 1.1 billion barrels of oil equivalent (boe). Australia's share prior to the conclusion of the Timor Sea Arrangement would have been 50%, or 550 million boe. At 10%, Australia's share is 110 million, i.e. a loss of 440 million boe.

believed it would be in East Timor's interest to break off negotiations and pursue a judicial settlement of the maritime boundary.

Australia did not necessarily need to be convinced of East Timor's claims, only that the cost of not conceding was 'no-agreement'. This is why Galbraith's speech, in Hobart in April 2001, proved to be such a decisive moment in the negotiations. It demonstrated that East Timor was prepared to fight for what was perceived to be the new nation's legal entitlement. This public commitment had an extremely powerful effect on the government. It shifted perceptions of the strength of UNTAET and East Timor's level of resolve, leading to a re-evaluation of the various risks involved for Australia. It was a watershed in the negotiating process. An official with the Department of Industry, Science and Resources said that whilst the speech upset investor confidence, "it helped focus people's attention on the issues".<sup>206</sup> Following the speech, the government moved rapidly to accommodate many of the UN and East Timor's key demands. Believing that the UNTAET team would not be moved in the core areas of revenue sharing and political/jurisdictional control of the zone, the government was forced into deciding between making concessions in these areas and aborting the talks completely. Given the high costs for Australia associated with the latter, in terms of loss of investment activity and a continuation of the dispute, the rational decision was to concede.

Thus, the influence of international law was not a direct form of influence; the Australian government was not moved by the 'power of the better argument'. The law exerted influence through the parties' strategies and tactics. Galbraith's planning and co-ordination of UNTAET's bargaining position and strategy was a key ingredient of UNTAET's success. Gavin Kennedy has noted that preparation is "the jewel in the crown of effective negotiation".<sup>207</sup> Within a remarkably short space of time, Galbraith had developed a clear position on a range of different issues, which allowed him to dominate the first round of discussions. This was achieved without any assistance from the UN Secretariat but with the help of just a handful of legal advisers and minimal financial resources. The United Nations Division of Ocean Affairs and Law of the Sea were not willing to commit legal or technical assistance to UNTAET in order to remain neutral in the dispute. Galbraith, somewhat like a jazz musician, had to rely on his skills of improvisation. Australia, on the other hand, despite having all the resources of its large government ministries, gave little consideration to the

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<sup>206</sup> 'Galbraith gets job done', *Upstream*, 6 July 2001.

<sup>207</sup> Kennedy, G., 2004. *Essential Negotiation*, Profile Books, London, p.157.

ways in which the negotiations could possibly develop. The government's strategy and approach was almost whimsical. It was malleable in the face of corporate pressure.

Indeed, the oil companies were continuously "walking into Downer's office", which was described to me by one government officer as a "leitmotif throughout the negotiations".<sup>208</sup> Australia's negotiators have acknowledged that they were outplayed and out-maneuvered by UNTAET in the negotiations. According to a senior DFAT official, "Alexander Downer proved to be no match for Peter Galbraith".<sup>209</sup> Galbraith was viewed by the Australian side as an "incredibly clever and aggressive advocate for East Timor...a formidable negotiator".<sup>210</sup> He was able to "up the ante and change the pace of the negotiations".<sup>211</sup> Galbraith's skill and experience meant that his personal involvement in the negotiations had an enormous impact upon outcomes, even to the extent whereby Australia's negotiators sometimes wonder "what could have happened without him".<sup>212</sup>

The final 'decision-making crisis' was resolved through a simple exchange of points. Writing in the *Australian Financial Review*, columnist Geoffrey Barker expressed the view that "the Australian side calculated that the 90/10 split was a fair price to pay for the Joint Petroleum Development Area...because, given the 1972 seabed boundary, it gave Australia the lion's share of the huge Sunrise gas field".<sup>213</sup> Barker was assuming that the apportionment of Sunrise had now been completely settled. Yet the situation was, in fact, far more complex. The Timor Sea Arrangement expressly stated that the revenue-sharing terms were to be "reconsidered" in the event of a permanent delimitation of the seabed between East Timor and Australia. Galbraith had personally drafted this provision (under Annex E, paragraph d) as a means of affording some legal protection to East Timor's claims to a larger portion of the reserves. If further concessions were not forthcoming in regard to the permanent delimitation of the seabed, it was in East Timor's power to take the dispute to the ICJ. The apportionment of Sunrise was therefore by no means concluded. East Timor still had other political options for pursuing what was considered to be a legitimate claim to a much larger share of the resource.

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<sup>208</sup> Pers. Comm. Senior Australian Government Official, April 2006.

<sup>209</sup> Pers. Comm. Senior Australian Government Official, June 2005.

<sup>210</sup> Pers. Comm. Senior Australian Government Official, April 2006.

<sup>211</sup> *Ibid.*

<sup>212</sup> Pers. Comm. Senior Australian Government Official, November 2005.

<sup>213</sup> 'The bottom line was not altruism', *Australian Financial Review*, 21 May 2002.



## 6. THE SUNRISE CONTROVERSY AND THE ‘50% SOLUTION’

Schelling has suggested that perceptually prominent alternatives serve a key function in permitting bargainers to come to an agreement. These alternatives acquire their salience because of their perceptual uniqueness, simplicity, or ‘good form’. Schelling has pointed out: ‘Most bargaining situations ultimately involve some range of possible outcomes within which each party would rather make a concession than fail to reach agreement at all...The final outcome must be a point from which neither expects the other to retreat; yet the main ingredient of this expectation is what one thinks the other expects the first to expect, and so on...These infinitely reflexive expectations must somehow converge on a single point, at which each expects the other not to expect to be expected to retreat’. A perceptually prominent agreement – for example, a ‘50-50 split’, ‘equal concessions’ – provides an obvious place to converge and to stop making or expecting further concessions. Research has provided some support for Schelling’s idea.<sup>1</sup>

This chapter continues the analysis of stakeholder interactions past the date of East Timor’s independence, on 20 May 2002, until the signing of the Treaty on Certain Maritime Arrangements for the Timor Sea, on 12 January 2006. Despite the conclusion of the Timor Sea Arrangement, the question of Greater Sunrise remained a source of deep division between the two sides. Australia’s objective was to manoeuvre East Timor into a position in which it accepted the lines of the JPDA as the *de facto* international boundaries – essentially, by embedding the Annex E provisions of the Timor Sea Arrangement within an international unitisation agreement. As East Timor was against that happening, the parties’ conflict of interest prevailed. Sunrise posed a dilemma for Australia because a failure to unitise on the basis of the existing line would not only result in a further erosion of federal revenues but, more importantly from the government’s perspective, would amount to recognition that East Timor’s sovereign rights extended beyond the limits of the JPDA. By contrast, the position of the new government of East Timor, led by Prime Minister Mari Alkatiri, was that an

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<sup>1</sup> Deutsch, M. and Schichman, S., 1986. ‘Conflict: a social psychological perspective’, in M. C. Hermann (ed.), *Political Psychology: contemporary problems and issues*, Jossey-Bass, San Francisco, p.240.

international unitisation agreement for Greater Sunrise should not be concluded until permanent maritime boundaries had been determined.

In this chapter, I investigate how this conflict of interest was eventually resolved. The analysis takes into account the political strategies pursued by the two governments as well as the actions of a diverse range of other stakeholders and interest groups who became involved in the dispute. The main objective is to understand the causes behind Australia's decision to finally accept East Timor's demands for a '50% solution' to Greater Sunrise. Although being the product of a dynamic chain of events that unfolded during a three year period, and over the course of several distinct phases of negotiation, it is argued that the Australian government's willingness to concede can best be understood as the product of the interaction between normative constraints and strategic behaviour. The chapter concludes with an appraisal of the causal dynamics of that interaction process.

### ***6.1 The Road to Independence***

The signing of the Timor Sea Arrangement took place just several days before major political changes were made in the administration of East Timor, in preparation for the final stages of the territory's transition to full independence. On 14 July, the 33-member National Council was dissolved and the next day a six-week election campaign began for the 88-member Constituent Assembly. The Constituent Assembly would become the first legislative body in an independent East Timor and would have the responsibility for drafting, as well as the authority to approve, the country's Constitution. Elections for the Assembly were held on 30 August 2001. Though sixteen different political parties fielded candidates for the elections, almost two-thirds (55) were won by FRETILIN. All 88 members were sworn in on 15 September and, five days later, Sergio Vieira de Mello appointed the "Second Transitional Government", comprising 20 ministers, vice-ministers and secretaries of state. This meant that all the Cabinet roles which had previously been exercised by international staff, including Peter Galbraith, were filled by East Timorese. Galbraith had left Dili after the interim replacement of the UNTAET Cabinet on 15 July, although would continue to remain in close contact with Alkatiri on Timor Sea matters. According to the UN, the new and enlarged administration was intended to "more closely prefigure the government structure of an

independent East Timor”.<sup>2</sup> It was the first time in history that executive government in the territory was controlled by East Timorese.<sup>3</sup> Mari Alkatiri was appointed Chief Minister and José Ramos Horta became the Senior Minister for Foreign Affairs. In national elections held on 14 April 2002, Xanana Gusmão was elected President.

After the intense and emotional period of negotiations between UNTAET and Australia during June, the commercial environment remained somewhat uncertain. The Phillips/Multiplex deal on the construction of the pipeline was allowed to lapse and, in August, Shell had put forward an alternative development plan for Greater Sunrise, thereby undermining Phillips’ Letter of Intent with El Paso.<sup>4</sup> In September, Methanex announced that it was considering alternative locations for the methanol plant originally planned for Darwin, on account of continuing delays and uncertainties relating to gas supply from the Timor Sea.<sup>5</sup> In retrospect, the El Paso deal seems to have been little more than a pressure tactic. Phillips had, for a number of months, been cultivating sales contracts for Bayu-Undan gas in Japan, the world’s largest LNG market.<sup>6</sup> Relations between the political parties throughout the second half of 2001, on the other hand, appeared to be relatively calm. Yet in the two months leading up to the date of East Timor’s independence, this situation suddenly and unexpectedly changed. The Australian government not only placed new demands upon East Timor for an international unitisation agreement (IUA) for Greater Sunrise to be concluded prior to the date of East Timor’s independence; the government also took the dramatic step of formally withdrawing from compulsory forms of third-party dispute resolution.

To prevent being exposed to the possibility of litigation on the question of maritime boundaries, the government executed two separate documents.<sup>7</sup> The first recorded Australia’s declaration that it did not recognise the compulsory jurisdiction of the International Court of Justice in any dispute concerning or relating to the delimitation of maritime zones. The second recorded Australia’s declaration that it did not accept any of the procedures provided for in section 2 of Part XV of the 1982 UN Convention on the Law of the Sea with respect to disputes concerning the interpretation or application of Articles 15, 74 and 83 relating to sea boundary delimitations. Both declarations were signed on 21 March 2002 and entered into force the following day. On 25 March, the government released a press statement announcing

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<sup>2</sup> UN doc., S/2001/719, 24 July 2001.

<sup>3</sup> *Ibid.*

<sup>4</sup> ‘Shell floats LNG spoiler’, *The Australian*, 10 August 2001.

<sup>5</sup> ‘Methanex may seek new site for large methanol project’, *Platts Commodity News*, 21 September 2001.

<sup>6</sup> Pers. Comm. Denis Burke, July 2004.

<sup>7</sup> Minister for Foreign Affairs and the Attorney General, *Joint Media Release*, ‘Changes to international dispute resolution’, 25 March 2002.

that “Australia’s strong view is that any maritime boundary dispute is best settled by negotiation rather than litigation”.<sup>8</sup> Prime Minister Howard referred to the protection of Australia’s sovereignty as a “legitimate national interest”.<sup>9</sup> The government had threatened to take such action on a number of previous occasions: ‘chiseling out’ of compulsory dispute resolution procedures had been described as Australia’s “get out of jail card”.<sup>10</sup> Yet, the timing of the decision was unexpected.

These developments appear to have been a response to a collection of different incidences and important changes in the strategic context for Australia during the latter part of 2001 and early 2002. One issue that emerged during this period concerned the possibility that East Timor might begin maritime delimitation negotiations with Indonesia. This had originally been proposed to UNTAET by Indonesian Foreign Minister, Hassan Wirajuda, in September 2001, and was publicly confirmed at a ‘High Level Bilateral Meeting between Indonesia and UNTAET/East Timor’ on 25 February 2002. In a joint statement that was issued pursuant to that meeting, the parties recorded the understanding that “Indonesia and East Timor will begin informal talks on the delimitation of maritime boundaries to prepare the ground work for formal negotiations”. This would have been of some concern for the Australian government because of the threat posed by Indonesia and East Timor potentially joining forces, either through negotiation or litigation, to have the existing lines in the Timor Sea redrawn.

A second factor which influenced the context related to the outcome of commercial tax negotiations between Phillips and East Timor, which had been ongoing since July 2001. An agreement had been reached in December which specified the fiscal arrangements that were to apply to the Bayu-Undan project.<sup>11</sup> A scheme was devised that had lower rates of return on downstream assets, such as the pipeline and liquefaction facilities, and higher rates of return on upstream operations. This intentionally worked to the advantage of East Timor, as against Australia, because of East Timor’s disproportionately larger share of the government revenues from upstream production in the JPDA. In effect, the deal squeezed the fiscal returns for Australia from downstream operations. For Phillips, it made no difference how the tax regime was structured as long as the overall tax burden delivered an acceptable

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<sup>8</sup> *Ibid.*

<sup>9</sup> ‘E. Timor inks oil accord with Australia’, *Kyodo News*, 21 May 2002.

<sup>10</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 23 November 2000.

<sup>11</sup> Fact Sheet 18, UNTAET Press Office, ‘Timor Sea’, April 2002; The agreement was titled the “Bayu-Undan Understandings”. It was subsequently incorporated into East Timorese law (No. 3/2003) on 1 July 2003.

rate of return. The Australian Treasurer, Peter Costello, was unhappy with the outcome to these negotiations, as he felt that Phillips and East Timor had collaborated at Australia's expense.<sup>12</sup>

A third factor which changed the context for Australia concerned the re-appearance of Oceanic Exploration during 2001, seeking to resuscitate its 1974 petroleum concession. On 17 January 2001, the President of Oceanic Exploration, Charles Haas, had written to the UN, both in New York and in Dili, "to request an opportunity to discuss...how the rights of Oceanic and Petrotimor can be protected".<sup>13</sup> Petrotimor (*Petrotimor Companhia de Petroleos S.A.R.L*) was the Timor-based subsidiary which had been created to administer the concession awarded by Portugal, on 11 December 1974. This concession was the only one in the area of the Timor Gap to have been granted by a "legitimate sovereign" in East Timor and, therefore, was considered by Oceanic to be a live asset – albeit one that had been lying idle for almost thirty years.<sup>14</sup> Representatives of the company had travelled to Dili in June 2001, to discuss with the UNTAET Cabinet the possibility of having the concession, which encompassed the entire Joint Petroleum Development Area, re-instated. In October, the company submitted a formal request to Sergio Vieira de Mello for an extension of the 1974 concession. The document stated that: "In conjunction with the grant of the Request, Oceanic and Petrotimor are prepared to work with the Second Transitional Government of East Timor and ultimately with the government of an independent East Timor to provide the necessary support required to establish its legitimate Exclusive Economic Zone in the Timor Sea".<sup>15</sup>

In order to regain title to the petroleum resources of the Timor Sea, Oceanic was prepared to support a case against the Australian government in the International Court of Justice for a permanent maritime boundary between East Timor and Australia. The company argued that a "legitimate seabed delimitation...would result in as much as 100% of the area known as Greater Sunrise falling within the new State's maritime jurisdiction rather than the 20% accorded to East Timor under the terms of Annex E of the proposed Timor Sea Arrangement".<sup>16</sup> The additional revenues that would be available to East Timor if it were to successfully litigate for 100 percent control of Greater Sunrise were projected to be US\$36

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<sup>12</sup> Pers. Comm., Philip Daniel, January 2005.

<sup>13</sup> Letter from C. Haas to S. V. de Mello, 17 January 2001.

<sup>14</sup> Oceanic Exploration, *Concession Request within Expanded Maritime Boundaries of East Timor*, October 2001.

<sup>15</sup> *Ibid.*

<sup>16</sup> *Ibid.*

billion.<sup>17</sup> Oceanic also highlighted the possibility of constructing a primary pipeline to East Timor, which “would not only make possible an LNG facility [in East Timor], it would eliminate the new State’s burdensome reliance in scarce foreign exchange reserves to import fuel for domestic energy requirements”.<sup>18</sup> It was noted that construction of gas processing and liquefaction facilities would result in “billions of US dollar investment in East Timor and create thousands of direct and indirect jobs with significant long term benefits to the economy”.<sup>19</sup>

To demonstrate the strength of East Timor’s case, Oceanic commissioned a legal Opinion, *In the Matter of East Timor’s Maritime Boundaries*, by Vaughn Lowe, Chichele Professor of International Law, Oxford University and a renowned international expert on maritime delimitation law.<sup>20</sup> The Opinion was co-authored by Christopher Carleton, the Head of the Law of the Sea Division, UK Hydrographic Office and Christopher Ward, of the Sydney law firm, Deacons. Drawing upon the major normative developments in the Law of the Sea contained in previous ICJ decisions, the authors noted that Australia’s seabed claim in the Timor Sea, based on the natural prolongation of the Australian shelf up to the Timor trough, was “inconsistent with international law”.<sup>21</sup> They also stated that “the eastern and western lateral lines of the 1989 Australia-Indonesia Timor Gap treaty (which are reflected in the 5 July 2001 Memorandum of Understanding) are equally indefensible in modern international law”.<sup>22</sup> It was argued that an ICJ decision would push the lateral lines outwards, which “would have the practical effect of placing most or all of the Greater Sunrise field within East Timorese jurisdiction, greatly increasing the resources under East Timor’s control”.<sup>23</sup>

The authors of the Opinion therefore advised that it would be “very imprudent” for East Timor to accept the proposed treaty arrangement with Australia “if it wished to preserve a claim to a wider entitlement particularly to any areas lying beyond the JPDA”; for a tribunal would regard the treaty “as limiting the area in need of delimitation to the area confined

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<sup>17</sup> *Ibid.*

<sup>18</sup> *Ibid.*

<sup>19</sup> *Ibid.*

<sup>20</sup> Lowe, V., Carleton, C. and C. Ward, 2002. *In the Matter of East Timor’s Maritime Boundaries: opinion*, unpublished, <http://www.petrotimor.com/img/LegalOp.pdf> <Accessed 19 May 2005> According to Vaughn Lowe, the Opinion had been written as Expert Witness, not as Counsel, and thus was an assessment of how a tribunal would decide the case, not even how East Timor should position itself to obtain the maximum result possible.

<sup>21</sup> *Ibid.*, para.36

<sup>22</sup> *Ibid.*, para.37

<sup>23</sup> *Ibid.*, para.41-2.

within the boundaries of the JPDA”.<sup>24</sup> Oceanic representatives arranged for these views to be given public exposure at a seminar in Dili, held on 23 and 24 March 2002. They had privately lobbied Ramos Horta as well as Peter Galbraith during January and February, for their support for the boundary dispute to be taken to the ICJ and to reject the Arrangement which had been negotiated with Australia. In November 2001, Oceanic representatives had personally advised Alkatiri that a permanent seabed delimitation could increase East Timor’s share in the JPDA from 90 to 100 percent and add additional producing areas on both the east and west laterals. Alkatiri was told that if East Timor re-instated Oceanic’s concession, the company would be willing to replace existing oil company contracts with equivalent ones but without the 127% cost recovery. Furthermore, the company would be prepared to contribute 10 percent of its net profits to the church or other charitable purposes in East Timor and invest an additional 10 percent in East Timor’s economy.<sup>25</sup>

On its face, this seemed like a pretty good deal that the company was offering but Alkatiri was unconvinced. He seems to have had suspicions about the company’s *bona fides* and its close links to some of his long-standing political rivals.<sup>26</sup> Furthermore, to renege on the Timor Sea Arrangement and pursue a litigated outcome would have been a risky course of action to take. Throughout the negotiations, Australia had been very hostile to any suggestion of the possibility of litigation and had warned that East Timor could expect reprisals from the Australian government if this option was pursued. Australia’s negotiators had let it be known that “there was simply not enough ballast in Australia/East Timor relations to sustain frontal litigation”.<sup>27</sup> The risks of litigation increased further when, on 12 March 2002, Phillips announced that a ‘Heads of Agreement’ had been signed with two Japanese utility companies for the purchase of three million tons of LNG per year.<sup>28</sup> This was a major commercial

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<sup>24</sup> *Ibid*, para.47.

<sup>25</sup> Record of meeting between Arthur Fredston, acting on behalf of Oceanic, and Mari Alkatiri, 1 November 2001.

<sup>26</sup> Oceanic Exploration is owned by American multi-millionaire entrepreneurs Neal and Linden Blue, who had close political links with the wealthy Timorese land-owning Carrascalão family. Joao and Mario Carrascalão had been leaders of FRETILIN’s long-time political opponents, the UDT. Mario had served as Indonesia’s governor of East Timor from 1982 to 1992 and was widely seen amongst members of FRETILIN as a collaborator. One must appreciate, also, the immense amount of pressure Alkatiri was under from Phillips to ignore Oceanic. Phillips was able to exert a tremendous amount of influence in Dili. In October 2000, the company had pressured Sergio Vieira de Mello into issuing an executive order prohibiting anyone from within UNTAET from talking to Oceanic without the express permission of his office. Phillips wanted to block Oceanic from having any kind of involvement in Timor Sea oil and gas development.

<sup>27</sup> Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 23 November 2000.

<sup>28</sup> ‘Participation in Bayu-Undan Project and Procurement of Darwin LNG’, *Press Release*, Tokyo Electric Power Company, 12 March 2002, <http://www.tepco.co.jp/en/press/corp-com/release/02031201-e.html> <Accessed 8 September 2005>

development. Feed gas for the LNG was to be sourced from the Bayu-Undan field and the proposed contract covered a 17 year production period, commencing in 2006. The deal would involve construction of a pipeline and LNG plant in Darwin, at a cost of about US\$3 billion. It seems that Alkatiri was disinclined to seriously consider litigation because he did not want to jeopardise the investment environment. Now that the Bayu-Undan tax arrangements had been finalised and a market for the gas had been secured, Alkatiri appeared to be firmly committed to both the project and the Treaty.

The sales agreement with the Tokyo utility companies also changed the political dynamics considerably in East Timor's favour. As Bayu-Undan gas would be developed as a stand alone project, commercial pressure upon East Timor to finalise arrangements for the unitisation of Greater Sunrise evaporated. Revenues from the liquids and gas components of Bayu-Undan would be more than sufficient to finance the country's basic needs in the short to medium term. From Alkatiri's standpoint, the issue of unitisation could therefore be revisited at a much later time within the context of boundary delimitation; and this would then provide a fresh opportunity of securing a larger portion of Greater Sunrise reserves. As a result, the Australian government found itself caught in an awkward strategic predicament. It had been outmanoeuvred in relation to the tax arrangements for Bayu-Undan; and, having already conceded so much of the JPDA, was therefore anxious not to lose any more of the petroleum reserves in Greater Sunrise.

Thus, after a period of several months since the conclusion of the Timor Sea Arrangement, during which time there had been little communication between the two sides concerning offshore matters, the Australian government began to apply enormous pressure upon Alkatiri to finalise an international unitisation agreement prior to East Timor's independence. The objective, it seems, was to embed the unitisation agreement within the joint development arrangement so that the 20:80 unitisation had the force of law. Alkatiri resisted this pressure, maintaining that ratification of the treaty "should not compromise his country's position on maritime frontiers".<sup>29</sup> The decision to withdraw from international dispute settlement mechanisms appears almost to have been a knee-jerk reaction to the atmosphere of uncertainty promoted by Oceanic during this period and a misplaced belief that key East Timorese personalities were "in the grip of unreason".<sup>30</sup> Internal warfare among

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<sup>29</sup> 'East Timor hits out at Australia over gap', 13 April 2002, *Australian Associated Press*.

<sup>30</sup> Pers. Comm. Senior Australian Government Official, July 2005.



several Australian Ministers as to how the government should proceed with the bargaining problem contributed to the Cabinet's lack of policy coherence.

At a high level ministerial meeting between East Timor and Australia on 10 May, the two sides agreed upon a political framework for handling the process by which the IUA for Greater Sunrise was to be concluded and the Timor Sea Treaty was to be ratified and brought into force. This was set out within a Memorandum of Understanding between the two countries signed on 20 May. The agreement embodied a fragile diplomatic compromise, which stipulated that:

1. The Government of Australia and the Government of the Democratic Republic of East Timor, reinforcing their wish to cooperate in the development of the petroleum resources of the Timor Sea in accordance with the Timor Sea Treaty ("the Treaty"), will work expeditiously and in good faith to conclude an international unitisation agreement ("the Agreement") for certain petroleum deposits in the Timor Sea known as Greater Sunrise by 31 December 2002.

2. The conclusion of the Agreement is without prejudice to the early entry into force of the Treaty, and is without prejudice to the agreement recorded in paragraph 9 of the 20 May 2002 Exchange of Notes between the Government of the Democratic Republic of East Timor and the Government of Australia which states that the Treaty is suitable for immediate submission to their respective treaty approval processes and that the parties will work expeditiously and in good faith to satisfy their respective requirements for the entry into force of the Treaty.<sup>31</sup>

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<sup>31</sup> On 20 May 2002, the date of East Timor's independence, Australia and East Timor signed three separate agreements:

- the *Timor Sea Treaty*;
- an *Exchange of Notes Constituting an Agreement between the Government of Australia and the Government of the Democratic Republic of East Timor concerning Arrangements for Exploration and Exploitation of Petroleum in an Area of the Timor Sea Between East Timor and Australia*; and,
- a *Memorandum of Understanding between the Government of Australia and the Government of the Democratic Republic of East Timor concerning an International Unitisation Agreement for the Greater Sunrise field*.

The Timor Sea Treaty incorporated the regime of the Timor Sea Arrangement. Although signed, the Timor Sea Treaty could not be ratified by the parties on this date and, therefore, did not have the force of law. Thus, pending the entry into force of the Timor Sea Treaty, the Exchange of Notes was agreed, which continued the existing legal framework as provided for under the Exchange of Notes of 10 February 2000, to avoid a legal

Australia's principal concern was with Clause 1 of this Memorandum of Understanding – with respect to the conclusion of the Sunrise IUA. East Timor had little interest in finalising unitisation arrangements at this stage but was greatly concerned with Clause 2 – the entry into force of the Timor Sea Treaty. East Timor's future economic survival depended on Bayu-Undan revenues; and production would not commence unless the Timor Sea Treaty was ratified by both states and had entered into force. The Memorandum of Understanding was drafted to prevent Australia from holding East Timor hostage on the ratification of the Treaty in order to secure a favourable outcome to the unitisation negotiations.

## ***6.2 IUA Negotiations***

The provisions for the unitisation of Greater Sunrise contained within the Timor Sea Treaty provided only a basis, or a starting point, upon which an IUA could be agreed. An IUA is a complex institutional arrangement, which normally establishes a comprehensive fiscal and regulatory framework to be applied to the development of a field that straddles two international jurisdictions and which governs operations over the lifetime of the project to which it applies. Annex E of the Timor Sea Treaty contained none of the detailed provisions that unitisation required; it was completely silent on the question of ownership but merely stipulated how production of Greater Sunrise was to be distributed between East Timor and Australia.

When IUA negotiations commenced in July 2002, East Timor was represented by Philip Daniel. The Australian delegation was led by John Hartwell. Australia wanted to rapidly conclude the negotiations by basing the agreement on the model of an existing IUA in operation in the North Sea. A draft Australian/East Timorese IUA based on a British/Dutch agreement had been prepared for the negotiations.<sup>32</sup> East Timor took a very different position, however. Daniel had been given instructions to treat the issue as a joint development area in recognition that Greater Sunrise was in disputed territory. The East Timor negotiating team

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vacuum. Under this arrangement, once the Timor Sea Treaty came into effect, all its provisions, including the 90/10 division of resources, would apply as from 20 May 2002.

<sup>32</sup> The agreement in question governed production of the Markham gas field, which straddled the British/Dutch boundary in the North Sea.

proposed creating another joint development zone for the Greater Sunrise area, with a separate Joint Authority to manage it.<sup>33</sup>

The East Timor position was a major set-back for Australia and, after the first round of negotiations, Hartwell was replaced by Geoff Raby (Department of Foreign Affairs and Trade). Raby advocated taking a hard-line against East Timor and, for tactical purposes, wanted to renege on the 20 May Memorandum of Understanding and make Australia's ratification of the Timor Sea Treaty conditional upon the conclusion of the Sunrise IUA. He explained the rationale behind this approach to the Parliamentary Joint Standing Committee on Treaties (JSCOT) in October 2002.<sup>34</sup> Raby advised the Committee that linking the Timor Sea Treaty with the IUA would, "from a negotiators point of view", increase "leverage around the negotiations".<sup>35</sup> He stated that the East Timorese interest "is with the early development of Bayu-Undan. We have some interest in Bayu-Undan, but Australia's bigger interest is demonstrably with the development of Greater Sunrise. To do the treaty without having concluded an IUA for Sunrise would leave us possibly in a situation of less confidence and less certainty than at present".<sup>36</sup> This approach was also encouraged by Woodside, the operator of Greater Sunrise, which warned the JSCOT that "the East Timor side may see benefit in allowing [the IUA negotiations] to drag as it becomes more important to Australia because Australia under the current structure enjoys more of the returns from the Greater Sunrise project. Allowing it to drag may be a negotiating tactic on the part of the East Timorese to extract more value out of the unitisation agreement".<sup>37</sup>

Reneging on a signed Memorandum of Understanding was highly unethical. What is interesting is the way in which Raby sought to justify this tactic. He explained to the Committee:

...there is a fundamental point here, and that is that it is Australia that made it possible for East Timor to realize its independence ambitions. We have a very large and expensive military presence in East Timor to underpin that act of

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<sup>33</sup> Pers. Comm. Philip Daniel, January 2005.

<sup>34</sup> The Timor Sea Treaty had been referred to the JSCOT by Foreign Minister Downer on 25 June 2002, consistent with Australia's international treaty ratification process.

<sup>35</sup> Joint Standing Committee on Treaties, Committee Hansard, 14 October 2002, p.275.

<sup>36</sup> *Ibid.*, p.273.

<sup>37</sup> *Ibid.*, 14 October 2002, p.262-4.

independence...ultimately we will be one of the main guarantors of the survival and stability of East Timor as an independent state.<sup>38</sup>

The rationale was one that used situational relativism. In other words, it was fair for Australia to act unethically in the negotiations due to the exceptional circumstances of Australia's relations with East Timor and the military and political commitment which had already been made to that country. It was a self-serving rationalisation designed to make a form of conduct seem acceptable that, by standard diplomatic protocols, would, in another situation, be deemed to be inappropriate.

The Committee, composed of cross-party Members of Parliament and Senators, were seemingly unperturbed by the ethical dilemmas posed by the government's tactics. They decided to endorse the negotiating strategy advocated by Raby and, in the Committee's Report on the Timor Sea Treaty, released in November 2002, advised that the International Unitisation Agreement for Greater Sunrise to be concluded "on or before the date on which the Timor Sea Treaty is ratified".<sup>39</sup> The one exception within JSCOT was the leader of the Australian Democrats, Senator Andrew Bartlett, who submitted a Minority Report which opposed this recommendation.<sup>40</sup>

What the Committee was advocating was clearly in breach of the Memorandum of Understanding signed on 20 May 2002, which although not being a binding instrument, had explicitly stipulated that negotiation of the IUA was to be without prejudice to the early ratification and entry into force of the Timor Sea Treaty. It not only went against the interests of East Timor but also against those of Phillips Petroleum and the company's joint venture partners in the Bayu-Undan development, who wanted to move their project forward as quickly as possible. On 2 October, Phillips representative, Mike Nazroo, had informed the JSCOT: "we do not advocate the simultaneous ratification of the Timor Sea Treaty and the international unitisation agreement; quite the opposite...I urge the committee to reject the

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<sup>38</sup> *Ibid.*, p.235.

<sup>39</sup> Joint Standing Committee on Treaties, *Report 49: Timor Sea Treaty*, November 2002.

<sup>40</sup> *Ibid.* Bartlett stated that:

The Australian Democrats believe that the revenue split of 90-10 in favour of East Timor represents a fair allocation of the resources within the JPDA, as it is defined within the Treaty. However, uncertainty regarding the legality of the boundaries of the JPDA is crucial when assessing the overall fairness of this allocation between Australia and East Timor.

In his Minority Report, Bartlett recommended that the Timor Sea Treaty should not be ratified and that: Australia and East Timor negotiate a definitive time frame, not exceeding five years, in which the seabed boundaries between the two countries will be delimited, and agree to refer their competing claims to the ICJ in the event that a fair agreement cannot be reached.

request for the simultaneous ratification of the treaty and the international unitisation agreement made in the submissions of Woodside Australian Energy”.<sup>41</sup> On 8 October, Santos, an Adelaide-based oil company and junior partner in the Bayu-Undan project told the Committee that “delaying the ratification of the Timor Sea Treaty pending the Sunrise international unitisation agreement would be against the terms and spirit of the 20 May Exchange of Notes and Memorandum of Understanding”.<sup>42</sup>

Alkatiri recognised that once the IUA was concluded, Australia would have no incentive to enter into maritime boundary negotiations. The eastern and western lateral limits of the JPDA were maximally advantageous for Australia. The whole purpose behind Australia’s drive to include the unitisation provisions within the Timor Sea Arrangement in the last stages of those negotiations had been to force East Timor to recognise these lines as legitimate international boundaries. Furthermore, Australia’s decision to withdraw from compulsory arbitration ensured that this position could not be challenged in a legal forum. On 27 November 2002, Alkatiri informed an Australian delegation led by Foreign Minister Downer that East Timor needed a “greater guarantee of maritime boundaries before the resources are exploited”.<sup>43</sup> The Australian side replied that the issue had already been settled. The 80 percent of Greater Sunrise lying outside the JPDA, “was in Australia to be administered by Australia”.<sup>44</sup> Downer told Alkatiri that, “on principle, we are surprisingly inflexible. What we can’t do is agree to joint petroleum development of Greater Sunrise”.<sup>45</sup> To Downer’s chagrin, the discussion was taped by the East Timorese delegation and a full transcript was subsequently leaked to the media.<sup>46</sup> On 13 December, *The Australian* reported:

...at the meeting, called to discuss the so-called international unitisation agreement on the Sunrise gas reservoirs, Mr Downer was ‘belligerent and aggressive’. He is reported to have banged the table as he criticised advice Dr Alkatiri was receiving from UN officials. After the meeting, the Australian

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<sup>41</sup> Joint Standing Committee on Treaties, Committee Hansard, 2 October 2002, p.50.

<sup>42</sup> *Ibid.*, 8 October 2002, p.213.

<sup>43</sup> Transcript of the negotiations between Australia and East Timor on an International Unitisation Agreement for the Greater Sunrise fields, 27 November 2002.

<sup>44</sup> *Ibid.*

<sup>45</sup> *Ibid.*

<sup>46</sup> The transcripts were leaked to an Australian political activist and news media internet company: [www.crikey.com.au](http://www.crikey.com.au) <Accessed 22 April 2003>

Government reneged on an understanding with East Timor that it would ratify the Timor Sea Treaty by the end of the year.<sup>47</sup>

Yet by choosing to delay the ratification of the Treaty for tactical advantage, the Australian government had in fact forced itself into a highly pressurized situation. On 17 December 2002, East Timor's legislative assembly ratified the Timor Sea Treaty, which placed the onus upon Australia to do the same. The Bayu-Undan joint venture partners warned the Australian government that unless they undertook to ratify the Treaty also, the sales agreement with the Japanese utilities would be placed in jeopardy. Even the World Bank urged the Australian government to ratify the treaty so that the commercial contracts could be signed and the necessary investment decisions could be made.<sup>48</sup> From the perspective of the World Bank, commercialization of Bayu-Undan was seen as East Timor's "exit strategy" from dependence on "external grant-based or concessional funding".<sup>49</sup> As the two Japanese utilities – Tokyo Gas Co. and Tokyo Electric Power Co. (TEPCO) – were state owned enterprises, there was pressure on Australia from the Japanese government also.<sup>50</sup> The deal with Phillips gave the utility companies a combined stake of 10.08 percent buy-in of the upstream project. That gave the Japanese government a major stake in the commercial success of the project.<sup>51</sup>

Alkatiri eventually agreed to sign the IUA in March 2003 but only, it seems, once Australia's negotiators had themselves caved-in on a number of key East Timorese demands: namely, an ability to tax downstream operations on infrastructure which would be located outside the JPDA; an unequivocal statement recognizing that Greater Sunrise was located in an area of disputed sovereignty; a strengthened 'without prejudice' clause; provisions for the re-determination of revenue apportionment subject to the delimitation of permanent maritime boundaries; and, a commitment from Australia to commence maritime boundary negotiations.<sup>52</sup>

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<sup>47</sup> 'Downer accused of abusing Timor PM', *The Australian*, 13 December 2002.

<sup>48</sup> Pers. Comm. Senior UNTAET Official, August 2004.

<sup>49</sup> 'End of beginning for East Timor', *Australian Financial Review*, 25 June 2001.

<sup>50</sup> Pers. Comm. José Teixeira, June 2004.

<sup>51</sup> The TEPCO and Tokyo Gas participation in the Bayu-Undan gas field was made through joint ownership of Tokyo Timor Sea Resources (incorporated in Australia). Thus, the two companies have become both buyers and sellers of the gas. TEPCO is contracted to receive 2 million tons of LNG *per annum*, Tokyo Gas, 1 million tons *per annum*. Another Japanese oil company, INPEX, has a 10.53 percent stake in the Bayu-Undan Darwin LNG project.

<sup>52</sup> Pers. Comm. Phillip Daniel, January 2005. The IUA stated that, "Timor-Leste and Australia have, at the date of this agreement, made maritime boundary claims, and not yet delimited their boundaries, including in an area

Shortly after the signature of the IUA in Dili, on 6 March 2003, the Australian government introduced legislation into parliament to ratify the Timor Sea Treaty allowing for the treaty's entry into force. This occurred on 2 April 2003, at an Exchange of Notes ceremony in Dili. The Australian government's attitude in the IUA negotiations received widespread condemnation. Alkatiri told the Australian Broadcasting Corporation (ABC) that the pressure from the Australian government had not been helpful to the process.<sup>53</sup> There was a perception that Prime Minister Howard had issued an ultimatum to Alkatiri: that being, 'sign the agreement or face an indefinite delay of Bayu-Undan revenue'.<sup>54</sup> The linkage strategy was seen by many as a crass attempt to exploit East Timor's economic dependence, which, in the absence of that country's ratification of the IUA would prove to be totally counterproductive anyway.<sup>55</sup> The IUA meant nothing until it had passed into law and, now that the Timor Sea Treaty was in force, the pressure upon East Timor to ratify the IUA automatically dissipated. The Australian government had gained no advantage through pursuing the linkage strategy and, in fact, had made the political context more difficult for itself.

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of the Timor Sea where Greater Sunrise lies". Recognition of East Timor's downstream taxation rights was not set out explicitly within the IUA but seems to have been rather awkwardly accommodated within a separate Memorandum of Understanding, which specified that if downstream processing facilities located inside the unit area (i.e. a floating LNG plant) were used to develop the reserves, then:

1. The Government of Australia will transfer to the Government of the Democratic Republic of Timor-Leste the sum of one million United States dollars (\$US1,000,000) *per annum* in freely disposable United States currency free of exchange and service charges.
2. The transfer of this sum will commence in the later of the calendar year in which installation of facilities in the Unit Area for the purpose of production begins and the calendar year five years before that in which production from the Unit Area is scheduled under the Development Plan to begin, and to continue each calendar year thereafter, up to and including the calendar year in which production from the Unit Area begins.
3. The Government of Australia will transfer to the Government of the Democratic Republic of Timor-Leste the sum of ten million dollars (\$US10,000,000) *per annum* in freely disposable United States currency free of exchange and service charges.
4. The transfer of this sum will commence in the calendar year in which production from the Unit Area begins, and continue each year thereafter up to but not including the calendar year in which production from the Unit Area ceases.

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See [http://www.austlii.edu.au/au/other/dfat/special/etimor/MOU-EastTimor\\_6\\_March\\_2003.html](http://www.austlii.edu.au/au/other/dfat/special/etimor/MOU-EastTimor_6_March_2003.html) <Accessed 15 September 2003>; See, also, 'Timor writes us a hefty gas bill', *The Australian*, 13 March 2003.

<sup>53</sup> 'Timor signs gas deal under pressure', *The Age*, 7 March 2003.

<sup>54</sup> 'East Timor bows to PM on gas', *The Age*, 6 March 2003.

<sup>55</sup> 'Blackmail claim clouds Timor pact celebrations', *The Australian*, 7 March 2003.

### *6.3 An End to the Dispute*

Following the entry into force of the Timor Sea Treaty, the Bayu-Undan project moved forward fairly rapidly. On 14 June 2003, the Timor Sea Designated Authority approved the plan that would cover the gas export/LNG phase of the development. On 30 August 2002, Phillips had merged with another US oil firm, Conoco, to create one of the world's largest exploration and production companies. Most of the new firm's combined 2004 exploration and production budget of US\$1.3 billion would be allocated for continued Bayu-Undan development, in addition to projects in Indonesia and China.<sup>56</sup> First production of condensate and LPGs (butane and propane) from Bayu-Undan were expected to commence in February 2004. Gross revenues were projected, at this time, to be about AUD\$30 billion.<sup>57</sup> The billion dollar contract for construction of the LNG plant at Wickham Point in Darwin Harbour was awarded to the US engineering firm, Bechtel.

The Greater Sunrise joint venture, however, remained in a state of comparative disarray. Woodside's efforts to find a buyer for the gas were frustrated by the commercial rivalries of Shell and Phillips, which stemmed from a broader struggle for control of the lucrative US west coast LNG market.<sup>58</sup> These problems were exacerbated by the continuing uncertainty over the legal status of the Australia/East Timor IUA. Alkatiri had no interest whatsoever in tabling the IUA in parliament until Australia had taken the strategic decision to accept the scope of East Timor's claims in the Timor Sea and negotiate in good faith towards a permanent settlement of the countries' maritime boundaries.<sup>59</sup> For Woodside, however, the IUA had to be ratified "before advancing to the next stage of development".<sup>60</sup> In June 2003, Woodside informed the Australian government that without the legal certainty that ratification and entry into force of the IUA would provide, the company would not be able to find a buyer for Sunrise gas.<sup>61</sup> Since 1997, Woodside had spent \$200 million on the Sunrise Project but, without a market for the gas, it was a lost cause and there was no point devoting any more resources to project development.

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<sup>56</sup> *Petroleum Economist*, 'Timor Sea: messy politics', March 2004.

<sup>57</sup> 'Final Bayu-Undan gas development approval', *Australian Stock Exchange Company Announcements*, 16 June 2003.

<sup>58</sup> 'Phillips, Shell Rivalry threatens Timor Sea gas', *Dow Jones International News*, 17 April 2002.

<sup>59</sup> 'Border battle for the newest nation', *The Times*, 21 June 2003.

<sup>60</sup> Woodside Energy, Submission #4, Joint Standing Committee on Treaties, *Review of Treaties tabled in May and June 2003*, 2003.

<sup>61</sup> *Ibid.*



Yet the chances of the Australian government accepting a permanent delimitation of boundaries on East Timor's preferred terms were practically zero. In May 2002, Downer had stated that the Australian government was obliged to consider any proposals put forward by East Timor, but a radical change to the existing lines would be unacceptable:

As I explained to the East Timorese some time ago, we are happy to hear what they have to say but we don't want to start renegotiating all of our boundaries, not just with East Timor, but with Indonesia. It has enormous implications. As I have explained to them, our maritime boundaries with Indonesia cover several thousand kilometres. That is a very, very big issue for us and we are not in the game of renegotiating them.<sup>62</sup>

In an interview with a weekly Australian news programme, on 23 May, Downer had again made the point that "if we get into the game of renegotiating all of our boundaries with Indonesia, I think that would be a deeply unsettling development in our relationship with Indonesia, and for our foreign policy in general".<sup>63</sup> The situation therefore appeared to be headed for a stalemate. East Timor would not ratify the IUA without a meaningful commitment from Australia to negotiate maritime boundaries; Australia had no real intention of negotiating permanent boundaries until the revenue sharing arrangements for Sunrise had been locked in. Following repeated requests by Alkatiri to begin discussions, however, Prime Minister Howard eventually agreed but on the condition that Australia would meet with East Timor's negotiators no more than twice a year.<sup>64</sup> From the perspective of East Timor, this did not amount to a meaningful commitment. After a preliminary meeting was held in November 2003, the first round of formal maritime delimitation negotiations took place in Dili, from 19 to 22 April, 2004. The Australian delegation was given a mandate to discuss only the north/south boundary. However, the question of the eastern and western laterals – East Timor's core concern – was "off the table".<sup>65</sup> This unilateral attempt to deny recognition of the full scope of East Timor's maritime claims was legally untenable and, in light of Australia's decision to withdraw from compulsory forms of arbitration, ethically questionable. As a result, pressure began to quickly build on the government to adopt a more cooperative

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<sup>62</sup> 'Downer rules E Timor seabed border changes out of bounds', *The Weekend Australian*, 25-26 May 2002.

<sup>63</sup> *Insight*, SBS, 23 May 2002.

<sup>64</sup> 'Canberra agrees to ETimor boundary talks', *The Australian*, 11 August 2003.

<sup>65</sup> 'Hands off my petroleum', *Time*, 10 May 2004, p.42.

and legally responsible position. This pressure came through the domestic and international media and from a range of Australian and international pressure groups.

Before discussing some of the specific cases in more detail, it is important to have in mind the fact that East Timor's independence was, in part, the result of a remarkably successful campaign spearheaded by a network of small non-governmental human rights organisations. Brad Simpson has argued that transnational activism was a crucial ingredient to the success of the independence movement – chiefly “by maintaining East Timor's visibility in the Western media from 1975 to 1991 and in pressuring Indonesia to allow a referendum on the territory's independence in 1999”.<sup>66</sup> Recognition of the important role played by “international civil society” was also given in the *Final Report of the Commission for Reception, Truth and Reconciliation in East Timor* released in January 2006. The Commission, which was established to investigate the facts about human rights violations committed in East Timor between 1974 and 1999, noted that: “During 25 years of struggle, a strong partnership was forged between many of Timor Leste's current leaders in all walks of life and international civil society that is rare in the history of nation-building”.<sup>67</sup> International civil society involvement in the East Timor conflict, though active since 1974, had risen sharply in response to the 1991 Santa Cruz massacre, through groups such as the Washington-based East Timor Action Network (ETAN) and, in Australia, Australians for a Free East Timor (AFFET), in addition to many others spread across Europe and Asia. East Timor had a high level of international support as well as political allies and during 2003 and 2004 some of these groups began to mobilize on behalf of East Timor's claims to a larger share of Timor Sea oil and gas.

The first major civil society action was a letter sent to John Howard, on 7 November 2003, by the Australian-based Aid-Watch, and which was signed by about 100 individuals representing non-governmental political and human rights organizations from around the world. In the letter, Australia's Prime Minister was urged to agree to set a three-year deadline for the resolution of permanent maritime boundaries between East Timor and Australia. Reference was made to the Australian government's decision to withdraw from international legal mechanisms to resolve boundary issues, which had been “widely interpreted as a hostile act to deliberately prevent East Timor from using its legal rights in the event of [Australia's]

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<sup>66</sup> Simpson, B., 2004. ‘Solidarity in an age of globalization: the transnational movement for East Timor and U.S. foreign policy’, *Peace and Change*, vol.29(3&4), p.454.

<sup>67</sup> *Chega!*, Final Report of the Commission for Truth, Reception and Reconciliation in East Timor, October 2005, Part 7, p.121.

refusal to enter timely and cooperative boundary negotiations.”<sup>68</sup> In the United States, the Washington-based ETAN concentrated its efforts in the US Congress, within which there existed a small, yet “strong and vocal group”, which had been supportive of East Timor for many years.<sup>69</sup> Democrats Representatives Jim McGovern and Barney Frank were willing to speak out publicly against Australia’s position in the maritime dispute during debates on the US-Australia Free Trade Agreement. In July 2004, McGovern told Congress that he was “deeply concerned” by Australia’s “ruthless treatment” and disregard of East Timor’s rights to oil and natural gas deposits in the Timor Sea.<sup>70</sup> In the same debate, Ohio Representative, Dennis Kucinich, noted that East Timor had a “rightful claim” that was “protected by international law”. He accused Australia of “displaying bad faith in the negotiation process”.<sup>71</sup>

The East Timor Action Network considered that whilst legal options to obtain a better result for East Timor had effectively been blocked by Australia, political avenues were still open.<sup>72</sup> In March 2004, the group arranged for another letter to be sent to John Howard, which was signed by 53 members of the US House of Representatives. The letter, which included the names of a number of influential figures in Washington and long-term advocates for East Timor, such as Rhodes Island Representative, Patrick Kennedy, stated that:

As the poorest country in Southeast Asia, East Timor’s dependence on foreign aid is one factor that keeps it from consolidating its stability and economic development, which of course adds greatly to the strain the country continues to face. This is why we support the statement our colleagues on the Senate Appropriations Committee included in its report that accompanied this year’s foreign aid bill underscoring how important the negotiations [with Australia] over the maritime boundary and the petroleum reserves are to the future economic development and security of East Timor. We also join our Senate colleagues in urging both governments to engage in good faith negotiations to

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<sup>68</sup> NGO Letter to Howard on Timor Boundary Talks, 7 November 2003, <http://etan.org/news/2003a/11ltr.htm> <Accessed 7 November 2005>

<sup>69</sup> Marker, J., 2003. *East Timor: a memoir of the negotiations for independence*, McFarland and Company, Jefferson, North Carolina, p.51.

<sup>70</sup> House Floor Statement by U.S. Rep. Jim McGovern on the U.S. – Australia Free Trade Agreement, 14 July 2004, <http://www.house.gov/mcgovern/floor071404australiatrade.htm> <Accessed 8 November 2005>; Representative Patrick Kennedy also raised the issue in the House of Representatives.

<sup>71</sup> Statement by Rep. Dennis Kucinich during FTA debate, <http://www.etan.org/et2004/july/15-21/14repkuc.htm> <Accessed 16 December 2005>

<sup>72</sup> Pers. Comm. Karen Orenstein, ETAN, August 2004.

resolve their maritime boundary in accordance with international legal principles and we hope both governments will agree to a legal process for an impartial resolution if the boundary dispute cannot be settled by negotiations. We also urge you to heed Prime Minister Alkatiri's call to conclude negotiations within three to five years. We were pleased that a preliminary meeting between your two governments was held in November, but we were disappointed by your government's insistence that bilateral meetings on the boundary be semi-annual and encourage you to hold them monthly, as requested by East Timor.<sup>73</sup>

The letter concluded:

We trust your country's commitment to the freedom and security of East Timor will include recognition of East Timor's territorial integrity and its right to a swift, permanent resolution of the maritime boundary dispute.<sup>74</sup>

At the same time, East Timor's three most influential political leaders – Gusmão, Alkatiri and Ramos Horta – made highly publicized efforts to pressure the Australian government into making concessions. Gusmão, for example, warned of the possibility of East Timor becoming a failed state – “a permanent beggar like the Solomon Islands or Haiti” – if denied access to the resources his country laid claim to.<sup>75</sup> Gusmão's Australian wife, Kirsty Sword Gusmão, publicly criticized Australia's lack of commitment and good faith in the negotiations.<sup>76</sup> She said that the government's attitude made her ashamed to be Australian.<sup>77</sup> These emotive statements were given full exposure by the Australian press, which was eager to exploit the political tensions surrounding the dispute, presented as a ‘David and Goliath battle’ for greater melodramatic effect.<sup>78</sup> These forces appeared to work against the Australian government. The decision to withdraw from compulsory forms of third-party dispute settlement had attracted bad publicity. Alkatiri, who had initially responded to the decision as

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<sup>73</sup> Letter to Prime Minister Howard, 8 March 2004, <http://etan.org/news/2004/03houseltr.htm#letter> <Accessed 22 November 2005>

<sup>74</sup> *Ibid.*

<sup>75</sup> ‘Timorese fury at “immoral oil grab”’, *The Guardian*, 19 April 2004; ‘How can we behave like beggars?’, *Sydney Morning Herald*, 25 May 2004.

<sup>76</sup> ‘East Timor's first lady calls for fair go on boundary’, *Australian Associated Press*, 26 April 2004.

<sup>77</sup> *Ibid.*

<sup>78</sup> ‘Interview, Joel Fitzgibbon’, *Dow Jones Newswires*, 4 June 2004.

“a sign of a lack of confidence in us and an unfriendly act”, continued to attack it as an “acknowledgement of the weakness of Australia’s legal case”.<sup>79</sup>

The East Timorese Prime Minister also publicly demanded that Australia exercise restraint in the exploitation of seabed areas to the west of the JPDA that fell within the limits of East Timor’s claim, where production of the Laminaria, Corallina and Buffalo fields was ongoing. The continued exploitation of these fields was a strong grievance against Australia; and the release, by Australia, of additional exploration acreage in areas of overlapping claims was seen not only as a provocation but as a violation of East Timor’s sovereign rights.<sup>80</sup> By the end of 2003, cumulative production from Laminaria/Corallina had surpassed 100 million barrels, which represented approximately half of their recoverable reserves.<sup>81</sup> In June 2004, Alkatiri declared that his government “had warned potential investors about taking up a permit in disputed areas, and notified those already operating in these areas that they have and continue to incur liability to Timor-Leste. They are on notice that Timor-Leste will take all lawful steps to prevent unlawful exploration for and exploitation of resources within its maritime zone”.<sup>82</sup>

The Australian government tried to fend off the growing level of domestic and international criticism. In May 2004, Foreign Minister Downer told the ABC that East Timor had made “a very big mistake thinking that the best way to handle this negotiation is trying to shame Australia, is mounting abuse on our country...accusing us of being bullying and rich and so on, when you consider all we’ve done for East Timor”.<sup>83</sup> In June, Downer wrote a letter to the editor of the *Wall Street Journal*, in which he described criticism of Australia’s position in relation to settlement of permanent maritime boundaries with East Timor as “offensive and disingenuous”.<sup>84</sup> His remarks seem to have been aimed primarily at the pro-East Timorese voices in Washington, D.C.:

To cede territory merely on the basis that a neighbour is poorer would reduce international law to a farce. Under such absurdity, we could see the Texas oil fields ceded to Mexico. It is clearly in Australia’s national interest that East Timor becomes a stable and self-sufficient neighbour. East Timor currently

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<sup>79</sup> ‘East Timor chief minister hits out at Australia over Gap’, *Australian Associated Press*, 13 April 2002.

<sup>80</sup> Brennan, F., 2004. *The Timor Sea’s Oil and Gas: what’s fair?*, The Australian Catholic Social Justice Council, Sydney; Bialek, D., 2002. Submission #38, Joint Standing Committee on Treaties, *Timor Sea Treaties*.

<sup>81</sup> Woodside Petroleum, *Concise Annual Report*, 2003.

<sup>82</sup> *The Diplomat*, ‘Australia, please don’t steal our oil’, June/July 2004.

<sup>83</sup> Australian Broadcasting Corporation, *Four Corners: rich man, poor man*, 10 May 2004.

<sup>84</sup> ‘Australia’s sovereign rights’, *The Wall Street Journal*, 25 June 2004.

stands to derive enormous economic benefits from the Timor Sea resources. However, those resources are not all East Timor's. Australia makes no apology for protecting its sovereign rights.<sup>85</sup>

In July 2004, the Department of Foreign Affairs released an information sheet on Australia's negotiating position. It stipulated that "international law supports Australia's claim to the full extent of its continental shelf northward to the deepest part of the Timor Trough".<sup>86</sup> Yet, despite these efforts, it was becoming obvious to the government that it was losing the public relations battle. The climate of domestic and world opinion was against them. During May and June, ETAN had worked with local activists and students in staging a number of high profile demonstrations outside Australian Embassies in Washington, D.C. and Dili;<sup>87</sup> and, the continued deterioration in political relations prompted public input from a variety of stakeholders seeking some form of constructive engagement on notions of 'the best way forward'.<sup>88</sup>

The Northern Territory's Chief Minister, Clare Martin, for example, suggested that the Greater Sunrise development should be "de-linked" from ongoing bilateral discussions on maritime boundaries and that the Australian government should make a more generous offer on the revenue split to ensure that the project moved ahead.<sup>89</sup> For Martin, it was irrelevant how much of government taxation from Greater Sunrise went to the Australian Treasury, as the key interest in the Northern Territory was the significant economic investment into the Darwin economy associated with downstream infrastructure development. Yet the solution of amending the revenue sharing terms as a means of breaking the deadlock had an air of inevitability to it. It was impossible to conceive of East Timor ratifying the IUA without the guarantee of a more equitable share of Sunrise; and, it was equally impossible, if not more so, to envisage the Australian government accepting any alteration to the existing framework of jurisdictional lines in the Timor Sea. Alkatiri was receptive to the idea of such a compromise and it is worthwhile to recall that the position which had originally been adopted by the UNTAET team during the Timor Sea Arrangement negotiations was that the only fair and

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<sup>85</sup> *Ibid.*

<sup>86</sup> Department of Foreign Affairs and Trade, 'Australia-East Timor Maritime Boundaries: finding an equitable outcome', July 2004.

<sup>87</sup> 'Bedevilled in the Timor Sea', *The Weekend Australian*, 29-30 May 2004.

<sup>88</sup> See, for example, Brennan, 2004, *op. cit.*

<sup>89</sup> 'One-off compromise gas proposal', *The Australian*, 8 June 2004.

reasonable basis upon which Greater Sunrise could be unitised pending a settlement of the boundaries was to split it 50:50.

In July, Woodside's new Chief Executive, Don Voelte, issued a warning to both governments that unless an agreement was concluded before the end of the year, further work aimed at progressing the Sunrise Project would be suspended indefinitely.<sup>90</sup> The leaders of both countries were told that the dispute was hampering efforts to market the gas, because it prevented the company from being able to guarantee potential customers that supplies would be secure.<sup>91</sup> This proved to be the key turning point. Shortly afterwards, the Australian government relented. On 11 August, Downer announced that Australia would be willing to accept a smaller share of Greater Sunrise revenues. Downer explained that "being a prosperous country, our concerns are less with the revenue we can extract from the Timor Sea than with the broader questions of sovereignty."<sup>92</sup> However, Australia's initial offer was a cash payment (reputed to be \$3 billion) rather than a percentage re-adjustment. The strategy it seems was to 'buy' East Timor's ratification of the IUA with additional payments from Australia's disproportionately larger share of Sunrise revenues.<sup>93</sup>

Yet the offer was rejected by Alkatiri, who argued that the central issue was not just about money but "East Timorese participation in the development of the disputed resources".<sup>94</sup> Furthermore, Alkatiri insisted that any negotiated settlement of the dispute over Greater Sunrise would have to include provisions for the gas resources to be processed in East Timor, rather than Australia.<sup>95</sup> After the third of a series of intensive meetings between representatives of East Timor, Australia and Woodside, during September and October 2004, Alkatiri released a press statement which stated:

In August, I welcomed Minister Downer's interest in reaching a creative solution to our dispute, and his recognition of Timor-Leste's just claims to areas beyond the JPDA. As I said then, any solution needs to fully reflect Timor-Leste's sovereign rights in the areas to the East and West of the JPDA. This means that, in order to resolve the Timor Sea dispute, we will have to find not only a fair means of sharing the upstream revenues from petroleum

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<sup>90</sup> 'U.S. chief pushes oil giant's moves beyond Australia', *New York Times*, 11 August 2004.

<sup>91</sup> *Ibid.*

<sup>92</sup> 'Downer offers Timorese a new deal', *Sydney Morning Herald*, 12 August 2004.

<sup>93</sup> 'Talks on Timor Gap reserves collapse', *Sydney Morning Herald*, 28 October 2004.

<sup>94</sup> 'All East Timor seeks is a fair go', *The Age*, 3 November 2004.

<sup>95</sup> *Ibid.*

resources, but will also have to deal fairly with the downstream, meaning petroleum transportation and processing. We put forward a range of options that would address these various elements of a resolution to our dispute. What the Australian Government delegation was willing to offer and explore did not come even close to recognizing our sovereign rights in the disputed areas. We were talking about Timor-Leste participation in the development of the disputed resources; they were talking about money. We were too far apart to reach agreement.<sup>96</sup>

The vision of an LNG export industry based in East Timor was one that had originally been promoted by Oceanic Exploration in late 2001. In attempting to revive their 1974 concession, the firm had actually commissioned a detailed engineering study of the feasibility and costs of constructing a pipeline across the deepwater Timor trough, in order to land gas from Timor Sea reserves in East Timor. Phillips, Woodside and the Northern Territory government had all claimed that the depth of the trough made laying a pipeline to Timor extremely uneconomical if not technologically impossible.<sup>97</sup> Yet the study, which was completed in May 2002, and distributed widely in Australia and East Timor, had concluded that it was not only technically feasible to install a pipeline to Timor but it could be done at less cost than a pipeline of similar capacity to Darwin.<sup>98</sup> For Oceanic, which had, by now, been totally sidelined from any involvement in the commercial development of Timor Sea resources, Alkatiri's endorsement of this plan added a degree of insult to injury. In March 2004, the company filed a US\$10.5 billion law suit in the United States against ConocoPhillips and the joint Timor Sea authorities, alleging violations under US anti-trust and racketeering laws. Charges of bribery and corruption were brought specifically against Mari Alkatiri.<sup>99</sup>

Despite the shift in Australia's position, however, the government continued to face a considerable degree of public pressure. Kathryn Khamsi has pointed out that the issue was "on the agenda" of a number of Australian NGO's such as Oxfam Community Aid Abroad and the Uniting Church as well as the Melbourne-based Timor Sea Justice Campaign, which

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<sup>96</sup> 'Statement by Timor Leste Prime Minister on Timor Sea Talks, 27 October 2004'. Following these comments, the leader of the Australian delegation, Doug Chester, responded that "Australia offered East Timor many billions of dollars in order to get them to ratify a treaty they have already signed"; See 'Australia blames East Timor for gas talks failure', *Australian Financial Review*, 29 October 2004.

<sup>97</sup> McKee, G. A., 2002. Submission #87, Joint Standing Committee on Treaties, *Timor Sea Treaties*.

<sup>98</sup> Imle, J., 2002. Submission #78, Joint Standing Committee on Treaties, *Timor Sea Treaties*.

<sup>99</sup> 'Conoco is sued over Timor field', *The Wall Street Journal*, 2 March 2004.



had been set up in April 2004 “to bring about a just and prompt resolution of the Timor Sea dispute”. The Australian section of the International Commission of Jurists had also issued a statement decrying the Australian position, and in particular, Australia’s refusal of neutral third-party adjudication.<sup>100</sup> Thirty-seven members of the European Parliament signed two petitions, sent to John Howard and the Australian Senate, in September 2004, which called upon Australia to “respect Timor’s territorial sovereignty concerning oil and gas deposits nearest to its shore”.<sup>101</sup>

The same month, a wealthy Australian businessman, Ian Melrose, launched a publicity campaign attacking the government through privately funded television advertisements. The image portrayed in the adverts was of an inhumane government denying East Timor access to revenues that it urgently needed for its basic needs, such as primary health care and schools.<sup>102</sup> Australian World War Two veterans were shown admonishing John Howard for his shameful disregard for East Timor’s rights. Although these were dismissed as being “deceptive and misleading”, the dispute was continuing to damage the government politically and was emerging as an election issue with general elections due to be held later in the year.<sup>103</sup> Opposition leader, Mark Latham, had announced in July that if the ALP were to come into government the negotiations would have to be started again. He stated that “from what I can gather, there’s been a lot of bad blood across the negotiating table and you never get it right in these sensitive areas unless you’re doing these things in good faith”.<sup>104</sup>

The impact of this pressure was a further softening in the government’s position. In January 2005, Australia invited East Timor to recommence negotiations. At a fresh round of discussions held in March, it emerged that Australia was prepared to raise its previous offer. However, as it was still based on a “financial deal” involving a fixed sum payment (now reported to be \$4 billion), East Timor rejected the offer.<sup>105</sup> Following a second meeting in Dili, at the end of April 2005, the breakthrough was made when Australia finally agreed to accept a 50:50 solution. After the meeting, Downer announced that the two sides were in “substantial agreement on all major issues”; and, after a subsequent round of discussions, in

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<sup>100</sup> Khamsi, K., 2005. ‘A settlement to the Timor Sea dispute?’, *Harvard Asia Quarterly*, vol.IX(4) <http://www.asiaquarterly.com> <Accessed 25 February 2006>

<sup>101</sup> ‘EU deputies urge Australia to respect East Timor’s rights in oil row’, *Agence France Press*, 15 September 2004.

<sup>102</sup> ‘Hosing down the East Timor gas fire’, *The Australian*, 7 June 2005.

<sup>103</sup> ‘Canberra hits Timor ads’, *The Age*, 1 February 2005.

<sup>104</sup> ‘Labor shifts stance on Timor gas’, *Australian Associated Press*, 22 July 2004.

<sup>105</sup> ‘E Timor expects early deal with Canberra’, *Financial Times*, 22 March 2005.

Sydney, on 13 May, a document outlining the terms of the agreement was drafted.<sup>106</sup> In a letter to the editor of the Melbourne-based newspaper, *The Age*, Ramos Horta described the “salient elements of an agreement”:<sup>107</sup>

The possible treaty would be "without prejudice" to Timor-Leste (East Timor) and Australia's sovereign maritime boundary claims. No acts or activities by either side under the treaty could be relied upon to assert, support, deny or further the legal position of either country. A 50-year moratorium would be agreed to for the duration of the treaty. In return for the moratorium on maritime boundaries, the parties would agree to share equally the total tax and royalty revenues from petroleum produced in the Greater Sunrise area. The Timor Sea Treaty of 2002 will continue to be observed and Timor-Leste will continue to receive 90 per cent of income from that area. The revenue split could mean more than \$US7 billion (\$A9.23 billion) to our impoverished country. Other fields underlying Greater Sunrise field either wholly or partly would be treated in the same manner as the Greater Sunrise field.<sup>108</sup>

On the question of the pipeline and LNG plant for the Sunrise development, Ramos Horta commented:

There are some issues to be resolved with the operator, Woodside, namely where the pipeline should go to. To Timor-Leste's south coast, which is much closer to Greater Sunrise and to the Asia-Pacific customers, or to the barren Northern Territory, which has a very small population and is far from everywhere? Our labour costs are also much lower than Australia, which faces labour shortages and has stringent immigration and labour laws that are a disincentive to foreign workers. Petroleum experts from Saudi Arabia, Dubai, Kuwait and Germany all believe bringing the pipeline to Timor-Leste is technically feasible and makes sense commercially.<sup>109</sup>

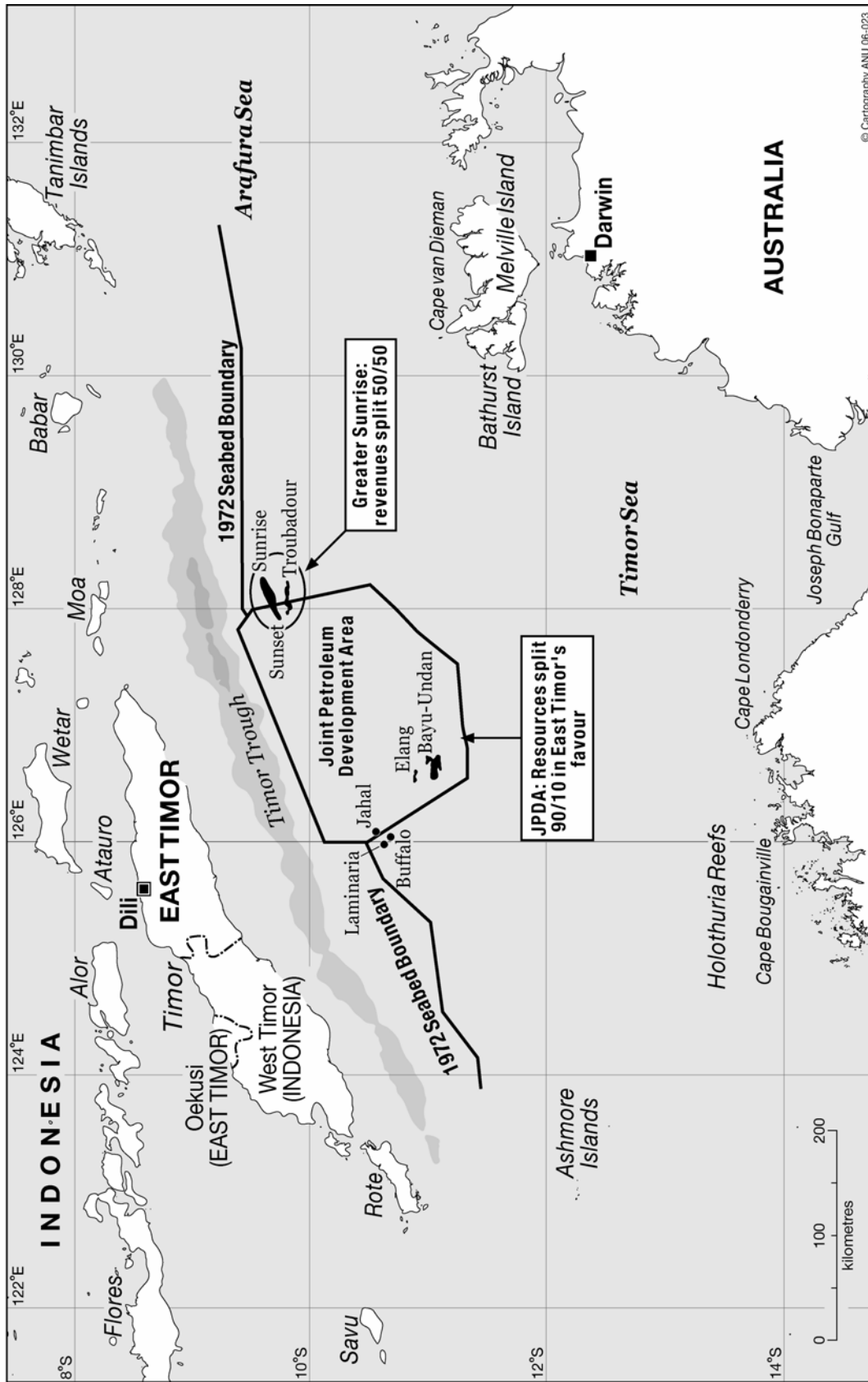
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<sup>106</sup> Deal reached on Timor Sea oil', *Sydney Morning Herald*, 30 April 2005.

<sup>107</sup> 'The shape of a fair deal for East Timor', *The Age*, 30 May 2005.

<sup>108</sup> *Ibid.*

<sup>109</sup> *Ibid.*



MAP 9

**The Final Settlement: Australia/East Timor Resource and Revenue Sharing Arrangements\***

\* The 2003 Timor Sea Treaty, the 2003 Sunrise IUA and the 2006 CMATS Treaty are interlinked to provide a comprehensive settlement of the dispute. Petroleum exploration and production in areas outside of the JPDA and Sunrise Unitisation Area and south of the 1972 seabed boundary are subject to Australian legislation. The moratorium on claims to maritime jurisdiction and boundaries is to last for fifty years or until five years after exploitation of Greater Sunrise ceases, whichever occurs earlier.

The goal of the East Timor government remains that of having a Sunrise LNG plant in East Timor, whereby the ‘value added’ onshore processing of Timor Sea hydrocarbons contributes to the development of a significant manufacturing sector, job creation and growth of the national economy. The oil companies view the situation differently, however. They see the political risks of investing in a fragile and institutionally weak democracy with a history of violent political conflict. Woodside’s and ConocoPhillips’ preference is to process Greater Sunrise gas in Australia, possibly through an expansion of the existing LNG plant in Darwin from a three to a ten million ton per annum LNG production facility. Phillips first notified the Northern Territory government of its plans to expand the capacity of the Darwin plant to this level in May 2001.

As technical negotiations continued on finalizing the terms of the arrangement, East Timor’s government turned its attention towards domestic petroleum issues, including the development of a national exploration and development regime and the launch of the country’s first domestic petroleum licensing round. A number of offshore blocks were offered in areas that extended out from the country’s south coast, over the Timor trough, to the northern side of the JPDA. Alkatiri led a delegation to Singapore, London, Calgary and Houston, during the first two weeks of September, to promote investment in what was being described as “Asia’s last hydrocarbons frontier”.<sup>110</sup> Negotiations between Australia and East Timor were eventually concluded on 29 November 2005. On 1 December, Downer informed parliament that officials had initialed an agreement and exchanged letters on the basis of an approved text, and that the East Timorese Prime Minister and Foreign Minister had agreed for there to be an official signing ceremony in January 2006.<sup>111</sup>

At a press conference in Dili on the 9 December, Alkatiri stressed that the compromise that had been reached with Australia over Sunrise was the best outcome for East Timor. Both countries would be bound by the treaty to undertake to not commence any dispute settlement proceedings against the other that would raise the delimitation of maritime boundaries in the Timor Sea. The Prime Minister explained that the option, potentially, of litigating for a permanent boundary was marred by a deep uncertainty: “no-one can affirm that the result of a court case would be better. Second, a court case would take years to finish...potentially

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<sup>110</sup> ‘Timor Leste: a new frontier’, *Petroleum Economist*, October 2005. In May 2006, the government announced that five offshore blocks had been awarded to the Italian oil company, ENI S.p.A; another block was awarded to Reliance Industries Ltd, of India.

<sup>111</sup> House of Representatives, *Official Hansard*, 1 December 2005, p.48.

compromising the social-economic development of Timor-Leste”.<sup>112</sup> Reflecting upon the starting point for the negotiations, in 1999, Alkatiri noted that the original arrangement with Australia awarded East Timor 50 percent of the revenues from the JPDA and about 10 percent of Greater Sunrise. “Today, we will receive 90 percent of the revenues of the JPDA, and with this new arrangement, we will receive a total of 50 percent of Greater Sunrise.”<sup>113</sup> After making an enormous diplomatic effort, over a period of more than five years, East Timor had achieved precisely the outcome that it had set out to obtain when negotiations commenced; namely, a result that was felt to be no less than the country was legally entitled to.

## CONCLUSION

The Treaty on Certain Maritime Arrangements in the Timor Sea was signed in Sydney on 12 January 2006. It interlinks with both the 2003 Sunrise IUA and the 2003 Timor Sea Treaty to provide a comprehensive, albeit unwieldy, settlement of the dispute. Under this arrangement, the Sunrise IUA remains valid, which means that the hydrocarbon resources will still be unitised according to the apportionment ratio specified under that agreement (that is, 20.1% is attributed to the JPDA and 79.9% is attributed to Australia). However, all government revenue derived from production, when that actually commences, will be shared equally between Australia and East Timor. The change in Australia’s share of the revenues is 31.91 percent, which is equivalent to the loss of more than three trillion cubic feet of gas and over 100 million barrels of condensate (more than half a billion barrels of crude oil equivalent).<sup>114</sup> A 50:50 unitisation of Sunrise had been offered to Australia by the UN/East Timor negotiating team in June 2001. It is interesting to note that had the government been willing to accept it at that time, East Timor was prepared to accept Australia’s demands for an 85:15 split of the JPDA. Thus, in striving for more advantageous terms, Australia actually ended up with less.<sup>115</sup>

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<sup>112</sup> Gabinete do Primeiro-Ministro, *Press Release*, 9 December 2005.

<sup>113</sup> *Ibid.*

<sup>114</sup> Under the terms of the IUA, Australia would have received 79.9% plus 10% of 20.1%, which equals 81.91%. Thus, the shift to 50:50 equates to a loss of 31.91%. The CMATS Treaty specifies that only revenues are to be shared, not resources, although the net result is exactly the same. The size of the reserves at Greater Sunrise is uncertain: estimates range from between 8 to 10 trillion cubic feet. The calculations of Australia’s losses are based on government sources, which estimate Greater Sunrise to hold 9.56 tcf of gas and 320 million barrels of condensate.

<sup>115</sup> The offer of an 85/15 split of the JPDA was made in the letter sent to John Howard by the UNTAET Cabinet on 20 June, which was quoted in Chapter Five.

The principal reasons behind Australia's eventual willingness to concede may be attributed to the political and commercial pressures which became more and more intense as the dispute dragged on. This chapter has documented many of the different lobbying efforts undertaken by various actors, which included a network of East Timor activists and NGOs as well as important commercial stakeholders, such as Woodside. As the costs of the impasse escalated, the incentive for the Australian government to make compromises and settle the dispute increased. Australia was prepared to yield because ultimately the costs of not having an agreement, and thus continuing the dispute, were considered to be greater than the price of accommodating East Timor's demands. Of course, international negotiation is a highly competitive activity and governments concede only if and to the extent to which they must. Therefore, Australia was willing to concede only to the extent that it believed East Timor would not give in. As Schelling has correctly observed, the logic of interdependent decision-making is such that each side's best choice of action depends upon what it expects the other side to do.<sup>116</sup> This is why the progress of the Bayu-Undan LNG project was so strategically important for East Timor. Once the deal with the Tokyo electric and gas companies had been sealed, it automatically had the effect of releasing the pressure upon Dili to ratify the Sunrise unitisation agreement. The important point is not so much that East Timor could afford to continue the dispute but that the Australian government perceived that the situation had changed; that the pressures facing each side were not the same.

On a tactical level, Australia's efforts to build-up 'situational power' within the negotiations failed.<sup>117</sup> Attempts to link the unitisation of Sunrise to the Timor Sea Treaty proved a costly mistake. The negative perceptions generated by the use of this tactic were compounded by the government's earlier decision to withdraw from compulsory forms of third-party resolution. These actions were roundly condemned by political opponents, both at home and abroad. In focusing narrowly on getting East Timor to concede, the government neglected to consider the effects of its actions or the chains of reactions which ensued. Australia's conduct was perceived both within East Timor and the wider community as inappropriate and unethical. The reaction, or feedback, from the use of such tactics undermined their effectiveness in ways that actually proved counterproductive. It was doubly absurd, given that East Timor would, at all times, hold veto control over the Sunrise Project

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<sup>116</sup> Schelling, T. C., 1980. *The Strategy of Conflict*, Harvard University, Cambridge, Massachusetts, p.15.

<sup>117</sup> The concept of situational power relates to the various aspects of the negotiation situation which influences a negotiator's willingness to be flexible or accommodative, such as time pressures, dependence upon the resources at stake, etc. See Druckman, D. 1993. 'The situational levers of negotiating flexibility', *The Journal of Conflict Resolution*, vol.37(2):236-76.

through the powers of the Joint Commission, established under the Timor Sea Treaty. Hence the only chances of the Project moving forward would be under circumstances whereby all parties – Australia, East Timor and the commercial operator – believed they were getting a reasonable return.

Such miscalculations are, in fact, not an uncommon feature of high-stakes negotiations. William Ury and Richard Smoke have noted that the failure to anticipate adequately a possible sequence of events results from the pressures upon political actors of being immersed in a dispute and under great stress.<sup>118</sup> Yet it may also be a symptom of asymmetric power perceptions.<sup>119</sup> Australia's leaders acted on the assumptions of their own power superiority, at times deeply condescending towards East Timor, whereas the latter sought ways of altering its power position, building leverage through the power of public opinion. One senses a certain tension and enormous frustration within the Australian government at not being able to convert its material supremacy over East Timor into greater success at the negotiating table. This became apparent during the meeting in Dili during November 2002, when Foreign Minister Downer appeared to lose composure, by banging his fist on the table.

Yet whilst public pressure may have been a decisive factor, it tells only half the story. What galvanized East Timor's supporters into action was the strong belief that East Timor's claims to a larger share of Timor Sea resources had the support of international law. Their motivation to act was the product of normative considerations. The Lowe Opinion played a crucial role in this regard. For it provided an authoritative statement of East Timor's maritime boundaries, based on the application of international jurisprudence. As one of the world's foremost experts on maritime delimitation law, Lowe's Opinion had a profound impact upon actors' conceptions of East Timor's legal entitlement. Lowe's basic argument was that the convergent lateral boundaries of the joint development zone were unfair and, therefore, inconsistent with the fundamental norm of equity. Whilst the Australian government maintained that East Timor's lateral boundary claims were "fictitious", the government was ultimately constrained in what it could achieve in the negotiations by the actions of many others who did accept this basic argument.

In fact, the Australian government was normatively constrained on two levels. Not only was it hampered by the actions of other actors motivated by normative considerations;

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<sup>118</sup> Ury, W. L. and Smoke, R., 1985. 'Anatomy of a crisis', *Negotiation Journal*, vol.1(1), p.94-5.

<sup>119</sup> Zartman, I. W. and Rubin, J. Z., 2000. *Power and Asymmetry*, University of Michigan Press, Ann Arbor, p.271-90.

the government was constrained also in the choices it had for settling the dispute. The government's initial attempt to unilaterally deny recognition of the full scope of East Timor's claims in the Timor Sea was legally invalid and, as a result, proved to be politically untenable. The Australian government found itself in a no-win situation. Having ruled out the possibility of any form of compulsory third-party resolution in the first instance, and unable to impose its preferred solution upon East Timor in the second, the government's last and only resort for settling the dispute was to return to consensus-based diplomacy. The result was that Australia was brought back to the negotiating table and had to make further concessions in order to bring the dispute to an end. To understand why Australia agreed to make additional concessions to East Timor, it is therefore not sufficient to consider only the strategic behaviour of the actors involved; one must look more deeply into the ways in which such behaviour is related to, and interacts with, the 'normative structure' of the dispute. The legitimate avenues available for dispute resolution constitute a key part of that structure. The duty to negotiate does not require states to make agreement at any price. The obligation refers to conduct rather than the substantive outcome to be achieved. States are under an obligation to enter into negotiations with a view to arriving at an agreement, and not merely go through a formal process of negotiation. Some give-and-take is implicit.



## CONCLUSION

The negotiations between Australia and East Timor provide a study of the political dynamics of bargaining for control of offshore energy resources. What makes this issue stand out as a topic of research is the sheer importance of the stakes to the parties involved. For East Timor's survival as an independent political entity, the issue is practically one of life and death. It is rare for maritime territorial disputes to reach such heightened levels of domestic and international concern. As a study of international negotiation, this research contributes in an area that occupies a central position in both the practice and study of international politics. Yet, as Cottam has pointed out, the study of international negotiation poses formidable analytical challenges:

Because documentary evidence of the details of the negotiations will often be classified for a generation, the academic evaluator will often be left with little more than public statements by those involved and the published outcome of the proceedings. The limitations thus placed on the academic analyst are profound...the data necessary to describe the actual negotiating process and to identify such important matters as negotiating intent and bargaining strategies followed are likely to be inadequate. Therefore, it is questionable whether the academic interested in negotiations can contribute much to an understanding of the process of negotiation.<sup>1</sup>

In light of this observation, it seems important to note that this research has been made possible because the documentary evidence of the details of the negotiations has been accessed and exhaustively analysed. The quality of this evidence has been further complemented and enhanced through interviews with individuals on both sides of the negotiations as well as with many of the key stakeholders around the negotiations. Thus, Chapters Four and Five provide an authoritative account of the actual negotiating process between Australia and UNTAET; the opening positions of the parties, their bargaining strategies, the timing and pattern of concessions and the process of convergence towards agreement. Chapter Six has relied somewhat more extensively upon publicly available

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<sup>1</sup> Cottam, R., 1986. 'Understanding negotiation: the academic contribution', Institute for the Study of Diplomacy, School of Foreign Service, Georgetown University, Washington, D.C.

sources of information, though it must be recognised that efforts of stakeholders and activists to influence the bargaining process during the final period were played out noticeably within the public sphere. As a result, conclusions can be drawn with a relatively high level of confidence.

Whilst the intrinsic historical importance of the events covered within this thesis provides a basic rationale for their analysis, the core question around which this research has been oriented is an explanatory one that concerns negotiated outcomes. Although both countries stand to derive substantial economic benefits from the practical arrangements that have been agreed, the final scorecard reads impressively in favour of East Timor. Australia has experienced a painful amputation of its reserves base. Hydrocarbon resources equal to about a billion barrels of crude oil that were considered to be federal property prior to the commencement of negotiations in March 2000, now effectively belong to the Democratic Republic of Timor Leste. The transition from the pre-1999 offshore legal framework to the post-2006 set of arrangements has thus been very costly for Australia. The percentage redistribution of Bayu-Undan and Greater Sunrise could have implications of tens of billions of dollars of fiscal revenues. Contrary to normal expectations, perhaps, the perceived stronger party has yielded significantly to the demands of the perceived weaker party.

One possible explanation is that the Australian government was willing to make concessions out of concern for the long-term economic viability of East Timor; or, put another way, that Australia had an interest in allowing East Timor to have a larger share of the resources so that it did not become overly dependent upon Australia for economic assistance. The implicit assumption of this argument is that, had the Australian government wanted to, it could have taken a tougher stance in the negotiations and made East Timor accept a smaller share. This research contradicts that proposition. From the beginning of the negotiating process, Australia has bargained hard in order to limit, to the greatest extent possible, the magnitude of concessions that have had to be made in order to reach a settlement of the dispute. The outcome is not one that the Australian government initially wanted or expected that it would have settled for at the outset of the bargaining process. The dramatic extent to which Australia has been moved in the negotiations has left a bitter taste in the mouth of Australian Ministers and senior bureaucratic staff.<sup>2</sup> East Timor was able to take on its powerful neighbour in these negotiations and emerge with better than expected results. The basic analytical question is, ‘how?’

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<sup>2</sup> Pers. Comm. Senior Australian Government Official, November 2005.

In this thesis, I have argued and sought to demonstrate that negotiated outcomes can be understood and explained as the product of the interaction between legal norms pertaining to the delimitation of the continental shelf, on the one hand, and strategic behaviour, on the other. Disputes over continental shelf rights do not arise within a vacuum; they take place in the shadow of the law. The normative framework of international law exerted influence in these negotiations through the different components of strategic choice – namely, the options available to the parties for pursuing their policy objectives, the relative costs and benefits associated with those choices and the beliefs of each party concerning the preferences of the other.<sup>3</sup> International law did not exert influence independently, such as through rule following or, indeed, through normative argumentation and suasion but, rather, through the dynamics of the parties’ interactions. East Timor has been able to achieve through negotiation the type of outcome, in terms of distribution of resources, which the government feels would have resulted if the case went to court. A wide level of support for this assessment can be found within expert legal opinion. Whilst East Timor has valid claims to 100% of the resources covered by the joint development arrangements, it would be “extremely unusual”, as Lowe, Carleton and Ward have pointed out, “for a tribunal to give 100% of a disputed maritime area to one of the disputing parties”.<sup>4</sup> Australia has valid claims to 100 percent of the resources also. The 90 percent of the JPDA and 50 percent of Sunrise is “substantively consistent” with the strength of East Timor’s claims both within the limits of the JPDA and in wider areas, beyond.<sup>5</sup>

East Timor’s success at the negotiating table is the result of the interplay between perceptions of context and negotiating tactics. The relationship between the two is the ‘incentives for action’ that different contextual factors produce.<sup>6</sup> UNTAET and East Timor’s solid belief in their entitlement to a mid-point maritime boundary coupled with the country’s enormous dependence upon the resources at stake acted as a powerful motivating force. Key personalities on the side of East Timor were able to harness that power and put it to greater tactical effect. Skillful diplomacy was an important factor in East Timor’s success. One of the widely cited paradoxes of international negotiation is that sometimes the party that has the

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<sup>3</sup> The strategic choice approach to the study of international relations and the components of strategic choice are discussed in: Lake, D. A. and Powell, R. (eds), *Strategic Choice and International Relations*, Princeton University Press, Princeton, New Jersey.

<sup>4</sup> Lowe, Carleton and Ward, 2002, *op. cit.*

<sup>5</sup> Khamsi, K., 2005. ‘A settlement to the Timor Sea dispute’, *Harvard Asia Quarterly*, vol.IX(4) <http://www.asiaquarterly.com> <Accessed 25 February 2006>

<sup>6</sup> Bacharach, S. B. and Lawler, E. J., 1981, *Bargaining Power, Tactics and Outcomes*, Jossey-Bass, San Francisco

most to lose from not settling can gain more from an opponent whose comparative costs of ‘no agreement’ are less.<sup>7</sup> Under normal circumstances, one would expect the least dependent, and therefore less vulnerable, party to use the threat of breaking the relationship as a form of influence over its more dependent counterpart. Bacharach and Lawler have suggested, however, that when one of the parties perceives that it is more dependent than the other, this may motivate it to devote more resources and effort to achieving its goals; a party with more at stake has every reason to push strongly in the negotiations, while “a party with less commitment might be more inclined to yield to a party with greater commitment to the outcomes”.<sup>8</sup> In this sense, weakness can sometimes be strength.

However, notwithstanding the critical role played by the tactical maneuvering of the principal actors both in and around the negotiations, the tight interdependence between the normative framework and negotiated outcomes in this study tells us something about governance in the international realm, which suggests that this research may have wider implications. The evolution of the regime of maritime delimitation is indicative of a particular pattern by which modes of international governance evolve through inter-state conflict and third-party dispute settlement. Alec Stone Sweet has observed that once treaty systems have been negotiated and established, the effect that the legal rules contained within those systems have upon future disputes and negotiations increases over time. This occurs by way of a process of “judicialization” that is dynamic, cyclical and self-reinforcing through time.<sup>9</sup> When third-party dispute settlement mechanisms are used to resolve points of legal interpretation and application, international legal regimes tend to be strengthened and come to exert greater influence over governments in their future dealings with one another. The use of international courts is critical for the construction of international governance, for it opens the deliberative space for further normative development. Normative development occurs through the process of judicial decision-making. The jurisprudence then feeds back into the negotiation process through the efforts made by negotiators to exert influence over their opponent through diplomatic negotiations. As Stone Sweet and Sandholtz have observed, legal rules:

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<sup>7</sup> See for example, Hirschman, A. O., 1978. ‘Beyond Asymmetry: critical notes on myself as a young man and on some other friends’, *International Organization*, vol.32(1), p.47; Baldwin, D. A., 1980. ‘Interdependence and Power: a conceptual analysis’, *International Organization*, vol.34(4), p.498.

<sup>8</sup> Bacharach and Lawler, 1981, *op. cit.*, p.96-7.

<sup>9</sup> Stone Sweet, A., 2000. *Governing with Judges: constitutional politics in Europe*, Oxford University Press, Oxford;

establish the social context in which actors' interests and strategies take shape. Rules define the game, establishing for players both the objectives and the range of appropriate tactics and moves. Actors behave in self-interested ways, but both the interests and the behaviours take form in a social setting defined by rules.<sup>10</sup>

This research provides cogent empirical support for the type of 'positive feedback' effect that Stone Sweet and others have documented within other international legal/political domains.<sup>11</sup> Though they may have been the product of tough and competitive bargaining, the agreements concluded by Australia and East Timor are fully consistent with the basic requirements of international law – that being, a set of provisional arrangements for the purposes of exploiting the resources pending delimitation; and the close correspondence between the jurisprudence and the percentage division of resources is illustrative of the way in which the normative framework governing maritime delimitation imposes itself upon political bargaining in this area of international relations. Thus, whilst international law provides states with *carte blanche* to divide maritime areas subject to their jurisdiction in whatever manner they see fit, the implications of this research is that states, in reality, face a much tighter range of possible outcomes. Unless both sides feel satisfied that the endpoint to negotiations reflects the type of outcome that could be obtained in court, the result is likely to be no agreement and either a costly litigation process or an uncertain future, as a consequence of leaving the dispute unresolved.

Identifying the causal mechanisms, or pathways, by which international law feeds back into bargaining processes and shapes political outcomes is of key interest within the study of International Relations.<sup>12</sup> As noted in Chapter One, different types of causal mechanisms may be distinguished. In this study, the process through which legal norms have primarily exerted influence is via the dynamics of strategic interaction and rational choice.

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<sup>10</sup> Stone Sweet, A. and Sandholtz, W. 1998. 'Integration, supranational governance, and the institutionalization of the European polity', in Sandholtz, W. and Stone Sweet, A. (eds), *European Integration and Supranational Governance*, Oxford University Press, Oxford, p.16.

<sup>11</sup> The most widely researched areas include international trade negotiations and EU policy-making. See Sandholtz, W. and Stone Sweet, A., 2004. 'Law, politics and international governance', in C. Reus-Smit (ed.), *The Politics of International Law*, Cambridge University Press, Cambridge; Palmetier, D. and Mavroidis, P. C., 2004. *Dispute Settlement in the World Trade Organization: practice and procedure*, 2<sup>nd</sup> Ed., Cambridge University Press, Cambridge; See, also, for a general elaboration of the theory, Mnookin, R. H. and Kornhauser, L., 1979. 'Bargaining in the shadow of the law: the case of divorce', *Yale Law Journal*, vol.88, p.950-97.

<sup>12</sup> Goldstein, J., Kahler, M., Keohane, R. O. and A. M. Slaughter, 2000. 'Introduction: legalization and world politics', *International Organization*, vol.54(3):385-99; Reus-Smit, C., 2004. 'Introduction', in C. Reus-Smit (ed.), *The Politics of International Law*, Cambridge University Press, Cambridge.

This is an important finding that correlates with other empirical studies of maritime boundary negotiations.<sup>13</sup> Whilst it may be possible for negotiators to gain concessions by convincing the other side of the merits of their claim, the more likely scenario is that concession-making will be a function of a ‘consequentialist logic’, in which perceived comparative resolve with elements of exchange and reciprocity play an important role. Yet, in a study such as this, the conclusions drawn are bound to be tentative. The story of the negotiations between Australia, the UN and East Timor is undoubtedly a unique one: it is a story of how multiple, interacting and yet seemingly unrelated processes – such as the evolution of the international law of the sea, the growth and development of global energy markets and a peoples’ struggle for self-determination over territory and resources – momentarily and dramatically combined within the one location, and at the same time, in a fashion that is unlikely to happen again, anywhere else in the world.

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<sup>13</sup> Oude Elferink, A., 1994. *The Law of Maritime Boundary Delimitation: a case study of the Russian Federation*, Martinus Nijhoff Publishers, Dordrecht, the Netherlands; Charney, J. I., 1994. ‘Progress in international maritime boundary delimitation law’, *American Journal of International Law*, vol.88(2):227-56; Colson, D. A., ‘Remarks’, paper presented at a workshop organized by the International Boundaries Research Unit, 15 December 1997.

## **KEY RESEARCH CONVERSATIONS AND INTERVIEWS\***

### **AUSTRALIA<sup>†</sup>**

Anja Hilkmeyer, Department of Foreign Affairs and Trade, April 2006, telephone conversation.

Robert Mollah, Timor Gap Joint Authority, July 2004, Brisbane.

Senior Official, Department of Industry, Tourism and Resources, November 2005, Canberra.

Senior Official, Department of Foreign Affairs and Trade, June 2005, Canberra.

### **UN/EAST TIMOR**

Nuno Antunes, Legal Consultant, October 2004, Darwin.

Niny Borges, Director, Legal, Timor Sea Designated Authority, May 2004, Darwin.

Philip Daniel, Economic/Tax Consultant, January 2005, London.

Peter Galbraith, UNTAET, Director of Political Affairs, August 2004, Washington, D.C.

Jonathan Morrow, UNTAET, Timor Sea Office, August 2004, Washington, D.C.

Hansjoerg Strohmeyer, UNTAET, Principal Legal Adviser to Sergio Vieira de Mello, August 2004, New York.

Jose Teixeira, Secretary of State for Tourism, Environment and Investment, July 2004, Dili.

### **NORTHERN TERRITORY**

Andrew Andrejewskis, Office of Territory Development, July 2004, Darwin.

Peter Blake, Department of Mines and Energy, July 2004, Darwin.

Denis Burke, Chief Minister (1999 to 2001), July 2004, Darwin.

Clair Martin, Chief Minister (2001 to present), July 2004, Darwin

### **OIL COMPANIES**

Arthur Fredston, Pillsbury Winthrop (for Oceanic Exploration), July 2005, New York.

James Godlove, ConocoPhillips, August 2004, Washington, D.C.

Vaughn Lowe, Oxford University (for Oceanic Exploration), January 2005, Oxford.

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\* The list includes ten people who were directly involved in the negotiations between Australia and East Timor over the course of the five year period.

<sup>†</sup> Two other senior officials from the Department of Foreign Affairs and two from the Attorney-General's Department who had played a role in the negotiations were contacted for the purposes of this research but they declined to be interviewed.

Mike Nazroo, ConocoPhillips, April 2005, Perth.

Adrian Wilks, Woodside Energy, April 2005, Perth.

**NGOs/Activists/Others**

Patrick Brazil, former Secretary, Attorney-General's Department, May 2005, Canberra.

Robert Furlonger, former Australian Ambassador to Indonesia, August 2004, telephone conversation.

Geoffrey McKee, petroleum consultant, November 2003, New South Wales.

Karen Orenstein, East Timor Action Network, August 2004, Washington, D.C.

Rob Wesley-Smith, Australians for a Free East Timor, July 2004, Darwin



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Cable from S. V. de Mello to B. Miyet, 'Timor Gap – First round of formal negotiations' (Dili 9-12 October), 12 October 2000.

Cable from S. V. de Mello to B. Miyet, 'Timor Gap negotiations', 27 October 2000.

Cable from S. V. de Mello to J. M. Guéhenno, 'Timor Gap Second Round of Formal Talks', 11 April 2001.

Cable from S. V. de Mello to J. M. Guéhenno, 'Timor Gap Second Round Follow-up', 12 April 2000.

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House Floor Statement by U.S. Rep. Jim McGovern on the U.S. – Australia Free Trade Agreement, 14 July 2004, <http://www.house.gov/mcgovern/floor071404australiatrade.htm> <Accessed 8 November 2005>

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<http://etan.org/news/2004/03houseltr.htm#letter> <Accessed 22 November 2005>

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Minutes from Australia-UNTAET/East Timor negotiations on Petroleum Activities in the Timor Sea, 14 June 2001.

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<http://etan.org/news/2003a/11ltr.htm> <Accessed 7 November 2005>

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Record of Meeting between Arthur Fredston, acting on behalf of Oceanic, and Mari Alkatiri, 1 November 2001.

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