

# Implications of recent changes to Timor-Leste's Petroleum Fund

Timor-Leste Studies Association 2019

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28 June 2019



## Petroleum Fund origin and objectives

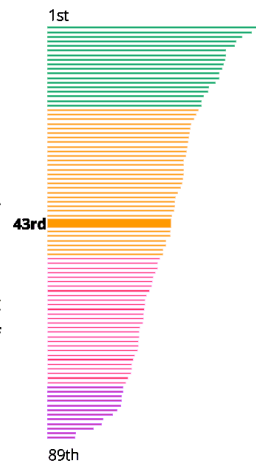
- **Avoid resource curse**
- **Stabilization – oil prices and production vary**
- **Sustainability – after the oil runs out**
- **Buffering – keep state expenditures separate from oil money**
- **Transparency – avoid corruption, inform citizens, improve policy decisions**
- **“For the benefit of current and future generations”**

## We were world leaders in 2006, average in 2017, and worse now.

### Timor-Leste

#### 2017 RESOURCE GOVERNANCE INDEX

Timor-Leste's oil and gas sector scores 49 of 100 points in the 2017 Resource Governance Index (RGI), ranking 43rd among 89 assessments and eighth among 15 assessments in the Asia Pacific region. This overall score is lowered by a poor score in the enabling environment component. Even though both extractive sector components, value realization and revenue management, achieve similar scores, there is great variation in performance at the subcomponent level. The oil and gas sector constituted 98 percent of exports and 97 percent of government revenues in 2013, making this sector a key facilitator of economic development.<sup>1</sup>



## Legal framework

- **Petroleum Activities Law no. 11/2005 (PAL)**

Regulates how Timor-Leste contracts with petroleum companies and what rules they must follow, transparency, environment, etc.

- **Petroleum Fund Law no. 9/2005 (PFL)**

- All oil money goes in to the Fund. Withdrawn only with Parliamentary approval (normally through GSB)
- Mandates regular publication, consultation and transparency.
- Estimated Sustainable Income (ESI) guideline: 3% of (balance + prudent projections of future petroleum revenue)
- Investment rules: Initially all U.S. gov't bonds; diversified in stages to international bonds and equities, and then to private debt.
- 2011 revision: Changed investment profile, weakened ESI and debt collateral rules
- 2018 unauthorized and authorized extraordinary withdrawals
- 2019 investment rules overridden by revision to PAL

## Public consultation & deliberations

Legislation	When	Days	Consultation	Parliament
Petroleum Fund Law no. 11/2005	2004-5	304	Three rounds of hearings nationwide, 25 submissions	Unanimous passage after two months of hearings and debate
Petroleum Activities Law no. 9/2005	2004-5	335	Many workshops, one round of hearings, nine submissions	Pending in PN for seven months, no hearings before enactment
Revisions to Petroleum Fund Law	2010-11	457	Many workshops, two hearings, four submissions	Discussed for two weeks, passed with few changes
\$70m extraordinary transfer from PF	May 2018	0	No legislative process, probably illegal	Not submitted for approval
\$140m extraordinary transfer from PF	July 2018	10	None. LH made submission to rumored broad draft, which was replaced by a one-time transfer	One-off transfer approved
Revisions to Petroleum Activities Law	Oct-Nov 2018	23	Secret draft. Brief Parliamentary hearing on preliminary version	Major addition just before final vote. Vetoed, overridden, challenged in court. Retroactive

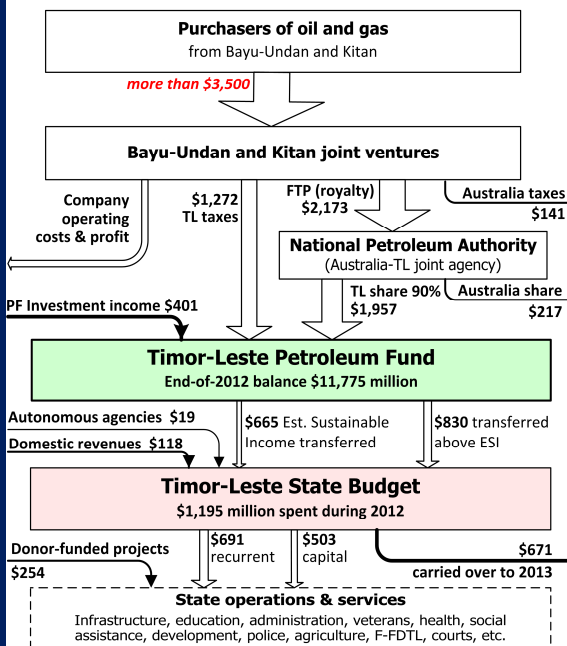
**Petroleum revenue peaked in 2012, and this is how it flowed in and out of the Petroleum Fund.**

**The basic structure hasn't changed, but details have.**

**From 2005 thru 5/2019:**  
 \$22.4 bn oil revenues  
 +\$ 5.3 bn invest. return  
**-\$10.7 bn withdrawn**  
**\$17.1 bn balance**

### Timor-Leste's Petroleum Revenue Streams

Totals for 2012. Millions of U.S. dollars, estimates in *italics*.

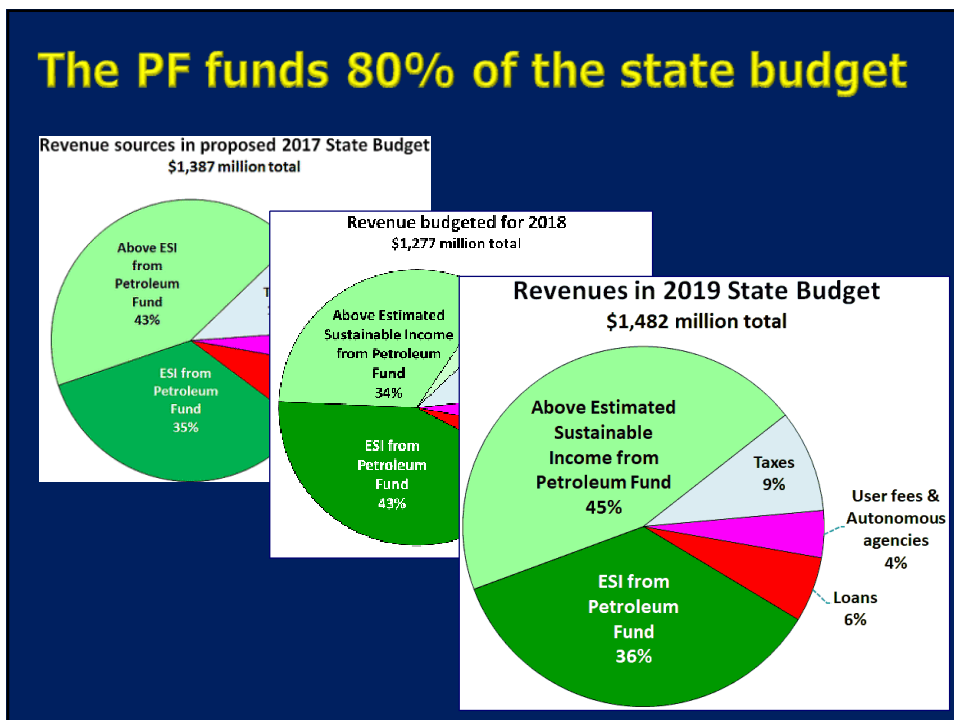


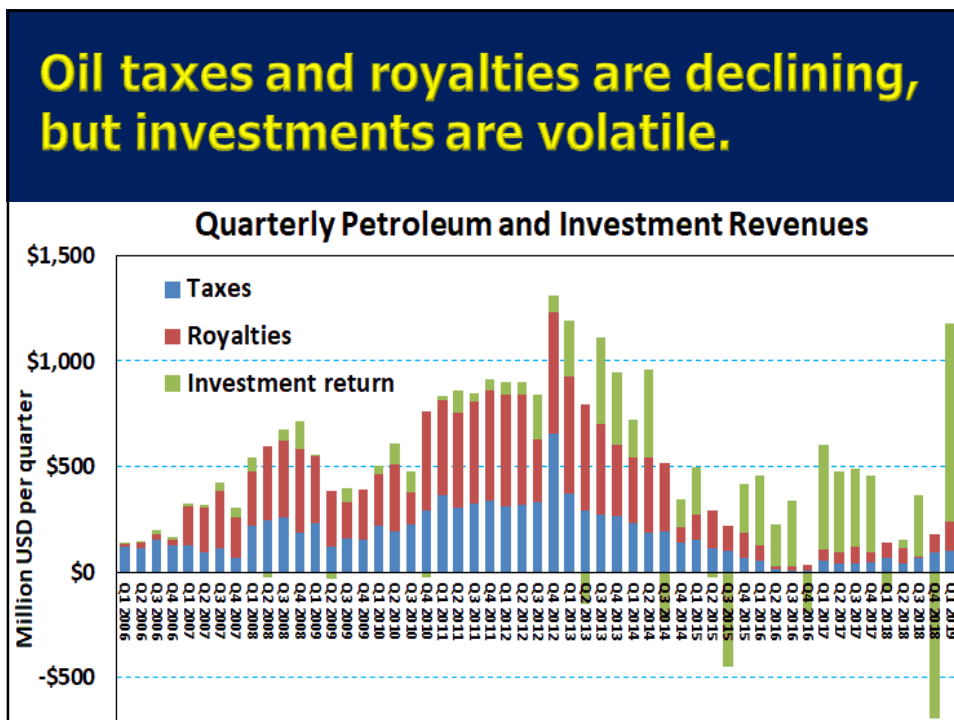
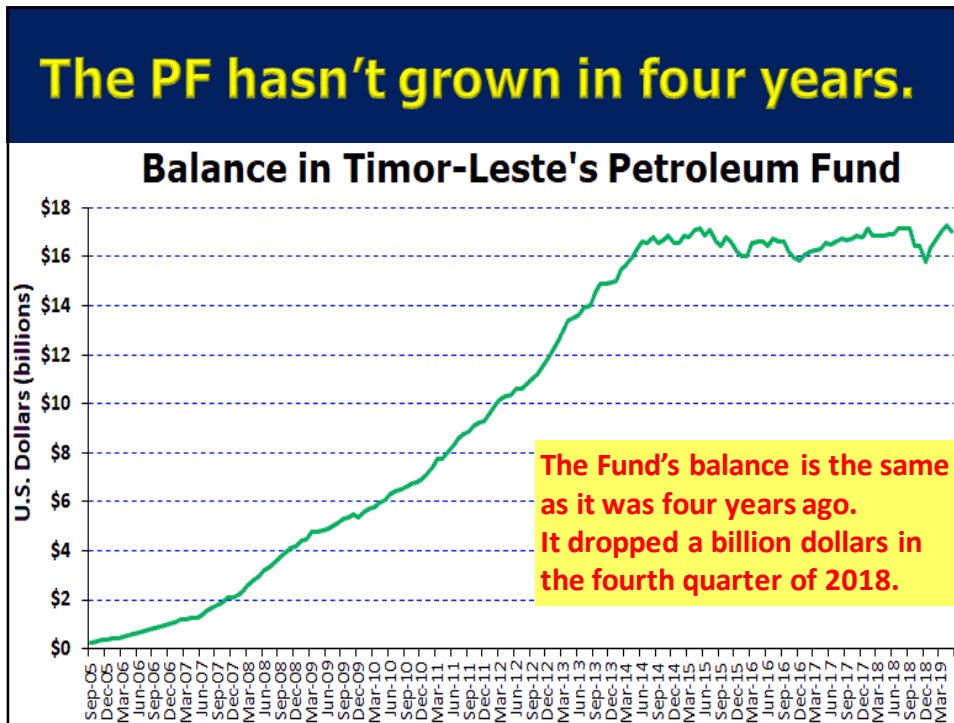
## Petroleum Dependency (nominal USD)

	2013	2014	2015	2016	2017
<b>Petroleum GDP</b>	<b>\$4,234</b> (75%)	<b>\$2,591</b> (64%)	<b>\$1,496</b> (48%)	<b>\$820</b> (33%)	<b>\$895</b> (36%)
<b>Non-oil GDP</b>	<b>\$1,403</b> (25%)	<b>\$1,451</b> (36%)	<b>\$1,597</b> (52%)	<b>\$1,684</b> (67%)	<b>\$1,593</b> (64%)
<b>Productive (agric. &amp; manuf.)</b>	<b>\$305</b>	<b>\$307</b>	<b>\$288</b>	<b>\$287</b>	<b>\$284</b>

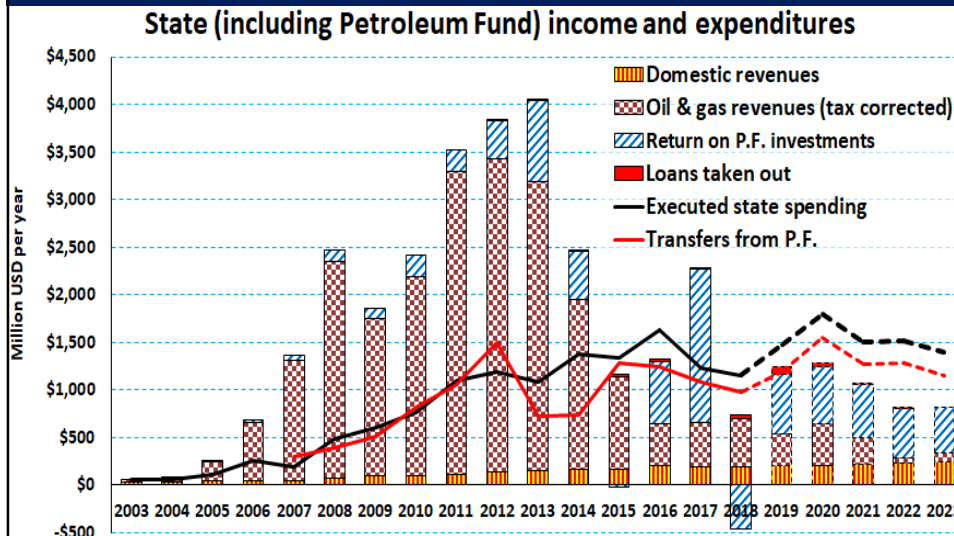
- **State revenues in 2018:..... \$154 million**  
 -\$460 million was lost from investing the Petroleum Fund  
 \$447 million from oil and gas revenues  
 \$167 million from non-petroleum sources
- **Executed 2018 State Budget:..... \$1,154 million** (\$1,277m appropriated)  
 \$983 million transferred from the Petroleum Fund  
 \$167 million from non-petroleum (domestic) revenues  
 \$ 39 million from loans which will have to be repaid
- State activities, paid for with oil money, are nearly half of the "non-oil" economy because some of this money circulates in the local economy.
- Petroleum and investment "income" goes to the state, not the people.

**Only South Sudan, Libya (and Equatorial Guinea?) are more dependent on oil and gas exports than Timor-Leste was before 2014.**

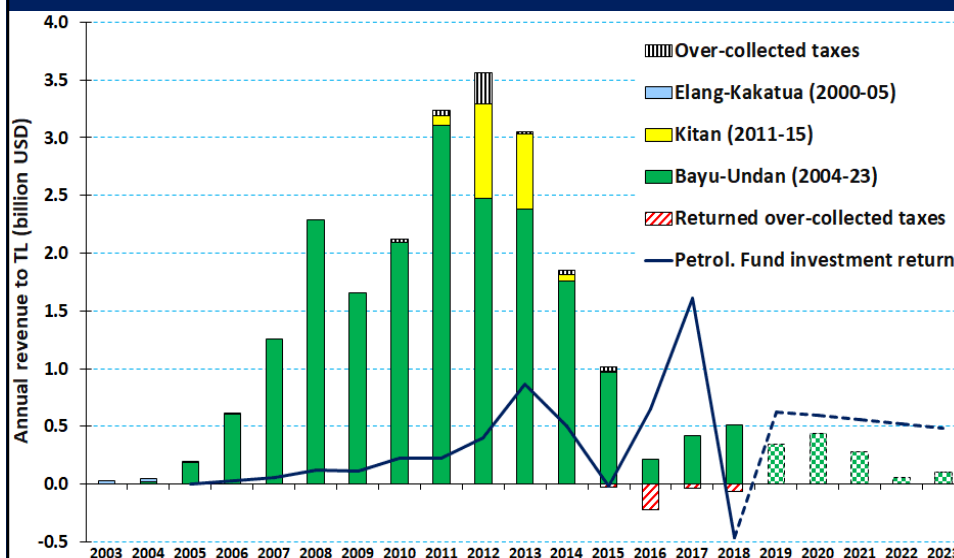




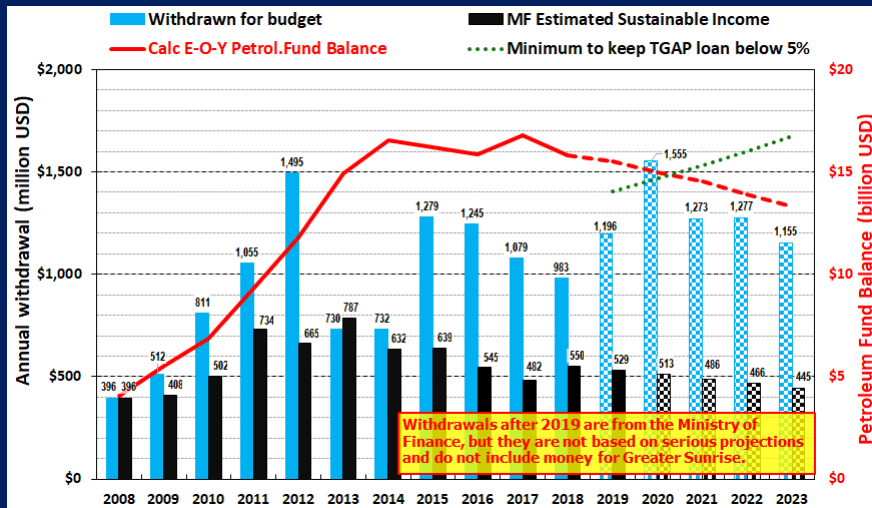
## We depend on investments now, not oil and gas.



## Where TL's oil income comes from



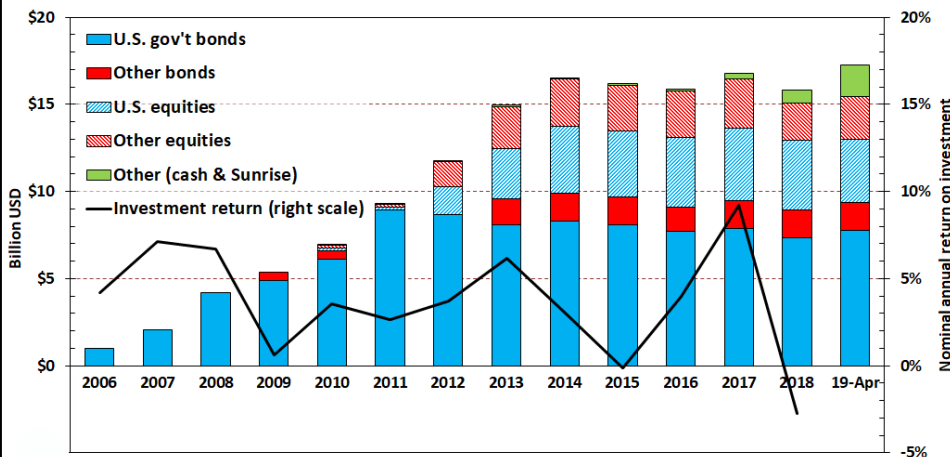
## Historic and planned PF withdrawals



The Petroleum Fund reached \$17.1 billion four years ago and has not increased since then. It is likely to decline from now on.

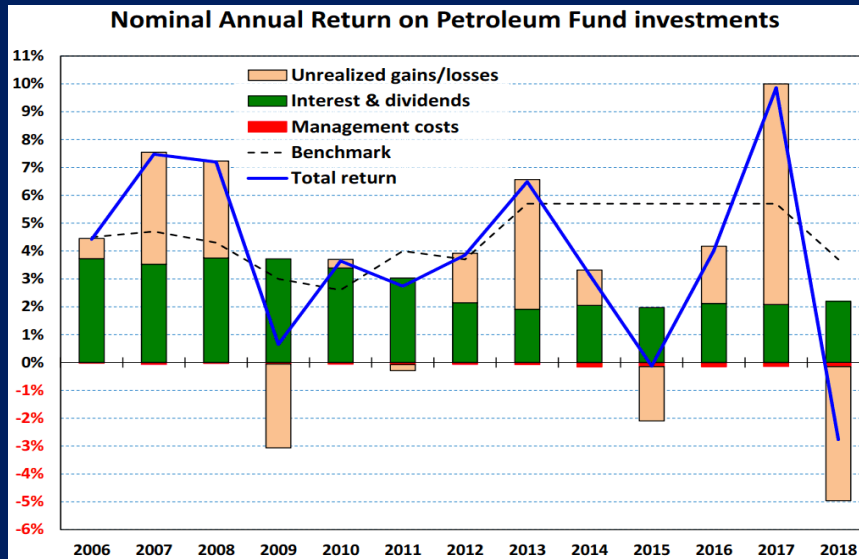
## Diversification of P.F. investments

How the Petroleum Fund is Invested



The 2011 revision allowed 40% in equities (stocks) and the recent change allowed 5% in "Petroleum Operations" (Greater Sunrise).

## More stocks bring more volatility



## 2018-2019 changes to Petroleum Activities Law

- Prohibits prior Audit Court review of petroleum-related contracts and agreements.
- Allows TimorGAP to own more than 20% of a project (which it already does for several projects).
- A last-minute addition overrides the P.F. Law to enable up to 5% of the Fund to be invested in petroleum operations within Timor-Leste.
- The law was vetoed by the President, but the veto was overridden.
- Promulgated as Law no. 1/2019 of 18 January 2019, retroactive to 27 September 2018.
- The Court of Appeal has ruled that the main points are legal and constitutional.



## PF Law Article 15: Investment Rules

- 1.** Under the criteria in this article, to qualify as eligible investment, the investment instrument must be issued or the investment be located abroad, in an internationally recognized jurisdiction.
- 4.** No more than 5% of the Petroleum Fund should be invested in other eligible investments, provided that:
  - a) The Minister has included such other asset class, which is part of the investment, in the proposed distribution of portfolios submitted to the National Parliament under Article 14.5, and
  - b) The rules and criteria for selection, management and evaluation of each individual financial instrument within a certain asset class, have been approved by the Minister and published.
- 5.** The exposure of the Petroleum Fund to:
  - a) Any company or the issuing entity for the eligible instruments, with the exception of sovereign states, can never exceed 3% of the total value of the Petroleum Fund;

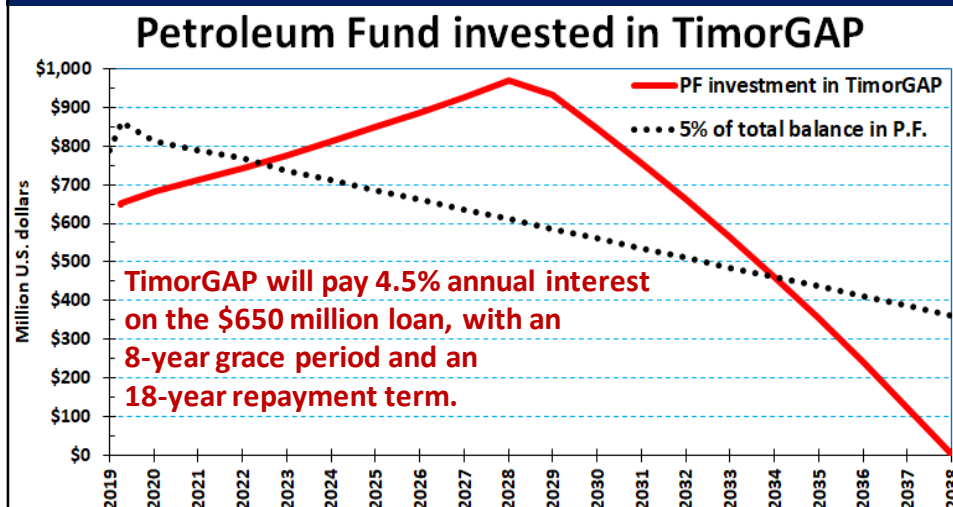
## Petroleum Activities Law as amended, Article 22: State Participation

- 6.** The Petroleum Fund may be applied directly in Petroleum Operations, in the national territory or abroad, through the execution of commercial transactions, through Timor Gap, E.P., pursuant to Article 15.4 of Law no. 9/2005 ... republished by Law no. 12/2011.
- 7.** Contracts for purchase and sale, acquisition, assignment, transfer, novation, merger, encumbrance or any other legal transaction entered into or payments made by Timor-Leste or any other Timorese public corporation, including entities wholly owned or controlled by them, is designed to allow the participation of Timor-Leste or any other Timorese public legal person, including through entities fully owned or controlled by them, or of the Petroleum Fund, in Petroleum Operations and, as well as for the conduct of these, are not subject to prior inspection by the Audit Chamber of the High Administrative, Tax and Audit Court.

## What just happened?

- Last September and October, Timor-Leste agreed to pay ConocoPhillips and Shell \$650 for their participation in the Greater Sunrise Joint Venture, amounting to 56.56% of the project.
- The proposed 2019 State Budget included \$350m for this, and Parliament added \$300m at the last minute. After a Presidential veto, the appropriation was removed from the Budget.
- In February, the interim Minister of Finance informed the Central Bank and Parliament of a new PF investment policy, which was then approved by the Council of Ministers. On 11 March, the Ministry signed a new management agreement with BCTL.
- On 10 April, the PF loaned \$650 million to TimorGAP for 18 years.
- On 16 April, following Australian regulatory approval, TimorGAP paid the money to ConocoPhillips and Shell.
- Timor-Leste now owns 57% of Sunrise, and will be responsible for 57% of the offshore, in-field capital costs and 100% of the on-shore costs. It may earn some revenues in the future.

## In four years, the loan to TimorGAP will exceed the 5% legal limit.



## Recent context and developments

- Very little future oil income. Kitan has finished and Bayu-Undan is 95% depleted. The Maritime Boundary Treaty will help a little, but Sunrise will probably provide less annual income than Bayu-Undan did.
- TL's population, expectations, maintenance and salaries keep going up.
- U.S. and global financial markets are volatile and uncertain.
- About 5% of the Petroleum Fund is no longer liquid or tradeable.
- No serious, comprehensive, unbiased public analysis has evaluated the financial, economic, social and environmental costs, benefits and risks of the Sunrise project to Timor-Leste's people, or the alternatives.
- Timor-Leste can force Sunrise gas to be liquefied in Beaçú, but will have to come up with \$10-\$20 billion in capital costs and find the expertise to design, build, manage and operate this complex project for the next 30 years. The money and attention given to it reduces the likelihood of more sustainable economic development options.
- Renewable energy is getting cheaper, and growing awareness of the climate emergency will make fossil fuels less valuable in the future.

## What will Tasi Mane really cost?

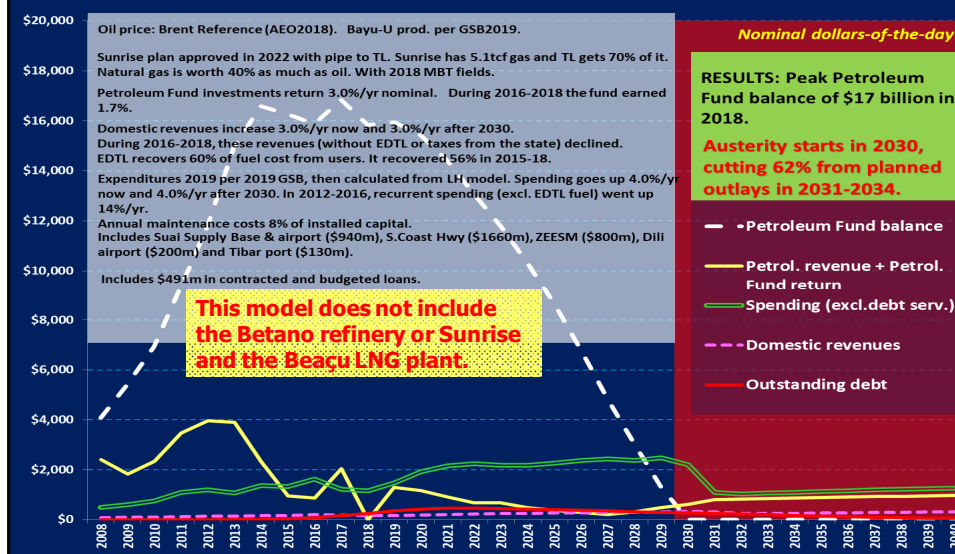
This estimates capital expenditures only, not operational costs. Most have never appeared in state budget forecasts.

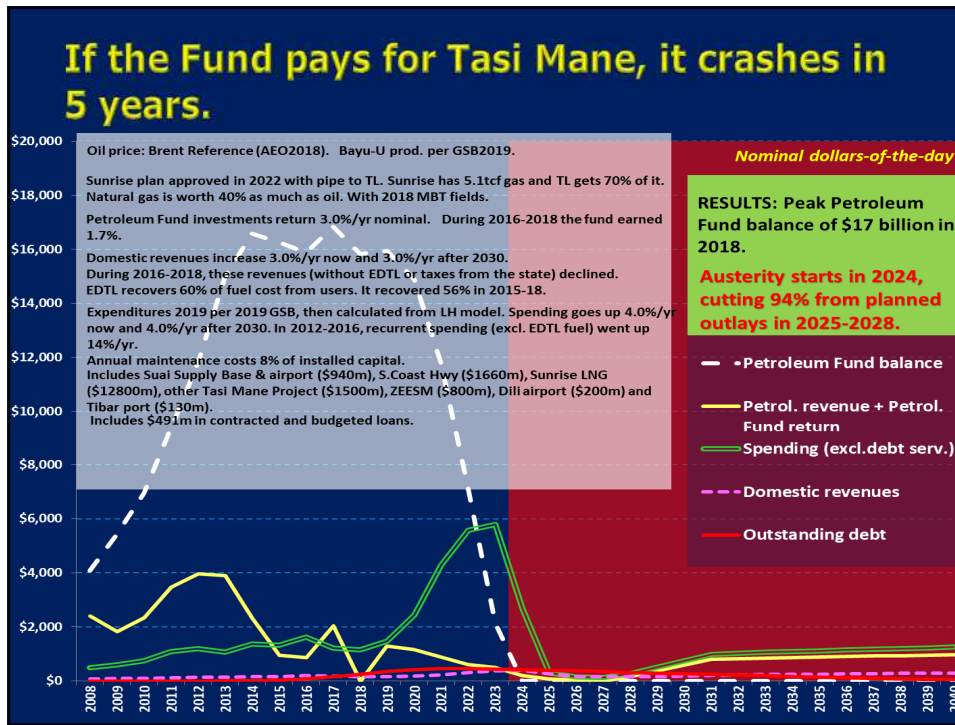
Money spent, budgeted and required for the Tasi Mane project (millions of USD)							
Component	Location	Status	Spent through 2018	Budgeted 2019	Budgeted 2020-2023	Estimated total capital cost	Percent budgeted
Airport	Suai	Constructed	70	10	3	90	92%
Supply base	Suai	Tender pending	6	10	668	850	80%
Highway	Suai-Fatukai	Mostly built	267	50	8	340	96%
Highway	Fatukai-Beaçú	Not started	3	-	-	1,320	0%
Airport	Viqueque	Not started	-	-	-	60	0%
Oil refinery & pipelines	Betano	Pending design	3	-	-	1,500	0%
Gas pipeline, LNG plant & port	Sunrise-Beaçú	Pending design, seeking financing	12	-	-	6,000	0%
57% share of Greater Sunrise Joint Venture	Offshore	Borrowed directly from the Petroleum Fund	-	650	-	650	100%
57% of Sunrise upstream capital expenditure	Offshore	Pending design, seeking financing	-	-	-	6,840	0%
Administrative and other costs	Dili	Ongoing	49	12	50	400	28%
<b>TOTAL</b>			<b>410</b>	<b>732</b>	<b>729</b>	<b>18,050</b>	<b>10%</b>

## What other changes are being considered?

- Seeking external financing for Tasi Mane infrastructure, but it may be hard to find
- Amending the PF and PA laws next month before ratifying the Boundary Treaty
- Legal changes needed before the loan to TimorGAP exceeds 5% of the PF
- Allocating part of the PF to invest in Timor-Leste outside of the budget process
- Eliminating the ESI guideline altogether
- Using the PF as collateral for debts
- Bankrupting the country

## If current plans continue, TL may be unable to finance its budget in 11 years. The Boundary Treaty and Sunrise help a little, but not enough.

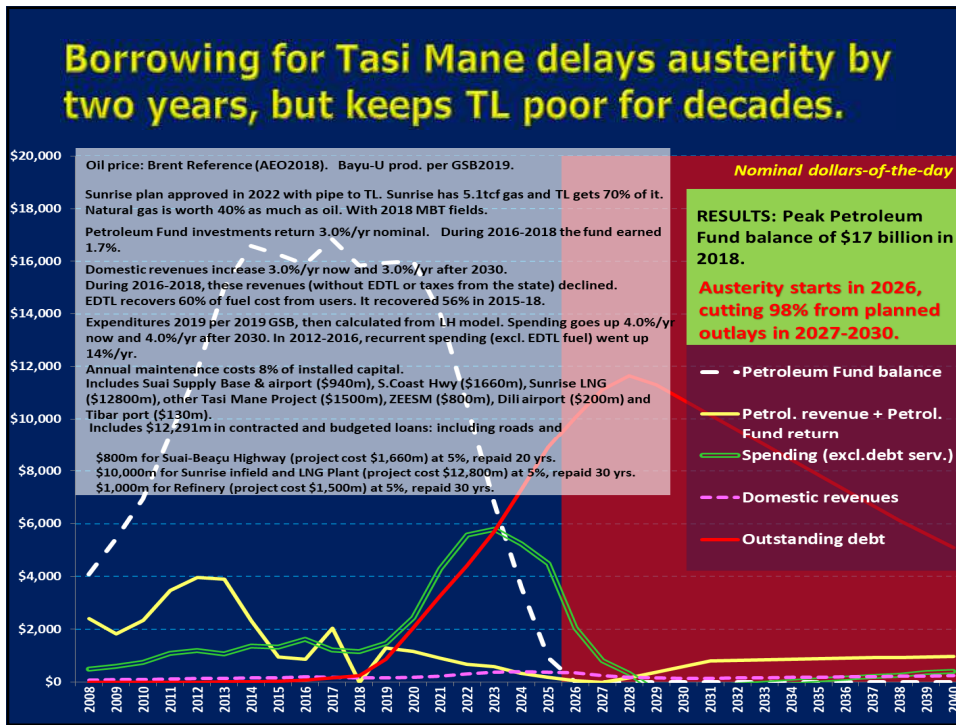




## From Final 2019 Budget Book 4B, ... but not in Book 1's totals or deficits.

**D2 - MINISTÉRIO DO PETRÓLIO E MINERAIS**  
**MINISTRY OF MINERAL RESOURCES AND OIL (\$'000)**  
**D20201 - DIRECÇÃO NACIONAL DE ADMINISTRAÇÃO E FINANÇAS**  
**NATIONAL DIRECTORATE OF ADMINISTRATION AND FINANCE (\$'000)**

Rubrica de Despesas / Expense Item	2018	2019	2020	2021	2022	2023
<b>Despesas / Expenses</b>	12,422	29,208	3,151,656	3,277,722	3,408,831	3,545,185
<b>Transferências / Transfers</b>	12,094	28,747	3,151,177	3,277,224	3,408,313	3,544,646
Pagamentos Pessoais / Personal Benefit Payments	-	-	-	-	-	-
Concessões Publicas / Public Grants	12,094	28,747	3,151,177	3,277,224	3,408,313	3,544,646



### We don't have very much oil.

	Timor-Leste (70% Sunrise)	TL without Sunrise	Australia	Brunei
Known oil and gas reserves per person at end of 2017	657 barrels	69 barrels	1,050 barrels+ (1,040 without Sunrise)	6,300 barrels
How long reserves will last at 2017 production rates	21 years	2 years	32 years+	24 years

**Thank you.**

**You will find more and updated information at**

- **La'ó Hamutuk's website**  
<http://www.laohamutuk.org>
- **La'ó Hamutuk's blog**  
<http://laohamutuk.blogspot.com/>

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