Global Arbitration Review

The Asia-Pacific Arbitration Review

2019

Oil and Gas Arbitration in the Asia-Pacific Region

The Asia-Pacific Arbitration Review

2019

Global Arbitration Review is delighted to publish The Asia-Pacific Arbitration Review 2019, one of a series of special reports that deliver business-focused intelligence and analysis designed to help general counsel, arbitrators and private practitioners to avoid the pitfalls and seize the opportunities of international arbitration.

Generated: February 8, 2024

GAR Global Arbitration Review

Oil and Gas Arbitration in the Asia-Pacific Region

Duncan Speller, **Jonathan Lim** and **Justin Li**
Wilmer Cutler Pickering Hale and Dorr LLP

Summary

INTRODUCTION
CURRENT TRENDS
ENHANCING THE APPEAL OF INTERNATIONAL ARBITRATION
INSTITUTIONAL DEVELOPMENTS
LEGISLATIVE CHANGES
ARBITRATIONS INVOLVING STATES OR STATE-LINKED PARTIES
COMMERCIAL ARBITRATIONS
INVESTMENT TREATY ARBITRATIONS
FUTURE DIRECTIONS
PRICE MOVEMENTS AND VOLATILITY
OTHER LNG DISPUTES
STATE-TO-STATE ARBITRATION DISPUTES
ENDNOTES

INTRODUCTION

The increased use of arbitration by parties in the Asia-Pacific region1 has been a consistent trend over the past decade, and shows no sign of declining. For example, the Singapore International Arbitration Centre (SIAC) recently announced that it administered an all-time record number of 452 new cases in 2017, up 32 per cent from 343 new cases in 2016 and a 67 per cent increase from the 271 new cases filed in 2015.2 The Chinese International Economic and Trade Arbitration Commission (CIETAC) also administered its all-time high of 2,298 new domestic and foreign-related cases in 2017, up from only 981 cases in 2006.3 The Hong Kong International Arbitration Centre (HKIAC) had a total of 460 new cases filed in 2016;4 of these new cases, 262 were arbitrations, 15 were mediations and 183 were domain name disputes.5

The importance of the oil and gas sector to the Asia-Pacific economies cannot be understated.6 It is therefore unsurprising that oil and gas arbitrations have continued to increase in both prominence and frequency.

Disputes arising out of the oil and gas sector, which is often characterised by large, complex and capital-intensive ventures involving participants from multiple jurisdictions, are particularly suitable for international arbitration. Indeed, in a survey by the Queen Mary University of London, 56 per cent of energy industry respondents preferred arbitration as a choice of resolving cross border disputes, and 78 per cent of energy industry respondents strongly agree or agree that arbitration is well suited to the energy industry.7

The Asia-Pacific region's share of global energy consumption is expected to rise to 49 per cent – or almost half of global consumption – by 2040.8 These dramatic increases in commercial and economic activity in the oil and gas sector portend an even greater role for international arbitration in the Asia-Pacific region.

The types of interests that may give rise to arbitration in the oil and gas sector are diverse, and vary within the region. Japan, South Korea, China (including Taiwan) and India accounted for 69 per cent of global liquefied natural gas (LNG) net imports in 2016, with Japan alone accounting for 32 per cent of global net imports.9 Australia, Malaysia, India and Indonesia, along with China, are the largest oil and gas producers in the Asia-Pacific region.10 Jurisdictions such as Timor Leste, Vietnam and the Philippines have significant amounts of unexplored oil and gas resources that are more recently being commercialised.

Although it is difficult to generalise about the varied contracts, practices and legal frameworks pertaining to oil and gas across the Asia-Pacific region, a few emerging trends can be identified. This article examines these trends and considers possible future directions for oil and gas arbitrations in the region.

CURRENT TRENDS

ENHANCING THE APPEAL OF INTERNATIONAL ARBITRATION

Several jurisdictions in the Asia-Pacific region have taken steps to make themselves more attractive to arbitration generally and oil and gas arbitration in particular. These have taken the form of institutional developments and legislative changes.

INSTITUTIONAL DEVELOPMENTS

Australia has introduced innovations specific to the oil and gas sector. In November 2014, the Perth Centre for Energy and Resources Arbitration (PCERA) was launched. As a specialised energy and resources arbitral institution with a dedicated panel of expert arbitrators, PCERA is the first of its kind in the Asia-Pacific region.11 In August 2017, PCERA published the PCERA Arbitration Rules 2017, which are based expressly on a modified version of the UNCITRAL Arbitration Rules.

Many institutions in the region have made changes that are designed to improve arbitration generally, but which will also, have a positive effect on oil and gas arbitrations. For example, the SIAC most recently revised its rules in 2016. A number of amendments will enhance the utility and attractiveness of the SIAC Rules to the oil and gas sector, including:

- the early dismissal of claims and defences procedure;
- provisions regarding joinder of additional parties and consolidation of multiple arbitrations; and
- further refinements to the existing emergency arbitrator and expedited arbitration procedures.12

Given that oil and gas disputes often involve multiple contracts and multiple parties, joining relevant parties or consolidating the dispute in a single arbitral forum will result in a more efficient resolution of the dispute, if it is fair and appropriate to do so. Disputing parties will also benefit from the enhancements made by the SIAC to its emergency arbitrator mechanism, which allows parties to obtain expedited interim relief before the constitution of the tribunal within 14 days,13 and to the expedited procedure, which allows parties to obtain an award within six months of the constitution of the tribunal.14

The SIAC has also released its first set of investment arbitration rules (SIAC IA Rules), which came into effect on 1 January 2017.15 The SIAC IA Rules were developed with a view towards issues 'unique to international investment arbitration'.16 Some of the key provisions under the SIAC IA Rules include:

- a default list procedure for the appointment of the sole or presiding arbitrator;
- an opt-in mechanism for the appointment of an emergency arbitrator;
- a procedure for early dismissal of claims and defences;
- provisions for submissions by non-disputing parties; and
- provisions to enable the tribunal to order the disclosure of third-party funding arrangements and to take such arrangements into account when apportioning costs.17

More recently, the SIAC proposed an innovative cross-institution consolidation protocol,-18 which is designed to facilitate the consolidation of international commercial disputes across multiple institutions. Such consolidation is currently not possible under the leading institutional arbitration rules. The SIAC has prepared a memorandum discussing the protocol for cross-institution consolidation,19 and is in the process of engaging with other arbitral institutions and the arbitration community on the protocol.

There is a degree of convergence among the rules of the leading centres in the Asia-Pacific region. The HKIAC revised its rules in 2013, and the latest version of the HKIAC Rules also include comprehensive provisions dealing with multiple contracts, joinder and consolidation, emergency interim relief and expedited procedures.20 CIETAC also revised its rules in 2015, and the revised rules also have provisions on multiple contracts, joinder and consolidation, and emergency interim relief and expedited procedures.21 In addition, on 1 October 2017, CIETAC has also released the International Investment Arbitration Rules (CIETAC IA Rules), the first set of investment arbitration rules promulgated by a Chinese arbitration institution.-22

In April 2016, India set up the Mumbai Centre for International Arbitration (MCIA), its first home-grown international arbitration centre.23 The MCIA Rules, like the other leading rules in the region, have provisions dealing with multiple contracts, joinder and consolidation, emergency interim relief and expedited procedures.

LEGISLATIVE CHANGES

Singapore and Hong Kong have periodically made refinements to their legal frameworks for arbitration to ensure that they remain ahead of latest developments in the field. Most recently, in 2017, both Singapore and Hong Kong took legislative steps to permit third party funding. Singapore introduced amendments to the Civil Law Act with effect from 1 March 2017 that abolished the common law torts of champerty and maintenance, and also provided that third party funding is not contrary to public policy or illegal when it is provided by qualifying funders in prescribed dispute resolution proceedings, details of which are set out in the Civil Law (Third Party Funding) Regulations 2017 (Regulations).24

In June 2017, Hong Kong passed the Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Ordinance 2017 to permit third-party funding. Unlike Singapore, Hong Kong does not mandate third-party funders to adhere to particular regulations. Hong Kong also adopted a broader definition of 'third-party funder' that is not limited to professional funders and includes any 'person who is a party to a funding agreement . . . and who does not have an interest recognised by the law in the arbitration other than under the funding agreement'.25 This would include lawyers and law firms (save for lawyers and law firms acting for a party in the arbitral proceedings).

These changes will provide additional options to arbitration users in the oil and gas sector in terms of funding their claims (although users should be aware that public policy issues may still arise if third party funding is prohibited in a jurisdiction where enforcement may be sought).

In 2015, Australia also made changes to its arbitration legislation that will have positive consequences for energy arbitrations. Notably, the amended International Arbitration Act now provides that arbitrations seated in Australia are presumptively confidential, subject to a number of limited exceptions, namely consent, third-party rights, enforcement of awards, public interest and natural justice.26 Confidentiality can be very important for the oil and gas industry, especially as highly valuable and proprietary information may be at stake, particularly in upstream exploration and appraisal ventures.

India has made significant strides to improve its reputation as a venue for arbitration, including revisions to its legal framework for arbitration through the 2015 Indian Arbitration and Conciliation (Amendment) Act which came into force on 23 October 2015.27 The key reforms made by the new act include:

-

that the provisions on court-ordered interim relief and court assistance in the taking of evidence would, subject to contrary agreement, apply to arbitrations seated outside India – a lacuna left by the much-criticised Balco decision;28

- strict time limits for an arbitral tribunal seated in India to render a final award;29 and
- limitations on the scope of 'public policy' as a ground for refusing enforcement of awards.30

Many of these changes are in line with modern arbitration practice (although some, such as the time limits, have been criticised) and, along with the introduction of the MCIA, will give India greater prominence as a potential seat for arbitration.

China is also continually improving its arbitration legal framework. Under Chinese law, before a lower court refuses recognition or enforcement of a foreign-related or foreign arbitration award, such decision has to be reported to the Supreme People's Court (SPC).31 In 2017, the SPC released two judicial interpretations on arbitration (the Interpretations).32 The Interpretations extend the SPC reporting system to domestic arbitral awards, permit parties to participate in the decision-making of the reviewing court and clarify the approach the SPC will take with respect to the law governing the arbitration agreement (which will not necessarily be the law governing the underlying contract).33

ARBITRATIONS INVOLVING STATES OR STATE-LINKED PARTIES

Oil and gas resources often take on a strategic, security or geopolitical significance for a state. The state is the resource-owner under the law for most countries in the region.-34 Producing states are thus key players in the oil and gas industry, and may take on a commercial interest in a particular oil and gas venture or contract, or exercise certain regulatory and control functions that affect a particular venture or contract. States can participate in a venture or contract in one or more of a variety of ways:

- they may participate through an oil and gas ministry or some type of government agency;
- they may participate through a national oil and gas company; or
- they may regulate through hydrocarbon laws, regulations or policies.35

Oil and gas arbitrations therefore frequently involve states or state-linked parties. These can include commercial arbitrations arising out of various contracts between private parties and states or state-linked parties, and also arbitrations under investment treaties.

COMMERCIAL ARBITRATIONS

States or their national oil companies are typically parties to upstream agreements granting private oil and gas companies the rights to certain oil and gas interests. These may take the form of a concession agreement, a licence agreement, a production sharing agreement or a service agreement. They may also take the form of a hybrid agreement that combines elements of the different types of granting agreements. In general, since the 1970s, the oil and gas industry has shifted from concession agreements, under which the state granted title over the resource to private companies, to production sharing agreements or service agreements, under which the state retains ownership over the resources but grants a private company the right to participate as an investor or a producer.36

Under a production sharing agreement, which is the most commonly encountered type of granting agreement, the investor takes on exploration and other risks in the venture, but has an entitlement to recover costs and share in the production as profit, once operations become commercial. Indonesia, in fact, introduced production sharing agreements in the 1960s.37 Production sharing agreements are now found across the Asia-Pacific region, including in Bangladesh, China, India, Malaysia, Myanmar, Philippines, Sri Lanka and Vietnam.38

Disputes that may arise under production sharing agreements include disputes regarding:

- the recovery of costs and accounting procedure under the agreement;
- the extent and nature of rights granted under the contract;
- non-payment of invoices or royalties;
- prices or price adjustments; and
- delays, disruptions or force majeure.

The nature and complexity of such disputes varies, and depend on factors such as the scale and complexity of the project, the parties involved and the political environment.

A large proportion of oil and gas arbitrations in the region have arisen out of production-sharing and other granting agreements – India has reportedly been involved in arbitrations relating to 22 out of its 310 production sharing agreements in the last 15 years.-39 Some arbitrations are illustrative of the range of issues that might be encountered. In November 2011, Reliance Industries filed a notice of arbitration against India regarding a dispute arising out of the cost recovery provisions its production sharing agreement over the KG-DG offshore gas block in the Bay of Bengal, which it operates in a joint venture with the Indian government, BP and Niko Resources, a Canadian company.40 Reliance Industries then filed another claim together with BP and Niko Resources in 2014 under the same agreement relating to the Indian government's delay in implementing a price hike for natural gas.41 This claim was later withdrawn.42 In November 2016, Reliance Industries began yet another arbitration under the same agreement after India imposed a US$1.55 billion fine on Reliance Industries and its partners for extracting certain gas that had migrated to the KG-D6 block from adjacent blocks owned by the Oil and Natural Gas Company (ONGC).43

Many oil and gas arbitrations in the region or involving parties from the region arise out of joint venture agreements as well. In June 2016, Sinopec, China's state-owned energy company, filed a US$5.5 billion claim against Repsol in Singapore over an investment in an ailing North Sea oil joint venture.44 In March 2017, PetroChina and five other Chinese state-owned oil companies submitted to arbitration under the AAA Rules a dispute over oil and gas fields in Chad against Carlton, a Texas energy investments company.45 This reflects a marked shift away from the reluctance that Chinese state-owned companies have sometimes had in the past to invoke formal dispute resolution procedures. In May 2017, MedocEnergi, an Indonesian oil company, won a US$24 million UNCITRAL award in a dispute with Singaporean and Australian partners arising out of a joint venture to operate the Jeruk oil field off the coast of East Java.46

INVESTMENT TREATY ARBITRATIONS

A significant number of oil and gas disputes in the Asia-Pacific region have also been submitted to arbitration under various investment treaties. Such treaties frequently provide for commitments by host states to certain standards of conduct with respect to the treatment of foreign investments, and for the states' consent that breaches of such standards may be submitted to arbitration. Countries in Asia are party to more than 1,200 bilateral investment treaties (BITs) or investment agreements, many of which provide for the arbitration of investment disputes.47

A number of multilateral treaties that cover the region, including the 2009 ASEAN Comprehensive Investment Agreement (ACIA) and the Trans-Pacific Partnership (TPP), also provide for arbitration. The status and effect of the TPP is unclear in light of the current US administration's withdrawal by executive order in January 2017; however, talks are reportedly under way between the other TPP signatories, China, and South Korea to revive the deal in a different form.48 Based on public statements by its foreign minister, China appears open to exploring the TPP, alongside other multilateral treaties that it is seeking to negotiate with trade partners in the Asia-Pacific, including the Regional Comprehensive Economic Partnership (RCEP) and the Free Trade Area of the Asia-Pacific (FTAAP).49

A substantial number of investment treaty arbitrations involving states in the Asia-Pacific region have related to oil and gas disputes. A large proportion of International Centre for Settlement of Investment Disputes (ICSID) arbitrations involving parties from the region have been related to the oil and gas sector. As of October 2016, out of the 46 ICSID cases involving a state from the South and East Asia and the Pacific, 45 per cent concerned the oil, gas and mining sector.50 A significant number of non-ICSID investment treaty arbitrations also relate to the oil and gas sector.

Given the complexity and variety of the security and political environments in which many oil and gas ventures operate, a wide range of different issues can give rise to investment treaty arbitration. For example, expropriation claims of various descriptions – whether framed as lawful or unlawful, direct or indirect – are not uncommon in the oil and gas sector. In 2016, a UNCITRAL tribunal dismissed two treaty claims brought by Progas Holdings, a Mauritian entity and its British-Iraqi shareholder against Pakistan for alleged expropriation of an LPG terminal in Port Qasim, Karachi.51 The awards are being challenged before the English court for an application to set aside filed by the investors.52

Retroactive taxation claims and other regulatory actions by governments also frequently give rise to investment treaty disputes. In March 2015, Cairn Energy, a Scottish oil company, initiated UNCITRAL arbitration against India under the UK-India bilateral investment treaty, alleging that India's demands for US$1.6 billion in retroactive taxes against its Indian subsidiary, as well as India's restrictions preventing Cairn from selling its remaining 10 per cent stake in its subsidiary, are in breach of the treaty.53 In May 2015, Hanocal Holding and IPIC International, Dutch subsidiaries of the International Petroleum Investment Company (IPIC), initiated ICSID arbitration for retroactive tax levied on the sale of a controlling stake in Hyundai Oilbank, which is a Korean petroleum and refining company.54 More recently, in July 2016, Royal Dutch Shell initiated ICSID arbitration against the Philippines for US$1.1 billion in retroactive tax bills levied by the Philippines auditing commission on the gas produced from the Philippines' first natural gas field in Malampaya.55 Samsung filed an ICSID claim against Oman, under the Oman-Korean bilateral investment treaty, in relation to a bidding process held by the state to find a contractor to undertake improvements to the Sohar refinery in northern Oman in 2015. The case has settled earlier in 2018.56

Investment treaty arbitration has also been subject to criticism in recent years, and the response of some states in the region has been to terminate or seek to renegotiate its bilateral investment treaties. As at March 2017, India notified 58 countries, including 22 EU countries, of its intention to terminate its BITs.[57] India has announced that it intends to replace those treaties by negotiating a new set of treaties based on the new Indian Model BIT, which it published in 2015.[58] It has been reported earlier this year that the new model treaty, in particular the arbitration clause requiring investors to resolve the dispute in Indian courts for at least five years before going for arbitration, has not been well received.[59]

Indonesia also announced at the end of 2014 that it would formally phase out its 67 BITs, and has proceeded to terminate a number of such treaties in accordance with that announcement.[60] There have been indications that Indonesia plans to negotiate new treaties on different terms, although reports are not conclusive. For treaties that have been terminated or are about to be terminated, investments made prior to the expiry of the treaties should continue to enjoy protection under 'survival' or 'sunset' clauses for up to 15 years.[61] Indeed, in August 2016, Oleovest, a Singapore-based subsidiary of an Australian renewable energy company, initiated ICSID arbitration against Indonesia under the Singapore-Indonesia bilateral investment treaty with respect to a palm oil oleochemical project in Sumatra. The treaty had lapsed in June 2016, but the relevant treaty contains a survival clause protecting existing investments for 10 years after June 2016.[62]

FUTURE DIRECTIONS

PRICE MOVEMENTS AND VOLATILITY

Price movements in oil and gas markets are a key driver of change in the industry. They are also a driver of disputes. Parties to energy-related contracts that were formed and negotiated in a different price environment may find themselves or their counterparts tied to agreements that are no longer as profitable as had been anticipated. Further exploration, appraisal or development of existing oil and gas assets may proceed on a slower and more conservative timescale. Parties may seek to get out of, or revise, a bad bargain. All of this can give rise to disputes – indeed, the recent low price environment has reportedly given rise to a number of disputes arising out of unpaid invoices or cost overruns, or the suspension, renegotiation or cancellation of oil exploration and drilling obligations.[63]

Price movements will continue to be volatile and difficult to predict. Future upward movements in oil and gas prices, or regional divergences in prices creating arbitrage opportunities, will very likely fuel an increase in disputes. Indeed, a study done by Chatham House shows a correlation between the oil and gas price level and the number of arbitrations – in other words, the highest incidence of arbitrations took place during the oil and commodity price boom from 2002–2008.[64]

Because gas is often sold in large volumes under 20-to-35-year long-term gas supply and purchase agreements, price movements and volatility often lead to very large and complex gas pricing disputes. In particular, many such contracts include a price review or price adjustment clause, which permits parties to revise the price formulae under their contract if a certain set of contractually defined criteria are satisfied.[65]

In Europe, various factors and developments have contributed to a proliferation of gas price arbitrations in the last decade involving disputes over the applicability and mechanics of such price review clauses. Commentators attribute this increase to the development of competitive natural gas markets and liquid gas hubs in some parts of Europe, leading to a mismatch between spot prices for gas and the prices paid under long-term gas supply contracts that predate those developments, which tend to be linked to oil and alternative fuels.66 Another driver of the increase in such disputes has been the oversupply of natural gas due to the development of shale gas in the US and China, and increased LNG imports from the Middle East and North Africa, which has led to a further divergence in the price-setting mechanisms in the oil and gas markets.67

Perhaps surprisingly, such gas price arbitrations have not been as common in the Asia-Pacific region – even though regional developments, including the dramatic spike in demand for LNG after the Fukushima nuclear power plant incident, have contributed to the increase in gas pricing disputes in Europe.68 One commentator's review of public LNG disputes found that, out of 72 LNG disputes observed globally since 2010, there have been no reports of arbitrations brought by a Japanese, Chinese or Korean LNG buyer (even though Japan, China and South Korea together account for more than half of global LNG imports).69

Recently, in February 2018, Korea Gas Corporation, a South Korean state-owned entity, brought a gas price review arbitration against the Australia's North West Shelf joint venture under supply contract that ended in 2016.70 It remains to be seen whether this is an isolated example or the first of a series of gas price review claims akin to the spate of such claims that has recently been seen in Europe.

Not much information is publicly available on the price revision mechanisms in gas or LNG supply and purchase agreements. However, commentators point to anecdotal evidence that long-term contracts in the Asia-Pacific region are traditionally set on the basis of Japan Customs-cleared Crude (JCC) prices and contain vague price review clauses that do not always provide for price revision through arbitration.71 There are also suggestions that Asian market participants prefer to negotiate rather than arbitrate price adjustment issues.72

However, more recent reports suggest that regional participants are now more seriously considering drafting or relying on gas price review mechanisms in their long-term contracts, in part because of a growing divergence between sellers' and buyers' positions. This will increasingly be the case as the JCC prices compete with the development of emerging gas trading markets in Singapore and Shanghai,73 which may develop in the future into gas hubs and a reference point for gas pricing. The European experience with liberalisation of gas markets and the emergence of gas hubs, and its impact on market behaviour and gas price reviews, suggests that gas price arbitrations will be a potential growth area for the future in the Asia-Pacific region.74

One important difference with Europe, however, is that the Asia-Pacific is not a single market, and does not have a coordinating political, legal or regulatory mechanism like the European Commission that can establish standards across-the-board for third-party access to infrastructure or to regulate anticompetitive contracting behaviour.75 This means that the development of a regional gas hub may take a longer time than it did in Europe.

OTHER LNG DISPUTES

The Asia-Pacific region has been referred to as the 'backbone' of the global LNG market,76 and it alone accounts for over two-thirds of the global LNG growth.77 In 2016, 53.6 per cent of global supply of LNG went to Asia,78 and as mentioned above, Japan, South Korea, and China are the world's top three LNG importers.79 As noted by one commentator, the 'largest global trade flow route continues to be Intra-Pacific trade, a trend which is poised to continue as that basin posted the largest gains in both supply and demand by region.'80 In the future, some commentators have predicted that, as result of increasing demand from Australia, India, Indonesia and Malaysia, the demand for LNG in the region is expected to be double or more by 2030.[81]

Besides the gas price review issues referred to above, there are other issues specific to LNG ventures and contracts that can give rise to disputes. In particular, unlike pipeline gas, LNG can be transported and delivered to destinations other than those specified in the parties' contract, and can also be re-exported after it is delivered. This creates opportunities for market participants to create additional value by sending LNG cargoes to a destination that has a higher price, which can give rise to disputes. For example, disputes have arisen out of destination restrictions or diversion provisions in LNG contracts, including whether a seller is entitled to refuse a diversion proposal, or whether and how profits on diverted cargoes are to be shared.[82]

As noted above, there is very little public information on LNG-related arbitrations involving parties from the Asia-Pacific region, and the anecdotal evidence suggests that parties have so far tended to avoid litigating or arbitrating disputes under such contracts. However, as LNG markets continue to mature in the Asia-Pacific, and with trading volumes continue to increase, it is likely that more of such disputes will arise in the future.

Another area to watch is LNG-related construction disputes. Australia currently has almost A$200 billion of LNG-related construction projects underway, which is part of a plan for Australia to overtake Qatar as the world's biggest LNG exporter by 2018.[83] However, the rush to build up Australia's LNG industry has also led to cost overruns of almost US$50 billion at multiple facilities operated by major oil and gas companies.[84] Along with other factors, this has predictably led to a number of LNG-related construction disputes being submitted to arbitration. For example, in September 2016, Chevron initiated UNCITRAL arbitration in Perth against CPB Contractors, an Australian construction company, and Saipem, its Italian counterpart, regarding a disputed request for US$1.5 billion in extra costs for constructing a jetty for the LNG project.[85]

STATE-TO-STATE ARBITRATION DISPUTES

As energy and resource security becomes an increasing concern for states in the Asia-Pacific region – which is likely given volatile energy prices and the reliance of China, Japan and South Korea on oil and gas imports[86] – there may also be more state-to-state arbitrations that are related to the oil and gas sector.

State-to-state disputes can arise out of oil and gas resources that straddle contested state boundaries. For example, in 2009 the Permanent Court of Arbitration (PCA) in The Hague administered an UNCITRAL arbitration between the Sudan People's Liberation Movement/Army and the government of Sudan regarding the contested borders of the Abyei region, which is located within the Muglad Basin and contains a number of oil and gas subsurface resources.[87] Similar disputes have arisen regarding land boundaries in the Asia-Pacific, most notably in the Kashmir region where Pakistan, India and China have all put forward competing claims,[88] although such claims have not been submitted to arbitration.

Similar disputes can also arise out of oil and gas resources that straddle maritime boundaries or exclusive economic zones. In July 2016, a five-member PCA tribunal constituted under the 1982 UN Convention on the Law of the Sea (UNCLOS) rejected territorial claims by China in the South China Sea, with respect to the status of the Scarborough Shoal, Itu Aba and certain features in the Spratly Islands.[89] China has however consistently rejected the legitimacy of the PCA award, on the basis that territorial questions are not subject to UNCLOS,[90] and rather than comply with the award, China has instead stepped up its construction activities and presence in the South China sea.[91] This goes to show how delicate and politically sensitive these boundary issues can be – and illustrates some of the limitations of the arbitration process in resolving such disputes.

Disputes could also arise out of agreements to share revenue between States. One example is the dispute between Australia and Timor Leste regarding a controversial Certain Maritime Arrangements in the Timor Sea (CMATS) treaty that sets out a method for dividing revenue from the very large and potentially lucrative Greater Sunrise oil and gas reserve.[92] CMATS split revenues on a 50-50 basis and imposed a 50-year moratorium on Timor Leste pursuing maritime boundary negotiations or claims. Timor Leste sought to terminate the CMATS.[93]

In September 2016, a five-member commission at the PCA found that it had jurisdiction to hear a compulsory conciliation proceeding under UNCLOS Annex V involving Australia and Timor Leste, which would require Australia to negotiate with Timor Leste regarding a permanent maritime boundary (Australia had expressly excluded disputes relating to sea boundary delimitation from compulsory arbitration and judicial settlement in 2002).[94]

After negotiations, Timor Leste and Australia reached an agreement on 30 August 2017 in Copenhagen on the 'central elements' of a permanent maritime boundary in the Timor Sea – ending a maritime boundary dispute affecting the fate of an estimated US$40 billion in oil and gas reserves. The agreement also addresses the legal status of the Greater Sunrise gas field located in the disputed waters and the establishment of a 'special regime' for the development of the field and the sharing of revenues.[95] The treaty was signed on 6 March 2018.[96]

The UNCLOS Annex 5 conciliation proceedings were the first of their kind. It remains to be seen how such procedures will be employed in future state-to-state disputes.

Endnotes

WILMERHALE

WILMER CUTLER PICKERING HALE AND DORR LLP ®

Duncan Speller duncan.speller@wilmerhale.com
Jonathan Lim jonathan.lim@rpc.com.sg
Justin Li justin.li@wilmerhale.com

7 World Trade Center, 250 Greenwich Street, New York, New York 10007, United States

https://www.wilmerhale.com/