



**JOINT DEVELOPMENT IN THE WEST PHILIPPINE SEA:
AN IDEA WHOSE TIME HAS COME**

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A proposed joint development (JD) in the West Philippine Sea (WPS) between the Philippines and China has revived debates on how best to move forward in the longstanding regional flashpoint. There should be no debate – the Philippines should enter into the JD, even if the partner is a state-owned entity, as long as it can deliver. Most importantly, JD does not necessarily impact adversely the 2016 arbitral ruling and the Philippine sovereignty and sovereign rights position on the WPS. The Philippine service contract (SC) system may offer a solution for both countries and can accommodate a JD. This approach to JD can enhance the country's energy security, create jobs, promote technology and knowledge transfer, and contribute in dispute management.

According to Philippine law, the government may directly undertake exploration and development of indigenous petroleum resources or indirectly by awarding SCs to technically competent and financially capable entities, local or foreign. Service contractors, in return, can partake of the revenue sharing to collect their service fees and operating expenses.

Pragmatism as regional norm

Southeast Asian countries are inclined to take a pragmatic approach on contested resource-rich areas. In fact, the Philippines is the only Southeast Asian country that has yet to enter into a JD with a neighbor over a disputed maritime area. Malaysia and Thailand (1979 MoU; 1990 JD Agreement), Malaysia and Vietnam (1992), Thailand and Vietnam (1997), Indonesia-Malaysia-Vietnam (2000), Vietnam and China (2000), Cambodia and Vietnam (2001), and Brunei and Malaysia (2009) have all entered into various forms of JD. It is no coincidence that Malaysia and Vietnam, the most active in JDs, are among the region's largest energy producers. State-owned energy firms (e.g., Malaysia's Petronas, Petrovietnam, Indonesia's Pertamina, Thailand's PTT) are at the forefront of these deals. Even tiny Timor Leste had a JD with Australia (2003), a case of a small and big neighbor setting aside dispute for a pragmatic resource cooperation.

The 1982 UNCLOS noted the dilemma of countries in need of harnessing resources in disputed maritime areas without diminishing their claims. Provisional arrangements in the exclusive economic zone (Part V Art 74 para 3) and continental shelf (Part VI Art 83 para 3) are enshrined in the constitution of the oceans and there is considerable jurisprudence and global state practice on it. Maritime delimitation need not even precede or its absence need not constitute an effective impediment as proven by some of the above-cited JDs.

Recognizing attendant political and legal risks, most JD agreements use standard clauses saying that such interim practical undertakings will not

jeopardize or affect the claims or positions of contracting parties. Even the controversial 2005 Tripartite Joint Marine Seismic Undertaking (JMSU) between the Philippines, Vietnam and China carried a similar clause: “WHEREAS, the Parties recognize that the signing of this Agreement shall not undermine the basic position held by the Government of each Party on the South China Sea issue.”

Constitutional openings

Political will is a key element of JD and President Duterte seems determined to turn the concept into reality. The Philippine Constitution (Art XII Sec 2) allows the president to enter into agreements with foreign companies for the exploration, development and utilization of minerals and petroleum, providing cover for JD. The exclusive use and enjoyment of marine wealth applies to all maritime zones, but curiously omitted is any mention of the continental/insular shelf, where seabed minerals, like oil and gas, are extracted. Perhaps the framers of the 1987 Constitution wanted to allow for the JD option given that provisional arrangements were encouraged by the 1982 UNCLOS.

Furthermore, the Constitution and Philippine petroleum law (PD 87) have no expressed prohibition on partnering with a state-owned firm. China’s key strategic sectors, such as energy, power, transportation, telecommunications and banking, are in the hands of the state so it is only likely that it will nominate a state-owned firm to work with its Philippine counterpart (e.g., state-owned PNOOC) to implement a JD if both sides agreed to it.

The 60/40 ownership ratio (in favor of the Philippines) stipulated in the Constitution is not an obstacle. The ratio does not apply to the SC stake/interest per se, but rather to the net proceeds arising from production sharing – at least that is how the Department of Energy has interpreted it. As such, SC57 has the following ownership stake breakdown: 51 percent CNOOC, PNOOC 28 percent and Mitra (Malaysian firm), 21 percent. SC38 in Malampaya, the country’s largest operating natural gas field, has a more lopsided breakdown in favor of foreign entities – 45 percent owned by Shell, 45

percent by Chevron and only 10 percent by PNOOC. This works well for joint developments, which are more concerned with cost and benefit sharing between contracting parties than ownership.

Search for a face-saving formula

Like any sovereign state, Philippines awarded offshore SCs in WPS without taking into account others’ claims, but the persistence of disputes affected the attractiveness of these SCs. The difference between a SC and JD seem clear from the Philippine standpoint, but the Chinese may prefer ambiguity for good reason. China can take part in a Philippine service contract (under Philippine law) and promote it domestically (in China) as JD (to save face at home), a point I made in an [earlier piece](#).

China has shown interest in being a Philippine service contractor – not even technically a JD partner. In 2006, CNOOC bought a 51 percent stake in SC57 (Calamian), but this was not acted upon. And, in 2013, CNOOC and the Philippine private energy firm Philex discussed partnership for SC72 (in Recto Bank), which is within China’s nine-dash line claim. These were reported as commercial deals and there was no substantial mention of JD. These examples are lost opportunities for both sides, especially Manila. It could have engaged China (via CNOOC) to explore and develop oil and gas in WPS under domestic law. It is likely China might want to package participation in a Philippine-based SC as JD for domestic public consumption.

Moving forward

Improving bilateral relations and confidence-building measures since 2016 are creating favorable conditions for the resumption of upstream activities in the area. JD will send a good signal to industry and make the Philippines attractive again to big players, including regional SOEs. JD is a political as much as commercial undertaking and government saw it as a realistic, feasible, and promising way forward in the WPS. Duterte can use his high public approval as a mandate to proceed. CNOOC has long expressed its interest in working with Philippine and/or other foreign partners. Manila should be open to all willing and capable

partners, regardless where they come from, and this seems to be the position of the current administration.

The present Philippine government has several cards to play. Duterte enjoys tremendous goodwill from China. JD is more important for Manila from an energy standpoint given increasing energy requirements and aging fields, while it is more important for Beijing to score political (at home) and diplomatic (peripheral diplomacy) points. Beijing may take a softer line and agree to be a contractor for SCs 57 or even 58 (further west), but may take a firmer stance for a JD in SC72. Proximity and existing infrastructure also work in Manila's favor. Palawan and Luzon are the nearest landmasses to WPS and there is a downstream infrastructure in Batangas and Bataan provinces (in Luzon) that can be bolstered to serve a burgeoning market. Lastly, the administration may have decided not to assert the 2016 arbitral ruling now, but that does not mean it cannot leverage it.

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