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International Law Briefing

Legal Implications for the Offshore Oil Industry of an Independent Scotland

On 16 January 2013, the UK Parliament adopted an Order in Council under Section 30 of the Scotland Act 1998 enabling the Scottish Parliament to legislate for a referendum on independence for Scotland to be held before the end of 2014. Such a referendum is foreseen in the agreement (the "[Edinburgh Agreement](#)") signed by UK PM David Cameron and Scottish First Minister Alex Salmond on 15 October 2012. Among the many issues to be addressed in the period leading up to the 2014 referendum, the legal implications for the UK oil and gas industry of an independent Scotland can be expected to take centre stage and no doubt will be given careful consideration by those involved and affected.

Benefits as well as Liabilities

Given that the prospect of an independent Scotland raises a whole range of complex and unprecedented legal issues, both domestically and internationally, affected industries need to factor into their future legal risk assessment the uncertainty and unpredictability resulting from this situation. While it is hoped that an independent Scotland would bring benefits not offered by the present state of affairs, it inevitably would also give rise to liabilities on the part of the Scottish Government under different legal regimes.

Domestic Legal Implications of an Independent Scotland

Filling the Legal Vacuum

It is assumed that if the result of the proposed referendum was in favour of independence, this would lead to the negotiation of an independence statute to achieve the result desired by majority of the Scottish people. In order to avoid a legal vacuum, in previous cases where former parts of the British Empire have been granted independence, the independence statute has provided that (with specific exceptions) all existing Westminster legislation which was applicable in the relevant territory immediately before independence continued in force immediately after independence unless and until repealed by the legislature of the newly independent state. It would therefore seem likely that all UK legislation currently applicable in Scotland would continue to be so unless and until repealed or amended by the new Scottish Parliament.

However, the arguments, currently largely academic, as to whether oil and gas licences are administrative or contractual in nature would come to the fore as, if

International Law Briefing

interpreted as contracts, any licences would need to be transferred in some manner from the UK Government to the Scottish Government and therefore the detailed terms of the independence statute would doubtless be subject to close scrutiny by the industry. Particular issues would arise in relation to the transfer of rights and obligations in relation to those licences (and in particular, producing fields) which straddled any putative delimitation line between the remaining parts of the UK and a new Scottish state (discussed further below).

Impact of Changes in Policy

In theory, therefore, the Petroleum Act 1998, currently administered by the Department of Energy and Climate Change (DECC), and licences issued under it, would continue to apply following independence unless and until the Scottish Government chose to alter it. It is unlikely that a new Scottish administration would wish to unsettle the industry by making any precipitate changes to the licensing and regulation of the oil and gas industry. It would be interesting, however, to see whether, given statements from SNP Ministers about the significance of the oil and gas industry to the Scottish economy and the potential benefits of increased oil and gas production to that economy, a new Scottish Government placed any increased obligations on oil and gas operators whether pursuant to changes to the Model Clauses incorporated into oil and gas licences or through the tax system. Any uncertainty as to the future policy of the Scottish administration in relation to oil and gas regulation and taxation would be certain to have a significant chilling effect on investment in the UK Continental Shelf and could potentially trigger early decommissioning of assets.

Decommissioning Tax Relief

Critical in this respect would be clarity as to the intention of any future Scottish Government with respect to the payment of tax relief in relation to the decommissioning of oil and gas infrastructure. The industry has devoted an enormous amount of time and energy over the past two years to the negotiation with the UK Treasury of a new mechanism to ensure certainty as to decommissioning tax relief through the use of decommissioning relief deeds (DRDs) which is due to be implemented through the Finance Bill 2013 – an effort matched only by the commitment of the Treasury to the process (see past Law-Nows). The aim of this has been to allow security for the costs of decommissioning to be given net of the significant tax relief due from the UK Government. However, many of the larger and more expensive installations to be decommissioned in future years are in northerly waters which can be expected to come under Scottish jurisdiction following independence. If there were to be any suggestion that the Scottish Government would not grant tax relief against the costs of decommissioning those assets and/or would fail to honour the guarantees given by the UK Government as to the amount of that relief pursuant to the proposed DRDs, then this could have serious implications

International Law Briefing

in terms of a return to pre-tax security (which in turn could trigger defaults under security agreements) and possibly premature decommissioning.

Replacing DECC

One of the urgent tasks of an incoming administration would be to replicate the administrative organisations of the United Kingdom, including its own equivalent of DECC, the Health and Safety Executive (HSE) and other institutions. The staff at DECC dealing with oil and gas matters are, even on the basis of current responsibilities, often overstretched and it is unlikely that the department could be divided into two organisations capable of exercising the same functions in separate jurisdictions without significant additional recruitment. This is a challenge for DECC even now given that it is competing for staff with a very high paying industry. Therefore, even if there is no immediate change in the legal regime governing oil and gas exploration and development, there is the potential for a significant chilling effect resulting from the inability of the new administration to find the staff to address matters such as licence applications, transfers, drilling consents, safety cases and the like.

International Law Implications of an Independent Scotland

The prospect of Scottish independence also raises a wide variety of international law issues, ranging from the membership of international institutions to succession of treaties and from succession of state property and debts to boundaries.

Treaty Succession: Scotland is South Sudan

The international law regarding state succession is unsettled, making it difficult to identify any hard-and-fast rules that can be applied in a reasonably predictable manner to the Anglo-Scottish case. The international community can be expected to treat the remainder of the UK as succeeding to the treaty rights and obligations of the UK, including the constituent treaties of international organisations of which the UK is a member. The question of Scottish membership of such organisations is primarily governed by the rules concerning acquisition of membership and any other relevant rules of the organisation concerned. As regards European Union membership, Scottish secession from the UK, an EU member state, would trigger an unprecedented situation, one which is not expressly foreseen within the EU legal framework.

As a result, the procedure for Scottish accession to the EU could be cumbersome. Based on precedent, the rest of the UK can be expected to remain a member of the United Nations and its 16 Specialised Agencies—including the International Financial Institutions—, with an independent Scotland having to apply for membership in such bodies, similar to the situation which South Sudan faced after it

International Law Briefing

seceded from the Republic of the Sudan following an independence referendum in January 2011.

Scottish independence would affect the status of the nearly 14,000 treaties, multilateral and bilateral, currently in force for the UK, including Scotland. In accordance with the rule of non-transmissibility, and similar to South Sudan, an independent Scotland would not automatically be a party to such treaties, except if they define boundaries or contain rules which are generally accepted as declaratory of general international law (such rules would continue to bind a new Scottish state). As regards offshore oil and gas production, the rule of non-transmissibility raises particular issues under the UN Convention on the Law of the Sea and the OSPAR Convention, which address liabilities arising from decommissioning of offshore installations and the maintenance of pipelines and cables.

Given that it is not clear what citizenship rules might apply in an independent Scotland, investors in the offshore oil industry might no longer be covered by the nearly 100 bilateral investment treaties which the UK has concluded with other countries and which provide for reciprocal protection through substantive and procedural guaranties. The same applies to multilateral treaties such as the Energy Charter Treaty and conventions governing the recognition and enforcement of international arbitral awards.

Succession to State Property and Debts

It is to be expected that an independent Scotland and the remainder of the UK would negotiate some kind of succession agreement addressing transitional and other matters arising from Scottish independence, including, following the precedent of Irish independence, an equitable apportionment of the UK's national debt. It is uncertain how long such negotiations would take.

While a new Scottish state would be free to regulate economic activity within its territory, governmental interference with existing property rights, including concessionary rights, could trigger Scotland's responsibility under international law. Future claims by what currently are UK parties might turn into international claims against an independent Scotland if such parties are not considered Scottish parties, and hence would be subject to different standards of scrutiny and compensation than is currently the case.

Where to Draw the Boundaries?

An independent Scotland would need to agree its boundaries with the rest of the UK in accordance with international law. Any boundary treaties in force for the UK would bind an independent Scotland. An independent Scottish Government and Westminster can be expected to advance overlapping maritime claims affecting licensed areas in the North Sea, while the western boundary would present its own complexities. If the Orkney Islands or the Shetland Islands did not join an

International Law Briefing

independent Scotland, the resulting situation would greatly complicate the maritime boundary delimitation process.

Assuming an independent Scotland and Westminster would consent to having the International Court of Justice decide the course of their disputed boundary, ICJ boundary cases have taken at least three, and sometimes more than 10, years to conclude—resulting in uncertainty in the intervening period. In drawing the Anglo-Scottish maritime boundary based on international law, a competent court or tribunal is likely to apply the equidistance method, which if strictly applied would result in a line that cuts through licensed areas and appears to favour Westminster in the North Sea given the geographical configuration of the relevant coast and area to be delimited. While Edinburgh and Westminster could, alternatively, agree to create a joint development zone or international unitisation in the North Sea, as the UK and Norway have done, it is not certain that an arrangement which is workable and sufficient to convince existing investors not to abandon their blocks is feasible in the Anglo-Scottish case.

About the Authors

The authors do not take a position for or against possible Scottish independence. This note merely highlights some of the legal implications of an independent Scotland which the offshore oil and gas industry and those planning for independence might wish to consider.

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International Law Briefing

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