SEMAPHORE

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Offshore Pollution – NZ Law Change Removes Protection of Compensation for Victims of Oil Pollution

In 2020, New Zealand made changes to its laws around financial security and compensation for pollution events from offshore installations. The New Zealand Branch of MLAANZ made a submission on the Maritime Transport (Offshore Installations) Amendment Bill. The amended legislation came into effect on January 20, 2020, with related changes to the Marine Protection Rules (MPR) that set out the criteria for the issue of a certificate of insurance taking effect on May 27, 2020. MLAANZ New Zealand Branch secretary and McElroys associate Stacey Fraser provides the following comment on the recent law changes. The views expressed here are the author's own.

Introduction

Writing on the topic of compensation for offshore pollution, Professor Nick Gaskell has said "it is a feature of human affairs that the focus tends to become more concentrated after a disaster rather than before it". It is a disappointing feature of New Zealand's recent law changes that despite coming almost ten years after New Zealand's own experience with the disaster of Rena, and international offshore pollution incidents such as Deepwater Horizon and Montara, the amendments failed to draw on international experience and create an offshore financial security compensation regime that is fit for purpose. The effect of the amendments is difficult to reconcile with their stated purpose being "to clarify and strengthen the requirements on owners of offshore oil and gas installations to hold insurance or other financial security in relation to their liability for clean up and compensation resulting from an oil spill". Instead, the changes to the Maritime Transport Act 1994 (MTA) and Part 102 of the MPR remove existing protections for some victims of pollution damage, increase the risk that insurance will not respond to an event, and make it more likely that litigation will be required to access compensation – defeating the very objective of the statutory regime.

Context

Oil pollution captures the public's attention. Images of oil slicks stretching across swathes of ocean, thick black oil suffocating seabirds, and washing up on the sand where bands of people are decked out in white overalls and gumboots are familiar to us all. As public awareness of social and environmental impacts has grown, so have expectations around accountability for those responsible for pollution and compensation to those who have been affected by it.

The international community has been dealing with oil pollution events since the Torrey Canyon in 1967, the first significant oil spill event from an oil cargo carrying ship. Initially, the costs to public authorities in cleaning up the oil spill were of primary concern. Over time, the impact on private interests has taken priority. This is most clearly reflected in the development of the international practice where States "stand last in queue", allowing private claimants to recover compensation before public authorities. After defining what pollution damage meant and making clear that it includes economic losses from impairment of the environment, the maritime sector has evolved to deal with the legal and practical challenges that followed. Essential to these is making liability strict, with limited exceptions, requiring shipowners to ensure they have the financial ability to pay compensation for their liabilities (evidenced by insurance or financial security) and the establishment of a fund with an amount that is available exclusively for oil pollution claims. It includes making publicly available information and guidance on admissible claims and detail on how to make a claim, with specific guidelines available for

fisheries, tourism, clean up, and environmental damage. In the event of an oil pollution event from an oil tanker, the International Oil Pollution Compensation (IOPC) Fund and insurer will appoint experts to monitor clean up operations, investigate the technical merits of claims and to make independent assessments of the losses. A claims office will be established to receive claims and there is a process to decide claims, with most claims settled without recourse to litigation.

In contrast, there are no equivalent measures in place for the offshore sector. Although there have been attempts to establish an international regime for civil liability and compensation for pollution from offshore operations, those have not eventuated. The significant difference being that while shipping requires international uniformity because of its very nature, and the limited jurisdiction of states beyond their territorial seas, states have sovereign rights and jurisdiction over offshore activities in their exclusive economic zone (EEZ) and continental shelf. There is not the same impetus for a uniform international regime, and given the absence of unified political will, one seems unlikely – though attempts continue to be made to progress this, including by the Comité Maritime International (CMI).

Wreck of the Rena

Whether to legislate specifically for offshore pollution events is a matter of domestic policy. Many states have established specific offshore domestic liability and compensation regimes, including the requirement in the United Kingdom for offshore operators to belong to the Offshore Pollution Liability Association (OPOL) – an industry regime – the Oil Pollution Act (OPA) 1990 requirements in the United States; and legislative regimes in Norway and Canada to name but a few.

New Zealand Legislation

In New Zealand, prior to recent amendments, the civil liability and compensation regimes for oil pollution damage were largely the same for ships and offshore installations. This was a deliberate policy decision by New Zealand Parliament when enacting the Maritime Transport Act in 1994 to align the requirements for the offshore sector with the existing regime for ships under earlier legislation. What is now Part 26A Maritime Transport Act 1994 (MTA), was originally enacted in the same Part 25 MTA that implements the Civil Liability Convention (CLC), setting out liability for ships carrying oil as cargo (tankers) that most members will be familiar with. The objective of those regimes is to provide prompt adequate and effective compensation for victims of oil pollution avoiding the need for litigation. All claimants are treated equally.

This meant that the civil liability and compensation regimes for oil tankers and offshore installations under New Zealand law had:

- the same strict liability for clean up cost and pollution damage as defined in the legislation;
- the same definition of pollution damage, being damage or loss of any kind and –

  (a) includes the costs of any reasonable preventive measures taken to prevent or reduce pollution damage and any damage or loss occurring as a result of those measures; and

  (b) includes the costs of reasonable measures of reinstatement of the environment that are undertaken or to be undertaken; and

  (c) includes losses of profit from impairment of the environment; but does not include any costs in relation to the impairment of the environment other than the costs referred to in paragraphs (b) and (c).

- the same requirement to have financial security for all pollution liabilities, evidenced by the issue of a certificate of insurance.
- the same direct right of action provisions against insurers for persons who had a claim for pollution damage under the MTA, with limited defences available.

There were some differences. While shipowners are entitled to limit liability in accordance with the conventions, the New Zealand policy is not to entitle offshore operators to limit liability, and therefore they will be liable for the full costs of any pollution damage. Unlimited liability is uninsurable, so as for ships a minimum amount of financial security is specified. The minimum levels of financial security required for the issue of a certificate of insurance are different, with the level of financial security for ships being set by the relevant international convention, and for the offshore sector, a domestic policy decision. The previous level of minimum financial security required for the offshore sector at SDR14 million was woefully low, being based on the original levels for shipowners under the 1969 CLC. However, unlike the CLC/fund regime, there will only be a single tier of compensation from the operator. Practically, the minimum requirement for insurance or financial security reflects a de facto limit of liability for the offshore sector.

Existing Problems

The fact New Zealand had a statutory regime from 1994 is progressive and something to be proud of. However, the New Zealand legislative regime for civil liability and compensation of offshore operators

Wreck of the Rena

in an offshore pollution incident has long been in need of improvement. While (what is now) Part 26A MTA and MPR 102 had set up a broad framework of an appropriate civil liability and compensation regime for offshore oil pollution incidents, there were weaknesses and gaps that needed to be improved to ensure effective compensation is available in a relatively prompt and efficient manner.

The low levels of financial security were desperately in need of attention. In addition, the offshore regime lacks the same supporting mechanisms to facilitate access to compensation. There is no guidance or process for making and deciding claims and no provision for the creation of fund, against which claims can be made, and are available exclusively for victims of pollution damage.

The offshore sector and their insurers do not have the systems, industry experience or international support in claims management as the maritime industry and the legislation has not filled this gap. The practical effect is a regime that lacks the operational systems needed to implement the objective of prompt and adequate compensation without the need for litigation. The lack of any plan or system for dealing with claims will lead to uncertainly and inconsistency in approach, delays, and ultimately significant public and political pressure on both the offshore operators and the Government to resolve compensation issues while dealing with the incident itself.

Overview of Legislative Amendments

One of the stated objectives of the proposed amendments to the MTA was to provide certainty in relation to the liability of insurers (or, in the case of financial security, the persons providing the financial security) to the Crown and to other third parties who are affected by the pollution. Although the requirements to obtain a certificate of insurance are set by the MPR, including the minimum amount of financial security, the direct right of action provisions sit under the MTA. The primary legislation did not provide any protection to those providing the financial security that their liability would be limited to the amount of financial security they had agreed to provide.

However the Bill also made less-widely-signalled changes to the direct right of action provisions, opened the door to self insurance, and amended the power of the Minister of Transport to set the criteria for the issue of a certificate of insurance, under MPR Part 102. The related changes to the scope and kind of security under MPR 102 fundamentally changed the existing framework, moving away from the internationally-recognised elements of effective compensation regimes.

The policy work on these changes started from the position that "in general the regime is working well". This is despite New Zealand not having undertaken any review of how the offshore compensation regime would practically operate to provide compensation to victims of oil pollution either by comparison to its own experience with Rena or lessons learned from international events such as Deepwater Horizon.

MLAANZ Submission

MLAANZ supported the general policy objective of providing certainty to insurers on the limit of their liability where they are subject to direct claims for pollution damage under the MTA. MLAANZ also recommended an amendment to the equivalent provision for insurers of oil tankers under Part 25 (Section 366 MTA), noting the current legislation did not properly implement the CLC 1992 and the protection afforded to insurers, as dealt with in an earlier edition of *Semaphore*.

The oral presentation to the Select Committee addressed the reasons why the New Zealand Branch of MLAANZ considered that the draft provision in the Bill did not achieve the stated policy objectives. MLAANZ considered that, instead of revoking and replacing the provisions that dealt with direct action as proposed (s385J), the policy objective should be achieved by appropriate amendment to the existing s385J – so that section and s366, which has the same general purpose in the context of claims against insurers of ships, continue to align.

Copies of the MLAANZ submission, the Bill and all submissions can be accessed via

- https://www.parliament.nz/en/pb/bills-and-laws/bills-proposed-laws/document/BILL_89360/maritime-transport-offshore-installations-amendment-bill

One Step Forward, Three Steps Back

The changes include a long-overdue increase in the minimum amount of financial security required for statutory pollution liabilities for an offshore pollution event. The minimum level of financial security for each offshore installation will now be determined using a scaled framework, with a point system, ranging in requirements from NZD$25 million up to a maximum of NZD$1.2 billion. But at a cost.

Together, the changes to the MTA and Part 102 of the MPR remove existing protections for some victims of pollution damage, increase the risk that insurance will not respond to an event, and make it more likely that litigation will be required to access compensation, as summarised briefly below.

Offshore Operators are no Longer Required to Provide Financial Security for the Full Scope of Statutory Oil Pollution Liabilities

Offshore operators are no longer required to provide financial security for the full scope of the statutory oil pollution liabilities. While the definition of pollution damage and strict liability remains, the amendments to MPR Part 102 remove the requirement to provide financial security for all statutory liabilities. Operators now only need to provide financial security to cover clean up costs and property damage. In particular, offshore operators are no longer required to provide financial security to cover statutory liabilities for claims relating to loss of profit from impairment of the environment (primarily affecting fisheries, agriculture and tourism business that will suffer economic loss from pollution damage) or the costs of reasonable measures of reinstatement of the environment.

The removal of these protections is all the more surprising given that when introducing the Bill to Parliament, the Associate Minister for Transport highlighted "the environmental, financial, and

cultural impacts of an incident, and the importance of protecting our environment" and safeguarding New Zealand's "natural capital of tourism and agriculture".

Environmental, tourism and agricultural interests have had their existing protections stripped away, not strengthened. These are the most vulnerable claimants. The changes mean there is now unequal treatment of claimants with the New Zealand regime creating two classes of victims of oil pollution damage. Those who have some protection of financial security and potential access to compensation and those who do not. Those who do not, including tourism operators and local fisheries, are unlikely to be able to recover their losses. Only the Crown and those who suffer property damage are protected by the financial security, but even those claimants face new challenges to accessing compensation.

The shift is entirely out of step with international developments that seek to improve environmental protections rather than remove them.

The belated justification for excluding such liabilities was the "unlimited liability" of the operator and the ability of those who suffer damage to still bring a claim against them. This ignores the fact that liability is meaningless if there is no ability to pay. The very purpose of a financial security regime is to address this risk and provide some protection of compensation for those affected by oil pollution without recourse to the courts.

The underlying policy documents and Cabinet papers make clear that the purpose of the changes was to meet the preference of the regulated industry to use an existing commercial insurance product (Energy Exploration and Development insurance, known as EED 8/86), primarily designed to provide cover for an out-of-control well, as the instrument to obtain a certificate of insurance for pollution liabilities. As EED does not cover all statutory liability, the regulatory requirements on offshore operators were reduced to match the commercial product.

Despite a wide range of financial instruments potentially available as financial security, no consideration was given to given to mutual assurance or pooling arrangements generally, or separately as an alternative to deal with claims for loss of profit or remediation of the environment.

Deep Water Horizon

Do Not Respond to Strict Liability

With respect to those statutory liabilities that are covered, it seems operators will not be required to have insurance or financial security that responds to the strict liability nature of statutory pollution liabilities.

The new legislation indicates that any policy that provides equivalent cover to EED is acceptable. Contrary to statements in the policy documents, EED is not accepted on standard terms for third-party pollution liabilities in the United Kingdom or the United States. Both require any EED insurance to have an additional endorsement to specifically cover the strict liabilities imposed by OPOL and OPA 1990, respectively.

The consequence is that, even where financial security is required, there is an increased risk that insurance may not respond to the pollution event.

More Defences

The new provisions for rights of actions against insurers reverse the previous provision that limited the defences an insurer can rely upon. Instead, the provisions now expressly provide that the insurer or person providing financial security is entitled to rely on any defence or any other matter in answer to the claim or in reduction of its liability to the claimant save for "any defence arising from an act or omission by the owner that occurred after the event that gave rise to the liability (for example, a defence based on a failure by the owner to comply with a condition that the owner provide information or assistance to the insurer)".

In addition, there is now a new requirement to have leave of the court to bring a claim against an insurer.

The change to the direct right of action provision was not discussed in consultation documents and was based on general Australian legislation unrelated to pollution regimes. The MLAANZ submission noted that the approach taken to direct action claims against insurers of ships and offshore installations should be consistent where pollution damage claims have the same statutory basis and there was no principled basis on which to import the general provisions from New South Wales law into a specific statutory regime.

The changes made, defeat rather than serve the objective of prompt and effective compensation for victims of oil pollution. They increase the likelihood of litigation and the risk that insurance cover may not be available at all.

Lack of Certainty for Insurer

Ironically, the changes do not achieve the intended certainty for insurers as to their limit of liability as intended. No limit is specified. Instead, the liability of the insurer or person providing financial security is by reference to the "indemnity" which is not defined. The indemnity is not the same as the minimum amount required to be provided under the marine protection rules. In a case where the EED policy is used, the policy will likely cover both the operator's own costs of dealing with an out-of-control well (under another statutory provision) as well as any potential pollution liabilities to third parties. The policy responds to out-of-control well cost first.

The regulator will need to make a "best guess" as to the estimated costs of well control and ensure that the amount of cover under the policy can respond to both potential first-party costs and third-party liabilities. But the cover under the policy for statutory pollution liabilities is not ring fenced. Whether the amount actually available is more or less than the minimum amount of security required under the rules will be entirely dependent on the costs associated with the control of the well and any redrilling and extra expense, which will be paid first.

Conclusion

Despite the stated purpose of the Bill "to clarify and strengthen the requirements on owners of offshore oil and gas installations to hold insurance or other financial security in relation to their liability for clean up and compensation resulting from an oil spill", on any basic analysis the proposed amendments do neither.

To "clarify" suggests making clear something that already exists but is ambiguous in its effect, when instead, the Act makes fundamental changes to the operation of the statutory framework. To "strengthen", suggests making improvements in a manner consistent with the existing scheme and purpose of the primary legislation. Here, the changes remove existing environmental protections and do not improve them.

The changes that have been made reflect the lack of a clear policy objective or understanding of pollution incidents and the principles and practice of compensation regimes. They fail to address existing gaps and significantly weaken the scope of protections for those who suffer loss or damage as the result of a pollution event.

In the heightened emotion of an actual offshore event, where the visual images of oil pollution are on display and livelihoods are at stake, what is theoretical now will matter. The effect of a major offshore oil pollution event will dwarf New Zealand's experience with Rena in scale, time and consequence. Instead of a fit-for-purpose regime designed to assist victims of oil pollution, there will be significant delays, cost and complexity associated with compensation claims, while simultaneously reducing the likelihood of effective recovery for all of those affected.

Both the offshore industry and Government can expect vocal public criticism and pressure for the failure to adequately plan and prepare for such an incident when there has been ample time to do so.

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