

Chair
Cabinet Economic Growth & Infrastructure Committee

APPROVAL TO ACCEDE: SUPPLEMENTARY FUND PROTOCOL

Proposal

1. This paper seeks agreement to accede to the Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992 (Supplementary Fund Protocol), pending the successful conclusion of parliamentary treaty examination and following the implementation of necessary domestic legislative changes.
2. Accession to the Supplementary Fund Protocol would increase the maximum level of compensation available to New Zealand in the event of a major marine oil spill from an oil tanker, from approximately \$377 million to approximately \$1.392 billion.

Executive summary

3. There is a low likelihood of a major marine oil spill from an oil tanker occurring in New Zealand, but the potential consequences could be severe, and the costs could be high.
4. The Supplementary Fund Protocol is part of the International Oil Pollution Compensation (IOPC) funds. The IOPC funds are intergovernmental organisations that provide additional levels of compensation for oil pollution damage from spills of oil from tankers carrying oil as cargo, to countries that have acceded to the fund conventions.
5. The first level of compensation available is from shipowners. Shipowners have strict but limited liability for clean up costs and pollution damage in the event of a marine oil spill. Strict liability means that the shipowner will be liable, regardless of whether negligence or carelessness can be proved. However, the shipowner's liability is limited up to a maximum of approximately \$166 million (depending on the size of the ship).
6. The second and third levels of compensation are available through two international funds. These two funds were established to manage the risk of the shipowner's liability being insufficient to meet the costs of a major marine oil spill from an oil tanker. The funds are funded by levies on oil imports in participating countries.
7. New Zealand is currently a party to one of these funds and has access to compensation of up to \$377 million in the event of a major marine oil spill from an oil tanker (including the liability to shipowners of \$166 million).

8. This paper proposes that New Zealand accedes to a second fund, the Supplementary Fund Protocol. This would increase the compensation available to New Zealand to approximately \$1.392 billion.
9. If New Zealand accedes to the Supplementary Fund Protocol, New Zealand oil companies would have to contribute to the Supplementary Fund. New Zealand's contribution would be between 0.27 and 0.53 percent of the compensation paid by the Supplementary Fund.
10. Based upon scenarios of between two and four major international oil spills in the next ten years, the potential costs to New Zealand oil companies (and their customers) are estimated to be in the order of \$0.6 million and \$1.7 million per year. This represents an increase in the cost of fuel of between 0.029 and 0.078 cents per litre (i.e. between a 35th and a 13th of one cent per litre), should oil companies pass these costs on to consumers.
11. The Supplementary Fund Protocol provides an inexpensive global insurance scheme. Oil spill costs are difficult to predict and have the potential to be in excess of the compensation currently available to New Zealand. The costs associated with the Supplementary Fund Protocol are relatively minor and are appropriate to the level of risk that New Zealand is exposed to from the transportation of oil.
12. If New Zealand does not accede to the Supplementary Fund Protocol, should an oil tanker spill in New Zealand result in costs in excess of the \$377 million of compensation currently available, the Crown could be exposed to costs, particularly for oil spill response and clean up.
13. Before New Zealand can accede to the Supplementary Fund Protocol, amendments to the Maritime Transport Act 1994 would be required. The National Interest Analysis attached to this paper identifies and details these amendments.

Previous Cabinet consideration of the Convention

14. Cabinet indicated support for accession in May 2014. Cabinet approved public consultation on a proposal to accede to the Supplementary Fund Protocol [CAB Min (14) 17/6 refers]. All submissions received supported New Zealand becoming a party to the Supplementary Fund Protocol and no significant issues were raised.
15. Cabinet also noted that the Minister of Transport would report back to Cabinet following consultation. This paper, supported by the National Interest Analysis, recommends that New Zealand accede to the Supplementary Fund Protocol.
16. The National Interest Analysis explains the benefits, costs, and legislative changes required to accede to the Supplementary Fund Protocol. The content of the National Interest Analysis is summarised in this paper.

The international regime of limited liability of shipowners means that the costs of a major marine oil spill may not be recovered from the polluter

17. There is a low likelihood of a major marine oil spill from an oil tanker occurring in New Zealand, but the potential consequences could be severe. Potential costs include:
 - measures to prevent or minimise damage of an oil spill
 - property damage
 - direct economic loss from interruption of business or fishing operations
 - actions taken to restore the environment¹
18. The first level of compensation available is from shipowners. Under widely adopted international conventions and New Zealand legislation, shipowners have strict but limited liability in the event of a marine oil spill, and are required to hold insurance cover. Oil tankers, depending on their size, have liability limited to up to \$166 million.² This is part of a widely established and long standing international regime, which is incorporated in section 347 of New Zealand's Maritime Transport Act 1994.
19. Effectively, the international limited liability regime is a compromise between the need for suitable compensation levels and the creation of strict liability.
20. Strict liability reflects the 'polluter pays' principle and avoids the need to prove negligence or carelessness. This system supports the prompt payment of compensation by seeking to avoid complex, time consuming, and costly court processes, with the prospect that funds received fall well short of the amount claimed.
21. The concept of limited liability has a long history and is entrenched in international maritime law. Limited liability was introduced to encourage trade and navigation given the inherent perils of the sea. The limit on liability support mandatory insurance at affordable levels.³ The requirement to hold insurance also protects against the risk that the shipowner is unable to make good any claims, for example because of insolvency.

Proposal to accede to the Supplementary Fund Protocol to ensure there is adequate compensation available to New Zealand

22. To manage the risk that the shipowner's liability is insufficient to meet the costs of a major marine oil spill from an oil tanker, two international funds (the second and third level of compensation) have been established. The funds pay additional compensation, and are funded by levies on oil imports in participating countries.

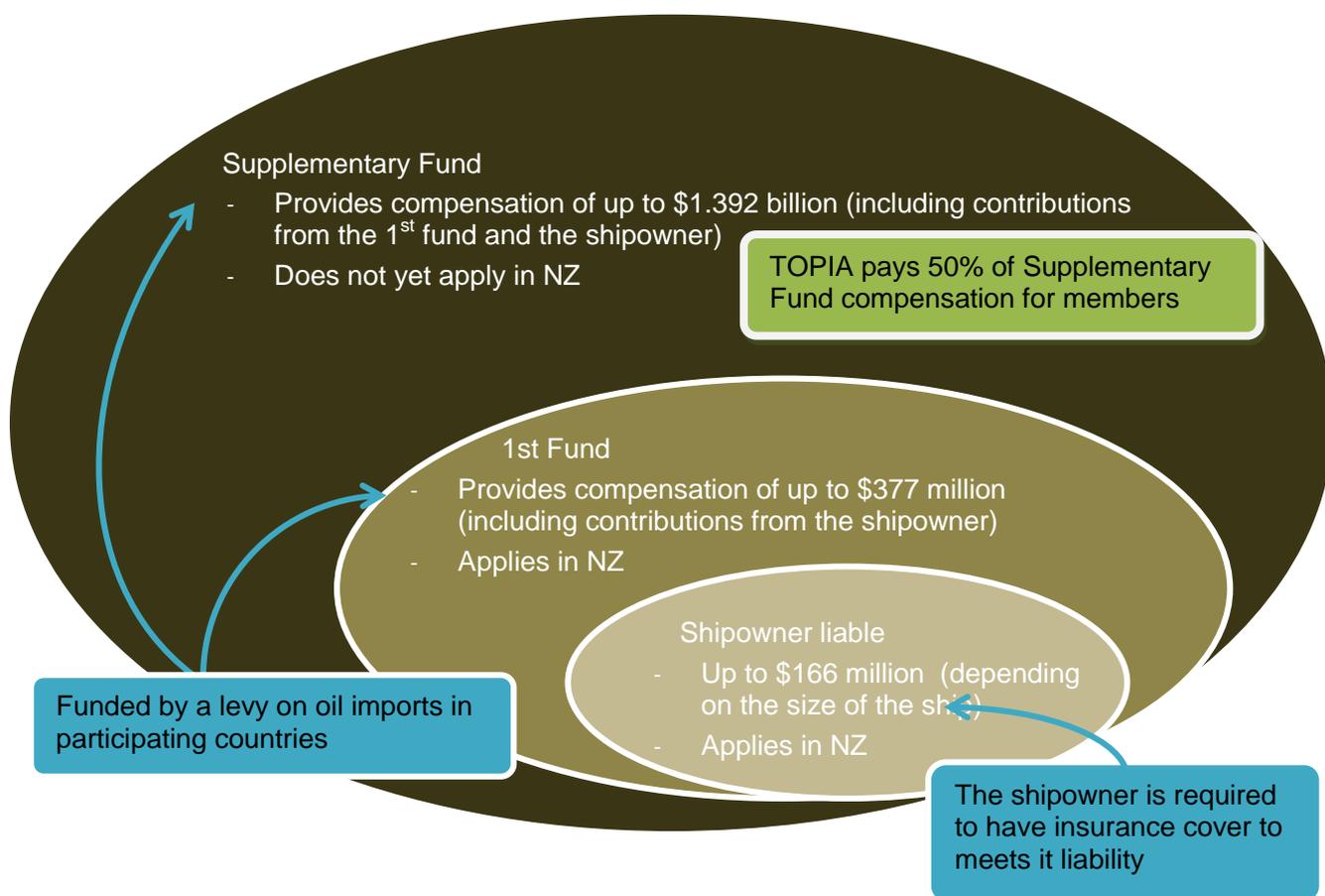
¹ Environmental costs, such as loss of ecosystems or wildlife, are outside the scope of compensation under the international regimes and the Supplementary Fund Protocol.

² International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992. This convention sets compensation limits in Special Drawing Rights (SDR), which are supplementary foreign exchange reserve assets defined and maintained by the International Monetary Fund.

³ Mandatory insurance for oil tankers is required under section 363 of the Maritime Transport Act.

23. New Zealand is a party to one of these funds. Through this fund New Zealand has access to a maximum of around \$377 million⁴ in the event of a major marine oil spill from an oil tanker (including the liability of the shipowner).
24. This paper proposes that New Zealand accede to the second fund, the Supplementary Fund Protocol. This would increase the maximum compensation available to New Zealand to around \$1.392 billion.⁵
25. The three levels of compensation under international regimes are outlined in Figure 1 below. New Zealand is a party to the 1992 Civil Liability Convention and the 1992 Fund Convention establishing the first two levels. This paper proposes that New Zealand become a party to the third level – the Supplementary Fund.

Figure 1 – The international regime for compensation in the event of a marine oil spill from an oil tanker



⁴ The compensation available to New Zealand depends on New Zealand's exchange rate. The 1992 Fund provides compensation up to 203 million SDR

⁵ The Supplementary Fund Protocol provides compensation up to a maximum of 750 million SDR. Amounts expressed in this document are in New Zealand dollars, at an exchange rate of 1.856 New Zealand dollars per Special Drawing Right as at 10 January 2014 (to remain consistent with the consultation document).

26. The Supplementary Fund Protocol is in force for 29 States.⁶ Excluding land-locked States, New Zealand is among six Organisation for Economic Co-operation and Development countries that have not acceded to the Supplementary Fund Protocol (New Zealand, Chile, Iceland, Israel, Mexico, and the United States; which is large enough to have its own system).
27. To reduce the impact of the Supplementary Fund Protocol on oil importers and to ensure adequate responsibility by ship owners, an international group of protection and indemnity insurers voluntarily agreed to pay half the compensation paid by the Supplementary Fund, where the tanker ship is insured by one of its members (the Tanker Oil Pollution Indemnification Agreement (TOPIA) 2006). This agreement represents 90 percent of the world's ocean-going oil tonnage.
28. The Supplementary Fund was created as a result of two particular major oil spills involving oil tankers, which demonstrated the potential for high cost incidents above previous compensation limits:
- The sinking of the *MV Erika* off the coast of France in 1999, where 19,800 tonnes of oil was spilt. The cost of clean up and damages was estimated at \$223 million in today's dollars.⁷
 - The sinking of the *Prestige* off the coast of Spain in 2002, where 63,272 tonnes of oil was spilt. The cost of clean up and damages was estimated at \$592 million in today's dollars.

Benefits of being party to the Supplementary Fund Protocol

29. Accession to the Supplementary Fund Protocol provides New Zealand with access to an inexpensive global insurance scheme that would increase the compensation available to New Zealand to around \$1.392 billion.
30. The regime supports the principle of user pays, with oil users contributing to the costs and inherent risks of the transportation and supply of oil.

Risks of not being Party to the Supplementary Fund Protocol

31. It is difficult to predict the expected cost of an oil spill, as costs vary widely depending on the type of oil spilt, weather and sea conditions, type of coastline affected, the difficulty of the response operation, and length of time that oil is spilling into the environment.

⁶ Australia, Barbados, Belgium, Canada, Congo, Croatia, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Latvia, Lithuania, Montenegro, Morocco, Netherlands, Norway, Poland, Portugal, Republic of Korea, Slovakia, Slovenia, Spain, Sweden, Turkey, United Kingdom of Great Britain and Northern Ireland.

⁷ Actual figures were US\$ 2009, but adjusted for US inflation and purchasing power parity. Source: *Consolidated dataset on oil spills*, MEPC 62/INF.24 (the International Maritime Organization), 6 May 2011.

32. It is likely that it would take an oil spill of at least 10,000–20,000 metric tonnes⁸ affecting particularly sensitive areas of New Zealand’s coast for the \$377 million of compensation currently available to be exceeded.⁹
33. The *MV Rena* was not an oil tanker and so is not covered by the discussion in this paper. However, as a comparison, the clean up of the *MV Rena*’s 350 tonnes oil spill cost \$47 million. The heavy oil it carried (1,700 tonnes at the time of the incident) was its own bunker fuel. On this basis, it would take an incident involving 30 to 60 times more oil than the *MV Rena* incident to exceed the \$377 million of compensation currently available.
34. Oil tankers in operation in New Zealand carry on average between 55,000 and 100,000 metric tonnes, but they are compartmentalised and double hulled to minimise oil losses.
35. The area most likely to experience a heavy oil spill from an oil tanker is the Whangarei Harbour, where oil tankers carry imported heavy oils to the Marsden Point Oil Refinery. The Northland East Coast approach to Marsden Point is also considered high risk, as is the Taranaki coast, due to oil tanker movement to collect oil from offshore installations. Floating production storage and offloading vessels are considered oil tankers when moving. Table 1 outlines the potential likelihood of such an event. More detail is provided in the attached National Interest Analysis.

Table 1 – New Zealand risk areas for a major marine oil spill from an oil tanker¹⁰

Area	Sensitivity factors	Spill size (tonnes)	Probability
Whangarei Harbour	Mangrove swamps, salt marshes and wildlife.	10,000	1 in 20 year event
		20,000 – 50,000	1 in 100 year event
Northland East Coast (Cape Reinga to Mangawhai)	Rocky coast, salt marshes, mangrove swamps. Wildlife and habitats.	10,000 – 20,000	1 in 100 year event
Taranaki Coast	Cobble or boulder beaches. Wildlife and habitats.		

⁸ The Supplementary Fund Protocol refers to ‘tons’, whereas New Zealand uses metric tonnes. 1 ton = 0.907 metric tonnes. Both amounts are referred to this in this paper, depending on whether the source is the Supplementary Fund Protocol or a New Zealand source.

⁹ This is based on international examples, as well as oil spill cost estimation models used by the United States Environmental Protection Agency and the International Maritime Organization.

¹⁰ These estimates are based on Maritime New Zealand’s Marine Oil Spill Risk Assessment, which models the probability of oil spills around the New Zealand coastline based on ship and oil tanker movements and considers the sensitivity of the shoreline and surrounding areas.

36. Should an oil tanker spill in New Zealand result in pollution damage that exceeds \$377 million, the Crown could be exposed to costs, particularly for oil spill response and clean up.
37. The fund was initially established in response to the potential for high costs on States for the clean-up of an oil spill. However, the economic consequences for private companies and individuals have become more pronounced in recent times. In many cases the government in the affected country allows private claimants to claim first, thereby increasing the risk that the government's costs will not be recovered.

Cost of being party to the Supplementary Fund Protocol

38. Oil spill costs are difficult to predict and have the potential to be in excess of the compensation currently available to New Zealand. The costs associated with the Supplementary Fund Protocol are relatively minor and are appropriate to the level of risk that New Zealand is exposed to from the transportation of oil.
39. The Supplementary Fund Protocol works on a pay-as-you-go basis. Levies on oil imports are only collected when there is a need to pay compensation, rather than regular annual levies building up the fund in anticipation. As compensation has never been paid from the Supplementary Fund, no levies have ever been collected.
40. Based upon scenarios of between two and four major international oil spills in the next ten years, the potential costs to New Zealand oil companies (and their customers) are estimated to be in the order of \$0.626 million and \$1.703 million per year. This represents an increase in the cost of fuel of between 0.029 cents per litre and 0.078 cents per litre, should oil companies pass these costs on to consumers. The National Interest Analysis provides further information on the two scenarios.
41. The Supplementary Fund Protocol does not provide compensation for spills from offshore oil installations. The regime described in the paper only relates to marine oil spills from oil tanker ships. The one minor overlap, is where floating platform storage and offloading vessels are in transit (they are excluded when they are anchored as part of oil production).

Balance of benefits and costs

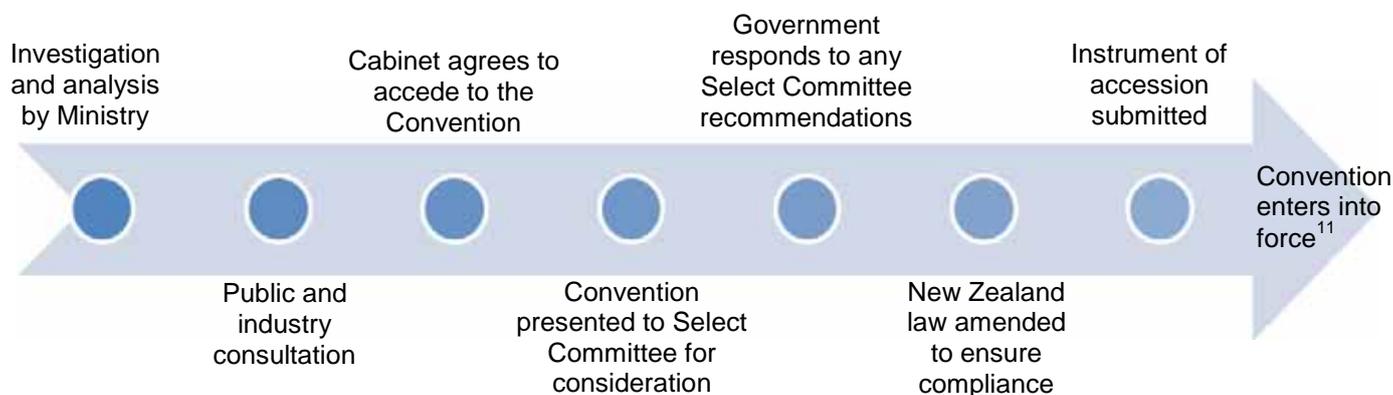
42. The Supplementary Fund Protocol provides an inexpensive global insurance scheme. Oil spill costs are difficult to predict and have the potential to be in excess of the compensation currently available to New Zealand. The costs associated with the Supplementary Fund Protocol are relatively minor and are appropriate to the level of risk that New Zealand is exposed to from the transportation of oil.

Decision sought and next steps

43. The process for consideration and ratification (or accession) to international conventions is outlined in Figure 2 below.
44. The first two stages have been completed. This paper seeks agreement to accede to the Supplementary Fund Protocol, pending the successful conclusion of the

remainder of the parliamentary treaty examination process, and the implementation of necessary domestic legislative changes.

Figure 2 – The process for consideration and accession of international conventions



Risks in the next steps

45. There is unlikely to be political or media interest through the next stages of the process, as the Supplementary Fund Protocol:
- relates to the very low probability scenario of a major marine oil spill from an oil tanker occurring in New Zealand
 - has very low costs associated with it, only in the event of a major international oil spill occurring in a member country
 - it is not relevant to the *MV Rena*
 - is not relevant to offshore oil installations (there are no liability limits for operators of offshore oil installations)
46. The Supplementary Fund Protocol would enter into force for New Zealand three months following the date of deposit of the Instrument of Accession.

Consultation

Interdepartmental consultation

47. The Ministry of Transport has consulted with the following agencies on this paper: the Ministry of Business, Innovation and Employment; the Environmental Protection Authority; Te Puni Kōkiri; Maritime New Zealand; the Treasury; the Ministry for the Environment; the Department of Conservation; the Ministry of Foreign Affairs and Trade. The Department of the Prime Minister and Cabinet was informed.

¹¹ In the case of the Supplementary Fund Protocol, 90 days after the submission of the instrument of accession.

Public consultation

48. The main parties affected by New Zealand's accession to the Supplementary Fund Protocol are the oil importing companies, oil cargo carriers, and local authorities. During consultation from 29 May 2014 to 27 June 2014, there were three submissions made. All submitters supported the proposal.
49. Local Government New Zealand supports the proposal, because an oil spill can damage aquaculture and fishing stocks, decrease demand for New Zealand seafood, hinder ship movements and harm New Zealand's tourism industry.
50. Seafood New Zealand stated that taking into account any expected impact on fuel prices relative to the benefits should a spill occur in New Zealand waters, the seafood industry supports the proposed accession to the Supplementary Fund Protocol.
51. Dr Bevan Marten referred to New Zealand's geographical isolation with a sensitive marine environment, and relatively few local resources for responding to a major oil spill, in supporting the proposed accession to the Supplementary Fund Protocol.
52. There may be opportunities for further public consultation on implementation measures during the Select Committee process for legislative changes, should Cabinet agree that New Zealand pursue accession to the Supplementary Fund Protocol.

Consultation with New Zealand oil companies

53. Z Energy and ExxonMobil provided responses supporting the proposed accession to the Supplementary Fund Protocol. During discussions with the Ministry of Transport, Chevron New Zealand indicated that it supports accession in principle. BP did not provide a response.
54. Submissions from the oil companies raised the need for the most transparent and open mechanism, with the earliest notice, possible for the collection of any additional levies, to allow the costs to be passed on to fuel users where needed.
55. The feedback from the oil companies, and further consultation with them, will be considered in the process of designing implementation options and drafting legislation.

Financial implications

56. There are no financial implications for the Government if New Zealand accedes to the Supplementary Fund Protocol.

Human rights, gender, and disability implications

57. There are no human rights, gender, or disability implications arising from this paper.

Legislative implications

58. Before New Zealand can accede to the Supplementary Fund Protocol, amendments to the Maritime Transport Act would be required. The National Interest Analysis attached to this paper identifies and details these amendments.
59. If Cabinet agrees to New Zealand acceding to the Supplementary Fund Protocol, legislative changes would follow the usual process.

National Interest Analysis

60. An extended National Interest Analysis is required with respect to the proposal to accede to the Supplementary Fund Protocol covered in this paper because of the legislative changes expected. The Ministry of Transport has prepared an extended National Interest Analysis, which includes a regulatory impact analysis, and is attached to this Cabinet paper.
61. The National Interest Analysis has been assessed by the Ministry of Transport Regulatory Impact Assessment Panel as meeting the quality assurance criteria.
62. I have considered the analysis and advice of my officials, as summarised in the attached National Interest Analysis. I am satisfied that, aside from the risks, uncertainties and caveats already noted in this Cabinet paper, the regulatory proposals recommended in this paper are required in the public interest and will deliver the highest net benefits of the practical options available.

Publicity

63. As accession to Supplementary Fund Protocol will be of public interest, I intend to make this Cabinet paper publicly available on the Ministry of Transport's website after the Cabinet Minute is finalised.
64. I will consider any publicity opportunities during the process of accession, should Cabinet agree to New Zealand acceding to the Supplementary Fund Protocol.

Recommendations

65. The Minister of Transport recommends that the Committee:

1. **note** that New Zealand's accession to the *Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992* (Supplementary Fund Protocol), would increase New Zealand's compensation for spills from oil tankers from 203 million Special Drawing Rights (equating to approximately NZ\$377 million) to 750 million Special Drawing Rights (equating to approximately NZ\$1.392 billion)
2. **note** that based upon scenarios of between two and four major international oil spills in the next ten years, the potential costs to New Zealand oil companies (and their customers) are estimated to be in the order of \$0.626 million and \$1.703 million per year. This represents an increase in the cost of fuel of between 0.029 cents per litre and 0.078 cents per litre, should oil companies pass these costs on to consumers
3. **approve** the text of the Supplementary Fund Protocol, which is attached
4. **agree** to accede to the Supplementary Fund Protocol subject to the satisfactory completion of the parliamentary treaty examination process and domestic implementation of the Supplementary Fund Protocol obligations through the necessary legislative changes
5. **approve** the content of the National Interest Analysis attached to this paper
6. **agree** to present the Supplementary Fund Protocol and National Interest Analysis to the House for the purposes of the parliamentary treaty examination process, under Standing Order 397
7. **invite** the Minister of Transport to issue drafting instructions to the Parliamentary Counsel Office for any amendments to Legislative Instruments required to accede to the Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992
8. **note** that this Cabinet paper will be made publicly available on the Ministry of Transport's website after the Cabinet Minute has been issued

Hon Simon Bridges
Minister of Transport

Dated: _____