Office of the Minister of Transport

Chair
Cabinet Economic Growth and Infrastructure Committee

CONSULTATION DOCUMENT – PROPOSAL TO ACCEDE TO THE SUPPLEMENTARY FUND PROTOCOL

Proposal

1. This paper seeks the Cabinet Economic Growth and Infrastructure Committee's agreement to the Ministry of Transport undertaking consultation on a proposal that New Zealand accedes 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).

2. Accession to the Supplementary Fund Protocol would increase the level of compensation available to New Zealand in the event of a major spill from an oil tanker, from $377 million to $1.392 billion.[1]

Executive summary

3. The Supplementary Fund Protocol provides up to $1.392 billion of compensation for oil pollution damage from oil tankers to those countries that have acceded to the Supplementary Fund Protocol. Should compensation be required from the Supplementary Fund, oil importers of countries that have acceded to the Supplementary Fund Protocol are levied proportionate to their annual oil imports.

4. New Zealand currently has access to compensation for oil tanker spills of up to $377 million, through its accession to international funds. Based on oil tanker movements around New Zealand's coast and the quantities of oil carried, it is likely that should a major spill event occur, compensation for preventative measures to stop oil pollution damage, property damage, economic loss, and clean up costs will exceed $377 million.

5. Based on New Zealand's oil imports, New Zealand's contribution would be 0.53 percent (half a percent) of the compensation paid by the Supplementary Fund. Based on New Zealand's share of global oil imports and a spill occurring somewhere in the world requiring the maximum compensation of $1.392 billion, New Zealand oil importers would, in most cases, be required to pay $2.796 million.

[1] International Oil Pollution Compensation Funds are set through Special Drawing Rights as defined by the International Monetary Fund. The Supplementary Fund Protocol provides compensation up to a maximum of 750 million Special Drawing Rights, which are converted to New Zealand dollars (1.392 billion). $377 million is equal to 203 million Special Drawing Rights. Amounts expressed in this document are in approximate New Zealand dollars, at an exchange rate of 1.856 New Zealand dollars per Special Drawing Right as at 10 January 2014. Because of this, all figures in this paper that are based on Special Drawing Rights amounts are approximate.

6. Based on two modelled scenarios, the average annualised costs to New Zealand's oil importers are estimated to be between $0.626 million and $1.703 million. This represents an increase in the cost of fuel of between 0.029 cents per litre and 0.079 cents per litre, should oil companies pass these costs on to consumers (i.e. 1/35th and 1/13th of a cent per litre respectively).

7. There have been no claims against the Supplementary Fund since it was established in 2003. Therefore, no contributions have been required from member states.

8. Accession to the Supplementary Fund Protocol provides New Zealand with access to 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. 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. Based on this, it is considered that the advantages of becoming party to the Supplementary Fund Protocol outweigh the disadvantages.

Background

9. In 2009 the government's Petroleum Action Plan[2] was launched. It was aimed at ensuring New Zealand is able to maximise the gains from the responsible development of its oil and gas resources. The Petroleum Action Plan comprised eight core work-streams, one of which was to commission an independent review of the adequacy of New Zealand's health, safety and environmental legislation for offshore petroleum operations.

10. The aim of the independent review was to ensure that the legislative structure, institutional capabilities, and practices in New Zealand were fit for purpose, and compared favourably to international best practice.

11. The review looked at the health, safety, and environmental regimes in four petroleum producing countries (Ireland, the United Kingdom, Norway and Australia) and compared these with New Zealand's regulatory frameworks for offshore petroleum operations to see if there were any major gaps.

12. The review was completed in December 2010 and concluded that New Zealand's health, safety, and environmental arrangements for offshore petroleum operations already incorporated a number of key characteristics of international best practice. However, the review also identified some areas where New Zealand's regulatory framework could be improved and made eight recommendations to that effect.

[2] http://www.med.govt.nz/sectors-industries/natural-resources/oil-and-gas/petroleum-action-plan

13. Government agencies involved in regulating the offshore industry have been working on giving effect to the recommendations of the independent review. They have strengthened the regulatory regime to cover all stages of offshore operations (exploration, production, and cessation) to ensure that processes are in place to manage health, safety, and environmental risks and ensure that New Zealand attracts high-quality operators that will comply with its standards.

14. One of the recommendations of the independent review was directed at the Ministry of Transport. The recommendation was that:

> *Government investigate whether current levels of insurance and liability are sufficient and consider ratifying international instruments which provide additional or stronger levels of insurance and liability in relation to both shipping and installations involved in offshore petroleum activities*

The nature of the Supplementary Fund Protocol

15. The Supplementary Fund Protocol is part of the International Oil Pollution Compensation (IOPC) fund conventions. The Supplementary Fund Protocol is a third level of international insurance.

16. The IOPC funds are intergovernmental conventions that provide three levels of compensation for oil pollution damage from oil tankers. The three levels of compensation are the:

    16.1. 1992 Civil Liability Convention (establishes that compensation is to be paid by the ship owner up to a limit of 89.777 million Special Drawing Rights, approximately $166 million)

    16.2. 1992 Fund Convention (establishes a fund that provides up to 170 million Special Drawing Rights, which is approximately $377 million of compensation including the 1992 Civil Liability Convention limit)

    16.3. Supplementary Fund Protocol (establishes a fund that provides up to a total of 703 million Special Drawing Rights, approximately to $1.392 billion of compensation, including the $377 million available from the 1992 Fund Convention and 1992 Civil Liability Convention)

17. The Supplementary Fund Protocol was established in May 2003 to provide no-fault compensation in the event of a major spill from an oil tanker where the maximum compensation available from the first two levels of compensation may be insufficient.

18. The Supplementary Fund Protocol provides compensation of up to $1.392 billion for:

    18.1. measures taken to prevent or minimise oil pollution damage

    18.2. property damage

    18.3. direct economic loss from interruption of business or fishing operations

    18.4. actions taken to restore the environment

19. Currently, New Zealand has access of up to $377 million of compensation through its accession to the 1992 Fund Convention. Should claims arising from an oil tanker spill be in excess of $377 million, compensation will be provided pro-rata to claimants and legal action will be required to recover outstanding payments. This could expose the Crown to unrecoverable costs, particularly for oil spill response and clean up.

20. Should a spill occur that requires compensation above $377 million, individual claimants may submit their claim to the IOPC Funds, although if claimants have claims for similar costs they may coordinate their submissions. Claims are required to have supporting evidence and technical experts are usually provided to monitor and provide advice on clean up action taken. Experts are used to assess the claims. The Director of the IOPC Funds then considers the claim and determines if compensation should be awarded.[3]

21. At the end of each year, the IOPC invoices oil importers within countries acceded to the IOPC Funds, for their contribution to the compensation that has been paid for that year.

22. The maximum level of compensation and therefore the potential costs to New Zealand may be amended in the future. A ‘tacit acceptance’ process applies for amendments to limits of the IOPC funds. An amendment to the limit previously circulated by the International Maritime Organization (IMO) and adopted by a meeting of the Legal Committee of the IMO will be deemed to be accepted 12 months after notification of its adoption to all State Parties, unless one quarter of those States advise that they do not accept the amendment. The amendment will come into force 12 months after it has been deemed to have been accepted.

Risk of an oil spill in New Zealand

23. There have been four spills that have exceeded the 1992 Fund Convention within the last 14 years. However, to date, no claim for compensation has been made under the Supplementary Fund Protocol, as the spills occurred either before 2003 or in non-member states.

[3] From the International Oil Pollution Compensation Fund 1992, Claims Manual 2008.

24. 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, and length of time that oil is spilling into the environment.

25. It is likely that it would take an oil spill of at least 10,000–20,000 tonnes affecting particularly sensitive areas of New Zealand's coast for the $377 million of compensation currently available to be exceeded.[4] This is based on international examples, as well as oil spill cost estimation models used by the United States Environmental Protection Agency and the IMO. Oil tankers in operation in New Zealand carry on average between 55,000 and 100,000 tonnes.

26. As a comparison, the clean up of the *Rena's* 350 tonnes oil spill cost $47 million. The *Rena* was not an oil tanker. 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 *Rena* incident to exceed the $377 million of compensation currently available.

27. 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. Legal action would be necessary to recover unpaid costs, and failure of this action may result in a shortfall to the Crown.

28. Maritime New Zealand has developed a New Zealand Marine Oil Spill Risk Assessment, which has modelled the probability of oil spills around the New Zealand coastline based on ship and oil tanker movements and the sensitivities of the shoreline and surrounding areas.

29. 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.

30. The table below identifies sensitivity factors of these coastlines and oil spill probability, based on the New Zealand Marine Oil Spill Risk Assessment undertaken by Maritime New Zealand.

[4] The Supplementary Fund Protocol refers to 'tons', whereas New Zealand uses metric tonnes. 1 ton = 0.907 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.

Marine Oil Spill Risk Assessment oil spill estimates

Area	**Sensitivity factors (environmental)**	**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.		

Cost of membership of the Supplementary Fund Protocol

31. To reduce the impact 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.

32. Based on New Zealand's share of global oil imports[5] and a spill occurring somewhere in the world requiring the maximum compensation of $1.392 billion, New Zealand oil importers would be required to pay:

    - $2.709 million should the tanker be part of TOPIA
    - $5.418 million should the tanker not be part of TOPIA

33. The Supplementary Fund Protocol works on a pay-as-you-go basis, where levies on oil imports are only collected when there is a need to pay compensation. These levies would only be required when there is a major spill in a signatory country, rather than being built up by regular annual levies. As compensation has never been paid from the Supplementary Fund, no levies have ever been collected.

[5] In 2012, New Zealand imported 5.608 million tons of oil. This represents 0.53 percent of the 1.045 billion tons of oil imported by Supplementary Fund Protocol member countries.

34. By becoming a party to the Supplementary Fund Protocol, New Zealand will be eligible to receive an increased amount of compensation for responding to an oil spill. This would provide access to total compensation of up to the $1.392 billion (including the first two levels) for any one incident without needing to prove fault.

35. The increased compensation could be used to prevent or minimise pollution damage, property damage, or direct economic loss from interruption of business or fishing operations. The compensation would also cover actions taken to restore the environment.

36. Certain environmental impacts, such as losses of ecosystems or wildlife, are outside the scope of the compensation regimes under the 1992 Fund Convention and the Supplementary Fund Protocol.[6]

37. To assess the potential cost impact on New Zealand oil imports from increased levies as a result of becoming party to the Supplementary Fund Protocol, two cost scenarios have been modelled. The costs are based on three and six spills occurring over a ten year period respectively, with some requiring the maximum $1.392 billion available from the Supplementary Fund Protocol and others requiring 75 percent of the maximum ($1.044 billion). The appendix provides further information on the two scenarios.

38. Based on the two modelled scenarios, the average annualised costs to New Zealand's oil importers are estimated to be between $0.626 million and $1.703 million. 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 (i.e. 1/35th and 1/13th of a cent per litre respectively).

39. The government could fund the cost to the Supplementary Fund to avoid the oil import industry having to contribute to the Supplementary Fund. However, this option has not been considered as the potential fuel cost increase is marginal (modelled at between 1/35th and 1/13th of a cent per litre) and is not expected to have a significant impact on consumers. In addition, voluntary government contributions or subsidies are likely to be administratively complicated and in contravention of the principle of 'user (or beneficiary/causer) pays'.

40. Should New Zealand accede to the Supplementary Fund Protocol New Zealand oil importers (BP Oil, Chevron NZ, Mobil Oil NZ, and Z Energy) would only be required to pay an additional levy on their share of imported oil when there is a spill requiring compensation in a member country.

[6] This would mean that claims made for compensation following the loss of a species are not compensated. This differs to claims made for economic loss due to reduced or damaged fish stocks.

41. There would be no significant administrative costs to becoming a party to the Supplementary Fund Protocol, as a levy is already collected from oil importers as part of New Zealand's accession to the 1992 Fund Convention.[7] Administrative costs of the IOPC are shared across the funds and are not significant.

42. Should New Zealand oil importers not fulfil their obligations to communicate information on oil receipts, and this results in a financial loss for the Supplementary Fund, the New Zealand Government would then be liable to compensate the Supplementary Fund for the loss.

43. New Zealand already communicates information on oil receipts in accordance with the 1992 Fund Convention and any communication made under the 1992 Fund Convention is deemed to be made under the Supplementary Fund Protocol.

44. The Supplementary Fund Protocol deems all Contracting States to receive at least 1 million tons of contributing oil. In the event that New Zealand receives less than 1 million tons, it is obliged to collect from New Zealand oil importing companies sufficient funds so as to cover the gap between oil actually received (for which contributions will have been made directly to the Supplementary Fund) and 1 million tons.

45. Currently, the New Zealand oil companies receive in total approximately 5.5 million tons of contributing oil per year, and it is unlikely that the New Zealand Government will be called upon to make any contribution. In the event that New Zealand's oil imports fall below the minimum threshold, the New Zealand Government would need to put in place arrangements with the New Zealand oil importing companies to meet this minimum payment.

46. Should annual oil imports consistently fall below the 1 million ton minimum, New Zealand could denounce the Supplementary Fund Protocol. Such denunciation would be effective 12 months after its deposit with the International Maritime Organization.

Benefits

47. Accession to the Supplementary Fund Protocol provides New Zealand with access to 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.

[7] Since 1996 New Zealand oil importers have contributed between $0.285 million and $0.385 million (2012 dollars) to the 1992 Fund Convention.[8] Australia, Barbados, Belgium, Canada, Croatia, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Latvia, Lithuania, Montenegro, Morocco, Netherlands, Norway, Poland, Portugal, Republic of Korea, Slovenia, Spain, Sweden, Turkey, United Kingdom of Great Britain and Northern Ireland. In 2014 Slovakia will become a Party to both the 1992 Fund Convention and the Supplementary Fund Protocol.

48. New Zealand’s accession to the Supplementary Fund Protocol would also be beneficial to the maintenance of New Zealand’s standing internationally. The Protocol is in force for 29 States.[8] It would support the New Zealand “brand” as a responsible maritime regulator and constructive participant in the international maritime system. 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 has its own system)).

Summary of costs and benefits

49. The cost associated with accession is relatively minor and is appropriate to the level of risk that New Zealand is exposed to from the transportation of oil. Based on this, it is considered that the advantages of becoming party to the Supplementary Fund Protocol outweigh the disadvantages.

Consultation

Interdepartmental consultation

50. 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; the Ministry for Primary Industries; Maritime New Zealand; the Treasury; the Ministry for the Environment; the Department of Conservation; and the Ministry of Foreign Affairs and Trade. The Department of the Prime Minister and Cabinet was informed.

Public consultation

51. This paper seeks Cabinet’s agreement to undertake consultation on the proposal that New Zealand accedes to the Supplementary Fund Protocol. 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.

52. There will be opportunities for further public consultation during the Select Committee process, should Cabinet agree that New Zealand pursue accession to the Supplementary Fund Protocol.

Financial implications

53. There are no immediate financial implications or decisions arising from this paper.

[8] Australia, Barbados, Belgium, Canada, Croatia, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Latvia, Lithuania, Montenegro, Morocco, Netherlands, Norway, Poland, Portugal, Republic of Korea, Slovenia, Spain, Sweden, Turkey, United Kingdom of Great Britain and Northern Ireland. In 2014 Slovakia will become a Party to both the 1992 Fund Convention and the Supplementary Fund Protocol.

Human rights, gender, and disability implications

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

Legislative implications

55. There are no immediate legislative implications or decisions arising from the proposed consultation. Should New Zealand accede to the Supplementary Fund Protocol, amendments to the Maritime Transport Act 1994 will be required. The National Interest Analysis attached to this paper identifies these amendments.

56. Following consultation, I would report back to Cabinet prior to proceeding with any legislative changes required for New Zealand to accede to the Supplementary Fund Protocol.

National Interest Analysis

57. A National Interest Analysis is required with respect to the proposal to accede to the Supplementary Fund Protocol covered in this paper. A National Interest Analysis has been prepared by the Ministry of Transport and is attached to this Cabinet paper.

58. The National Interest Analysis has been assessed by the Ministry of Transport Regulatory Impact Assessment Panel as meeting the quality assurance criteria.

59. I have considered the analysis and advice of my officials, as summarised in the attached National Interest Analysis and 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; will deliver the highest net benefits of the practical options available; and are consistent with our commitments in the government statement “Better Regulation, Less Regulation.”

Publicity

60. The Ministry of Transport will consult oil importing companies, oil cargo carriers, fishing interests, and local authorities directly, and provide a six-week consultation period. The documents will also be publicly available on the Ministry of Transport’s website to allow other members of the public to provide comment.

61. The timing of the consultation of this proposal will be undertaken concurrently with the proposed consultation on the increased insurance requirements for offshore installations, which is the subject of a separate Cabinet paper. Consultation is proposed to occur in late April/early May 2014.

62. As it will be of public interest, I intend to make this Cabinet paper publicly available on the Ministry of Transport’s website at the start of the consultation period.

Recommendations

63. 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, 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. **agree** that the Ministry of Transport undertakes public consultation on the proposal that New Zealand accedes to the Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992, using the attached consultation document (subject to any further editorial changes)

3. **note** that this Cabinet paper will be made publicly available on the Ministry of Transport's website from the start of the consultation period

4. **note** that following consultation, the Minister of Transport will report back to Cabinet prior to proceeding with any legislative changes required for New Zealand 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

Hon Gerry Brownlee
Minister of Transport

Dated: ____________________________

Appendix – Modelled oil spill scenarios and cost impacts on New Zealand

	Scenario A (3 spills over 10 years)	*Scenario B (6 spills over 10 years)*
Spills requiring maximum compensation available ($1.392 billion)	***1 covered by TOPIA***	***1 covered by TOPIA*** ***1 not covered by TOPIA***
Spills requiring 75 percent of maximum compensation available ($1.044 billion)	***2 covered by TOPIA***	***3 covered by TOPIA*** ***1 not covered by TOPIA***
Total cost to New Zealand per year	*$0.626 million*	*$1.703 million*
Increase in fuel cost (cents/litre)	*0.029 cents*	*0.078 cents*
Percentage increase in pump price for fuel based on notional cost of $2.16 per litre of petrol	*0.013 percent cost increase*	*0.036 percent cost increase*