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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

on liability, compensation and financial security for offshore oil and gas operations pursuant to Article 39 of Directive 2013/30/EU

{SWD(2015) 167 final}

INTRODUCTION

This report provides an overview how liability for damage from offshore accidents in oil and gas prospection, exploration and production is addressed in the EU. In effect, it analyses how Europe deals with a series of societal dilemmas arising in relation to offshore oil and gas: first, who is liable for what kinds of damage and loss to whom; second, how to ensure that liable parties have sufficient financial capacity to provide rightful compensation for the damage and loss they are liable for; and third, how compensation should be disbursed so that it reaches legitimate claimants quickly and the risks of cascading impacts to the broader economy are minimized.

There has not been a major offshore accident in the EU since 1988 and 73% of oil and gas production in the EU comes from North Sea Member States already recognized as having the world's best performing offshore safety regimes. Despite this, the EU put in place a common regulatory framework for offshore oil and gas operations following the April 2010 Deepwater Horizon disaster in the Gulf of Mexico in order to raise the safety and environmental protection standards of all EU offshore operations further and make them consistent. Directive 2013/30/EU[1] (henceforth the Offshore Safety Directive or OSD) defines the elements of such a comprehensive EU-wide framework for preventing major accidents and limiting their consequences. The ratification of the Offshore Protocol of the Barcelona Convention by the Council[2] was also part of the EU response to the Deepwater Horizon disaster.

The OSD creates a harmonized EU-wide regulatory regime that establishes a goal-setting regulatory framework built around the concept of a "safety case" (a Report on Major Hazards) and enforced by offshore regulators whose competence and independence the OSD aims to ensure; it also fosters effective cooperation between such regulators. Furthermore, the OSD introduces EU-wide requirements on transparency, including the sharing of information on accidents and near misses as well as on other indicators of the safety performance of industry and regulators in the sector.

As regards liability for offshore accidents and their consequences, the OSD channels it unequivocally to offshore licensees, i.e. the individual or joint holders of authorizations for oil/gas prospection, exploration, and/or production operations issued in accordance with Directive 94/22/EC[3]. It also makes the licensees strictly liable for any environmental damage resulting from their operations. Nevertheless, the OSD does not aim to harmonize the liability rules in the EU for other forms of damage and loss that may result from offshore operations, reflecting the inconclusive results of the corresponding analyses in the impact assessment[4] during the OSD's preparatory stages.

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[1] Directive 2013/30/EU of the European Parliament and the Council of 12 June 2013 on the safety of offshore oil and gas operations and amending Directive 2004/35/EC, OJ L 178 of 28.6.2013 p.66.

[2] Council Decision of 17 December 2012 on the accession of the European Union to the Protocol for the Protection of the Mediterranean Sea against pollution resulting from exploration and exploitation of the continental shelf and the seabed and its subsoil (2013/5/EU). See also Milieu (2013) Safety of offshore exploration and exploitation activities in the Mediterranean: creating synergies between the forthcoming EU Regulation and the Protocol to the Barcelona Convention.

[3] Directive 94/22/EC of the European Parliament and of the Council of 30 May 1994 on the conditions for granting and using authorizations for the prospection, exploration and production of hydrocarbons, OJ L 164 of 30.6.1994, p.3.

[4] Impact assessment accompanying the document 'Proposal for a regulation of the European Parliament and of the Council on safety of offshore oil and gas prospection, exploration and production activities', SEC(2011) 1293 final.

This report aims to fulfil the Commission's obligations under Article 39 of the OSD, which requires the Commission to submit reports on the following:

- An assessment of the effectiveness of the liability regimes in the Union in respect of the damage caused by offshore oil and gas operations, including an assessment of the appropriateness of broadening liability provisions;
- An examination of the appropriateness of bringing certain conduct leading to a major accident within the scope of Directive 2008/99/EC[5] (the Environmental Crime Directive);
- A description of the availability of financial security instruments for offshore operations; and
- A description of the handling of compensation claims for offshore accidents.

These topics are very closely related and addressing them together in one report facilitates their coherent analysis. An accompanying Staff Working Document (SWD(2015) 167 final[6], henceforth Liability SWD) provides additional details on the issues addressed, as well as on the analyses conducted in-house by the Commission and contracted from external experts and stakeholders in the preparation of this report.

The present report and the Liability SWD focus on the member countries of the European Economic Area (EEA) with offshore oil and gas activities. These 'Focal States' comprise (in alphabetical order) Bulgaria, Croatia, Cyprus, Denmark, France, Germany, Greece, Iceland, Ireland, Italy, Latvia, Lithuania, Malta, the Netherlands, Norway, Poland, Portugal, Romania, Spain and the United Kingdom. Operations outside the EEA are not the primary focus.

ENVIRONMENTAL, CIVIL AND CRIMINAL LIABILITY AND THEIR INTERCONNECTEDNESS

It is important to distinguish between different types of liability. First, there is civil liability for damage caused to natural or legal persons. The kinds of damage and loss in this broad category include bodily injury, property damage and economic loss. This damage is commonly referred to as third party damage or 'traditional damage' in the EU *acquis*. In the particular case of economic loss, some legal systems may make a further distinction between *consequential* economic loss, which is economic loss resulting from bodily injury or property damage, and *pure* economic loss, which is economic loss in the absence of bodily injury or property damage.

Second, there is environmental liability within the meaning of the Environmental Liability Directive[7] (ELD), which refers to liability for ecological damage to protected species and natural habitats, damage to water and damage to soil. Environmental liability is based here on a public approach, where the affected party is not a concrete natural or legal person but society as a whole due to the public and universal character of the effects of any damage to shared natural resources. The role of the claimant is fulfilled by public authorities, whose job it is to ensure that polluters remedy the ecological damage they cause. It is therefore for the public authority entrusted with environmental protection to ensure

[5] Directive 2008/99/EC of the European Parliament and of the Council of 19 November 2008 on the protection of the environment through criminal law, OJ L 328 of 19.11.2008, p.28.
[6] Commission Staff Working Document: Civil Liability, Compensation and Financial Security for Offshore Accidents in the European Economic Area, SWD(2015) 167 final.
[7] Directive 2004/35/CE of the European Parliament and of the Council of 21 April 2004 on environmental liability with regard to the prevention and remedying of environmental damage, OJ L 143 of 30.04.2004, p.56.

that the liable operator is identified, the causal link is established, the remediation plan is established and approved, the necessary preventive action or remedial action is taken, etc.[8]

Thirdly, criminal liability refers to liability that arises out of committing a criminal act qualified as such by the law. There is a fundamental difference between civil as well as environmental liability on the one hand and criminal liability on the other. Whereas the liability rules on the former result, in principle[9], in penalties that are exclusively financial and aimed at compensating and remedying damage caused, criminal liability aims at punishing wrongful conduct and penalties may include imprisonment as well as fines and other non-custodial punishments.

THE APPROPRIATENESS OF CRIMINAL LIABILITY FOR OFFSHORE ACCIDENTS AND RESULTING DAMAGE

The European Court of Justice confirmed in 2005[10] that the European Community had the competence to adopt criminal law measures related to the protection of the environment if this is necessary to ensure the efficient implementation of its environmental policy. Based on this case-law, the Environmental Crime Directive (ECD) – the first EU directive to contain criminal liability provisions – laid down in 2008 a list of environmental offences that Member States must consider criminal if committed intentionally or with serious negligence. The EU thus introduced harmonized criminal penalties for infringements of EU environmental legislation in addition to the compensation-centred civil penalties that were already in place.

Under the ECD, Member States must attach criminal sanctions to certain acts that cause or are likely to cause death or serious injury, or substantial damage to the quality of air, the quality of soil or the quality of water, or to animals or plants. However, the scope of the ECD is limited: the Directive only criminalizes the infringement of certain pieces of EU legislation that are listed in the Annexes of the Directive. The criminalized acts include, for example, the illegal discharge of hazardous substances into surface water if it causes or is likely to cause death or injury to persons or significant damage to the environment; the illegal shipment of waste from the European Union only if a significant quantity of waste is involved and if there is a clear intention to make a profit out of it; and the illegal export of ozone depleting substances to developing countries; but not the activities covered by OSD.

As reflected in Article 39(3) of the OSD, this prompts considerations of also bringing certain conduct leading to offshore accidents under the scope of criminal law through EU legislation. While criminal liability for offshore safety breaches would not directly affect the remediation of damage caused, it adds a separate layer of deterrence beyond civil and environmental liability, which could improve the protection of the environment and compliance with offshore safety legislation.

Offshore safety breaches already fall under the criminal code of some Focal States. For example, the laws of both the United Kingdom (UK) and Denmark contain provisions criminalizing certain compliance failures[11]. However, neither the definition of the criminal offences nor the minimum type and level of sanctions are harmonized in the EU. There are strict legal preconditions that must be fulfilled before considering whether to criminalize offshore safety breaches through EU legislation.

[8] An overlap between civil and environmental liability exists, see the Introduction of the Liability SWD.
[9] With the exception of the so-called "punitive damages" in common law systems.
[10] Case C-176/03, *Commission* v. *Council*, judgment of 13 September 2005.
[11] See Liability SWD, ANNEX II.

Article 83(2) of the Treaty on the Functioning of the European Union establishes the legal basis for creating minimum rules for the definition of criminal offences and sanctions in a particular EU policy area. This expressly enables EU legislators to adopt: "minimum rules with regard to the definition of criminal offences and sanctions in the area concerned" if this "proves essential to ensure effective implementation of a Union policy in an area which has been subject to harmonisation measures".

The adoption of EU criminal law measures is therefore subject to the assessment of whether they are "essential" to achieving effective policy implementation. As such, the decision to include breaches of the OSD under the scope of criminal law can only follow a thorough necessity and proportionality test on whether criminal law measures would be essential to achieve the stated objective. This cannot be done before the OSD in its current form has been transposed in national law of Focal States and some experience with its effectiveness has been gained.[12] Member States have not yet decided on the penalties for infringements of the national laws transposing the OSD; they had until 19 July 2015 for the OSD transposition and any such decision may be made in that context or in the process of law implementation following the transposition. It is therefore too early at present to assess whether penalties to be devised by Focal States in the context of the OSD transposition and subsequent implementation will provide sufficient deterrence consistently across the EU, or whether EU criminal penalties would be essential to ensure the fully effective safety of offshore operations.[13]

If it were to be determined in the future that the OSD in its present form cannot sufficiently ensure the safety of offshore operations as intended, and that it is essential to link its aims with criminal liability for offshore breaches, such liability could be introduced as a new provision in the OSD through an amendment of that Directive. It could also be introduced through a standalone new legal act. However, the most coherent way would be to harmonize criminal sanctions through the ECD. This would avoid creating a different standard for criminal sanctions compared to the one established by the ECD for many environmental offences. It is why Article 39(3) of the OSD foresees the criminalization of offences under the OSD via an amendment of the ECD. In practical terms, this would mean amending Annex A of the ECD to include the OSD in its listing of legislation the infringement of which constitutes unlawful conduct.

[12] Communication from the Commission: Towards an EU Criminal Policy: Ensuring the Effective Implementation of EU Policies through Criminal Law ', 20 September 2011, COM (2011) 573, available at http://ec.europa.eu/justice/criminal/files/act_en.pdf.

[13] The Commission shall, no later than 19 July 2019, report on the experience of implementing this Directive pursuant to its Article 40.

Conclusions and proposals

Article 39 of the OSD tasks the Commission with examining the appropriateness of bringing certain conduct leading to a major accident within the scope of the ECD. However, at this point in time, it is too early to properly assess whether EU criminal law measures would be essential to achieving effective levels of offshore safety in the Union. In order to conclude whether certain conduct leading to a major accident should be brought under the scope of the ECD, the EU must gain some experience with the OSD's effectiveness.

The Commission will prepare a first implementation report on the OSD by 19 July 2019. It will be important that the Commission returns to this subject at that time, and for Member States determine if it is appropriate to bring conduct leading to a major accident within the scope of the ECD. In the meantime, the Commission can arrange for Member States to share their experiences regarding criminal penalties and risk management in undertakings from a broad range of economic activities.

In accordance with the above conclusion, the rest of this report deals only with civil and environmental liability for offshore accidents.

LIABILITY REGIME EFFECTIVENESS

The effectiveness of liability regimes can be judged by how clearly they define: a) who is liable; b) for what kinds of damage and loss; and c) to whom.

a) Who is liable?

The OSD introduces in this regard two important points of harmonization.

First, it always channels the liability to the licensee (i.e. the holder or joint holders of an authorization for oil/gas prospection, exploration and/or production operations issued in accordance with Directive 94/22/EC). It is important that the OSD establishes this principle as it provides full legal clarity and should ensure that licensees take primary responsibility for controlling the risks they create through their operations.

Second, as regards environmental damage from offshore accidents, provisions introduced by the OSD include offshore operations under the ELD. [14] This means that strict liability now always applies for environmental damage – i.e. every licensee is henceforth liable for such damage without the need to prove negligence on their part as long as a causal link is established.

Whilst the OSD has harmonised these two aspects of liability for offshore accidents, it has not provided for harmonization with respect to civil damage. Here, offshore accidents mostly fall under the tort law of Focal States and there are significant differences in the way national laws deal with licensees who have caused civil damage through negligence compared with licensees whose actions have not breached a standard of due care.

While the establishment of a causal link between the activity and the damage is always necessary, the negligence rule often applies which means that courts must first rule that the liable party breached a standard of care in order for civil liability to arise and for corresponding damages to be awarded.

[14] Article 7 of the OSD amends the ELD to make licensees financially liable for the prevention and remediation of environmental damage as defined in the latter Directive.

Whether the negligence rule or strict liability applies for civil damage varies from country to country depending on the kind of damage and loss[15].

b) What are they liable for?

Liability for *environmental* damage from offshore accidents is available throughout the EU on the basis of the ELD. This legislation also sets the extent of damage to be remedied and compensated. Accordingly, the licensee(s) will be held liable for damage to protected species and natural habitats as defined in the Birds[16] and Habitats[17] Directives, as well as damage to water as defined in the Water Framework Directive[18] and the Marine Strategy Framework Directive[19] anywhere in the EU. They will have to compensate public authorities for any work done to restore the environment to its baseline condition, or do this work themselves.

Whilst EU law harmonizes liability for environmental damage, and whilst the law in Focal States always provides for claims for bodily injury and property damage from offshore accidents, liability for different kinds of economic loss varies significantly. For example, the law in Focal States differs on how directly related an economic loss claim must be to an accident in order to be compensable ("directness provisions"). The law of Focal States such as Cyprus and the United Kingdom excludes outright economic loss claims in the absence of bodily harm or property damage (the "exclusionary rule").

There are also differences in whether and how the legislation in Focal States deals specifically with industry sectors that rely on the good condition of the shared marine environment for doing business, such as the fishing industry. Experience has shown that these sectors, which often include many small and medium-sized enterprises, could suffer significant economic loss in the event of a major offshore accident[20].

Norway has in this regard put in place perhaps the most comprehensive legislation to deal with civil liability for offshore pollution. This not only imposes strict liability for bodily injury, property damage and economic loss, including pure economic loss[21], it also specifically states that "financial losses incurred by Norwegian fishermen as a result of petroleum activities" are compensable[22].

c) To whom are they liable? Who can claim for compensation?

The right to compensation for damage suffered can be based on legal provisions (the general rule in the offshore sector) or contractual provisions and is in principle awarded following a claim introduced by the affected party. In specific cases, compensation can also be 'automatic' (little action necessary

[15] A full description of these differences can be found in Table 2 and Annex III of the Liability SWD.
[16] Directive 2009/147/EC of the European Parliament and of the Council of 30 November 2009 on the conservation of wild birds, OJ L 20 of 26.1.2010, p.7.
[17] Council Directive 92/43/EEC of 21 May 1992 on the conservation of natural habitats and of wild fauna and flora, OJ L 206 of 22.7.1992, p.7
[18] Directive 2000/60/EC of the European Parliament and of the Council of 23 October 2000 establishing a framework for Community action in the field of water policy, OJ L 327 of 22.12.2000, p. 1.
[19] Directive 2008/56/EC of the European Parliament and of the Council of 17 June 2008 establishing a framework for Community action in the field of marine environmental policy, OJ L 164 of 25.6.2008, p. 19.
[20] Economic loss claims made up to 96% of claims from the Gulf Coast Claims Facility following the 2010 Deepwater Horizon incident in the United States.
[21] Albeit with limitations stemming from the need to establish that the economic loss suffered was sufficiently direct.
[22] See Annex III of the Liability SWD.

from the affected party), for instance within "opt-out" types of class actions[23] or where legal or contractual provisions specify so.

As defenders of the common interest, public authorities bring claims against liable parties for environmental damage. In the case of civil damage and loss, any legal or natural person suffering damage or loss from offshore operations has a right to bring a claim, as equal treatment under the law is a central tenet in the Focal States.

However, there are legitimate questions as to whether, and to what degree, tortfeasors are liable to claimants in other countries harmed by their operations. Here, three interdependent questions must be resolved:

1. Jurisdiction: Which court/s should try the case?
2. Choice of law: What law/s should that court apply?
3. Foreign judgements: Will a judgment be recognised or enforced in another country?

Two existing EU regulations address these questions. With regards to the question of jurisdiction, the Brussels I Regulation[24] grants victims of offshore accidents the right to bring proceedings against defendants domiciled in the Union in either the country in which the defendant is domiciled, the country in which the accident occurred or the country in which the damage was sustained. These rules also apply in Norway and Iceland on the basis of the 2007 Lugano Convention[25].

This means, for example, that a (natural or legal) person in the Netherlands who suffered damage from an offshore accident caused in the UK waters by an Italian company may choose to pursue compensation in the courts of either the Netherlands, the UK or Italy, depending on where they thought they would get the most suitable treatment and outcome.

With regards to the second and third questions on choice of law and foreign judgements, under the Rome II Regulation,[26] the law governing non-contractual liability arising out of offshore accidents is the law of the country in which the damage occurs, irrespective of where the accident occurred. If the damages claimed are environmental damage or damage sustained by persons or property as a result of such damage, victims may also choose to rely on the law of the country in which the accident occurred. It should be noted that the applicable law may be the law of a Member State or of a third country outside the EU[27].

This means, for example, that a Norwegian claimant for damage from an oil spill resulting from an offshore accident in the Netherlands may choose to pursue compensation under either the laws of Norway or the Netherlands, depending on which would be most favourable to them.

Assessment of the effectiveness of liability regimes and the appropriateness of broadening liability provisions

[23] Where one or several named plaintiffs make a claim on behalf of a proposed class of individuals or business entities that have suffered a common injury or injuries, and individuals must file a request for their exclusion from the class should they not wish to be automatically included.
[24] Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. OJ L 012 of 16 January 2001.
[25] Convention on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, 2007. See Section 2.10 of the Liability SWD.
[26] Regulation (EC) No. 864/2007 of the European Parliament and of the Council on the law applicable to non-contractual obligations. OJ L 199 of 31.7.2007, p.40. The Regulation does not apply to Denmark.
[27] See Section 2.10 of the Liability SWD.

As sketched out above and described in detail in the Liability SWD, liability for bodily injury and property damage is already available in the Focal States and environmental liability has been harmonised through EU legislation. However, Focal States approach civil liability for offshore accidents in different ways and may limit it to different degrees. For example, whereas the laws of Cyprus and the United Kingdom tend to impose greater limitations on liability by requiring a proof of negligence or of the directness of economic loss suffered, the laws of other Focal States such as Denmark, France, Iceland the Netherlands and Norway are more favourable to claimants[28].

However, it is important to note that, in spite of the differences between Focal States, it is difficult to clearly identify any as being less effective in dealing with possible claims arising from offshore accidents.

The situation in at least some national regimes may also be changing: several Member States have indicated in contacts with the Commission (including in meetings of the EU Offshore Authorities Group - EUOAG[29]) that they may reappraise their existing liability regimes for offshore accidents in tandem with the obligation to put in place compensation procedures pursuant to Article 4(3) of the OSD. Whilst changes to the handling of civil liabilities are not explicitly required by the Directive, liability and compensation are closely related issues, and changes to one may necessitate changes to the other. The obligation under Article 4(3) of the OSD may thus lead to a broadening of liability provisions in some Focal States.

Broadening liability provisions at EU level could entail making strict liability apply to more categories of civil damage and loss in the Focal States and/or making more kinds of economic loss available for compensation – particularly the kinds of economic losses likely to be sustained by the fishing sector and local coastal economies (such as in seaside tourist destinations). Where a degree of ambiguity in the relevant legal texts makes some economic loss claims uncertain, the legislation could be clarified with specific reference to the kinds of damage likely to result from offshore accidents and/or the parties likely to be affected. Finally, while existing laws appear comprehensive as regards access to justice across borders, broadening liability provisions could entail making redress more accessible for offshore damage claimants by introducing the possibility of opt-out class actions for offshore accidents.

It can be argued that holding firms accountable for *all* damage and loss caused by offshore accidents facilitates access to justice for victims. It incentivizes firms to take adequate precautions and develop safer ways of operating. It also helps ensure that offshore activities only take place if their benefits outweigh their risks.

However, limiting liability is a practical necessity. Most notably, oil spill claims litigation can be complex and a balance needs to be struck between the need to compensate victims adequately and preventing the payout of 'illegitimate' claims. Economic losses are likely to be serially linked to one another in the economy and so well-defined liability parameters are essential to preventing excessive liability – also known as the floodgates issue[30] – in the interest of the desirable exclusion of more indirect, speculative claims. Legal traditions determine how the justice systems of Member States distinguish between legitimate claims and ordinary risks faced by participants in the economy.

[28] More details in Section 2.2 and Sections 2.5 to 2.7 of the Liability SWD.
[29] Commission Decision of 19 January 2012 on setting up of the European Union Offshore Oil and Gas Authorities Group, OJ C 18 of 21.1.2012, p. 8.
[30] Impossibility to prevent remote claims that society would not view as legitimate but that would be likely to succeed.

Conclusions and recommendations

Whilst there are national differences in the way liability regimes govern access to justice for victims of offshore accidents, no clear case can be made at the present time that any of the current approaches to civil liability in the Focal States is less effective in reinforcing the OSD's aim of ensuring the safety of offshore oil and gas operations across the EU.

However, it is clear that the transposition of the OSD in national law will prompt Member States to explore in which ways their liability rules will best protect general public interest in line with the compensation requirements of Article 4(3) of the OSD. Because ensuring the adequate handling of compensation claims may entail changes to the liability regime giving rise to compensation, some Member States may revise their national regimes for determining the extent of liability from offshore oil and gas operations.

When reviewing their liability regimes in the context of implementing the OSD in national law, Member States should also consider adopting provisions specifically for economic sectors most vulnerable to offshore accidents without introducing the widespread uncertainty on financial responsibility levels that might impede the development of offshore oil and gas resources. These efforts should be tailored to the substantial national differences in the economic benefits and risks derived from offshore operations that exist, as well as the industries exposed to offshore accidents in different Member States. For example, Member States with significant offshore activities as well as large fishing and/or coastal tourism sectors should examine whether a reinforcement of economic loss provisions specifically for these sectors, as for example Norway has already done for its fishing sector, would be desirable.

Furthermore, the Brussels I and Rome II regulations mean that Focal States must factor into their financial security requirements the potential damages that their licensees and operators could incur in other jurisdictions. These damages could be much larger than the damages incurred domestically due to the large geographical footprint of major accidents and the possibility of more stringent civil liability rules in other jurisdictions.

The Commission is well placed to raise awareness of these specific transposition issues through fora such as the EU Offshore Authorities Group (EUOAG), together with national authorities, the oil and gas industry, other industries and civil society. It has regularly brought the discussion on the agenda of EUOAG meetings and will continue to do so through targeted seminars and structured best practice exchange sessions.

However, the Commission should go beyond stimulating discussions with stakeholders and ensure that all Member States address the points raised above through conformity checks that are focused on the relevant liability and compensation provisions in the OSD. In parallel, the Commission will use EUOAG meetings for systematic data gathering covering all liability-related aspects of the Member States' newly transposed laws.

These three measures will allow the Commission to include in its first implementation report a comprehensive analysis of the changes to individual national regimes specifically with respect to the effectiveness of liability provisions. On the basis of this, the Commission should be well placed to conclude on the need for further steps.

FINANCIAL SECURITY INSTRUMENTS AND THEIR AVAILABILITY

Once liability is established, the question naturally turns to how the tortfeasor will finance the damages they are liable for. Deepwater Horizon showed that the worst offshore accidents can cause such great damage that only the largest firms would be able to fully absorb their costs. This raises questions about the existence of financial security instruments that will ensure compensation is available, and companies remain solvent, following a major accident.

There is broad variety of financial security products available to hedge oil and gas companies' operating risk. These range from self-insurance options[31], to third-party insurance[32], to mutual schemes such as the Offshore Pollution Liability Association Ltd (OPOL)[33], to alternative risk transfer mechanisms[34] and others.

Text Box: OPOL

The Offshore Pollution Liability Association Ltd (OPOL) is an industry mutual agreement open to offshore operators in many Focal States. Member companies benefit from a guarantee that other companies in the scheme will pay for any liabilities they are financially unable to pay for themselves up to set financial limits ($125 million for remediation costs and $125 million pollution damage). Following an incident, claims are not made directly against OPOL itself, but against the member company liable for damage and loss.

OPOL is not a compensation fund nor is it a guarantee against a company's bankruptcy for the company itself. This mutualisation of insolvency risk borne by the third parties helps reduce insurance costs and reassure regulators and the public of the financial capacity of offshore licensees. The criteria on OPOL membership also adds a layer of industry mutual monitoring that complements the regulatory scrutiny of companies' financial capacity at licensing.

OPOL membership requires operators to accept strict liability for damage and loss and is a prerequisite of licensing in the UK. Membership of the scheme also satisfies Ireland's licensing terms for offshore operations. However, OPOL's $250 million cap on reimbursement and compensation per incident may not cover all damage and loss from the worst accidents.
More details in Sections 2.3 and 4.2 of the Liability SWD.

Whilst not all of these products may currently be in widespread use by the offshore industry, the marketplace for financial security instruments appears to have the depth and innovation necessary to cater to all oil and gas companies operating under the current EEA liability obligations. It also allows oil and gas companies to spread their risk to a diversity of market actors, from insurers and reinsurers, to financial market actors such as private equity groups and hedge funds, as well as to other oil and gas companies.

In spite of this, there is currently a lack of uptake of financial security instruments to cover all damage from the most infrequent and costly offshore accidents. There could be several reasons for this, one of which has already been discussed in this report: the scope of liability for damages may not in certain Focal States make such products necessary at present.

Another key contributing factor is that many Focal State regulators limit what forms of coverage they accept, precluding outright the provision of a range of innovative solutions. Twelve out of twenty

[31] Liability SWD, pp. 35-36.
[32] Liability SWD, pp. 36-38.
[33] Liability SWD, pp. 40-41.
[34] Liability SWD, p. 41.

Focal States explicitly specify insurance as a financial security mechanism for licensing and/or operations, of which nine do not specify any other type of mechanism. This high proportion of Focal States that favour insurance may be even higher because the model contractual agreements for six Focal States were not available for review[35].

This prevents a full understanding of the extent to which other factors may be limiting the development of financial security instruments for offshore liabilities. These other factors may include a lack of regulatory requirement for appropriate levels of coverage. Coverage may be beyond individual insurers' capacities, or the availability of reinsurance on the market. Alternatively, where coverage is available, insurers and the offshore industry may be unable to agree on risk levels and therefore a price for these products, leading to their non-provision.

This situation is likely to change with the implementation of the OSD. Articles 4(1) to 4(3) of the OSD put in place exposure-based financial security requirements, obliging Member States to take due account of license applicants' "financial capabilities, including any financial security, to cover liabilities potentially deriving from the offshore oil and gas operations in question".

In addition, Article 4(3) of the OSD also requires Member States to "facilitate the deployment of sustainable financial instruments and other arrangements to assist applicants for licences in demonstrating their financial capacity". Several steps could be taken here, including broadening the forms of coverage accepted by national authorities.

The provisions in the OSD are further echoed by Offshore Protocol of the Barcelona Convention, which has recently become a part of the EU acquis.[36] This Protocol stipulates in its Article 27(2)(b) that Parties shall ensure that operators have and maintain insurance cover or other financial security for damages caused by activities covered by the Protocol.

The experience of the ELD shows that a competitive market for financial security instruments – pools, insurance, bonds, guarantees etc. – can develop following a significant EU regulatory change, albeit with a time lag to allow for market players to adjust to the new requirements.[37] The availability and uptake of financial security instruments for offshore accident risk can therefore be expected to improve in the years following the implementation of the OSD in national law.

Conclusions and recommendations

Although financial security instruments to cover all damage from the most infrequent and costly offshore accidents are not readily available from the insurance market, the market appears to have the depth and innovation necessary to cater to all oil and gas companies operating under the current EEA liability obligations. Furthermore, the market for financial security instruments can be expected to adapt to new requirements introduced by Article 4 of the OSD, particularly if national authorities broaden the forms of financial instrument coverage they accept. Such anticipated changes should be seen following the July 2015 implementation deadline for the OSD and the implementation of the

[35] See Liability SWD, Section 3.2.

[36] Council Decision of 17 December 2012 on the accession of the European Union to the Protocol for the Protection of the Mediterranean Sea against pollution resulting from exploration and exploitation of the continental shelf and the seabed and its subsoil (2013/5/EU), OJ L 4 of 9.1.2013, p.13.

[37] Report from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions under Article 14(2) of Directive 2004/35/CE on the environmental liability with regard to the prevention and remedying of environmental damage, 12/10/2010, COM(2010) 581 final.

Offshore Protocol of the Barcelona Convention. The Commission will make the full implementation of Article 4 a priority area of scrutiny in the conformity checks for the Directive.

The decision on whether to accept or require membership of a mutual insurance scheme like OPOL for offshore licensing is best left to Member States as it is closely linked to their national liability regimes, the characteristics of the scheme in question, the licensees in their waters and the risks faced by these licensees. The significant regional differences in offshore operations within the EEA – and therefore the kinds and levels of risk faced by operators – might lead to an unjustified cross-subsidization of risk between these regions and potential moral hazard in case of a one-size-fits-all solution.

HANDLING COMPENSATION CLAIMS

Having established the extent of liability and ensured the capacity to finance the compensation due for the damage either from a company's own resources or through a financial instrument, the final piece of the puzzle is how to disburse this compensation so that it reaches legitimate claimants quickly. The 2010 Deepwater Horizon disaster showed that major offshore accidents can affect a large number of people and stretch the resources of any scheme set up to process claims and provide compensation to victims. It demonstrated the importance of proactively putting in place well thought through compensation mechanisms before major accidents occur to minimize the cascading effects of loss through the economy.

There are just two compensation mechanisms currently in place specifically for oil and gas accidents in the Focal States. First, Norway has established a legislative compensation mechanism to deal with offshore accidents. Its Petroleum Activities Act codifies rules for managing aggregated claims and compensation to fishermen. The legislation also provides for transboundary claims from Denmark, Finland and Sweden, as established by the Nordic Environmental Protection Convention[38].

Second, OPOL, although primarily an industry mutual agreement, also outlines procedures aimed at expediting claims without the resort to court proceedings. An important shortcoming of the OPOL compensation scheme, however, is its stipulation that the liable operator decides whether claims against them are applicable under the OPOL agreement in the first instance [39].

In the absence of a purpose-built compensation scheme for offshore oil and gas accidents, claims would proceed under national tort law. Here, civil rules of procedure apply[40] and cases can be expected to last for between six months and several years (decades in some cases) if they are not settled outside court. Whilst Belgium, Italy, Portugal and the Netherlands have recently adopted new legislation to simplify mass claims, even this could be streamlined further to better handle the specific forms of damage an offshore accident might cause and the needs of the sectors likely to be affected – fishing and tourism, in particular[41].

Whilst there are currently very few compensation regimes for offshore accidents in the EEA, this situation should change significantly with the implementation of the OSD. Pursuant to Article 4(3) of the OSD, Member States are obliged to put in place procedures for ensuring the prompt and adequate

[38] See Liability SWD, Section 4.1.
[39] See Liability SWD, Sections 2.3 and 4.2.
[40] The rules that courts follow when adjudicating civil lawsuits.
[41] More details in the Liability SWD, Section 4.3.

handling of compensation claims, including transboundary claims, as far as liability is provided by national law. There may be several ways to improve on the current provisions. These include:

- independent claim-handling;
- equal treatment for transboundary claims;
- refining the accessibility, clarity and simplicity of claim procedures;
- clear accountability for claims management responsibility;
- pre-defined timing obligations that minimize delay; and
- means for redress in the case of system failures.

Conclusions and recommendations

Whilst there are just two compensation mechanisms currently in place specifically for oil and gas accidents in the Focal States, the OSD obliges Member States to put in place procedures for ensuring the prompt and adequate handling of claims. The Commission can, by working together with Member States, help achieve adequate safeguards for claimants in this regards. Should the new national compensation schemes not succeed in establishing adequate safeguards for victims of offshore accidents and fully reflect the rights of transboundary claimants under Brussels I and Rome II, there may be a need for the Commission to reassess in or after OSD's first implementation report whether and what further EU action could achieve these objectives.

OVERALL CONCLUSIONS

The effects of the OSD, as implemented by Member States, will show in the coming years whether it is appropriate to bring certain conduct leading to major offshore accidents within the scope of criminal law for further re-enforcing offshore safety. When appropriate, the Commission will put forward a legislative proposal.

Broadening liability provisions through EU legislation does not appear appropriate at this juncture. In certain cases, the Brussels I and Rome II regulations prevent differences in national regimes from disadvantaging claimants from other EU Member States. In addition, some Member States may be reappraising their existing liability regimes for offshore accidents in tandem with other changes introduced by the OSD.

However, the Commission will be able to conclude on the need for further steps by the time of the OSD's first implementation report. Notably the Commission can:

- continue to advance liability issues through structured EUOAG discussions;
- focus on liability-related provisions in the OSD conformity checks; and
- use EUOAG meetings for systematic data gathering covering all liability-related aspects of newly transposed laws.

There is currently a lack of uptake of financial security instruments to fully cover the more infrequent and costly offshore accidents in the EEA. In addition, there are just two compensation mechanisms currently in place specifically for oil and gas accidents in the Focal States. However, provisions in the OSD should lead to significant improvements in both of these areas.

Should the new national laws not improve the availability of financial security instruments and put in place procedures for ensuring prompt and adequate handling of compensation claims, the Commission will reassess whether and what further EU action could achieve these objectives.

The Commission encourages Member States to share their experiences on financial security instruments, liability, compensation and criminal penalties, first of all, in the framework of the European Offshore Authorities Group. After the implementation of the Directive and based on experiences of Member States working with the new legal basis the Commission may update its assessment as provided by this report.