In confidence

Office of the Minister of Energy and Resources and Office of the Associate Minister of Transport

Chair, Cabinet Economic Development Committee

Strengthening the financial assurance regime for offshore oil and gas installations

Proposal

1. This paper seeks agreement to policy proposals to strengthen requirements on owners of offshore oil and gas installations to have insurance, or other financial assurance, for their liabilities for pollution damage resulting from an oil spill.

2. The paper seeks approval to introduce the Maritime Transport (Offshore Installations) Amendment Bill to implement some of the proposed changes. Other proposals will be implemented through amendments to the Marine Protection Rules Parts 102 (relating to financial assurance requirements) and 131 (relating to marine oil spill contingency), which will be made by the Associate Minister of Transport.

Executive summary

3. There has never been a significant oil spill from an offshore installation in New Zealand waters. While the likelihood of a spill is very low, we need to prepare for such an event by ensuring we have an effective financial assurance regime for offshore oil and gas installations.

4. We recommend that the Cabinet Economic Development Committee approves the following proposals to strengthen the requirements on owners of offshore oil and gas installations to have insurance, or other forms of financial assurance, for their liabilities under Part 26A of the Maritime Transport Act 1994 (the MTA) for pollution damage resulting from an oil spill:

    4.1. Owners require a certificate of insurance providing financial cover to an amount, based on a scaled framework, related to an estimate of the cost of a credible worst-case spill for each of their installations. The cost estimate and scaled framework will take account of factors influencing the pollution damage resulting from an oil or gas spill, including: geology; depth of water; and type of hydrocarbon.

    4.2. That the upper limit of the financial cover required under the scaled framework will be $1.2 billion. This reflects the modelled uppermost estimate for clean-up costs from an oil spill. For existing installations, and planned exploration activities, the amount of assurance that will be required under the scaled framework is likely to be lower than this proposed limit (instead of the current arrangements, which require fixed cover of at least NZ$27.7 million).[1] The proposed upper limit will future-proof the scaled framework in the event that a new installation proceeds in a higher-risk, deep water location.

[1] All figures are in New Zealand dollars, unless otherwise specified.

4.3. The Crown and affected third parties can bring a direct claim under an insurance policy, or other financial assurance, against the party providing financial assurance to an owner of an offshore installation

4.4. Owners are able to meet assurance obligations using insurance policies, available from the international market, that cover the key risks (e.g. well blow-out, pipeline rupture) associated with their operations and are consistent with internationally available best practice policy wording.

4.5. Third parties are still able to make claims under the insurance contract, but these claims are limited to the scope and quantum of the policy agreed between the owner and insurance provider, which has been approved by the Director of MNZ, in accordance with the Marine Protection Rules (MPR) – Part 102. This reverses the current provision – instead of the insurer standing in the shoes of the insured, the claimant would now stand in the shoes of the insured.

4.6. In addition, owners are required to provide financial assurance for the cost of well control.

4.7. Any insurance policies provided for under this regime must be consistent with New Zealand's relevant insurance legislation and subject to the jurisdiction of New Zealand courts.

4.8. From the date the regime comes into force (likely to be mid-December 2019), new installations will have three months to comply with the new regime, and existing installations will have up to 31 July 2020 to comply.

5. These proposals are designed to address issues with the current offshore financial assurance (OFA) regime which:

5.1. requires insufficient assurance relative to the potential risk and impact of an oil or gas spill;

5.2. provides a wider scope of liability under the MTA than is generally insurable in the international insurance market, making it challenging for owners to secure insurance even at the very low level currently required; and

5.3. contains no direct financial assurance requirements on owners for well capping and containment.

6. Amendments are required to the MTA and the MPR Parts 102 and 131 to give effect to the recommended changes to, and clarify the implementation requirements of, the offshore assurance regime. All other elements of the current offshore financial assurance regime will remain the same.

7. The proposed changes to the offshore financial assurance regime have been developed following significant consultation with stakeholders, including the insurance and oil and gas industries, since 2017. They also draw on decisions made by the previous government that were not brought into force prior to the 2017 general election.

8. Owners and insurers support increased levels of financial assurance[2] being required, and consider that insurance should be able to be secured if the scope of an insurance policy can be relied on.

9. An environmental stakeholder has conveyed that they support the objectives that sit behind the proposed changes to the regime, and increasing the upper limit of financial assurance required. They consider that the upper limits discussed, ranging from $800 million to US$1 billion were too low. They, however, also recommended that the regime go further to protect claimants from pure economic loss.

10. Our recommendations fulfil the objectives for the regime, in that: owners will provide assurance proportionate to the modelled consequences of a credible worst-case scenario spill; the Crown, and other parties, are protected from significant financial risks; and, the requirements on owners are clear and insurable. They are also consistent with practice in other jurisdictions.

11. In order to deliver an insurable financial assurance regime, with significantly higher levels of assurance, the paper proposes to limit the scope for third party claims against those providing assurance (including insurers). This means that third party loss of profit from impairment of the environment resulting from an oil spill at an offshore oil and gas installation, that does not result from damage to that person's property (referred to as pure economic loss), will be excluded from the scope of the financial assurance regime. This approach is necessary because officials and the insurance market have not been able to identify a credible method of including coverage for pure economic loss claims into the recommended assurance requirements.

12. As owners retain unlimited liability for losses within the scope of Part 26A of the MTA, third parties retain an existing avenue to seek redress for any loss. This recommendation is in line with the previous government's proposed rule amendments to the OFA regime, which were agreed but not brought into force prior to the 2017 general election.

13. Financial capability tests are applied to owners under the Crown Minerals Act 1991 (CMA) when a permit is awarded. These tests also provide a level of assurance that owners are capable of meeting some of their financial obligations before insurance is drawn down. [redacted]

Withheld due to active consideration

Background to the current regime and previous policy considerations

14. There has never been a significant oil spill from an offshore installation in New Zealand waters. Although the likelihood of a major marine oil spill is very low, the environmental, financial and cultural impacts of such an incident are likely to be significant.

15. There are six producing fields in New Zealand. The exact risks of an oil spill posed by these fields are dependent on various factors, including the location and type of activity being undertaken.

[2] A higher limit of US$1 billion was also discussed as a possibility, however, the limit of $800 million was the focus of discussions during stakeholder engagement.

16. New Zealand's regulatory regime for offshore oil and gas installations exists to ensure essential protections, such as those to mitigate environmental risks, are in place, while capturing the economic benefits of these activities.

17. We use a prevention-control-response-recovery framework to regulate offshore oil and gas exploration and production. This includes ensuring permit holders have plans, resources and capabilities in place to minimise hazards and the likelihood of a spill, and reduce the impacts if an adverse event does occur.

Owners have unlimited liability for pollution damage should a spill occur – and this will not change

18. Under Part 26A of the MTA, owners of offshore oil and gas installations (usually the permit holders)[3], have unlimited liability for the cost of pollution damage resulting from a spill at their facilities in New Zealand waters. This means that anyone affected by oil damage from an offshore installation is entitled to make a claim.[4] This liability includes the cost of measures to prevent or reduce pollution damage; the cost of reasonable measures to reinstate the environment; and the loss of profit from impairment of the environment (these are covered in sections 385B and 385C of the MTA).

19. An assurance regime, with a low minimum requirement, is in place to provide confidence that some of an owner's potential liabilities are guaranteed and to mitigate financial risks to the Crown and other parties,[5] should the operator be unable or unwilling to meet their liabilities. The key principle of this regime is that assurance is provided by a third party.

20. Since 1998[6], offshore oil and gas installation owners have been required to obtain a "Certificate of Insurance" from the Director of Maritime New Zealand (MNZ), (under section 385H of the MTA) that certifies that they have complied with financial assurance requirements.

21. MPR Part 102, and associated guidance, set out the requirements operators must meet for the Director to issue a Certificate of Insurance. MPR Part 102 requires owners to demonstrate they have third party financial assurance to cover their liabilities in the event of an oil or gas spill, for a sum not less than 14 million International Monetary Fund (IMF) Units of Account (approximately $27.7 million)[7].

22. Under current arrangements, owners most commonly meet their assurance obligations through an insurance policy, financial bond or a parent company guarantee.

23. These protections are in place to reduce the risk that pollution damage costs will fall on the Crown, or other affected parties, particularly as the immediate response to an oil or gas spill will likely be coordinated by government agencies, such as MNZ.

24. While it does not replace or limit an owner's unlimited liability for pollution damage under the MTA, the OFA regime seeks to provide confidence that owners can meet their potential

[3] Usually the holders of prospecting, exploration or mining permits under the Crown Minerals Act 1991.
[4] Including the Crown and marine agencies (e.g. MNZ and regional councils).
[5] Particularly as the immediate response to an oil and gas spill will likely be coordinated by government agencies, such as MNZ.
[6] In 1998, this requirement was in section 364 of the MTA 1994.
[7] Based on exchange rates as at April 2017.

liabilities to a specified level. The current minimum requirement of $27.7 million is, however, highly unlikely to cover the full extent of an owner's MTA liability in the event of any spill of more than minimal size.

Other protections exist to prevent, and manage, oil spills

25. MPR Part 131, prevents offshore installations operating unless they have an oil spill contingency plan approved by MNZ.

26. An oil spill contingency plan must identify and assess risks, and ensure that appropriate prevention measures are in place. Where relevant to the nature of the operation, the plan will cover the owner's arrangements for well capping and/or well containment. However, when a plan is approved there are no specific requirements in MPR Part 131 to consider the owner's ability to fund the plan, or for the owner to provide financial assurance to cover the costs of implementing the plan.[8]

27. [redacted]

Withheld as commercially sensitive

28. Under the CMA regime, permit applicants are required to demonstrate that they are financially capable of giving effect to an agreed work programme. Financial capability assessment of an applicant includes consideration of other firm obligations, assets and sources of revenue. These financial fitness tests are applied at the time an owner applies for a permit, prior to commencement of drilling or oil and gas extraction. This provides a level of assurance that owners are capable of meeting some of their financial obligations before insurance is drawn down.

29. [redacted]

Withheld due to active consideration

Improvements to the OFA regime have been under discussion for some time

30. The OFA regime (specifically, MPR Part 102) has been under review since 2011. Public consultation on previously proposed changes to the regime was undertaken twice in 2017, and again in 2018.

31. The drivers behind the ongoing policy work have been, and remain: concerns that the regime provides insufficient third party assurance relative to the potential risk and impact of an oil or gas spill; and, the insurability of the assurance regime (these issues are discussed further in paragraphs 39-41 below).

32. In 2017, the key proposals consulted on were:

[8] MNZ undertakes financial due diligence in regards to the plan feasibility using a provision in the MTA requiring the holder of a Maritime Document to possess the means to execute the functions covered by the document. The plan approval is a Maritime Document.

32.1. introducing a scaled framework for third party provided assurance requirements[9], ranging from $25 million to $800 million, depending on the level of risk posed by an operation; and[10]

32.2. refining the scope of liabilities, to exclude claims for pure economic loss or compensation for the broader impairment to the environment, to align with insurance products available in the energy market.

33. The 2017 proposals above were approved by the previous government, including an upper limit to a scaled framework of $600 million, and were included in an amendment to MPR Part 102, which was signed but not brought into force prior to the general election.[11]

34. In February 2018, Cabinet noted the intention to consult on increasing the maximum level of financial assurance required under the scaled framework from $600 million to $800 million, to better address the financial risk associated with a potential oil spill [CAB-18-MIN-0041 refers].

Industry representatives and insurers advise that the MTA makes the regime uninsurable

35. During consultation in 2017, oil and gas industry representatives and insurers were broadly supportive of those proposed changes to the assurance regime (for example, the scaled framework) but raised concerns about the insurability of the regime.

36. Industry representatives and insurers reiterated their views that the regime is uninsurable during consultation in 2018 on the detailed rule.

37. Stakeholders conveyed that the regime, in its current state, implies a requirement for a "financial guarantee", which when coupled with the higher amounts of assurance required, would make the regime uninsurable.

38. Insurers have said that financial guarantees to the quantum of several hundred million dollars cannot be obtained due to limitations imposed by insurance regulators and the risk appetite of the insurance market.

39. Further consultation in 2018 with the Insurance Council of New Zealand (ICNZ) supported these concerns. [redacted]

Withheld to maintain professional legal privilege

[9] To be determined by the Director of MNZ, under Part 102.
[10] The previous government had also consulted on an $800 million maximum, but decided to set the limit at $600 million because it aligned more closely with the Australian regime.
[11] Another reason it was not brought into force was to allow for the development of operational guidance to help offshore installation owners understand how to meet their obligations under the proposed regime.

[redacted]

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40. [redacted]

41. [redacted]

We want to clarify and strengthen the offshore financial assurance regime

42. Officials have been working with stakeholders, including the oil and gas industry and insurance representatives, to develop proposals to clarify and strengthen New Zealand's OFA regime.

43. Subject to the proposed transitional arrangements outlined in paragraphs 82-83, the intention is to have new arrangements in place as quickly as possible, and ideally during the 2019/20 summer. [redacted]

Withheld as commercially sensitive

44. The objectives for the OFA regime are outlined in figure one below.

Figure one: Objectives of an effective OFA regime

Owners provide assurance proportionate to their risk profile

- New Zealand is assured that owners provide assurance proportionate to the risk profile of their operations.

The Crown, and other parties, are protected from financial risk

- The risk is managed so that the Crown, or other parties, do not carry the cost of pollution damage.

Requirements on owners are proportionate to their risk, clear and insurable

- Balances the potential economic benefits and costs of the operation by placing reasonable and proportionate compliance costs on business.
- Requirements on owners, and insurers, are clear and insurable.

45. To ensure we meet these objectives, we need to address the following:

45.1. insufficient assurance requirements to meet potential clean-up costs associated with a credible worst-case spill;

45.2. a wide scope of liability, which would make the requirement uninsurable if higher levels of assurance were required; and

45.3. no specific assurance requirements for well control measures.

Issue 1: Insufficient assurance to meet potential clean up costs.

Context

46. Scenario modelling undertaken by Navigatus Consulting estimated that the median clean-up costs from a credible worst-case spill scenario could cost around $800 million. The uppermost (fifth quintile) estimate in the modelling for the clean-up costs from an oil spill at an offshore installation in New Zealand was $1.2 billion.[14]

47. Navigatus also estimated that oil spill clean-up costs from existing offshore production installations could be between $171 million and $361 million (excluding well-control, pure economic loss, or compensation for the broader impairment to the environment).

48. Under the MTA, and MPR Part 102, despite their unlimited liability for costs (sections 385B and 385C of the MTA), owners are only required to provide assurance for their statutory liabilities to a minimum of 14 million IMF Units of Account (approx. $27.7 million).

Impact

49. Despite the unlimited liability for owners under the MTA, and depending on the operation, there is likely to be a significant gap between the minimum level of assurance currently required, and the potential cost of pollution damage and other covered losses from an oil or gas spill.

50. [redacted]

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Issue 2: Wide scope of liability, making insurance hard to secure

Context

51. Section 385J of the MTA enables third parties to bring claims against those providing insurance, or other financial guarantee, for an owner's liability for pollution damage, beyond the financial limit and, arguably the scope, of the assurance provided. Effectively, the insurers stand in the shoes of the insured (owners) and would, potentially, have to meet claims that are un-quantified.

52. [redacted]

Withheld to maintain legal professional privilege

[14] Based on a modelled estimate for Deepwater Taranaki done by ocean modelling experts, Navigatus Consulting.

Withheld to maintain legal professional privilege

[redacted]

53. The MTA provision seeks to protect third parties in the event that the owner (insured party) does not make a claim from the insurer, or if owners become insolvent.

Impact

54. [redacted]

Withheld as commercially sensitive

55. [redacted]

Issue 3: No assurance requirements for well capping and containment

Context

56. MPR Part 131 requirements are not within the scope of Part 26A of the MTA and MPR Part 102. It does not specifically require financial assurance to cover the cost of well control measures (including capping/containment if appropriate) should a spill occur.

57. Initial estimates of the potential cost of well control measures where capping/containment are required in New Zealand waters, are between $120 million and $360 million.

58. Whilst some owners already insure for this type of loss, the financial assurance requirements for these activities are not as clear as they could be and amendments to the MPR Part 131 are recommended to address this.

Impact

59. A strong regime requires financial assurance to be held for both well control measures (MPR Part 131) and for clean up and compensation (MPR Part 102). Costs for well control are usually the first drawn down. By ensuring that there is assurance for MPR Part 131, we can have greater confidence that the financial assurance quantum held under MPR Part 102 can be preserved for clean-up and compensation. Without financial assurance for MPR Part 131, a necessary part of the regime will remain unclear, especially in terms of how it relates to the assurance required to be held to meet an owners' MPR Part 102 liabilities.

[15] Claims could relate to direct costs and indirect costs. Direct costs include direct pollution damage and associated costs, clean-up costs, preventative measures to reduce pollution damage. Indirect costs include loss of profit arising from impact to the environment, measures to accelerate natural recovery of the environment, non-market damages and damage to ecosystem services.

[redacted]

Withheld as commercially sensitive

Potential approaches for the offshore assurance regime

60. Drawing on the analysis above, we have considered two potential approaches (please refer annex one for a visual representation) to the OFA regime (excluding the status quo). Each approach seeks to address all of the three issues summarised above). The approaches have been developed following significant engagement with industry, the insurers and other stakeholders. While a limit to the scaled framework of around US$ 1 billion was discussed, an $800 million limit to the scaled framework was the focus of this engagement.

61. Both approaches:

    61.1. retain an owner's unlimited liability for pollution damage under Part 26A of the MTA;

    61.2. empower the making of marine protection rules:

        61.2.1. specifying the liabilities and amounts for which insurance or other financial security that must be held for a certificate of insurance to be issued; and

        61.2.2. to require insurance or other financial security to be held in respect of the costs of implementing a marine oil spill contingency plan;

    61.3. provide greater levels of financial assurance than status quo arrangements; and

    61.4. require insurance policies provided by owners to be consistent with New Zealand's relevant insurance legislation and subject to New Zealand's jurisdiction.

Approach one – a single tiered scaled framework

62. Owners have unlimited liability for pollution damage (as outlined in sections 385B and 385C of the MTA).

63. Owners require a certificate of insurance for the estimated cost of a credible worst case spill at an installation, based on a scaled framework, applied up to a maximum of $1.2 billion, for each of their installations.

64. The scope of section 385J of the MTA is amended, so that third parties are still able to be make claims under the insurance contract, but these claims are limited to the scope and quantum of the policy agreed between the owner and insurance provider, which has been approved by the Director of MNZ, in accordance with the MPR – Part 102. This reverses the current provision – instead of the *insurer* standing in the shoes of the insured, the *claimant* would now stand in the shoes of the insured.

65. Owners are able to meet assurance obligations by covering significant, insurable liabilities through insurance policy wording. For example, standard 'cost-of-control' policy wording, which will cover claims relating to clean up, third party property damage and loss of use of property.

66. These are aligned to covering the key risks (including well-out-of-control and pipeline rupture) associated with the operation, and that are consistent with international best practice policy wording. Standard cover does not cover pure economic loss, or compensation for the broader impairment to the environment.

67. Owners are required to provide additional financial assurance for well control measures outlined in their response plans (MPR Part 131).

68. Owners can meet their assurance obligations for MPR Parts 102 and 131 through a combined single limit insurance policy (i.e. cover all of their insurable liabilities under one policy) for each installation, provided that the single limit is assessed to provide sufficient cover for the individual components by the Director of MNZ.

Approach two – two-step scaled framework

69. Owners have unlimited liability for pollution damage (as outlined in sections 385B and 385C of the MTA).

70. Owners require a certificate of insurance for the estimated cost of a credible worst case spill at an installation, based on a scaled framework, applied up to a maximum of $1.2 billion, for each of their installations.

71. The scope of section 385J of the MTA is amended, so that third parties claims rights are limited to the scope and quantum of the policy agreed between the owner and insurance provider, which has been approved by the Director of MNZ, in accordance with the MPR – Part 102.

72. The difference with this approach is that insurance requirements will have two parts. The first part will have a base level of cover up to the current minimum requirement of $27.7 million, the scope of this part of the assurance must cover all of the owner's liabilities under Part 26A of the MTA. The second part will follow approach one – where owners can use internationally available policy wordings to cover their main risks.

73. Owners required to provide financial assurance for well control measures outlined in their response plans (MPR Part 131).

74. The table overleaf analyses each scenario against the objectives of the OFA regime.

Option	Objectives		
	Provide assurance	**Protect the Crown and others**	**Insurable**
Approach One *Single-tiered scaled framework* *Changes to be given effect via amendments to the MTA and MPR Parts 102 and 131*	Meets	Partially meets	Meets
	• The scaled framework provides greater assurance that owners have assurance for the likely cost of a spill proportionate to the risk profile of their operation. Insurance policies, available on the international market can be used to cover the main risks requiring cover. The $1.2 billion limit of the scaled framework reflects the uppermost estimate for clean-up costs from an oil spill and serves to future-proof proof the scaled framework in the event that a new installation proceeds in a high-risk, deep water location.[17] This upper limit of $1.2 billion would only be required for an installation where the estimated clean-up costs of an oil spill is estimated to cost up to this amount. Based on our understanding of current operators, we would not expect this to be the case. • Insurance policies offered on the international market should align to the installation insurance that creates the biggest risk, for example a floating production, storage and offloading unit (FPSO) out of control covered by P&I insurance[18], and provide cover for the direct costs relating to the impact of the installation releasing oil into the environment. • In practice these policies, are likely to cover most of an owner's liabilities under sections 385B and 385C of the MTA. Standard cover, however, does not cover pure economic loss, or compensation for the broader impairment to the environment.[19] • Third parties' claims are limited by the scope and quantum of the policy agreed between the owner and insurance provider. No other changes to the types of loss provided for in the MTA, and the owner's unlimited liability for this loss. • Owners and insurers support the increased levels of assurance and consider that insurance should be able to be secured if the scope of an insurance policy can be relied on. In practice, owners are already using these types of policies to cover their operations. • The most consistent approach with other jurisdictions. • Policies covering liabilities of this nature are generally provided through a combined single limit (CSL) policy. CSL policies do not have the ability to prioritise charges (e.g. ring fence amounts for specific liabilities such as well containment). Owners will need to prove to MNZ that their insurance is sufficient to meet all estimated costs (including Part 131). • No other changes to the types of loss provided for in the MTA and the owner's unlimited liability for this loss.		

[17] Ibid.
[18] P&I (protection and indemnity) insurance is cover for third party liabilities incurred by shipping and offshore installation owners, arising from the operation of ships and offshore installations.
[19] Again, limiting the scope of assurance was also the intent of the previous government. The purpose was make the regime insurable at the required financial levels.

Option	Objectives		
	Provide assurance	**Protect the Crown and others**	**Insurable**
Approach Two *Two-step scaled framework* *Changes to be given effect via amendments to the MTA and MPR Parts 102 and 131*	Meets	Partially meets	Partially meets
	• The scaled framework provides greater assurance that owners have provision for the likely cost of a spill proportionate to the risk profile of their operation. The $1.2 billion limit of the scaled framework reflects the uppermost estimate for clean-up costs from an oil spill and serves to future-proof proof the scaled framework in the event that a new installation proceeds in a high-risk, deep water location. This upper limit of $1.2 billion would only be required for an installation where the estimated clean-up costs of an oil spill is estimated to cost up to this amount. Based on our understanding of current operators, we would not expect this to be the case. • Oil and gas and insurance industry representatives have expressed their doubts that this two-step approach will be insurable, in combination with the higher upper limit of the scaled framework. This is despite some owners currently holding insurance from the international market for up to $27.7 million covering the full scope of liabilities under the MTA. Alternatives such as parent company guarantees may be harder to secure due to the increased quantum required. • Preserves current scope for third party claims against insurers for a specified (low) amount, though the scope of claims is limited under part two. • Insurance policies offered on the international market should be able to provide cover for part two. In practice part two should cover an owner's most significant liabilities (though not for third party loss of profit from impairment of the environment). • Policies covering liabilities of this nature are generally provided through a combined single limit (CSL) policy. CSL policies do not have the ability to prioritise charges (e.g. ring fence amounts for specific liabilities such as well containment). Owners will need to prove to MNZ that their insurance is sufficient to meet all estimated costs (including MPR Part 131). • In practice, the first tier ($27.7 million), will be used to cover the first costs incurred, which is likely to be containment and capping costs. • No other changes to the types of loss provided for in the MTA and the owner's unlimited liability for this loss.		

We recommend Approach One – a single-tiered scaled framework with an upper limit of $1.2 billion

75. Approach One is the strongest of the two scenarios outlined above and mostly meets all of the OFA regime's objectives as it:

    75.1. significantly increases the level of assurance required of owners, proportionate to the risk of their operation;

75.2. provides protection for the Crown, and reasonably enables third parties to make a claim against those providing assurance;

75.3. is expected to be insurable through existing insurance policies available to the energy sector; and

75.4. provides financial assurance for well control measures.

76. This approach does not fully achieve all objectives because it limits the scope for third party claims to the scope of the agreed insurance policy between the owner and insurance provider. These standard wordings do not generally cover pure economic loss and damages incurred due to the impairment to the environment. Examples of what would be excluded by the proposed regime is loss of profit to a tourism company that cannot bring tourists to a beach because it has been fouled by an oil spill, and lost fishing quota.[20][21]

77. Noting this, we understand that insurance policies available will cover the biggest risks we are concerned about and that this option is necessary to ensure the regime is insurable.

78. Owners will also still retain unlimited liability for losses within the scope of Part 26A of the MTA, and therefore third parties will retain an existing avenue to seek redress for any loss (provided the operator is solvent).

Changes to the MTA and MPR Parts 102 and 131 are required to implement this approach

79. Amendments are required to the MTA and MPR Parts 102 and 131 to give effect to the recommended changes. This paper seeks approval to introduce the Maritime Transport (Offshore Installations) Amendment Bill to implement the necessary changes to the MTA.

80. The amendments to the MPR Parts 102 and 131, which will be approved by the Minister of Transport, are being prepared. The proposed changes to the MPR will be publicly consulted on.

81. MNZ is also updating the guidance it provides to owners to support their compliance with the OFA regime.

Transitional and timing arrangements

82. It was always intended that owners would be provided with a transitional period once the new regime was in place. Transitional arrangements will take into consideration the time it may require time to assess, align and underwrite insurance policies to the new regime requirements.

83. We propose that from the date the new OFA regime comes into force:

83.1. new installations will have up to three months to comply with the new regime; and

83.2. existing installations will have up to 31 July 2020 to transition to the new regime.

[20] Claims of this nature are still possible under Part 26A of the MTA however.
[21] Oil damage to property used for fishing would be covered, fishing quota would not be covered by this proposed regime. While a fishing quota is property, it is intangible, existing as a legal concept, whose physical manifestation consists only of entries in a register kept at the Ministry of Primary Industries. It is not the type of property that is susceptible to damage from hazardous substances that might be discharged into the marine environment.

84. During engagement on the policy proposals in this paper, stakeholders from all the sectors engaged, conveyed it would be more efficient and effective to review the proposed regime (the Bill and associated MPR Parts 102 and 131) together.

85. To enable stakeholders to do this, and noting that the Bill and MPR Parts 102 and 131 are consistent with the policy decisions set-out in this paper, we are seeking agreement that MPR Parts 102 and 131 be available for public consideration and submissions during the Select Committee process. Following public consultation, we intend that the Associate Minister if Transport take the finalised Rules back to Cabinet for consideration.

Legal measures in place to manage the regulatory regime

86. While the risk of a significant oil spill is low, the potential impacts to the environment and the scale of the Crown's and other parties' financial exposure from the potential clean-up costs from such an event are significant. This exposure is increased if operators are not meeting their legal obligations, for example by operating without a certificate of insurance.

87. Given this, while officials were scoping the new requirements for this regime, they also considered the levers in place to manage the offshore regulatory regime. This work focussed on the certificate of insurance because this is the mechanism that gives legal effect to the assurance requirements of the regime.

88. [redacted]

89. [redacted]

Withheld to maintain legal professional privilege

90. [redacted]

Consultation

91. As noted above, public consultation was undertaken in 2017 and 2018 on proposals. There has been further engagement with oil and gas operators, the insurance industry and an environmental stakeholder, in the development of this paper.

92. The following agencies were consulted on this paper: The Ministry of Business, Innovation and Employment, MNZ, Ministry for the Environment, Te Puni Kōkiri and the Treasury. The Department of Prime Minister and Cabinet was informed.

Financial implications

93. There are no direct costs to the Crown associated with the proposals in this paper. The proposals in this paper are not expected to increase the costs to MNZ, associated with managing the OFA as all activities are cost recovered. MNZ charges a fee for the time taken to process an application, and the Maritime Levies Regulations 2016 enable MNZ to recover the external specialists' costs (assess the proposals made under the rule requirements), from the applicant), from the applicant.

94. Under the proposals in this paper, owners will be required to hold higher levels of assurance which is likely to be an additional operating cost. Increased assurance requirements on owners are intended to reduce the risk that the Crown, marine agencies and other third parties, and enable these parties to recover the costs and loss associated with pollution damage from an oil and gas spill.

95. Owners are most likely to meet the increased assurance requirements through insurance. The exact additional costs (to insurance premiums for example) will depend on their existing insurance arrangements and the nature of their operations. The key proposals have been publicly consulted on, with the potential increase in costs signalled with owners for some time.

96. The proposed amendments will bring New Zealand in-line with equivalent regimes in other countries. While the exact costs to business are unknown, stakeholders have not suggested that the proposed changes to the OFA regime will deter investment in New Zealand.

Legislative implications

97. As noted above, amendments to the MTA and MPR are required to implement the policy decisions outlined in this paper. The sections below outline the legislative implications of the proposals.

Compliance

98. The Maritime Transport (Offshore Installations) Amendment Bill complies with the:

    98.1. principles of the Treaty of Waitangi;

    98.2. rights and freedoms contained in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993;

    98.3. principles and guidelines set out in the Privacy Act 1993;

    98.4. relevant international standards and obligations; and

    98.5. Legislation Guidelines (2018 edition).

Binding on Crown

99. The Bill will bind the Crown in the same manner as the principal Act.

100. Creating new agencies or amending law relating to existing agencies

101. The Bill will not create any new agencies and will not amend the existing coverage of the Ombudsmen Act 1975, the Official Information Act 1982 or the Local Government Official Information and Meetings Act 1987.

Allocation of decision making powers

102. The Bill will not involve the allocation of decision making powers between the executive, the courts, and tribunals.

Associated regulations and other Instruments

103. Regulations are not needed to bring the Bill into operation.

104. Some of the policy proposals in this paper will be brought into force through amendments to the Parts 102 and 131 of the MPR. The amended rules are expected to come into force with the Bill, in November 2019.

Definition of Minister/department

105. The Bill does not define 'Minister', 'government department' or 'chief executive'.

Commencement of Legislation

106. The Bill is expected to be enacted in November 2019 and come into force in December 2019.

Parliamentary stages

107. The Bill is to be introduced in May 2019 and should be passed by October 2019.

108. It is proposed that the Bill be referred to the Transport and Industrial Relations Select Committee.

109. The Minister responsible for the Bill will be Hon Julie Anne Genter, Associate Minister of Transport.

110. The Bill holds a category 2 priority on the 2019 Legislation Programme.

Impact analysis

111. The Regulatory Impact Assessment (RIA) was originally prepared for the public consultation undertaken in 2017. The Transport Sector Regulatory Impact Assessment Quality Assurance Panel (the Panel) reviewed the original RIA and considered that the information and analysis summarised in the RIA partially meet the quality assurance criteria.

112. The nature of the problem was comprehensively described. However, the issues are complex and intertwined. Information is lacking on the actual extent and magnitude of gaps in financial assurance. The likely extra costs to industry are therefore not set out. As noted in the financial implications sections, implementation costs for owners are not fully known and will depend on the nature of an owner's operation and existing insurance arrangements.

113. The RIA has been updated since the 2017 version to reflect the discussion in this paper, the Panel reviewed the updated RIA and consider that the information and analysis summarised partially meets the quality assurance criteria. The nature of the problem is comprehensively described. The analysis builds on the regulatory impact statement completed in 2017. The likely extra costs to industry associated with the proposals are not known. Implementation costs are still not fully known.

Human rights implications

114. The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Gender implications and disability perspective

115. There are no gender implications, or considerations for people with disabilities, associated with the proposals in this paper.

Publicity

116. Public consultation was undertaken on the substantive proposals in this paper in 2017 and 2018.

117. We intend to issue a press release to support the introduction of the Bill. The proposals are likely to attract some attention given the broader policy settings for oil and gas exploration in New Zealand.

118. Significant consultation has already been undertaken with oil and gas industry, insurance and the environmental sector representatives. It is possible that some of these groups will make public statements on the Bill, including through the Select Committee process. We expect officials to continue to work with stakeholders as the Bill progresses.

Proactive release

119. This Cabinet paper will be proactively released, with appropriate redactions of commercially sensitive and any legally privileged information. The supporting documents, such as the draft guidance to support MPR Parts 102 and 131 will also be released.

120. The Bill will be publicly available when it is introduced in May 2019.

Recommendations

121. The Minister for Energy and Resources and Associate Minister for Transport recommend that the Committee:

1. **note** that on 19 September 2018, the Cabinet Economic Development Committee:

1.1. **noted** that due to the concerns about the insurability of the offshore financial assurance regime the Associate Minister of Transport decided not to bring either the 2017 amendment to the Marine Protection Rules Part 102, or the proposed 2018 amendments to the Marine Protection Rules Part 102, which were publicly consulted on, into force; and

1.2. **noted** that in September 2018, the Associate Minister of Transport directed officials to scope changes to the Maritime Transport Act 1994 and the offshore financial assurance regime with the objective of ensuring an insurable regime is in place for the commencement of the 2019/20 drilling season [DEV-18-MIN-0208];

Policy decisions

2. **agree** that owners of offshore oil and gas installations require a certificate of insurance for each of their installations for at least the estimated cost of a credible worst case spill, based on a scaled framework which takes account of factors that influence the pollution damage resulting from an oil or gas spill, including geology, depth of water, and type of hydrocarbon;

3. **note** that the proposal that was consulted on with stakeholders had an upper limit for clean-up and compensation costs of $800 million, which is lower than the $1.2 billion upper limit proposed by this paper;

4. **agree** that the upper limit for the scaled framework referred to in recommendation 2 will be $1.2 billion;

5. **agree** that the Crown and affected third parties can bring a direct claim under an insurance policy, or other financial assurance, against the party providing financial assurance to an owner of an offshore installation by effectively standing in the shoes of the insured;

6. **agree** to empower the making of marine protection rules:

6.1. specifying the liabilities and amounts for which insurance or other financial security that must be held for a certificate of insurance to be issued; and

6.2. to require insurance or other financial security to be held in respect of the costs of implementing a marine oil spill contingency plan;

7. **agree** that owners offshore oil and gas installations will be able to meet assurance obligations using insurance policies that cover the key risks associated with their operations and are consistent with internationally available best practice policy wording;

8. **agree** that owners of offshore oil and gas installations must hold financial assurance for the cost of well-control measures, with the level of assurance required based on an assessment of the cost associated with implementing their oil spill contingency plans;

9. **agree** that insurance policies and other financial security provided by offshore oil and gas installations must be subject to New Zealand law and the jurisdiction of New Zealand courts;

10. **agree** that new installations have up to three months to comply with the new regime, and existing installations have up to 31 July 2020, to transition to the new regime;

11. **note** that all other elements of the current financial assurance regime for offshore oil and gas installations remain the same, including the retention of unlimited liability on owners of regulated offshore installations;

12. **note** that to deliver an insurable financial assurance regime at the significantly higher limits recommended above, officials have not been able to identify a credible method of including pure economic loss claims into the assurance requirements;

13. [redacted]

Withheld due to active consideration

Primary and secondary legislation changes

14. **note** that amendments are required to the Maritime Transport Act 1994 to give effect to recommendations 5 and 6;

15. **note** that the Maritime Transport (Offshore Installations) Amendment Bill (the Bill) holds a priority of category 2 (must be passed in the calendar year) in the 2019 Legislation Programme;

16. **approve** the Bill for introduction, subject to the final approval of the Government caucus and sufficient support in the House of Representatives;

17. **agree** that the Bill be introduced in May 2019;

18. **agree** that the Government propose that the Bill be:

18.1. referred to the Transport and Infrastructure Select Committee for consideration;

18.2. enacted, if possible, by November 2019;

19. **note** that to give effect to recommendations 2, 4, 7, 8, 9 and 10, amendments are required to the marine protection rules, which are made by the relevant Minister under the Maritime Transport Act 1994;

20. **note** that the Marine Protection (Parts 102 and 131) Amendment Rules 2019 (the Rules) will make the necessary changes in the marine protection rules;

21. **note** that the Bill and the Rules are a package of measures and that:

21.1. consultation on the draft Rules needs to occur in parallel to the Parliamentary process for the Bill so that the Rules are able to be brought into force as soon as practicable after the Bill is enacted;

21.2. submitters to the Select Committee and the Select Committee will want to have access to the draft Rules when they consider the Bill; and

22. **approve** the Associate Minister of Transport carrying out public consultation on the Rules alongside the progress of the Bill;

23. **agree** that, following public consultation, the Associate Minister of Transport bring the finalised Rules to Cabinet for consideration;

Authorised for lodgement

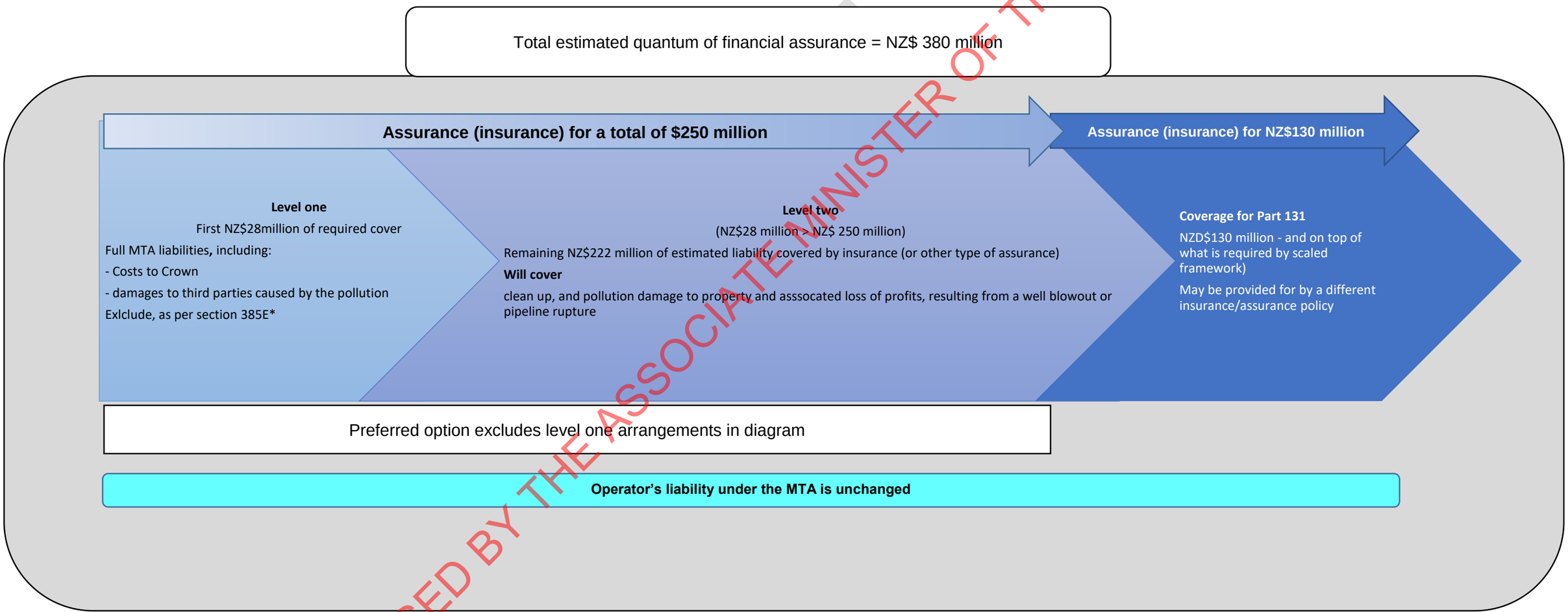
Hon Dr Megan Woods
Minister for Energy and Resources

Hon Julie Anne Genter
Associate Minister for Transport

Annex one – visual representation of approaches one and two

Example:

Operator X has been assessed as needing assurance for NZ$250 million using the scaled framework.
Estimated coverage under Part 131 is another NZ$130 million.
Total coverage required is therefore: NZ$380 million.



- acts of war, hostilities, civil war, insurrection, or a natural phenomenon of an exceptional, inevitable, and irresistible character; and/or
- wholly caused by the act or omission of a third person, other than the employee or agent of the owner or the person in charge, as the case may be, with intent to cause damage.