

# ENVIRONMENTAL REGULATION

INTERNATIONAL COMPENSATION SYSTEMS FOR OIL  
SPILLS IN RELATION TO REFORM IN NIGERIA

**SDN**



A REPORT PREPARED BY SDN

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## EXECUTIVE SUMMARY

Compensation for oil spills should be a straightforward matter, but it has the capacity to become extraordinarily complicated. To avoid the development of this extreme complexity, the global trend has been towards the avoidance of single or class actions in local courts through tort action. Instead, the consensus has increasingly been to regularize payments of compensation through government defined rules for loss, paid for by funds created by the potential polluter. Local civil, legal actions have been found to create uncertainty as to liability, insurance needs and often create conflicts regarding jurisdiction. Sometimes such cases get progressively more complex through the appeals system and occasionally go into the courts of the countries where the polluting companies are domiciled or have assets, rather than the country where the pollution occurs. Varied damages tend to be awarded without consistency by judges and the cost of the cases reduces the compensation paid to the victims and delays its payment. The longer the process goes on, the more expensive the legal fees, with diminished compensation to the victims of the oil spill.

The development of more systematic compensation systems grew out of tanker accidents in the 1960s. This was in recognition that tanker accidents frequently occurred outside the jurisdiction of any national court, while owners could frequently escape liability for the damage caused. Civil and criminal litigation turned out to be incredibly difficult. This led the UN International Maritime Organisation (IMO) to create the Civil Liability Convention, establishing strict liability, and subsequently the Fund Convention created a fund paid for by oil companies to supplement the compensation paid by ship owners. In effect, since local jurisdiction was impossible, international rules and funding was required.

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One of the ways in which compensation issues was taken out of the hands of local courts, defined by case law and individual cases was to define potential liability by international agreement and create a mutual fund. Such funds do not pay compensation if a claimant seeks legal redress elsewhere.

These funds, whether that of the UN International Maritime Agency (IMO), the European Offshore Pollution Liability Association (OPOL) or the US Coastguard run OPA-OSLTF super funds, require a claim to be made against the responsible party, but do not support victims who take independent legal action through the courts.

This alone deters private suits. If there are disputes about the money paid out of such funds, the aim is to seek national or international arbitration rather than legal action. These funds are sometimes funded by a tax of a few cents per barrel of oil produced or imported, or through mutual insurance systems.

One complication relating to compensation is precisely what it is being paid for. In the US, this compensation has been defined by monetary loss, most notably in that paid after the Macondo spill. This was defined purely by comparisons of income before and after the spill using insurance loss adjusters. This has been controversial and takes no account of losses to the environment. By contrast, in less developed societies, there is less ability to define matters purely in financial loss, not least because financial records before and after the accident are unavailable. In these cases, monetary value must be attached to the physical asset damaged, crops destroyed and fisheries polluted. To avoid widely differing financial compensation for similar incidents by different courts, some standardization by the state is needed. This needs to be updated on a regular basis.



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Nigeria currently has no mechanism to standardize compensation, although one was created by the DPR in 1998, but never passed into law. As a result, the current system is largely led by the companies through Oil Producers Trading Section of the Lagos State Chamber of Commerce. While widely regarded as government sponsored, this in fact has little to do with the Government and has little 'source credibility'. Rates are widely regarded as too low. As a result, Nigeria's system of compensation still extensively uses the courts, with delays, highly variable rates of compensation and high legal costs.

One potential solution to this problem would be to create a 'source credible' government list of value for losses due to pollution by either the DPR or NOSDRA. This might then be reinforced by a fund, administered by a respected body. This would not pay out in the event of any claimants going to law.

Nigeria is in a unique position in terms of compensation regime. Nowhere else in the world is the compensation system seen as a justification for actually creating damage to oil installations because of poverty.

This makes the creation of a fairer and more systematic way of defining both liability and payment even more urgent here than elsewhere. While in the case of deliberate damage, liability has to be limited to clean-up costs and not compensation, this position has to be made much clearer to those living near oil installations than it currently is. This can only be done by a major programme of education in the Niger Delta and a significant improvement in relations between operators and the local civil societies. In addition, in cases where deliberate damage has been done and prosecuted under criminal law, victims of such pollution should be able to sue the perpetrators for damages under civil law, backed by state agencies.

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## SEEKING COMPENSATION THROUGH THE COURTS

Compensation for pollution from oil grew out of the civil courts with private actions taken against anyone whose actions caused damage to another person. Generally known as tort law, such actions did not involve the state, unless criminality was involved. It was either the product of an individual action, or 'a class action' where individuals similarly affected, joined together to take those responsible to court.

The majority of oil spill cases on land result in some form of such civil action, but most never get to court, or are settled before the court comes to any conclusion in most developed country jurisdictions. This is largely the result of pragmatism on behalf of the polluter, who admits liability and pays compensation on the basis of a predictable scale of damages. Those taking such private civil actions may be supported by various regulatory authorities in local and national government, with technical expertise. Polluters know that such actions can escalate.

However, if they do come to court, achieving a result can take decades. A case against ExxonMobil over groundwater contaminated with MTBE in New Hampshire, USA, took over ten years to come to court, with \$700 million in damages at issue, 230 witnesses and over 100 lawyers involved in late 2012. ExxonMobil had already had a similar case in 2009 with New York City. After six years argument it was forced to pay out \$105 million. Significantly regarding the advantages of settlement as opposed to going to court, 23 other companies sued by New York settled quickly for a total of \$15 million.

By comparison, in many developing countries civil legal actions over oil spills do frequently reach the courts, since civil legal action is seen by those in areas affected as the only means to receiving redress. This may be because the oil industry pays any compensation for long-term damage directly to governments, or because the compensation on offer has been set many years previously and is regarded as inadequate.

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Much depends on the civil courts within the country and the development of existing case law to establish principles of compensation and an expected rate. However the major problem in creating a fair and quick system of compensation lies in the ability to appeal to successive higher courts, thus increasing legal fees and causing considerable delay.

A classic current case of a pollution case going wrong is the \$18 billion action taken by “Los Afectos”, a group of local indigenous people in Ecuador, against Chevron over damage relating to spills as far back as 1972. Texaco, which was then producing oil in the Amazon, mishandled oil pits in places where oil residues contaminated the local water supply. In spite of the fact that the site was 95% owned by the state national oil company Petroecuador, when Texaco left after 20 years, it agreed to carry out \$40 million-worth of remediation, which was accepted by the government.

However subsequently Texaco was sued in a US Federal court, but this decided that the case should have been initially taken to the Ecuadorian courts. These threw out the claims, after experts asserted that samples taken by experts were essentially within legally acceptable limits. However during 1999, the Government of Ecuador enacted legislation enabling groups to file suit for further environmental damages.

By this time Chevron had taken over Texaco. Although Chevron had no assets in Ecuador and never had had, the plaintiffs saw Chevron as the primary and indeed only source of potential compensation.

The litigants subsequently took Chevron to court again in Ecuador in February 2012. Amidst allegations that the original samples had been faked, an Ecuadorian judge awarded them \$8.6 billion in clean-up costs and \$8 billion in punitive damages; \$16.6 billion in all. The company appealed, alleging fraud.

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After Chevron's refusal to pay or admit liability, the litigants then took Chevron to court in Canada, not because Chevron in Canada had done anything wrong but because Chevron had substantial assets in Canada, which it could, in theory, be legally sequestered.

This process of seeking compensation has now taken 50 years since the original damage was established and has produced no payment to those who suffered the damage. It has cost a small fortune and has ended up with legal action against an oil company that was not responsible, in a country where the pollution did not take place. That there was substantial pollution cannot be disputed, but it is also the case that the corporation that benefitted most of all from the oil produced was Petroecuador and consequently the state of Ecuador, itself. The national oil company has not been prosecuted in any way.

A similar situation has developed Peru, where Occidental is accused of polluting the Corrientes River in production begun in 1972. A suit was filed in the US Courts in 2007 on behalf of the indigenous Achuar people, which was promptly sent back to the Peruvian Courts. Occidental had actually ended activities in Peru in 1999, but had plans to return. This suit is now being further examined in Los Angeles, where Occidental is domiciled, decades after the damage was done. An added complication is that the government of Peru has taken legal action against the Achuar, for preventing the return of Occidental to Peru in 2006.

These are extreme examples of a new pattern for seeking damages and thus compensation in foreign courts. Shell is also going through the same process, although it settled one case for \$15.5 million brought by the family of Ken Saro-Wiwa in the US Courts in 2009, without admitting liability. It currently faces another suit in European Courts.



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Clearly, such international action through foreign courts against large multinational companies has obvious advantages in terms of the publicity generated. It allows indigenous peoples, whose plight would otherwise go unnoticed to bring it to global attention. Certainly senior management within such multinational companies are alarmed at this trend and it undoubtedly plays a major motivation for improved practice. This is further emphasized by the post-Macondo settlement, where damages have reached well above \$30 billion.

However what it does not do is ensure a rapid clean-up of the damage done, quick remediation of the area or provide compensation rapidly to the people who have suffered the damage. Not only does it not provide a quick response, but it also costs very large amounts of money. Indeed, if and when very substantial damages are finally awarded in millions, if not billions of dollars, there are considerable problems of distribution.

This, in itself, raises problems in relation to development. Even in the context of best practice in oil field development in an area of, say, subsistence farming, the amounts of money handed out in payment for the use of land, or the rehousing of local people, can cause conflicts. Those on the edge of such development can see an injustice in the sudden riches given to their neighbours. The same clearly applies to large amounts of damages given after lengthy international court battles. All too often such damages are seen as a sudden windfall to the national or local government, and thus take even longer to percolate down to the local communities, often in a form not chosen by them.

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This is complicated by another factor. National oil companies are rarely, if ever, sued for damage to the environment. In the case of the destructive XTOC 1 blow out in the Gulf of Mexico, Pemex, the Mexican oil company simply claimed sovereign immunity and paid no compensation. As noted, Petroecuador has not been involved in any of Texaco's legal problems, in spite of being the primary beneficiary of the polluting operation. The result may be that international civil legal suits are increasingly seen as an unfair way to increase state revenue for past failures of national regulation from the larger international companies.

In summary, civil litigation for compensation for pollution damage is a hit and miss affair, but an obvious route to pursue. It is thus unsurprising that the initial development of a more systematic way to provide compensation arose out of a situation where it was impossible to sue in any single national jurisdiction.

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## DEALING WITH TANKERS

The obvious example where it was difficult was to pursue a company for damages for civil damages in national courts was shipping. And the greatest example of damaging shipping was the oil tanker. Perhaps surprisingly, for not only was tanker traffic growing around the world in the 1960s and the size of the individual tankers themselves was increasing rapidly, there really was no adequate system for paying for any damage and cleaning up costs, let alone compensation until 1969.

Predictably, it took a major accident to clarify liability if anything went wrong. On the 18th March 1967, the tanker Torrey Canyon hit a reef off the south-west coast of the UK, revealing that, that not only did worldwide governments have no idea how to deal with such an event, but had no mechanism to define liability for it either. Ten days after the ship hit the reef, the RAF attempted to bomb it to set the oil on fire and thus prevent the slick from spreading, without much success. Foam booms were a failure and the ship eventually sank, after dispersing 120,000 tons of crude oil into the sea.

The state of the liability problem can be gauged by the fact that the ship was registered in Liberia, owned by a subsidiary of Union Oil in the US, carrying a cargo for BP and the cause of the problem was that the Captain had taken a short cut, under time pressure to deliver the oil. The ship, of course, was in 30 metres of water and thus worthless. At the time, maritime law only dealt with responsibility to collisions.

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The only way the British and French governments could seek damages was by attempting to arrest a sister ship, the Lake Palourde when it sought supplies in Singapore. Famously the ship was finally arrested when a British lawyer got on board pretending to be a Whisky salesman. The French never actually managed to catch the vessel. By this time the ship's owners, the Barracuda Tanker Corporation, incorporated in Bermuda, had infuriated the British, not only by creating a delay before it sank on the grounds that it was salvageable, but also tried to use the US Courts to limit their liability to \$50. BP naturally denied all liability, but conveniently provide the experimental liquid dispersants, which failed to deal with the slick.

The British eventually got £3 million in damages. This was far less than spent on the clean up, but the result was the International Maritime Organisation's Civil Liability for Oil Pollution Damage (CLC) adopted in 1969. This established strict liability with a number of specific exceptions.

It is the duty of the owner to prove in each case that any of the exceptions should in fact operate. However, except where the owner has been guilty of actual fault, they may limit liability in respect of any one incident. The Convention requires ships covered by it to maintain insurance or other financial security in sums equivalent to the owner's total liability for one incident.

It applies to all seagoing vessels actually carrying oil in bulk as cargo, but only ships carrying more than 2,000 tons of oil are required to maintain insurance in respect of oil pollution damage. The amount of damages and thus insurance was set on a sliding scale according to the size of the ship, initially set at 59.7 million SDRs for ships over 140,000 dwt, subsequently raised to 89.77 SDRs (\$138 million) in 2000.

It was widely recognized that this was unlikely to be enough and handing the entire responsibility for compensation onto tanker owners, who in some circumstances might have only one ship, was unfair. Shortly after in 1971, the International Convention on the establishment of an International Fund for Compensation for Oil Pollution Damage (1971 Fund Convention) was set up.

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This was to be collected from a levy on companies receiving more than 150,000 tonnes of crude or heavy oil by sea, decided on a national basis.

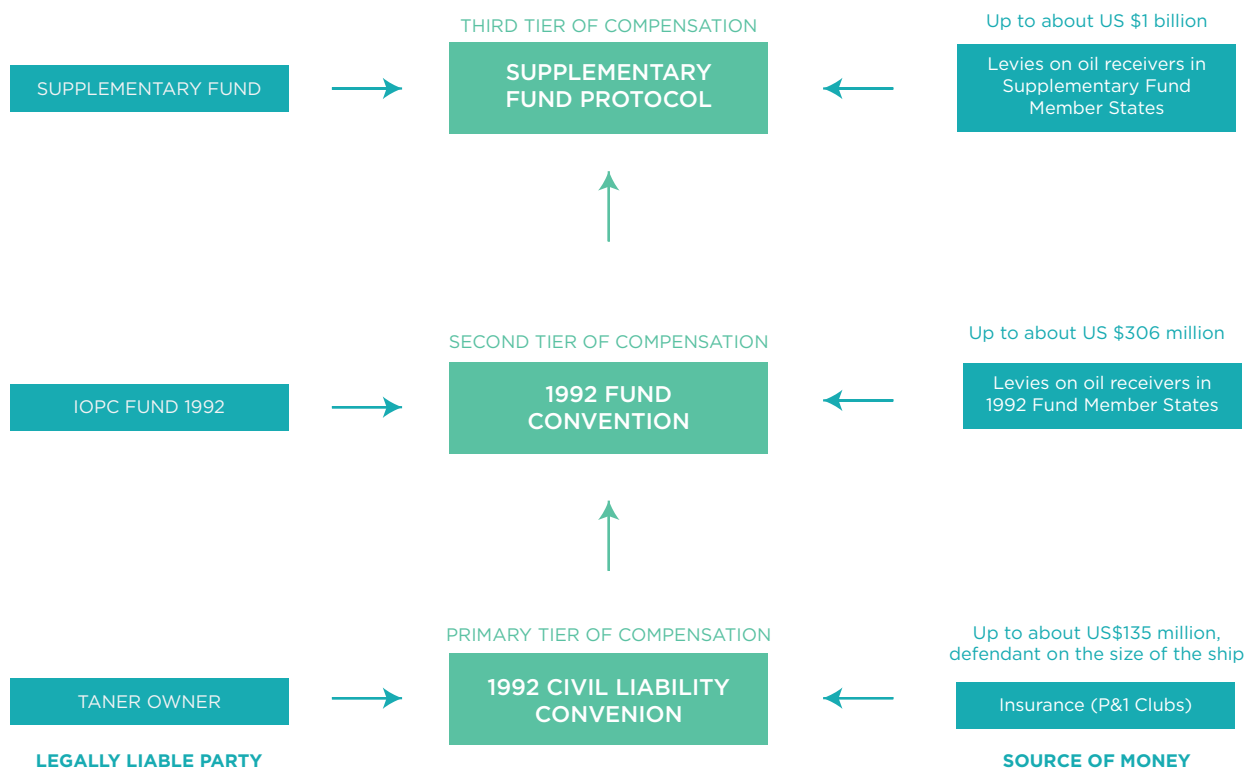
In fact, both the CLC and the 1971 Fund Convention took a considerable time to be ratified, coming into force in 1996, after substantial amendment – increasing the value of the liability and the fund. However, significantly, before they came into force and very quickly after the Torrey Canyon disaster, both tanker owners and oil companies formed their own private system.

Known respectively as TOVALOP, standing for the Tanker Owners Voluntary Agreement Concerning Liability for Oil Pollution and CRISTAL, the Contract Regarding a Supplement to Tanker Liability for Oil Pollution, were created in 1968 and only ceased to operate in 1997 when the IMO conventions came fully into force. It was rapidly realized by the industry that a systematic process for dealing with compensation was much better than the chaos of civil litigation.

It is worth examining how this system for tanker spills works, because it provides a model for a strict liability, with limits and how an insurance pool actually works. It is three tiered, each of which has its own source of funding. If the required level of compensation is inadequate, then the next tier is used. This in effect prevents the bankruptcy of the initial funds, provided by the tanker owner, through his own insurance.

The 1992 CLC is based on the principle of ‘strict liability’. This means that the owner of the tanker which spills the oil is liable regardless of whether or not he was actually at fault, subject to very few exceptions (e.g. if the damage resulted from an act of war or grave natural disaster, was wholly caused by sabotage by a third party, or was wholly caused by the negligence of public authorities in maintaining lights or other navigational aids). As a result, claimants can receive compensation promptly, without the need for lengthy and costly litigation.

However, that liability is limited to the size of the tanker, unless the accident is caused intentionally, or recklessly in the knowledge that a disaster will result. The net result is that compensation is paid, while those responsible for the pollution know the extent of their liabilities and can thus insure them.



There is a further philosophical justification for system. It is based on the premise that consumers in the major industrialized countries are ultimately responsible for crude oil being shipped on the oceans and seas of the world. The CLC/Fund regime recognizes that it would be inequitable for tanker owners to bear all the compensation attributable to extensive pollution damage, and that receivers of crude oil and heavy fuel oil cargoes in all States should contribute to a secondary layer of compensation. The CLC/Fund regime established this principle, but only for ships. There were comparatively few offshore oil facilities in 1969 so there was no provision for spills from offshore rigs and platforms. This would come later, with the OPA.



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## THE US OIL POLLUTION ACT 1990

The US did not become a signatory to the CLC/Fund regime, but rapidly found out about the serious problems of civil and criminal law in relation to tanker accidents when the Exxon Valdez ran aground in Alaskan waters in 1989. The result was a legal battle that is still going on some 22 years later. It generated some 150 lawsuits, against the captain, against Exxon, against Exxon Shipping and against the Alyeska Pipeline Consortium.

The captain, was charged with negligence, being drunk at the time. The shipping company was charged with, in effect, having employed him, while Exxon's corporate officers were charged with being criminally liable because their position in the company made them responsible regardless of their actual knowledge of the facts surrounding the accident and whether they contributed to it.

In 1994, a court found Exxon guilty of recklessness and it was ordered to pay \$5 billion in damages. While saying that it was willing to pay \$25 million, Exxon appealed and has appealed every judgment since. In 2006, the Supreme Court cut the damages to \$2.5 billion, but Exxon has asked the court to reconsider. While Exxon apparently spent \$3 billion on the clean up of the spill, nobody whose life was affected by the spill has been compensated for their loss.

Unsurprising then, that examining this potential legal morass, the US Environmental Protection Agency suggested that the US join the CLC/Fund regime shortly the accident, or failing that, develop a regime for the US rather like it. The result was the Oil Pollution Act of 1990 (OPA), which transformed the US system of oil spill regulation.

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Passed unanimously by Congress, the OPA established a Federal liability system for all oil spills. This put the liability directly onto the oil company concerned, thus squeezing out the courts in term of establishing which party caused the spill. These liabilities were in excess of clean up costs, which were also mandatory. It established penalties for tankers, onshore and offshore facilities, starting with tankers above 3,000 dwt at \$1,200 per gross ton. Onshore facilities were limited to \$350 million and offshore operators up to \$75 million per spill, plus removal costs.

The Act confers on the company the cost of cleanup, but that cleanup has to be in line with the National Oil and Hazardous Substances Pollution Contingency Plan, which was also a product of the Act. It cannot choose how it is done.

Equally, the range of things for which damages are to be paid was substantially increased, particularly regarding economic damage, loss of revenues, property losses, earning capacity and the cost of public services like fire protection. In the case of subsistence use, the new system requires that any claimant who uses the natural resources, which are damaged, must be compensated regardless of the ownership of those resources. Exxon had effectively avoided such damages. The defense against liability were only limited to acts of war, acts of God or actions of a third party, which became liable instead. Damages included the cost of assessing the damage.

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Liability limits are effectively controlled so that if there has been a fault or violation of statutes then the liability becomes unlimited. Equally, if the spill is not reported properly, liability again becomes unlimited. Fines for failure to report a spill were substantially increased, while failure to comply with a Federal clean up order, were put at \$25,000 per day.

The Act introduced a requirement for evidence of financial responsibility for those running tankers of \$150 million and for those operating oil installations of an ability to meet their potential liabilities. It greatly increased Federal planning and emergency response to oil spills and, creating a revolution in global tanker traffic, banned all single-hulled vessels from entering US waters after 2010. It did however follow the precedent of the CLS/Fund system, by reintroducing the Oil Spill Liability Trust Fund (OSLTF). However unlike the CLS/Fund system, this was designed to pay out, if the oil company did not and then recoup the money from it.

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## OIL SPILL LIABILITY TRUST FUND (OSLTF)

Ironically, the OSLTF had been proposed in 1987, before Exxon Valdez disaster, but Congress could not agree on how to fund it. The aim was not merely to fund any emergency response and clean up effort by the Federal Government, but also pay out if the 'responsible party' refused to do so. This made the whole process much quicker than the claims through the civil courts.

The aim of the fund was also to pay out compensation, if the damage was greater than the liability limits demanded by the OPA from the responsible party. The total amount that could be payable was fixed at \$1 billion per incident. Before Maconda, this maximum had been seen as more than adequate. Of the 51 spills recorded between 1990 and early 2010, only 10 had required the OSLTF to pay out, amounting to a total expenditure of \$640 million; well within the Trust's capacity to pay.

The fund was funded by a per-barrel excise tax, initially of 5 cents per barrel on petroleum produced in or imported into the US and levied on the companies. This source ended in 1994, but was reintroduced in 2005 and increased to 8 cents per barrel. It will go up to 9 cents in 2017. The fund consolidated all other federal funds for oil spills, but is controlled by the US Treasury with accrued interest. Up to \$50 million from the fund is allotted each year for emergency response and available quickly to the Federal On-scene Coordinator. The fund totaled \$1.7 billion in 2010.

Furthermore, all the money reclaimed from 'responsible parties' goes straight back into the fund, as does any penalty payments and fines incurred under OPA, which amounts to around \$4 to \$7 million a year. The Fund is administered by the National Pollution Fund Center (NFPC), run by the US Coast Guard based in Arlington, Virginia. This agency also issues the Certificates of Financial Responsibility (COFRS) that are required to operate in US waters

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The claims process is intended to be simple. The claimant must first make a claim from the 'responsible party' and give them 90 days to respond. If they do not respond, then the claim can be sent to the NPFC. It is then decided by the NPFC officials on the basis of evidence produced and an offer made. The claimant has 60 days in which to accept the offer or appeal for a reassessment. Payment is normally made within 30 days of acceptance. Making a fraudulent claim is a criminal offence.

This process is not easy. To use the example of fishing, the claimant must produce a description of the business, evidence that the spill prevented them from fishing, maps of the area, witness as to loss of income, tax returns to show loss of money, wage cost, records for three years, ships logs, registration documents and licenses. All claims are put in terms of monetary value lost.

Perhaps the most interesting aspect of the NPFC administration is that the fund will not help if a claimant goes to law and tries to sue the responsible party. The claimant is perfectly free to go to law independently, but the NPFC will not fund the claimant if it does so. Effectively this discourages individual cases, leaving the NPFC to tackle the responsible party. As the claims instructions make very clear "the NPFC cannot evaluate, decide, or pay any claim that is part of a court case, including a class action suit, to recover the costs or damages in your claim."

As the NPFC has the force of the Coast Guard behind it, the process effectively means that the claimant gets his money without a court case and much more quickly. It also creates an atmosphere where the oil company responsible is pressured to respond to claimants quickly, because after 90 days, the payment assessment passes to the NPFC and out of its hands. The NPFC will then claim back whatever sum it pays out from the company. The mere threat of action by the federal system thus helps to speed up the compensation process.

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## DEEPWATER HORIZON AND BP

The clarification of liability under OPA and the OSLTF system, made it inevitable that BP would admit liability for the Deepwater Horizon, Macondo oil spill. Assuming that no case of negligence was actually found, then BP could, in theory, have limited its damages under OPA to \$75 million. However, not only was the US a major market for the company, but there was more than a fair chance that some form of negligence would be found, thus unleashing unlimited liability anyway.

By their nature, drilling rigs and production platforms are highly complex and there is thus some likelihood that mistakes will be found. The best strategy was to pay compensation as quickly as possible.

One major problem occurred very rapidly. This was the sheer volume of claims that came forward, notably from every state in the Union. Ten months after the initial spill, there were 680,000 claims and the number was still rising. Only 255,600 had actually been paid in some form or other. The claimants had three options; to go direct to BP, to go through to the NFPC after 90 days if there was no BP response, or to sue in a single or class action in the courts.

In fact, given the sheer number claims, the NFPC was largely sending claimants back to BP or rejecting them for inadequate information, since BP was supposed to be operating on the same principles as NFPC anyway. In the end, the job of processing claims was handed to the newly created Gulf Coast Claims Facility (GCCF); a body headed by Kenneth Feinberg, a distinguished arbitration lawyer with a large band of other lawyers, arbitrators and loss adjusters. This move was intended to prevent the accusation that BP was controlling the level of compensation, but critics pointed out that BP was paying for the GCCF in any case.



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The GCCF faced two complications, relevant to any system of compensation. The pressure to pay acceptable damages quickly introduced a system of 'quick payments', interim payments and payments in 'final settlement'. This enormously complicated the system, but the logic was obvious; 'quick payments' were necessary for those whose losses would bring on bankruptcy.

Secondly, the calculation of compensation through comparisons of income before and after the oil slick necessitated some kind of cut off in time for which payments would be made. It was thus pronounced that for everything other than oyster farming, all the damage would be considered finished after December 2012. This was highly controversial, since many environmentalists were convinced that the damage would last a lot longer.

Linked with this was the basis for comparison of previous income. To make a claim for lost profits required proof that oil must have caused the loss of profit and the amount claimed was appropriate. This involved providing:

- Documentation of the property or natural resources damaged, or lost
- Documentation of how income was reduced due to the damage and how much
- Documentation of profits and earnings over similar time periods
- Evidence of any savings in overheads and other normal expenses saved as a result of the slick
- Details of income from any alternative occupation taken up instead

It was thus hardly surprising that the greatest reason for turning down an application was the failure to produce enough documentation. And even if the documentation was provided, critics of the system pointed out that some people did not file taxes with the Internal Revenue Service and others that the Gulf region was only just recovering from Hurricane Katrina and thus annual comparisons of revenue lost were too low. Profits after 2005 were lower compared with before, so 2009 figures gave too low a figure for compensation.

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## LESSONS OF MACONDO

The first and obvious lesson of Macondo was that the liability limit for damages for offshore installations at \$75 million per spill was far too low, necessitating the intervention of the NPFC far too early. Had BP not admitted liability and waived its right to a cap on damages, NPFC would have quickly had to limit compensation to its own limit of \$1 billion per spill.

BP quickly set aside \$20 billion for claims and clean up and the eventual cost was around \$38 billion, far beyond the total of the existing NPFC's capacity to pay. However, if the accident had happened to a much smaller company, NPFC would have exhausted its funds very quickly.

In Congress, following the accident, there was talk about removing all limits to liability in the event of a spill, but it has generally been felt that this would not be a good idea. Obviously the limits are too small for a Macondo event, but such events are relatively rare. Removing the liability limit would be no guarantee that the company would or even could actually pay, or find insurance, but simply go bust. BP could afford to self-fund the compensation, but it was still under threat for survival. If there were to be defaults, then the OSLTF would run out of funds, even after it had increased in it per barrel tax.

However, Macondo did reveal the value of the OPA/OSLTF process. BP was in no position to behave as Exxon had done over Exxon Valdez and significant damages were paid. A significant number of class actions in the civil courts were bought by those rejecting the offers made by the GCCF. However these were considerably smaller in number than would have been the case without the OSLTF process followed by the GCCF.

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In the end, the Federal judicial system itself prevented the development of an endless litigation lasting years. A Plaintiffs Steering Committee (PSC) was formed to channel all the litigation into one negotiating body and a settlement was made out of court in late 2012. By comparison with the Exxon Valdez legal fiasco, Macondo did compensate its victims. It also sent a message to the oil industry, that massive damages could and would be awarded for oil spills.

## A EUROPEAN APPROACH

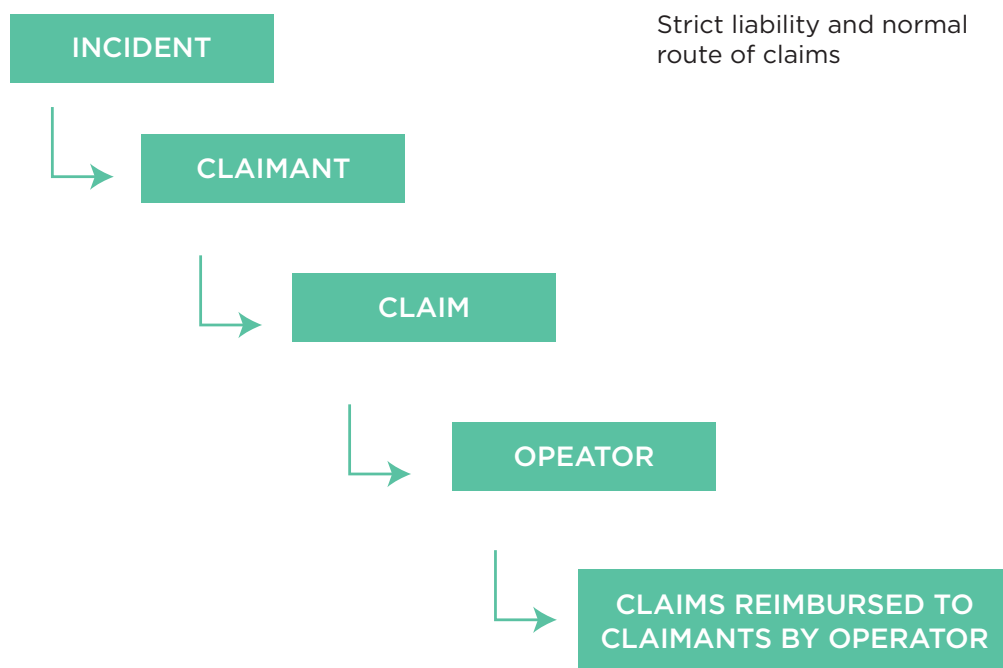
The Europeans were aware of the potential for offshore accidents from offshore oil exploration and production, causing pollution. They were also aware that the CLC/Fund system from IMO was directed at ships, not offshore installations. Consequently as North Sea oil got seriously underway, the States around the shoreline attempted to create a Convention of Civil Liability for Oil Pollution Damage Resulting from Exploration and Exploitation of Seabed Mineral Resources (CLEE).

This was adopted in 1976, but never came into force, largely because the number of States where it was seen as necessary was too small. Instead, the oil industry itself, with government encouragement, created the Offshore Pollution Liability Agreement, known as OPOL. This was initially a British initiative, but now includes Denmark, Ireland, Norway, France, Germany, the Netherlands, the Faroe Islands and Greenland. It does not, yet, include the Mediterranean or the Baltic, but it is open to any other states to join. Membership is compulsory for all those wishing to drill in the territorial waters of these countries.

OPOL defines liability and then combines it with an agreement to limit liability and creating what is in effect a mutual insurance system. The maximum liability under the system is \$250 million per incident, half of which is to cover pollution damage claims and half for remedial measures. However, if the claims are higher than the cost of clean up, the money can be transferred and vice-versa. A crucial factor is that anyone operating an installation has to maintain financial responsibility for not less than \$250 million for any incident and \$500 million annually.

There are two types of claimants. Governments and Public Authorities can claim for remedial measures taken to “prevent, mitigate or eliminated pollution damage, or to remove or neutralize the oil following an escape or discharge”. Actions by the operator can be set off against this charge, but these do not include any money spent controlling a well or measures taken to protect, repair or replace an installation.

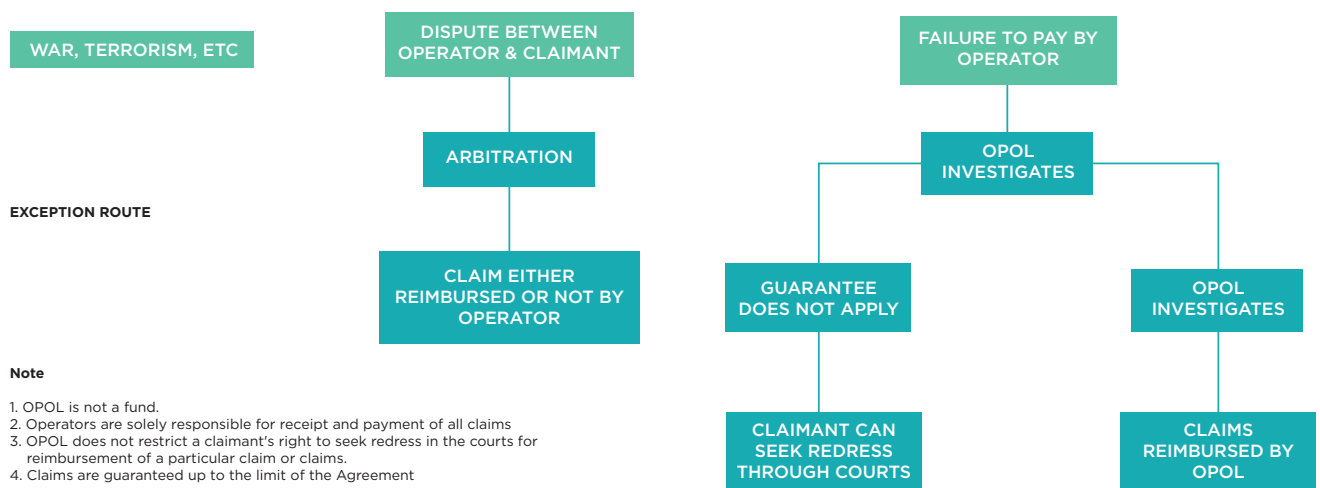
### SCHEMATIC OPOL CLAIMS PROCESS



Anyone else, including a Public Authority, “may claim compensation for pollution damage. This is defined as direct loss or damage caused by contamination, but excludes loss of or damage to the facility, which is the source of the escape or discharge of oil. Claims are made directly against the party concerned, and must be filed within one year of the date of the incident, which resulted in the escape or discharge of oil.”

If there is a failure to pay by any operator, then other operators pay for them, according to the level of their operations in the North Sea. If there is a dispute about the level of compensation, it is sent to arbitration according to the rules of International Chamber of Commerce. The OPOL agreement does not specifically rule out a claimant’s right to seek redress through the Courts for losses, which exceed the maximum recoverable under the Agreement, or those beyond the scope of the Agreement. However under the Agreement any payment made is required to be in full and final settlement of the claim against the operator. In other words, going to court is seriously discouraged if a claimant wants a quick solution.

## EXCEPTIONS



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## INCIDENTS ON LAND

The systems discussed above seem primarily related to major offshore and tanker incidents, which undoubtedly receive the greatest publicity. Certainly IMO's CFC/Fund system relates to tanker accidents. However the US OPA does relate to spills on the ground from tanks and pipelines, which is policed by the US Environmental Protection Agency, rather than the Coast Guard. In Europe, onshore spills are largely handled by general environmental legislation. In this regard, liability for such spills are largely governed by the "polluter pays principle".

First and foremost, the European Union (EU) has some 200 Directives dealing with the regulation of the environment, the latest of which is Directive 2004/35/EC. This puts the liability on the operator of an installation to remediate the land "to its baseline condition" and obliges member states to do so, if the operator does not. It does not demand compensation for those affected by the damage, although Sweden and Denmark have laws so demanding, but it does encourage NGOs and individuals to bring problems to the attention of the authorities.

The EU is currently trying to unify environmental criminal law across the union and has developed a group to co-ordinate inspections. Known as IMPEL for the Implementation and Enforcement for Environmental Law, this provides a forum for the exchange of information and any cross-border problems.

The lack of any legal demand for compensation under EU law, does not mean that anyone affected by an oil spill is purely reliant on the Civil Courts to seek damages. On the contrary, the agencies of the government are very much involved in the process.



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In England, for example, the Environment Agency, an Executive Agency responsible to the Minister for the Environment has extensive enforcement powers. It can prohibit an activity. It can issue injunctions to stop work. It can carry out remedial works and then make the polluter pay for them and it can bring criminal proceedings if relevant.

However it is has also been given new powers to introduce ‘civil sanctions’, specifically created to avoid having to take a polluter to court. There are six types of these sanctions, ranging in severity from sending a compliance notice to a polluter, demanding compliance with the law, to a ‘stop notice’, which demands the immediate end to the activity concerned. Between these are demands for restoration, a fixed or variable financial penalty and in cases where there can be no restoration, a requirement to donate significant sums to the amenities of the area affected. The central point to this is that a state agency provides support to the victims of pollution, but avoids the problems of civil court action by individuals. The agency itself is open to requests for action by the public. The process also builds up in stages. Under the scheme, a polluter may make an ‘enforcement undertaking’, which sets out what it will do to escape potential court action, and this includes compensation to the victims. This in turn must be acceptable to the Environment Agency.

In Australia, environmental protection and the enforcement of laws are handled by the individual states. However, as in England, agencies like the South Australia Environment Protection Authority have a whole battery of powers to enforce environmental regulations. Licenses can be cancelled, warnings given, and clean up orders delivered, prior to any court orders or authority-led prosecutions. If the authority is required to remediate an area, the polluter will not only be charged the cost, but an additional 25%. South Australia even has a specialist court to deal with any prosecution. Other Australian States have similar arrangements. Once again the state takes charge of the process of enforcement, not an individual or class action in the civil courts.

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It is also important to note that the agencies that enforce environmental regulations are normally connected directly to Ministries of the Environment. They enforce existing national laws, but not merely through prosecution, but also initially through letters, orders and civil sanctions. The aim is to replace private civil actions with a government-backed process that is predictable and powerful.

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## THE BASIC PRINCIPLES OF COMPENSATION SCHEMES

All these systems for damages and compensation have various things in common:

- They largely arose as a result of the recognition that the normal route to compensation in the civil courts did not work well in large accidents

They all establish strict liability, with the exceptions of war, or 'Act of God'

- This liability is limited up to a specific total
- The figure for this specific total is generally regularly revised upward, when deemed necessary
- They are largely international in extent, allowing cross-border pollution to be treated the same
- They all demand that any company operating where there is a danger of a spill has the financial resources available to meet this limit
- In the event of the liability limits being exceeded by claims, a fund is available to meet such claims
- This fund may be state operated and claimed back by the state from the responsible party or funded collectively by the potentially responsible parties, or from an insurance pool
- They all discourage claimants from taking the 'responsible party' to court, either individually or in class actions
- They try to develop a methodology to define the validity of claims, in order to standardize them, relative to the damage
- They set out a pathway by which compensations can be paid
- Significantly, the industry largely welcomed these systems, or set them up itself after major incidents
- The existence of such schemes increases the likelihood of compensation being paid rapidly
- It may also reduce the potential for extensive awards of 'punitive damages' that are unlikely to be paid

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There are obvious advantages to such schemes, not least because they take the liability to be that of the operator. This removes an area of defense against civil action and so enormously reduces the complexity of any case.

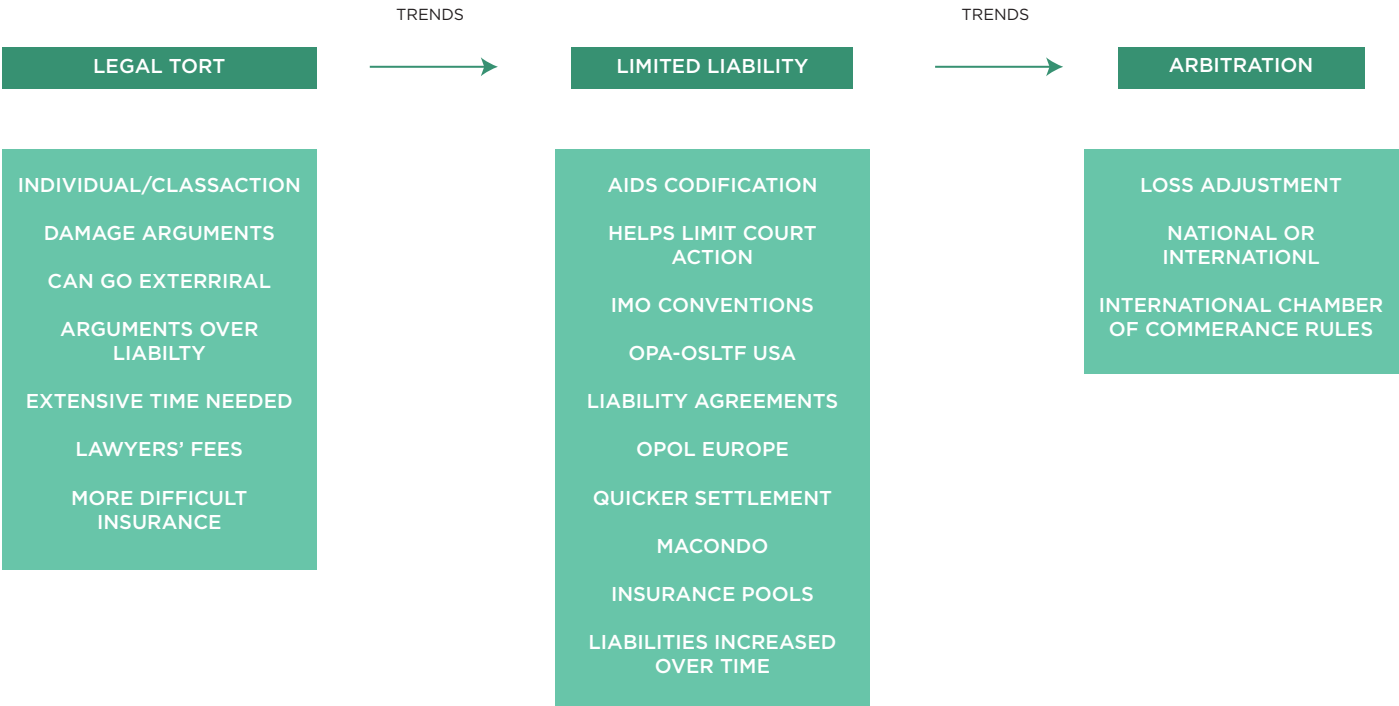
Not least of the issues facing the standard litigation in civil actions is the problem of ‘proximate cause’. Without a definition and acceptance of strict liability, an operator can argue that the incident in question was caused by a single contractor, or indeed an individual as in the case of the Exxon Valdez. The result can produce extensive technical arguments in court about what actually caused the accident.

Equally, ‘proximate cause’ problems can work to inflate damages and demands for compensation. In the Macondo case, for example, some argued that the loss of fishing opportunities impacted not just on the fisherman’s income, but on the fish retailer and then on to supermarkets in other states of the Union and indeed on the price of fish generally. Limited liability closes down potential arguments about the outward ripple effect of an accident on those not directly affected.

There is also a value in appointing a single arbiter about the amount of damages to be paid and codifying the information required to be presented by the claimant to that arbiter. This is an improvement on civil litigation, not least because the arbiter – like the US Coast Guard – will be familiar with many cases of such damage and thus with the level of compensation paid out previously. In civil litigation, the judge may operate on precedent, but not always.

Overall, the shift away from civil action in the courts towards state and industry based schemes has greatly simplified the system of clean up, remediation and compensation. Payment is quicker and more predictable. This allows the industry to insure, or at minimum predict its potential liabilities. This in turn allows the state to demand that the industry has the necessary financial resources to satisfy any future claims in the event of an incident.

COMPENSATION SYSTEMS



TRENDING AWAY FROM INDIVIDUAL CASES TOWARDS LIABILITY FUNDS AND ARBIRATION. DAMAGES TRENDING UPWARDS

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## NIGERIA'S SITUATION

In Nigeria, by contrast, the process of claiming compensation for damage caused by oil pollution is still dominated by the civil courts. Indeed, the system seems to push victims towards seeking redress in the courts, because the alternatives appear inadequate.

The legal basis for entitlement to compensation and damages comes from Sections 11 and 20 of the Oil Pipelines Act. The parameters for compensation are wide, including damage done to buildings, crops and trees. It includes disturbance to the user, damage suffered by neglect, leaking pipelines and loss in the value of the land.

The procedure requires that the claimant, be they individuals, families or communities, have to notify the company concerned, with as much detail as possible. There is then a joint investigation visit involving the claimants, their counsel, representatives of the oil company and representatives of local government. Such investigations also include the Department of Petroleum Resources (DPR) and the National Oil Spills Detection and Response Agency (NOSDRA). The requirement is to reach unanimous agreement on where culpability lies, the places negatively affected and the terms for the beginning of settlement and negotiation for adequate compensation.

The claimants may then agree with the oil companies to seek arbitration from experts, like estate valuers, soil scientists and quantity surveyors and settle the matter with the compensation paid relatively quickly. However, what happens frequently in practice, is that the offer made in compensation is according to the rates stipulated by the Oil Producer Trading Section (OPTS) of the Lagos State Chamber of Commerce. This is made up of a coalition of multinational oil companies currently operating in Nigeria. This stipulates the rates of compensation on offer, first produced in 1997 and not subsequently revised.



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While widely regarded as government sponsored, this in fact has little to do with the Government and has little ‘source credibility’. The government itself has no standardized compensation scheme, although one was created by the DPR in 1998. This outlined in great detail the amount payable for a wide variety of damage, including damage to crops, trees, fishing and waterways, allocating specific sums to each loss. It was the product of a joint effort with a variety of ministries and agencies, but unhappily never passed into law.

As a result, the current system is still largely led by the companies through OPTS. Consequently the offered rates in compensation are widely regarded as far too low and unrevised for a decade. The net result is that the quicker options of money from OPTS are widely rejected, the alternative being to take the companies to court in civil actions. Indeed, lawyers and their agents positively encourage potential claimants to do so in the hope of better offers.

As elsewhere in the world with civil action, the consequence is that the compensation system rapidly produces a large number of cases, which open up complex questions of liability and fault. However, in contrast with the US, where such cases are largely settled out of court because the companies are concerned about the escalating cost of legal action, in Nigeria, many claims actually do come to trial.

As the system allows for multiple appeals up the judicial system, the process can go on and on. These appeals are comparatively cheap for the companies if not for the claimants. The companies in particular can thus be accused of seeing the appeals system as a means to avoid payment, while for the claimant the costs escalate, even on the basis of “no-win, no fee”. Consequently when the cases are finally settled, the compensation is likely to be substantially reduced by the costs of the action. They are also likely to be very variable, depending on the judges and also at what level of the judicial system, they are awarded.

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The OPTS compensation rates are not the production of a neutral umpire, like the government. Equally they lack legal force and enforceability, being unrelated to any regulation or legislation. Where the claimants have access to legal advice and representation, the legality of the OPTS rates are usually questioned and fiercely resisted. If no arbitration is agreed, the obvious place to go is the courts.

This is particularly likely to happen if there is no agreement following the joint investigation visit. Indeed such is the mutual antipathy between the DPR and NOSDRA, that unanimous agreement as to the cause of any incident is generally unlikely. This is particularly the case where there is a suspicion and/or allegations about third-party activity, notably sabotage, artisanal refining or oil theft. Once the matter gets into the adversarial system in the courts, the possibility for a quick resolution is reduced, compensation often taking years, not least because the oil companies have – as noted – sufficient resources to appeal individual judgments, while it is also in the interests of the legal representatives of the claimants to prolong the case.

The calculation of compensation is further confused by the issue of damage done. Nigerian law recognizes four types of damages; special, general, exemplary and aggravated, with different levels of proof. General damages are those given for losses that naturally flow from the wrongful conduct of the defendant and require less proof than special damages. They can be awarded for ‘injuriously affection’ where the land of the claimant is rendered useless by the polluter. They can also be awarded for ‘disturbance’ where the loss is due to the disturbance by the polluter. No provisions are made for damages for health hazards, shock and fear, inconvenience, injury, pain and suffering, but they are available through common law.

General damages awarded by Nigerian courts are largely at the discretion of the court and the exercise of this discretion is rarely disturbed by the appellate court. Nor is the court bound by precedent. The quantum of damages is judged on the volume of oil spilt, the size of the area it affects, the population affected, any future effect on the environment and its people, whether

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the effect is continuous and whether there is a remediation plan available. The attitude of the polluter may also be taken into account.

This latter may also affect the type of damages awarded. If the conduct of the polluter is deemed to be malevolent or spiteful, then aggravated damages can be awarded. Exemplary damages can be awarded if the conduct of the polluter has been shown to be outrageous or scandalous and must be done with guilty knowledge of the economic advantage of the defendant outweighs the penalty that would ordinarily be imposed by the court where liability is established. Yet both aggravated and exemplary damages demand high standards of proof.

This lack of consistency creates its own problems for both parties to any dispute. For the companies, it makes it extremely difficult to plan financially for any prospect damages, through insurance, or insurance pool. What starts as a prospective small payment through OPTS has the capacity to grow, not merely into aggravated damages, but also – potentially – to international litigation. For the claimant, variations can cause disputes where very similar cases produce widely different results. This, in turn, propels the appeals systems higher up the judicial chain, but also may aggravate local disputes.

What is also lacking is a significant involvement of state agencies in resolving disputes through enforcement notices and ‘civil sanctions’. Nor is there a mechanism, as in the US like the NFPC, to help the claimant to seek damages. Experience has shown that the oil industry is generally rather more willing to settle compensation out of court, if the state is likely to be the principle potential opponent in judicial action.

In summary, there is no fixed government rate of approved compensation rates. The rates currently used are fixed by the oil industry. These rates are outdated and have little legal credibility. The process of dispute resolution currently involves the alternatives of mediation, arbitration, negotiation and litigation, but there is no mechanism to compel the use of these amicable forms

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of dispute resolution. Consequently litigation is the most common form of assessing damages. This process is extremely slow and complicated by procedural technicalities, which results in frustration and bitterness amongst the claimants. General damages are paid largely on the exercise of the discretionary powers vested in the courts and may well not be consistent.

There is currently no government fixed and approved system of compensation rates, that could be used as the basis for initial agreement. The DPR's set of guidelines on the issue, produced in 1998 was not gazetted. Such a state defined list, regularly updated to deal with inflation, would be a first step away from the current domination of unpredictably court action.

Finally, the whole question of liability remains difficult. While it is clear who has responsibility for clean up and remediation, the guidelines as to compensation in the event of third party action has to be not only clarified, but also more widely understood in the communities, where there are oil installations. At the moment, two state agencies, the DPR and NOSDRA are highly likely to be in conflict as to their interpretation of fault in the event of an oil spill. This regrettably fuels the potential for complexity as claims go through the judicial system.

Currently, there is no compensation system at all for spills that are caused by third-party action, merely remediation. As a consequence, many communities are blighted by the illegal actions of the few. Such third parties are rarely prosecuted. However, when they are, it would be of considerable deterrent value to such activities that they should be liable in the civil courts for the damages to those communities.

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The ideal solution to this problem would be to create a 'source credible' government list of value for losses due to pollution by either the DPR or NOSDRA. This might then be reinforced by a fund, administered by a respected body, which would not pay out in the event of any claimants going to law.

Nigeria is in a unique position in terms of compensation regime. Nowhere else in the world is the compensation system seen as a justification for actually creating damage to oil installations because of poverty. This makes the creation of a fairer and more systematic way of defining both liability and payment even more urgent here than elsewhere. While in the case of deliberate damage, liability has to be limited to clean-up costs and not compensation, this position has to be made much clearer to those living near oil installations than it currently is. This can only be done by a major programme of education in the Niger Delta and a significant improvement in relations between operators and the local civil societies.