

Protecting Taxpayers and the Environment Through Reform of Canada's Offshore Liability Regime

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A recent series of major oil pollution incidents has generated serious concern about the adequacy of Canada's oil pollution liability regimes. In Canada, distinct liability regimes govern different aspects of hydrocarbon resource development. This article assesses the statutory civil liability regime governing the exploration and production of offshore oil and gas resources. The existence of an adequate offshore liability regime is an issue of importance to all Canadians. Appropriate allocation of risks will ensure that taxpayers are protected from the financial consequences of a spill, which may amount to tens of billions of dollars in the offshore context. Appropriate allocation will also promote improved industry safety practices, thus reducing the likelihood of pollution incidents.

This article assesses the strengths and weaknesses of the various legislative components that combine to form the overarching "patchwork" civil liability regime for oil and gas activities in the Canadian offshore. It concludes

that the existing liability regime fails to adequately implement the polluter-pays principle and provides a wholly inadequate measure of protection to Canadians and the Crown against offshore-related environmental liabilities. At the same time, the existing regime fails to promote an appropriate industry safety culture, creating a moral hazard that increases the risk of a worst-case scenario oil pollution incident.

The article proposes legislative reforms to correct these flaws, including, among others, the elimination of or a substantial increase to the existing cap on an operator's absolute liability, and the explicit recognition of the availability of compensation for natural resource damages. These reforms are necessary to establish a modern liability regime that provides Canadians and the environment with an appropriate level of protection in the event of an offshore pollution incident.

Plusieurs incidents récents de pollution pétrolière majeure ont suscité de sérieuses inquiétudes quant à l'efficacité du régime canadien de responsabilité dans ce type d'affaires. Au Canada, des régimes de responsabilité distincts régissent différents aspects de l'exploitation des ressources en hydrocarbures. Cet article évalue le régime législatif de responsabilité civile concernant la recherche et l'exploitation en mer des ressources de pétrole et de gaz. La présence d'un régime de responsabilité adéquat pour l'exploitation en mer est une question importante pour tous les citoyens canadiens. Une répartition appropriée des risques permettra de s'assurer que les contribuables sont protégés contre les conséquences financières d'une marée noire, qui peuvent se chiffrer en dizaines de milliards de dollars. Cette répartition appropriée des risques promouvra aussi l'amélioration des mesures de sécurité des industries, réduisant ainsi les risques d'incidents polluants.

Cet article examine les forces et les faiblesses de diverses mesures législatives qui, une fois assemblées, forment un régime global de responsabilité civile pour les

activités pétrolières et gazières au large du Canada. La conclusion en est que le régime de responsabilité actuel ne parvient pas à implanter efficacement le principe de pollueur-payeur et offre des mesures de protection totalement inadéquates pour les Canadiens et la Couronne contre les dommages environnementaux causés en mer. Parallèlement, ce régime ne parvient pas non plus à promouvoir une culture axée sur la sécurité pour les entreprises, et ce vide juridique scabreux encourage le risque d'accidents de pollution pétrolière de la pire espèce.

Cet article propose des réformes législatives afin de remédier à ces défauts, incluant, entre autres, l'élimination de la responsabilité absolue des opérateurs ou une augmentation substantielle des limites à cette forme de responsabilité. L'article promeut également la reconnaissance explicite de des compensations disponibles pour les dommages posés aux ressources naturelles. Ces réformes sont nécessaires afin d'établir un régime de responsabilité moderne qui apporterait une protection suffisante pour les Canadiens et pour l'environnement en cas de pollution en mer.

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The purpose of this article is to assess Canada's current liability regime for one aspect of hydrocarbon resource development: offshore oil and gas operations. Section One explains the factual and political context that gives rise to the need for offshore liability reform. Section Two provides an overview of Canada's liability regime for offshore oil operations. Section Three identifies and explores the regime's weaknesses and proposes solutions thereto, while Section Four summarizes the conclusions reached and reforms proposed in this article.

1.2 BACKGROUND

A series of significant and highly publicized high-risk, low-probability oil pollution incidents has caused a groundswell of public opposition to hydrocarbon resource development in certain instances. The recent occurrence of several such incidents may be attributed to a number of causes, including: (a) the increasing scale of hydrocarbon resource development; (b) the expansion of such development into increasingly challenging environments; and (c) the deficiencies of industry safety practices and an offshore safety culture that has been corrupted by "systematic failures".¹ Offshore drilling accidents (e.g., the *Deepwater Horizon* spill in the Gulf

¹ National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, *Deep Water: The Gulf Oil Disaster and the Future of Offshore Drilling*, (United States, 2011) at vii-ix [*National Commission Report*].

of Mexico, the *Terra Nova* spill off Newfoundland,¹ and the Montara spill off Australia²) have caused significant environmental harm. The *Deepwater Horizon* disaster, for example, resulted in the oiling of over 1,000 kilometres of sensitive coastal habitats³ and affected thousands of marine creatures, including mammals, sea turtles, seabirds, and fish.⁴ The environmental impacts of the spill extend to the depths of the ocean. For example, the death of a deep-sea coral reef has been linked to the blowout.⁵ Although many of the long-term environmental impacts of the spill have yet to be determined, studies are beginning to provide disturbing insights into potential long-term impacts. One study conducted by US federal scientists found severe health problems in a population of dolphins affected by the spill.⁶

Although the environmental impacts of the *Deepwater Horizon* spill were catastrophic, the potential environmental consequences of an offshore oil spill in the Arctic or the Atlantic may be even greater. In particular, the potential consequences of an Arctic oil spill, while not fully understood, are likely to be severe, given the unique and sensitive nature of the Arctic ecosystem.⁷ For example, the Arctic's frigid climate has been found to increase the persistence of oil in the environment,⁸ and oil movement may be affected by the presence of sea ice.⁹ Wildlife in the Arctic may be more vulnerable to oil spill impacts due to cold temperatures (e.g., the decreased capacity of oiled seabirds to regulate body temperature may result in "massive acute die-off" in cold climates rather than less severe health impacts).¹⁰

¹ The *Terra Nova FPSO* drilling vessel off the coast of Newfoundland spilled an estimated 165,000 litres of oil in a 2004 incident (Canada-Newfoundland and Labrador Offshore Petroleum Board, *Annual Report 2005-2006* (St. John's, Canada: Newfoundland and Labrador Offshore Petroleum Board, 12 June 2006) at 60). No estimate of costs associated with the clean-up of the spill was provided by the report.

² The operator of the Montara well estimated clean-up costs for the well blowout to be USD \$319 million (The Honourable Martin Ferguson, "Statement by the Minister for Resources and Energy, the Hon Martin Ferguson, AM, MP: The Report of the Montara Commission of Inquiry and the Australian Government Draft Response" (Statement delivered 24 November 2010), online: Department of Resources, Energy and Tourism <<http://www.ret.gov.au/Department/Documents/MIR/montara-ministerial-statement.pdf>> at 51).

³ The 650 miles of oiled shoreline do not even represent the worst-case scenario, as "wind and currents helped keep most of the spilled oil offshore" (*National Commission Report, supra* note 1 at 173).

⁴ *Ibid* at 181.

⁵ Helen K White et al, "Impact of the *Deepwater Horizon* oil spill on a deep-water coral community in the Gulf of Mexico" (2012) 109:50 *Proceedings of the National Academy of Sciences* 20303.

⁶ US National Oceanic and Atmospheric Administration, "Study by NOAA and Partners Shows Some Gulf Dolphins Severely Ill", online: NOAA <<http://www.gulfspillrestoration.noaa.gov>>. The cause of these problems has not yet been scientifically proven, but the dolphins were studied in Barataria Bay, which was "heavily oiled for a prolonged time" during the disaster (US National Oceanic and Atmospheric Administration, "Gulf Dolphins Questions & Answers", online: NOAA <<http://www.gulfspillrestoration.noaa.gov>>).

⁷ The Pew Environment Group, *Oil Spill Prevention and Response in the U.S. Arctic Ocean: Unexamined Risks, Unacceptable Consequences*, (November 2010), online: The Pew Charitable Trusts <<http://www.pewtrusts.org>> at 3, 5 [*Pew Report*].

⁸ *Ibid* at 52.

⁹ *Ibid* at 44.

¹⁰ *Ibid* at 59.

Suboptimal response conditions are likely to compound the risks that the heightened sensitivity of Arctic ecosystems pose. The National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling (“National Commission”) noted that “favourable conditions [present in the Gulf are] not present in colder offshore energy regions.”¹¹ The Arctic offshore, in particular, presents unique environmental challenges and hazards that may impede response efforts.¹² At the same time, the sparsely populated nature of the Canadian Arctic territories renders the duplication of the massive workforce mustered for the *Deepwater Horizon* response efforts effectively impossible.¹³

The sheer magnitude of environmental harm that may be caused by an offshore accident has generated public opposition to offshore drilling in frontier areas such as the Arctic and the Gulf of St. Lawrence. In the wake of the *Deepwater Horizon* explosion and spill, for example, public opinion research indicated that 52 percent of Canadians supported at least a temporary moratorium on offshore drilling.¹⁴ Catastrophic pipeline spills (e.g., Enbridge’s

¹¹ *National Commission Report*, *supra* note 1 at 174. While the National Commission Report refers specifically to the impact of the Gulf’s warm temperature on the activity level of oil-degrading microbes, the comment is equally applicable to a variety of favourable conditions that aided *Deepwater Horizon* response efforts, such as proximity to numerous spill response resources and the absence of difficult weather conditions.

¹² Such challenges and hazards include sea ice, low-visibility conditions caused by fog and polar darkness, extreme cold, and severe weather. These challenges are compounded by the Arctic’s relative lack of infrastructure, such as navigational charts, communications systems and deep-water port facilities, as well as by the region’s vast size and remoteness: (*Pew Report*, *supra* note 8 at 65-67).

¹³ The scope of the *Deepwater Horizon* response force, totalling 45,000 responders at its peak, was facilitated by the rig’s proximity to the populous Gulf Coast states (*National Commission Report*, *supra* note 1 at 133). The size of that response force exceeds the total population of any Canadian Arctic territory. The combined population of the Yukon Territory, Northwest Territories and Nunavut is approximately 114,000. As of September 2012, the population of the Yukon Territory was 36,304 (Yukon Bureau of Statistics, *Yukon Statistical Overview*, online: Yukon Executive Council Office <<http://www.eco.gov.yk.ca>>). As of January 2013, the population of the Northwest Territories was 43,407 (Northwest Territories Bureau of Statistics, *Current Indicators*, online: Northwest Territories Bureau of Statistics <<http://www.statsnwt.ca>>). As of October 2012, the population of Nunavut was 34,028 (Nunavut Bureau of Statistics, *Nunavut Quick Facts*, online: Nunavut Bureau of Statistics <<http://www.stats.gov.nu.ca/en/home.aspx>>).

¹⁴ EKOS Politics, News Release, “Most Canadians Want Offshore Drilling Suspended or Stopped” (20 May 2010) online: EKOS Politics <<http://www.ekos.com/admin/articles/cbc-2010-05-21.pdf>> at 3. The Standing Senate Committee on Energy, the Environment and Natural Resources cited this poll in its consideration of the risks of offshore drilling in Canada (Standing Senate Committee on Energy, the Environment and Natural Resources, *Facts Do Not Justify Banning Canada’s Current Offshore Drilling Operations: A Senate Review in the Wake of BP’s Deepwater Horizon Incident, Eighth Report of the Standing Senate Committee on Energy, the Environment and Natural Resources* (2010), online: Standing Committee on Energy, the Environment and Natural Resources <<http://www.parl.gc.ca>> at 2, 9 [*Senate Committee Report*]).

Kalamazoo River system spill in Michigan¹⁵, Rainbow pipeline spill in Peace River, AB¹⁶) and oil tanker spills¹⁷ (e.g., the *Exxon Valdez* spill off Alaska, the *Prestige* spill off Spain¹⁸) have also fuelled public opposition to proposed projects such as the Keystone XL pipeline, the Northern Gateway pipeline, and increases in oil tanker traffic associated with the latter off the coast of British Columbia.

Managing both real and perceived risks of future “black swan” incidents is a difficult issue confronting all governments. Loss of public trust and confidence, caused in part by these recent events, makes it difficult for hydrocarbon resource developers to generate public support and social licence for their projects. In this context, the federal government has committed itself to “developing Canada’s extraordinary resource wealth in a way that protects the environment”¹⁹ and to “responsible resource development.”²⁰

¹⁵ As of October 31, 2011, clean-up costs associated with the Kalamazoo pipeline spill totalled approximately \$767 million (US, National Transportation Safety Board, *Pipeline Accident Report: Enbridge Incorporated, Hazardous Liquid Pipeline Rupture and Release, Marshall Michigan, July 25, 2010* (10 July 2012), online: National Transportation Safety Board <<http://www.nts.gov/doclib/reports/2012/par1201.pdf>> at 19).

¹⁶ The Rainbow pipeline in Alberta spilled an estimated 4.5 million litres of oil in 2011, resulting in clean-up and remediation costs of \$70 million (Matt McClure, “Critics seethe over lack of fines in Alberta oil spill” *Calgary Herald* (28 February 2013), online: Calgary Herald <<http://www.calgaryherald.com/news/alberta/Critics+seethe+over+lack+fines+Alberta+spill/8026456/story.html>>).

¹⁷ A recent study by the University of British Columbia Fisheries Centre examined the potential costs of an oil tanker spill incident off the North Coast region of British Columbia. For a “medium impact tanker spill of 10,000 m³ of hydrocarbons, the regional economy could suffer total losses of \$41-\$189 million in output [of ocean-based industries], 399-1,314 PYs [person-years] of employment and \$23-\$98 million in GDP over 50 years.” For a “high impact spill of 41,000 m³ of hydrocarbons...the North Coast region could experience total losses of \$87-\$308 million in output, 1,652-4,379 PYs of employment and \$72-\$205 million in GDP.” Furthermore, these figures “do not include the cost of spill response, clean-up and litigation activities (estimated to be \$2.4 billion CAD for a medium impact spill and \$9.6 billion CAD for a high impact spill) as well as the economic value of social, cultural and environmental damages.” In short, the economic harm caused by a high impact tanker spill off British Columbia’s North Coast could well exceed \$10 billion (Ngaio Hotte & U Rashid Sumaila, “Potential economic impact of a tanker spill on ocean-based industries in British Columbia” (2012) 20:7 Fisheries Centre Research Reports at 2, online: UBC Fisheries Centre <<ftp://ftp.fisheries.ubc.ca>>). By comparison, the *Exxon Valdez* spill released an estimated 11 million gallons of crude oil, which translates to 41,000 m³ (*National Commission Report*, *supra* note 1 at 70).

¹⁸ The 2002 sinking of the oil tanker *Prestige* off the coast of Spain “ended up spilling 20 million gallons of oil into the sea” and Spanish and French governments affected by the spill have initiated an action seeking approximately €4.4 billion (approximately CAD \$5.7 billion) to “cover the costs [and damages] of the spill” (Raphael Minder, “Spanish Court Opens Trial Over Giant Prestige Oil Spill” (16 October 2012), online: New York Times <<http://www.nytimes.com>>).

¹⁹ This commitment was made in the 2011 Speech from the Throne (Canada, *A Stronger Canada. A Stronger Economy. Now and for the Future. Speech from the Throne to the Open Third Session of the Fortieth Parliament of Canada*, (Ottawa: 3 March 2010) at 11, online: Speech from the Throne <<http://www.speech.gc.ca>>). See also *House of Commons Debates*, No 002 (3 June 2011) at 18 (Hon Andrew Scheer).

²⁰ Canada, *Budget Plan 2012: Jobs, Growth and Long-term Prosperity – Economic Action Plan 2012*, (Ottawa: Public Works and Government Services Canada, 2012), online: Government of Canada <<http://www.budget.gc.ca/2012/plan/pdf/Plan2012-eng.pdf>> at 87. See also *House of Commons Debates*, No 102 (29 March 2012) at 6715 (Hon Jim Flaherty).

In order to move towards these goals, the federal government must reform and modernize liability regimes that are ill-equipped to deal with the demonstrated risks of serious spill incidents occasioned by an expanding offshore industry. Certainly, such reform is a necessary component of any responsible resource development. However, the federal government must also recognize that comprehensive liability reform is only one step towards establishing a more robust environmental protection regime that prioritizes taxpayers and the Crown's role as trustee of our shared natural resources.²¹

1.3 HEEDING THE BP WAKE-UP CALL

The failings of Canadian liability regimes expose taxpayers to the proven financial risks of catastrophic environmental harm. This is particularly troubling in the wake of the *Deepwater Horizon* incident. To date, BP has paid more than \$28 billion USD in clean-up costs and private civil claim settlements for the *Deepwater Horizon* incident. This figure will increase, as remaining claims are still being resolved and does not include civil or criminal penalties imposed on BP.²²

The *Deepwater Horizon* incident and its staggering price tag raise serious questions about the adequacy of the US offshore liability regime, particularly regarding its ability to protect American governments (and taxpayers) from exposure to financial liability for the costs and damages of an oil spill.²³ Staff for the National Commission criticized the regime for failing to adequately incentivize industry to implement preventive measures, and for “limit[ing] the ability of those who suffer damages to receive full compensation.”²⁴ Staff for the National Commission highlighted this glaring weakness:

[T]he fact that BP is able to provide full monetary compensation for damages that it causes is no more than a fortuity, not a product of regulatory design. If a

²¹ See *British Columbia v Canadian Forest Products Ltd*, 2004 SCC 38 at para 76, [2004] 2 SCR 74 [*Canfor*] on the Crown's role as trustee.

²² “BP and the Deepwater Horizon disaster: Cleaning up the legal spill”, *The Economist* (15 November 2012) online: The Economist <<http://www.economist.com>> [BP and the Deepwater Horizon disaster]. The article clarifies that this figure does not include criminal penalties, for which BP has agreed to pay \$4.5 billion, and that “BP must still settle federal and state claims for compensation for environmental damage to the Gulf coast states – perhaps \$5 billion or more - and private civil claims as yet unsettled.”

²³ The *Deepwater Horizon* incident generated a groundswell of academic literature in the United States, but the disaster's implications in the context of Canada's offshore liability regime have received little consideration. The most recent academic consideration of the Canadian offshore liability regime provided a cursory overview of the legal framework (Wylie Spicer & Tanya Bath, “The Canadian Arctic: The Changing Seascape of Offshore Oil and Gas Exploration Issues” (2010) 48 *Alta L Rev* 255). Much of the literature concerning the Canadian offshore liability regime is decades old: see the materials surveyed in A William Moreira, Cecily Y Strickland & David G Henley, “Liability for Marine Pollution from Offshore Operations” (2003) 26 *Dal LJ* 429; Edgar Gold, David VanderZwaag & Meinhard Doelle, “Economic loss and environmental damages: developments in claims for offshore oil pollution” (1991) 1 *J Envtl L & Prac* 129.

²⁴ Staff of National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, *Liability and Compensation Requirements under the Oil Pollution Act: Staff Working Paper No. 10*, online: National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling <<http://www.oilspillcommission.gov>> at 1, 5 [*Staff Working Paper No 10*].

company with less financial means had caused the spill, the company would likely have declared bankruptcy long before paying anything close to the damages caused.²⁵

The *Deepwater Horizon* incident raised similar concerns in Canada, spurring the Standing Senate Committee on Energy, the Environment and Natural Resources to recommend “a comprehensive review of the issue of liability, including whether the thresholds should be adjusted to reflect current economic realities,”²⁶ and leading the National Energy Board to conduct a *Public Review of Arctic Safety and Environmental Offshore Drilling Requirements* (“*Arctic Offshore Drilling Review*”) that examined, among other issues, the Canadian Arctic offshore liability regime.²⁷ The National Energy Board began public consultations on updated financial responsibility requirement guidelines in early 2013 as one component of a broader effort, initiated by the *Arctic Offshore Drilling Review*, to foster a more robust industry safety culture.²⁸ The *Arctic Offshore Drilling Review* also provided civil society members with an opportunity to voice serious concerns with Canada’s offshore liability regime, and groups such as Oceans North,²⁹ WWF,³⁰ and Ecojustice³¹ have consistently advocated for liability reform.

Natural Resources Canada is currently assessing options to reform the offshore liability regime, and to that end convened an “invitation only” meeting of regulators, industry representatives, academics and environmental groups in October 2012.³² The extent of consultations with aboriginal groups as part of this initiative is unknown, but given the importance of the *Inuvialuit Final Agreement* (“*IFA*”)³³ as a component of the overall liability regime, the

²⁵ *Ibid.*

²⁶ *Senate Committee Report*, *supra* note 15 at 5.

²⁷ National Energy Board, *Review of Offshore Drilling in the Canadian Arctic* (Canada: National Energy Board, 2011) at 47-48 [*Arctic Offshore Drilling Review*]. See also National Energy Board, *Appendix B: Backgrounder – Financial Responsibility and Liability*, online: National Energy Board <<https://www.neb-one.gc.ca>> [*NEB Liability Backgrounder*]. Neither of these documents considered offshore drilling liability in the Gulf of St. Lawrence.

²⁸ National Energy Board, *Draft Financial Viability and Financial Responsibility Guidelines*, online: NEB, <<http://www.neb-one.gc.ca/clf-nsi/rpblctn/ctsndrgltn/rgltnsdgdlnsprnttthtrct/cndlnsgsprntstct/fnnclvbltyrspnsbltygdln/drftfnnclvbltyrspnsbltygdln-eng.pdf>>.

²⁹ Louie Porta & Nigel Bankes, *Becoming Arctic-Ready: Policy Recommendations for Reforming Canada’s Approach to Licensing and Regulating Offshore Oil and Gas in the Arctic* (2011) at 6-8, online: Oceans North Canada <<http://oceansnorth.org>> [*Becoming Arctic-Ready*]. The report was submitted to the *Arctic Offshore Drilling Review* and can be accessed, along with supporting documents online: National Energy Board <<https://www.neb-one.gc.ca>>.

³⁰ WWF and Ecojustice submitted joint comments to the *Arctic Offshore Drilling Review*. Chapter 8 of the joint comments addresses the issue of liability reform (World Wildlife Fund & Ecojustice, *Arctic Offshore Drilling Review: Additional Response to CFI #1 and #2*, 1 April 2011, online: WWF Canada <http://awsassets.wwf.ca/downloads/wwf_canada_submission_to_neb_review_april_2011.pdf> at 56-65).

³¹ *Ibid.* One author has been advocating for liability reform since 2010. See Will Amos, “If there’s an oil spill, who’s at risk? Canadian taxpayers” *The Globe and Mail* (14 July 2010), online: The Globe and Mail <<http://www.theglobeandmail.com>>.

³² The authors of this report were invited to and personally attended this meeting.

³³ *The Western Arctic Claim: Inuvialuit Final Agreement as Amended*, between the Committee for Original Peoples’ Entitlement & the Government of Canada, 15 January 1987, online: Inuvialuit Regional Corporation <<http://www.inuvialuitland.com>> [*IFA*].

Inuvialuit (along with other Inuit rights holders) will have important contributions to make in this regard.

With Imperial Oil having recently released its preliminary information plans for future Beaufort Sea exploratory drilling,³⁴ and with the federal Commissioner of the Environment and Sustainable Development having tabled in Parliament an audit report calling for reforms to the laws governing liability for offshore oil spills in early 2013,³⁵ the time is ripe for legislative and regulatory reform. In light of the demonstrated environmental and financial risks facing Canadians in the event of a major oil spill,³⁶ we argue that Canadian voters will support a federal initiative to modernize and strengthen the liability regime not only for the offshore industry, but for all facets of hydrocarbon resource development, including pipelines and tanker shipping.³⁷

1.4 THE NEED FOR LIABILITY REFORM

Implementation of the “polluter-pays” principle lies at the heart of any environmental liability regime. This principle, as it has been defined by the Supreme Court of Canada, “assigns polluters the responsibility for remedying contamination for which they are responsible and imposes on them the direct and immediate costs of pollution.”³⁸ The environmental protection aspect of liability regimes is equally significant.³⁹ An appropriate liability regime can decrease the risk of environmental harm by rewarding improved industry safety practices. Fundamentally, the strength of a statutory civil liability regime depends on the degree to which it:

- guarantees full and fair compensation in the event of a pollution incident; and
- encourages behaviour modification within industry to minimize the risk of environmental harm.

³⁴ Imperial Oil Resources Ventures Limited, *Beaufort Sea Exploration Joint Venture: Preliminary Information Package* (December 2012), online: Imperial Oil <<http://www.imperialoil.com>>; “Imperial Oil lays out preliminary plans to drill in the Beaufort Sea” *Times Colonist* (17 December 2012), online: Times Colonist <<http://www.timescolonist.com>>.

³⁵ Canada, Office of the Auditor General of Canada, *Report of the Commissioner of the Environment and Sustainable Development. Chapter 2: Financial Assurances for Environmental Risk* (Ottawa: Public Works and Government Services, 2012) at 19-20, online: Office of the Auditor General of Canada <<http://www.oag-bvg.gc.ca>>.

³⁶ Canada, Office of the Auditor General of Canada, *Report of the Commissioner of the Environment and Sustainable Development: The Commissioner’s Perspective* (Ottawa: Public Works and Government Services, 2012) at 5, online: Office of the Auditor General of Canada <<http://www.oag-bvg.gc.ca>>.

³⁷ The federal government may share the belief that voters will support such reform, with Minister of the Environment Peter Kent acknowledging that the government is “well aware” of the need to overhaul federal laws governing civil liability for offshore oil spills and pledging “significant” changes to those laws (Margo McDiarmid, “Polluters to face greater liability for offshore drilling spills” *CBC News* (30 January 2013), online: CBC News <<http://www.cbc.ca>>).

³⁸ *Imperial Oil Ltd v Quebec (Minister of the Environment)*, 2003 SCC 58 at para 24, [2003] 2 SCR 624 [*Imperial Oil*].

³⁹ “At the same time, polluters are asked to pay more attention to the need to protect ecosystems in the course of their economic activities” (*ibid*).

Communities and individuals in close proximity to industrial activities are at risk of suffering significant losses and damages from pollution (including, but not limited to, major spills) caused by those activities, and are entitled to a liability regime that guarantees full and fair compensation. Meanwhile, governments (whether federal, provincial, territorial, or aboriginal) that are legally bound to steward public resources are right to question the environmental protection and risk management aspects of the liability regimes, on behalf of present taxpayers and future generations. Given the low absolute liability limits and uncertain coverage of natural resource damages provided by current liability regimes, these regimes amount to an industry subsidy as they disproportionately shift the risks and the burdens of offshore oil and gas activities from industry to taxpayers. This subsidy creates a moral hazard⁴⁰ by allowing industry to retain the benefits of engaging in high-risk, high-reward behaviour such as offshore drilling without bearing the full risks thereof. The aftermath of the *Deepwater Horizon* blowout exposed this moral hazard:

[T]he 1990 Oil Pollution Act capped firms' liability for economic damages from oil spills at \$75 million, and this cap effectively shields companies from responsibility for their decisions. This misalignment of incentives is a classic case of what economists like to call moral hazard. Firms just behave differently when they are protected from the consequences of their decisions.⁴¹

In this context, liability reform is an issue of fiscal responsibility of significant importance to all Canadian taxpayers.

Beyond demonstrating sensitivity towards the concerns of voters, liability reform also presents the government with an opportunity to develop world-class standards that befit a global energy producer. An investment in liability reform will yield twin benefits: appropriate allocation of risks will incent industry to improve safety practices, reducing the likelihood of pollution incidents, and will also ensure that taxpayers are protected from the financial consequences of a spill. Ultimately, liability reform will benefit industry, insofar as it represents an important step towards securing a social license to operate and allaying public concerns over such development.

⁴⁰ A moral hazard occurs where a person “exposes themselves to risk and does not fairly assume the full consequences and responsibilities of their actions” (Garrett Dolan & Davin J Wallace, “Policy and management hazards along the Upper Texas coast” (2012) 59 *Ocean Coast Management* 77 at 78). Consequently, the person is encouraged to accept risks that would not otherwise be acceptable, “knowing that if there is a catastrophic failure a third party, often society, will shield them from their loss.” Although the concept of moral hazard arose initially in the insurance context, economists have more recently “conceptualized moral hazards as inefficiencies in the market system whereby risks are dissociated from gains” (*ibid*).

⁴¹ US, *Liability and Financial Responsibility for Oil Spills under the Oil Pollution Act of 1990 and Related Statutes: Hearing Before the Committee on Transportation and Infrastructure, House of Representatives*, 111th Cong (2010) at 30 (Michael Greenstone, MIT).

While recognizing that the liability regimes for pipeline⁴² and shipping activities⁴³ could also benefit from reform and modernization, the article will focus on analyzing the adequacy of the current Canadian liability regime for offshore oil and gas operations as a tool for both promoting desirable industry practices (safety culture) and alleviating taxpayer exposure to environmental liabilities. The article will subsequently assess options for potential changes to Canada's offshore liability regime. In doing so, the article will consider the liability regimes in place across the world and the post-*Deepwater Horizon* debate in the United States concerning liability reform, while recognizing Canada's unique circumstances and context. Despite the paper's relatively narrow focus, many of the problems and recommendations pertaining to the offshore liability regime will be relevant and transferable to other liability regimes.

2. THE LIABILITY REGIME FOR OFFSHORE OIL OPERATIONS IN CANADA

2.1 VARIOUS STATUTES AND REGULATIONS COMBINE WITH THE COMMON LAW TO ESTABLISH THE OFFSHORE LIABILITY REGIME

In the environmental context, the fundamental purpose of a statutory civil liability regime is to give effect to the polluter-pays principle, which "has become firmly entrenched in environmental law in Canada."⁴⁴ In the context of offshore oil operations, the statutory civil liability regime implicitly aims to ensure that victims of pollution damage are compensated for their losses by the party responsible for the pollution.⁴⁵

⁴² Offshore pipeline liability, like offshore liability, is governed by the *Canada Oil and Gas Operations Act*, RSC 1985, c O-7 [*COGOA*], the *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act*, SC 1988, c 28 [*NS Accord Act*], and the *Canada-Newfoundland Accord Implementation Act*, SC 1987, c 3 [*NL Accord Act*] where these acts apply. The *Arctic Waters Pollution Prevention Act*, RSC 1985, c A-12 [*AWPPA*], and the *Fisheries Act*, RSC 1985, c F-14 [*Fisheries Act*] may also apply. Onshore pipeline liability is governed by *COGOA* in the Northwest Territories, Nunavut and Sable Island, as well as in submarine areas within Canada's internal waters that do not fall within a province (*ibid*, s 3). Onshore pipelines are regulated by the provinces where the pipelines do not cross provincial boundaries and are subject to provincial liability regimes: see e.g. *Pipeline Act*, RSA 2000, c P-15, s 36. Onshore interprovincial pipelines are regulated by the National Energy Board pursuant to the *National Energy Board Act*, RSC 1985, c N-7; see also *National Energy Board Onshore Pipeline Regulations*, SOR/99-294. Although the federal onshore pipeline regulatory regime establishes goals of environmental protection (see e.g. *ibid*, s 48, which provide that: "[a] company shall develop, implement and maintain an environmental protection program that anticipates, prevents, manages and mitigates conditions that could adversely affect the environment") it does not expressly incorporate civil liability provisions.

⁴³ Liability for oil spills caused by ships, including oil tankers, is governed by a number of federal statutes. Of primary importance are the *Marine Liability Act*, SC 2001, c 6 [*MLA*] and the *AWPPA*, *supra* note 43.

⁴⁴ *Imperial Oil*, *supra* note 39 at para 23.

⁴⁵ See e.g. *COGOA*, *supra* note 43, s 25(7), which imposes unlimited strict liability on polluters for spill response costs. Section 26's limited absolute liability regime implicitly adopts the polluter-pays principle by imposing "exceptional" and "rarely seen" compensation requirements on polluters: see *Arctic Offshore Drilling Review*, *supra* note 28 at 47 on the exceptional nature of absolute liability.

The governance of oil spill liability has been described, in the US context, as a “patchwork”⁴⁶ where any single law “is far from the only legal determinant of oil spill liability”:⁴⁷

[T]he wide range of applicable laws makes resolution of oil spill liability exceedingly complex. Principles of strict liability and channelling reduce that complexity somewhat by reducing the number of determinations that must be made by courts. But the availability of different legal regimes (civil or criminal) and jurisdictions (state and federal) [adds] significant complexity and uncertainty before litigation even reaches the trial phase. The existence of liability limits (and exceptions to them that must be explored by courts) adds complexity to the damages phase of litigation as well. Litigation over the *Deepwater Horizon* spill is likely to proceed along all of these pathways. The end result is substantial uncertainty for both victims and responsible parties.⁴⁸

The complexity of the US offshore liability regime is mirrored by that of the Canadian offshore liability regime, where the underlying common law, which establishes private law remedies for victims of spill damage, is augmented by a statutory civil liability regime.⁴⁹ Three main laws establish the statutory civil liability regime for offshore oil operations in Canada: the *Canada Oil and Gas Operations Act* (“COGOA”), the *Canada-Newfoundland Atlantic Accord Implementation Act*, and the *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act* (“Accord Acts”). While the latter two laws concern liability in the Newfoundland and Nova Scotia offshore oil fields under joint federal-provincial jurisdiction, the former concerns the liability in the remainder of Canada’s offshore areas, including the Arctic, which falls under purely federal jurisdiction.⁵⁰ A number of regulations complement these statutes, including COGOA’s *Oil and Gas Spills and Debris Liability Regulations*.⁵¹ Finally,

⁴⁶ Nathan Richardson, *Deepwater Horizon and the Patchwork of Oil Spill Liability Law* (Washington, DC: Resources for the Future, 2010) at 1, online: Resources for the Future <<http://www.rff.org>>.

⁴⁷ *Ibid* at 3.

⁴⁸ *Ibid* at 5.

⁴⁹ This article focuses on the civil liability regime for offshore oil and gas operations. It does not consider the potential criminal liabilities that may arise from an oil spill.

⁵⁰ Sections 91, 92 and 92A of Canada’s *Constitution Act, 1867* allocate law-making powers between the federal and provincial governments. The territories are not granted constitutional law-making powers. Typically, the provincial governments have legislative jurisdiction over matters of regional or local significance, such as the exploitation of natural resources within the province and the solemnization of marriage within the province (*Constitution Act, 1867* (UK), 30 & 31 Vict, c 3, ss 92A(1), 92(12), reprinted in RSC 1985, App II, No 5 [*Constitution Act, 1867*]). The federal government is given legislative jurisdiction over matters of national significance, including the postal service, the military, and currency (*ibid* at ss 91(5), (7), (14)). Furthermore, the federal government has the residual power to make laws for the peace, order and good government of Canada with respect to any matter not within the exclusive jurisdiction of the provinces. Some matters, such as the environment, are not assigned to the exclusive jurisdiction of either level of government. With respect to these matters, both the federal and provincial governments can enact valid legislation.

⁵¹ SOR/87-331 [*Liability Regulations*]. Equivalent regulations exist in Nova Scotia (*Canada-Nova Scotia Oil and Gas Spills and Debris Liability Regulations*, SOR/95-123 [*NS Liability Regulations*]) and in Newfoundland (*Canada-Newfoundland Oil and Gas Spills and Debris Liability Regulations*, SOR/88-262 [*NL Liability Regulations*]).

in certain circumstances, offshore oil and gas operations may attract civil liability under the *Arctic Waters Pollution Prevention Act*,⁵² the *IFA*,⁵³ and/or the federal *Fisheries Act*.⁵⁴

These distinct statutory regimes provide wholly inadequate protection to Canadians and the Crown against offshore oil-related environmental liabilities.

2.2 DISTINGUISHING OFFSHORE LIABILITY RULES, REGULATORY OFFENCES, AND FINANCIAL RESPONSIBILITY (ASSURANCE) REQUIREMENTS

2.2.1 OFFSHORE LIABILITY RULES AND REGULATORY OFFENCES

Pollution caused by offshore oil operations can also attract regulatory penalties, including fines or imprisonment.⁵⁵ In particular, regulatory liability can be triggered by causing or permitting a spill,⁵⁶ by failing to report a spill,⁵⁷ or by engaging in offshore activities without approval.⁵⁸ Regulatory offences must be distinguished from statutory civil liability provisions. In *R v Wholesale Travel Group Inc.*, the Supreme Court of Canada noted that:

The objective of regulatory legislation is to protect the public or broad segments of the public...from the potentially adverse effects of otherwise lawful activity...[R]egulatory measures are generally directed to the prevention of future harm through the enforcement of minimum standards of conduct and care.”⁵⁹

Penalties for regulatory offences are intended to promote objectives of “punishment along with deterrence of further violations.”⁶⁰ In short, regulatory penalties are compliance tools that aim to ensure that “considerable emphasis is placed on the goal of environmental protection in the public interest that underpins the overall regulatory regime.”⁶¹ They are not intended to compensate for environmental damage that does occur, nor are they intended to protect governments and taxpayers from the risk of spill-related environmental liabilities.

⁵² *AWPPA*, *supra* note 43.

⁵³ *IFA*, *supra* note 34 at s 13.

⁵⁴ *Fisheries Act*, *supra* note 43, s 42. This will be discussed in greater detail below.

⁵⁵ *COGOA*, *supra* note 43, s 60(2) provides for fines of up to \$1 million and imprisonment for up to five years for contravening the statute. See also *NS Accord Act*, *supra* note 43, s 199(2); *NL Accord Act*, *supra* note 43, s 194(2).

⁵⁶ *COGOA*, *supra* note 43, s 25(1) prohibits causing or permitting a spill and contravention of the prohibition constitutes an offence pursuant to s 60(1)(a). See also *NS Accord Act*, *supra* note 43, s 199(1)(a); *NL Accord Act*, *supra* note 43, s 194(1)(a).

⁵⁷ *COGOA*, *supra* note 43, s 25(2) imposes reporting requirements on offshore operators, and contravention of such requirements constitutes an offence pursuant to s 60(1)(a). See also *NS Accord Act*, *supra* note 43, s 199(1)(a); *NL Accord Act*, *supra* note 43, s 194(1)(a).

⁵⁸ *COGOA*, *supra* note 43, s 60(1)(c) makes it an offence to carry on offshore activities without obtaining approval in accordance with s 5(1)(b). See also *NS Accord Act*, *supra* note 43, s 199(1)(e); *NL Accord Act*, *supra* note 43, s 194(1)(e).

⁵⁹ *R v Wholesale Travel Group Inc.*, [1991] 3 SCR 154 at 219, 84 DLR (4th) 161.

⁶⁰ Jamie Benidickson, *Environmental Law*, 3d ed (Toronto: Irwin Law, 2009) at 179.

⁶¹ *Ibid.*

By contrast, statutory civil liability provisions are primarily compensatory in nature, building on the existing common law tort architecture.⁶² Rather than promoting compliance with legislation, statutory civil liability provisions are intended to ensure that victims of pollution incidents receive appropriate compensation from the party responsible for the pollution. Statutory civil liability provisions aim to achieve these objectives by facilitating access to private law remedies that provide direct compensation to an injured person for certain losses. These provisions facilitate access to these remedies in two ways. First, they reduce the evidentiary burdens on plaintiffs.⁶³ Second, these provisions dispense with the need to establish elements typically required in common law tort claims, such as “the obligation to show that the defendant owed [the plaintiff] a duty of care, or of establishing the relevant standard of care which the defendant failed to meet.”⁶⁴ The imposition of absolute liability and the “channeling” of liability further simplify litigation.⁶⁵

In light of this distinction, this article will focus on statutory civil liability provisions applicable to the offshore industry, evaluating how they aim to implement the polluter-pays principle and ensure that governments and taxpayers are not held responsible for environmental liabilities arising from an offshore oil pollution incident.

2.2.2 OFFSHORE LIABILITY RULES AND FINANCIAL RESPONSIBILITY REQUIREMENTS

A distinction must also be made between liability rules and financial responsibility (or assurance) requirements imposed by regulators as a condition of drilling authorization. These distinct components of an overarching liability regime are often conflated. They are related insofar as financial responsibility requirements support the effective operation of the liability rules by ensuring that potential polluters have the financial wherewithal to compensate affected parties in the event of a spill. However, they are separate components of a comprehensive regime: financial responsibility requirements are designed to ensure that a potential polluter has the ability to pay,⁶⁶ while liability provisions are designed to establish rules pursuant to

⁶² Although statutory civil liability rules provide important behaviour modification incentives for industry to improve safety practices and decrease moral hazard, such incentives lack a punitive objective.

⁶³ Through the establishment of strict or absolute liability regimes: see e.g. *COGOA*, *supra* note 43, s 26.

⁶⁴ Benidickson, *supra* note 61 at 115. The need to establish these common law elements is obviated by the creation of a statutory civil cause of action: see e.g. *Canadian Environmental Protection Act, 1999*, SC 1999, c 33, s 40 [*CEPA*].

⁶⁵ Richardson, *supra* note 47 at 2. Note that this is an American text, so discussion of “strict liability” refers to “absolute liability” in Canada. Statutory civil liability provisions “channel” liability onto a pre-determined party, often the operator, by “specifying exactly who is to be treated as the responsible party for liability purposes” (*ibid*).

⁶⁶ “Proof of financial responsibility might include letters of credit, bonds, insurance, guarantees and audited financial statements” (*NEB Liability Backgrounder*, *supra* note 28 at 1). In the past, the Nova Scotia and Newfoundland Offshore Petroleum Boards have sought proof of financial responsibility in the amount of \$350 million, while the NEB has required proof of financial responsibility in the amount of approximately \$1 billion in the Arctic (House of Commons, Standing Committee on Natural Resources, *Evidence*, 40th Parl, 3rd Sess, No 022 (15 June 2010) at 10). See also Canada-Nova Scotia Offshore Petroleum Board & Canada-Newfoundland and Labrador Offshore Petroleum Board, *Guidelines Respecting Financial Responsibility Requirements for Work or Activity in the Newfoundland and Nova Scotia Offshore Areas* (St. John’s: Canada-Newfoundland and Labrador Offshore Petroleum Board, 2000), online: The Canada-Newfoundland and Labrador Offshore Petroleum Board <<http://www.cnlpb.nl.ca>>.

which a person responsible for a spill would have to pay. In short, the financial responsibility requirements imposed on operators of offshore facilities must be distinguished from the liability rules set out in section 26 of *COGOA*.⁶⁷ Financial responsibility requirements effectively prevent undercapitalized or otherwise unqualified operators from engaging in inherently risky offshore oil operations. In effect, these requirements limit access to Canada's offshore to large, experienced oil companies. The appropriate threshold of financial assurance is set, on a project-specific basis, pursuant to the regulator's assessment of various risk factors (e.g., drilling depth, flow rates, geological features). While operators predictably oppose the carrying costs associated with financial assurance,⁶⁸ the National Energy Board has unequivocally declared its support for financial responsibility requirements in the Arctic offshore, stating that:

[W]e find it desirable that sufficient financial resources be available to address loss or damage ... and that a portion of these funds be available to quickly compensate people of the Arctic.⁶⁹

2.3 *COGOA* AND THE *ACCORD ACTS*

Until 1992, offshore oil and gas operations were primarily regulated pursuant to the *Oil and Gas Production and Conservation Act*. In 1992, the federal government made significant amendments to the *Oil and Gas Production and Conservation Act*, including renaming the statute the *Canada Oil and Gas Operations Act* ("*COGOA*").⁷⁰ The amendments established, for the first time, an explicit set of purposes to be achieved through the regulation of offshore oil and gas operations: to promote safety, environmental protection, conservation of hydrocarbon resources, joint production arrangements and economically efficient infrastructures.⁷¹

The *Canada-Newfoundland Atlantic Accord Implementation Act*, enacted in 1987, and the *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act*, enacted in 1988, implement federal-provincial agreements respecting the joint management of hydrocarbon resources in the Atlantic offshore. The *Accord Acts* set out purposes that are substantially the same as those set out in *COGOA*.

COGOA and the *Accord Acts* govern a wide range of activities, including "the exploration and drilling for and the production, conservation, processing and transportation" of offshore

⁶⁷ This distinction between financial responsibility requirements and rules of liability is mirrored in the US *Oil Pollution Act of 1990*, which requires a responsible party with respect to an offshore facility to provide evidence of its financial responsibility (i.e., ability to pay compensation were a spill to occur) in an amount that may range from \$10 million to \$150 million (*Oil Pollution Act of 1990*, 33 USC §§ 2716(c)(1)(B)-(C) (2012) [*OPA*]). However, these requirements impose no liability on the responsible party with respect to potential pollution incidents. Instead, separate rules of liability render a responsible party liable for certain response costs and damages associated with a spill (*ibid* at § 2702).

⁶⁸ It should be noted that the amount required to prove financial responsibility need not equal the amount of maximum liability imposed on operators. Indeed, the NEB "has full discretion over the forms and amounts of the financial responsibility that the operator must put in place" (*NEB Liability Background*, *supra* note 28 at 1).

⁶⁹ *Arctic Offshore Drilling Review*, *supra* note 28 at 48.

⁷⁰ Bill C-58, *An Act to amend the Oil and Gas Production and Conservation Act and other Acts in consequence thereof*, 3rd Sess, 34th Parl, 1992, cl 2 (assented to 23 June 1992), SC 1992, c 35 [*Bill C-58*].

⁷¹ *Ibid*, cl 4. See also *COGOA*, *supra* note 43, s 2.1.

hydrocarbon resources.⁷² All three statutes regulate these activities through the imposition of pre-operation licensing requirements.⁷³ The statutes also regulate several of the financial and physical aspects of operation, including such matters as production arrangements and the prevention of and liability for spills.⁷⁴ The spills and liability provisions in all three acts are substantially the same,⁷⁵ and apply to a broad spectrum of spill accidents, ranging from minor operational discharges⁷⁶ to large-scale catastrophic loss of well-control events (i.e., blowouts).

The core elements of the *COGOA* liability regime include:

- regulatory imposition of financial responsibility (assurance) requirements on the operator⁷⁷;
- prohibition against causing or permitting a spill;
- imposition of a duty on the operator to take all reasonable spill response measures and, where a third party is ordered to undertake reasonable spill response measures, imposition of unlimited liability on the operator for all costs of such measures;
- imposition of limited absolute liability on the operator for all actual loss or damage resulting from a spill and for the costs and expenses of all reasonable government and third-party voluntary spill response measures;
- establishment of a maximum absolute liability limit;

⁷² *COGOA*, *supra* note 43, s 3; *NS Accord Act*, *supra* note 43, s 139; *NL Accord Act*, *supra* note 43, s 136.

⁷³ *COGOA*, *supra* note 43, ss 5-5.37; *NS Accord Act*, *supra* note 43, ss 142-143.2; *NL Accord Act*, *supra* note 43, ss 138-139.2.

⁷⁴ *COGOA*, *supra* note 43, ss 24-48; *NS Accord Act*, *supra* note 43, ss 165-188; *NL Accord Act*, *supra* note 43, ss 160-183. It should be noted that the *Accord Acts* also create joint federal-provincial offshore regulatory boards and set out a regime for issuing interests in offshore hydrocarbon resources (*NS Accord Act*, *supra* note 43, ss 9(1), 49-137; *NL Accord Act*, *supra* note 43, ss 9(1), 47-134).

⁷⁵ For the sake of clarity, subsequent references are to provisions in *COGOA*, with footnotes to the corresponding provisions in the *Accord Acts*, unless otherwise indicated. References in the text to the National Energy Board should, when referring to the relevant provisions of the *Accord Acts* in the footnotes, be taken to mean the Canada-Nova Scotia Offshore Petroleum Board or the Canada-Newfoundland and Labrador Offshore Petroleum Board, as the case may be.

⁷⁶ The liability provisions apply even to “any discharge, emission or escape of oil or gas that is authorized by regulation”: see *COGOA*, *supra* note 43, s 26(1); *NS Accord Act*, *supra* note 43, s 167(1); *NL Accord Act*, *supra* note 43, s 162(1).

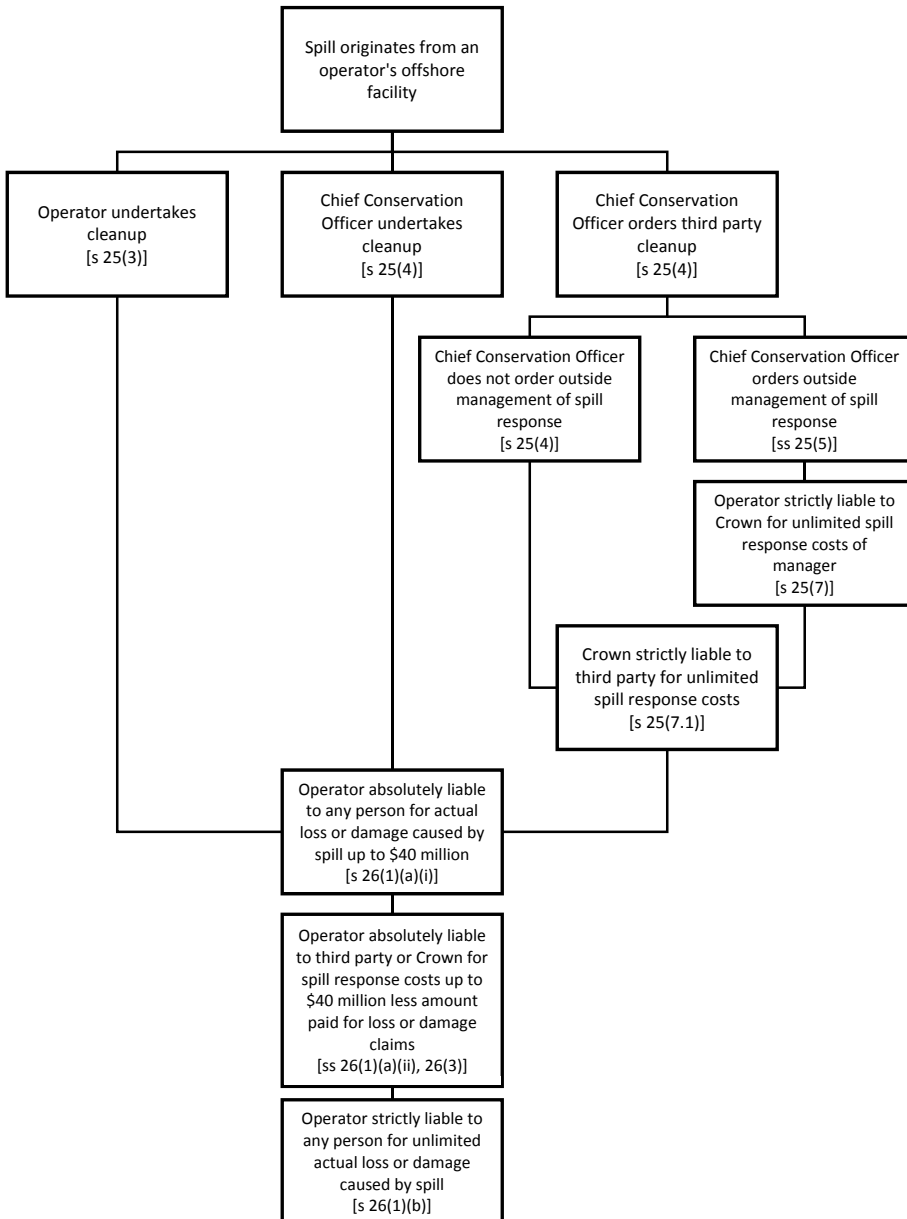
⁷⁷ The “operator”, for the purposes of the *COGOA* liability regime, is the person who obtained an authorization under s 5(1)(b) of *COGOA* to carry on the offshore activity. Such an authorization is available to the holder of an operating licence (*Canada Oil and Gas Operations Regulations*, SOR/83-149, s 3). A corporation or any individual who is 18 years of age or older may apply for an operating licence (*ibid*, ss 3(1)(a-c)). Similarly, operators under the *Accord Acts* are those individuals or companies that obtain authorization to carry on the offshore activity (*NS Accord Act*, *supra* note 43, s 142(1)(b); *NL Accord Act*, *supra* note 43, s 138(1)(b), *Newfoundland Offshore Area Oil and Gas Operations Regulations*, SOR/88-347, s 3). Although an individual may technically be an operator, the operator will typically be an oil or gas company. For example, operators in the Newfoundland offshore during 2011-2012 included Statoil, Husky and Suncor (Canada-Newfoundland and Labrador Offshore Petroleum Board, *Annual Report 2011-12*, at 22-23, online: CNLOPB <<http://www.cnlopb.nl.ca>> [*CNLOPB Annual Report 2011-12*]).

- imposition of unlimited fault-based (strict) liability on the operator; and
- prohibition against operator exposure to double liability.

Conspicuously absent from the *COGOA* regime is any explicit recognition of the polluter-pays principle.

Figure 1 provides an extremely simplified representation of the *COGOA* liability regime as it applies in the Arctic offshore.

Figure 1: Simplified *COGOA* Liability Regime



2.3.1 *FINANCIAL RESPONSIBILITY REQUIREMENTS ARE IMPOSED ON THE OPERATOR AS A CONDITION OF DRILLING AUTHORIZATION*

Prior to obtaining an authorization for offshore operations, the operator is required to “provide proof of financial responsibility in the form of a letter of credit, a guarantee or indemnity bond or in any other form satisfactory to the National Energy Board [“Board”], in an amount satisfactory to the Board.”⁷⁸ Currently, there is no upper limit on the amount of financial responsibility which the Board may require.⁷⁹ Proof of financial responsibility must remain in force throughout the operational lifespan of the offshore project.⁸⁰ Any claims arising from section 26 of *COGOA* may be paid, up to an amount determined by the Board, out of the funds made available pursuant to the financial responsibility requirements,⁸¹ and an equivalent amount must be deducted from any subsequent awards made to the claimant pursuant to section 26.⁸² The Board has determined that, in the context of the Arctic offshore, it must “have unfettered access to a portion of the funds provided as proof of financial responsibility” in order to ensure that victims receive prompt compensation and avoid delays associated with litigation.⁸³

2.3.2 *SPILLS ARE PROHIBITED UNDER COGOA*

The foundation of *COGOA*'s liability regime is the prohibition against causing or permitting a spill.⁸⁴ A spill is defined as:

a discharge, emission or escape of petroleum, other than one that is authorized under the regulations or any other federal law or that constitutes a discharge from a vessel

⁷⁸ *COGOA*, *supra* note 43, s 27(1). Similar provisions are found in the *Accord Acts*, although the Canada-Nova Scotia Offshore Petroleum Board and the Canada-Newfoundland and Labrador Offshore Petroleum Board that oversee financial responsibility of operators under those acts (*NS Accord Act*, *supra* note 43, s 168(1); *NL Accord Act*, *supra* note 43, s 163(1)).

⁷⁹ *NEB Liability Backgrounder*, *supra* note 28 at 1.

⁸⁰ *COGOA*, *supra* note 43, s 27(1.1); *NS Accord Act*, *supra* note 43, s 168(1.1); *NL Accord Act*, *supra* note 43, s 163(1.1).

⁸¹ *COGOA*, *supra* note 43, s 27(2); *NS Accord Act*, *supra* note 43, s 168(2); *NL Accord Act*, *supra* note 43, s 163(2).

⁸² *COGOA*, *supra* note 43, s 27(4); *NS Accord Act*, *supra* note 43, s 168(4); *NL Accord Act*, *supra* note 43, s 163(4).

⁸³ *Arctic Offshore Drilling Review*, *supra* note 28 at 48.

⁸⁴ *COGOA*, *supra* note 43, s 25(1); *NS Accord Act*, *supra* note 43, s 166(1); *NL Accord Act*, *supra* note 43, s 161(1).

to which Part 8 or 9 of the Canada Shipping Act, 2001 applies or a ship to which Part 6 of the Marine Liability Act applies.⁸⁵

2.3.3 *THE FEDERAL GOVERNMENT AND, IN LIMITED CIRCUMSTANCES, THE OPERATOR ARE SUBJECT TO UNLIMITED STRICT LIABILITY FOR THE REASONABLE COSTS OF SPILL RESPONSE MEASURES*

If a spill occurs, all persons engaging in hydrocarbon resource development activities in the area of the spill are required to “take all reasonable measures consistent with safety and the protection of the environment” to contain, clean up and mitigate the damage caused by, or reasonably expected to be caused by, the spill.⁸⁶ Such measures may include operating response vessels and undertaking response measures such as in-situ burning, deployment of containment booms, and use of dispersants.⁸⁷ The federal government or a third party⁸⁸ may be ordered to undertake spill response measures, which may include the assumption of management and control of response efforts,⁸⁹ where the Chief Conservation Officer, appointed by the National Energy Board under *COGOA*, determines that the necessary measures have not been and will not be undertaken by the operator.⁹⁰

If the Chief Conservation Officer orders a third party to undertake spill response actions without designating the third party as a spill response manager, the third party is entitled to

⁸⁵ *COGOA*, *supra* note 43, s 24(1); *NS Accord Act*, *supra* note 43, s 165(1); *NL Accord Act*, *supra* note 43, s 160(1). Part 8 of the *Canada Shipping Act, 2001* “[does] not apply in respect of a vessel that is on location and engaged in the exploration or drilling for, or the production, conservation or processing of, oil or gas in an area described in paragraph 3(a) or (b) of the *Canada Oil and Gas Operations Act*” and Part 9 is similarly excluded from application (*Canada Shipping Act*, SC 2001, c 26, ss 166(2), 186(2)). Sections 3(a) and (b) of *COGOA* refer respectively to “the Northwest Territories, Nunavut and Sable Island” and “submarine areas, not within a province, in the internal waters of Canada, the territorial sea of Canada or the continental shelf of Canada” (*COGOA*, *supra* note 43, ss 3(a)-(b)).

⁸⁶ *COGOA*, *supra* note 43, s 25(3); *NS Accord Act*, *supra* note 43, s 166(3); *NL Accord Act*, *supra* note 43, s 161(3).

⁸⁷ *Pew Report*, *supra* note 8 at 73; *Arctic Offshore Drilling Review*, *supra* note 28 at 49.

⁸⁸ In the Gulf of St. Lawrence, the operator would likely contract the services of the Eastern Canada Response Corporation (ECRC), a certified third party spill response organization, prior to obtaining the necessary *Accord Act* authorizations (ECRC, *ECRC Profile*, online: ECRC <<http://www.ecrc.ca/en/home/default.asp>>). Currently, there is no such response organization operating in the Canadian Arctic (Transport Canada, *Response Organizations*, online: Transport Canada <<http://www.tc.gc.ca>>). Although the Mackenzie Delta Spill Response Corporation provides oil spill response services in the Mackenzie River Delta, it currently lacks the capability to conduct offshore spill response activities in the Beaufort Sea (MDSRC, *MDSRC Corporate Profile*, online: MDSRC <<http://deltaspillresponse.ca>>; SL Ross Environmental Research Ltd, DF Dickins Associates LLP & Envision Planning Solutions Inc, *Beaufort Sea Oil Spills State of Knowledge Review and Identification of Key Issues: Environmental Studies Research Funds Report No 177* (Calgary: Environmental Studies Research Funds, 2010) at 73).

⁸⁹ “For the purposes of [taking spill response action or directing a third party to do so], the Chief Conservation Officer *may* authorize and direct such persons as may be necessary to enter the place where the spill has occurred and take over the management and control of any work or activity thereat” [emphasis added] (*COGOA*, *supra* note 43, s 25(5)). See also *NS Accord Act*, *supra* note 43, s 166(5); *NL Accord Act*, *supra* note 43, s 161(5).

⁹⁰ *COGOA*, *supra* note 43, ss 25(4)-(6); *NS Accord Act*, *supra* note 43, ss 166(4)-(6); *NL Accord Act*, *supra* note 43, ss 161(4)-(6).

recover the reasonable costs of spill response measures directly from the federal government.⁹¹ The government must seek to recover these costs from the operator pursuant to the limited absolute liability regime discussed below.

If the Chief Conservation Officer directs outside management of the spill, “the person who obtained an authorization [pursuant to *COGOA*] in respect of the work or activity from which the spill emanated” is clearly and unequivocally liable for “any costs”⁹² of “all reasonable measures in relation to the spill.”⁹³ In other words, unlimited strict liability is imposed on the ‘operator,’ which means the oil company ultimately responsible for the offshore drilling operation. Significantly, only the federal government or the relevant federal-provincial board is entitled to recover such costs from the operator.⁹⁴ The government remains strictly liable to the third party manager for the reasonable costs of spill response measures undertaken by the latter.⁹⁵

2.3.4 *OPERATORS ARE SUBJECT TO LIMITED ABSOLUTE LIABILITY FOR ALL ACTUAL LOSS OR DAMAGE RESULTING FROM A SPILL AND FOR ALL REASONABLE GOVERNMENT AND THIRD-PARTY VOLUNTARY SPILL RESPONSE COSTS*

In the event of any spill, the operator alone is subject to limited absolute liability for:

- i. all actual loss or damage incurred by any person as a result of the spill or the authorized discharge, emission or escape of oil or gas, and
- ii. the costs and expenses reasonably incurred by Her Majesty in right of Canada or any other person in taking any action or measure in relation to the spill or the authorized discharge, emission or escape of oil or gas ...⁹⁶

The phrase “as a result of the spill” is not defined in *COGOA*, nor has subsection 26(1) received judicial consideration in Canada. However, the Saskatchewan Court of Appeal has held that the availability of compensation, where limited by similar statutory language, “clearly requires a

⁹¹ *COGOA*, *supra* note 43, s 25(7.1). In both the Nova Scotia and Newfoundland offshore, the federal government remains liable; the provincial governments do not assume this liability (*NS Accord Act*, *supra* note 43, s 166(7.1); *NL Accord Act*, *supra* note 43, s 161(7.1)).

⁹² *COGOA*, *supra* note 43, ss 25(5-7); *NS Accord Act*, *supra* note 43, ss 166(5-7), *NL Accord Act*, *supra* note 43, ss 161(5-7).

⁹³ *COGOA*, *supra* note 43, s 25(6); *NS Accord Act*, *supra* note 43, s 166(6); *NL Accord Act*, *supra* note 43, s 161(6). Liability for these costs is to be “borne by the person who obtained an authorization...in respect of the work or activity from which the spill emanated” (*ibid*).

⁹⁴ *COGOA*, *supra* note 43, s 25(7); *NS Accord Act*, *supra* note 43, s 166(7), *NL Accord Act*, *supra* note 43, s 161(7).

⁹⁵ *COGOA*, *supra* note 43, s 25(7.1). *NS Accord Act*, *supra* note 43, s 166(7.1); *NL Accord Act*, *supra* note 43, s 161(7.1).

⁹⁶ *COGOA*, *supra* note 43, s 26(1)(a); *C.f.* *NS Accord Act*, *supra* note 43, s 167(1)(a), *C.f.* *NL Accord Act*, *supra* note 43, s 162(1)(a).

causal link⁹⁷ between an accident and an injury. This suggests that, in the context of *COGOA*, a causal link must be established between the spill and the claimant's damages before compensation can be paid.

Notably, *COGOA* does not attempt to apportion absolute liability between the various parties that may be involved in the day-to-day operations of an offshore oil facility. Although the operator may lease the offshore facility from a third party, and may engage contractors and sub-contractors, the simple approach to liability allocation represents a strength of the current liability regime. Any statutory regime that attempted to apportion liability among such diverse parties would be extremely complex, unwieldy and administratively inefficient. The law of contracts provides a much more suitable mechanism for appropriate allocation of risk and apportionment of liability among sophisticated private parties. Furthermore, it is the operator who is required to demonstrate its financial responsibility and who receives the necessary authorizations to engage in offshore operations. Therefore, any reform of the liability regime should not disturb the current allocation of full liability to the operator.

Three important distinctions must be drawn between the liability rules set out in sections 25 and 26. First, like section 25, section 26 of *COGOA* sets out liability rules pursuant to which governments and third parties may obtain compensation for the reasonable costs and expenses of spill response measures. However, the two provisions impose liability for such costs on different parties. Where section 25 applies, the federal government is liable to compensate a third party for spill response costs. The government may then seek to recover these costs from the operator under section 26 or, where appropriate, under subsection 25(7). Where section 26 applies, the government is not liable to a third party. Instead, the operator is liable for the reasonable spill response costs incurred by a third party.

Second, while section 25 imposes unlimited strict liability on the federal government and, to a limited extent, an operator for certain reasonably incurred spill response costs, it does not impose liability for environmental or economic damages or losses incurred by government or private third parties. Operator liability for actual loss or damage that occurs "as a result of" a spill is instead governed by section 26.⁹⁸

Third, and perhaps most crucially, liability under section 25 is strict and unlimited, while liability under section 26 is absolute and limited. The Supreme Court of Canada confirmed the existence of three categories of liability for regulatory offences in *R. v. Sault Ste Marie*: criminal, strict, and absolute.⁹⁹ Criminal liability can only be established if the prosecutor proves that the accused committed an offence with *mens rea* (i.e., intentionally or recklessly). In cases where

⁹⁷ *Saskatchewan Government Insurance v Pipchuk*, 2008 SKCA 82 at para 37, 311 Sask R 81. The Court of Appeal was called upon to interpret s 113(2) of the provincial *Automobile Accident Insurance Act*, RSS 1978, c A-35, which provides that insurance benefits are available where a claimant is unable to work "as a result of an accident." The court noted that this language "clearly requires a causal link between a motor vehicle accident and an injury before benefits can be paid" (*ibid* at para 37). Furthermore, the court noted that the requisite causal link was lacking in that case because "there was no cause-in-fact relationship between the accident and the back injury" (*ibid* at para 39).

⁹⁸ "Actual loss or damage" includes loss of income, including future income, and, with respect to any aboriginal peoples of Canada, includes loss of hunting, fishing and gathering opportunities" (*COGOA*, *supra* note 43, s 24(3); *NS Accord Act*, *supra* note 43, s 165(3); *NL Accord Act*, *supra* note 43, s 160(3)).

⁹⁹ *R v Sault Ste Marie (City)*, [1978] 2 SCR 1299, 85 DLR (3d) 161 [*Sault Ste Marie*].

liability is strict or absolute, intent need not be proven. Liability will arise if it is proven that the defendant committed the prohibited act, whether intentionally or not. However, strict liability regimes offer a defence of due diligence to defendants, enabling non-negligent defendants to escape liability. By comparison, absolute liability regimes impose liability when the defendant is shown to have committed the prohibited act. No defence of due diligence applies under an absolute liability regime, and even non-negligent defendants will be held liable.¹⁰⁰ Absolute liability regimes are appropriate “where, as with oil spills, precautions can best be taken by one of the parties (and where large numbers of third-party victims make bargains between the parties difficult or impossible).”¹⁰¹ The court in *Sault Ste Marie* discussed these standards of liability in the context of regulatory offences, which differ in purpose from rules of civil liability. Although regulatory offences and rules of civil liability must be distinguished, the court’s discussion remains pertinent in the context of civil liability, as the basic elements of strict and absolute liability regimes (e.g., standard of proof, availability of due diligence defence) are identical in both contexts.

The Supreme Court has held that liability imposed by regulatory (as opposed to criminal) legislation is presumed to be strict and that the legislature can impose absolute liability only by “[making] it clear that guilt would follow proof merely of the proscribed act.”¹⁰² Primary factors to consider when assessing whether liability is strict or absolute include “[t]he overall regulatory pattern adopted by the Legislature, the subject matter of the legislation, the importance of the penalty, and the precision of the language used.”¹⁰³ In *COGOA*, Parliament has made clear its intent to impose absolute liability under section 26 through its use of the words “without proof of fault or negligence”.¹⁰⁴

2.3.5 *THE MAXIMUM AMOUNT FOR WHICH AN OPERATOR CAN BE ABSOLUTELY LIABLE IS LIMITED BY STATUTE*

In the Arctic offshore, the absolute liability of the operator is limited to a maximum of \$40 million,¹⁰⁵ while the absolute liability of an operator in the Atlantic (including the Gulf of St. Lawrence) offshore is limited to a maximum of \$30 million.¹⁰⁶

2.3.6 *OPERATORS ARE SUBJECT TO UNLIMITED FAULT-BASED (STRICT) LIABILITY FOR ALL ACTUAL LOSS OR DAMAGE*

Where the fault or negligence of the operator, or any other person, has contributed to a spill, an unlimited (strict) liability regime applies and the polluters are:

¹⁰⁰ *Ibid* at 1325-26.

¹⁰¹ Richardson, *supra* note 47 at 2.

¹⁰² *Sault Ste Marie*, *supra* note 100 at 1326.

¹⁰³ *Ibid*.

¹⁰⁴ *COGOA*, *supra* note 43, s 26; *NS Accord Act*, *supra* note 43, s 167; *NL Accord Act*, *supra* note 43, s 162.

¹⁰⁵ Section 26 of *COGOA* authorizes a prescribed liability limit, which is capped at \$40 million (*Liability Regulations*, *supra* note 52, s 3). Note that this limit is subject to the limit imposed under the *Arctic Waters Pollution Prevention Act*, which will be discussed further below.

¹⁰⁶ In Nova Scotia, the maximum absolute liability limit is capped at \$30 million (*NS Liability Regulations*, *supra* note 52, s 2). In Newfoundland and Labrador, the maximum absolute liability limit is capped at \$40 million in Arctic waters and \$30 million elsewhere (*NL Liability Regulations*, *supra* note 52, s 3).

jointly and severally liable, to the extent determined according to the degree of the fault or negligence proved against them, for all actual loss or damage incurred by any person as a result of the spill or the authorized discharge, emission or escape of oil or gas.¹⁰⁷

Pursuant to this regime, neither the operator nor any other person who has contributed to a spill is liable for costs and expenses related to government or third party spill response measures.

2.3.7 COGOA PROHIBITS DOUBLE RECOVERY

Recognizing the potential application of other liability regimes, *COGOA* makes it clear that double liability cannot be imposed on an operator. Subsection 26(2.1) states that there is to be “no double liability”:

Where subsection (1) or (2) applies, no person is liable for more than the greater of the prescribed limit referred to in paragraph (1)(a) or (2)(a), as the case may be, and the amount for which the person would be liable under any other law for the same occurrence.¹⁰⁸

This provision is intended to prevent recovery under both *COGOA* and another liability regime, such as those in the *Arctic Waters Pollution Prevention Act*, the *IFA* or the *Fisheries Act*.

2.4 ARCTIC WATERS POLLUTION PREVENTION ACT

The *Arctic Waters Pollution Prevention Act* (“*AWPPA*”) was enacted in 1970 amid concerns regarding Canada’s Arctic sovereignty following the transit of the American oil tanker *Manhattan* through the Northwest Passage.¹⁰⁹ The purpose of the *AWPPA* is to regulate pollution caused by the exploitation and transportation of natural resources in Canada’s Arctic. In furtherance of this purpose, the *AWPPA* establishes a civil liability regime that governs the exploration for and exploitation of offshore hydrocarbon resources in the Canadian Arctic.

The *AWPPA* applies to the “arctic waters” of Canada.¹¹⁰ It defines “arctic waters” as:

[T]he internal waters of Canada and the waters of the territorial sea of Canada and the exclusive economic zone of Canada, within the area enclosed by the 60th parallel of north latitude, the 141st meridian of west longitude and the outer limit of the exclusive economic zone; however, where the international boundary between Canada and Greenland is less than 200 nautical miles from the baselines of the territorial sea of Canada, the international boundary shall be substituted for that outer limit.¹¹¹

¹⁰⁷ *COGOA*, *supra* note 43, s 26(1)(b); *C.f. NS Accord Act*, *supra* note 43, s 167(1)(b); *C.f. NL Accord Act*, *supra* note 43, s 162(1)(b).

¹⁰⁸ *COGOA*, *supra* note 43, s 26(2.1). See *NS Accord Act*, *supra* note 43, s 167(2.1); *NL Accord Act*, *supra* note 43, s 162(2.1).

¹⁰⁹ Arctic Council, *Arctic Marine Shipping Assessment 2009 Report* (April 2009) at 39, online: Protection of the Marine Environment <http://www.pame.is/images/stories/AMSA_2009_Report/AMSA_2009_Report_2nd_print.pdf>.

¹¹⁰ *AWPPA*, *supra* note 43, s 3.

¹¹¹ *Ibid*, s 2.

In most of the Arctic offshore, the liability provisions of the *AWPPA* operate in conjunction with, and may in some circumstances supersede those of *COGOA*.¹¹²

Under the *AWPPA*, limited absolute liability¹¹³ is imposed on “any person who is engaged in exploring for, developing or exploiting any natural resource on any land adjacent to the arctic waters or in any submarine area subjacent to the arctic waters.”¹¹⁴ Operators are absolutely liable, up to a prescribed maximum limit, for all reasonable government spill response costs and expenses and for all actual loss or damage suffered by any other person as a result of a deposit of waste into the arctic waters.¹¹⁵ The prescribed maximum absolute liability limit under the *AWPPA* is \$40 million for offshore oil operations.¹¹⁶

Absolute liability under the *AWPPA* is further limited by a narrow exception: liability may be avoided or reduced, with respect to a particular claimant, where a claimant has caused or contributed to the causation of the pollution.¹¹⁷ Although this exception weakens the *AWPPA* liability regime relative to *COGOA*, its application appears to be restricted to an individual claimant where that claimant has contributed to his or her own damages. On a plain reading of the provision, operator liability to other claimants in such circumstances remains absolute and limited only by the statutory cap.

2.5 INUVIALUIT FINAL AGREEMENT – ABSOLUTE LIABILITY FOR WILDLIFE HARVEST LOSS

The *Inuvialuit Final Agreement* (“*IFA*”) is a comprehensive land claim agreement under which the Inuvialuit surrendered certain interests in traditional territory to the federal government.¹¹⁸ In exchange, the Inuvialuit received certain rights, including rights to land within the Inuvialuit Settlement Region and rights related to wildlife harvesting. Notably, the *IFA* establishes a liability regime that provides Inuvialuit with a right to financial compensation for harm caused to wildlife harvesting rights.

Unlike *COGOA*, the *IFA* provides a pre-litigation venue for the contemplation of liability, as it requires (1) an environmental impact assessment of any proposed offshore oil or gas activity “that could have a significant negative impact on present or future wildlife harvesting”¹¹⁹

¹¹² Neither statute is expressly granted precedence over the other in the case of a conflict, but the supremacy of the *AWPPA* in the context of liability for offshore pollution incidents is implied by the language used in the *Arctic Waters Pollution Prevention Regulations*, as will be discussed in greater detail below. The *NL Accord Act* also interacts with the *AWPPA*, because Newfoundland’s offshore includes areas north of 60°N. The *AWPPA* does not interact with the *NS Accord Act*, as Nova Scotia has no offshore areas north of 60°N.

¹¹³ *AWPPA*, *supra* note 43, s 7(1).

¹¹⁴ *Ibid*, s 6(1)(a).

¹¹⁵ *Ibid*, s 6(2). ‘Waste’ is defined to include, *inter alia*, “any substance that, if added to any water, would degrade or alter or form part of a process of degradation or alteration of the quality of that water to an extent that is detrimental to their use by man or by any animal, fish or plant that is useful to man” (*ibid* at s 2). This definition clearly encompasses oil.

¹¹⁶ *Arctic Waters Pollution Prevention Regulations*, CRC, c 354, s 8(f).

¹¹⁷ *AWPPA*, *supra* note 43, s 7(1).

¹¹⁸ *IFA*, *supra* note 34. The *IFA* was approved, given effect and declared valid by the *Western Arctic (Inuvialuit) Claims Settlement Act*, SC 1984, c 24, s 3(1).

¹¹⁹ *IFA*, *supra* note 34, s 13.(8).

and (2) where such an environmental impact assessment is required, the explicit estimation of a developer's total potential liability in the event of worst-case spill.¹²⁰

The innovative liability regime of the *IFA* applies to all developments in the Inuvialuit Settlement Region, including offshore oil operations.¹²¹ The goals of the *IFA* liability regime are:

- a. to prevent damage to wildlife and its habitat and to avoid disruption of Inuvialuit harvesting activities by reason of development; and
- b. if damage occurs, to restore wildlife and its habitat as far as is practicable to its original state and to compensate Inuvialuit hunters, trappers and fishermen for the loss of their subsistence or commercial harvesting opportunities.¹²²

To further these objectives, the *IFA* liability regime imposes unlimited¹²³ absolute liability on the “developer”¹²⁴ of any development for all actual wildlife harvest loss or future harvest loss caused by the development.¹²⁵ Where there is more than one developer, each is jointly and severally liable.¹²⁶ Where the loss was caused by development generally, but is not attributable to any particular developer, joint and several liability is imposed on all “developers whose activities were of such nature and extent that they could reasonably be implicated in the loss.”¹²⁷

Unlike the liability regimes of *COGOA* and the *Accord Acts*, the *IFA* regime explicitly imposes liability for damages to natural resources, including both wildlife and wildlife habitat.¹²⁸ Inuvialuit who earn “a material part of their gross income” from hunting, trapping or fishing are entitled to compensation under the *IFA* regime when actual wildlife harvest loss is caused by development,¹²⁹ as are Inuvialuit who harvest wildlife for subsistence purposes.¹³⁰ Types of compensation contemplated by the *IFA* include the cost of temporary or permanent

¹²⁰ *Ibid*, s 13.(11)(b). Indeed, failure to present a realistic estimation of liability in the event of a worst-case scenario proved fatal to Gulf Canada Resources' proposed offshore drilling program in the early 1990s: see Environmental Impact Review Board, *Public Review of the Gulf Canada Resources Limited Kulluk Drilling Program 1990 – 1992* (Inuvik, Northwest Territories: Environmental Impact Review Board, 1990) at 16, 19 [*Kulluk Report*].

¹²¹ *IFA*, *supra* note 34, s 13.(15).

¹²² *Ibid*, s 13.(1).

¹²³ Subject to the definitions in the *IFA*.

¹²⁴ Section 2 of the *IFA* defines a developer as “a person, the government or any other legal entity owning, operating or causing to be operated any development in whole or in part in the Inuvialuit Settlement Region, and includes any co-contractant of such owner or operator. For greater certainty, “developer” includes any Inuvialuit developer” (*IFA*, *supra* note 34, s 2).

¹²⁵ *IFA*, *supra* note 34, s 13.(15)(a).

¹²⁶ *Ibid*, s 13.(15)(b). *IFA*, s 13.(2) defines ‘actual wildlife harvest loss’ as “provable loss or diminution of wildlife harvesting or damage to property used in harvesting wildlife, or both” while ‘future harvest loss’ “means provable damage to habitat or disruption of harvestable wildlife having a foreseeable negative impact on future wildlife harvesting.”

¹²⁷ *Ibid*, s 13.(15)(c).

¹²⁸ *Ibid*, s 13.(15).

¹²⁹ *Ibid*, s 13.(18)(a).

¹³⁰ *Ibid*, s 13.(18)(b).

relocation, replacement of equipment, reimbursement in kind subject to harvestable quotas, and payments in lump sum or instalments.¹³¹ Furthermore, any definable Inuvialuit group or community affected by future harvest loss is entitled to seek recommendations from the Arbitration Board¹³² “with respect to remedial measures, to the extent reasonably practicable, including clean-up, habitat restoration and reclamation.”¹³³

Thus, the *IFA* provides clarity regarding natural resource (use) damages for which compensation will be provided in the event of an offshore spill. While the *IFA* does not prescribe processes for assessing natural resource damages, it clearly defines the available recourses and establishes procedures for recovering compensation,¹³⁴ reducing uncertainty as to liability. Furthermore, where a polluter, such as the operator of an offshore oil facility, cannot discharge its liability obligations under the *IFA*, the federal government assumes that liability.¹³⁵

2.6 *FISHERIES ACT*—ABSOLUTE LIABILITY FOR UNAUTHORIZED DISCHARGE OF A DELETERIOUS SUBSTANCE IN WATER FREQUENTED BY FISH

First enacted in 1868, the *Fisheries Act* governs the management and use of Canada’s fishery resources. To promote the long-term viability of Canada’s fisheries, the *Act* prohibits the destruction of fish habitat¹³⁶ and the pollution of fish-bearing waters.¹³⁷ The *Act* also establishes a civil liability regime that aims to protect fish-bearing waters and may, in limited circumstances, be engaged in the event of an offshore oil pollution incident.¹³⁸

Civil liability for an offshore oil pollution incident may arise under the *Fisheries Act* if oil is discharged into fish-inhabited waters. Where, without authorization,¹³⁹ a “deleterious substance [is deposited] in water frequented by fish,” the *Fisheries Act* imposes joint and several liability on any party that “own[s] the deleterious substance or [has] the charge, management or control thereof [...]”¹⁴⁰ Although such liability is absolute, it will not arise if the pollution results from an act of war, natural disaster, or malicious third party conduct.¹⁴¹ In addition to this absolute liability regime, the *Fisheries Act* imposes joint and several liability on every person found to have caused or contributed to the causation of pollution through fault or negligence.¹⁴²

¹³¹ *Ibid*, ss 13.(18)(a)-(b).

¹³² The Arbitration Board is established under s 18.(2) of the *IFA* and given jurisdiction to make recommendations under s 18.(35)(h) (*ibid*).

¹³³ *Ibid*, s 13.(18)(c).

¹³⁴ *Ibid*, ss 13.(18)-(24).

¹³⁵ Unless the federal government was not involved in establishing the terms and conditions for development (*IFA*, *supra* note 34, s 13.(16)).

¹³⁶ *Fisheries Act*, *supra* note 43, s 35.

¹³⁷ *Ibid*, s 36.

¹³⁸ *Ibid*, s 42.

¹³⁹ Authorization may be obtained pursuant to section 36 of the *Fisheries Act* (*ibid*).

¹⁴⁰ *Ibid*, s 42(1).

¹⁴¹ *Ibid*, s 42(4).

¹⁴² *Ibid*, s 42(1)(b).

Liability pursuant to the *Fisheries Act* regime encompasses the full costs, reasonably incurred, of government remediation and mitigation measures, as well as all loss of income incurred by licensed commercial fishermen, to the extent that such loss was caused by the deposit.¹⁴³

The most significant strength of the *Fisheries Act* liability regime is its lack of maximum statutory absolute liability limits. As a result, the compensation available for an offshore oil pollution incident under the *Fisheries Act* may exceed that available under *COGOA* or the *Accord Acts*.

3. CRITIQUE OF THE CURRENT OFFSHORE LIABILITY REGIME

3.1 THE LIABILITY REGIMES ESTABLISHED BY *COGOA* AND THE *ACCORD ACTS* SUFFER FROM A NUMBER OF WEAKNESSES THAT ARE NOT ADEQUATELY ADDRESSED BY AUXILIARY LIABILITY REGIMES

The offshore liability regimes established by *COGOA* and the *Accord Acts* suffer from a number of weaknesses that expose taxpayers to an unjustifiable degree of financial risk and decrease accident prevention incentives for industry. These weaknesses will be discussed in this section and include, in descending order of importance:

- inappropriately low maximum absolute liability limits;
- the uncertain availability of environmental damages under liability statutes;
- an absence of express recognition of the polluter-pays principle;
- a lack of complementary mechanisms to ensure remediation and compensation even where the operator is unwilling or unable to fund these efforts;
- a lack of clarity as to what will constitute “reasonable” spill response measures and costs and when an operator will be liable for such costs;
- an apparent restriction on the imposition of joint and several liability;
- a lack of clarity with respect to the interaction between the *COGOA* and *AWPPA* liability regimes; and
- an apparent drafting error that may affect the non-availability of double liability.

The complementary liability regimes set out in the *AWPPA*, the *IFA* and the *Fisheries Act* are, for various reasons, incapable of filling the gaps in the liability regimes of *COGOA* and the *Accord Acts*. A comprehensive suite of legislative reforms to *COGOA* and the *Accord Acts* can, however, address those gaps and strengthen the offshore liability regime.

3.1.1 WEAKNESSES OF THE ARCTIC WATERS POLLUTION PREVENTION ACT

In some cases, as will be discussed below, the liability regime established by the *AWPPA* may supersede *COGOA* and Newfoundland’s *Accord Act* in the Canadian Arctic. Due to limita-

¹⁴³ *Ibid*, ss 42(1), (3).

tions of its own, however, the *AWPPA* regime does not adequately address the weaknesses of *COGOA* and the *Accord Act*.

The *AWPPA* liability regime is subject to certain limitations that are not present in the liability regimes established by *COGOA* and the Newfoundland *Accord Act*. In addition to providing the aforementioned exception pursuant to which operators may avoid absolute liability, the *AWPPA* also imposes more restrictive time requirements on victims seeking to recover compensation. The limitation period for bringing a claim under the *AWPPA* is two years from the date on which the deposit of waste “occurred ...or could reasonably be expected to have become known to those affected thereby.”¹⁴⁴ No absolute limitation period is prescribed under the *AWPPA*. By comparison, the limitation period for bringing a claim under *COGOA* or the *Accord Act* is three years from the date of occurrence of loss or damage with an absolute limitation period of six years from the pollution incident.¹⁴⁵ The risk posed by these limitation periods to potential claimants is exacerbated by uncertainty surrounding the interaction between the *AWPPA* and *COGOA/Accord Act* regimes, as will be discussed below.

3.1.2 WEAKNESSES OF THE INUVIALUIT FINAL AGREEMENT

The innovative natural resource damages regime established under the *IFA* would increase the chances of a negotiated settlement in the event of a catastrophic blowout in the Beaufort Sea, and can serve as a useful model for correcting certain weaknesses of *COGOA* and the *Accord Acts*, as will be discussed below. Nevertheless, the limitations of the *IFA* liability regime render it incapable of filling the gaps left by *COGOA*.

Beyond harvest loss, the *IFA* does not specify how damages to ecological systems that long-term harvesting depends on will be compensated. The Inuvialuit, like other Canadians, must rely on *British Columbia v. Canadian Forest Products Ltd.*¹⁴⁶ and the common law to seek compensation for damages to ecological systems in the event of an offshore oil spill. The *IFA* also does not create a right to compensation for damages to every natural resource. Only resources directly related to wildlife harvesting give rise to a right to compensation.

This weakness is compounded by the *IFA* liability regime’s limited scope: the *IFA* applies only within the Inuvialuit Settlement Region, and only Inuvialuit are entitled to compensation pursuant to its liability provisions.

Furthermore, while the *IFA* provisions are quite detailed, the standard for required mitigation and remediation remains unclear. Anderson and Nesbitt note:

Mitigative and remedial measures require restoration of wildlife and habitat to its ‘original state as far as practicable.’ This includes cleanup, habitat restoration and reclamation. The ‘original state’ of the wildlife populations and habitat is not defined.¹⁴⁷

¹⁴⁴ *AWPPA*, *supra* note 43, s 6(5).

¹⁴⁵ *COGOA*, *supra* note 43, s 26(5); *NL Accord Act*, *supra* note 43, s 162(5).

¹⁴⁶ *Canfor*, *supra* note 22.

¹⁴⁷ James Anderson & Brian Nesbitt, “Financial Liability Requirements for Oil and Gas Activities in Canadian Frontier Areas” (Paper delivered at the International Oil Spill Conference, 10 March 1999), (1999) 1999:1 International Oil Spill Conference Proceedings 651 at 653. The issue of restoration to an “original state” speaks directly to the broader issue of establishing knowledge of baseline ecological conditions prior to authorizing drilling in the Beaufort Sea.

Finally, the federal government has, in the past, taken the position that “developer’s liability can be limited [by the federal government] under the IFA, and that Canada’s “backstop” liability [pursuant to s. 13.(16)] can be similarly limited.”¹⁴⁸ The Inuvialuit disagree with this interpretation,¹⁴⁹ and it is unclear whether the government currently takes this position. If, however, this is the government’s current position, this substantially weakens the *IFA* liability regime.

Regardless of the government’s current position on the interpretation of the “backstop” provision, the federal government’s assumption of a polluter’s compensation obligations demonstrates the need for reform of the federal liability regimes.¹⁵⁰ Although not a weakness of the *IFA* regime per se, this provision, coupled with the current lack of clarity under various federal laws as to the availability of natural resource damages and inadequate statutory maximum absolute liability limits, places the Government of Canada, and by extension taxpayers, at risk of assuming liability for damages which may not be recoverable at common law or pursuant to statute.

3.1.3 WEAKNESSES OF THE FISHERIES ACT

While compensation under the *Fisheries Act* liability regime could exceed that available under *COGOA* and the *Accord Acts*, the *Fisheries Act* regime suffers from a number of weaknesses that prevent it from adequately addressing the concerns identified with *COGOA* and the *Accord Acts*.

Although the liability of an operator under the *Fisheries Act* regime is ostensibly absolute, requiring no proof of fault or negligence, several statutory exceptions limit operator liability. While these exceptions to the absolute liability regime are narrow and do not include a due diligence defence, they nonetheless detract from the absolute nature of *Fisheries Act* liability in a manner that is not duplicated in the absolute liability regimes established by *COGOA* and the *Accord Acts*. The natural disaster exception, in particular, may allow offshore operators to escape liability for spills in the Arctic, where environmental conditions are inherently challenging.

More importantly, the scope of absolute liability is extremely limited under the *Fisheries Act* regime. The government is entitled to recover costs of clean-up and remediation efforts, but liability for damages is limited to compensation for loss of income suffered by licensed commercial fishermen. Liability does not extend to compensation for loss of income suffered by any other persons as a result of the spill, including tourism and outdoor recreation operators (e.g., whale-watching or bird-watching businesses) who stand to suffer economic harm due to an oil spill.

While a narrow scope of liability may be appropriate in the context of the statute, which is intended to regulate fisheries, the current scope of liability is so narrow as to be under-inclu-

¹⁴⁸ Task Group Three (Inuvialuit Regional Corporation), *Volume 4, Report of Task Group Three: Compensation and Financial Responsibility* (for the Beaufort Sea Steering Committee) (April 1991) at 8, online: Arctic Institute of North America <<http://pubs.aina.ucalgary.ca/misc/33781.pdf>>. This position, adopted by the [then] Department of Indian Affairs and Northern Development, is based on “clauses 13.(18)(c), 13(9) and others, read in the context of section 13 as a whole” (*ibid*).

¹⁴⁹ *Ibid*.

¹⁵⁰ *IFA*, *supra* note 34, s 13.(16).

sive, even in the statute's limited context. By restricting the availability of compensation to licensed commercial fishermen, the regime ignores both Aboriginal and recreational fisheries, although both are expressly contemplated in recently enacted (albeit not yet in force) amendments to the *Fisheries Act*.¹⁵¹ People relying on Aboriginal and recreational fisheries for food and/or income are no less economically vulnerable to oil pollution damage than commercial fishermen, and may be forced to turn to government assistance programs if they cannot recover compensation from the party responsible for the pollution.

Accordingly, while the *Fisheries Act* liability regime could alleviate concerns about the inappropriately low maximum absolute liability limits of *COGOA* and the *Accord Acts* in very limited factual circumstances, the overall effectiveness of the *Fisheries Act* regime as a taxpayer protection mechanism is limited. At a minimum, the *Fisheries Act* liability regime must be reformed to include statutory civil liability provisions that implement the polluter-pays principle with respect to oil pollution damage suffered by fishermen dependent on Aboriginal and recreational fisheries.

3.1.4 *A COMPREHENSIVE SET OF LEGISLATIVE REFORMS IS NECESSARY TO ADDRESS THE WEAKNESSES OF CANADA'S OFFSHORE LIABILITY REGIME*

The weaknesses identified and discussed below highlight the failings of Canada's current offshore liability regime, particularly with respect to implementation of the polluter-pays principle. The legislative reforms proposed below are intended to correct the regime's weaknesses and enhance implementation of the polluter-pays principle. In other words, the reforms are intended to ensure that the polluter pays for the full costs and damages associated with an offshore oil spill, while also providing incentives to offshore oil and gas operators to adopt appropriate safety practices, thereby reducing the risk that such a spill will occur.

Some of the proposed reforms aim to transfer the burden of financial liability for a spill to the operator by increasing the maximum amount of funds available for compensation (e.g., increasing or abolishing maximum absolute liability limits and adopting complementary compensation mechanisms). Other reforms aim to transfer the financial risk of a pollution incident to industry by eliminating barriers that increase the difficulty of recovering compensation from a polluter (e.g., clarifying the availability of natural resource damages, codifying a method for assessing and calculating the quantum thereof, and removing the restriction on joint and several liability). This dual approach to reform of the offshore liability regime is critical, as merely imposing more stringent liability obligations on a polluter will have little practical effect if procedural and practical barriers to compensation continue to shield the polluter from liability.

3.2 INAPPROPRIATELY LOW MAXIMUM ABSOLUTE LIABILITY LIMITS

3.2.1 *WEAKNESS: PRESCRIBED MAXIMUM ABSOLUTE LIABILITY LIMITS FAIL TO PROMOTE A DESIRABLE INDUSTRY SAFETY CULTURE AND FAIL TO PROTECT CANADIAN TAXPAYERS FROM POTENTIALLY MASSIVE LIABILITY*

¹⁵¹ See *Jobs, Growth and Long-term Prosperity Act*, SC 2012, c 19, s 133(3), which amends s 2(1) of the *Fisheries Act*, *supra* note 43, to incorporate definitions of Aboriginal and recreational fisheries.

Section 26 of *COGOA* imposes liability on operators, regardless of fault or negligence, for “all actual loss or damage incurred by any person as a result of the spill or authorized discharge, emission or escape” and, with respect to measures taken in response to a spill or authorized spill, for “the costs and expenses reasonably incurred by [the federal government] or any other person.” As discussed above, the liability imposed on operators pursuant to section 26 is absolute, subject to a cap.

Absolute liability is appropriate for the offshore liability regime as it promotes a “high standard of care and attention” on the part of the offshore industry and provides “an incentive to take precautionary measures beyond what would otherwise be taken, in order that mistakes and mishaps be avoided.”¹⁵² In short, absolute liability promotes the development of an industry safety culture.¹⁵³ At the same time, it ensures that compensation for damages caused by spills is accessible to injured parties by reducing the burden of proof on injured parties. Given that evidence necessary to establish fault or negligence is often in the hands of the polluter, this facilitates the recovery of compensation by injured parties and lessens the impetus for polluters to litigate with a view to minimizing compensation outlays.

Absolute liability regimes are controversial because they may impose liability on a “morally innocent” person.¹⁵⁴ It is for this reason that courts are loath to impose such liability on an offender absent clear legislative intent. In the case of *COGOA*, Parliament’s intent to impose absolute liability on operators is clear. However, Parliament also imposed a maximum cap on an operator’s absolute liability under *COGOA*. In principle, a liability cap is a fair and reasonable mechanism for balancing the concerns discussed above. These concerns will be perfectly balanced where the absolute liability cap equals the expected harm of a worst-case spill, less any additional criminal, civil or administrative penalties for which the operator may be liable.¹⁵⁵ In such a situation, the liability cap will protect taxpayers by requiring polluters to internalize the full costs of pollution, while ensuring that liability is not imposed on a morally innocent party to advance a punitive objective.

As discussed above, however, operator absolute liability is currently limited to \$40 million in the Arctic offshore and to \$30 million in the Atlantic (including the Gulf of St. Lawrence) offshore. The Arctic absolute liability cap was last updated in 1980,¹⁵⁶ while the Atlantic caps have not been updated since their respective enactments.¹⁵⁷ The federal government has been aware of the inadequacy of the Arctic absolute liability cap since at least 1990, when a panel of

¹⁵² *Sault Ste Marie*, *supra* note 100 at 1310-11.

¹⁵³ “An important method by which firms are made to internalize the environmental and economic costs associated with a spill – and therefore are given incentives to invest in preventing or reducing damages— is tort liability... The possibility of [civil] legal actions creates an incentive for a responsible party to adopt a stronger safety culture to reduce the probability and severity of a spill” (Mark A Cohen et al, *Deepwater Drilling: Law, Policy, and Economics of Firm Organization and Safety* (Washington, DC: Resources for the Future, 2011) at 27, online: Resources for the Future <<http://www.rff.org>> [Cohen]).

¹⁵⁴ *Sault Ste Marie*, *supra* note 100 at 1310.

¹⁵⁵ Cohen, *supra* note 153 at 27.

¹⁵⁶ SOR/80-413, s 1. This amendment decreased the maximum absolute liability cap under the *AWPPA* for offshore oil operations; prior to 1980, the maximum absolute liability cap for offshore oil operations was, in some areas of the Arctic, \$50 million dollars (SOR/80-75, s 1).

¹⁵⁷ In 1988 for Newfoundland, and in 1995 for Nova Scotia.

the Inuvialuit Environmental Impact Review Board recommended against the approval of an offshore exploration project, largely because of concerns related to liability:

The basis for setting the limit at \$40 million is not only unclear, but it would appear to be contrary to various indicators of which DIAND [Department of Indian Affairs and Northern Development] has undoubtedly been aware. Not only have they routinely been tendered financial insurance instruments (insurance policies) greatly in excess of that limit, [then-regulator] COGLA [Canada Oil and Gas Lands Administration] itself in a study, admittedly now out of date, has estimated offshore cleanup costs vastly in excess of that sum.

It is painfully obvious that DIAND's policies and practices with respect to limits on absolute liability ... require serious over-haul and extensive critical analysis.¹⁵⁸

Nevertheless, in the intervening decades, the prescribed liability limits have not even been updated to account for inflation, let alone to reflect the realities of the post-*Deepwater Horizon* world. By comparison, although the maximum liability cap in the United States is more than double that in Atlantic Canada, the National Commission urged Congress to "significantly increase"¹⁵⁹ the cap, recognizing that:

The amount of potential damage caused by a major spill clearly exceeds the existing caps, and one cannot fairly assume that the responsible party causing a future spill will, like BP, have sufficient resources to fully compensate for that damage. Nor should the spill's victims or federal taxpayers have to pay the bill for industry's shortcomings. Increasing liability limits would also serve as a powerful incentive for companies to pay closer attention to safety, including investing more in technology that promotes safer operations.¹⁶⁰

Staff working for the National Commission confirmed that the US maximum liability cap "provides little incentive for improving safety practices to decrease the likelihood of major spills, and it limits the ability of those who suffer damages to receive full compensation."¹⁶¹

In the Canadian context, where compensation for spill response costs may only be available through the absolute liability regime, an inappropriately low absolute liability cap is of substantial concern where the government, pursuant to section 25 of *COGOA*, assumes unlimited strict liability for most third party spill response costs. Any response to a major offshore blowout will, by necessity, involve thousands of responders (e.g., the *Deepwater Horizon*'s peak response force of 45,000 responders) who will, particularly in the remote and environmentally challenging Arctic, incur significant response costs. While the government may seek to recover any funds paid to qualifying third party responders from the operator pursuant to the limited absolute liability regime, the weaknesses of that regime render the likelihood of obtaining full and fair compensation remote. Not only is the operator's absolute liability limited to a maximum of \$40 million, but claims brought by any persons for actual loss or damage caused

¹⁵⁸ *Kulluk Report*, *supra* note 122 at 52.

¹⁵⁹ *National Commission Report*, *supra* note 1 at 284. Congress did "consider raising ... [the liability] cap significantly (to as much as \$10 billion) or even eliminating it altogether" (*ibid* at 245).

¹⁶⁰ *Ibid* at 245-46.

¹⁶¹ *Staff Working Paper No 10*, *supra* note 25 at 1.

by the blowout have precedence over claims for response costs and expenses.¹⁶² In the event of a major blowout, actual loss or damage caused by the spill will exceed \$40 million, meaning that no recovery of compensation for costs and expenses will be possible under the absolute liability regime. However, the residual unlimited strict liability regime established by paragraph 26(1) (b) of *COGOA* does not render the operator liable for the costs and expenses incurred by the government or third parties. The government will therefore have no mechanism, save the common law, by which to recover the costs and expenses paid to third party responders, exposing taxpayers to substantial financial risk.¹⁶³

Canada's outdated and inappropriately low liability caps are no longer serving Parliament's policy objective of encouraging industry to adopt the most risk-averse, world-class safety practices.¹⁶⁴ Furthermore, they fail to promote innovation in spill response technology and ultimately shift the costs of a major spill onto the Crown, taxpayers, and the environment. The top priority of any liability reform, as will be discussed below, must be to increase the absolute liability caps to accurately reflect the reality of offshore risks.

3.2.2 *WEAKNESS: BEYOND THE INAPPROPRIATELY LOW ABSOLUTE LIABILITY LIMITS, THE UNLIMITED FAULT-BASED (STRICT) LIABILITY DOES NOT ADEQUATELY PROTECT CANADIANS*

Where fault or negligence has resulted in an offshore spill, *COGOA* imposes liability on:

all persons to whose fault or negligence the spill or the authorized discharge, emission or escape of oil or gas is attributable or who are by law responsible for others to whose fault or negligence the spill or the authorized discharge, emission or escape of oil or gas is attributable ...¹⁶⁵

Where the fault or negligence of any of those persons is proven, joint and several liability is imposed "to the extent determined according to the degree of the fault or negligence proved against them, for all actual loss or damage incurred by any person as a result of the spill or the authorized discharge, emission or escape of oil or gas."¹⁶⁶

The problems posed by inadequate absolute liability limits cannot be remedied by reliance on residual strict liability provisions for spills caused by an offshore company's own fault or negligence. Launching a civil action against a major global oil company (and a series of

¹⁶² *COGOA*, *supra* note 43, s 26(3); *NS Accord Act*, *supra* note 43, s 167(3); *NL Accord Act*, *supra* note 43, s 162(3).

¹⁶³ Even if claims for actual loss or damage do not total \$40 million, nothing in *COGOA* grants the government's claim for costs and expenses precedence over the claims for costs and expenses of voluntary third party responders (e.g., the waterfront property owner who undertakes response actions to prevent harm to his or her property without being ordered to do so by the Chief Conservation Officer). The *Accord Acts* explicitly rank claims for costs and expenses "without preference" (*NS Accord Act*, *supra* note 43, s 167(3); *NL Accord Act*, *supra* note 43, s 162(3)).

¹⁶⁴ In the United States, liability caps that are "far below worst-case damages...likely reduce the aggregate expected damages payments from a spill to some degree...with corresponding effects on safety incentives" (Cohen, *supra* note 155 at 31).

¹⁶⁵ *COGOA*, *supra* note 43, s 26(1)(b); *C.f.* *NS Accord Act*, *supra* note 43, s 167(1)(b); *C.f.* *NL Accord Act*, *supra* note 43, s 162(1)(b).

¹⁶⁶ *Ibid.*

contractors and sub-contractors) and proving that company's negligence or fault involves substantial barriers to compensation recovery for injured plaintiffs, whether they are citizens or governments, even in the context of a class action. Costs associated with lawyer fees and expert evidence would quickly mount as judicial processes move slowly. Litigation related to the *Exxon Valdez* spill, which occurred in 1989, was still ongoing in 2012, more than two decades later.¹⁶⁷ Complex multi-district litigation related to the *Deepwater Horizon* blowout, involving more than one hundred thousand individual plaintiffs, has reached trial after nearly three years,¹⁶⁸ and other claims continue to be filed.¹⁶⁹

In the context of a large- or even a medium-scale spill, particularly in the Arctic where remediation efforts are likely to be substantially more costly due to environmental and operational challenges,¹⁷⁰ reliance on strict liability provisions decreases access to justice and compensation for victims of pollution damage, but does not reduce administrative inefficiency. Although many claims against Exxon related to the *Exxon Valdez* spill were ultimately dismissed, the courts were forced to accommodate over 250 separate private civil actions.¹⁷¹

Furthermore, strict liability provisions do less to promote a world-class offshore industry safety culture. Once the absolute liability cap has been surpassed, this approach tends to impose the front-end clean-up and compensation costs of a spill on the Crown. This approach also imposes litigation costs on the Crown if it seeks to recover those costs from the operator through the courts.

3.2.3 SOLUTION: ABOLISHING THE MAXIMUM ABSOLUTE LIABILITY LIMIT

Any reform to the offshore liability regime that fails to address the maximum absolute liability limit cannot be characterized as a success for taxpayers or in terms of environmental protection. As discussed above, in the wake of the *Deepwater Horizon* incident, the National Commission recommended that maximum liability caps for offshore operations, which are set at USD \$75

¹⁶⁷ The US District Court recently rejected Exxon's motion for an order to enforce a consent decree that would allow Exxon to avoid paying approximately USD \$92 million for the costs of habitat restoration related to the *Exxon Valdez* spill (*US v Exxon Corp*, 2012 WL 604388 (D Alaska 2012)).

¹⁶⁸ "BP oil spill trial begins Monday in New Orleans almost three years after one of the worst spills in US history", *Times-Picayune* (22 February 2013), online: Times-Picayune <http://www.nola.com/news/gulf-oil-spill/index.ssf/2013/02/bp_oil_spill_trial_begins_mond.html>.

¹⁶⁹ See e.g. Kevin Spear, "Deadline triggers rush of Gulf oil-spill lawsuits, including some from interior Florida" *Orlando Sentinel* (2 June 2013), online: Orlando Sentinel <http://articles.orlandosentinel.com/2013-06-02/news/os-cfb-cover-bp-litigation-0603-20130602_1_biggest-offshore-spill-gulf-oil-spill-south-florida>.

¹⁷⁰ Arctic Monitoring and Assessment Programme, *Arctic Oil and Gas 2007* (Oslo: Arctic Monitoring and Assessment Programme, 2007) at 33.

¹⁷¹ Robert E Jenkins & Jill Watry Kastner, "Running Aground in a Sea of Complex Litigation: A Case Comment on the Exxon Valdez Litigation" (1999/2000) *UCLA J Envtl L & Pol'y* 151 at 159.

million in the United States,¹⁷² should be “significantly increase[d].”¹⁷³ Meanwhile, Greenland imposes unlimited absolute liability,¹⁷⁴ although liability may be avoided or reduced where:

- pollution damage was caused by an activity that “was performed in accordance with indispensable directions laid down by a public authority, unless the directions follow from enforcement notices or instructions that are due to the responsible party’s own activities or circumstances”;¹⁷⁵ or
- an affected claimant contributed to his or her damages intentionally or by his or her own gross negligence.¹⁷⁶

Similarly, Norway imposes unlimited absolute liability on offshore operators, subject to the following exceptions:

If it is demonstrated that an inevitable event of nature, act of war, exercise of public authority or a similar force majeure event has contributed to a considerable degree to the damage or its extent under circumstances which are beyond the control of the liable party, the liability may be reduced to the extent it is reasonable, with particular consideration to the scope of the activity, the situation of the party that has sustained damage and the opportunity for taking out insurance on both sides.¹⁷⁷

Insurance costs associated with substantial liability limits became a focus in the US liability reform debate, particularly in the context of the many smaller operators engaged in offshore activities in the Gulf of Mexico. The National Commission’s recommendation to increase liability limits generated concern that many of these smaller operators would be forced to cease operations in the face of unsustainable insurance costs, resulting in a loss of jobs, lease revenues, and production levels.¹⁷⁸

In the Canadian context, the argument that the significant new insurance costs resulting from an unlimited absolute liability regime would effectively deter development of Canada’s offshore hydrocarbon resources is overstated. While insurance costs are a relevant factor to consider, Canadian offshore operators tend to be mid-sized or major international oil companies,

¹⁷² *OPA*, *supra* note 68, § 2704(a)(3). This cap is in addition to the costs of containing and removing oil from the environment (*ibid*, § 2704(a)(3), 2701(30), (31)).

¹⁷³ *National Commission Report*, *supra* note 1 at 284.

¹⁷⁴ *Mineral Resources Act*, Greenland Self-Government 2009, Part 14, ss 63-69, online: Bureau of Minerals and Petroleum <<http://www.bmp.gl>>.

¹⁷⁵ *Ibid*, s 69(2).

¹⁷⁶ *Ibid*, ss 69(3)-(4).

¹⁷⁷ Norway, *Petroleum Activities Act*, c 7, ss 7-3, online: Norwegian Petroleum Directorate <<http://www.npd.no>>.

¹⁷⁸ The National Commission recognized the concern presented by both large and small operators that the “result would be detrimental, among other reasons, because the independent producers develop many smaller and end-of-life oil fields that the larger firms find uneconomic” (*National Commission Report*, *supra* note 1 at 246).

not the smaller operators that are ubiquitous in the United States.¹⁷⁹ Thus, as regards vulnerabilities to increased insurance costs, there is no constituency of small, independent Canadian operators to protect.

Furthermore, in fostering an offshore industry, and particularly in the Arctic, Canada should actively seek to exclude small, less-capitalized operators (except where they partner with large operators that assume full liability) because the risks they present to Canadian taxpayers substantially outweigh any benefits received. Unlimited absolute liability regimes are no bar to experienced global oil companies. BP, ConocoPhillips, and ExxonMobil all operate under an unlimited absolute liability regime in the Norwegian offshore. A senior Imperial Oil official has attested to his company's willingness to operate under the unlimited absolute liability regime of the *IFA*, stating: "if we can afford to drill in this environment, then we should have the financial strength to fund any cleanup".¹⁸⁰

Unlimited absolute liability would not prevent major oil companies from developing Canada's offshore hydrocarbon resources. Although substantial insurance costs would likely be incurred, those costs are more appropriately borne by the operator than by the Canadian taxpayer, and any oil company large enough to meet stringent financial responsibility standards will be able to absorb these costs in any event.¹⁸¹

Finally, the dollar amount required by the regulator to prove financial responsibility need not equal the absolute liability cap, so increasing the limit would not necessitate an equivalent increase in financial responsibility requirements. While financial responsibility requirements should be increased to adequately reflect any change in liability limits, and ensure that operators could satisfy maximum absolute liability obligations in the event of a spill, the require-

¹⁷⁹ Immediately after the *Deepwater Horizon* disaster, the five largest independent operators in the Gulf of Mexico had an average market capitalization of \$23 billion. However, in the Gulf of Mexico, independent operators were the largest shareholders in 66 percent of all offshore leases and in 81 percent of producing offshore leases. In total, these operators accounted for 900,000 barrels per day of oil equivalent from the deepwater region alone (IHS Global Insight, *The Economic Impact of the Gulf of Mexico Offshore Oil and Natural Gas Industry and the Role of Independents* (Washington, DC: IHS Global Insight, 2010) at 4, 6, online: Fulbright <<http://www.fulbright.com>>). By contrast, offshore operators in Canada's Atlantic region are almost exclusively supermajor multinational corporations, including ExxonMobil, Chevron and ConocoPhillips, often working in consortiums. Large independents with global operations, including Husky Energy (market capitalization \$29.8 billion in May 8, 2013) and Suncor Energy (market capitalization \$48.6 billion in May 8, 2013), also conduct offshore operations in the Canadian Atlantic offshore, often in consortiums with the supermajors (Stock Market Quotes, *Husky Energy Inc* (16 April 2013), online: Toronto Stock Exchange <<http://web.tmxmoney.com>>; Stock Market Quotes, *Suncor Energy Inc* (16 April 2013), online: Toronto Stock Exchange <<http://web.tmxmoney.com>>; *CNLOPB Annual Report 2011-12*, *supra* note 77). No offshore rigs are currently operating in the Canadian Arctic (National Energy Board, *Weekly Status of Oil and Gas Activities on Frontier Lands* (4 June 2013), online: NEB, <http://www.neb-one.gc.ca/clf-nsi/rnrgynfmitn/ststsc/wklyststslgsfrntr/2013/wklyststslgsfrntr2013_06_04.pdf>).

¹⁸⁰ *Arctic Offshore Drilling Review*, *supra* note 28 at 48, citing Mike Peacock, Exploration Manager, Imperial Oil Limited.

¹⁸¹ Note that pooled insurance policy options adopted in the United Kingdom represent a potential mechanism to address higher insurance costs. However, such options fail to achieve the desired behaviour modification goals and must be designed with this weakness in mind.

ments need only be increased to a level that will eliminate financially unqualified operators from seeking drilling authorizations.

i. *Alternative Solution: Significantly Increasing the Maximum Absolute Liability Limit and Creating an Exception to the Cap Where Operators Contravene Federal Laws*

An unlimited absolute liability regime provides Canadians with the most substantial protection against the environmental liabilities of an offshore oil spill, and is therefore preferable to an absolute liability regime that caps maximum absolute liability.

However, if the maximum absolute liability cap in the Canadian offshore liability regime is not abolished, it must be significantly increased. Furthermore, the cap should not apply where an operator has violated a federal statute or regulation directly related to an offshore development activity.

The starting point for any discussion about reforming the current liability regime is *Bill C-15*, which proposed to raise the absolute liability cap for damages resulting from a nuclear incident from \$75 million to \$650 million.¹⁸² Although the consequences of a nuclear incident are different in nature than those of a worst-case spill, this figure remains relevant because the risk of a spill incident is higher than that of a nuclear incident. Technological limitations, particularly in the Arctic offshore, the potential of an uncontained blowout occurring under the winter ice, and the multiple offshore oil projects anticipated each serve to increase the risk of occurrence of a worst-case spill scenario.

While \$650 million is an order of magnitude larger than existing Canadian and US liability limits, the inadequacy of the current US limit was laid bare in the wake of the *Deepwater Horizon* incident.¹⁸³ In fact, even a \$650 million limit is grossly inadequate given how many billions of dollars BP will eventually pay to fulfil its civil liability obligations.¹⁸⁴ One cannot help but wonder if a higher absolute liability cap – or no cap at all – would have modified behaviour and averted the disaster.

Calculation of the quantum of the absolute liability limit should be based on the worst-case blowout scenarios for distinct regions. These may vary with the different anticipated social, economic and environmental damages in each drilling location. For example, a spill

¹⁸² Canada, Bill C-15, *An Act respecting civil liability and compensation for damage in case of a nuclear incident*, 3rd Sess., 40th Parl., 2010, cl. 21(1) (First Reading completed 16 April 2010) [*Bill C-15*]. This bill, along with a number of similar bills, have enjoyed House of Commons support only to die on the order paper on various occasions: see Library of Parliament, *Legislative Summary of Bill C-15: An Act respecting civil liability and compensation for damage in case of a nuclear incident* (Ottawa: Library of Parliament, 2010) at 2. The Government of Canada has recently announced its intention to table new legislation in fall of 2013 that would raise the absolute liability limit for a nuclear incident to CAD \$1 billion and would also require Canada to participate in an international fund that could provide up to \$450 million in compensation per incident (Natural Resources Canada, Media Release, “Harper Government to Strengthen Liability Regime for Nuclear Industry” (10 June 2013), online: Natural Resources Canada, <<http://www.nrcan.gc.ca/media-room/news-release/2013/7188>>).

¹⁸³ See *National Commission Report*, *supra* note 1 at 245.

¹⁸⁴ For a preliminary summary of BP’s partial liability obligations, see BP and the *Deepwater Horizon* disaster, *supra* note 23.

in the Beaufort Sea (where conditions make spill response efforts very difficult) and the Gulf of St. Lawrence (a near-enclosed water body relied on by five provinces for other economic activities) should be subject to a higher cap than the Atlantic offshore. Although conducting baseline studies to assess the rough monetary value of a worst-case scenario in different regions would be preferable prior to amending the applicable regulations,¹⁸⁵ the appropriate range is certainly in the billions of dollars.

In the United States, the statutory liability limit does not apply where there is a “violation of federal regulations.”¹⁸⁶ If Canada’s offshore liability regime continues to limit an operator’s maximum absolute liability, contraventions of federal statutes or regulations that “can be connected to the spill”¹⁸⁷ should similarly eliminate the cap.

3.3 UNCERTAIN AVAILABILITY OF ENVIRONMENTAL DAMAGES UNDER LIABILITY STATUTES

3.3.1 WEAKNESS: FEDERAL LIABILITY REGIMES DO NOT EXPRESSLY ALLOW FOR COMPENSATION FOR DAMAGES TO NATURAL RESOURCES, AND COMMON LAW AVAILABILITY OF SUCH COMPENSATION LACKS CLARITY

One of the biggest weaknesses of existing statutory offshore liability regimes is their lack of specificity about damages to the environment and natural resources. These resources are held in trust by the Crown for present and future generations, pursuant to its *parens patriae* jurisdiction,¹⁸⁸ and must be clearly protected as under United States legislation.¹⁸⁹

The problem is that the extent of compensation available for “all actual loss or damage” pursuant to section 26 of *COGOA* is unclear. Subsection 24(3) provides some clarification, but does not comprehensively define the scope of compensable damages:

In section 26, “actual loss or damage” includes loss of income, including future income, and, with respect to any aboriginal peoples of Canada, includes loss of hunting, fishing and gathering opportunities.

Although the statute does not expressly define compensable damages to include environmental or natural resource damages, the broad and undefined scope of compensable damages suggests that natural resource damages would be compensable under the *COGOA* liability regime. However, given the magnitude of the environmental damage that may be caused by an offshore blowout, governments have the responsibility of clearly articulating the inclusion of these damages, rather than relying on more general common law precedent to protect taxpayers and their natural heritage.

¹⁸⁵ *Liability Regulations*, *supra* note 52; *NS Liability Regulations*, *supra* note 52; *NL Liability Regulations*, *supra* note 52.

¹⁸⁶ Richardson, *supra* note 47 at 3.

¹⁸⁷ *Ibid.*

¹⁸⁸ *Canfor*, *supra* note 22 at para 76.

¹⁸⁹ Several United States statutes protect natural resources by establishing statutory civil liability regimes, including resource damage valuation mechanisms, for harm caused to natural resource: (*OPA*, *supra* note 68; *Comprehensive Environmental Response, Compensation and Liability Act*, 42 USC §§ 9601ff (2012) [*CERCLA*]).

In *Canfor*, the Supreme Court of Canada recognized the availability at common law of natural resource damages, or damages which compensate for harm to use value, passive use value, and inherent value of the natural environment.¹⁹⁰ Evidently, the Crown would, in appropriate circumstances, be entitled to seek such damages in relation to an offshore oil pollution incident.¹⁹¹

However, natural resource damages claims at common law are currently subject to uncertainties. First, the process for assessing natural resource damages is ill-defined, reflecting a lack of baseline ecological information and the inherent difficulty in assigning monetary values to environmental values. Second, it is unclear whether private third parties, beyond aboriginal peoples, would be entitled to advance claims for environmental damages.

3.3.2 *SOLUTION: INCORPORATE AN EXPLICIT STATUTORY NATURAL RESOURCE DAMAGE COMPENSATION MECHANISM, DRAWING ON CANADIAN AND AMERICAN MODELS*

The adoption of a comprehensive statutory assessment and liability regime for such damages could significantly reduce uncertainty and associated transaction costs, while increasing taxpayer protection. Statutory natural resource damage mechanisms are not without precedent, as they are incorporated into a number of North American laws.¹⁹² Examples of model statutory regimes in the offshore context include the US *Oil Pollution Act of 1990*¹⁹³ (“OPA”) and the *IFA*¹⁹⁴ in Canada. However, the US natural resource damage regime is more comprehensive and merits emulation.

i. Natural Resource Damages in the US Oil Pollution Act

The OPA was enacted in response to the *Exxon Valdez* spill and governs the assessment of and liability for natural resource damages caused by an oil pollution incident. Where a spill occurs as a result of offshore oil operations, every “responsible party”¹⁹⁵ is liable for “removal costs and damages” resulting from the spill.¹⁹⁶ The OPA expressly defines damages to include:

¹⁹⁰ *Canfor*, *supra* note 22 at para 72.

¹⁹¹ *Ibid* at para 81.

¹⁹² See e.g. *CEPA*, *supra* note 64, ss 40, 274(1)(a); *CERCLA*, *supra* note 191. See also *MLA*, *supra* note 44, s 77(2) and *Bill C-15*, *supra* note 184, cl 17, which recognize (a limited subset of) environmental damage as a category of compensable damage. The Yukon, Northwest Territories and Nunavut have basic natural resource damage regimes that do not establish a process to assess and negotiate a settlement with respect to natural resource damages. Significantly, these regimes do enable private parties to bring an action for natural resource damages (*Environmental Rights Act*, RSNWT 1988, c 83 (Supp), s 6; *Environmental Rights Act*, RSNWT 1988, c 83 (Supp), s 6, as enacted for Nunavut pursuant to the *Nunavut Act*, SC 1993, c 28; *Environment Act*, RSY 2002, c 162, ss 8, 12).

¹⁹³ *OPA*, *supra* note 68.

¹⁹⁴ *IFA*, *supra* note 34, s 13.

¹⁹⁵ Defined, in the context of offshore oil facilities, as “the lessee or permittee of the area in which the facility is located” (*OPA*, *supra* note 68, § 2701(32)(C)).

¹⁹⁶ *Ibid*, § 2702(a).

Damages for injury to, destruction of, loss of, or loss of use of, natural resources, including the reasonable costs of assessing the damage, which shall be recoverable by a United States trustee, a State trustee, an Indian tribe trustee, or a foreign trustee.¹⁹⁷

Natural resources under the *OPA* include:

[L]and, fish, wildlife, biota, air, water, ground water, drinking water supplies, and other such resources belonging to, managed by, held in trust by, appertaining to, or otherwise controlled by the United States (including the resources of the exclusive economic zone), any State or local government or Indian tribe, or any foreign government ...¹⁹⁸

The US federal government, state governments, Indian tribes, and, in certain circumstances, foreign governments are entitled to receive compensation for natural resource damages under the *OPA*.¹⁹⁹ These entities may be designated as natural resource trustees for the purposes of assessing natural resource damages.²⁰⁰ However, private citizens are not entitled to compensation for natural resource damages.

Regulations enacted under the *OPA* also prescribe a detailed process for assessing natural resource damages, further reducing or eliminating some of the litigation uncertainties associated with the Canadian common law process.²⁰¹ Pursuant to the *OPA*, designated natural resource trustees are required to “develop and implement a plan for the restoration, rehabilitation, replacement, or acquisition of the equivalent, of the natural resources under their trusteeship.”²⁰² Although the process is not perfect, and still suffers from baseline ecological data insufficiencies, it adds a great deal of clarity to the identification and quantification of damages to natural resources.

ii. Ahead of the Curve: IFA Protects Inuvialuit From Some, But Not All, Potential Natural Resource Damages

In Canada, the *IFA* liability regime discussed above explicitly provides for compensation for damage to natural resources. Although not perfect, the *IFA* provisions can serve as a useful model for the development of a federal natural resource damages liability regime, provided that the weaknesses discussed above are accounted for and addressed.

Accordingly, legislative amendments should make explicit the availability of natural resource damages, building on the models provided by the *OPA*, the *IFA*, and other statutory natural resource damages regimes. Legislative amendments to *COGOA* and the *Accord Acts* need only enable, pursuant to regulation, the establishment of a more detailed natural resource assessment and compensation regime.

¹⁹⁷ *Ibid*, § 2702(b)(2)(A).

¹⁹⁸ *Ibid*, § 2701(20).

¹⁹⁹ *Ibid*, § 2706(a).

²⁰⁰ *Ibid*, § 2706(b)-(d).

²⁰¹ 15 CFR § 990.40 *et seq.*

²⁰² *OPA*, *supra* note 68, § 2706(c)(1)(C).

3.4 ABSENCE OF EXPLICIT RECOGNITION OF THE POLLUTER-PAYS PRINCIPLE

Although implementation of the polluter-pays principle must be a fundamental principle of the statutory liability regimes created by *COGOA* and the *Accord Acts*, none of these statutes explicitly adopts that principle.

Explicit recognition of the polluter-pays principle, particularly when coupled with substantial increases to or the outright elimination of statutory maximum absolute liability limits, sends a clear signal to industry that it will be held liable for the costs of pollution. Without this signal, industry may have more incentive for risky behaviour, knowing that the taxpayer will ultimately subsidize the consequences of such behaviour. The certainty provided by an explicit statutory recognition of the polluter-pays principle removes this incentive and instead promotes industry behaviour that seeks to “protect ecosystems in the course of ... economic activities.”²⁰³ The *COGOA* liability regime should be amended to incorporate a provision that expressly identifies the implementation of the polluter-pays principle as an objective of the liability regime.²⁰⁴

3.5 LACK OF COMPLEMENTARY MECHANISMS TO ENSURE REMEDIATION AND COMPENSATION IN CASES WHERE THE OPERATOR IS UNWILLING OR UNABLE TO FUND THESE EFFORTS

3.5.1 *WEAKNESS: THE CANADIAN OFFSHORE LIABILITY REGIME LACKS COMPLEMENTARY ('SAFETY NET') COMPENSATION MECHANISMS TO PROTECT TAXPAYERS WHERE POLLUTERS CANNOT OR WILL NOT PAY*

The Canadian offshore liability regime does not incorporate complementary mechanisms designed to fund remediation and compensate victims in circumstances where the polluter cannot or will not do so itself or where the magnitude of the pollution damage exceeds absolute liability limits and tort claims fail to bridge the gap. Consequently, remediation and compensation in such circumstances must be undertaken at the expense of the taxpayer, or not at all. While complementary mechanisms may provide a necessary safety net that would insure the taxpayer against gaps in the liability regime, these measures should be viewed as ancillary or complementary to, and not a replacement for, the statutory absolute liability regime.²⁰⁵

3.5.2 *SOLUTION: ADOPT A COMPLEMENTARY ('SAFETY NET') COMPENSATION MECHANISM SUCH AS A MUTUAL INSURANCE POOL OR A DEDICATED REMEDIATION AND COMPENSATION FUND*

Two complementary mechanisms that merit consideration for inclusion in federal liability reforms are a mutual insurance pool and a dedicated remediation and compensation fund. To be clear, neither of these mechanisms should be viewed as a substitute for abolishing (or significantly increasing) maximum absolute liability limits, making explicit the availability of

²⁰³ *Imperial Oil*, *supra* note 39 at para 24.

²⁰⁴ Such a provision could be inserted between sections 24 and 25, and might read “The purposes of sections 25 to 27 are to ensure that the polluter bears the costs of pollution and to promote the internalization of environmental costs.”

²⁰⁵ Dedicated, industry-capitalized funds, for example, do “not affect responsible parties’ liability” (Richardson, *supra* note 47 at 3).

natural resource damages, and clarifying operator liability for spill response costs. Rather, these mechanisms should only be adopted in addition to all three aforementioned reforms.

i. Mutual Insurance Pool

One proven mechanism for transferring the risk of liability for oil pollution damages away from taxpayers is a mutual insurance pool. The pooled insurance approach has been embraced in the UK, where the government requires all offshore operators to be members of the Offshore Pollution Liability Association (“OPOL”).²⁰⁶ Membership in OPOL is contingent on the operator assenting to OPOL’s Offshore Pollution Liability Agreement, which makes the operator strictly liable for damages caused by a spill, up to a maximum of USD \$250 million per incident.²⁰⁷ Furthermore, in the event that any member cannot or will not discharge its liability obligations, the remaining OPOL members are responsible for doing so.²⁰⁸

While it reduces taxpayer exposure to the risk of financial liability for oil pollution remediation and compensation, the mutual insurance pool model has obvious weaknesses. By effectively requiring large operators to subsidize small operators, the model risks encouraging free-rider behaviour and decreases incentives for smaller operators to operate in optimally safe and environmentally responsible manners. This may give rise to a moral hazard. Furthermore, the model does not encourage desirable behavioural modifications at the level of individual companies.

On the other hand, some of these weaknesses may be less applicable in the Canadian context. For example, the absence of small operators in Canada’s offshore reduces the subsidization and free-riding drawbacks. While a mutual insurance pool inadequately encourages individual company behaviour modification, Canada’s liability regime, unlike that of the United Kingdom, imposes a mix of strict and absolute liability, and increases to absolute liability limits could effectively achieve the safety culture goal. Adopting a mutual insurance pool may also reduce the insurance premium increases generated by an absolute liability limit.

In the Canadian context, therefore, the weaknesses of the mutual insurance pool may be outweighed by its significant benefits as a guaranteed source of private sector funds, but only if it is implemented in addition to abolition of – or significant increases to – the absolute liability cap, explicit statutory incorporation of natural resource damages, and clarification of operator liability for spill response costs.

²⁰⁶ Oil & Gas UK, *Background Information*, online: Oil & Gas UK Knowledge Centre <<http://www.oilandgasuk.co.uk>> [Oil & Gas UK].

²⁰⁷ The Offshore Pollution Liability Association Ltd, *Offshore Pollution Liability Agreement*, clause IV(A), online: OPOL: <<http://www.opol.org.uk>>. Operators must also carry insurance of at least USD \$500 million in the annual aggregate (OPOL, *Rules of The Offshore Pollution Liability Association Limited*, Form B, online: OPOL: <<http://www.opol.org.uk>>).

²⁰⁸ *Ibid*, clause III(2); see also Oil & Gas UK, *supra* note 208.

ii. Dedicated Fund For Remediation and Compensation

A second complementary mechanism worth considering is a dedicated fund for remediation and compensation.²⁰⁹ Establishing and maintaining such a fund with industry contributions would pre-emptively transfer the risks of financial liability for remediation (i.e., containment and clean up of oil spills) and compensation from taxpayers to industry, reducing the potential difficulties of enforcing liability obligations after a spill has occurred.

Although the Canadian offshore liability regime does not require industry to make payments into a dedicated oil spill remediation and compensation fund, the US regime does. The US *Internal Revenue Code* establishes the Oil Spill Liability Trust Fund²¹⁰ (“OSLTF”), while the *OPA* authorizes its use to fund oil spill remediation (including containment and other clean-up costs) and compensation costs.²¹¹ The OSLTF is funded by industry through penalty payments, cost recovery payments, and a per-barrel tax on imported and domestically produced petroleum.²¹²

Canada’s Ship-source Oil Pollution Fund (“SSOPF”), maintained pursuant to the *Marine Liability Act*, is similar in concept to the OSLTF.²¹³ The SSOPF is funded by industry through the imposition of levies on the metric tonnage of oil shipped as cargo into or from within Canada.²¹⁴ In 2012, the levy was 47.94 cents per metric ton of oil.²¹⁵ As a number of other international funds are available to provide compensation for ship-source oil spills, the SSOPF is only a partial solution.²¹⁶

The SSOPF operates as a last resort mechanism for compensating victims of oil pollution originating from ‘ships,’ allowing victims to receive compensation when polluters cannot or will not pay, or where the identity of the polluter is unknown.²¹⁷ For the purposes of the SSOPF, a ‘ship’ is defined as:

[A]ny vessel or craft designed, used or capable of being used solely or partly for navigation, without regard to its method of propulsion or lack of propulsion, and includes

(a) a ship in the process of construction from the time that it is capable of floating; and

²⁰⁹ Again, the authors recommend the implementation of a dedicated, industry-capitalized compensation fund in addition to, and not as a replacement for, abolishing (or significantly increasing) the maximum absolute liability limit, making explicit the availability of natural resource damages, and clarifying operator liability for spill response costs.

²¹⁰ *Oil Spill Liability Trust Fund*, 26 USC § 9509 (2012).

²¹¹ *OPA*, *supra* note 68, § 2712.

²¹² US Coast Guard, *The Oil Spill Liability Trust Fund (OSLTF)*, online: National Pollution Funds Center <<http://www.uscg.mil>>.

²¹³ *MLA*, *supra* note 44, ss 91-125.

²¹⁴ *Ibid*, s 112(2).

²¹⁵ Government Notice, (2012) C Gaz Vol 146, No 18 (*Marine Liability Act*).

²¹⁶ See e.g. *MLA*, *supra* note 44, s 57, Schedule 6 (the funds available under the International Fund for Compensation for Oil Pollution Damage) and *ibid*, s 63, Schedule 7 (the International Oil Pollution Compensation Supplementary Fund).

²¹⁷ *Ibid*, ss 101, 103, 107.

(b) a ship that has been stranded, wrecked or sunk and any part of a ship that has broken up.²¹⁸

However, SSOPF funds cannot be accessed where a spill is caused by “a drilling ship that is on location and engaged in the exploration or exploitation of the seabed or its subsoil in so far as an escape or discharge of oil emanates from those activities.”²¹⁹ The SSOPF could easily, and should be, made applicable to spills caused by such mobile offshore drilling units through an amendment to the *Marine Liability Act*.

While effective at transferring liability risk from taxpayers to industry, such dedicated funds are not without weaknesses. In addition to the concerns discussed above in relation to mutual insurance pools, which also apply in the context of a dedicated fund, industry may decry the ineffective use of capital that such funds can represent, as resources may be accumulated and frozen for years. The effectiveness of funds may also be restricted by inappropriate per-incident liability limits,²²⁰ while administration of a fund may create procedural inefficiencies in recovering compensation. For the SSOPF or another offshore-specific fund to be appropriately applied, these latter two aspects would require particular attention.

While there are disadvantages to dedicated funds, they also enjoy advantages similar to those discussed above in the context of mutual insurance pools. Innovative fund structures could, for example, direct reinvestment of a percentage of accumulated capital into scientific monitoring or baseline data collection. Such innovative structuring could mitigate some of the main concerns with the fund model while improving taxpayer protection pursuant to other aspects of the liability regime. Furthermore, the reassurance that the presence of such a fund can provide to taxpayers should not be understated.

3.6 LACK OF CLARITY AS TO WHAT CONSTITUTES “REASONABLE” SPILL RESPONSE MEASURES AND COSTS AND WHEN OPERATOR WILL BE LIABLE FOR SUCH COSTS

Many of the preceding gaps in Canada’s offshore liability regime arise in the context of operator liability for loss or damage resulting from a spill. While liability for spill response costs must be distinguished from liability for damages, the regime’s provisions in relation to the former nevertheless suffer from weaknesses.

3.6.1 WEAKNESS: THE EXTENT OF OPERATOR LIABILITY FOR COSTS RELATED TO IMMEDIATE SPILL RESPONSE AND CLEAN-UP IS UNCLEAR

Operator liability for “any” spill response costs, pursuant to section 25(7) of *COGOA*, can only arise in respect of a “reasonable measure in relation to the spill.” Although the term is

²¹⁸ *Ibid*, s 91(1).

²¹⁹ *Ibid*, s 101(2).

²²⁰ For example, the per-incident compensation from the SSOPF was limited to \$159,854,965 for the fiscal year beginning April 1, 2012 (Administrator of the Ship-source Oil Pollution Fund, *The Administrator’s Annual Report 2011-2012* (Ottawa: Office of the Administrator of the Ship-source Oil Pollution Fund, 2012) at iii). This limit should be abolished or substantially increased. For example, the OSLTF per-incident limit is \$1 billion, though this per-incident limit is also subject to criticism for being too low (Richardson, *supra* note 47 at 3, 5).

not explicitly defined in *COGOA*, it appears that a ‘reasonable measure in relation to the spill’ includes:

...all reasonable measures consistent with safety and the protection of the environment to prevent any further spill, to repair or remedy any condition resulting from the spill and to reduce or mitigate any danger to life, health, property or the environment that results or may reasonably be expected to result from the spill.²²¹

Unfortunately, this list is non-exhaustive and ambiguous, and provides no guidance as to what measures will be considered reasonable. Furthermore, the term has not received judicial consideration in Canada. As a result, the extent to which liability arises under section 25 of *COGOA* is unclear. “Reasonable measures in relation to the spill” could potentially be interpreted narrowly to include only those spill control measures necessary for emergency response. Alternatively, the term could be interpreted broadly to include long-term rehabilitation measures necessary to effect ecosystem restoration, including post-spill monitoring and evaluation, which could conceivably extend over decades.

COGOA’s lack of clarity about the extent of operator liability for spill response costs risks encouraging time-consuming litigation that may undermine response efforts, as “[a]ny extensive delay could have a dramatic impact on the region and jeopardize the survival of those who rely on the land and ocean.”²²²

3.6.2 SOLUTION: CLARIFY THE EXTENT TO WHICH OPERATORS ARE LIABLE FOR SPILL RESPONSE COSTS BY PROVIDING MORE SPECIFIC, NON-EXHAUSTIVE GUIDANCE CONCERNING WHAT WILL CONSTITUTE A “REASONABLE MEASURE IN RELATION TO THE SPILL”

The lack of clarity as to what will constitute a “reasonable measure in relation to the spill” can be easily remedied by amending *COGOA* to clearly incorporate long-term ecological monitoring and evaluation.

In addition, the term could be more exhaustively defined. The US *OPA* may provide a useful model for this amendment. Parties responsible for an oil spill in the United States are, pursuant to the *OPA*, liable for the full “removal costs” associated with such a spill.²²³ In the event of a spill, removal means:

[C]ontainment and removal of oil or a hazardous substance from water and shorelines or the taking of other actions as may be necessary to minimize or mitigate damage to the public health or welfare, including, but not limited to, fish, shellfish, wildlife, and public and private property, shorelines, and beaches.²²⁴

²²¹ *COGOA*, *supra* note 43, s 25(3); *NS Accord Act*, *supra* note 43, s 166(3); *NL Accord Act*, *supra* note 43, s 161(3). *COGOA*, s 25(6) makes reference to “reasonable measures in relation to the spill that are referred to in subsection (3)”; see also *NS Accord Act*, *supra* note 43, s 166(6); *NL Accord Act*, *supra* note 43, s 161(6). Pursuant to *COGOA*, *supra* note 43, s 26(2.1), spill response costs incurred under subsection 25(7) of *COGOA* do not count toward the statutory liability limits; see also *NS Accord Act*, *supra* note 43, s 167(2.1); *NL Accord Act*, *supra* note 43, s 162(2.1).

²²² *Arctic Offshore Drilling Review*, *supra* note 28 at 47-48.

²²³ *OPA*, *supra* note 68, § 2702(a).

²²⁴ *Ibid.*, § 2701(30).

The use of the phrase “including, but not limited to” provides needed clarity without stifling innovation and the development of world-class safety standards by being overly prescriptive. Amendments to *COGOA* to clarify what will constitute a “reasonable measure in relation to the spill” would benefit from a similar degree of specificity.

3.7 RESTRICTION ON THE IMPOSITION OF JOINT AND SEVERAL STRICT LIABILITY

The imposition of joint and several liability on at-fault or negligent polluters aims to ensure that victims of pollution damage are fully compensated by allowing victims to recover the full amount of compensation from any one, or any combination of, the polluters. The polluters are left to apportion liability, in accordance with degree of fault, among themselves.

However, the joint and several nature of liability under *COGOA* is qualified by the phrase “to the extent determined according to the degree of fault or negligence proved against them.”²²⁵ The apparent requirement to apportion liability pursuant to this phrase fundamentally contradicts the notion of joint and several liability. The conflict created by this unnecessary limitation on joint and several liability will likely lead to lengthy and time-consuming litigation and may prevent some victims from receiving compensation. The apportionment of liability in accordance with the degree of fault or negligence should reflect the concept of “channelling” embodied in the absolute liability regime. The ambiguity can, however, be easily remedied by legislative amendment. Reforms to *COGOA* should eliminate the qualification on the joint and several nature of strict liability.

3.8 THE INTERACTION BETWEEN THE *AWPPA* AND *COGOA* LIABILITY REGIMES IS UNCLEAR

Although *COGOA* and the *AWPPA* are clearly intended to operate in conjunction to ensure that an operator is in no case absolutely liable for more than \$40 million, the prioritization between the two regimes lacks clarity.

As discussed above, the maximum absolute liability limit under *COGOA* for areas to which the *AWPPA* applies is:

[T]he amount by which 40 million dollars exceeds the amount prescribed pursuant to section 9 of [the *AWPPA*] in respect of any activity or undertaking engaged in or carried on by any person or persons described in paragraph 6(1)(a) of [the *AWPPA*].²²⁶

As the *AWPPA* currently limits operator absolute liability to \$40 million, a plain reading of the preceding provision leads to the conclusion that the current *COGOA* absolute liability limit for areas to which the *AWPPA* applies is \$0 (i.e., \$40 million equals, but does not exceed,

²²⁵ *COGOA*, *supra* note 43, s 26(1)(b); *NS Accord Act*, *supra* note 43, s 167(1)(b); *NL Accord Act*, *supra* note 43, s 162(1)(b).

²²⁶ *Liability Regulations*, *supra* note 52, s 3(a); *NL Liability Regulations*, *supra* note 52, s 3(a).

the amount prescribed pursuant to the *AWPPA*).²²⁷ Accordingly, all claims for compensation arising from spills in areas in which the *AWPPA* applies must proceed in accordance with the procedures²²⁸ established under that statute.

This lack of harmonization creates unnecessary complexities in the offshore liability regime that may allow polluters to escape liability. For example, where compensation for the full amount of the absolute liability limit cannot be obtained under the more restrictive *AWPPA* regime, it appears as though a claimant cannot resort to the *COGOA* regime to recover the shortfall.²²⁹ Furthermore, if the maximum absolute liability limit under the *AWPPA* is altered in the future, such that the *COGOA* absolute liability limit would be greater than \$0, the lack of harmonization between the two regimes would result in unnecessary administrative inefficiencies. Therefore, insofar as they apply to offshore oil operations, the two regimes should be harmonized.

3.9 THE PROVISION PROTECTING OPERATORS AGAINST DOUBLE LIABILITY APPEARS TO IMPOSE A CAP ON THE AMOUNT FOR WHICH AN OPERATOR CAN BE LIABLE, EVEN IF FOUND TO BE AT FAULT OR NEGLIGENT

As discussed above, subsection 26(2.1) of *COGOA* precludes the imposition of “double” absolute liability under *COGOA* and another statute. However, the drafting of this provision has been subject to criticism that subsection 26(2.1) would restrict compensation to the prescribed maximum absolute liability limit even where fault or negligence in relation to a spill can be

²²⁷ This interpretation was adopted by a panel of the Inuvialuit Environmental Impact Review Board during its review of the proposed Isserk offshore drilling program (Environmental Impact Review Board, *Public Review of the Esso Chevron et al Isserk I-15 Drilling Program* (Inuvik, Northwest Territories: Environmental Impact Review Board, 1989) at 26 [*EIRB Esso Chevron*]). The panel went on to note that participants in the review process had voiced concerns with the complexity and uncertainty surrounding the interaction between the liability regimes of the *AWPPA* and what was then the *Oil and Gas Production and Conservation Act* (*ibid*). It should be noted that the current *Liability Regulations*, on which the Isserk panel based this interpretation, have not been changed since the Isserk decision was released and continue to refer to the *Oil and Gas Production and Conservation Act*, even though that act was renamed the *Canada Oil and Gas Operations Act* (*Liability Regulations, supra* note 52, s 2; *Bill C-58, supra* note 71, cl 2).

²²⁸ Notably, the *AWPPA* does not protect operators against double liability. While it is clear that an operator’s combined maximum absolute liability under the *AWPPA* and *COGOA* cannot exceed \$40 million, the *AWPPA* regime leaves open the possibility that operators may be exposed to double liability in conjunction with other laws. Furthermore, the limitation period for bringing a claim under the *AWPPA* differs from that for bringing a claim under *COGOA* or the *NL Accord Act*, as discussed above.

²²⁹ In the past, the Inuvialuit Environmental Impact Review Board has taken the position that the *AWPPA* liability regime supersedes that of *COGOA* (*EIRB Esso Chevron, supra* note 229 at 26). Take, for example, a plaintiff seeking to recover compensation for an oil spill three years after the spill. The *AWPPA* limitation period has expired, so compensation cannot be received pursuant to that regime. However, because the *AWPPA* regime supersedes the *COGOA* regime, it appears as though the plaintiff is barred from recovering damages under the latter regime as well, even though the latter regime’s limitation period has not expired.

established.²³⁰ Critics argue that subsection 26(2.1) ought to read “subsection (1)(a) or (2)(a)” as opposed to “subsection (1) or (2).” At the very least, the provision lacks clarity, a problem that could be fairly easily remedied while undertaking more substantive reforms.

4. CONCLUSIONS

Canada’s current offshore liability regime suffers from a number of weaknesses that actually increase the risk of a worst-case scenario oil pollution incident by failing to promote an appropriate industry safety culture, while exposing Canadian taxpayers to potentially massive liabilities in the event of a serious spill. These weaknesses include:

- inappropriately low maximum absolute liability limits;
- uncertain availability of environmental damages, and no mechanism for assessing the costs of long-term ecological system damage;
- an absence of express recognition of the polluter-pays principle;
- lack of a dedicated, industry-capitalized fund or mutual insurance pool to ensure remediation and compensation even where the operator is unwilling or unable to finance these efforts;
- lack of clarity regarding the breadth of operator liability for spill response costs;
- a restriction on the imposition of joint and several liability under the residual strict liability regime;
- lack of clarity regarding the overlap between the *COGOA* and *AWPPA* liability regimes; and
- a drafting error pertaining to the non-availability of double liability.

Complementary liability provisions (i.e., under the *AWPPA*, the *IFA* and the *Fisheries Act*) do not remedy the weaknesses of the main *COGOA* liability regime because of their limited scope of application.

In order to effectively reduce the risks borne by taxpayers in the event of an offshore oil pollution incident to an appropriate level, liability reforms must:

- 1) a. Remove the limit on operator’s maximum absolute liability;
b. In the alternative, significantly increase maximum absolute liability limits and create an exception to the cap where operators contravene federal laws;
- 2) Increase financial responsibility requirements to screen out fiscally unqualified operators, although not necessarily to the level of the absolute liability cap;

²³⁰ Boris B de Jonge, “Financial Responsibility Requirements for Oil and Gas Activities Offshore Nova Scotia and Newfoundland” (2001) 24 Dalhousie LJ 109 at 113, note 11. De Jonge notes that the *NS Accord Act* provision, which is identical to that found in *COGOA*, “provides that where the statutory liability provisions apply, no person will be liable for more than the greater of the prescribed limit for absolute liability for spills or debris...and the amount for which the person would be liable under any other law for the same occurrence. This subsection is not limited to the paragraphs dealing with absolute liability but applies to all of s. 167(1) and (2), including the paragraphs creating liability in cases of fault or negligence.”

- 3) Make explicit in relevant statutes the availability of and procedure for assessing natural resource damages;
- 4) Adopt a purposive or preambular provision acknowledging that implementation of the polluter-pays principle is a primary objective of the liability regime;
- 5) Incorporate complementary mechanisms, such as a mutual insurance pool or a dedicated remediation and compensation fund, having regard to potential problems of free-ridership, as an addition to (rather than an alternative to) the reforms proposed under points 1, 3 and 6;
- 6) Clarify the extent to which operators are liable for spill response costs by providing specific, but non-exhaustive, guidance as to what measures will be considered reasonable “in relation to a spill”;
- 7) Remove the limitation on joint and several strict liability in paragraph 26(1)(b) of *COGOA*;
- 8) Clarify the interaction between the *AWPPA* and *COGOA* liability regimes; and
- 9) Correct the drafting error in subsection 26(2.1) of *COGOA* to clarify the restriction on double liability.