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Clinique de droit environnementale
Environmental Law Clinic

Ecojustice Memorandum

Re: Who pays when an oil spill occurs off Canada's coasts? Answer: the Canadian taxpayer

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Executive Summary

Oil companies are engaging in offshore oil operations on Canada's Atlantic and Arctic coasts under a limited liability regime that would have taxpayers and the environment footing the bill for any disasters that occur. The ongoing disaster in the Gulf of Mexico will cost untold billions of dollars to clean up. However, under Canadian laws, a company causing a similar spill would see their liability for remediation and restoration costs capped at \$40M or less, with the remainder to be absorbed by governments and the environment itself. The Canadian taxpayer's exposure to the proven financial risks of ecological catastrophe begs a comprehensive and independent review of these industry-friendly rules.

Offshore oil activities are governed by three main statutes: 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* (offshore Accord Acts). While the latter two laws concern the Newfoundland and Nova Scotia offshore oil fields which are both under joint federal-provincial jurisdiction, the former concerns the remainder of Canada's offshore areas, including the Arctic, which falls under purely federal jurisdiction.

All three acts are substantially the same regarding spills and liability provisions. 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". When unauthorized spills occur, the laws stipulate that the costs associated with their management are to be borne by the party originally authorized for the offshore drilling work (e.g. the oil company).

However, regulations under these laws impose strict limits on an oil company's spill liability. For spills under the National Energy Board's jurisdiction in Arctic waters, liability is capped at \$40M.

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For Atlantic offshore oil areas, including those regulated by federal-provincial offshore petroleum boards, the liability limit is \$30M. But both of these limits apply only if the spill is not attributable to the authorized party's fault or negligence. In other words, an offshore oil company may invoke a "due diligence" defence in order to shelter themselves from liability above the cap.

Conversely, for any party (including authorized oil companies and third parties they may contract to work on the offshore rigs) whose fault or negligence is established in relation to the spill, liability is unlimited by the regulations. It must be noted that a potential "loophole" in the legislation could be interpreted to cap liability even where a company has been negligent. This matter should be rectified immediately.

When authorizing a project, each of the three Boards can also impose other conditions on the proponent generally relating to "liability for loss, damage, costs or expenses". The Boards therefore reserve the right to further reduce the liability exposure for offshore oil companies in a particular case, or for classes of offshore projects (e.g. shallow water versus deep water drilling). It is important to note that any decisions to limit liability, being a matter within the Boards' discretion, would not face independent oversight or be subject to the will of Parliament. On the flipside, the Boards do not have the discretion to raise the ceiling on liability beyond the \$30M (Atlantic) or \$40M (Arctic) limit. Where a company has been negligent and damages exceed the statutory caps, victims must seek compensation before a court, rather than the relevant Board.

The two Atlantic Offshore Boards have issued guidelines requiring companies to demonstrate financial resources sufficient to cover potential liabilities. However, given the magnitude of costs and liabilities now facing BP, these "financial responsibility" guidelines require relatively modest resources, and need to be substantially increased to ensure that similar liabilities do not go unpaid in Canada.

Note that the preceding discussion refers to spills at offshore oil and gas operations sites. For spills associated with oil tanker shipping, the liability regime is different, governed by the *Marine Liability Act*. Ships under 300 tonnes have their liability capped at CDN \$500,000 for oil pollution damage, while larger ships of up to 5,000 tonnes have a liability limit of approximately USD \$6,650,000. Ships above 5,000 tonnes have liability limits increased proportionately with each additional tonne, up to an absolute maximum of approximately USD \$132,400,000.

It is also possible that the liability regime under the federal *Fisheries Act* could be applied to offshore oil and gas operations. If a "deleterious substance" is deposited without authorization in waters frequented by fish, as per section 36, the corresponding cleanup and spill mitigation costs, as well as economic compensation payments to fishermen could exceed any limitation of liability contemplated by COGOA or the offshore Accord Acts. In this case, the "no double liability" provision in subsection 26(2.1) of COGOA and corresponding provisions in the accord acts, would allow liability to go beyond the prescribed limits.

However, penalties under the *Fisheries Act* liability regime are open to certain limited defenses, which are not available under COGOA or the offshore Accord Acts. Liability under these latter statutes is absolute, making it easier for the public to recover costs relating to spills.

In the wake of the BP tragedy unfolding in the Gulf of Mexico, the issues of environmental cost internalization and appropriate environmental risk balancing have been brought to the fore.

When offshore oil companies are given statutory guarantees that their spill liability cannot exceed \$40M for operations in Canada, it arguably *increases* the risk of environmental damage, since liability caps make it economically attractive for industry to take risks. It also makes it more attractive for private equity to support such economic ventures with their investment dollars, as risk levels are always factored into market investment decisions.

This is not to suggest that offshore oil companies have an incentive to act irresponsibly; rather, it simply points to the fact that federal and provincial governments have, by these statutory limitations on liability, made conscious decisions to remove a disincentive to engage in an economic activity that has the proven potential to cause irreparable environmental and economic damage. Such liability limits amount to a public subsidy of the offshore oil industry: by effectively committing public funds to cover any costs above the cap, oil companies are allowed to escape the prospective costs of a disaster and to anticipate the shifting of such costs onto the public. Canadian taxpayers should consider themselves forewarned.

Not surprisingly, U.S. politicians are taking a hard look at offshore liability caps, given that the anticipated damages associated with the Deepwater Horizon tragedy are now being assessed at upwards of USD \$100B (which represents roughly 20% of Canada’s entire federal debt). Developments on this front are unfolding in the U.S. Senate presently, and debate is focused on the appropriateness of eliminating liability limits – it is a virtual certainty that limits will be increased, and possibly retroactively so in order to cover the BP situation.

Canada needs to follow suit. With the National Energy Board about to commence a review of the safety and environmental requirements associated with Arctic offshore drilling, the time is right to conduct a comprehensive re-examination of Canada’s offshore oil liability regime. However, given that this NEB hearing will not examine offshore oil operations on the East coast, it remains to be seen how the federal government (along with the governments of Newfoundland and Nova Scotia) will ensure that Canadian taxpayers are not left to assume the financial, let alone environmental risks of this economic activity. In the authors’ opinion, if oil companies are not prepared to accept the full costs of potential liability arising from such high-risk activities as offshore oil drilling, perhaps they should not be in this business in the first place.

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Introduction

The sinking of the Deepwater Horizon oil rig in the Gulf of Mexico and the ensuing oil spill have raised awareness of the issue of spill liability caps. With cleanup costs already in the billions of dollars, and with U.S. taxpayers becoming increasingly aware of the potential economic and environmental liabilities associated with offshore drilling, the U.S. government is re-examining the rules related to liability limitation for offshore oil and gas operations. Canada should do the same.

In the U.S. *Oil Pollution Act* of 1990, parties responsible for an oil spill are currently liable for no more than \$75 million in economic damage.¹ This cap applies in cases where there is no finding of fault for a spill.² The liability cap does not include containment and cleanup costs; there is no limit on what a company must pay for such costs.³ Additionally, if an oil company is found at fault for a spill, there is no limit on compensatory or punitive damages an oil company must pay. The Interior Department has the power to adjust the liability cap every three years in order to account for inflation, although it has not been adjusted for 20 years.⁴ In response to the BP disaster, however, a U.S. Senate committee voted on June 30, 2010 to remove this cap altogether.⁵

This memorandum will explore the applicable regime of limited liability for offshore oil operations in Canada. In Canada, the liability caps *do* include containment and cleanup costs, and the cap is far lower—up to a maximum of \$30 million in Atlantic waters, or \$40 million in Arctic waters. As in the U.S., proof of fault or negligence would remove this limitation on liability.

When offshore oil companies are given statutory guarantees that their spill liability cannot exceed \$40M for operations in Canada, it arguably *increases* the risk of environmental damage, since liability caps make it economically attractive for industry to take risks. It also makes it more attractive for private equity to support such economic ventures with their investment dollars, as risk levels are always factored into market investment decisions.

This is not to suggest that offshore oil companies have an incentive to act irresponsibly; rather, it simply points to the fact that federal and provincial governments have, through these statutory limitations on liability, made conscious decisions to remove a market-based disincentive to

¹ Lorber, Janie. (2010, June 9). Democrats push to eliminate liability cap. The Caucus, <http://thecaucus.blogs.nytimes.com/2010/06/09/democrats-push-to-eliminate-liability-cap/?scp=1&sq=oil%20spill%20liability&st=cse>.

² McGowen, Elizabeth. (2010, May 27). U.S. Policy experts: Premature to pass oil spill liability bill. Solve Climate, <http://solveclimate.com/blog/20100527/u-s-policy-experts-premature-pass-oil-spill-liability-bill>

³ *Ibid.*

⁴ *Ibid.*

⁵ <http://www.reuters.com/article/idUSTRE65T4SA20100630?type=politicsNews>

engage in an economic activity that has the proven potential to cause irreparable environmental and economic damage. Such liability limits amount to a public subsidy of the offshore oil industry: by effectively committing public funds to cover any costs above the cap, oil companies are allowed to externalize the prospective costs of a disaster and to anticipate the shifting of such costs onto the public. Canadian taxpayers should consider themselves forewarned.

By way of contrast, liability ceilings are presently being reviewed for the Canadian nuclear industry. Although it now stands at \$75M, a federal bill has passed first reading that would raise the cap under the *Nuclear Liability Act* to \$650 million.⁶ Notwithstanding concerns that even this proposed cap is inappropriate, no such action has been taken with respect to Canada's offshore petroleum industry.

With the National Energy Board about to commence a review of the safety and environmental requirements associated with Arctic offshore drilling, the time is right to conduct a comprehensive re-examination of Canada's offshore oil liability regime. However, given that this NEB hearing will not examine offshore oil operations on the East coast, it remains to be seen how the federal government (along with the governments of Newfoundland and Nova Scotia) will ensure that Canadian taxpayers are not left to assume the financial, let alone environmental risks of this economic activity. In the authors' opinion, if oil companies are not prepared to accept the full costs of potential liability arising from such high-risk activities as offshore oil drilling, perhaps they should not be in this business in the first place.

The main issues examined in this memorandum are as follows:

1. Does Canadian law provide for total cost recovery from an operator for an oil spill?
2. If not, what losses and expenses would be covered in the event of a spill?
3. Are there any differences between the liability regimes for offshore oil operations on the Atlantic coast as opposed to the Arctic coast?
4. What, if any, are the limitations on spill liability?

Analysis:

A) *COGOA and the Atlantic Accord Acts*

The main statute governing oil and gas operations in Canada's Northwest Territories, Nunavut, and most submarine areas is the *Canada Oil and Gas Operations Act (COGOA)*. It does not include oil sands operations. The offshore jurisdictions of Nova Scotia and Newfoundland and Labrador are governed by separate "accord acts"⁷, but for present purposes, their content is substantially the same as COGOA. Subsequent references are to provisions in COGOA, with

⁶ Bill C-15, the *Nuclear Liability and Compensation Act*,
<http://www2.parl.gc.ca/HousePublications/Publication.aspx?Docid=4436026&file=4>

⁷ *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act*, 1988, c. 28.
Canada-Newfoundland Atlantic Accord Implementation Act, 1987, c. 3.

footnotes to the corresponding sections of the “accord acts”.

i) “Spill” defined

Sections 24-27 of COGOA concern “Spills and Debris”.⁸ Section 24 defines “Spill” 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 ship to which Part XV of the *Canada Shipping Act* or Part 6 of the *Marine Liability Act* applies.”⁹ The *Canada Shipping Act, 2001* and *Marine Liability Act* are discussed further below.

ii) Those engaged in oil and gas operations must take all reasonable measures to contain and clean up a spill

Subsection 25(3)¹⁰ of COGOA requires that those responsible for a spill take all reasonable measures to contain and clean up the spill.

iii) If such measures are not being taken, the Chief Conservation Officer has power to direct management of the spill

If such measures are not being taken, subsections 25(4)-(6)¹¹ grant the Chief Conservation Officer the power to direct the management of the spill. The Chief Conservation Officer is designated by the National Energy Board, and there is a Chief Conservation Officer designated by the respective Atlantic offshore boards.

iv) Spill management costs are to be borne by the party authorized for the work

Subsection 25(7)¹² states that any costs incurred through such spill management action are to be borne by the party who originally received authorization for the work (e.g. the oil company). The costs can be recovered in court, and until paid they are a debt to the federal government. Costs incurred in operations in the Newfoundland and Nova Scotia offshore jurisdictions constitute a debt to their respective offshore boards, rather than the federal government.

v) Other parties can recover cleanup costs from federal government

Subsection 25(7.1)¹³ also provides that any other persons who, of their own initiative, take actions to manage the spill, can recover *their* costs from the federal government. However, the federal government would then be able to recover these costs from the company.

⁸ Ss. 160-64 of the Newfoundland accord act; ss. 165-69 of the Nova Scotia accord act

⁹ Only the C-NLOPB has updated this section to refer to Parts 8 and 9 of the newer *Canada Shipping Act, 2001*, rather than Part XV of the older *Canada Shipping Act*. Parts 8 and 9 “[do] 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*.” Sections 3(a) and (b) of COGOA refer 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.”

¹⁰ 161(3) for NFLD, 166(3) for NS.

¹¹ 161(4)-(6) for NFLD, 166(4)-(6) for NS.

¹² 161(7) for NFLD, 166(7) for NS.

¹³ 161(7.1) for NFLD, 166(7.1) for NS. Even cleanup costs in the NFLD and NS offshore zones are recoverable from the federal government.

vi) Liability can be limited both by regulations and by Board authorizations

While subsection 25(7) says that “any costs incurred” in managing the spill are to be borne by the party authorized for the work, parties governed by COGOA may have liability limits imposed through regulations, or by the National Energy Board. Subsection 5(4)(a)¹⁴ states that any authorized works are subject to other Board-determined requirements relating to “liability for loss, damage, costs or expenses”.

Subsection 26(1)(a) states that, for any spill, the person authorized for the work is liable “up to any prescribed limit on liability”. The person is liable for “all actual loss or damage incurred by any person as a result of the spill” and “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” [26(1)(a)(i)-(ii)].¹⁵

26. (1) Where any discharge, emission or escape of oil or gas that is authorized by regulation, or any spill, occurs in any area to which this Act applies,
- (a) the person who is required to obtain an authorization under paragraph 5(1)(b) in respect of the work or activity from which the spill or authorized discharge, emission or escape of oil or gas emanated is liable, without proof of fault or negligence, up to any prescribed limit of 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...

vii) Liability is absolute: no proof of fault or negligence required, no statutory defence

This liability does not require proof or fault of negligence by the party authorized for the work, making it a standard of absolute liability.¹⁶ While the *Fisheries Act* and *Marine Liability Act* offer narrow statutory defences to liability, as discussed below, there are no such defences available under COGOA or the offshore Accord acts.

viii) Examples of loss, damage and costs

It would be reasonable to state that “all actual loss or damage incurred by any person as a result of the spill” could include economic losses of people relying on fisheries, adversely affected tourism businesses, interrupted shipping or transportation routes, human health effects as a result of the spill, and any damage to property or loss of property value. However, it is unclear whether or not such loss or damage could be interpreted to include the consequences of ecological destruction.

The “costs and expenses reasonably incurred” by the government or others in taking action

¹⁴ 138(4)(a) for NFLD, 142(4)(a) for NS.

¹⁵ 162(1)(a)(i)-(ii) for NFLD, 167(1)(a)(i)-(ii) for NS. For these accord acts, liability includes costs incurred by either the federal government, the respective province, or any other person taking action to clean up the spill.

¹⁶ In the “Compensation Guidelines” adopted by the two Atlantic offshore boards, they define “absolute liability” as follows: “Absolute liability means that the person in whose name the work or activity has been authorized, is liable without proof of fault or negligence up to a specified limit for certain damages or expenses attributable to such work or activity.”

<http://www.cnsopb.ns.ca/pdfs/CompGuidelines.pdf> (foreword).

relating to the spill would include cleanup and spill mitigation costs, but may not be limited to that. The broad wording, “taking any action or measure in relation to the spill”, could reasonably include moving expenses or any other cost “reasonably incurred” as a result of the spill. It is also arguable that such costs and expenses could include long term environmental rehabilitation costs.

ix) Fault or negligence allow for unlimited, joint and several liability

It is important to note that the “prescribed limit of liability” in subsection 26(1)(a) only applies to the person authorized for the work, e.g. the oil company. Subsection 26(1)(b) also imposes unlimited liability on “all persons to whose fault or negligence the spill...is attributable or who are by law responsible for others to whose fault or negligence the spill...is attributable”. They are “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...” Joint and several liability allows the full amount to be recovered from any party whose fault or negligence is attributable to the spill, and then that party could in turn recover a share of the liability from any other parties whose fault or negligence also contributed to the spill.

26. (1) Where any discharge, emission or escape of oil or gas that is authorized by regulation, or any spill, occurs in any area to which this Act applies,

[...]

(b) 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 are 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.

x) Party authorized to do work not protected by liability cap if at fault or negligent

The “prescribed limits on liability” described in subsection 26(1)(a) do not apply to those whose fault or negligence contributed to the spill. Thus, while the party authorized for the work is normally protected by the limit prescribed under 26(1)(a), this limit would be removed if that party was at fault or negligent, or was “by law responsible” for another person who was at fault or negligent, as per 26(1)(b).

xi) No double liability: if liability is higher under other legislation, higher amount applies

Subsection 26(2.1)¹⁷ 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.

Accordingly, if there is higher liability to be found under other another law, then this higher

¹⁷ 162(2.1) for NFLD, 167(2.1) for NS.

amount would apply. However, liability cannot be found simultaneously under COGOA or the Accord acts as well as under another law.

It is important to note that there has been confusion about the applicability of this provision since at least 2001, when Boris de Jonge, an expert on Atlantic Canada's offshore petroleum regulation regime, identified a probable drafting error in this provision.¹⁸ De Jonge believes that subsection 26(2.1) ought to read "subsection (1)(a) or (2)(a)" as opposed to "subsection (1) or (2)". As it stands now, this provision would apply the prescribed limit on liability even to parties whose fault or negligence in relation to a spill can be demonstrated.

De Jonge notes, for example, that the original liability provisions in the Nova Scotia accord act, passed in 1988, were understood to impose unlimited liability given fault or negligence. This "no double liability" provision was introduced as an amendment in 1992, both to COGOA and to the accord acts, and its marginal heading—"no double liability"—clearly marks its purpose. Similarly, the Compensation Guidelines issued jointly by the Nova Scotia and Newfoundland and Labrador Offshore Boards state that amounts above the limit can be recovered in a court of law given proof of fault or negligence.

The abovementioned analysis clearly gives rise to the need for COGOA to be amended pursuant to the planned hearing into Arctic offshore safety and environmental requirements.

xii) Regulations under COGOA and the Atlantic Accord acts limit offshore liability to \$30 million, or \$40 million in Arctic waters

The limits of liability under COGOA are prescribed by the "*Oil and Gas Spills and Debris Liability Regulations*".¹⁹ The regulation limits liability to \$40M in arctic waters or lands adjacent to arctic waters – such waters being defined as those north of 60 degrees latitude. For subarctic offshore areas, the limit is \$30M. For areas within the Yukon and Northwest Territories that are less than 200 m from a lake or river, the limit is \$25M. For other areas on land in the Yukon and NWT, the limit is \$10M.

Under the Newfoundland & Labrador accord act, the regulation is titled *Canada-Newfoundland Oil and Gas Spills and Debris Liability Regulations*, SOR/88-262, which also limits liability to \$40M in Arctic waters or lands adjacent to Arctic waters. For subarctic offshore areas, the limit is \$30M.

For Nova Scotia, the regulation is titled *Canada-Nova Scotia Oil and Gas Spills and Debris Liability Regulations*, SOR/95-123, and, having no jurisdiction north of 60 degrees latitude, it limits liability to \$30 million for spills.

¹⁸ Boris B. de Jonge, "Financial Responsibility Requirements for Oil and Gas Activities Offshore Nova Scotia and Newfoundland" (Spring, 2001) 24 Dalhousie L.J. 109 at 113, note 11.

¹⁹ SOR/87-331. The Act to which this regulation refers is called the "*Oil and Gas Production and Conservation Act*", which is only available in print, not on CanLII, Quicklaw, nor Justice Canada's website. There is no reference to this act in COGOA either. The regulation refers to section "19.2" of that Act. Section 19.2 was amended by the *Canada Oil and Gas Act*, 1980-81 c. 81. That section is substantially the same as section 26 of COGOA. Counsel for the National Energy Board has stated that, for all intents and purposes, the regulation may be understood as applying to section 26 of COGOA, even though counsel was of the opinion that the regulation ought to be updated to refer to COGOA.

B) Compensation Guidelines

The Newfoundland & Labrador and Nova Scotia offshore Boards have adopted guidelines entitled “Compensation Guidelines Respecting Damages Relating to Offshore Petroleum Activity”.²⁰ As guidelines they are non-binding, but meant to ensure “flexibility and clarity” within the regulatory regime. The guidelines “describe the various compensation sources available to potential claimants for loss or damage related to petroleum activity offshore Nova Scotia and Newfoundland and Labrador” and “outline the regulatory and administrative roles which the Boards exercise respecting compensation payments for actual loss or damage directly attributable to offshore operators.”²¹

The guidelines identify practices regarding compensation from various sources, including: compensation directly from industry, through the Boards themselves, through court action, from the Canadian Association of Petroleum Producers Commercial Fisheries Compensation Program, and from Canada’s Ship source Oil Pollution Fund. These cover both “attributable damage”—i.e. where the source of the spill is known—and “non-attributable damage”—i.e. where the source of the spill is not known. The guidelines also set out policy and procedure in cases where compensation is sought directly from the Boards.

i) Boards may limit liability below the limit set out in regulations

The guidelines confirm that the Boards may limit liability to less than the prescribed maximum of \$30 million. It is important to note that, as a matter within the Board’s discretion, such decisions to limit liability further would not be subject to oversight by the provincial legislatures or Parliament. These guidelines affirm that, in cases of fault or negligence, liability may go beyond \$30 million.

The amount of the claim must be within the applicable limit. As a condition of conducting work or activity within the offshore area, the operator must provide the appropriate Board with financial security in order to deal with spill or debris related claims or classes of claims, up to a maximum amount of \$30 million. In the east coast offshore area operators are held liable without proof of fault or negligence up to such maximum amount. Notwithstanding this maximum aggregate amount, the Board reserves the right to limit the amount provided for each case or class of cases depending upon the number and scope of claims arising for any given incident. Beyond this allowable amount, the claimant must establish proof of fault or negligence through a court of law or through settlement with the particular person at fault.²²

C) Financial Responsibility Guidelines

i) Federal and Provincial Boards have discretion to require deposits/financial responsibility from operators

The Boards have discretionary powers to require deposits from companies, which could be

²⁰ <http://www.cnlopb.nl.ca/pdfs/guidelines/compgle.pdf>

²¹ *Ibid.* at 1.

²² *Ibid.* at 7-8.

applied to requirements for financial security to cover potential spill liabilities. This power exists pursuant to subsections 5(3) and (4) of COGOA, 138(3) and (4) of NL Accord Act, and 142(3) and (4) of NS Accord Act, all of which are identical:

Requirements for operating licence

(3) An operating licence shall be subject to such requirements as the National Energy Board determines or as may be prescribed and to such fees and deposits as are prescribed.

Requirements for authorization

(4) An authorization shall be subject to such approvals as the National Energy Board determines or as may be granted in accordance with the regulations and such requirements and deposits as the National Energy Board determines or as may be prescribed, including

- (a) requirements relating to liability for loss, damage, costs or expenses;
- (b) requirements for the carrying out of environmental programs or studies;

ii) No offshore oil regulations prescribe particular fees or deposits, though Atlantic Boards have issued "financial responsibility" guidelines

Despite these discretionary powers to enact regulations prescribing fees and deposits, no such regulations have been created aside from operator's license application fees of \$25.

The two Atlantic Boards have, however, issued joint guidelines regarding requirements for "Financial Responsibility".²³ The NEB has issued no such guidelines.

The Atlantic Boards' power to require proof of financial responsibility exists pursuant to subsections 163(1) of the NL Accord Act and 168(1) of the NS Accord Act. Subsection (1.1) requires that this financial responsibility endures for the duration of the project. Subsection (2) states that claims are to be paid out of those funds shown by the company as proof of financial responsibility.

Financial responsibility

163. (1) An applicant for an authorization under paragraph 138(1)(b) in respect of any work or activity in any portion of the offshore area shall 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 Board, in an amount satisfactory to the Board.

Continuing obligation

(1.1) The person who has obtained an authorization under paragraph 138(1)(b) shall ensure that the proof of financial responsibility remains in force for the duration of the work or activity in respect of which the authorization is issued.

Payment of claims

(2) The Board may require that moneys in an amount not exceeding the amount prescribed for any case or class of cases, or determined by the Board in the absence of regulations, be paid out of the funds available under the letter of credit, guarantee or indemnity bond or other form of financial responsibility provided pursuant to subsection (1), in respect of any claim for which proceedings may be

²³ See *Guidelines Respecting Financial Responsibility Requirements for Work or Activity in the Newfoundland And Nova Scotia Offshore Areas*, <http://www.cnsopb.ns.ca/pdfs/2031guidelines.pdf>

instituted under section 162, whether or not such proceedings have been instituted.

iii) Restoring and preserving the natural environment are among the objectives of the financial responsibility guidelines

The objectives of these financial requirement guidelines are defined in section 3:

- (a) providing financial compensation to any party respecting claims attributable to the work or activity. These would include without limitation, claims by third parties, the Crown or its agents, the Board including the Chief Conservation Officer and Board delegates. Eligible claims would include those relating to loss of or damage to property, financial loss, or injury/death;
- (b) restoring and preserving of the natural environment, including the sea bed, while the work or activity is going on and after it is completed and abandoned; and
- (c) ensuring that the operator will properly terminate the authorized work or activity, having regard to environmental, safety, and other concerns.

iv) Total requirements for “financial responsibility” are approximately \$500-600M

The Atlantic Boards’ guidelines for companies to demonstrate “financial responsibility” (or capacity to pay) may be distinguished into two types of requirements. The first requirement reaches up to \$100 million, and involves enforceable mechanisms to recover the funds. The second reaches up to \$450 million plus up to 25% of the reinstatement cost of the property, but can be met with “softer” evidence such as audited financial statements.

a) Claims relating to spills and debris, and costs incurred by government in terminating the well can require up to \$100 million

Section 5.4(a) of the guidelines states that an aggregate of \$100 million must be shown by the company to cover claims relating to spills, debris, and costs incurred by the government in properly terminating the well. Of this \$100 million, \$30 million must be readily available, with unfettered access by the Board when needed, and proven either through a letter of credit, indemnity bond, financial institution guarantee, or other means acceptable to the Board. The remaining \$70 million may be backed by a promissory note, insurance policy, or other enforceable means, but does not require the same immediate, unfettered access by the Board.

b) Atlantic Boards may require proof of up to \$450 million plus 25% of the reinstatement cost of the property for other financial liabilities, including well blowouts, pollution liability and third party liability

The guidelines also require a second category of evidence of financial responsibility so as to demonstrate the companies’ capacity to cover their prospective liabilities: see section 5.4(b). This evidence of sufficient available funds is in addition to the \$100 million noted above. This is to cover “any financial liability that may occur”, including well blowouts, pollution liability, removal of wrecks and debris, and third party liability.

For removal of debris, the limit is up to 25% of the reinstatement cost of the property; for third party liabilities the limit is up to \$200 million; and for well control, making wells safe, and pollution clean up, the limit is up to \$250 million. Financial evidence of these latter amounts can

be given in the form of audited financial statements, corporate guarantee by a third party, insurance, or another form acceptable to the Board.

vi) Amounts are not “deposits” and do not alter or limit the liabilities themselves; guidelines are non-binding and may be varied

It is important to note that none of the aforementioned “financial responsibility” provisions are actual deposits *per se*. They merely require companies to demonstrate adequate resources up to a certain minimum amount, in the *event* that they incur liabilities such as pollution claims, etc. Each of these guidelines may be varied on an *ad hoc* basis by the Boards since they do not constitute binding law.

vii) Existing “financial responsibility” requirements are insufficient to cover major liabilities

Given that the BP incident in the Gulf of Mexico is expected to incur tens of billions of dollars in liabilities, it is insufficient for the Atlantic Boards to require companies to demonstrate “financial responsibility” of only about \$500 million or less. These guidelines need a substantial adjustment to account for real-world liabilities. Otherwise, companies may be allowed to drill without having nearly enough resources to cover actual liabilities.

D) Fisheries Act

i) Prohibition on the destruction of fish habitat and depositing “deleterious substances” into waters frequented by fish

Sections 35 and 36 of the *Fisheries Act*²⁴ prohibit the destruction of fish habitat and the unauthorized deposit of any “deleterious substance” into waters frequented by fish. A “deleterious substance” is “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 so that it is rendered or is likely to be rendered deleterious to fish or fish habitat or to the use by man of fish that frequent that water.”²⁵

ii) All owners and persons in charge are jointly and severally liable for penalties and moneys recoverable under the Act

Section 80 provides that, unless specified otherwise, “every proprietor, owner, agent, tenant, occupier, partner or person actually in charge, either as occupant or servant” are jointly and severally liable for all penalties and moneys recoverable under the *Fisheries Act*. This joint and several liability would apply to the following criminal and civil liability provisions.

iii) Criminal penalties for deposit of deleterious substances

Destruction of fish habitat and the depositing of “deleterious substances” into waters frequented

²⁴ R.S., 1985, c. F-14.

²⁵ S. 34.

by fish are both classified as hybrid offences, granting the Crown the choice of whether to prosecute as summary or indictable offences. For a summary prosecution the maximum punishment is a fine of \$300,000, or 6 months imprisonment, or both. For an indictable prosecution the maximum punishment is a fine of \$1,000,000, or 3 years imprisonment, or both.²⁶ Moreover, unlike the civil liability provision further below, ships are not excluded from these criminal liability provisions.

Harmful alteration, etc., of fish habitat

35. (1) No person shall carry on any work or undertaking that results in the harmful alteration, disruption or destruction of fish habitat.

Deposit of deleterious substance prohibited

36. (3) Subject to subsection (4), no person shall deposit or permit the deposit of a deleterious substance of any type in water frequented by fish or in any place under any conditions where the deleterious substance or any other deleterious substance that results from the deposit of the deleterious substance may enter any such water.

iv) Criminal penalties open to due diligence defence

Criminal penalties, as opposed to the civil liability provisions under COGOA and the accord acts, are not absolute liability provisions and may not be imposed “without proof of fault or negligence”.

“Intent” to deposit a deleterious substance is not required, as per subsection 40(5)(a). However, the accused can defend the charge by making out a “due diligence” defence on a balance of probabilities.²⁷ In other words, if the accused is found to have taken all reasonable steps to avoid committing the offence, there will be no conviction.

The accused may also defend the charge if it can be proven that, at all material times, the waters in question were not frequented by fish.²⁸

v) Civil liability for deposit of deleterious substance is unlimited for costs or expenses re: cleanup and economic compensation for fishermen

Subsection 42(7) exempts ships from the preceding civil liability provision, since they are covered by the *Canada Shipping Act, 2001* (see discussion below). However, offshore oil and gas drilling operations are not exempted and may fall within the *Fisheries Act* civil liability regime if a blow-out or spill were to occur.

The Act imposes civil liability on any party who deposits a deleterious substance into waters frequented by fish, recoverable by the federal or provincial governments for required cleanup or mitigation activities. Subsection 42(3) also imposes civil liability in regard to fishermen for loss of income: those responsible for depositing a deleterious substance are “jointly and severally liable for all loss of income incurred by any licensed commercial fisherman, to the extent that the loss can be established to have been incurred as a result of the deposit or of a prohibition to fish resulting therefrom...”

²⁶ Subsections 40(1) and (2), regarding contraventions of subsections 35(1) and 36(1) and (3).

²⁷ http://www-heb.pac.dfo-mpo.gc.ca/habitat_policy/enforcing_the_act_e.htm

²⁸ Subsection 40(5)(b)

Civil liability to Her Majesty

42. (1) Where there occurs a deposit of a deleterious substance in water frequented by fish that is not authorized under section 36 or a serious and imminent danger thereof by reason of any condition, the persons who at any material time

(a) own the deleterious substance or have the charge, management or control thereof, or

(b) are persons other than those described in paragraph (a) who cause or contribute to the causation of the deposit or danger thereof,

are, subject to subsection (4) in the case of the persons referred to in paragraph (a) and to the extent determined according to their respective degrees of fault or negligence in the case of the persons referred to in paragraph (b), jointly and severally liable for all costs and expenses incurred by Her Majesty in right of Canada or a province, to the extent that those costs and expenses can be established to have been reasonably incurred in the circumstances, of and incidental to the taking of any measures to prevent any such deposit or condition or to counteract, mitigate or remedy any adverse effects that result or may reasonably be expected to result therefrom.

vi) Further statutory defences to civil liability are limited

The *Fisheries Act* offers a narrow defence to civil liability in rare cases such as war, natural phenomena of an “exceptional, inevitable and irresistible character”, and third party intent to cause damage. This is not the same as a “due diligence” defence. Subject to one of the listed cases, liability is absolute.

Defences to liability

42. (4) The liability of any person described in paragraph (1)(a) is absolute and does not depend on proof of fault or negligence but no such person is liable for any costs and expenses pursuant to subsection (1) or loss of income pursuant to subsection (3) if he establishes that the occurrence giving rise to the liability was wholly caused by

(a) an act of war, hostilities, civil war, insurrection or a natural phenomenon of an exceptional, inevitable and irresistible character; or

(b) an act or omission with intent to cause damage by a person other than a person for whose wrongful act or omission he is by law responsible.

vii) Civil liability under Fisheries Act can be higher than caps set under COGOA and Accord Acts

Due to the “no double liability” provision in COGOA and the Accord Acts, if the liability for spill cleanup, mitigation, and fishermen compensation under the *Fisheries Act* is greater than the limit prescribed under the three offshore petroleum acts, then this greater amount under the *Fisheries Act* would apply. Civil liability under the *Fisheries Act* is not limited.

E) Marine Liability Act

The *Marine Liability Act* implements several international conventions, in whole or in part, which relate to marine liability.²⁹ Section 77 of the *MLA* says that the owner of a ship is liable for oil

²⁹ These include the *Convention on Limitation of Liability for Maritime Claims, 1976*, the *International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001*, the *International Convention on Civil Liability for Oil Pollution Damage, 1992*, and the

pollution damage from the ship, the costs and expenses incurred by the government or any other party in cleaning up the spill, and for the costs of “reasonable measures of reinstatement” of the environment, if there is environmental damage.

i) Maximum liability for ships of less than 300 tonnes is \$500,000 CDN

This liability does not require proof of fault or negligence, but is subject to narrow statutory defences. These include: if the spill resulted from war or natural phenomena of an exceptional nature, if the spill was wholly caused by a third party’s act or omission with intent to cause damage, or if it was wholly caused by the negligence of an authority responsible for maintaining lights or navigational aids. The limit on liability for ships of less than 300 gross tonnage, for cases other than loss of life or personal injury, is \$500,000 CDN.³⁰

ii) For larger ships, maximum liability from oil pollution ranges from \$6,650,000 US to \$132,400,000 US depending on weight; limit is removed in rare cases

For larger ships, Canada has adopted the *International Convention on Civil Liability for Oil Pollution Damage, 1992*,³¹ which limits liability according to the weight of the ship. For ships of less than 5,000 units of tonnage, the maximum liability is 4,510,000 “units of account”, which is approximately \$6,650,000 USD.³² For larger ships, each unit of tonnage increases liability proportionately, to an absolute maximum of 89,770,000 units of account, or approximately \$132,400,000 USD.

The limit is removed only in rare cases where the owner or operator had intent to cause damage, or was reckless and had the knowledge that such damage was likely.

1. The owner of a ship shall be entitled to limit his liability under this Convention in respect of any one incident to an aggregate amount calculated as follows:

- (a) 4,510,000 units of account for a ship not exceeding 5,000 units of tonnage;
- (b) for a ship with a tonnage in excess thereof, for each additional unit of tonnage, 631 units of account in addition to the amount mentioned in subparagraph (a);

provided, however, that this aggregate amount shall not in any event exceed 89,770,000 units of account.

2. The owner shall not be entitled to limit his liability under this Convention if it is proved that the pollution damage resulted from his personal act or omission, committed with the intent to cause such damage, or recklessly and with knowledge that such damage would probably result.³³

F) Canada Shipping Act, 2001

International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992.

³⁰ Section 29.

³¹ See section 48 and Schedule 5 of the *Marine Liability Act*.

³² Units of Account refer to the Special Drawing Right of the International Monetary Fund. See http://www.imf.org/external/np/fin/data/rms_sdrv.aspx

³³ Article V of the *International Convention on Civil Liability for Oil Pollution Damage, 1992*. See also Article III for other parties who can be held liable, given intent or recklessness.

For those ships *not* on location at an oil drilling, processing or conservation operation (e.g. not docked at an oil rig) the *Canada Shipping Act, 2001* would apply. Parts 8 and 9 of this act apply to such ships, and part 8 also applies to an “oil handling facility”, which is a facility that loads oil onto or from ships, such as an oil terminal.

i) No additional liability for spills or limits on liability

Parts 8 and 9 impose various requirements for pollution prevention plans, emergency plans, required arrangements with response organizations in the event of oil pollution, define the powers of a pollution response officer, provisions for pollution response incidents, and other related provisions. However, there are no new provisions imposing or limiting spills liability in this Act.

ii) Liability for expenses relating to detention

The only relevant provision regarding liability relates to expenses incurred in detention of a vessel in breach of the Act.³⁴

iii) Federal government to compensate for services rendered pursuant to ministerial order

Regarding pollution response measures, compensation is to be paid for the services of any party (aside from the party responsible for a spill) who follows a direction (under 180(1)(c)) by the Minister of Fisheries and Oceans:

180. (3) “Compensation shall be paid by Her Majesty in right of Canada for the services of any vessel or person, other than a vessel or the operator of an oil handling facility that had discharged, was discharging or was likely to discharge a pollutant, that has complied with a direction issued under paragraph (1)(c).”

Subsection 181(1) says that anyone taking action pursuant to such a direction is not to be held criminally or civilly liable.

Subsection 181(3) states that: “Nothing in subsection (1) exempts or lessens the liability of the owner of a vessel for the occurrence that necessitated the response operation.”

Conclusions:

For offshore oil and gas operations, *COGOA* provides that “any costs incurred” in managing a spill are payable to the federal government. This is, however, subject to other sections that allow for limitations to be placed on such liability. Regulations under *COGOA* and the Accord acts place limits of \$30 million in subarctic waters, and \$40 million in arctic waters. The NEB and Atlantic offshore boards also have discretion to reduce liability further below this limit. Any decisions made by the Boards in this respect would not be subject to any oversight. Proof of

³⁴ Subsection 177(9), “Liability for Expenses”, states, “The authorized representative or, if there is no authorized representative, the owner of a vessel that is detained under this section is liable for all expenses incurred in respect of the detained vessel.”

fault or negligence, however, makes parties jointly and severally liable to an unlimited amount.

COGOA and the accord acts provide for “no double liability” under additional statutes, but do allow for higher liability to be found elsewhere. It is therefore possible that higher amounts of liability could be found under the *Fisheries Act*. The civil liability provisions under the *Fisheries Act* are not subject to any limitations. They are, however, subject to limited defences, which would not be available under COGOA or the accord acts, and apply only to fish habitat and “waters frequented by fish”.

The two Atlantic Offshore Boards have issued guidelines requiring companies to demonstrate resources sufficient to cover potential liabilities. However, given the magnitude of costs and liabilities now facing BP, these “financial responsibility” guidelines require relatively modest resources, and need to be substantially increased to ensure that similar liabilities do not go unpaid in Canada.

For ships, the liability regime is different, governed by the *Marine Liability Act*. Ships under 300 tonnes have a liability limit of \$500,000 CDN for spills damage, and larger ships of up to 5,000 tonnes have a liability limit of around \$6,650,000 USD. Ships above 5,000 have their liability limits increased proportionately with each additional tonne, up to an absolute maximum of around \$132,400,000 USD.

With Canada’s National Energy Board about to commence a policy review of Arctic offshore drilling, we cannot wait any longer for a more comprehensive re-examination of Canada’s offshore petroleum regulatory regime, with particular attention to the issue of spills liability. U.S. developments on this front are ongoing: a U.S. senate committee recently voted in favour of the removal of such liability caps altogether. Canada needs to follow suit. If companies are not prepared to accept the full costs arising from such high-risk activities as offshore oil drilling, they should not be in this business in the first place.

APPENDIX: Applicable Law

Canada Oil and Gas Operations Act, R.S.C. 1985, c. O-7

Operating Licences and Authorization for Work

5. (4) An authorization shall be subject to such approvals as the National Energy Board determines or as may be granted in accordance with the regulations and such requirements and deposits CHECK FOR THESE as the National Energy Board determines or as may be prescribed, including

(a) requirements relating to liability for loss, damage, costs or expenses;

Spills and Debris

Definition of "spill"

24. (1) In sections 25 to 28, "spill" means 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 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.

25.

...

Duty to take reasonable measures

(3) Every person required to report a spill under subsection (2) shall, as soon as possible, take 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.

Taking emergency action

(4) Where the Chief Conservation Officer, on reasonable grounds, is satisfied that

- (a) a spill has occurred in any area to which this Act applies and immediate action is necessary in order to effect any reasonable measures referred to in subsection (3), and
- (b) such action is not being taken or will not be taken under subsection (3),

he may take such action or direct that it be taken by such persons as may be necessary.

Taking over management

(5) For the purposes of subsection (4), 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.

Managing work or activity

(6) A person authorized and directed to take over the management and control of any work or activity under subsection (5) shall manage and control that work or activity and take all reasonable measures in relation to the spill that are referred to in subsection (3).

Costs

(7) Any costs incurred under subsection (6) shall be borne by the person who obtained an authorization under paragraph 5(1)(b) in respect of the work or activity from which the spill emanated and until paid constitute a debt recoverable by action in any court of competent jurisdiction as a debt due to Her Majesty in right of Canada.

Recovery of costs

(7.1) Where a person, other than a person referred to in subsection (7), takes action pursuant to subsection (3) or (4), the person may recover from Her Majesty in right of Canada the costs and expenses reasonably incurred by that person in taking the action.

Recovery of loss, damage, costs or expenses

26. (1) Where any discharge, emission or escape of oil or gas that is authorized by regulation, or any spill, occurs in any area to which this Act applies,

(a) the person who is required to obtain an authorization under paragraph 5(1)(b) in respect of the work or activity from which the spill or authorized discharge, emission or escape of oil or gas emanated is liable, without proof of fault or negligence, up to any prescribed limit of 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;
and

(b) 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 are 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.

...

No double liability

(2.1) 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.

Oil and Gas Spills and Debris Liability Regulations, SOR/87-331

CANADA OIL AND GAS OPERATIONS ACT

REGULATIONS RESPECTING LIMITS OF LIABILITY FOR SPILLS, AUTHORIZED DISCHARGES AND DEBRIS EMANATING OR ORIGINATING FROM WORK OR ACTIVITY RELATED TO THE EXPLORATION FOR OR PRODUCTION OF OIL AND GAS

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SHORT TITLE

1. These Regulations may be cited as the *Oil and Gas Spills and Debris Liability Regulations*.

INTERPRETATION

2. In these Regulations, "Act" means the *Oil and Gas Production and Conservation Act*. (Loi)

LIMITS OF LIABILITY

3. For the purposes of section 19.2 of the Act, the limits of liability are
- (a) in respect of any area of land or submarine area referred to in paragraph 6(1)(a) of the *Arctic Waters Pollution Prevention Act*, the amount by which 40 million dollars exceeds the amount prescribed pursuant to section 9 of that Act in respect of any activity or undertaking engaged in or carried on by any person or persons described in paragraph 6(1)(a) of that Act;
 - (b) in respect of any submarine area lying north of the sixtieth parallel of north latitude and to which paragraph (a) does not apply, the amount of 40 million dollars;
 - (c) in respect of any area within the Yukon Territory or Northwest Territories covered by or located a distance of 200 metres or less from any river, stream, lake or other body of inland water and to which paragraph (a) does not apply, the amount of twenty-five million dollars;
 - (d) in respect of any area within the Yukon Territory or Northwest Territories to which neither paragraph (a) nor (c) applies, the amount of 10 million dollars; and
 - (e) in respect of any area to which the Act applies and for which no other limit is prescribed by these Regulations, the amount of 30 million dollars.

Arctic Waters Pollution Prevention Regulations, C.R.C., c. 354

Limits of Liability

8. For the purposes of section 6 of the Act, the maximum amount of liability of an operator in respect of each deposit of waste is as follows:

...

(f) in the case of an operation engaged in exploring for, developing or exploiting oil and gas, \$40 million³⁵

³⁵ This regulation refers to the *Arctic Waters Pollution Prevention Act*. The complicated calculation referred to in subsection 3(a) of the previous regulation is therefore rendered moot, as both regs effectively set a \$40 million limit on liability for oil spills.