

Compensation and prevention of damage resulting from offshore drilling in China

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Impact Statement

For such a socially relevant matter as compensation and prevention arising from oil pollution, it is of great significance to reflect upon the (potential) impact that this study may have on a social or economic level. The following paragraphs briefly outline how this research contributes to this process.

Research findings

In the past four decades that China has devoted to its offshore oil exploration and production, a model of joint development between the China National Offshore Oil Corporation (CNOOC) and foreign operators has been used. Drilling for oil offshore is a challenging task with multiple hazards, as oil spills from daily operations and offshore accidents endanger the marine ecosystem of nearby waters. In addition to traditional damage (i.e., personal injury and property damage) via the environment, tort liabilities resulting from marine ecological damage require special attention due to its particular features. The *Bohai Bay Oil Spill* in 2011 demonstrated that China was in urgent need of dealing with this issue in practice.

Against this background, the questions of how victims are eventually compensated and how potential polluters are incentivised to prevention become relevant and important. Accordingly, the research question in this thesis is: does China have a legal system in place to remedy the damage arising from offshore drilling, providing adequate compensation and incentives for prevention to risk creators?

The answers to the question are a mixed blessing. Currently (2022), there are applicable rules in China regarding the compensation and prevention of offshore oil damage, which involve major matters of the offshore oil business, liability attribution, tort damages, claims process, financial security, and safety regulation. Hence, China has a legal framework on paper that governs offshore oil damage and there is also a set of procedural methods and rules to implement the remedy as well. From a law and economics perspective, the existing system has advantages in handling offshore oil damage. In general, the strict liability system with no financial caps in China, leaving aside the insolvency issue, is theoretically favourable to tackle offshore oil damage.

Moreover, victims with personal injury or economic loss are granted to pursue compensation awards, while marine administrative organs, legally mandated NGOs and procuratorates are entitled to require ecological restoration. In addition, offshore oil companies can voluntarily purchase financial tools or count on self-insurance. Finally, a set of safety standards and a specific internal compliance mechanism within the companies are also formulated to regulate and monitor offshore oil operations. Meanwhile, the study critically analysed the strengths and weaknesses of the applicable rules based on economic theory. It provides China with a fresh insight into the evaluation of the existing legal system. The study of the compensation mechanism of offshore drilling reflected that the legislation and the implementation of laws are prompted with Chinese characteristics. Some issues deviate from the economic theory, creating an insolvency risk associated with under-compensation and under-deterrence: (i) the liability is exclusively channelled to operators, while the joint developer CNOOC bears no liability; (ii) there is no mandatory financial security to offshore oil companies; and (iii) the current claims procedure relies heavily on the public administration and is thus not independent enough compared with other types of oil spill settlement solutions, such as the ADR mechanism or the judicial system.

Social relevance

After the major incident with the *Deepwater Horizon* in the Gulf of Mexico, western legislators and legal scholars have shown great interest in the compensation mechanism for offshore oil pollution, but mainly from the perspectives of the US and the EU. In China, although the exploration and production of oil in the offshore industry grow rapidly, and this leads to significant potential risks, legislators and scholars rarely concentrate on the legal remedies for offshore oil damage.

When it comes to marine oil pollution, most literature pays attention to vessel-induced damage. Moreover, legislators have formulated several regulations aiming at vessel-source pollution in recent years, and these specific legal documents have entered into force. The rules related to offshore-related damage are scattered in dozens of legal documents, while quite a few relevant provisions are either unclear or unspecific.

Although the *Bohai Bay Oil Spill* in 2011 triggered a heated discussion about compensation for oil spill related damage, the focus was on the accident response

rather than digging into the legal arrangement of this particular type of damage. In academia, there has so far not been any comprehensive study on how China legally remedies the damage arising from offshore drilling. This study, therefore, is formulated to fill in the blank spots on this research map.

Target audience and proposals

As China becomes a major country in the offshore oil business and this simultaneously brings tremendous risks, the legal system that governs this environmentally sensitive industrial sector and the way it is implemented in practice deserve special attention. After all, studying the applicable rules is not merely a necessity for China to prepare for the hazards *ex ante* and to tackle them *ex post*; moreover, offshore oil operators worldwide need clear and specific legal guidance for their business activities in Chinese waters. Moreover, people closely related to offshore oil activities (i.e., offshore oil operators, potential victims of offshore oil risks, fishermen en tourism providers, environmental NGOs, etc.) will find useful legal guidance in this book.

Regarding the proposals to the government, although we have offered three pieces of advice based on the limitations of the current system, it is not an easy task to implement these particular policy recommendations in the context of China. We need to come down to earth when modifying the current legal regime; we also need to tailor each suggestion according to actual circumstances. After all, whether and when these policy recommendations will be introduced or not largely depends on political necessity. Despite all kinds of problems discussed above, the existing system in China can largely deal with the compensation associated with oil spills. The fact that the public administration has a powerful impact on nearly every aspect of offshore drilling seems to be continued in the near future. However, from an economic perspective, we could prefer and suggest a more structured and systematic solution in line with the policy recommendations mentioned above.