WRECK REMOVAL IN THE 21ST CENTURY

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Removal of wreck and debris ("ROW/D") has always been a "big ticket" item in marine insurance. The hurricanes of 2005 in the Gulf of Mexico brought this home with a vengeance, and introduced a host of legal issues that previously lain just below the surface, like the wreck of a sunken vessel. This paper will discuss the basic issues of owner liability and coverage under standard marine policies for ROW/D, and touch on some of the new issues that floated to the surface in the last couple of years.

I. Vessel owner's liability for wreck removal

A. Liability under the Wreck Act

The principal basis for liability for ROW/D is under the Wreck Act. This statute requires the owner of a sunken vessel sunk to mark and remove it. By its terms, the statute only applies to "navigable channels," "waters, in respect of which the United States has jurisdiction," and "any river, lake, harbor, sound, bay, canal, or other navigable waters of the United States." Thus, this statute would appear to be limited to territorial waters of the United States, which only extend 12 miles from shore.

With respect to offshore oil operations, the extent of jurisdiction is extended. The Outer Continental Shelf Lands Act ("OCSLA")provides that the Wreck Act applies to "artificial islands, installations, and other devices" described in OCSLA. These devices include mobile offshore drilling units ("MODUs") while attached to the seabed, but would not include service vessels. Accordingly, a MODU that sinks while attached to the seabed would be subject to the Wreck Act.

The courts have held that the Wreck Act only applies when a sunken vessel is a hazard to navigation. The regulations promulgated by the Coast Guard and Corps of Engineers specify that the following factors be considered in making this determination:

(1) Location of the obstruction in relation to the navigable channel and other navigational traffic patterns.

(2) Navigational difficulty in the vicinity of the obstruction.

(3) Clearance or depth of water over the obstruction, fluctuation of water level, and other hydraulic characteristics in the vicinity.

(4) Type and density of commercial and recreational vessel traffic, or other marine activity, in the vicinity of the obstruction.

(5) Physical characteristics of the obstruction, including cargo, if any.

(6) Possible movement of the obstruction.

(7) Location of the obstruction in relation to existing aids to navigation.

(8) Prevailing and historical weather conditions.

(9) Length of time the obstruction has been in existence.

(10) History of vessel accidents involving the obstruction.

33 C.F.R. § 245.20.

At one time, the non-negligent owner of a sunken vessel could avoid personal liability for wreck removal by abandoning the vessel to the United States government. In 1986, however, the Wreck Act was amended, and this protection was taken away.

B. Potential liability under tort theories

The owner of a sunken vessel may also face potential liability under tort theories. For example, if the owner of a vessel is negligent and the ship sinks in such a way as to cause damage to a third party, such as by blocking access to an offshore platform, the owner could be liable for the costs of removal.

It is less clear whether a non-negligent vessel owner whose vessel sinks can be held liable to third parties. In *Continental Oil Co. v. Bonanza Corp.*, 677 F.2d 455 (5th Cir. 1982), *reversed,* 706 F.2d 1365 (5th Cir. 1983) (en banc) ("the *AQUA SAFARI*"), the court held that a non-negligent time charterer did not face liability for the cost of wreck removal.

C. Potential liability under Minerals Management Service regulations

For companies conducting oil and gas operations on the Outer Continental Shelf, there is also potential liability under the regulations promulgated by the Minerals Management Service ("MMS"). These regulations require the owners of mineral leases to remove obstructions and facilities within one year after the termination of the lease. There is also potential liability for a contractor that performs the act of installing a facility or creating an obstruction. For example, a contractor that built an offshore platform might be liable along with the lessee to remove the platform at the termination of the lease.

These regulations only apply to devices that are attached to the seabed, and thus do not apply to traditional vessels. It is also not at all clear whether these regulations apply to MODUs.

II. Coverage for ROW/D

A. Coverage under traditional marine P&I policies

Coverage for removal of wreck is traditionally covered under P&I policies. The typical P&I policy will provide coverage for the cost of removing the insured vessel "when removal is compulsory by law." This has been the subject of much litigation.

The term "compulsory by law" initially came before the courts in *Seaboard Shipping Corp. v. Jocharanne Tugboat Corp.*, 461 F.2d 500 (2d Cir. 1972). There, a barge loaded with gasoline went aground in Lake Ontario, and began leaking gasoline into the water and onto the adjacent shoreline. Operations were undertaken to offload the gasoline and refloat the barge.

The barge was then towed to New York City, where it was declared a constructive total loss. The hull underwriters, having paid the costs associated with these operations, sued the P&I insurer, claiming that pressure from the Coast Guard and the local authorities made removal "compulsory by law." The court rejected this argument, stating that

> "compulsory removal" is a term of art in admiralty law and refers to a situation in which a hull has been abandoned by the owner and the hull underwriter but, pursuant to government order, must be removed from navigable waters.

Id. at 504. Based on this language, for about a decade, the common understanding was that removal was only "compulsory by law" when the government had ordered removal.

The extent of coverage for wreck removal was greatly expanded in *Progress Marine, Inc. v. Foremost Ins. Co.*, 642 F.2d 816 (5th Cir. 1981). There, a jackup workover rig capsized and sank while under tow as the result of negligence on the part of the rig's tool pusher and barge captain. The rig came to rest in 56 feet of water only eight feet below the surface. The rig was about 1500 feet from a manned platform, and 300 feet from a high pressure pipeline. The Coast Guard notified the owner that it was a hazard to navigation and instructed the owner to mark the wreck, but the Corps of Engineers did not order removal. The assured proceeded to remove the wreck, but its P&I insurer denied coverage on the theory that under *Seaboard Shipping Corp. v. Jocharanne Tugboat Corp,* removal was not "compulsory by law" because removal had not been ordered by the government.

The court held that removal was "compulsory by law," rejecting the argument that this requirement could only be met if the government ordered removal. According to the court, removal could also be "compulsory by law" "where failure to remove would have reasonable [sic] exposed an insured to liability imposed by law sufficiently great to justify the expense of removal." As possible sources of such liability, the court cited the possibility of another vessel

colliding with the wreck or the wreck rupturing a pipeline, presumably on the theory that the wreck could have moved and struck the pipeline some 300 feet away. The court then added that in order for removal to be "compulsory by law," removal must not only be objectively necessary, but the assured's action in removing the wreck must be subjectively motivated by the belief that removal was necessary to avoid legal consequences. The court then remanded the case to the district court to determine whether the newly announced standards for determining whether removal was "compulsory" had been met.

The notion that civil liability as well as a governmental order could serve as a basis for coverage was significantly refined in *Continental Oil Co. v. Bonanza Corp.*, 677 F.2d 455 (5th Cir. 1982), *reversed,* 706 F.2d 1365 (5th Cir. 1983) (en banc) ("the *AQUA SAFARI*"). There, Conoco hired Bonanza to provide the M/V AQUA SAFARI to support its drilling operations on the OCS. Conoco was named as an additional assured on Bonanza's P&I policy. As a result of negligence on the part of Bonanza, the AQUA SAFARI sank underneath the jack-up rig that was conducting the drilling operations and next to the well. Conoco removed the wreck, and sought coverage under the P&I policy, claiming that removal was "compulsory by law."

Initially, the Fifth Circuit held that removal was "compulsory by law." 677 F. 455. With respect to the objective prong of the test announced in *Progress Marine*, the court held that a balancing test should be applied, whereby the likelihood that the wreck could cause damage, the likelihood that the assured would be found liable for the damage, and the magnitude of the potential damage were factored together and then weighed against the cost of removal. *Id.* at 463. The court then proceeded to apply this balancing test. With respect to whether the wreck could have caused damage, the court stated that "the likelihood that a storm would drive the Aqua Safari onto a nearby pipeline is difficult to estimate, but it is virtually certain that storms

will sweep the Gulf," and that "Conoco could not count on the Aqua Safari to remain in the mud." *Id.* With respect to the likelihood that Conoco would be held liable if this happened, the court stated that "liability was not certain, but it was a significant possibility," particularly "in the light of expanding concepts of enterprise and vicarious liability." *Id.* at 462, 463. According to the court, "Conoco could [not] have stood idly by and awaited an oil pipeline to burst with the cool certainty that Bonanza, not it, would pay." *Id.* Since the "potential damages were incalculable," and the cost of removal relatively insignificant, the court held that the objective prong of *Progress Marine* had been met. *Id.* The court also held that fear of legal consequences need not be the only motivation to meet the subjective prong of the *Progress Marine* test.

One of the judges registered a blistering dissent, and on our petition the entire Fifth Circuit decided to rehear the case en banc. On rehearing, the court reversed the panel decision, and held that removal was not compulsory by law.

First, the court refined the *Progress Marine* test by eliminating the subjective element of the test. The court then stated the new test as follows:

> To be compelling, the duty must be clear and the sanctions for its violation both established and sufficiently severe to be impelling, that is to warrant the cost of removal. But removal occasioned by a reasonable apprehension of slight consequences for inaction or by an unreasonable apprehension even of grave consequences is not compelled.

706 F.2d at 1370.

The court then proceeded to address the questions of whether Conoco faced potential legal liability and whether the wreck was likely to cause damage. With regard to Conoco's potential liability, the court noted that there was no evidence that Conoco had been negligent. The court then addressed the possibility that Conoco might have been found liable based upon "expanding concepts" of liability, and held that "[i]n the absence of established legal obligation

to third parties, Conoco was not reasonably exposed to liability justifying the expense of removal." *Id.* at 1373. To meet this standard, there must be "a clear legal obligation to remove, imposed by statute or by judicial decision." *Id.* at 1377. The court also addressed the potential that the wreck would cause damage, and pointed out that the wreck was half-covered with mud, and was some 2000 feet from the property owned by third parties, and that the possibility was slight that it could be transported across the lease, or that it would be a hazard to vessels navigating the surface as it lay on the seabed.

Conoco also argued that it faced legal exposure under its lease obligations to the federal government. The court rejected the notion that these obligations could trigger the sort of legal obligation necessary to make removal "compulsory by law":

> The regulations impose no present duty to remove the wreck . . . but only the duty to remove property "upon termination of the lease, an event that would not occur until Conoco either violated the lease or mineral production ceased . . . Thus, Conoco's duty would not arise for many years.

Id. at 1371. The court also pointed out that Conoco might have been allowed to leave the wreck in place even after the lease terminated, and that the lease could be construed to apply only to property that Conoco intentionally placed on the lease and not to property of third persons that accidentally ended up on the lease. In any event, "Conoco made no effort even to ascertain whether removal would be required [and] [i]t had a duty to do that in order to minimize its expense before seeking to tax the insurer." *Id.* at 1372 n. 9.

The final chapter in the book on the meaning of "compulsory by law" is *Grupo Protexa, S.A. v. All American Marine Slip*, 753 F.Supp. 1217 (D.N.J. 1990), *reversed,* 954 F.2d 130 (3d Cir. 1992), *on remand,* 1993 WL 166275 (D.N.J. May 12, 1993), *affirmed* 20 F.3d. 1224 (3d Cir. 1994). There, Protexa's diving support vessel sank 45 miles off the coast of Mexico in 150 of water. The Mexican government issued a wreck removal order, and Protexa proceeded to

remove the wreck. The sinking had resulted in the deaths of 33 crewmen, and the assured was under immense pressure to remove the wreck from Mexico's most powerful union that wanted its members' bodies recovered for burial. Protexa was also under immense pressure to remove the wreck from Pemex, who insisted that the vessel be removed from the oil field where Pemex was operating.

The P&I insurers denied coverage on the basis that the Mexican wreck removal statutes did not authorize the Mexican government to order wreck removal outside of Mexican territorial waters, and that removal was thus not "compulsory by law." The assured argued that removal was compulsory anytime the government ordered removal, without regard to whether the order was technically valid or not. The district court rejected both of these arguments, and instead held that the balancing test announced in *Progress Marine* and refined in the *AQUA SAFARI* applied even when a wreck removal order has been issued. Thus,

> the determination of whether removal of a vessel was "compulsory by law" must be decided by looking to the state of affairs as they would appear to a reasonable owner under the circumstances and examining whether failure to remove a wreck would likely expose such owner to liability imposed by law sufficiently great in amount and probability of occurrence to justify the expense of removal.

753 F.Supp. at 1230.

In light of the district judge's ruling that the validity of the order was but a factor in determining whether removal was "compulsory by law," trial of the case focused on the reasonableness of Protexa's decision to remove the wreck. Without determining whether the order was valid or not, the district judge found that the maximum fines for disobeying the order would have been at most $50,000, and that this did not justify incurring the millions of dollars expended to remove the wreck.

On appeal, the Third Circuit reversed in an opinion by Hon. Samuel Alito, recently confirmed as an associate justice of the United States Supreme Court. 954 F.2d 130 (3d Cir. 1992) (“*Grupo Protexa I*”). The court held that the balancing test devised by the Fifth Circuit and applied by the district court only applied when the assured claimed that removal was “compulsory by law” based upon potential civil or criminal exposure, and not in the case of a governmental order to remove the wreck. When removal is ordered by the government, on the other hand, the test initially fashioned by the Second Circuit in *Seaboard Shipping* is applicable. The court stated the test as follows:

> We interpret the in banc opinion in *Continental Oil*, like the earlier opinion in *Progress Marine*, to impose a two-part test under which removal is considered compulsory by law if either 1) the removal is directed by governmental order, statute or regulation or 2) if removal is reasonable under a cost-benefit analysis taking into consideration the probable cost of removal and both the likelihood and amount of liability which could be imposed for failing to remove the wreck.

Id. at 137-138.

While rejecting the applicability of the *AQUA SAFARI* balancing test when a wreck removal order had in fact been issued, the court accepted the argument that removal would not be compulsory if the order was invalid; “[u]nder the correct interpretation of the phrase ‘compulsory by law,’ the . . . validity of the Port Captain’s order [is a] critical factor.” *Id.* at 138. Accordingly, the court remanded the case for retrial to determine whether the order was valid. The district court held that the Mexican statutes only applied in territorial waters, and that removal was not compulsory, and the Third Circuit affirmed. 20 F.3d 1224 (3d Cir. 1994) (“*Grupo Protexa II*”).

From these cases it is possible to draw the following conclusions about the extent of coverage under traditional P&I policies:

(1) Removal will be "compulsory by law" when there is an applicable statute or valid order requiring removal. For example, when a vessel sinks in territorial waters and is a hazard to navigation, the owner is liable to remove the vessel under the Wreck Act without the need for any order, and removal is thus "compulsory by law."

(2) Removal will be "compulsory by law" when the owner faces liability in tort and the likelihood of liability and the potential consequences are sufficient to outweigh the cost of removal. For example, if a vessel sinks outside of territorial waters, but the wreck is sufficiently close to the surface that traffic in the area could strike the wreck, and there is some reason to believe that the owner faces responsibility for the sinking, the cost of removal will probably be covered.

(3) Removal is not compulsory when there is an invalid order, the statute does not apply, or the concerns about civil liability are not reasonable.

B. Coverage under "broad form" ROW/D clauses

Particularly in the offshore oil industry, it is typical to expand the coverage for ROW/D beyond situations when removal is "compulsory by law." A typical Energy Package ROW/D clause for an offshore drilling contractor might provide that ROW/D is covered "when removal is compulsory by law, statute or regulation, when required by contract, or when necessary for the Assured's/Operator's operations." This would provide coverage in an number of situations beyond those covered under a standard P&I policy.

Most drilling contracts at least to some extent require the contractor to remove the debris of the rig. Thus, if the rig sinks on location and the contractor is required to remove it under the drilling contract, the contractor would have coverage for removal as "required by contract." The

broad form coverage would also provide coverage when removal was necessary to continue operations at the site.

It is typical in the offshore industry for ROW/D coverage to be carried under the Physical Damage section of the policy, and coverage is usually limited to 25% of the insured value (which may or may not include Increased Value values).

C. Coverage for ROW/D under excess liability policies: square pegs in round holes

As noted above, it is typical to limit ROW/D coverage under Energy Package policies to 25% of insured value. The hurricanes of 2005 revealed that this amount is almost invariably insufficient to pay for the cost of removal, even if the asset is adequately insured. The combination of inadequate ROW/D coverage and massive numbers of assets that had been destroyed created a perfect storm of controversy over whether assureds could claim coverage for ROW/D under the excess liability policies.

The typical excess liability policy provides coverage for "liability imposed upon the insured by law or assumed under contract . . . for damages . . . for . . . property damage." This policy language raises a number of questions regarding the applicability of coverage for ROW/D.

1. "Liability"

As with traditional P&I coverage for ROW/D, removal is only covered when the assured is legally liable for the cost of removal. In many instances, this is highly questionable—is the owner of a drilling rig that sinks outside of territorial waters as a result of a Force 5 hurricane "liable"? There may be instances where the answer is yes, since as noted above, the Wreck Act does apply to MODUs operating on the Outer Continental Shelf, and liability under the Wreck Act does not depend upon fault, but there are many instances in which liability will be very doubtful.

2. "imposed by law"

This has been a significant battleground. The courts have held that a "liability imposed by law" is to be distinguished from liability one voluntarily assumes under a contract. Mineral lessees whose platforms have been destroyed undoubtedly are liable to remove the debris under the MMS regulations and their leases with the government. But is this a "liability imposed by law"? The regulations merely reiterate the language of the MMS leases, and the regulations specifically provide that the obligation is imposed on lessees. Insurers have argued with considerable logic that the liability of a mineral lessee is a contractual liability arising under or derived from the mineral lease, not a liability "imposed by law."

3. "assumed under contract"

On its face, this might seem to encompass the liability of a mineral lessee to remove debris, or the liability of a drilling contractor under a drilling contract to remove a wreck. However, the courts have held that the term "liability assumed under contract" is limited to liabilities whereby the insured agrees to assume the tort liability of a third person. Mineral lessees may be liable under their leases to remove debris, but this obligation is not an obligation to indemnify the government for the government's tort liability. Nor does a contractor's removal obligation fit very well within this definition, since, as discussed above, the lessee's obligation would appear to be more accurately characterized as arising in contract rather than tort. Thus, the liability that a drilling contractor assumes in his drilling contract to remove the wreck of his rig would not appear to be a liability to indemnify the lessee for the lessee's tort liability.

4. "for damages"

There is difficulty here as well, since one normally thinks of "damages" as something one pays to an injured third person to satisfy a judgment or settle a claim, not expenses incurred by

the insured himself, and ROW/D expenses are typically paid by the insured to contractors to remove the wreck or debris, not paid to the injured third person. There are precedents in other areas of law, however, where the courts have given a liberal reading to this term. For example, the courts have held that expenses incurred to mitigate a pollution incident are "damages" within the meaning of liability policies, and the argument could logically be made with respect to ROW/D claims.

5. "on account of property damage"

This is similarly problematic, since it immediately raises the question of whose property has been damaged. Of course, the vessel that has become the wreck has been damaged, but most excess liability policies contain an express exclusion for damage to property of the insured. One must then find some third party whose property has been damaged in order to trigger coverage.

In certain instances, this is not particularly difficult. Most liability policies define "property damage" to include "loss of use of tangible property caused by an occurrence." Accordingly, if the wreck impedes access to a platform, it would appear to fall within this definition.

But what if the wreck is in the open ocean away from any platform? Under international law, the U.S. government's has "sovereign rights" in the Exclusive Economic Zone ("EEZ") to exploit the natural resources of the EEZ, and one could argue that a wreck in the EEZ that is a hazard to fishing or mineral exploration causes damage to the government's rights in the waters and seabed of the EEZ, and that this constitutes "loss of use of tangible property," i.e., the EEZ. This is an issue yet to be decided.

III. Nairobi Convention on the Removal of Wrecks

In May 2007, a diplomatic conference in Nairobi, Kenya adopted the Nairobi Convention on Removal of Wrecks. It has not yet entered into force, and will almost certainly not be adopted in the United States. The impetus behind the Convention was the need, as witnessed by the *Protexa* case discussed above, to provide a legal regime to govern the removal of wrecks beyond the territorial sea. The Convention contains provisions dealing with reporting wrecks to the nearest coastal state, criteria for determining the hazard posed by wrecks, liability of the owner for the removal and marking of wrecks, and compulsory insurance provisions.

IV. Conclusion

As long as there is maritime commerce, ships will on occasion go to the bottom in places where the wreck is of some concern to someone. Accordingly, ROW/D is destined to be an issue for shipowners and marine insurers as long as there is maritime commerce.