

Convention on Supplementary Compensation: Liability Implications for the Nuclear Industry

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Now that Japan's Diet, as of November 21, 2014, has approved Japan's ratification of the Convention on Supplementary Compensation for Nuclear Damage (CSC) and implementing domestic legislation, Japan presumably will soon deposit its instrument of ratification with the International Atomic Energy Agency (IAEA). Ninety days following such action by Japan, the CSC will enter into force, since its requirement for entry into force (a minimum of five ratifying parties collectively having at least 400,000 MW(t) of installed nuclear generating capacity) will have been satisfied. While the additional compensation aspect of the CSC's impending entry into force has attracted global attention, less consideration has been given to the CSC's impact on the nuclear liability of sellers and purchasers of components, nuclear fuel and related technology and services for the construction and operation of nuclear power stations. This client alert provides our views concerning the most significant near-term implications of the CSC's entry into force.

Benefits for the Nuclear Industry

While the long-awaited entry into force of the CSC—which was originally adopted by the participating countries and opened for signature in 1997—will clearly be a “watershed” event, the immediate benefits (and costs) to nuclear suppliers and purchasers will be relatively modest, except with respect to U.S. and other suppliers that (1) are located in a country that has ratified the CSC; and (2) provide products or services for the construction, operation, maintenance or decontamination/decommissioning (D&D) of a nuclear power station in a country that has ratified the CSC. Since only five countries (the United States, Romania, Argentina, Morocco and the United Arab Emirates) have ratified the CSC, Japan's ratification of the CSC will cause the CSC, once in force, to be applicable only to nuclear incidents at facilities within

those six countries, as well as certain nuclear incidents that occur during transportation of nuclear material to or from facilities in those countries. Unless additional countries that have leading roles as consumers or suppliers of such components, services and nuclear materials become parties to the CSC, the protective effect of the CSC will be geographically narrow. Progress toward the goal of near-universal adherence to the CSC is likely to be quite slow, especially in view of the apparent reluctance of the Western European countries to become CSC parties.

Despite the limited geographic reach of the CSC, upon its entry into force with the above-mentioned six countries as CSC parties, the benefits of CSC adherence are likely to be significant, in some situations. Suppliers in CSC countries that provide such support to nuclear power stations in other CSC countries will immediately benefit, in two principal ways: (1) lawsuits against such suppliers in their own countries or other CSC countries should be dismissed since the CSC directs or “channels” jurisdiction over such lawsuits exclusively to the courts of the CSC country in which the nuclear incident took place; and (2) a second tier of “supplementary” compensation will be paid by the CSC parties if the first tier amount that must be maintained by CSC parties (at least 300 million Special Drawing Rights [SDRs] or about \$440 million) is exhausted. Since a large nuclear incident comparable to the incidents at the Chernobyl or Fukushima Daiichi plants would likely produce nuclear damage greatly exceeding both the CSC’s required first and second tiers of compensation, the supplementary compensation aspect of the CSC may not be sufficient to reduce the risk to suppliers of lawsuits being filed against them in countries that are not parties to the CSC (“third countries”). While the benefits of the CSC’s supplementary compensation provisions have received more attention than the “jurisdiction channeling” aspect of the CSC, the latter aspect may be more significant for vendors of materials and services to nuclear power plants in CSC countries.

Reevaluation of Nuclear Liability Contractual Provisions in Light of the CSC

In our view, the CSC’s entry into force provides a prime opportunity for both suppliers and consumers of such nuclear materials, components and services to reconsider the nuclear liability provisions of the contracts that have been the basis for such sales. For many years, these provisions were sometimes considered to be “legal boilerplate” that required far less attention than the price, delivery and other commercial terms that were unique to each contract. However, the nuclear incident at Fukushima Daiichi Nuclear Power Station and the resulting compensation (currently totaling about \$38 billion) plainly provide a strong rationale for all nuclear suppliers and consumers to evaluate the extent to which such nuclear liability provisions actually protect them, or conversely, expose them to risk.

In the absence of any widely used “model” terms, the text of such provisions usually results from case-by-case negotiations. In some instances, the terms date from the 1960’s or 1970’s, and the origins of many nuclear liability provisions currently in use may be traced to contracts executed decades previously. However, “old” contract terms often do not adequately address “modern” circumstances, including the presence or absence of protection pursuant to modern nuclear liability laws or international nuclear liability conventions. Accordingly, it would behoove suppliers and customers to “mind the gaps” that expose the parties to risk, as such gaps often are not adequately or correctly understood. Proper assessment of these risks at least will enable parties to consider their ability or willingness to share these “residual” risks under indemnification provisions, waivers or other contractual provisions.

Responsibility of Some Industry Participants to Fund CSC Supplementary Compensation Payments

A second major near-term task for nuclear vendors (as well as operators of nuclear power stations in CSC countries) is to assess their potential financial liability for their countries’ payments toward the CSC’s “international fund” of supplementary compensation following a nuclear incident in a different CSC country.

The extent of such liability of nuclear industry participants depends on the manner in which their governments, upon adherence to the CSC, will allocate the cost of such countries' payment of supplementary compensation in response to any future requests by other CSC parties for supplementary compensation, following a nuclear incident that exceeds the "first tier" of nuclear liability protection in the CSC country in which the nuclear incident took place.

In the United States, Congress passed legislation in 2007 requiring U.S. nuclear vendors to bear the cost of such supplementary compensation payments following a nuclear incident in another CSC country that exceeds that country's national compensation threshold. More than three years following the date when the U.S. Department of Energy (DOE) was required by Congress to promulgate a rule to allocate such costs among U.S. nuclear vendors, DOE has not published a proposed rule. DOE published a Notice of Inquiry in 2010 that sought to obtain comments on certain aspects of a proposed rule. However, according to a knowledgeable DOE official, DOE will soon publish the proposed rule, likely before the end of 2014. The industry will have an opportunity to comment on the proposed rule. Based on the industry's responses to DOE's previous Notice of Inquiry, DOE's proposed rule will likely be opposed by some major nuclear vendors, particularly if commercially available insurance continues to be unavailable to fund such payments.

Additional information concerning the purpose and status of the CSC is set out below.

Purpose of the CSC

The goal of the CSC is to create an "umbrella" nuclear liability regime that covers any country currently party to (1) the Paris Convention; (2) the Vienna Convention; or (3) no international convention on nuclear liability, but which is party to the Convention on Nuclear Safety, and whose national laws comply with the requirements of the Annex to the CSC (including a minimum liability limit of 300 million SDRs, with strict or absolute [no fault] liability exclusively channeled to the Operator of the nuclear installation at which a nuclear incident occurs).

The CSC also seeks to harmonize international nuclear liability laws, many of which are presently subject to key ambiguities. Another key objective of the CSC is to channel exclusive jurisdiction to courts of the CSC party within which the nuclear incident occurs (the "Installation State").

Much of the commentary on the CSC has focused on its establishment of a system of supplementary compensation in the event of a nuclear incident to ensure that adequate compensation for third parties suffering nuclear damage is available, as follows:

- 1st tier: national compensation amount (minimum 300 million SDRs or approximately \$440 million)
- 2nd tier (if 1st tier is inadequate): international fund established under the CSC to which all parties contribute based on each party's (1) installed nuclear capacity and (2) United Nations rate of assessment

Status of the CSC

Entry into force of the CSC requires at least five ratifying countries, with a cumulative 400,000 MW(t) of installed nuclear capacity. Current countries that have ratified the CSC (often called "contracting states") are as follows: United States, Argentina, Romania, Morocco and the United Arab Emirates, collectively having a total installed nuclear capacity of 318,349 MW(t), according to IAEA statistics.

Ratification of the CSC by Japan, which currently has a total of 131,077 MW(t) of installed nuclear capacity, will contribute more than the additional 81,651 MW(t) of installed nuclear capacity that is needed to bring the CSC into force. In addition to Japan, countries that have expressed an interest in joining the CSC are as follows:

1. Republic of Korea (59,908 MW(t))
2. Canada (45,625 MW(t)) (signed the CSC in 2013)
3. China (56,923 MW(t))
4. India (19,911 MW(t)) (signed the CSC in 2010)

Action by Japan's Diet to Approve Japan's Ratification of the CSC

On October 31, 2013, Japan's foreign minister indicated to the U.S. Secretary of Energy, during meetings in Tokyo, that Japan intended to join the CSC, in particular to enable foreign entities to participate in efforts for the cleanup and decommissioning of the Fukushima Daiichi Unit 1 reactor. According to press reports, on November 19, 2014, Japan's Diet approved legislation to authorize Japan's ratification of the CSC. Subsequently, on November 21, 2014, Japan's Diet approved two bills to conform Japan's nuclear damage compensation program with CSC requirements. Although all nuclear power stations in Japan remain temporarily offline, Japan's installed nuclear capacity is reported by the IAEA to be 131,077 MW(t). According to Article IV(3) of the CSC, installed nuclear capacity does not include reactors from which fuel has been permanently removed. If Japan's installed nuclear capacity is determined to be at least 81,651 MW(t), then Japan's ratification of the CSC will cause the CSC to enter into force 90 days following the date of Japan's deposit of its instrument of ratification. The following table shows the hypothetical amounts of CSC international fund contributions if a nuclear incident occurred and CSC parties consisted of the current contracting states in addition to Japan.

Contracting Party	Installed Nuclear Capacity (MW(t))	UN Rate of Contribution	Contribution (SDR)
Argentina	5,365	0.432%	1,780,068
Japan	131,077	10.833%	27,931,332
Morocco	0	0.062%	24,480
Romania	4,375	0.226%	1,401,732
United Arab Emirates	0	0.595%	234,926
United States	308,609	22.000%	44,493,174
TOTAL	449,426	34.148%	75,865,712

Result: A total of 75.86 million SDRs (approximately \$117 million) would be available in the CSC's second tier of compensation.

Calculations prepared using CSC calculator spreadsheet incorporating formula specified in CSC and based on IAEA reactor database.

Prospects for Global Adherence to the CSC

A key question is whether the long journey toward the CSC's entry into force portends slow progress in achieving global adherence to the CSC. A major aspect of such a prediction is whether the countries that are parties to the existing Paris Convention or Vienna Convention join the CSC. In view of statements by governmental officials in Western Europe concerning the reluctance of Paris Convention countries to join the CSC, a recent joint U.S.-France statement has been widely discussed, particularly with respect to whether it suggests that France may join the CSC. The U.S.-France Joint Statement on Liability for Nuclear Damage (August 28, 2013) emphasized the CSC's important role as the bedrock of a worldwide nuclear liability regime. In that statement, the U.S. and France committed to "[c]oordinate their actions in encouraging adherence to the enhanced international nuclear liability instruments, including, as appropriate, the revised Paris Convention (together with the revised Brussels Convention) or the revised Vienna Convention, which may be linked by the Joint Protocol, and the CSC, **with an initial step being the entry into force of the CSC**" (emphasis added).

Notably, according to one Belgian official, "most of the Parties to the [Paris Convention and Brussels Supplementary Convention¹ have] claimed...it [is] hard to envisage signing two complementary conventions with different mechanisms, allocation rules and beneficiaries."²

Moreover, at a recent meeting of the International Nuclear Law Association, a Russian participant questioned the utility of the CSC in light of the existing Vienna and Paris Conventions, stating that the CSC "may create a separate nuclear liability regime and will add fragmentation" to the Paris-Vienna regime.

CSC's Jurisdictional Provision

The CSC's jurisdiction "channeling" aspect is particularly important from the standpoint of risk exposure for nuclear suppliers and operators following a nuclear incident. Article XIII(1) of the CSC provides as follows: "Except as otherwise provided in this article, jurisdiction over actions concerning nuclear damage from a nuclear incident shall lie only with the courts of the Contracting Party within which the nuclear incident occurs."

Thus, upon the CSC's entry into force, courts of non-CSC parties would not have jurisdiction to rule on the merits of lawsuits brought by persons who claim nuclear damage allegedly caused by a nuclear incident in another country that is a CSC party. In such cases, the courts of the country where the nuclear incident occurred (the "Installation State") have exclusive jurisdiction, among countries that are CSC parties. However, this channeling and exclusive jurisdiction are applicable only to suits in CSC parties claiming nuclear damage from a nuclear incident in a CSC party.

Plaintiffs claiming nuclear damage caused by a nuclear incident at a facility in a CSC party country may attempt to avoid the CSC's "channeling" of jurisdiction exclusively to the courts of the Installation State. For example, such plaintiffs who claim nuclear damage may file lawsuits against a nuclear vendor who

¹ Paris Convention countries that are parties to the Brussels Supplementary Convention are as follows: Belgium, Denmark, Finland, France, Germany, Italy, Netherlands, Norway, Slovenia, Spain, Sweden and United Kingdom.

² Roland Dussart-Desart, Head of Division in the Office of President, Service public fédéral Economie, PME, Classes moyennes et Energie, Belgium, 2006 (quoted in Julia Schwartz, *International Nuclear Third Party Liability Law: The Response to Chernobyl*, in *International Nuclear Law in the Post-Chernobyl Period*, at page 52).

supplied services or components to the nuclear facility that suffered the nuclear incident in a “third” country that is not a CSC party. If a court in such a third country enters a judgment in favor of such plaintiffs, awarding them compensation for nuclear damage, they may seek to enforce that judgment in the courts of a CSC party in which such nuclear vendor has business operations or assets. Under generally applicable U.S. law on enforcement of foreign judgments, “a final judgment of a court of a foreign state granting or denying recovery of a sum of money . . . is conclusive between the parties, and is entitled to recognition in courts in the United States.”³ A prominent federal litigation guide comments as follows regarding the process for obtaining recognition and enforcement of a foreign judgment:

“U.S. courts have been quite liberal in their recognition and enforcement of foreign judgments. As a result, once the party seeking recognition of a foreign judgment has established the judgment’s existence, the burden is generally on the party resisting recognition to prove grounds for non-recognition.”⁴

U.S. Ratification and Implementation of the CSC

Over a decade ago, the United States was the first country to sign the CSC, following the CSC’s adoption after prolonged negotiations under the auspices of the IAEA. After signing the CSC on September 29, 1997, the United States began a slow journey toward ratification, which could not occur until the U.S. Senate gave its advice and consent to ratification and Congress enacted implementing legislation.

On December 19, 2007, President George W. Bush signed into law the Energy Independence and Security Act (EISA). Section 934 of EISA directs the DOE to promulgate rules for contingent cost allocation associated with U.S. contributions to the CSC international fund within three years (i.e., by December 19, 2010). Section 934 utilizes the existing Price-Anderson Act funding mechanism to cover U.S. contributions for any nuclear incident within the United States at a nuclear installation covered by the Price-Anderson Act. In contrast, for nuclear incidents outside the United States not covered by the Price-Anderson Act, Section 934 allocates the cost of U.S. contribution to the CSC’s international fund among U.S. nuclear suppliers on the basis of risk, under an allocation formula to be determined by DOE.

On May 21, 2008, the U.S. finally ratified the CSC. In accordance with its important role under Section 934, on July 27, 2010, DOE issued a Notice of Inquiry and Request for Comment on proposed CSC retrospective risk pooling program. Comments from U.S. nuclear industry participants expressed pessimism regarding the impacts on the industry of the contingent cost allocation approach and its insurability. In its comments to DOE, the Nuclear Energy Institute (NEI) stated as follows:

“NEI believes that DOE should seriously consider the negative impact that requiring domestic suppliers to bear the burden of the U.S. contingent costs under the CSC will have on their ability to compete in the global market. [...] Given that the CSC is not yet in force and not likely to come into force in the near-term, DOE has time to ensure the implementing rule is both technically sound (from a risk-informed perspective) and not an impediment to domestic suppliers’ efforts to compete in the global nuclear market.”

American Nuclear Insurers (ANI) commented as follows concerning the availability of commercial insurance to cover the cost allocation among suppliers: “ANI considers it unlikely that its members would

³ Restatement (3d) on Foreign Relations, § 481.

⁴ Ronald Brand, *Federal Judicial Center International Litigation Guide: Recognition and Enforcement of Foreign Judgments* (2012).

participate in a program to insure the contingent cost to the United States under the terms of the CSC and collected from nuclear suppliers through the retrospective risk pooling program established in Subsection 934(e).”

Conclusion

The impending entry into force of the CSC will mark a significant milestone in international efforts to promote a global nuclear liability and compensation regime. Of particular significance to nuclear suppliers and customers is the CSC’s jurisdictional channeling feature, as well as the mechanism by which each CSC party’s supplementary compensation contribution will be funded. These developments afford nuclear industry participants a valuable opportunity to assess their actual risk exposure and means of protection.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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