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Report on negotiations held by the Chairman and co-ordinators of the working group of 21

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28. We all look forward to the last phase of this Conference and to a viable convention that will instil the conditions of peace into international relations among nations.

ANNEX

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Report on negotiations held by the Chairman and co-ordinators of the working group of 21

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At this resumed session, the working group of 21 continued its work in the form of meetings and consultations. It was chaired over-all by the Chairman of the First Committee, who also co-ordinated the negotiations on the Assembly and the Council. Mr. Njenga co-ordinated the negotiations on the system of exploration and exploitation. Mr. Koh co-ordinated the negotiations on financial arrangements, Mr. Wuensche acted as co-ordinator but held separate meetings of the group of legal experts, the results of which were reported to the working group of 21. The suggestions resulting from consultations held by the Chairman and the co-ordinators of the working group of 21 are given in document WG21/2 (appendix A). The report of Mr. Wuensche is incorporated in this report as appendix B.

The working group of 21 considered the hard-core issues in the following order: first, the Assembly and the Council: composition of the Council, decision-making system and interrelationship between the Council and the Assembly; secondly, financial arrangements; and thirdly, the system of exploration and exploitation.

I. The Assembly and the Council

The working group of 21 addressed the issues under this heading, bearing in mind the need to assemble a mini-package consisting of the interrelationship of the principal organs of the Authority, mainly regarding the scope of the powers and functions of the Assembly and the Council, and the decision-making system in the Council.

Document WG21/2 contains suggestions which were made during consultations held by the Chairman and co-ordinators following negotiations. Those relating to the Assembly and Council were chosen because it is the impression of the Chairman, in co-ordinating the negotiations, that they had been the basis for intense negotiations. Some of the suggestions were accepted on an *ad referendum* basis. Others, notably the ideas on the decision-making system, did not enjoy complete consensus, especially as the number of members required for a blocking majority remains unsettled and reservations have been expressed by some representatives regarding the list of subjects requiring a special voting régime.

The suggestions, all part of a "package", do not assume more than the role of providing indication as to the trends of negotiations. It is only the reaction of the membership of the First Committee that will dictate the capacity of any ideas to enter into the second revision of the negotiating text.

1. *Interrelationship*

The suggestions attempt to resolve the existing issues relating to the concept of the supremacy of the Assembly, which appeared to present difficulty to the industrialized countries. They also seek to clarify the scope of exercise of the powers and functions of each organ.

First, the suggested revision of article 160 states that the Assembly shall be considered the supreme organ of the Authority. The sources of its supremacy lie in its membership consisting of all the members of the Authority, in its accountability for the other principal organs of the Authority, in its "incidental powers" as defined in article 157 and its residual powers as referred to in new paragraph 2 (*o*) of article 160.

Secondly, the relationship of powers and functions of the principal organs of the Authority is defined in article 158, paragraph 4, which makes it explicit that each organ, in exercising its powers and functions, shall avoid taking any action which may derogate from or impede the exercise of specific powers and functions conferred upon another organ. Paragraph 2 (*o*) of article 160 gives the Assembly power to discuss and decide upon any question within the competence of the Authority, and to decide which organ shall deal with any question not specifically entrusted to a particular organ. The revised paragraph 2(*r*) of article 162 gives the Council power to make recommendations to the Assembly concerning policies on any question within the competence of the Authority.

A related issue is that of the interrelationship of the Council and its subsidiary organ, the Legal and Technical Commission. Paragraph 2 (*j*) of article 162 of the revised negotiating text provides that the Council shall act expeditiously in its approval of formal, written plans of work following the review of the Commission. It then provides that such plan of work shall be deemed to have been approved unless a decision to disapprove it is taken within 60 days upon its submission by the Commission. It is this latter provision that has proved to be a highly contested issue, the opponents considering that it erodes the supremacy of the Council over its subsidiary organ.

The suggested article 162, paragraph 2 (*j*) seeks to accomodate this serious preoccupation. It restricts the operation of such automatic approval system only to a plan of work which is not contested by a competing application. It also prescribes that a plan may be deemed to have been approved unless a proposal for its approval or disapproval has been voted upon within 60 days.

On an *ad referendum* basis, it would appear that these suggestions attract consensus.

2. *The decision-making system in the Council*

This has been perhaps the most difficult issue to tackle in the absence of a resolution of other issues in the mini-package. The clause of the revised negotiating text, stipulating that all decisions on questions of substance are to be taken by a three-fourths majority of members present and voting, clearly does not enjoy a consensus. It appears to be generally accepted now that no traditional veto system as known in the United Nations system is acceptable. There has also been widespread rejection of the concept of "chamber" voting, in which identified interest categorization could block a decision.

Consequently, some attempt has been made to identify special or sensitive issues over which the industrialized countries need special protection. The list of these was, however, not forthcoming. It was thought expedient to review issues over which no special régime or procedure of voting was acceptable.

The suggestions relating to article 161 reflect this new approach. It contains three new points. First, the decisions on questions of procedure shall be taken by a majority of the members present and voting. Secondly, certain questions of substance which are enumerated in subparagraph (*b*) shall be taken by a two-thirds majority of the members present and voting provided that such majority includes a majority of the members of the Council. Thirdly, decisions on all other questions of substance shall be taken by a two-thirds majority of members present and voting, provided a specific number of members, still to be settled, has not cast negative votes. When the issue arises as to whether the question is covered by this subparagraph or not, the questions shall be treated as so covered unless otherwise decided by the Council by the majority required for questions under the paragraph.

The acceptance of this system itself will depend on a satisfactory resolution of two main questions. The crucial one is that of the blocking figure under subparagraph (*c*). As the suggestions indicate, that figure is somewhere between 5 and 10, both of which are clearly unacceptable as basis for consensus. The other, perhaps to a lesser extent, relates to the list of issues contained in subparagraph (*b*).

It is generally felt that the system, as stated, is not to be considered as a basis of a viable consensus until these issues are satisfactorily resolved. Consequently, it would appear inadvisable to consider the inclusion of these latter suggestions in any further revision of the negotiating text before that event. However, it is also clear that the system must be kept in view as an idea which may lead to a consensus, if the revised negotiating text continues to present difficulties.

II. Financial arrangements

Annex III: Financing the Enterprise

The Chairman of negotiating group 2 began his report by explaining the revisions which he proposed to annex III, the statute of the Enterprise.

The first revision proposed is to article 3. Mauritius pointed out that there is a need to make a cross-reference between article 3 and article 10 in order to make explicit the fact that article 3 is subject to article 10. The Chairman accepted this point and proposed the addition of the words "subject to article 10, paragraph 3, below". Since

this revision is only by way of clarification, it should not be controversial.

The second revision proposed is to article 10. Following a suggestion by India, he reformulated article 10, paragraph 2 (*c*) as a new paragraph 3. The Chairman deleted the words "to the extent that such funds are not covered by the other funds referred to in paragraph 1".

The new paragraph 3 contains the following salient points:

First, the Enterprise is assured of the funds necessary to carry out one fully-integrated mining project. An integrated mining project would enable the Enterprise to process up to four metals, namely, cobalt, copper, manganese, and nickel. The Enterprise has the discretion to decide whether to utilize these funds by investing them in one project of its own, or to invest them in joint ventures. During the consultations, the Chairman raised the question whether the amount of the funds should be specified. He asked this question because many Governments would like to know the extent of their obligations. Members of the Group of 77 were, however, against specifying an amount. They pointed out that estimates of the capital required to carry out one fully-integrated project varied greatly. The original estimates by the Massachussets Institute of Technology, based upon a three-metal case, and upon 1976 prices, were $560 million. The new estimates, based upon 1979 prices, suggest an amount of $750 million. Other estimates, however, based upon a four-metal case, are much higher and suggest a total amount exceeding $1 billion. The Chairman suggested specifying the amount of $1 billion, together with an escalating factor to take care of inflation. Members of the Group of 77 could not accept his proposal because they feared cost overruns would not be taken care of by the escalating factor. For these reasons, therefore, he left the amount unspecified. The amount would be determined by the Assembly, upon the recommendation of the Council, on the advice of the Governing Board of the Enterprise.

The next salient point is the ratio between the interest-free loans from States parties and the guaranteed interest-bearing loans. In dealing with this question, an analogy was often made with the debt-equity ratio of a company. The interest-free loans are compared with the equity capital of a company. The interest-bearing loans are compared with the debt capital of a company. Some delegates objected to this analogy on the ground that the shareholders of a company expect to earn dividends on their equity, whereas the lenders of the interest-free loans to the Enterprise would not receive any dividends. One answer to this criticism is that lenders of the interest-free loans to the Enterprise also expect to earn dividends by way of sharing the profits made by the Enterprise which will be distributed to States parties by the Authority. In his consideration of this question, the Chairman found the analogy with the debt-equity ratio a helpful one.

The members of the Group of 77 contend that the ratio of the interest-free loans to the guaranteed interest-bearing loans should be 1:1. Industrialized market-economy countries contend that the ratio should be 1:2. The Chairman has asked the United Nations Centre on Transnational Corporations to undertake a survey of the debt-equity ratios of mining companies in the industrialized market-economy countries. The results of the survey are contained in a document which is attached to this report as annex A. The table shows support for both a debt-equity ratio of 1:1 and a debt-equity ratio of 2:1. In view of this and in view of the fact that the Enterprise will be a new institution with no assets and no track record, he thought a ratio of interest-free loans to guaranteed interest-bearing loans of 1:1 would be justifiable.

The third salient point is the scale which will determine the contributions by States parties of interest-free loans as well as their guarantees of the debts of the Enterprise in raising the remaining half of the capital required. The Chairman of negotiating group 2 considered various possibilities, but came to the conclusion that the best scale to use is the scale referred to in article 160, paragraph 2 (*e*), which is based upon the United Nations scale. Several representatives of the Group of 77 pointed out, during consultations, that since the Enterprise belongs to all, no State Party should be exempted from making a contribution to the Enterprise. They also said that the contributions by States parties should reflect their varying capacities to help and that the most widely acceptable scale for doing this is the United Nations scale.

The fourth salient point concerns the repayment of the interest-free loans to States parties. The Chairman proposed that the repayment of interest-bearing loans shall have the priority over the repayment of interest-free loans. He also proposed that, upon the recommendation of the Council, on the advice of the Governing Board of the Enterprise, the Assembly shall adopt a schedule for the repayment of the interest-free loans to the States parties.

Annex II: Financial terms of contracts

Turning to article 12 of annex II of the revised negotiating text, the Chairman proposed a number of changes to this article, and attempted to explain the more important of these proposals. In paragraph 1, the Group of 77 has proposed the addition of a subparagraph (*f*) which would state the general principle that the financial terms of sea-bed mining should be comparable to the financial terms of land-based mining. The evil which the Group of 77 wishes to avoid is that investment would be artificially diverted from land-based mining to sea-bed mining if the financial terms of sea-bed mining were unduly favourable compared to those of land-based mining. As a result of consultations the Chairman proposed a new subparagraph (*f*) which he hoped would be generally acceptable.

The mixed system

The Chairman then turned to the mixed system of financial payments contained in article 12, paragraph 6. The Group of 77 did not like the proposal but could accept it. The industrialized countries said, however, that they could not accept the proposal. They had several complaints. The first complaint was that the production charge should be based upon the attributable gross proceeds and not on the gross proceeds. Secondly, the said that the production charge rates of 2 per cent in the first period and 5 per cent in the second period were too high. The best offer they were willing to make was 1 per cent in the first period and 2 per cent in the second period. Their third complaint was against the proposal that the attributable net proceeds should be equal to 35 per cent of the contractor's net proceeds. They said that the figure of 35 per cent was arbitrary and that it should be replaced by the ratio of the development costs of the mining sector to the contractor's total development costs. Fourthly, they complained that the trigger mechanism of recovery of twice the development costs was an inadequate method of reflecting the opportunity cost of capital invested in the project. Fifthly, they complained that the tax rates of 45 per cent in the first period and 65 per cent in the second period were too high. The best offer they were willing to make was for 25 per cent in the first period and 50 per cent in the second period. Finally, they complained that the tax system was inflexible in that it did not vary with the contractor's return on investment. It was regressive in that the Authority's relative share was larger when the contractor's return on investment was low and smaller when his return was high.

Proposal by Norway

In order to bridge the considerable gap existing between the Group of 77 and the industrialized market-economy countries, the representative of Norway, Mr. Evensen, made a very interesting proposal. A copy of his proposal is attached as annex B. Briefly, the production charge rates would be 2 per cent in the first period and 4 per cent in the second period; the attributable net proceeds would be 20 per cent in the first period and 40 per cent in the second period; the trigger mechanism would be the same as in paragraph 6 (*e*); and the tax rates would be 40 per cent in the first period and 75 per cent in the second period. In the Chairman's view, Mr. Evensen's proposal was a considerable improvement on his own proposal as contained in the revised negotiating text. Unfortunately, Mr. Evensen's proposal was not acceptable either to the group of 77 or to the industrialized market-economy countries.

New proposal on the mixed system

As a result of the intensive consultations and negotiations which took place at this resumed session of the Conference, the Chairman proposed a new package on the mixed system of financial payments which he hoped would be acceptable to both the Group of 77 and the industrialized market-economy countries.

Production charge

The Chairman had retained the idea that the production charge should be based upon the market value of the processed metals, or the Contractor's gross proceeds, rather than on the attributable gross proceeds. For the first period, he did not propose to change the rate, which remains at 2 per cent. For the second period, he proposed a reduction from 5 per cent to 4 per cent. During the consultations, some members of the Group of 77 indicated their willingness

to accept a production charge rate of 4 per cent for the second period.

The Chairman knows that the production charge rate of 4 per cent, based upon the market value of the processed metals, can be a heavy burden for the Contractor, even in the second period, if in a particular year the Contractor's project is doing badly. This is a legitimate concern and in order to take care of the concern he proposed a new safeguard. The safeguard is that if, in any financial year, the contractor's return on investment is less than 15 per cent, he shall pay a production charge of 2 per cent instead of 4 per cent. Return on investment is arrived at by dividing the attributable net proceeds by the development costs of the mining sector. The Chairman hopes that with this additional safeguard, the production charges of 2 per cent and 4 per cent, based upon the market value of the processed metals, will be acceptable to both the Group of 77 and the industrialized market-economy countries.

The attributable net proceeds

Perhaps the most difficult issue in the negotiations is the question how to determine the Authority's tax base if the Contractor's project is partially or fully integrated. In the revised negotiating text, the Chairman proposed a predetermined constant ratio of 35 per cent. This was not acceptable to the industrialized market-economy countries who complained that any predetermined constant ratio was arbitrary. They insisted that the most objective and logical method of determining the attributable net proceeds was to use the ratio of the development costs in the mining sector to the Contractor's total development costs.

In order to assist delegates in negotiating this difficult issue, negotiating group 2 prepared a paper. This paper is attached as annex C. The paper identifies four methods of determining the attributable net proceeds. First, the predetermined constant ratio method; second, the cost-ratio method; third, the net-back method; and fourth, the cost-plus method. Each of the four methods has its advantages and disadvantages.

The major disadvantage of the predetermined constant ratio method is that the ratio is derived from certain assumptions and the actual financial outcome may not conform to these assumptions. The actual ratio may turn out to be higher or lower than the predetermined constant ratio. If higher, the Authority's tax base, calculated by this method, is lower. If the actual ratio is lower, the tax base of the national taxing Authority is lower and the contractor's tax burden may be higher.

The cost-ratio method assigns the value of the nodules, if any, to the mining and the processing sectors proportionately to the development costs of the two sectors. A major disadvantage of the cost-ratio method is that it may vary from project to project, and thus the Authority has a less stable tax base compared with the predetermined constant ratio method.

The Chairman of negotiating group 2 was unable to convince the industrialized market-economy countries to use the net-back method or the cost-plus method. The intensive negotiations on this issue have resulted in the combination of the cost-ratio method and the predetermined constant ratio method. The latter will act as a floor above which the attributable net proceeds will be determined by the cost ratio. The Chairman suggested a floor of 25 per cent for a fully integrated three-metal project. In all other cases, including four metal projects producing nickel, copper, cobalt and manganese, he proposed that the Authority may, by regulations, prescribe appropriate floors which will bear the same relationship to each case as does the 25 per cent floor to the three-metal case.

The tax system

In order to assist representatives in the negotiations on the tax system and tax rates, negotiating group 2 prepared a paper entitled: "An alternative scheme of taxation: variable incidence". This paper is attached as annex D and deals with the trigger mechanism as contained in paragraph 6 (*e*) and with the relative merits of single rate and variable rate tax systems.

The paper suggests that, from the points of view of both the Authority and the contractor, a trigger mechanism whereby development costs are recovered with an interest rate on the unrecovered part of the development costs would be preferable to the proposal of twice the recovery of development costs. The reason is that it is possible for a project to achieve a more than adequate over-all return on investment before 200 per cent of development costs are recovered. In such an event, the contractor would continue to pay production charge and tax rates of the first period. This would consequently reduce the income to the Authority. For this reason, the Chairman reformulated the trigger mechanism. Under his new proposal, the first period would come to an end when the contractor recovered his development costs with interest at 10 per cent on that portion of his development costs not recovered by his cash surplus. Cash surplus means the contractor's gross proceeds, less his operating costs, less his payments to the Authority. This is the same as the contractor's net proceeds plus his annual recovery of development costs, as stated in paragraph 6 (*j*) of his new text, less his payments to the Authority.

The paper also demonstrates that from the points of view of both the Authority and the contractor, a flexible tax system based upon an incremental scale would be preferable to a single-rate system. Under a single tax rate the Authority would not be able to capture additional revenues during the years when the profits were high. For various reasons, the Chairman therefore proposed a change in the tax system to a flexible one using the contractor's return on investment. He proposed three incremental steps. The first would be when the contractor's return on investment was greater than 0 per cent but less than 10 per cent. That part of the attributable net proceeds falling within that increment would be taxed at 35 per cent in the first period and 40 per cent in the second period. The second step would be when the contractor's return on investment was 10 per cent or greater, but less than 20 per cent. That part of the attributable net proceeds falling within that increment would be taxed at 42.5 per cent in the first period and 50 per cent in the second period. The third step would be when the contractor's return on investment was 20 per cent or greater, when the applicable tax rates would be 50 per cent in the first period and 70 per cent in the second period.

The single system

One of the fundamental principles of our negotiations is that the single system and the mixed system must be equalized. The Chairman used the contractor's internal rates of return to equalize the two systems. Because of the changes he proposed to the mixed system, it would be necessary to propose some changes to the single system. He suggested reducing the production charge in the first period from 8 per cent to 5 per cent, and from 13.5 per cent to 12 per cent in the second period.

Monetizing the proposals

The single system and the mixed system contained in his new proposal would produce different amounts of income for the Authority and different internal rates of return for the contractor depending upon the technical and economic outcomes of sea-bed mining projects. It is nevertheless useful to examine payments to the Authority and the contractor's internal rates of return under several sets of possible circumstances.

The calculations which follow (annex E) are based upon a version of the Massachusetts Institute of Technology model of a vertically integrated sea-bed mining operation. These figures permit the comparison of the Authority's income and the contractor's internal rates of return, but they assume a mining operation financed with 100 per cent equity which pays United States taxes after sharing with the Authority, and which has a 25-year period of commercial production and not 20 years. For these reasons, the figures are not directly comparable with those reported in document NG2/12/Rev.1.[33] The internal rates of return would be higher by about one to three percentage points in the different cases if national taxes were not levied. The internal rates of return would also differ if debt-equity ratio was 1:1.

Case C is the original Massachusetts Institute of Technology baseline set of assumptions. Case A represents a low-profit situation with higher costs and lower ore grade (development costs and operating costs are increased by 25 per cent, research and development costs are increased to $150 million, and ore grade is reduced to 2.4 per cent). Case B is the same as case A but with metal prices increasing 1 per cent per year. Case D increases metal prices to near-current levels and the original Massachusetts Institute of Technology baseline costs. Case E is the same as case D except that the original Massachusetts Institute of Technology baseline development and operating costs are increased by 25 per cent and prices are allowed to increase by 2.5 per cent per year. Case F is the same as case E but with the original MIT baseline cost estimates.

[33] *Ibid.*, vol. XI (United Nations publication, Sales No. E.80.V.6), document A/CONF.62/C.1/L.22, annex III.

Table 1 in annex E shows payments to the Authority under the mixed system which are from about $260 million to about $2 billion as the contractor's internal rates of return range from about 6 per cent to 24 per cent. In the baseline case, payments to the Authority are $574 million. Under the single system, payments range from about $527 million to about $1.3 billion with payments in the baseline case equal to $599 million. The contractor's internal rates of return range from about 5 per cent to 25 per cent.

Case E represents the situation in which the original baseline price and cost estimates are revised to reflect more current values, and metal prices are allowed to increase 2.5 per cent per year. Some observers believe this case to be more realistic. Payments to the Authority in case E would be $1,792 million under the mixed system and $1,312 million under the single system.

Table 2 in annex E compares three proposals, namely my new proposal, the proposal contained in the revised negotiating text and the proposal by the United States.

ANNEX A

DEBT-EQUITY RATIOS OF MINING COMPANIES

	1958	1963	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Australia												
BHP	—	—	20/80	22/78	20/80	19/81	23/77	20/80	17/83	22/78	25/75	17/83
Western M	—	—	—	—	31/69	19/81	13/87	16/84	23/77	41/59	41/59	36/64
Canada												
Alcan	58/42	58/42	45/55	45/55	47/53	46/54	47/53	44/56	45/55	47/53	40/60	34/66
Falconbridge	4/96	1/99	1/99	1/99	1/99	50/50	56/44	50/50	47/53	45/55	41/59	43/57
Inco	—	—	16/84	16/84	21/79	30/70	28/72	25/75	28/72	29/71	35/65	35/65
Noranda	18/82	5/95	40/60	32/68	35/65	42/58	42/58	37/63	36/64	43/57	46/54	44/56
Sherrit G	—	—	26/74	26/74	21/79	14/86	32/68	32/68	25/75	22/78	19/81	34/66
France												
Imetal	—	—	—	—	—	—	—	—	—	18/82	17/83	16/84
Pechiney	—	—	32/68	25/75	35/65	—	46/54	46/54	45/55	50/50	54/46	54/46
Germany, Federal Republic of												
Metallgesell.	—	—	52/48	57/43	57/43	62/38	59/41	58/42	53/47	56/44	55/45	52/48
Preussag	—	—	—	—	—	—	—	63/37	56/44	56/44	53/47	59/41
Japan												
Mitsubishi	—	—	44/56	41/59	48/52	55/45	61/39	60/38	62/36	71/29	77/23	78/22
Mitsui	—	—	50/50	57/43	59/41	58/42	62/38	62/38	63/37	62/38	67/33	70/30
Nippon H	—	—	63/37	61/39	67/33	64/36	70/30	72/28	72/28	76/24	76/24	76/24
Sumitomo	—	—	44/56	49/51	47/53	55/45	65/35	61/39	61/39	67/33	73/27	73/27
South Africa												
Anglo	—	5/95	4/96	11/89	11/89	11/89	15/85	12/88	11/89	12/88	11/89	16/84
Sweden												
Boliden	—	—	33/67	28/72	46/54	51/49	52/48	53/47	53/47	62/38	67/33	70/30
Switzerland												
Alusuisse	—	—	29/71	38/62	38/62	44/56	50/50	45/55	50/50	56/44	53/47	52/48
United Kingdom												
Goldfields	7/93	28/72	33/67	42/58	38/62	34/66	30/70	30/70	29/71	22/78	24/76	27/73
RTZ	16/84	28/72	40/60	39/61	46/54	56/44	52/48	46/54	44/56	46/54	48/52	48/52
Selection T	—	—	—	—	—	—	7/93	19/81	33/67	39/61	41/59	31/69
United States												
Amax	6/94	20/80	28/72	25/75	28/72	36/64	39/61	34/66	29/71	28/72	29/71	29/71
Asarco	—	11/89	5/95	4/96	3/97	5/95	7/93	11/89	12/88	28/72	32/68	33/67
Anaconda	10/90	9/91	20/80	21/79	24/76	32/68	22/78	19/81	18/82	22/78	27/73	27/73
Alcoa	40/60	32/68	38/62	39/61	41/59	43/57	40/60	39/61	38/62	44/56	41/59	39/61
Bethlehem	9/91	7/93	16/84	18/72	23/77	22/78	23/77	23/77	21/79	25/75	28/72	35/65
Hanna M.	—	—	17/83	14/86	11/89	11/89	11/89	12/88	16/84	9/91	7/93	10/90
Kaiser	60/40	48/52	50/50	45/55	44/56	48/52	48/52	48/52	49/51	47/53	46/54	43/57
Kennecott	1/99	1/99	19/81	15/85	13/87	21/79	18/82	14/86	14/86	22/78	28/72	27/73
Newmont	—	—	—	11/89	19/81	30/70	31/69	28/72	25/75	28/72	31/69	34/66
Phelps D.	—	—	5/95	14/86	12/88	19/81	20/80	26/74	27/73	37/63	39/61	37/63
Reynolds	53/47	44/56	56/44	55/45	53/47	56/44	58/42	57/43	55/45	51/49	50/50	46/54
St. Joe	24/76	16/84	9/91	8/92	7/93	6/94	16/84	18/82	11/89	9/91	9/91	13/87
Texasgulf	—	—	30/70	26/74	26/74	33/67	34/66	28/72	21/79	28/72	26/74	33/67
Union C.	35/65	28/72	35/65	34/66	34/66	33/67	32/68	31/69	26/74	32/68	34/66	32/68
US Steel	14/86	19/81	32/68	29/71	29/71	29/71	30/70	27/73	23/77	24/76	28/72	31/69

ANNEX B

PROPOSAL BY NORWAY ON ANNEX II, ARTICLE 12, PARAGRAPH 6

6. If a contractor chooses to make his financial contribution to the Authority by paying a combination of a production charge and a share of net proceeds, such payments shall be determined as follows:

(*a*) The production charge shall be fixed at a percentage of the market value of the processed metals produced from the nodules extracted from the contract area in accordance with the following schedule:

(i) First period of commerical production: 2 per cent

(ii) Second period of commercial production: 4 per cent

(*b*) The said market value shall be the product of the quantity of the processed metals and the average price for those metals during the relevant accounting year. The average price shall be determined in accordance with paragraphs 7 and 8.

(*c*) The Authority's share of net proceeds shall be taken out of an amount equal to 20 per cent of the contractor's net proceeds for the first period of commercial production and 40 per cent for the second period of commercial production to represent the net proceeds attributable to mining of the resources of the contract area. This amount shall be referred to hereinafter as the attributable net proceeds.

(*d*) The Authority's share of attributable net proceeds shall be determined in accordance with the following schedule:

(i) First period of commercial production: 40 per cent

(ii) Second period of commercial production: 75 per cent

This latter percentage shall not be applicable if the net profit of the mining of the resources in an area is less than 10 per cent.[34]

(*e*) The first period of commercial production referred to in subparagraphs (*a*) and (*d*) shall commence in the first year of commercial production and terminate in the year in which the contractor's total net proceeds plus his recovery of development costs less his payments to the Authority in the form of share of attributable net proceeds in the preceding accounting years are equal to twice the development costs incurred prior to the commencement of commercial production. The second period of commercial production referred to in subparagraphs (*a*) and (*d*) shall commence in the following accounting year and continue until the end of the contract.

ANNEX C

DETERMINATION OF THE TAX BASE FOR THE AUTHORITY

1. In the absence of a competitive market for nodules, the net proceeds of an integrated operation would need to be divided between the mining sector and the processing sector. This note deals with:

(i) The methods of determining the net proceeds of the mining sector, i.e., the Authority's tax base;

(ii) The implications of these methods.

2. Annual gross proceeds from the sale of metals processed from the nodules mined from the area are, in the accounting sense,

= Operating costs in the processing sector
+ Annual recovery of development costs in the processing sector
+ Return on development costs in the processing sector
+ Operating costs in the mining sector
+ Annual recovery of development costs in the mining sector
+ Return on development costs in the mining sector
+ "x" (a positive or negative amount reflecting other market factors).

As is evident from this schematic presentation, net proceeds of the integrate operation will be the sum of return on development costs in the processing sector and in the mining sector, and "x". The tax base of the Authority is return on development costs in the mining sector + "x", or the portion thereof assigned to the mining sector.

Of the accounting items above, gross proceeds, operating costs in the processing sector, recovery of development costs in the processing sector, operating costs in the mining sector, and recovery of development costs in the mining sector are directly ascertainable. Return on development costs in the processing sector and in the mining sector and "x" are not directly ascertainable and depend for their values on judgement. Hence, the problem of assignment of net proceeds to each of the two sectors arises.

3. There are several methods to deal with the problem, four of which are described below:

(*a*) Predetermined constant ratio;

(*b*) Ratio of development costs in the mining sector to total development costs;

(*c*) Net-back;

(*d*) Cost-plus.

4. Predetermined constant ratio

Tax base

= Predetermined constant ratio multiplied by total net proceeds.

Total net proceeds

= Gross proceeds
− Operating costs in the processing sector
− Annual recovery of development costs in the processing sector
− Operating costs in the mining sector
− Annual recovery of development costs in the mining sector
= Return on development costs in the processing sector
+ Return on development costs in the mining sector
+ "x"

The predetermined constant ratio is a negotiated figure aimed at assigning as great a portion of "x" as feasible to the mining sector, consistent with a reasonable return on development costs in order to ensure a fair value to the nodules. The value "x" is calculated on the basis of specific financial outcome.

(i) This method places a value on the nodules.

(ii) The Authority is assured of a stable tax base. This is one of the three factors accounting for the stability of the Authority's income. The other two factors are the actual financial outcome and the tax rate.

(iii) Risk-sharing by the mining sector is predetermined, as it is based on the estimated financial outcome. Actual financial outcome may not conform to the assumptions. The actual ratio may turn out to be higher or lower than the predetermined constant ratio. If higher, the Authority's tax base, as calculated above, is lower. If lower, the tax base of the national taxing authority is lower, and the contractor's tax burden may be higher.

5. The ratio of development costs in the mining sector to total development costs

$$\text{Tax base} = \text{Ratio of } \frac{\text{Development costs in the mining sector}}{\text{Development costs in the processing sector and in the mining sector}} \times \text{Total net proceeds}$$

The ratio is applied to total net proceeds to obtain the net proceeds in the mining sector. "x" is assigned to both sectors according to this ratio.

(i) Under this method the value of the nodules is assigned to both sectors proportionately.

(ii) Development costs in each sector earn the same rate of return, and hence this method does not favour investments in either the mining sector or the processing sector.

(iii) Risk is shared proportionately by both the sectors. Risk borne is based on actual outcomes, not estimates.

(iv) The ratio may vary from project to project and, thus, the Authority has a less stable tax base compared with the first method.

(v) According to the Massachusetts Institute of Technology baseline case and the European base case, the ratio will be lower than in annex II, article 12 of the revised negotiating text.

6. Net-back

Tax base

= Gross proceeds
− Operating costs in the processing sector
− Agreed return on development costs in the processing sector
− Annual recovery of development costs in the processing sector
− Operating costs in the mining sector

[34] The 40 per cent tax (on 40 per cent of attributable net proceeds) would apply. An alternative would be a formulation whereby in the second period a 40 per cent tax should always apply to the first 10 per cent of the profit and 75 per cent to additional profits. My proposal referred to the first solution, not the alternative.

– Annual recovery of development costs in the mining sector
= Return on development costs in the mining sector
+ "x"

Under this method, "x" is assigned to the mining sector.

(i) As the payments in the processing sector are assured, changes in gross proceeds affect the mining sector only. The risk resulting from changes in gross proceeds is borne by the mining sector. Consequently, net proceeds in the mining sector are subject to fluctuations in gross proceeds. The tax base of the Authority is the least stable.

(ii) Depending on the agreed rate of return on development costs in the processing sector, the tax base may be the highest in good years and the lowest in bad years, compared with other methods.

(iii) The impact on the investment decisions in the processing sector is minimal.

7. Cost-plus

Tax base
= Agreed return on development costs in the mining sector
Gross proceeds
– Operating costs in the processing sector
– Recovery of development costs in the processing sector
– Operating costs in the mining sector
– Recovery of development costs in the mining sector
– Agreed return on development costs in the mining sector
= Return on development costs in the processing sector
+ "x"

"x" is assigned to the processing sector. This is the converse of the net-back method.

(i) As the payments in the mining sector are assured, changes in gross proceeds affect the processing sector only. The risk resulting from changes in gross proceeds is borne by the processing sector. The mining sector bears no risk and net proceeds in the mining sector do not vary with gross proceeds.

(ii) The Authority has a stability of tax base compared with other approaches.

(iii) The impact on the investment decisions in the mining sector is minimal.

ANNEX D

AN ALTERNATIVE SCHEME OF TAXATION: VARIABLE INCIDENCE

1. In order to ensure that the Authority's share of the net proceeds will be maximized throughout the life of the project, the system of taxation should respond to the financial outcome of sea-bed mining; that is, a system in which the incidence of taxation (or tax burden) will rise or fall with corresponding changes in annual net proceeds. The system should provide that the contractor's share of the net proceeds is not less than the "opportunity" cost of the capital he would tie up in sea-bed mining in order that he does not select another investment as preferable. At the same time, the system should limit the contractor's net proceeds to no more than would otherwise be needed to attract his investment, so that the Authority's share is maximized.

2. The uncertainty of the financial outcome of sea-bed mining and the likely difficulty in implementing changes in the financial terms of the contract, which might be desirable in light of any re-evaluation of the project, complicate any effort to arrive at a single correct tax rate. This tax rate, if it could be devised, would achieve the dual objectives of maximizing the Authority's share of the net proceeds and of encouraging investments in sea-bed mining at a level of return to the contractor no higher than necessary to undertake the investment. Yet there is a great risk that a single tax rate would be either too low, in which case the Authority's share of net proceeds would fall below what it could obtain and still attract investment, or too high, and thus discourage investment in sea-bed mining. It is likely that in view of the uncertain financial outcome of sea-bed mining, a rate of taxation appropriate to a low financial outcome would be chosen to safeguard the viability of investment in case such an outcome results. In the event that the outcome was more favourable, under the single low rate chosen, the Authority's share of income would be adversely affected.

3. Under a single tax rate, the Authority also runs the risk of failing to capture additional revenue from more profitable operations. For example, with a single tax rate system, if there were two mining operators, one whose net proceeds were low and the other whose net proceeds were high, both would pay at the same rate to the Authority. Yet the Authority could impose a high tax rate on the contractor whose net proceeds were higher without discouraging him from investing in the area.

4. The "trigger" clause under the mixed system of financial arrangements (A/CONF.62/WP.10/Rev.1, annex II, art. 12, para. 6 (*e*)) addresses this issue from the perspective of protecting the contractor from a higher tax incidence if his returns are low. But its impact on the Authority's share is uncertain because the timing of the increase from the low to the high rate could materially alter the financial outcome of the project. As such, the Authority's share might be less than it needs to be. Moreover, it is possible for a project to achieve a more-than-adequate over-all return before 200 per cent of development costs are recovered—a situation in which the Authority's share would continue needlessly to be taken at a low rate. If recovery of 200 per cent of development costs occurs late in a project's life, however, the over-all return to the contractor may be unacceptably low even to withstand higher sharing rates. From the perspective of either party, therefore, this mechanism can be improved. Of course, any such "trigger" clause fails to respond to annual changes in profitability.

5. An effective way of dealing with the uncertain financial outcome of sea-bed mining, while at the same time achieving the objectives of maximizing the Authority's share of net proceeds and of ensuring investment in the area, is to devise a system of taxation which will respond to annual changes in net proceeds of any one operation as well as to different annual levels of net proceeds among individual contractors. Such a system would ensure that when annual net proceeds were high, the tax burden would be higher than when annual net proceeds were low. It would also ensure that, in any one year, contractors whose net proceeds were higher than other contractors would contribute relatively more to the Authority's share of net proceeds.

6. The rate of tax which determines the Authority's share of net proceeds will be subject to the constraint of maintaining incentives to invest in the area by ensuring that the return to the contractor is not less than the "opportunity" cost of his money. This objective will be achieved if the tax payments to the Authority are structured so that, when the contractor's over-all profitability is low, these payments result in a small reduction in the profitability of the project, whereas when the over-all profitability of the project is high, these payments substantially reduce its profitability. The effective level of taxation will thus vary with the over-all level of profitability.

7. Since the over-all profitability of the project can be evaluated only in the context of the whole financial history of the project, some care needs to be taken in determining rates of incidence and their timing. This can be achieved by the use of two complementary mechanisms: first, by having two schedules for sharing net proceeds, one to apply before over-all project profitability approaches a threshold level, and the other, higher schedule to apply subsequently; secondly, by having both rate schedules vary with annual profitability. The first mechanism would help to ensure that higher sharing rates would apply to a project when it had achieved an acceptable threshold internal rate of return. The second mechanism of variable rates would ensure that annual payments would apply progressively with annual returns.

8. The over-all economic status of a project is best measured by the extent to which its capital is recovered, taking into account its "opportunity cost", or the rate of return forgone by capital tied up in the project. This will be achieved by signalling the second higher sharing schedule to come into effect once the project's cash flow is sufficient to recover the development costs with a minimum required rate of interest.

9. In both cases, payments to the Authority will be maximized. In the first case, before the recovery of the cost of development, the Authority's share will increase as net proceeds increase. Where different contractors' net proceeds vary, they will be taxed in accordance with their ability to pay. Contractors whose net proceeds are higher than those of other countries will pay more in both proportional and absolute terms.

10. After the costs of tied-up capital are recovered, higher rates will apply. The reason for higher rates is that having recovered his tied-up capital with interest, the contractor's risk project is minimized. As such, the contractor's share of net proceeds could be less than it was before recovery of development costs. Thus, this

part of the financial arrangements would not have a negative impact on his investment planning. Moreover, after capital recovery, the contractor would have received the internal rate of return, equal to the interest rate used. Subsequent additions to that internal rate of return, though a significant and necessary element in the over-all profitability of the project, are less critical once the risk of a return less than the interest rate has been reduced.

11. The incidence of tax would apply to the contractor's net proceeds arising from the exploitation of resources in the area. The appropriate rate of incidence would depend on the success of his undertaking and would be calculated annually. A measure which is likely to reflect the success of the investment is a ratio of the contractor's "cash surplus" to his development costs. While net proceeds alone are a more frequently used and a more direct measure of profitability, their use in evaluating the outcome of sea-bed mining is limited, at least in the initial stages, because of the uncertainties of development costs, and other capital requirements. Hence, there is a need to use a measure related to development costs.

ANNEX E

TABLE 1. MONETIZATION OF THE PROPOSED TAX SYSTEMS

	Mixed system			*Single system*	
Case	*Payments ($ millions)*	*Internal rates of return (percentage)*	*First year of second period (year)*	*Payments ($ millions)*	*Internal rates of return (percentage)*
A	258	6.1	—	527	5.1
B	429	8.5	20	638	7.9
C	574	13.8	8	599	13.9
D	1 015	19.5	5	807	20.1
E	1 792	20.2	6	1 312	20.9
F	1 964	23.9	5	1 312	25.0

TABLE 2. COMPARATIVE TABLE FOR THE AUTHORITY'S INCOME AND CONTRACTOR'S INTERNAL RATES OF RETURN UNDER THE MIXED SYSTEM

	Document WG21/2		*Informal composite negotiating text*		*United States proposal August 1979*	
Case	*Authority's income ($ millions)*	*Contractor's internal rates of return (percentage)*	*Authority's income ($ millions)*	*Contractor's internal rates of return (percentage)*	*Authority's income ($ millions)*	*Contractor's internal rates of return (percentage)*
A	258	6.1	455	5.7	141	6.5
B	429	8.5	745	7.9	203	8.9
C	574	13.8	882	13.2	372	14.5
D	1 015	19.5	1 464	18.6	641	20.4
E	1 792	20.2	2 484	19.4	1 103	21.0
F	1 964	23.9	2 696	23.0	1 185	25.0

III. SYSTEM OF EXPLORATION AND EXPLOITATION

The Chairman of negotiating group 1 on the system of exploration and exploitation still considers that definitive answers to the questions of who will exploit the area and how the area will be exploited are to be found not very far from the solutions he previously proposed in formulae now incorporated in the revised negotiating text. Indeed, although in the new proposal now submitted, some amendments have been introduced and some new provisions added, the essential characteristics of the system have been kept unchanged. These amendments and additions refer to very specific points and either improve the draft without altering the substance or develop some ideas that were summarily mentioned in the text.

All the amended provisions but one belong to annex II. The exception is article 140 of the convention on the principle of the benefit of mankind into which it was decided to insert a reference to General Assembly resolution 1514 (XV) and other General Assembly resolutions relevant to the question of peoples who have not attained full independence or other self-governing status. This inclusion was proposed by the delegation of Qatar on behalf of the Arab group towards the end of the first part of this session. The proposal has been endorsed by the Group of 77. It is believed that this addition to article 140 reflects the wishes of the overwhelming majority of the group of 21. It must be added that, in the opinion of some representatives, the question of implementation of this provision is a problematic one and will require careful scrutiny at the next stage of the negotiations.

Concerning the provisions of annex II, at the beginning of the deliberations at this resumed session it was proposed to this group, and accepted, that the discussions be confined to the following issues:

(1) (*a*) Training of personnel (art. 2, para. 1 (*b*));

(*b*) Right of the Authority to close a particular sector of the area (art. 2, para. 1 (*d*));

(2) Scope of the undertaking by the applicant concerning transfer of technology which he is not entitled to transfer and which is not available on the open market (art. 5, para. 2);

(3) Procedure in case of failure of negotiations concerning terms and conditions of transfer of technology (art. 5, para. 2);

(4) Transfer of processing technology (art. 5, para. 3);

(5) Anti-monopoly clause (arts. 6 and 7);

(6) Priority given to the Enterprise when competing with other applicants for contracts (art. 7, para. 4);

(7) Undertaking by the applicant concerning transfer of data necessary to assess value of the sites (art. 8);

(8) Joint arrangements (art. 10);

(9) Applicability of annex II to the activities conducted by the Enterprise (art. 11);

(10) Scope of undertaking by contractor to transfer data to the Authority (art. 13);

As a result of the discussions and of the informal consultations changes were introduced in articles 1 to 4, 6, 8 and 10 and 13 of annex II.

The new draft of article 1 on title to minerals is a drafting change and seems to be more general without affecting its substance. It also makes it clear that title would also pass to the Enterprise as well as to the prospector with respect to the samples collected, in accordance with the relevant provisions. In article 2, paragraph 1 (*b*), it was decided to replace the reference of the training of personnel nominated by the Authority by a reference to articles 143 and 144 which deal respectively with marine scientific research and transfer

of technology. Article 2 of annex II, dealing with prospecting, is not the right place to set forth the obligations related to training of personnel. What is necessary is to indicate the scope of the obligations of the prospector with respect to training, which is dealt with in articles 143 and 144. It was not necessary to establish a separate or new obligation in this provision but it would be sufficient to provide for the co-operation of the prospector in the training programmes so that the personnel of the Authority and the developing countries would be able to acquire prospecting skills.

Since the nature of prospecting activities is such that it is unlikely to have such major effects as to cause irreparable harm to the marine environment or interfere seriously with other uses of the area, the Chairman of negotiating group 1 decided to delete the provision in paragraph 1 (*d*) of the same article. The protection of the marine environment as well as the accommodation of different activities in the area are matters which have been taken care of in other provisions of the convention dealing particularly with operations of exploration and exploitation which are likely to have a greater impact on the environment.

In article 3, two new paragraphs were added, namely paragraphs 1 and 2. These new paragraphs deal with the presentation of plans of work by the Enterprise or other entities. The addition of these provisions was necessary as a general introduction to the other provisions of the same article since they refer to the first steps in a sequence developed in the other paragraphs of article 3 and in the following articles. Paragraph 2 states clearly and categorically that the Enterprise may apply for a plan of work in respect of any part of the area, either reserved or non-reserved. In light of this change, the saving clause in article 8, paragraph 4, of the annex is no longer necessary. The amendment in paragraph 4 (*c*) of the same article was made to delimit the scope of the exclusive right conferred on the operator.

Also for the sake of clarification, the word "qualification" was added before "standards" in article 4, paragraph 1. The amendment in paragraph 4 of the same article is a consequence of the addition made in paragraph 1. Paragraphs 2 and 3 are new and deal with the question of sponsorship of applicants by States parties, a question that until now was mentioned briefly in the text without providing any detail. In these two paragraphs general rules are set forth on sponsorship of national and multinational entities and on responsibility of the sponsors. It is hoped that these new additions will command general acceptance since they fill a lacuna in the existing text. However, it should be pointed out that some delegations have serious reservations about the need to have such provisions at all.

Article 6, paragraph 3, on the procedures to be followed by the Authority after receiving the proposed plan of work, has been amended to clarify its meaning. No other changes have been made to this article.

In article 8, relating to the reservation of sites, some amendments were introduced in order to ensure that the Authority would obtain all the data necessary to make the right decision on the selection of the reserved site. There is a new sentence, according to which the Authority may request an independent expert to assess whether the applicant submitted all data required. It has been considered convenient to separate into two different articles the provisions of article 8 in the revised negotiating text. The existing and new provisions dealing with the conditions under which activities in reserved sites will be carried out are grouped in a new article (art. 8 *bis*). Paragraphs 1 and 4 of this new article are to clarify the process according to which the Enterprise shall decide whether it will carry out activities in the reserved site and the extent to which developing countries may have access to the reserved sites if the Enterprise decides not to exploit the sites itself or in joint ventures with such countries. The new paragraph 2 deals with the conclusion of contracts by the Enterprise for the execution of parts of its activities, as well as entry into joint ventures with other entities on a voluntary basis. The matters dealt with in the new paragraphs 2, 3 and 4 are quite complex and in many respects delicate, and consequently further discussions on these matters may be required.

In article 10, the introduction of the words "when the parties so agree" in paragraph 1 has been made in order to stress the voluntary character of joint arrangements between the contractor and the Authority. Paragraph 3 is a new one and establishes the obligation of the partners of the Enterprise in joint ventures in reserved sites to pay the financial contributions required by article 12 to the extent of their share, subject to financial incentives as provided for in article 12.

The new wording of article 13, paragraph 3, appears in document WG21/2. The amendments introduced in this provision are meant to make more precise the responsibilities of the Authority and the Enterprise concerning the disclosure of proprietary data.

Unfortunately, the group could not deal extensively with other important matters still pending, the consideration of which would have required more time and additional negotiations. One of these matters is the problem of transfer of technology. Although during the last two sessions of the Conference tremendous progress was made in this field, some delegations consider that the present text, in particular article 5 of annex II, does not provide a totally satisfactory solution to the problem and that we have to work out such provisions in order to make the undertaking of the contractors more specific and mandatory. However, no one gave any concrete proposals on these matters and, therefore, detailed discussions on the issues could not be conducted.

It is hoped that the next session of the Conference will provide the opportunity to make a last attempt to find a solution on this matter acceptable to all sectors concerned.

With regard to the anti-monopoly clause, the delegation of France submitted to the group a proposal suggesting a new wording for article 6, paragraphs 3 and 4, and article 7, paragraphs 2 and 3. This proposal and an explanatory note are contained in document WG21/Informal Paper 3, of 10 August 1979. Since the proposal deals in part with a technical subject which is extremely complex, there was not sufficient time to examine it and discuss it thoroughly. Another opportunity will be provided to take up this matter in the future.

The question of the moratorium in case of failure of the review conference to reach an agreement within five years was not considered by the group during the resumed session. Since this is a very important problem and also because of the polarization of the positions of the delegations on this issue, it was proposed to the group to leave this matter to be treated either in a forum broader than the group of 21 or in any case at a later stage after other, less intractable issues have been dealt with.

APPENDIX A

Suggestions resulting from consultations held by the Chairman and co-ordinators of the working group of 21*

A. System of exploration and exploitation

Article 140. Benefit of mankind

1. Activities in the Area shall be carried out for the benefit of mankind as a whole, irrespective of the geographical location of States, whether coastal or land-locked, and taking into particular consideration the interests and needs of the developing countries and peoples who have not attained full independence or other self-governing status recognized by the United Nations in accordance with General Assembly resolution 1514 (XV) and other relevant General Assembly resolution as specifically provided for in this Part of the present Convention.

Annex II

Article 1. Title to minerals

1. Title to minerals shall pass upon recovery in accordance with the present Convention.

Article 2. Prospecting

1. (*a*) The Authority shall encourage the conduct of prospecting in the Area.

(*b*) Prospecting shall be conducted only after the Authority has received a satisfactory written undertaking that the proposed prospector shall comply with the present Convention and the relevant rules and regulations of the Authority concerning protection of the marine environment, co-operation in training programmes according to articles 143 and 144 and accepts verification by the Authority of compliance. The proposed prospector shall, together with the undertaking, notify the Authority of the broad area or areas in which prospecting is to take place.

(*c*) Prospecting may be carried out by more than one prospector in the same area or areas simultaneously.

(*d*) [*Deleted*]

2. Prospecting shall not confer any preferential, proprietary, exclusive or any other rights on the prospector with respect to the

*Document WG21/2.

resources. A prospector shall, however, be entitled to recover a reasonable amount of resources of the Area to be used for sampling.

Article 3. Exploration and exploitation

1. The Enterprise, States Parties, and the other entities referred to in article 153, paragraph 2 (*b*), may apply to the Authority for approval of plans of work covering exploration and exploitation of resources of the Area.

2. The Enterprise may apply with respect to any part of the Area, but applications by others with respect to reserved areas are subject to the additional requirements of article 8.

(Formerly para. 1) 3. Exploration and exploitation shall be carried out only in areas specified in plans of work referred to in article 153, paragraph 3, and approved by the Authority in accordance with the provisions of this annex and the relevant rules, regulations and procedures of the Authority.

(Formerly para. 2) 4. Every plan of work approved by the Authority shall:

(*a*) Be in strict conformity with the present Convention and the rules and regulations of the Authority;

(*b*) Ensure control by the Authority of activities in the Area in accordance with article 153, paragraph 4;

(*c*) Confer on the operator exclusive rights for the exploration and exploitation of the specified categories of resources in the area covered by the plan of work in accordance with the rules and regulations of the Authority. If the applicant presents a plan of work for one of the two stages only, the plan of work may confer exclusive rights with respect to such a stage.

(Formerly para. 3) 5. Except for plans of work proposed by the Enterprise, each plan of work shall take the form of a contract to be signed by the Authority and the operator or operators upon approval of the plan of work by the Authority.

Article 4. Qualifications of applicants

1. Applicants, other than the Enterprise, shall be qualified if they have the nationality or control and sponsorship required by article 153, paragraph 2 (*b*), and if they follow the procedures and meet the qualification standards established by the Authority by means of rules, regulations and procedures.

2. Sponsorship by the State Party of which the applicant is a national shall be sufficient unless the applicant has more than one nationality, as in the case of a partnership or consortium of entities from several States, in which event all States Parties involved shall sponsor the application, or unless the applicant is effectively controlled by another State Party or its nationals, in which event both States Parties shall sponsor the application.

3. The sponsoring State or States shall, pursuant to article 139, have the responsibility to ensure, within their legal systems, that a contractor so sponsored shall carry out activities in the Area in conformity with its obligations under the present Convention and the terms of its contract. A sponsoring State shall not, however, be liable for damage caused by any failure of a contractor sponsored by it to comply with its obligations if that State Party has enacted legislation and provided for administrative procedures which are, within the framework of its legal system, reasonably appropriate for securing compliance by persons under its jurisdiction.

(Formerly para. 2) 4. Except as provided in paragraph 6, such qualification standards shall relate to the financial and technical capabilities of the applicant and his performance under previous contracts with the Authority.

(Formerly para. 3) 5. The procedures for assessing the qualifications of States Parties which are applicants shall take into account their character as States.

(Formerly para. 4) 6. The qualification standards shall require that every applicant, without exception, shall, as part of his application, undertake:

(*a*) To accept as enforceable and comply with the applicable obligations created by the provisions of Part XI, rules and regulations of the Authority, decisions of the organs of the Authority, and terms of his contracts with the Authority;

(*b*) To accept control by the Authority of activities in the Area, as authorized by the present Convention;

(*c*) To provide the Authority with a written assurance that his obligations under the contract will be fulfilled in good faith;

(*d*) To comply with the provisions on the transfer of technology set forth in article 5 of the present annex.

Article 6. Approval of plans of work submitted by applicants

1. Six months after the entry into force of the present Convention, and thereafter each fourth month, the Authority shall take up for consideration proposed plans of work.

2. When considering an application for a contract with respect to exploration and exploitation, the Authority shall first ascertain whether:

(*a*) The applicant has complied with the procedures established for applications in accordance with article 4 of the present annex and has given the Authority the commitments and assurances required by that article. In cases of non-compliance with these procedures or of absence of any of the commitments and assurances referred to, the applicant shall be given 45 days to remedy such defects;

(*b*) The applicant possesses the requisite qualifications pursuant to article 4.

3. All proposed plans of work shall be dealt with in the order in which they were received, and the Authority shall conduct, as necessary and as expeditiously as possible, an inquiry into their compliance with the terms of the present Convention and the rules, regulations, and procedures of the Authority, including the operational requirements, the financial contributions and the undertakings concerning the transfer of technology. As soon as the issues under investigation have been settled, the Authority shall approve such plans of work, provided that they conform to the uniform and non-discriminatory requirements established by the rules, regulations, and procedures of the Authority, unless:

(*a*) Part or all of the proposed area is included in a previously approved plan of work or a previously submitted proposed plan of work which has not yet been finally acted on by the Authority;

(*b*) Part or all of the proposed area is disapproved by the Authority pursuant to article 162, paragraph 2 (*w*);

(*c*) Selection among applications received during that period of time is necessary because approval of all plans of work proposed during that period would be contrary to the production limitation set forth in article 151, paragraph 2, or to the obligations of the Authority under a commodity agreement or arrangement to which it has become a party, as provided for in article 151, paragraph 1;

(*d*) The proposed plan of work has been submitted or sponsored by a State Party which has already had approved:

(*i*) Three plans of work for exploration and exploitation of sites not reserved pursuant to article 8 of the present annex within a circular area of 400,000 square kilometres which is centred upon a point selected by the applicant within the requested additional site;

(*ii*) Plans of work for exploration and exploitation of sites not reserved pursuant to article 8 which in aggregate size constitute 3 per cent of the total sea-bed Area which is not reserved pursuant to that article or otherwise withdrawn by the Authority from eligibility for exploitation pursuant to article 162, paragraph 2 (*w*).

4. For the purpose of the standard act set forth in paragraph 3 (*d*) above, a plan of work proposed by a consortium shall be counted on a *pro rata* basis among the States Parties whose nationals compose the consortium. The Authority may approve plans of work covered by paragraph 3 (*d*) if it determines that such approval would not permit a State Party or persons sponsored by it to monopolize the conduct of activities in the Area or to preclude other States Parties from activities in the Area.

Article 8. Reservation of sites

Each application, other than those proposed by the Enterprise or by any others for reserved sites, shall cover a total area, which need not be a single continuous area, sufficiently large and of sufficient estimated commercial value to allow two mining operations. The proposed operator shall indicate the co-ordinates dividing the area into two parts of equal estimated commercial value and submit all the data obtained by him with respect to both parts of the area. Within 45 days of receiving such data the Authority shall designate the part which is to be reserved solely for the conduct of activities by the Authority through the Enterprise or in association with developing countries. This designation may be deferred for a further period of 45 days if the Authority requests an independent expert to assess whether all data required by this article has been submitted to the Authority. The area designated shall become a reserved area as soon

as the plan of work for the non-reserved area is approved and the contract is signed.

Article 8 bis. *Activities in reserved sites*

1. The Enterprise shall be given an opportunity to decide whether it intends to carry out activities in each reserved site. This decision may be taken at any time, unless a notification pursuant to paragraph 4 is received by the Authority, in which event the Enterprise shall take its decision within a reasonable time. The Enterprise may decide to exploit such sites in joint ventures with the interested State or entity.

2. The Enterprise may conclude contracts for the execution of part of its activities in accordance with article 11 of annex III. It may also enter into joint ventures for the conduct of such activities with any willing entities which are eligible to carry out activities in the Area pursuant to article 153, paragraph 2 (*b*). When considering such joint ventures, the Enterprise shall offer to States Parties which are developing countries and their nationals the opportunity of effective participation.

3. The Authority may prescribe, in the rules, regulations, and procedures of the Authority, procedural and substantive requirements with respect to such contracts and joint ventures.

4. Any State Party which is a developing country or any national entity sponsored by it which is a qualified applicant or any group of the foregoing, may notify the Authority that it wishes to apply for a plan of work pursuant to article 6 of the present annex with respect to a reserved site. The plan of work shall be considered if the Enterprise decides, pursuant to paragraph 1 above, that it does not intend to carry out activities in that site.

Article 10. Joint arrangements

1. Contracts for the exploration and exploitation of the resources of the Area may provide for joint arrangements, when the parties so agree, between the Contractor and the Authority through the Enterprise, in the form of joint ventures, production sharing or service contracts, as well as any other form of joint arrangement for the exploration or exploitation of the resources of the Area.

2. Contractors entering into such joint arrangements with the Enterprise may receive financial incentives as provided for in the financial arrangements established in article 12 of the present annex.

3. Joint venture partners of the Enterprise in the reserved sites shall be liable for the payments required by article 12 of the present annex to the extent of their joint venture share, subject to financial incentives as provided for in article 12.

Article 13. Transfer of data

1. The operator shall transfer in accordance with the rules and regulations and the terms and conditions of the plan of work to the Authority, at time intervals determined by the Authority, all data which are both necessary and relevant to the effective implementation of the powers and functions of the principal organs of the Authority in respect of the area covered by the plan of work.

2. Transferred data in respect of the area covered by the plan of work, deemed to be proprietary, may only be used for the purposes set forth in this article. Data which are necessary for the promulgation of rules and regulations concerning protection of the marine environment and safety shall not be deemed to be proprietary.

3. Data transferred to the Authority by prospectors, applicants for contracts for exploration and exploitation, and contractors deemed to be proprietary shall not be disclosed by the Authority to the Enterprise or outside of the Authority. Such data transferred by such persons to the Enterprise shall not be disclosed by the Enterprise to the Authority or outside of the Authority. The responsibilities set forth in article 168, paragraph 2, are equally applicable to the staff of the Enterprise.

B. Financial arrangements

1. Financial terms of contract

Annex II

Article 12

1. In adopting rules, regulations and procedures concerning the financial terms of a contract between the Authority and the entities referred to in article 153, paragraph 2 (*b*), in accordance with the provisions of Part XI of the present Convention, and in negotiating the financial terms of a contract in accordance with the provisions of Part XI and those rules, regulations and procedures, the Authority shall be guided by the following objectives:

(*a*) To ensure optimum revenues for the Authority from the proceeds of commercial exploitation;

(*b*) To attract investments and technology to the exploration and exploitation of the Area;

(*c*) To ensure equality of financial treatment and comparable financial obligations on the part of all States and other entities which obtain contracts;

(*d*) To provide incentives on a uniform and non-discriminatory basis for contractors to undertake joint arrangements with the Enterprise and developing countries or their nationals, to stimulate the transfer of technology thereto, and to train the personnel of the Authority and of developing countries;

(*e*) To enable the Enterprise to engage in sea-bed mining effectively at the same time as the entities referred to in article 153, paragraph 2 (*b*);

(*f*) To ensure that the financial incentives provided to contractors under paragraph 14 of this article, or under the terms of contracts reviewed in accordance with article 18, or under the provisions of article 10 with respect to joint ventures, shall not result in subsidizing contractors with a view to placing them at an artificial competitive advantage relative to land-based miners.

2. A fee shall be levied for the administrative cost of processing an application for a contract of exploration and exploitation and shall be fixed at an amount of $500,000 per application. If the cost incurred by the Authority in processing an application is less than $500,000, the Authority shall refund the difference to the applicant. The amount of the fee shall be reviewed from time to time by the Council in order to ensure that it covers the administrative cost of processing such an application.

3. A Contractor shall pay an annual fixed fee of $1 million from the date of entry into force of the contract. From the commencement of commercial production, the Contractor shall pay either the production charge or the annual fixed fee, whichever is greater.

4. Within a month from the date of commencement of the commercial production, in conformity with paragraph 3, a Contractor shall choose to make his financial contribution to the Authority by either:

(*a*) Paying a production charge only, hereinafter referred to as the single system; or

(*b*) Paying a combination of a production charge and a share of net proceeds, hereinafter referred to as the mixed system.

5. (*a*) If a Contractor chooses to make his financial contribution to the Authority by paying a production charge only, it shall be fixed at a percentage of the market value of the processed metals produced from the nodules extracted from the contract area in accordance with the following shedule:

(i)	Years 1-10 of commercial production:	5 per cent
(ii)	Years 11-20 of commercial production:	12 per cent

(*b*) The said market value shall be the product of the quantity of the processed metals produced from the nodules extracted from the contract area and the average price for those metals during the relevant accounting year, as defined in paragraph 7 below.

6. If a Contractor chooses to make his financial contribution to the Authority by paying a combination of a production charge and a share of net proceeds, such payments shall be determined as follows:

(*a*) The production charge shall be fixed at a percentage of the market value of the processed metals produced from the nodules extracted from the contract area in accordance with the following schedule:

(i)	First period of commercial production:	2 per cent
(ii)	Second period of commercial production:	4 per cent

If, in the second period of commercial production, as defined in subparagraph (*d*), the return on investment in any accounting year, as defined in subparagraph (*n*) below, shall fall below 15 per cent, the production charge shall be 2 per cent instead of 4 per cent in that accounting year.

(*b*) The said market value shall be the product of the quantity of the processed metals produced from the nodules extracted from the contract area and the average price for those metals during the relevant accounting year as defined in paragraph 7 below.

(*c*) (i) The Authority's share of net proceeds shall be taken out of that portion of the Contractor's net proceeds which is attributable to the mining of the resources of the contract area, referred to hereinafter as attributable net proceeds.

(ii) The Authority's share of attributable net proceeds shall be determined in accordance with the following incremental schedule:

Return on investment	*First period of commercial production*	*Second period of commercial production*
Greater than 0 per cent, but less than 10 per cent	35 per cent	40 per cent
Equal to or greater than 10 per cent, but less than 20 per cent	42.5 per cent	50 per cent
Equal to or greater than 20 per cent	50 per cent	70 per cent

(*d*) The first period of commercial production referred to in subparagraphs (*a*) and (*c*) above shall commence in the first accounting year of commercial production and terminate in the accounting year in which the Contractor's cash surplus, that is, his total gross proceeds less his operating costs, less his payments to the Authority in the form of shares of attributable net proceeds, in the preceding accounting years shall exceed for the first time the Contractor's development costs with interests at 10 per cent on that portion of his development costs not recovered by his cash surplus. The second period of commercial production referred to in subparagraphs (*a*) and (*c*) above shall commence at the conclusion of the first period and continue until the end of the contract.

(*e*) The amount of attributable net proceeds shall be the product of the Contractor's net proceeds and the ratio of the development costs in the mining sector to the Contractor's development costs. In the event that the Contractor engages in mining, transportation of nodules and production primarily of three processed metals, namely, cobalt, copper and nickel, the amount of attributable net proceeds shall not be less than 25 per cent of the Contractor's net proceeds. In all other cases, including those where the Contractor engages in mining, transportation of nodules, and production primarily of four processed metals, namely, cobalt, copper, manganese and nickel, the Authority may, by regulations, prescribe appropriate floors which shall bear the same relationship to each case as the 25 per cent floor does to the three-metal case.

(*f*) The term "Contractor's net proceeds" shall mean the Contractor's gross proceeds less his operating costs and the recovery of his development costs as set out in subparagraph (*j*) below.

(*g*) (i) In the event that the Contractor engages in mining, transportation of nodules and production primarily of three processed metals, namely, cobalt, copper and nickel, the term "Contractor's gross proceeds" shall mean the gross revenues from the sale of the processed metals, and any other monies deemed to be reasonably attributable to the operation of the contract in accordance with the financial rules, regulations and procedures of the Authority.

(ii) In the event that the Contractor engages in mining only, the term "Contractor's gross proceeds" shall mean the gross revenues from the sale of the nodules, and any other monies deemed to be reasonably attributable to the operation of the contract in accordance with the financial rules, regulations and procedures of the Authority.

(iii) In all cases other than those specified in subparagraphs (i) and (ii) above, the term "Contractor's gross proceeds" shall mean the gross revenues from the sale of the semi-processed metals from the nodules extracted from the contract area, and any other monies deemed reasonably attributable to the operation of the contract in accordance with the financial rules, regulations and procedures of the Authority.

(*h*) The term "Contractor's development costs" shall mean:

(i) All expenditures incurred prior to the commencement of commercial production which are directly related to the development of the productive capacity of the contract area and the activities related thereto for operations under the contract, in conformity with generally recognized accounting principles, including, *inter alia*, costs of machinery, equipment, ships, construction, buildings, land, roads, prospecting and exploration of the contract area, research and development, interest, required leases, licences, fees; and

(ii) Similar expenditures, incurred subsequent to the commencement of commercial production, for the replacement, improvement, or addition of machinery and equipment.

(*i*) The proceeds from the disposal of capital assets and the market value of those capital assets which are no longer required for operations under the contract and which are not sold shall be deducted from the Contractor's development costs during the relevant accounting year. When these deductions exceed the Contractor's development costs the excess shall be added to the Contractor's gross proceeds.

(*j*) The Contractor's development costs referred to in subparagraph (*h*) (i) shall be recovered in 10 equal annual instalments from the date of commencement of commercial production. The Contractor's development costs referred to in subparagraph (*h*) (ii) shall be recovered in 10 or fewer equal annual instalments so as to ensure their complete recovery by the end of the contract.

(*k*) The term "Contractor's operating costs" shall mean all expenditures incurred after the commencement of commercial production in the operation of the productive capacity of the contract area and the activities related thereto, for operations under the contract, in conformity with generally recognized accounting principles, including, *inter alia*, the fixed annual fee or the production charge, whichever is greater, expenditures for wages, salaries, employee benefits, supplies, materials, services, transportation, marketing costs, interest, utilities, preservation of the marine environment, overhead and administrative costs specifically related to the operation of the contract, and any net operating losses carried forward from prior accounting years.

(*l*) (i) In the event that the Contractor engages in mining, transportation of nodules and production primarily of three processed metals, namely, cobalt, copper and nickel, the term "development costs of the mining sector" shall mean the portion of the Contractor's development costs which is directly related to the mining of the resources of the contract area, in conformity with generally recognized accounting principles, and the financial rules, regulations and procedures of the Authority, including, *inter alia*, application fee, annual fixed fee, and, where applicable, costs of prospecting and exploration of the contract area, and a portion of research and development costs.

(ii) In the event that the Contractor engages in mining only, the term "development costs of the mining sector" shall mean the Contractor's development costs.

(iii) In all cases other than those specified in subparagraphs (i) (ii) above, the term "development costs of the mining sector" shall be defined as in subparagraph (i) above.

(*m*) The term "operating costs of the mining sector" shall mean the portion of the Contractor's operating costs which is directly related to the mining of the resources of the contract area, in conformity with generally recognized accounting principles, and the financial rules, regulations and procedures of the Authority.

(*n*) The term "return on investment" in any accounting year, shall mean the ratio of attributable net proceeds in that year to the development costs of the mining sector. The development costs of the mining sector for the purpose of this subparagraph shall include additions to the development costs of the mining sector incurred prior to the commencement of the commercial production, in order to carry out the specified plan of work. It shall also include expenditures on new or replacement equipment in the mining sector less the original cost of the equipment replaced.

(*o*) The costs referred to in subparagraphs (*h*), (*k*), (*l*) and (*m*) above, in respect of interest paid by the Contractor may only be allowed if, in all the circumstances, the Authority approves, pursuant to article 4, paragraph 1, the debt-equity ratio and the rates of

interest as reasonable, having regard to existing commercial practice.

(*p*) The costs referred to in this paragraph shall not be interpreted as including payments in respect of corporate income taxes or similar charges levied by States in respect of the operations of the Contractor.

7. (*a*) The term "processed metals" referred to in paragraphs 5 and 6 above, shall mean the metals in the most basic form in which they are customarily traded on international terminal markets. For the metals which are not traded on such markets, the term "processed metals" shall mean the metals in the most basic form in which they are customarily traded in representative arm's-length transactions. For this purpose, the Authority shall specify, in the financial rules, regulations and procedures, the relevant international terminal market.

(*b*) In the event that the Authority cannot otherwise determine the quantity of the processed metals produced from the nodules extracted from the contract area referred to in subparagraphs 5 (*b*) and 6 (*b*) above, the quantity shall be determined on the basis of the metal content of the nodules extracted from the contract area, processing recovery efficiency and other relevant factors in accordance with the rules, regulations and procedures of the Authority, and in conformity with generally recognized accounting principles.

8. If an international terminal market provides a representative pricing mechanism for processed metals, nodules and semi-processed metals from the nodules, the average price on such a market shall be used. In all other cases, the Authority shall, after consulting the Contractor, determine a fair price for the said products in accordance with paragraph 9 below.

9. (*a*) All costs, expenditures, proceeds and revenues and all determinations of price and value referred to in this article shall be the result of free market or arm's-length transactions. In the absence thereof, they shall be determined by the Authority, after consulting the Contractor, as though they were the result of free market or arm's-length transactions, taking into account relevant transactions in other markets.

(*b*) In order to ensure enforcement of, and compliance with, the provisions of the present paragraph, the Authority shall be guided by the principles adopted for, and the interpretation given to, arm's-length transactions by the Commission on Transnational Corporations established by the Economic and Social Council, the Expert Group on Tax Treaties between Developed and Developing Countries and other international organizations, and shall adopt rules and regulations specifying uniform and internationally acceptable accounting rules and procedures, and the means of selection by the Contractor of independent certified accountants acceptable to the Authority for the purpose of auditing in compliance with the said rules and regulations.

10. The Contractor shall make available to the accountants, in accordance with the financial rules, regulations and procedures of the Authority, such financial data as are required to determine compliance with the article.

11. All costs, expenditures, proceeds and revenues, and all prices and values referred to in this article, shall be determined in accordance with generally recognized accounting principles and the financial rules, regulations and procedures of the Authority.

12. The payments to the Authority under paragraphs 5 and 6 may be made either in a freely convertible currency or in a currency agreed upon between the Authority and the Contractor, or, at the Contractor's option, in the equivalents of processed metals at market value. The market value shall be determined in accordance with paragraph 5 (*b*).

13. All financial obligations of the Contractor to the Authority, as well as all his fees, costs, expenditures, proceeds and revenues referred to in this article, shall be adjusted by expressing them in constant terms relative to a base year.

14. The Authority may, taking into account any recommendations of the Economic Planning Commission and the Legal and Technical Commission, adopt rules and regulations that provide for incentives, on a uniform and non-discriminatory basis, to Contractors to further the objectives set out in paragraph 1.

15. In the event of a dispute between the Authority and a Contractor over the interpretation or application of the financial terms of a contract, either party may submit the dispute to compulsory and binding commercial arbitration.

2. FINANCING OF THE ENTERPRISE

Annex III

Article 3

Subject to article 10, paragraph 3 below, no member of the Authority shall be liable by reason only of its membership for the acts or obligations of the Enterprise.

Article 10

Delete paragraph 2 (*c*) and insert a new paragraph 3:

3. (*a*) The Enterprise shall be assured of the funds necessary to explore and exploit one mine site and to transport, process and market the metals recovered therefrom, namely, nickel, copper, cobalt and manganese, and to meet its initial administrative expenses, or the equivalent amount thereof. The said amount shall be determined by the Assembly upon the recommendation of the Council, on the advice of the Governing Board of the Enterprise.

(*b*) States Parties shall make available to the Enterprise an amount equivalent to one half of the funds referred to in paragraph 3 (*a*) above by way of long-term, interest-free loans in accordance with the scale referred to in article 160, paragraph 2 (*e*). Debts incurred by the Enterprise in raising the balance of the funds shall be guaranteed by all States Parties in accordance with the said scale. Upon request by the Enterprise, a State Party may provide a guarantee covering debts additional to the amount it has guaranteed in accordance with the said scale. In lieu of debt guarantee, a State Party may make a voluntary contribution to the Enterprise of an amount equivalent to that portion of the debts which it would otherwise be liable to guarantee.

(*c*) The repayment of the interest-bearing loans shall have priority over the repayment of the interest-free loans. The repayment of interest-free loans shall be in accordance with a schedule adopted by the Assembly, upon the recommendation of the Governing Board of the Enterprise.

C. THE ASSEMBLY AND THE COUNCIL

Article 157

Add a new paragraph 1 *bis*:

The powers and functions of the Authority shall be those expressly conferred upon it by the provisions of this Part and by annexes II and III. The Authority shall have such incidental powers, consistent with the provisions of this Convention, as are implicit in and necessary for the performance of these powers and functions with respect to activities in the Area.

Article 158

Revise paragraph 4 to read:

4. The principal organs shall each be responsible for exercising those powers and functions which have been conferred upon them. In exercising such powers and functions each organ shall avoid taking any action which may derogate from or impede the exercise of specific powers and functions conferred upon another organ.

Article 160

Revise paragraph 1 to read:

1. The Assembly, as the sole organ of the Authority consisting of all the members, shall be considered the supreme organ of the Authority to which the other principal organs shall be accountable as specifically provided for in this Part. The Assembly shall have the power to establish general policies in conformity with the provisions of this Part on any question or matter within the competence of the Authority.

Add a new paragraph 2 (*o*):

(*o*) Dicussion of any question or matter within the competence of the Authority and decisions as to which organ shall deal with any such question or matter not specifically entrusted by the provisions of this Convention to a particular organ of the Authority, consistent with the distribution of powers and functions among the organs of the Authority.

Article 161

Paragraph 7

Revise subparagraphs (*a*) and (*b*) to read:

(*a*) Decisions on questions of procedure shall be taken by a majority of the members present and voting;

(*b*) Decisions on questions of substance arising under article 162, paragraph 2 (*b*) to (*i*) and (*o*), (*r*) and (*t*) in cases of non-compliance by a contractor or a sponsor, (*u*) and (*v*) provided that orders issued under this subparagraph may be binding for no more than 10 days unless confirmed by a decision taken in accordance with subparagraph (*c*) below, (*x*) and (*y*) shall be taken by a two-thirds majority of the members present and voting, provided that such majority includes a majority of the members of the Council;

Present trend for subparagraph (*c*) appears as follows:

(*c*) In order to promote the resolution of particularly sensitive issues by means of consensus, decisions on all other questions of substance shall be taken by a two-thirds majority of members present and voting, provided that . . .[35] members have not cast negative votes. When the issue arises as to whether the question is within this subparagraph or not, the question shall be treated as within this subparagraph unless otherwise decided by the Council by the majority required for questions under this subparagraph.

Article 162

Paragraph 2

Subparagraph (*f*):

After "of the Authority" add "and within its competence"

Revise subparagraph (*i*) to read:

(*i*) Issue directives to the Enterprise in accordance with article 170;

Subparagraph (*j*):

Delete second and third sentences and replace by the following:

The Council shall act within 60 days of the submission of a plan of work by the Legal and Technical Commission at a session of the Council. Except where selection must be made among applicants, a plan of work shall be deemed to have been approved unless a proposal for its approval or disapproval has been voted upon within the aforementioned period of 60 days;

Revise subparagraph (*r*) to read:

(*r*) Make recommendations to the Assembly concerning policies on any question or matter within the competence of the Authority;

D. Settlement of disputes relating to Part XI and connected issues

Article 168. International character and responsibilities of the secretariat

1. In the performance of their duties, the Secretary-General and the staff shall not seek or receive instructions from any Government or from any other source external to the Authority. They shall refrain from any action which might reflect on their position as international officials of the Authority responsible only to the Authority. Each State Party undertakes to respect the exclusively international character of the responsibilities of the Secretary-General and the staff and not to seek to influence them in the discharge of their responsibilities. Any violation of responsibilities by a staff member shall be submitted to the appropriate administrative tribunal as provided in the staff rules of the Authority.

2. The Secretary-General and the staff shall have no financial interest whatsoever in any activity relating to exploration and exploitation in the Area. Subject to their responsibilities to the Authority, they shall not disclose, even after the termination of their functions, any industrial secret or data which is proprietary in accordance with article 13 of annex II to the present Convention, or other confidential information of commercial value coming to their knowledge by reason of their official duties with or on behalf of the Authority.

3. Violations of the obligations of a staff member of the Authority set forth in paragraph 2 shall, on the request of a State Party affected by such violation, or a natural or juridical person sponsored by a State Party as provided for in article 153, paragraph 2 (*b*), and affected by such violation, be submitted by the Authority against the staff member concerned to an appropriate tribunal. The Party affected shall have the right to take part in the proceedings. If the tribunal so recommends, the Secretary-General shall dismiss the staff member concerned.

4. The elaboration of the relevant provisions of this article shall be included in the staff regulations of the Authority.

Section 6. Settlement of disputes and advisory opinions

Article 187. Jurisdiction of the Sea-Bed Disputes Chamber

The Chamber shall have jurisdiction under this Part and the annexes relating thereto in the following categories of disputes with respect to activities in the Area:

1. Disputes between States Parties concerning the interpretation or application of this Part and the annexes relating thereto.

2. Disputes between a State Party and the Authority concerning acts or omissions of the Authority or of a State Party which are alleged to be in violation of this Part or the annexes relating thereto, or of rules, regulations or procedures promulgated in accordance therewith, or acts of the Authority alleged to be in excess of jurisdiction or a misuse of power.

3. Disputes between parties to a contract, being States Parties, the Authority or the Enterprise, State entities and natural or juridical persons as referred to in article 153, paragraph 2 (*b*), concerning:

(*a*) The interpretation or application of a relevant contract or a plan of work;

(*b*) Acts or omissions of a party to the contract relating to activities in the Area and directed to the other party or directly affecting its legitimate interests.

4. Disputes between the Authority and a prospective contractor who has been sponsored by a State as provided for in article 153, paragraph 2 (*b*), and has duly fulfilled the conditions referred to in article 4, paragraph 4 and article 12, paragraph 2, of annex II, concerning the refusal of a contract, or a legal issue arising in the negotiation of the contract.

5. Disputes between the Authority and a State Party, a State entity or a natural or juridical person sponsored by a State Party as provided for in article 153, paragraph 2 (*b*), where it is alleged that the Authority has incurred liability as provided for in article 21 of annex II.

6. Any dispute for which jurisdiction of the Chamber is specifically provided for in this Part and the annexes relating thereto.

Article 188. Submission of disputes to a special chamber of the Law of the Sea Tribunal or an ad hoc *chamber of the Sea-Bed Disputes Chamber or to binding arbitration*

1. Disputes between States Parties referred to in article 187, paragraph 1, may be submitted:

(*a*) To a special chamber of the Law of the Sea Tribunal to be established in accordance with articles 15 and 17 of annex V, upon the request of the parties to the dispute; or

(*b*) To an *ad hoc* chamber of the Sea-Bed Disputes Chamber to be established in accordance with article 36 *bis* of annex V, upon the request of any party to the dispute.

2. Disputes referred to in article 187, paragraph 3, shall be submitted to binding commercial or other arbitration, in so far as this is provided for in any contract between the parties to the dispute, at the request of any party thereto. Failing agreement of the parties, the procedure in accordance with commercial arbitration rules to be specified shall apply.

Article 191. Participation and appearance of sponsoring States Parties

1. In any dispute referred to in article 187 when a natural or juridical person is a party, the sponsoring State shall be given notice thereof, and shall have the right to participate in the proceedings by submitting written or oral statements.

2. In any dispute referred to in article 187, paragraph 3, if an action is brought against a State Party by a natural or juridical person, of another nationality, the State Party sponsoring that person may be requested by the respondent State Party to appear in the proceedings on behalf of that person. Failing such appearance, the respondent State may arrange for the appearance on its behalf of a juridical person of its nationality.

[35] The figure is still being negotiated; current proposals range from 5 to 10.

Annex II

Article 21. Liability

Any responsibility or liability for wrongful damage arising out of the conduct of operations by the Contractor shall lie with the Contractor, account being taken of contributory factors by the Authority. Similarly, any responsibility or liability for wrongful damage arising out of the exercise of the powers and functions of the Authority, including liability for violations under article 168, paragraph 2, shall lie with the Authority, account being taken of contributory factors by the Contractor. Liability in every case shall be for the actual amount of damages.

Annex V

Article 4. Procedure for nomination and election

1. Each State Party may nominate not more than two persons having the qualifications prescribed in article 2. The members of the Tribunal shall be elected from a list of persons thus nominated.

2. At least three months before the date of the election, the Secretary-General of the United Nations in the case of the first election and the Registrar of the Tribunal in the case of subsequent elections shall address a written invitation to the States Parties to submit their nominations for members of the Tribunal within two months. He shall prepare a list in alphabetical order of all the persons thus nominated, with an indication of the States Parties which have nominated them, and shall submit it to the States Parties before the seventh day of the last month before the date of each election.

3. The first election shall be held within six months of the date of entry into force of the present Convention.

4. Elections of the members of the Tribunal shall be by secret ballot. They shall be held at a meeting of the States Parties convened by the Secretary-General of the United Nations in the case of the first election and by procedure agreed to by the States Parties in the case of subsequent elections. At that meeting, for which two thirds of the States Parties shall constitute a quorum, the persons elected to the Tribunal shall be those nominees who obtain the largest number of votes and a two-thirds majority of votes of the States Parties present and voting, provided that such majority shall include at least a majority of the States Parties.

Article 36. Composition of the Chamber

1. The Sea-Bed Disputes Chamber established in accordance with article 14 shall be composed of 11 members, selected by a majority of the members of the Tribunal from among its members.

2. In the selection of the members of the Chamber, the representation of the principle legal systems of the world and equitable geographical distribution shall be assured. The Assembly of the Authority may adopt recommendations of a general nature relating to such representation and distribution.

3. The members of the Chamber shall be selected every three years and may be selected for a second term.

4. The Chamber shall elect its President from among its members, who shall serve for the period for which the Chamber has been selected.

5. If any proceedings are still pending at the end of any three-year period for which the Chamber has been selected, the Chamber shall complete the proceedings in its original composition.

6. Upon the occurrence of a vacancy in the Chamber, the Tribunal shall select a successor from among its members who shall hold office for the remainder of the term of his predecessor.

7. A quorum of seven members shall be required to constitute the Chamber.

Article 36 bis. Ad hoc *chambers of the Sea-Bed Disputes Chamber*

1. The Sea-Bed Disputes Chamber shall form an *ad hoc* chamber, composed of three of its members, for dealing with a particular dispute submitted to it in accordance with article 188, paragraph 1 (*b*). The composition of such a chamber shall be determined by the Sea-Bed Disputes Chamber with the approval of the parties.

2. If the parties do not agree on the composition of an *ad hoc* chamber referred to in paragraph 1, each party to the dispute shall appoint one member, and the remaining member shall be appointed by them in agreement. If they disagree, or if any party fails to make an appointment, the President of the Sea-Bed Disputes Chamber shall promptly make such appointments from among the members of the Sea-Bed Disputes Chamber, after consultation with the parties.

3. Members of the *ad hoc* chamber must not be in the service of, or nationals of, any of the parties to the dispute.

APPENDIX B

Report by the Chairman of the group of legal experts on the settlement of disputes relating to part XI

Though the questions of the settlement of disputes were not discussed in the group of 21, the Chairman of the group of legal experts on the settlement of disputes relating to part XI presented his report to the group of 21, before presenting it in the First Committee.

The group of legal experts held three meetings during the resumed eighth session in New York. After each of the meetings, the Chairman had intensive consultations with interested delegations, on the basis of which he attempted to reach compromise solutions. This process followed the procedure which had been agreed to by the Group.

At the opening of the first meeting, the Chairman stated that he had, on 25 April 1979, reported to the Chairman of the First Committee on the results of the work of the group, setting out fully the status of the work at the conclusion of the first part of the eighth session at Geneva (A/CONF.62/C.1/L.25 and Add.1[36]). That report identified the outstanding issues which were not discussed at all and those that were discussed, though not fully.

The Chairman suggested that the outstanding issues be dealt with in the following sequence:

(1) The manner of selection of members of the Sea-Bed Disputes Chamber of the Law of the Sea Tribunal and the necessary changes to annex V;

(2) The suggestion regarding *ad hoc* chambers of the Sea-Bed Disputes Chamber;

(3) Liability of the Authority, in cases of staff members violating their duty not to disclose confidential information, and in other cases;

(4) Aspects of contractual disputes for which commercial arbitration would be appropriate.

The Chairman also pointed out the need to consider articles 187, 189, 190 and 191 which the group had formulated at the first part of the session, as incorporated in part XI, section 6, because there could be some matters that needed clarification. However, he suggested that this be taken up last, after the negotiations on the outstanding issues had been subject to the same process of negotiation as those issues in respect of which texts had been included in the revised negotiating text.

This course of procedure was accepted by the Group.

1. Selection of members of the Sea-Bed Disputes Chamber

On the first issue, which was the manner of selection of members of the Chamber, the Chairman stated that, after the original discussion at Geneva, he had the impression that it would be possible to provide that members of the Chamber be selected by the Law of the Sea Tribunal itself. The Tribunal was to be elected by the Conference of States Parties, who would be the same as the members of the Assembly, and there appeared to be no need for a second vote of confidence. Should there be agreement that the Chamber be selected by the Tribunal, consideration could then be given to whether the Assembly should be empowered to make recommendations that the principles of equitable geographical distribution and the representation of the principal legal systems be followed.

A clear desire to compromise was shown. A willingness to accept that the members of the Tribunal itself should select the members of the Chamber was expressed by those who had originally opposed it. Those who opposed the role of the Assembly in that regard, also in a spirit of compromise, agreed that the Assembly could be empowered to make recommendations of a general nature regarding equitable geographical distribution and the representation of the principle legal systems which was to be assured in the Chamber. It was also

[36] See *Official Records of the Third United Nations Conference on the Law of the Sea*, vol. XI.

agreed that the selection of the members of the Chamber would be made by the decision of a majority of the members of the Tribunal. A consensus was reached in the group on this compromise solution. The text drafted on this basis is to be found in annex V, article 36, in appendix A above.

2. Special and *ad hoc* chambers of the Sea-Bed Disputes Chamber

Regarding the second item, namely, the formation of *ad hoc* chambers of the Sea-Bed Disputes Chamber (art. 188, para. 1, of the revised negotiating text), there was an exhaustive expression of views. Some felt that for disputes between States the choice of procedures available in article 287 should be available, as that would ensure consistency of application of dispute settlement procedures in all cases of interpretation or application of the convention. That view was strongly opposed by those who advocated unity of jurisdiction of the Chamber for all matters in part XI and the related annexes.

All sides were of the opinion that the concept of *ad hoc* chambers represented a compromise on their part. Those who advocated unity of jurisdiction emphasized that the *ad hoc* chambers could only be envisioned as an exception to the general rule. For this reason, they felt strongly that resort to the *ad hoc* chambers could only be had upon agreement of the parties. Those who opposed the exclusive jurisdiction of the Chamber envisioned the *ad hoc* chambers as a parallel system for the settlement of sea-bed disputes. They insisted that resort to the *ad hoc* chambers should be allowed upon the request of any party to the dispute.

It was suggested that if there could be agreement in the group on the composition of the *ad hoc* chamber, that might facilitate the reaching of a compromise of the divergent views. In that connexion, the size of the *ad hoc* chamber; the question of whether to allow the selection of judges who were of the same nationality as a State party; and the question of whether the judges should be selected from among the members of the Chamber or of the Tribunal appeared to be the critical factors. Several alternative compromises were presented but, rather than a single trend, two alternative suggestions emerged as commanding support. The alternatives presented in article 188, paragraphs 1 (*a*) and (*b*), contained in appendix A above seemed to offer the best prospects for widespread support.

This article provides that on the agreement of the parties, a special chamber could be established on the lines set out in annex V, articles 15 and 17, which provide for the inclusion of national members and the selection from among the 21 members of the Tribunal. The alternative presented in this paragraph permits one party to request an *ad hoc* chamber which consists only of three members to be selected from among the members of the Chamber, excluding nationals of the parties.

3. Liability of the Authority for staff violations and other matters

The third item, the question of liability of the Authority for the unauthorized disclosure of secret data by its staff, had been raised in the first part of the session, but it had not been dealt with by the group. It was noted that this liability would be in addition to the liability of the staff member concerned, which article 168, paragraph 2, already provided for. The Chairman pointed out that the responsibility of the Authority for wrongful damage was referred to in annex II, article 21. Liability under article 168, paragraph 2, could also be set out in that article. The group agreed upon such an approach and, accordingly, provision was included in annex II, article 21 (see appendix A above) for liability of the Authority in the case of staff members' violations.

The Chairman suggested that it might be desirable to provide jurisdiction of the Chamber for all such questions of liability of the Authority. The group agreed to that suggestion. Accordingly, such provision was included in article 187, which deals with the jurisdiction of the Chamber, in a new paragraph 5 (*ibid*).

4. Commercial arbitration

In considering the fourth question, commercial arbitration in cases of contractual disputes, the Chairman drew the attention of the group to some aspects of the issues that arose regarding the present article. He pointed out that article 188, paragraph 2, referred to article 187, subparagraph (*c*). That paragraph was again subdivided into: the interpretation or application of contracts or plans of work and acts or omissions relating to activities in the area. While commercial arbitration was suited to the first such category of disputes, its appropriateness to the second category was raised.

The Chairman suggested that the intention of providing commercial arbitration appeared to be because of the expeditious nature of the procedure and its suitability in disputes of a technical or commercial nature.

He explained that it might be found unnecessary at the time of contracting to include a detailed arbitration procedure and for that reason the existing second sentence of article 188, paragraph 2, suggested that a standard form procedure be specified where the contract itself did not provide it.

A lengthy discussion ensued. Some felt that commercial arbitration might be appropriate for disputes of a purely commercial and technical nature, provided that the parties had agreed thereto, and that in no case should the commercial arbitration tribunal be empowered to determine questions of the interpretation or application of the convention.

In that connexion a compromise suggested was that the scope of the article should be limited to article 187, subparagraph (*c*) (i). Those who were of the view that in all cases agreement of the parties was needed felt that agreement could be evidenced either by a provision regarding commercial arbitration in the contract or by subsequent agreement on the subject. The opposing view, also strongly expressed, was that the request to resort to arbitration could be made by either party, whether or not the contract so provided.

The interpretation of the existing text of article 188, paragraph 2, appeared to present difficulties to both sides and attempts to reconcile doubts on the text only led to a further polarization of positions.

It became clear that in order to move towards reconciling the divergence, it was necessary to set out clearly the principle that the arbitral tribunal would not be competent to determine questions of the interpretation or application of the convention, and that its competence should be limited strictly to the interpretation or application of relevant contracts or plans of work. If that were done, it might be possible to allow for resort to commercial arbitration at the request of any party, whether or not it was provided for in the contract. Time, however, did not permit a full consideration of the question and it would most certainly need to be examined thoroughly at the very beginning of the next session.

The rules of the United Nations Commission on International Trade Law (UNCITRAL) appeared to command wide acceptance and, in the absence of specific arbitration rules in the contract, there appeared to be agreement that standard-form arbitration rules, such as the UNCITRAL rules, could apply. As an alternative, or in addition, the Authority could specify other rules in its rules, regulations and procedures.

No conclusions were reached regarding article 188, paragraph 2, and no suggestions were sufficiently widely accepted to warrant any change in the present text.

5. Jurisdiction of the Sea-Bed Disputes Chamber and limitations thereof; participation of sponsoring States and advisory opinions

In the consideration of articles 187, 189, 190 and 191, the Chairman pointed out that these articles were very closely linked and that the substance of those provisions form a composite unit; he therefore suggested that the articles be considered in conjunction. The Chairman also noted that it was the decision of the Conference that no changes could be made to any texts unless there was widespread and substantial support. He therefore urged members of the group to refrain from making suggestions which were not likely to receive such support and that a constructive attempt be made to arrive at compromise solutions. That procedure was adopted by the Group.

Regarding article 187, the suggestion was made that paragraph (*a*) should be deleted and that disputes covered under that provision should be subject to the general dispute settlement procedures under part XV. That was strongly opposed on the grounds that a uniform legal order must be maintained for all sea-bed questions.

Regarding paragraph (*b*) of article 187, it was generally agreed that the wording contained in the revised negotiating text was acceptable.

Regarding paragraph (*c*), it was noted that this referred to a "plan of work". The point was made that this wording implied that the Sea-Bed Disputes Chamber would have jurisdiction over disputes between the Authority and the Enterprise. Strong and widespread opposition was recorded to this possibility on the basis that, since the Enterprise was an arm of the Authority, any possible conflict between them should be resolved by the Council of the Authority. It was urged that some formulation be arrived at whereby the possibility of the Chamber exercising jurisdiction over such disputes should be avoided at all costs.

The question was raised as to whether article 187, subparagraph (*c*) (i), dealt with disputes only between the Authority, as one party, and the other possible contractors. If that was the case, it was suggested that the reference to "plan of work" be deleted. On the other hand, the point was made that there should be provision covering disputes between contractors who had independent contracts with the Authority although they did not have a contract between themselves. If this interpretation was not possible under article 187, paragraph (*c*); it was a question that needed resolution and would have to be considered at the beginning of the next session.

Regarding article 187, paragraph (*d*), some wanted it deleted while others wanted to strengthen it by eliminating the necessity to comply with any conditions. It was the Chairman's impression, in the light of the discussions, that the existing text represented the best basis for a possible compromise. Concern was expressed as to the possibility of unsuccessful applicants impeding the work of those to whom contracts had been awarded by bringing disputes and obtaining restraining orders from the Chamber.

A proposal was made to provide for jurisdiction of the Chamber in disputes between prospectors and the Authority, but there was a lack of support for such provision, it being pointed out that prospectors had no contractual rights to be safeguarded.

No points were raised regarding articles 189 and 190 dealing, respectively, with advisory opinions and limitations on the jurisdiction of the Chamber. The Chairman noted that the group found these acceptable and there was no desire expressed to make any changes in the text.

There was much discussion on the question of the appearance and participation in proceedings of sponsoring States, and a clear division of views regarding article 191, paragraph 2. On the one hand, it was argued that such a provision was necessary to protect the juridical personality of a State. In this respect, it was noted that, according to the general principles of international law, a State always enjoyed immunity from legal process compared to a natural or juridical person, and that therefore a safeguard clause, whereby the State sponsoring the applicant person must join the proceedings, was needed. Counter to this argument was the view that a State could not be compelled to participate in the proceedings merely because its sponsored natural or juridical persons wished to bring a claim against another State. It was felt that this should be a matter of discretion with the State. Supporters of this view advocated the deletion of paragraph 2.

In the spirit of compromise, it was suggested that perhaps paragraph 2 could be reformulated whereby the Chamber would have no jurisdiction in cases where the sponsoring State of a natural or juridical person did not agree to participate in the proceedings. An alternative compromise was suggested whereby the respondent State party could nominate a natural or juridical person of its own nationality to participate in the proceedings in its place. A combination of these two suggestions led to further consultations which provided the basis for the revised draft of article 191 in appendix A above. This draft could seem to command widespread support.

6. Other issues

All drafting suggestions made in the course of the negotiations or submitted to the Chair have been closely examined and wherever practicable have been incorporated in the Chairman's suggested text. Due regard was given to avoiding the inclusion of any drafting suggestions that might have had implications on substantive issues. It was suggested, however, by many participants that the texts should be examined as a whole for consistency and accuracy of drafting and translation. Reference was also made to the need to examine the titles of all articles and some changes that were agreed upon have been incorporated in the new draft.

The sequence of the articles may need to be changed. In this regard it was suggested that article 189 concerning advisory opinions appear last or as a separate section.

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Report of the Chairman of the Second Committee

[Original: Spanish]
[24 August 1979]

1. The Conference decided to establish seven negotiating groups to concern themselves with the most difficult questions. Three of those groups, negotiating groups 4, 6 and 7, were to concern themselves with matters which were completely or partially within the competence of the Second Committee.

2. At the present resumed eighth session, only negotiating groups 6 and 7 held meetings. Negotiating group 4 did not hold any meetings.

3. The Second Committee also devoted a number of meetings to the consideration of other questions, apart from those which were within the competence of the negotiating groups. I shall refer to those meetings later in this report.

Negotiating groups

4. Negotiating group 7, presided over by Mr. E. J. Manner of Finland, concerns itself with the definition of the maritime frontiers between adjacent States and between States whose coasts lie opposite each other—subjects within the competence of the Second Committee—and with the settlement of disputes related thereto, a matter dealt with by the plenary Conference.

5. Negotiating group 6, of which I am Chairman, is concerned with the definition of the outer limit of the continental shelf and the question of payments and contributions in connexion with the exploitation of the continental shelf beyond 200 miles, or the question of revenue sharing.

6. At its 126th informal meeting on 22 August 1979, the Second Committee received the reports of the Chairmen of negotiating groups 6 and 7 on the work done during the current second stage of the eighth session.

7. Owing to lack of time and in order to avoid duplication of work, it was agreed that no substantive comments would be made concerning the report of Mr. Manner on the work of negotiating group 7, since any delegations interested in commenting could do so in the plenary Conference. The report will be published as informal document NG7/45. I wish to express once more my gratitude to Mr. Manner for his untiring efforts to find solutions to the problems dealt with by his group.

8. My report to the Second Committee on the activities of negotiating group 6 is contained in informal document paper NG6/19, which is now in the hands of delegations. I do not propose to repeat it in this forum and shall merely refer in a general way to the group's work. Negotiating group 6 held five meetings, and at its meeting of 13 August 1979, at the request of several delegations, it established the so-called group of 38, an open-ended group formed on the basis of registration of delegations interested in dealing with the same subjects in a smaller framework. The group of 38 also held five meetings and considered the following items: the outer limit of the continental shelf; payments and contributions for the exploitation of the continental shelf beyond 200 miles; submarine oceanic ridges; the commission on limits; and the problem of Sri Lanka.

9. Concerning these items, delegations presented various informal suggestions which helped to determine more precisely the various positions and the possible solutions. I hope that the deliberations and extensive consultations held during this stage have prepared the ground for finding satisfactory solutions on these items at the next session.

Other matters

10. There were two informal meetings of the Second Committee devoted to other matters than those assigned to