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OIL POLLUTION
COMPENSATION
FUND 1992

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Agenda item 26

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WORKING CAPITAL

Note by the Director

Introduction

- 1 The 1992 Fund's Financial Regulations provide that a working capital shall be maintained at such a level as the Assembly may decide from time to time (Financial Regulation 7.1(b)).

- 2 Under Financial Regulation 7.1(c), the 1992 Fund shall have a General Fund which shall be used:
 - (i) for the satisfaction of claims of the kind referred to in Article 12.1(i)(b) of the 1992 Fund Convention including the first four million SDR of claims in respect of any one incident where the aggregate amount of all claims exceeds four million SDR;
 - (ii) to make provisional payments pursuant to Internal Regulation 7.9;
 - (iii) to meet the costs and expenses of the administration of the 1992 Fund and any other expenditure which may be authorised by the Assembly or, where appropriate, by a subsidiary body established by the Assembly in accordance with Article 18.9 of the 1992 Fund Convention;
 - (iv) to make loans to a Major Claims Fund for the satisfaction of claims of the kind referred to in Article 12.1(i)(c) of the 1992 Fund Convention, above the first four million SDR in respect of any one incident, to the extent that sufficient money is not available in that Major Claims Fund.

- 3 Separate major claims funds shall be established in respect of each larger incident, ie each incident where the aggregate amount of the payments by the 1992 Fund exceeds 4 million SDR (approximately £3.3 million). Such a major claims fund shall be used for the payment of claims arising from the relevant incident, provided that

the first 4 million SDR in respect of each incident are to be paid from the General Fund (Financial Regulation 7.2(a) and (d)).

4 At its 1st extraordinary session, the Assembly decided to set the working capital of the 1992 Fund at £7 million (document 92 FUND/A/ES.1/22, paragraph 18).

5 The Assembly is invited to review the level of the 1992 Fund's working capital.

Consideration by the Director

6 The working capital should be available to meet claims in respect of smaller incidents and the necessary administrative expenses of the 1992 Fund, and to make loans to major claims funds, as required. If the working capital were to fall below an amount reasonably required to meet the administrative expenses and anticipated claims, annual contributions should be raised to restore the working capital to the level fixed by the Assembly.

7 Under Internal Regulation 7.4, the Director may make final settlement of any claim for compensation without the prior approval of the Assembly, if he estimates that the total cost to the 1992 Fund of satisfying all such claims arising out of the relevant incident is not likely to exceed 2.5 million SDR (approximately £2.1 million). The Director may in any case make final settlement of claims from individuals and small businesses up to an aggregate amount of 666 667 SDR (approximately £550 000) in respect of each incident. The Assembly may authorise the Director to settle claims beyond this limit in respect of a particular incident (Internal Regulation 7.5).

8 At the time of the 2nd session of the Assembly, 15 States will be Members of the 1992 Fund. During the following 12 months, the 1992 Fund Convention will enter into force for at least a further 11 States. It is expected that in the next few years, a considerable number of other States will join the 1992 Fund. The larger the number of Member States, the greater the risk that the 1992 Fund will be called upon to pay compensation for oil pollution incidents. Although the limitation amount applicable to the shipowner is significantly higher under the 1992 Civil Liability Convention than under the 1969 Civil Liability Convention, the shipowner may in some cases be able to invoke the lower limits under the latter Convention (eg *Nakhodka* and *Osung N°3* incidents).

9 There is a considerable element of uncertainty in the estimates that form the basis of the Assembly's decision to levy contributions. This is due partly to the comparatively long period of time involved. It has been the policy of the Director to include in his estimates for the 1971 Fund, which form the basis of the 1971 Fund Assembly's decision, only those incidents in respect of which that Organisation's payments can be assessed with a reasonable degree of accuracy. The Director considers that the same policy should apply to the 1992 Fund except during the first years, when a certain flexibility would be required. The estimates would normally be made in July or August, and would be reviewed immediately before the session of the Assembly. The decision to levy contributions would usually be taken by the Assembly in October, say in October 1997, and the contributions would then be due by 1 February 1998. No further contributions would normally be levied until the Assembly fixed the 1998 contributions in October 1998, for payment by 1 February 1999. Although the Assembly decided at its 2nd extraordinary session, held in April 1997, to make a supplementary levy of contributions in respect of a major incident which had occurred after the Assembly's decision in October 1996, the Director considers that such a supplementary levy should normally be avoided.

10 At its 1st session, the Assembly introduced a deferred invoicing system. Under this system the Assembly would fix the total amount to be levied in annual contributions for a given calendar year. At the same time, the Assembly may decide that only a specific lower total amount should be invoiced for payment by 1 February in the following year, the remaining amount, or a part thereof to be invoiced later in the year if it should prove to be necessary (document 92FUND/A.1/34, paragraph 16.2). It was stressed by a number of delegations that the introduction of a deferred invoicing system should not be applied in such a way that the 1992 Fund would not have sufficient funds for the prompt payment of claims for compensation (document 92FUND/A.1/34, paragraph 16.4). The system nevertheless allows greater flexibility in the levy of contributions, *inter alia* with regard to the level of the working capital.

11 It would be possible to keep the working capital of the 1992 Fund at a comparatively low level if the Director's estimates for the assessment of contributions included figures based on the worst possible outcome from the 1992 Fund's point of view in respect of various incidents. However, this would be at variance with the method of assessment applied by the 1971 Fund, and the Director is not in favour of a change in this direction. In any event, such an approach would not take into account incidents which take place after the Assembly's decision.

12 It has been the policy of the 1971 Fund that victims of oil pollution incidents should be compensated as soon as possible. This has been the policy underlying the decisions of the 1971 Fund's Assembly and the Executive Committee in respect of claim settlements, and it has guided the Director of the 1971 Fund in his negotiations with claimants. The Director is of the view that the 1992 Fund should emulate the 1971 Fund's policy of paying compensation to victims of oil pollution incidents as soon as possible.

13 The Director considers that the prompt payment of compensation is of crucial importance. The 1992 Fund should, in the Director's view, hold sufficient liquid funds to enable it to pay claims without having to wait for the next payment of contributions. In addition, the Director considers that the working capital should be sufficiently large so that bank loans are not required for the prompt payment of accepted claims, at least not in normal circumstances. Another option could be that the 1992 Fund would, if required, take loans from the 1971 Fund, if the 1971 Fund Assembly were to agree to such a procedure. The Director believes, however, that it would be preferable if such a solution could be avoided.

14 In recent years there have been several incidents involving the 1971 Fund in which there was no P & I insurer who could make payments promptly to individual claimants and small businesses. In such cases involving the 1992 Fund, it will be imperative that the 1992 Fund is in a position to act promptly in order to mitigate undue financial hardship to the victims. This is particularly important in respect of individuals and small businesses, and generally in respect of victims in developing countries. It should also be recalled that, as a consequence of the wider definition of 'ship' in the 1992 Fund Convention, the 1992 Fund may be called upon to pay compensation in cases where it is not possible to identify the owner of the tanker which caused a spill; reference is made to the oil spill which occurred in the North Sea in June 1996 (1996 Annual Report, page 105).

15 It will be recalled that at its 19th session the Assembly of the 1971 Fund reduced the working capital of the 1971 Fund from £15 million to £10 million. It should be noted, however, that the working capital was reduced to this level, because in respect of the 1971 Fund it is possible to take loans from the considerable amounts available in several major claims funds of the 1971 Fund. There is at least at present no such possibility for the 1992 Fund. It should also be noted that the Director has submitted a proposal to the Assembly of the 1971 Fund to reduce the working capital of that Organisation to £5 million (document 71FUND/A.20/23).

Director's proposal

16 In the light of experience gained by the 1992 Fund since May 1996, and by the 1971 Fund over the years, it would appear that the 1992 Fund would in the long run need a sizeable working capital in order to ensure prompt payments. The Director is of the view that the 1992 Fund should hold sufficient liquid funds to enable it to pay claims during 1998 without having to wait for the receipt of contributions in February 1999. The Director is nevertheless aware of the importance of limiting the financial burden on contributors. In his view, the working capital of the 1992 Fund should be built up in stages. For this reason, he proposes that at this stage the working capital be increased from £7 million to £12 million.

17 The Assembly may wish to instruct the Director to submit the question of the level of working capital to the Assembly for renewed consideration at its 3rd ordinary session.

Action to be taken by the Assembly

18 The Assembly is invited to consider the Director's proposal to increase the working capital of the 1992 Fund from £7 million to £12 million at this stage.
