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REVIEW OF THE INTERNATIONAL COMPENSATION REGIME

POSSIBLE IMPROVEMENTS TO THE INTERNATIONAL COMPENSATION REGIME FOR OIL POLLUTION DAMAGE – AN OCIMF PERSPECTIVE

Submitted by the Oil Companies International Marine Forum (OCIMF)

Summary:	See Executive Summary, page 3
Action to be taken:	The Working Group is requested to consider the proposals put forward in this paper in accordance with the Resolution adopted at the Diplomatic Conference in May 2003 (LEG/CONF.14/DC/4).

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EXECUTIVE SUMMARY

The IOPC Intersessional Working Group at its meeting in February 2004 will discuss the need for, and possibilities of, improving the compensation regime established by the 1992 Civil Liability and 1992 Fund Conventions. OCIMF believes that the "relationship between shipowner liability and oil receiver contributions" must continue to be considered by the Working Group as a priority and in accordance with the Resolution adopted at the Diplomatic Conference in May 2003[<1>].

OCIMF welcomes the opportunity to work closely with State delegations and key industry stakeholders to seek proposals designed to achieve the primary objectives set out below. Clear and effective dialogue between all parties is essential to promote the further development of the international regime that has served victims and the international community so well in the past.

In this context OCIMF proposes the following for consideration:

1. Either (i) the Supplementary Fund should consist of two parts, divided between oil receivers and shipowners, or, (ii) there should be a significantly increased limit of liability in CLC 92, or, (iii) a combination of (i) and (ii). Adoption of any of these options will provide a mechanism for encouraging improvements in maritime safety and pollution prevention.

2. Recognising that spills from small vessels can be as expensive as spills from big vessels it is illogical and inappropriate to have a sliding scale limit of liability. Therefore OCIMF proposes a flat rate CLC limit to apply to all tankers regardless of size or capacity, (Because this may have adverse effects on small ships in some CLC States, OCIMF proposes a provision, similar to the HNS Convention, which enables States to exclude tankers under a certain gross tonnage engaged in domestic coastal trade from the application of the Conventions and to impose their own national requirements on this sector).

3. All ships, which carry oil in bulk as cargo, regardless of the amount, should be required to maintain insurance or other financial security in accordance with Article VII of the Civil Liability Convention to cover liability for oil pollution damage.

4. A redefinition of the test of shipowners' ability to limit liability to ensure that these limits can be broken in cases where there is demonstrable failure by the shipowner, for example, by reverting to the 'fault or privity' test in the 1969 CLC, or a similar alternative test (this test was used successfully for a period of many years which suggests a mechanism of this type is practicable).

OCIMF firmly believes that addressing the above key issues will ensure that the primary objectives of the Conventions are achieved, namely:

(a) Persons suffering damage from oil spills continue to be properly and promptly compensated;

(b) The scheme creates an incentive for a reduction in the occurrence of oil spills by providing a mechanism for encouraging improvements in maritime safety. This will only be achieved if shipowners, who are the sole responsible party for the quality of their ships, play a major part in the solution.

OCIMF has established that the changes proposed are perfectly feasible in legal terms.

1 Introduction

1.1 The membership of Oil Companies International Marine Forum (OCIMF) comprises virtually all the world's major oil companies.

1.2 The Civil Liability Convention (CLC) is a liability based system in which the owner of the spilling ship pays for the spill, up to a financial limit determined by reference to the size of that ship, and insures that liability through his P&I (liability) insurer. Once the CLC limit is exhausted, the 1992 International Oil Pollution Compensation (IOPC) Fund Convention is activated.

1.3 The 1992 International Oil Pollution Compensation (IOPC) Fund Convention is a contribution-based system funded by oil receivers in States party to the Convention in proportion to the volumes of their persistent oil cargo imports by sea.

1.4 With the adoption of the Protocol for the Establishment of a Supplementary Fund for the Compensation of Oil Pollution Damage at the IMO Diplomatic Conference on 16 May 2003, oil receivers in those States which become party to the Protocol will potentially face a more than three-fold increase in their contributions to the Fund. As a corollary, shipowners potentially have a significantly reduced share of responsibility for the compensation liabilities following an incident and, thus, no incentive to improve the safety of their operations.

1.5 The adoption of the Supplementary Fund means there is now a significant amount of compensation available to victims but the overarching issue of safety and pollution prevention has yet to be satisfactorily addressed. It is immutable that the compensation regime must be consistent with the general principle of safe operations and pollution prevention. This was one of the founding principles of the 1969 Liability Convention and was enshrined in the 1971 Fund Convention[<2>]. The regime currently has the unfortunate effect of increasing the risks of future pollution incidents by shielding shipowners from the financial consequences of major pollution, thus facilitating the continued operation of substandard ships. This has to be tackled by changing the relationship between shipowner liability and oil receiver contributions therefore exposing shipowners to significantly increased liability. If these issues are not addressed the international community will have effectively signalled that it is willing to pay for accidents irrespective of negligence, and this in turn gives no incentive for insurers and others to deny support to substandard vessels.

1.6 OCIMF members therefore have considerable interest in the review of the CLC and Fund Conventions and OCIMF presents the following information as part of its contribution to this important international discussion.

2 The Fund

2.1 Members of OCIMF have been actively involved in the development of the international oil spill compensation schemes since they were first introduced in the 1960s. We believe that there are two important criteria for such schemes:

(a) Persons suffering damage from oil spills should be properly and promptly compensated.

(b) The compensation scheme should be consistent with a general objective to improve maritime safety and reduce the occurrence of oil spills.

2.2 The first criterion has generally been met by the Civil Liability Convention and the International Oil Pollution Fund Convention which provide for funding by shipowners and oil receivers respectively, although the pollution from the foundering of *Erika* off France in 1999 and *Prestige* off the Galician coast in 2002 has focused attention on the amount of compensation available.

However, as explained later, OCIMF are concerned that the second criterion may be compromised.

2.3 The new limits adopted for the 1992 CLC and Fund Protocols, excluding the Supplementary Fund, resulted in an increase of some 50% of the compensation available for pollution damage and came into force in November 2003. This increase is supported by the international membership of OCIMF.

3 The Supplementary Fund – an additional level of immunity for substandard shipowners?

3.1 The 1992 Fund Assembly adopted a draft Protocol in October 2001 to establish an 'opt-in' Supplementary Fund which will provide a substantial additional fund for those States Parties who become signatories. The Protocol was adopted by a Diplomatic Conference held at the Headquarters of the International Maritime Organization (IMO) in London in May 2003. The total amount of compensation payable for any one incident will be 750 million Special Drawing Rights (SDR), including the amounts payable under the existing 1992 Civil Liability and Fund Conventions.

3.2 The Protocol will enter into force three months after it has been ratified by at least eight States which have received a combined total of at least 450 million tons of contributing oil in a calendar year. The Supplementary Fund will only pay compensation for pollution damage in the waters of States which are Parties to the Supplementary Fund for incidents which occur after the Protocol has entered into force.

3.3 OCIMF accepts that the costs of pollution clean up and compensation vary around the world and recognises the perceived need for such an 'opt-in' Fund in certain States.

3.4 However, a Supplementary Fund, funded in perpetuity, entirely by oil receivers, with no contribution from shipowners, will clearly distort the existing relationship between the liability of the spilling ship and the additional contribution made by the oil industry. This will shield low quality shipowners from the consequences of their actions and hence will provide no incentive to improve either the quality of their ships or the standards of operation. Nor will it provide a mechanism to assist P&I insurers to impose controls and conditions on the provision of insurance to shipowners. As such, an arrangement of this nature whilst increasing available compensation will nevertheless facilitate the continued operation of low quality vessels. OCIMF therefore strongly believes that it is essential for the shipowner either to have a significantly increased liability in CLC 92 or to have a meaningful stake in the Supplementary Fund, thereby providing a tangible incentive for quality ships and ship operations and maintaining the direct connection between the activities of the shipowner and the consequences of those activities.

4 The Supplementary Fund can only be an interim solution – enhancement of safety remains to be addressed

4.1 To preserve the global nature of the existing compensation system there was a need to take prompt action.

4.2 OCIMF has supported the Supplementary Fund being funded entirely by oil receivers in the opt-in countries but only as an interim solution. This support has been given despite the concern that the Supplementary Fund may be thinly populated, in its early stages, with a small number of contributors and that the cost impact on each contributor will potentially be very large indeed. Many of the contributors will be present in each of the 'opt-in' States and will therefore be major contributors in each of those States and to the Fund as a whole. Thus there will be a loss of mutuality both at State and contributor level.

4.3 The willingness of OCIMF to support such an interim funding arrangement was premised on the IOPC Fund Assembly working group concluding:

- a detailed analysis of the financial burden of oil spills in the past and future to ensure equitable apportionment of those costs between shipowners and oil receivers and;

- a meaningful review of shipowner liability (CLC).

4.4 Shipowners and their P&I insurers are proposing the introduction of a voluntary scheme to increase the 1992 CLC minimum liability threshold to 20 000 000 SDRs for all vessels, regardless of their gross tonnage, where they spill oil in waters of a state party to the Supplementary Fund.

4.5 OCIMF is concerned that the proposed increase by P&I insurers of the minimum liability threshold will still fall significantly short of the envisaged increased burden to the oil receiver in the revised overall compensation regime. It will therefore have no impact in terms of creating drivers to improve ship standards and operations. It is important to note that the original texts of the CLC and Fund Conventions **did not** contain any reference to equal sharing of liability[<3>] between shipowners and oil receivers, yet shipowners (and their P&I Clubs) have suggested that this is an immutable principle. However, as mentioned above, the original texts **did** refer to embracing 'conditions designed to ensure compliance with safety at sea'. OCIMF believes it is essential that this founding concept of the Conventions is recognised in the current debate. OCIMF further suggests that, as a matter of public policy, it must be a priority to prevent accidents and therefore it is questionable to promote legislation which financially protects the culpable behaviour which may result in environmental damage.

4.6 The above review and consideration of the financial burden of oil spills must take into account the effect on future P&I liabilities of the accelerated phase out of all single hulled vessels, the tighter voluntary inspection regimes of charterers, the increased stringency of the inspection regime under Port State Control, the tightening of Classification Society Standards and the ability of P&I Clubs to introduce formal arrangements by which they deal, through insurance premia penalty, with substandard vessels. These measures will only be truly effective if the one player with control over the vessel, ie the shipowner, has a more meaningful and responsible stake in the compensation regime.

5 A permanent, lasting solution is available

5.1 It is the sole and unique responsibility of the shipowner to provide and maintain a safe and seaworthy ship. This is a long established principle of maritime law that is enshrined in all the relevant International Conventions and against which there can be no rational or reasonable objection.

5.2 The CLC Convention provides for strict liability and channelling of liability. The 1969 CLC Convention introduced these very positive benefits to the victims of oil pollution, providing for prompt payment of admissible claims and reducing the need for litigation. The provision of these two facilities by shipowners and their P&I insurers was, however, at the cost of the CLC limits being maintained at a low level.

5.3 In the absence of any increase in the liability of shipowners under CLC, the exposure of oil receivers in States that are party to the Supplementary Fund will be wholly disproportionate to that of shipowners. An undesirable effect will be that owners and insurers of low quality ships will continue to be sheltered from the financial consequences of pollution that their ships have caused.

5.4 OCIMF believes that a permanent, lasting solution can only be achieved by either (i) including a layer, split between oil receiver and shipowner, in the Supplementary Fund, or, (ii) significantly increasing the limit of liability in CLC 92, or, (iii) a combination of (i) and (ii). There is adequate insurance available to provide for this. This would further ensure that low quality shipowners are neither subsidised in the future by quality operators within the mutual P&I insurance system or by

oil receivers, nor sheltered from the financial consequences of their actions and any resultant pollution incident. It would provide the good quality shipowners with a real incentive to continue improving their operational performance.

5.5 Meaningful shipowner participation in the compensation regime will be a visible demonstration of their desire to deliver a safe ship and a safe and environmentally responsible operation. This will also preserve the direct connection between activities of the shipowner and the consequences of those activities.

5.6 In recognition that spills from small vessels can be as expensive as spills from big vessels, and that it is therefore illogical and inappropriate to have a sliding scale limit of liability, OCIMF proposes for consideration a flat rate CLC limit to apply to all tankers regardless of size or capacity.

5.7 There may be possible adverse impacts of this proposal on domestic small ships in some States party to the CLC Convention. This can be overcome by adopting a provision similar to that used in the HNS Convention (Article 5) which enables States to exclude tankers under a certain gross tonnage engaged in domestic coastal trade from the application of the Convention and to impose their own national requirements on this sector.

Option 1

5.8 Figure 1 below illustrates the current CLC and Fund limits with the Supplementary layer shared between shipowners and oil receivers and a flat rate CLC limit of liability of 90 million SDRs for shipowners of all ships regardless of size.

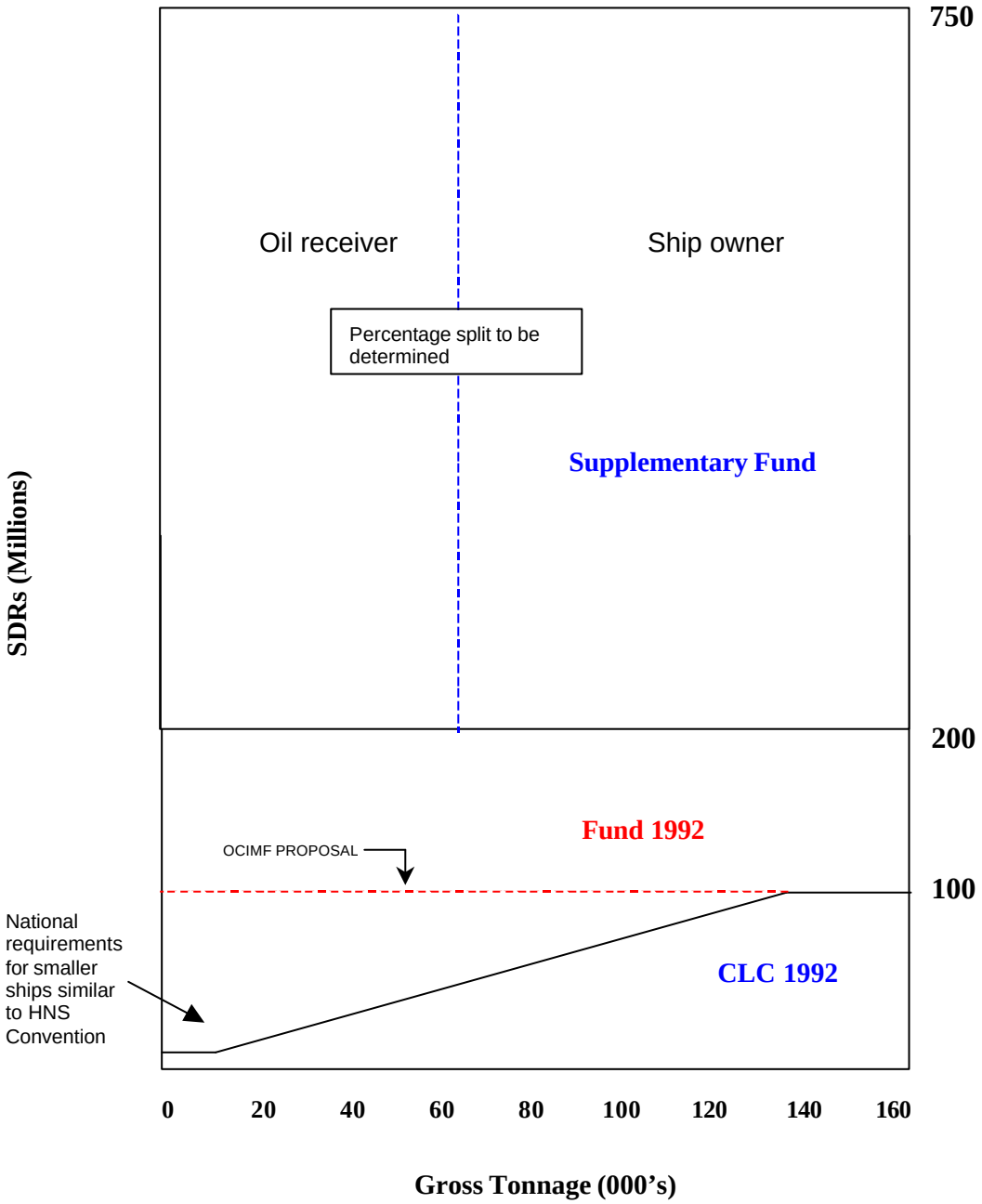

Figure 1

Option 2

5.9 Figure 2 below illustrates the current CLC limit with a significantly increased limit of liability under CLC, together with a corresponding increase in the 1992 Fund limit, and a flat rate limit of liability for shipowners of all ships regardless of size, (Precise figures have not been given in the sketch but it is OCIMF's position that shipowners should have a significantly increased stake in the compensation regime.)

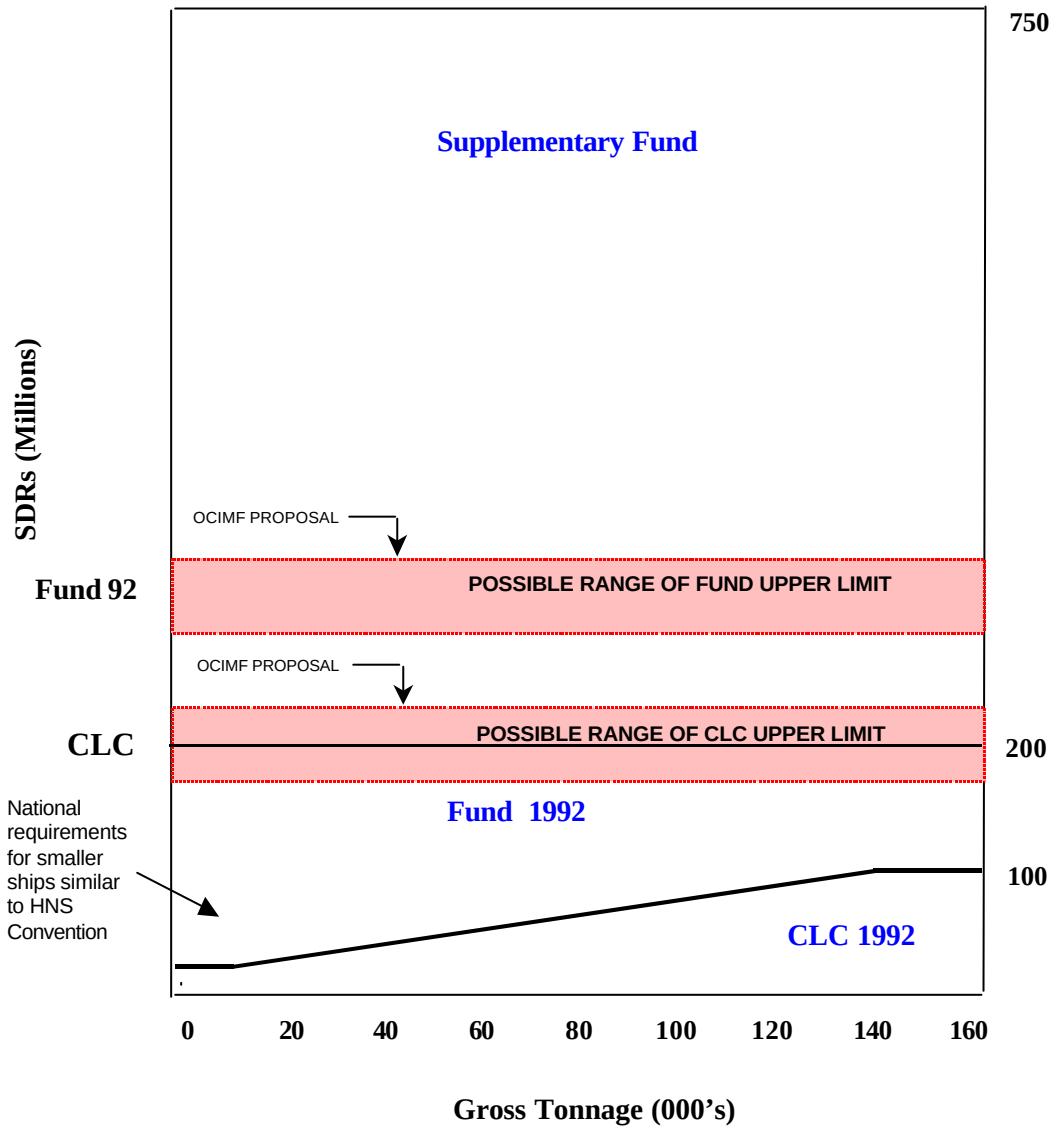

Figure 2

5.10 Furthermore, OCIMF proposes that all ships (subject to the option to exclude domestic coastal trade referred to above), which carry oil in bulk as cargo, regardless of the amount, should be required to maintain insurance or other financial security in accordance with Article VII of the Civil Liability Convention to cover liability for oil pollution damage.

Should the test for breaking the limits be changed? – a theme common to both options proposed

5.11 In keeping with the aim to have a scheme that is consistent with the principle of improving maritime safety and reducing the occurrence of spills OCIMF additionally proposes a redefinition of the test of shipowners ability to limit liability to ensure that these limits can be broken, in cases where there is demonstrable failure by the shipowner, for example, by reverting to the 'fault or privity' test in the 1969 CLC, or a similar alternative test. (This test was used successfully for a period of many years which suggests a mechanism of this type is practicable). In cases where there is a dispute between the shipowner and Fund as to whether the limit should be broken, the Fund should, in the interim period, compensate victims above the CLC limit until the dispute is resolved. This will ensure that the prompt payment of victims will not be compromised.

5.12 OCIMF is aware that the current test, is, in practical terms, all but impossible to breach and has the effect of providing no tangible incentive for substandard shipowners to improve their performance. OCIMF therefore believes that issues of responsibility and liability are matters that should be addressed by the international community and consideration should be given to a review of the test.

Note <1>:LEG/CONF.14/DC/4

1. REQUESTS THE 1992 Fund Assembly to continue to consider enhancements that can be made to the 1992 Liability Convention and the 1992 Fund Convention
2. URGES all Contracting States to the 1992 Liability Convention and the 1992 Fund Convention to place a high priority on the ongoing work towards a comprehensive review of the 1992 Conventions; and
3. REQUESTS the International maritime Organisation to consider the outcome of the deliberations within the 1992 Fund Assembly and to take appropriate actions as necessary.

Note <2>:International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971
Article 2
1. …"The Fund", is hereby established with the following aims:
..
(b) to give relief to shipowners in respect of the additional financial burden imposed on them by the Liability Convention, **such relief being subject to conditions designed to ensure compliance with safety at sea** and other conventions;"

Note <3> The preamble to the 1992 Fund Convention states that *"CONSIDERING FURTHER that the economic consequences of oil pollution damage ….. should not exclusively be borne by the shipping industry but should **in part** be borne by the oil cargo interests,"*