INTERNATIONAL OIL POLLUTION COMPENSATION FUND 1992

THIRD INTERSESSIONAL
WORKING GROUP
Agenda item 2

92FUND/WGR.3/19/9
13 February 2004
Original: ENGLISH

REVIEW OF THE INTERNATIONAL COMPENSATION REGIME

Submitted by the International Group of P&I Clubs

Summary:	See Executive Summary
Action to be taken:	The Working Group is asked to note the views expressed in the following submission.

Executive Summary.

The International Group believes that the three outstanding issues before the Working Group do not justify re-opening the Conventions for the following reasons:

(a) Shipowner's right to limit.

(i) If this were weakened the result would be that the oil industry would very rarely be involved in compensation in respect of oil pollution damage. States may find that this is politically unacceptable.

(ii) The compensation system cannot be used to punish the substandard operator. Insurers already have stringent terms in their policy conditions and shipowners who incur more claims already pay more by way of premium. Exposure to large claims falls randomly on all shipowners and should be shared by the shipowning community.

(b) Channelling.

Without channelling the efficiency of the compensation system would suffer because litigation would be inevitable.

(c) Sharing.

The share of compensation borne by the shipping and oil industries historically have been roughly comparable. This position is expected to be maintained in the future by voluntary contribution from the shipowner.

The issue of substandard shipping is addressed in a separate submission from the International Group of P&I Clubs (document 92FUND/WGR.3/19/10).

1 Introduction

1.1 The work of the Third Intersessional Working Group has reached a watershed. It has successfully addressed the principal reason why it was brought into being by undertaking the preparatory work for the Diplomatic Conference at which it was agreed to make provision for an optional Supplementary Fund. However, there are other issues outstanding which can only be addressed by revision of the 1992 Conventions. If such a revision were to take place it would inevitably be broad in scope and would, equally inevitably, require an enormous amount of preparatory work. Moreover, the transition from the present system which has been adopted in 86 States would plainly give rise to substantial upheaval. This upheaval could be contemplated if it were demonstrated that the Conventions were seriously flawed. However, without such justification it would be a serious mistake to disturb one of the most successful initiatives in international legislation which has provided a compensation system which has served the victims of oil spills well for thirty years without in general having to resort to litigation. The purpose of this submission is to explain why the remaining issues do not justify re-opening the Conventions.

1.2 The Working Group agreed at its last session to address the issues identified by the Assembly in the manner which had been proposed by the Chairman (see paragraph 5.1, document 92FUND/WGR.3/15) which in effect isolated those issues which, in the view of some delegations, would justify the re-opening of the Conventions. These are:

(a) the level of shipowners' limitation amount and its relationship with the liability funded by the oil receivers;
(b) the test to determine the shipowners' right to limitation; and
(c) channelling of liability.

However, despite vigorous debate, conclusions on these issues were deferred until the IOPC Funds' Secretariat had prepared claims statistics based on data provided by the International Group.

2 Statistics

Paragraph 6.19 of the Report of the fifth meeting (document 92FUND/A/ES.7/6) suggests that the study to be carried out by the Secretariat should reflect the costs of past spills and the apportionment of those costs between the shipping and oil industries on the basis of values in 2003 and the likely values in the future, taking into account inflation indices for individual States. These informal terms of reference are sufficiently broad to permit a number of different approaches so that by applying inflation indices and other assumptions in different ways the results may differ, demonstrating that either ship or cargo interests would have contributed more over time. This study will undoubtedly provide interesting background information but since both ship and cargo interests have contributed roughly comparable amounts in cash terms over the period covered by the study, its conclusions should not of themselves determine the views of the Working Group on the outstanding issues which are considered below.

3 The test to determine the shipowners ' right to limitation.

3.1 At the last session of the third intersessional Working Group some States argued that the shipowner should be denied the right to limit liability if negligence could be proved. Before going on to consider the merits of this suggestion it is worth examining more closely the consequences of this proposition. As virtually the sole providers of CLC certificates the Clubs have been involved in most of the major spills that have taken place during the last thirty years. It is not an exaggeration to suggest that most of those spills have involved an element of negligence, ranging from the substantial to the trivial – even involving vessels of impeccable quality like the *Amoco Cadiz* or *Exxon Valdez*. If in all these cases the shipowner were to lose the right to limit liability then the IOPC Funds and cargo interests would not be required to contribute at all.

3.2 It is suggested that States might find this consequence politically unsustainable for the following reasons:

(a) as a general matter the public perception is that spills are a consequence of the carriage of oil which yields substantial profits to the oil companies.

(b) When a substandard vessel is employed to carry an oil cargo the public is increasingly aware that cargo interests may have been seriously at fault in chartering a substandard vessel when the more responsible approach adopted by some companies would require looking at factors other than cost alone.

(c) As recent spills have demonstrated once again, the damage arising from oil spills reflects the nature of the cargo carried. In the public perception it would be wrong for the owner of a cargo like heavy fuel oil to escape all responsibility, particularly when he has arranged carriage on a substandard ship.

3.3 Leaving aside the consequences of the proposal that the right to limit should be lost in case of negligence, it is necessary in order to consider the issue properly, to look into the historical background.

4 Historical Background.

When the *Torrey Canyon* went aground in the English Channel in 1967 claimants (principally the UK government) faced not only jurisdictional problems but also questions concerning title to sue. These problems were squarely faced by the Conferences which broke new ground in agreeing the 1969 International Convention on Civil Liability for Oil Pollution Damage (CLC) and the 1971 International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage (Fund Convention). The touchstone adopted at these Conferences was that victims should not have to shoulder the financial burden of pollution arising from oil spills at sea but would instead receive rapid and adequate compensation in accordance with the Polluter Pays Principle. Then, as now, there were sterile arguments about the identity of the 'Polluter' – on the one hand it was argued that it was the nature of the cargo that caused the damage and that oil receivers should therefore be characterised as the 'Polluter' and made solely liable. On the other hand it was argued that the shipowner should be regarded as the 'Polluter' because he had taken charge of the cargo and that he therefore should be solely liable. In the event the Conferences pursued the goal of providing an efficient compensation system. The proportions in which the two industries were to contribute were originally determined by events: during the preparatory work on CLC (which had been undertaken by the CMI) there had been much support for the proposal that all liability should be shouldered by the oil receivers but this was deflected on the understanding that the oil industry would respond in excess of the limit of the shipowners' liability determined by the then capacity of the insurance market. The notion of sharing which guided the 1984 revision conference was developed from this de facto split in responsibility.

5 Compensation not Punishment.

5.1 In order to facilitate ready recovery, liability under CLC was not imposed on the party at fault but on the party most easily identified, that is the registered owner of the tanker. Equally, the cargo contribution was levied not against the individual oil company concerned, but against the IOPC Funds to which all oil receivers contributed. However it was recognised that the corollary of this simplicity was that the individual ship operator, who may have been negligent in the operation of the ship, or the individual oil company charterer, who had chartered a substandard vessel, would not be punished and would not have to bear any individual liability under the Conventions. The system has worked well in practice since claimants do not have the burden of establishing the liability of the 'guilty' party and payments can be quickly made. However, the consequences of this enviably efficient system are that in several recent cases, notably the *Erika* and the *Prestige*, it

has been alleged that substandard shipowning and chartering practices have not been sufficiently punished by the imposition of liability.

5.2 The criticism of the existing system and the allegations outlined in the previous paragraph rest on two misunderstandings:

6 Does good behaviour follow the imposition of liability?

A shipowner who incurs claims will have to pay a higher premium and this will obviously affect his behaviour. However, because of the pooling arrangement explained in the following paragraph, the effect is only really felt at relatively low levels of liability. In the experience of the Clubs, there is no evidence that there is a necessary link between the imposition of civil liability at high levels and the quality of ships and their operators. A shipowner whose liability in respect of any risk is substantial will already have taken all available steps to minimize that liability and the imposition of further liability is unlikely to produce any further improvement. Furthermore, it is the function of mutual insurance to absorb high level liability by spreading the cost across the whole shipping industry. A shipowner, like other commercial parties, is always able to insure his potential liability (and under CLC is compelled to do so) with the consequence that the direct link between liability and conduct is lost, particularly at the higher level of liability. Insurers in their turn try to ensure that the ships and ship-operators they cover are of an appropriate standard but, even though the Clubs run extensive survey programmes in order to supplement the work of Classification Societies and Port State authorities, it is not possible for insurers alone to compel the proper performance of the shipowner's obligation to ensure that all ships are maintained and operated to an appropriate standard. This obligation must be encouraged in practice by other methods: Port State Control, the vetting procedures of oil company charterers and the introduction of the ISM Code are all having a beneficial effect in this connection. The Clubs already try to ensure ship quality by the steps outlined in a separate submission (document 92FUND/WGR.3/19/10). However, it is recognised that this issue can only be tackled on an industry-wide basis and will require the involvement of States.

7 Can the individual be punished by the imposition of liability?

7.1 The Clubs in the International Group share the liability risks of over 90% of the world's tonnage. Their cover is structured in such a way that the individual owner will bear the first layer of any claim, typically $10 000, and the excess of the that amount up to $5million will be covered by the Club in which the vessel is entered. If an owner incurs claims his premium for the following year will reflect that since premium is based on record. This is obviously an incentive towards better performance. However, claims in excess of $5million are shared under the Pooling Agreement by all Clubs and the incremental cost of such large claims is of necessity spread across the industry and not focussed on the individual assured. Therefore, just as all oil receivers share in the funding of pollution claims falling on the Fund, so major claims under CLC are in practice borne by all shipowners. The drafters of the original Conventions were well aware of this structure and the benefits it provided which is why the burden of the compensation has been shared across the totality of the industries concerned, the shipping industry and the oil industry.

7.2 The background which has been sketched in the paragraphs above will serve to illuminate why many of the suggestions made in the aftermath of the *Erika* and *Prestige* are not well-founded. The following paragraphs will examine particular issues and seek to explain why it is not possible to maintain the present efficient compensation system at the same time as introducing elements which would be more responsive to the 'moral' point of view.

8 The Right to Limit under CLC

8.1 In order to maintain the sharing of the burden between the tanker and oil industries it is essential that the shipowner, the responsible party under CLC, should be entitled to limit his liability. Moreover, it is important that the right to limit should be very clear in effect since it is an integral

part of the compensation system that both paying parties should be clearly aware at the outset of their exposure in relation to each incident. Anything that would encourage regular litigation by the Fund on this point following spills would risk a breakdown in the current close co-operation between the Clubs and the IOPC Funds, resulting in compensation payments being delayed to the detriment of victims.

8.2 These points were well understood by the delegates to the first revision Conference in 1984: Article V.2. of CLC 1969 provided that the shipowner would lose his right to limit if it could be shown that the incident was caused by his 'actual fault or privity'. However, litigation in several jurisdictions had demonstrated that the courts were construing this test as bordering on simple negligence, thus undermining the purpose of the Convention. The consequence was that in 1984 the more stringent test (which had first been introduced in LLMC 1976) was adopted, which provided that the shipowner would lose his right to limit if it was proved 'that the pollution damage resulted from his personal act or omission, committed with the intent to cause such damage, or recklessly and with knowledge that such damage would probably result'. In this way the revision Conference of 1984 ensured that the aim of the compensation system established in 1969/71 would be maintained by avoiding needless litigation about degrees of negligence while ensuring the sharing of the burden between the two industries involved.

9 Channelling of Liability.

As explained above, the drafters of the 1969/71 system deliberately imposed strict liability under CLC only on the registered owner. Their purpose in doing so was to facilitate the bringing of claims and their swift conclusion, even though it was recognised that the registered owner may not have been involved in the operation of the ship at all and might be, for example, a bank or leasing company. If this were not done and an attempt were made instead to impose liability on the negligent charterer or operator then litigation would inevitably ensue in order to determine whose fault had given rise to the spill. The victim would remain uncompensated until the litigation had been concluded. The public may abhor the fact that an operator is not held immediately liable for the consequences of a spill which has been caused by his negligence. Nonetheless, it is suggested, and has been recognised by successive revision Conferences, that this is a price that should be paid in order to ensure prompt compensation to victims – particularly bearing in mind that the liability of the registered owner is covered by compulsory insurance. Moreover, it should always be borne in mind that although the victim will only be able to claim against the registered owner, the recourse action that the owner will undoubtedly bring in domestic law will ensure that any other party at fault will be ultimately held liable – but without impeding the action of the claimant.

10 Sharing the Burden.

Claims history suggests that third tier in excess of the 2003 CLC and Fund limits would rarely be called upon. Nevertheless, instead of voluntarily increasing the limits for small ships, the Clubs and their shipowner members are prepared to explore other voluntary proposals to address the oil industry's concerns about the impact of the Supplementary Fund on the concept of sharing if that issue is also of concern to States, since it is recognised that voluntary industry solutions on sharing can obviate the legal and practical problems that would arise if the Conventions were formally amended.

11 Conclusion.

We remain strongly of the view that the international compensation system regime for oil pollution damage has been remarkably successful. We fear that attempts to amend the substance of the Conventions will destroy the system while failing to produce any dividend in terms of improvements in performance from the perspective of claimants. Any transition to a new system would take many years and require a great deal of preparatory work. This upheaval could be contemplated if it had emerged that the Conventions were seriously flawed, but the detailed work

of the Working Group has revealed no such flaws. We would therefore urge that no attempt be made to re-open the Conventions.
