INTERNATIONAL
OIL POLLUTION
COMPENSATION
FUND 1992

THIRD INTERSESSIONAL
WORKING GROUP
Agenda item 2

92FUND/WGR.3/22/2
11 May 2004
Original: ENGLISH

REVIEW OF THE INTERNATIONAL COMPENSATION REGIME

AMENDMENTS TO THE CIVIL LIABILITY AND FUND CONVENTIONS

A discussion paper

Submitted by Spain and France

Summary:	At its 7th meeting in February 2004, the Working Group examined various proposals aimed at promoting quality shipping by the use of disincentives. This paper follows this approach and presents some draft amendments to the 1992 Civil Liability Convention.
Action to be taken:	See paragraph 9

1 Introduction

1.1 At the 7th meeting of the third intersessional Working Group in February 2004, three documents were introduced (documents 92FUND/WGR.3/19/7, 92FUND/WGR.3/19/8 and 92FUND/WGR.3/19/12) relating to the question of quality shipping and the way to insert into the 1992 Civil Liability Convention (CLC) and the 1992 Fund Convention disincentives to deter substandard shipping. At the end of a thorough debate interested delegations were invited to prepare draft texts in order to make clear the possible impact of the proposed changes. The French delegation, whose submission had attracted interest from various countries, was also requested to present a revised text. The present submission is in response to that invitation.

1.2 First of all, the sponsoring delegations want to reaffirm their constant preoccupation that any changes made to the 1992 Conventions should not hinder the payment of prompt and adequate compensation to victims. This has been the rationale of all previous proposals and is considered as being of paramount importance.

1.3 It is the view of the sponsoring delegations that in most cases, the current regime, offering a civil liability regime seconded by a mutual regime, has been successful. This has been particularly the case where incidents occurred due to unforeseeable events. In such cases, the civil liability regime, as a non fault-based regime, has proven to be a very adequate framework for prompt compensation to victims.

1.4 This said, it has to be acknowledged that some changes to the current regime have to be introduced in order to address its most unacceptable feature which is to offer the same protection to all shipowners, regardless of the way they maintain their ships.

1.5 It is the strong view of the sponsoring delegations that quality shipping is a comprehensive policy and that all IMO conventions within their respective areas should aim at enhancing safe and quality shipping.

1.6 As one of those instruments, the CLC does have an impact on that comprehensive policy. On the other hand, it is also well acknowledged by the legal doctrine that the principle of civil liability in itself constitutes an important part of a prevention policy because of the threat it places on the liable parties of being faced with having to pay compensation. As it was stated several times within the Working Group the international regime is not only a compensation regime, as some delegations maintained, but is primarily a liability regime.

1.7 Turning to the way in which differentiation could be introduced into the current regime, the following points should be addressed:

- What are the situations most unacceptable under the current regime and how can they be defined?
- Is the present test for denying the shipowner's right to limit his liability a valid test to address this situation?
- Is the test effective?
- What steps could be taken to strengthen its effectiveness?
- What would be the effect of such steps as regards the position of victims?

2 What is the situation to be addressed?

2.1 As it has been stated, the only cases that have shown unacceptable protection of shipowners under the present regime are those where the incident which caused the damage was due to a **structural defect** of the ship concerned (*inter alia Tanio, Nakhodka, Erika*). Such a defect may have two causes which are often cumulative: the age of the ship or the poor maintenance of it.

2.2 The present proposal seeks to address this issue but it is not the intention of the sponsoring delegations to embark on a theoretical definition of so called 'substandard' ships.

2.3 To deal with this issue and in order to achieve uniformity in the application of the Convention it may be necessary to add to the present Article 1 the following definition of the concept 'structural defect' which differs from the non-compliance with statutory requirements:

'Structural defect': means a defect due to decay or lack of maintenance of a ship, in part or whole, which is contributing to the incident.

2.4 This wording emphasized that not all defects or lack of maintenance may be considered as structural defects, but only those which contribute to the incident. For instance a helm damage is a well known event and seamen are trained to take remedial measures. If such an event occurs, it will not constitute as such a structural defect, but it will if it can be shown that this damage was due to the fact that there was no maintenance of the steering-gear.

3 Is the current wording of the text appropriate to deal with such situations?

3.1 Article V.2 of CLC stipulates:

> 'The owner shall not be entitled to limit his liability under this Convention if it is 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.'

3.2 It is the assumption of the sponsoring delegations that pollution damage resulting from a structural defect of a ship clearly falls under the scope of this provision. Poor maintenance up to a degree resulting in an incident would constitute 'omission of the owner committed recklessly and with knowledge that such damage would probably result'.

3.3 If there is a consensus on that meaning of the wording of the Convention, there would be no need to change the current text. If it is not the case, a new sentence should be added to introduce this exception from the right to limitation of liability, which could be worded as follows:

'A shipowner shall not be entitled to limit his liability if the pollution damage occurred due to structural defect of the ship at the origin of the incident.'

However it has to be considered how such a provision should be applied?

At this point, two options may be considered:

Option 1: **it is for the claimant to prove the structural defect**. No change is needed in the present wording of the Convention.

Option 2: **it is for the owner to demonstrate that the incident did not occur due to structural defect**. If such an option were to be retained, it would be necessary to add a provision to the existing text, for instance a new paragraph inserted between Article V.1 and Article V.2 which could read as follows:

'**To be entitled to benefit from the right to limitation provided for in paragraph 1 of this Article, the owner shall satisfy the competent court under Article IX of the present Convention, that the incident did not occur due to a structural defect.**'

3.4 If, at first sight, option 2 seems to be more straightforward and puts the burden of proof on the shipowner, experience shows that, in such cases, the gathering of evidence may take considerable time and that *prima facie* evidence disclosed by the shipowner on the maintenance of the ship (ie paper evidence) may be contradicted by facts and samples. In such conditions it may be difficult to decide immediately if the shipowner has the right to limit his liability.

3.5 Such questions have to be taken into account when the effects of the proposed 'new test' on prompt compensation of victims is considered.

4 Would such a test be sufficient to eliminate the use of such ships?

4.1 The aim of any test for denying the shipowner their right to limitation of liability is to sanction a behaviour which falls below the standard reasonably expected from a prudent shipowner. When the owner fails to comply with this principle he has to bear the economic consequences of his behaviour.

4.2 But it has long ago been pointed out that shipowners using poorly maintained ships protect themselves from the economic consequences of their behaviour by creating separate legal entities, limiting their liability to the assets of the company that owned the ship at the origin of the incident.

4.3 It has also been demonstrated that when the shipowner is deprived of his right to limitation, his insurer may be relieved from his duty to provide cover.

4.4 In that sense, even the 'new test' will not in itself constitute a sufficient deterrent to use ships in poor condition.

5 What could be done to make the test effective?

5.1 The conclusion of the previous paragraph shows the need to make other parties that are involved in the operation of such ships affected by the financial consequences of incidents.

5.2 As stated at the beginning of this document, quality shipping requires constant vigilance from all parties involved. As for the particular issue of incidents due to structural defect of ships, Flag States are the most concerned because of their international liability which may be challenged according to Article 94-6 and part XV of the United Nations Convention on the Law of the Sea (UNCLOS).

5.3 However, within the private sector of the shipping industry there are also other key players who cannot be ignored, such as classification societies, P&I Clubs and charterers.

5.4 As far as the CLC is concerned, it seems that the classification societies, although being of primary importance in the overall quality shipping chain, are not at stake because they do not fall within the scope of this liability regime and they do not have any special involvement in the direct functioning of the regime. The situation is not the same in respect of insurers and charterers.

6 Involvement of P&I Clubs

6.1 At the 7th meeting of the Working Group several delegations supported the views expressed in document 92FUND/WGR.3/19/7, and it was decided to give consideration to the ongoing OECD work concerning the role of insurance in shipping. However, since the 8th meeting of the Working Group, which will examine this study, will take place at the same time as the Maritime Transport Committee of OECD, it seems premature to draw conclusions from this study at this stage.

6.2 Nevertheless, as was pointed out in the document submitted by France at the last meeting of the Working Group, attention should be drawn to some aspects of the role of P&I Clubs and their relationship with shipowners.

6.3 P&I Clubs, which grant insurance cover to tanker owners, are at the core of the system for various reasons, the most evident being that without such cover any tanker carrying more than 2 000 tons of oil would not be allowed to operate.

6.4 On a more factual basis, P&I rules give the Club the means to be fully aware of the maintenance of the ship and in fact, they are - as demonstrated by the handling of the *Alambra* incident, where the Club disclosed very detailed information that was not even in the log book.

6.5 In order to illustrate this relationship between shipowners and P&I Clubs, reference should be made to the common rules concerning pre-entry survey and obligation to notify the Club of all changes. Those rules clearly show that P&I Clubs are constantly aware of current ship incidents (by virtue of a specific rule providing that if the Club is not informed of the occurrence of an incident, the insurance cover does not apply) and their degree of maintenance.

6.6 P&I rules provide for disclosure to the Clubs of other information which is not available to third parties. For example, concerning entry of fleet, a rule which is common to all Members of the International Group of P&I Clubs reads:

> 'where more than one ship is entered by one or more Members and the managers agree in writing that those ships will be treated as a single fleet for underwriting purposes, those

members, if more than one, shall be jointly and severally liable for all and any obligations arising under those rules as to payment of premiums and for the purposes of the same shall be deemed to be a single member and the entered ships deemed to be entered on that single Member's behalf.'

6.7 Such a rule allows Clubs to know, for underwriting purposes, who are the beneficial owners of single ship companies.

6.8 Furthermore, it has also to be taken into account that according to available statistics, there are in fact not so many shipowners. The world tanker fleet consists of about 7 500 units, half of which being under 10 000 dwt. It appears from the figures made available by Intertanko, whose members are independent owners of tankers of more than 10 000 dwt, that the ownership of the 2 137 tankers entered in this association is concentrated among 235 members. It must also to be recalled that some big independent companies owning several dozen tankers are not members of Intertanko, the same being the case in respect of state or oil company owned tankers.

6.9 In conclusion, the real ownership of the world fleet is not so widespread as it may appear through the numerous separate legal entities which are created in order to operate it. In that sense it may be appropriate to put P&I Clubs, because of their intimate knowledge of ships and owners, at risk of having to pay when an incident occurs due to structural defect of the ship.

6.10 The sponsoring delegations of this paper acknowledge the statements made by representatives of the shipping industry according to which they intend to put in place a thorough examination policy and to use premium rates as a disincentive. This is a welcome step towards an involvement of P&I Clubs as key players in quality shipping. However, as regards the last proposal, it has to be said that differentiation of premiums alone is not considered sufficient to eliminate the use of such ships because premiums may vary but will still be related to the limitation amount which in no way reflects the damage value. In order to be a deterrent for such shipowners, premiums should equal the risk.

6.11 Such a policy alone might result in ships fleeing towards other Clubs with a less strict policy, which does not meet the objective. That is why, to counterweight such a negative effect, it seems necessary to put all providers of insurance cover at risk of having to pay for damage caused by such ships.

6.12 In order to meet this aim, it is proposed to modify Article VII.8 of CLC i to read:

'Any claim for compensation for pollution damage may be brought directly against the insurer or other person providing financial security for the owner's liability for pollution damage. In such case the defendant may, even if the owner is not entitled to limit his liability according to Article V, paragraph 2, avail himself of the limits of liability prescribed in Article V, paragraph 1,**except when the incident was caused by structural defect of the insured vessel**'

6.13 The question of the extent of the additional financial burden which such an amendment would impose on insurers is not dealt with in this document. Should the Working Group retain the proposed modification, this question should be addressed and three options should in this case be considered:

- an unlimited obligation to compensate;
- an obligation to compensate within the framework of the P&I oil pollution coverage rule, ie up to US$1 billion;
- another amount to be agreed upon.

7 A systematic approach to recourse actions

7.1 The Working Group has made a thorough examination of the channelling provisions and has concluded that to deviate from the present wording would lead to considerable difficulties in the prompt payment of compensation to victims. But, at the same time, it seems that, in the situations addressed in this submission, there is a duty to exert the right of recourse which is given to the 1992 Fund, regardless of the prospects of the outcome of such an action.

7.2 Up to now, whereas the Assembly of the Fund has decided that recourse actions should be pursued every time there are legal grounds to do so, the practice of this principle shows that, in fact, financial prospects have often lead to postpone or refrain from taking such actions.

7.3 It is the view of the sponsoring delegations that there is a need to take in such cases systematically recourse actions against the shipowner and against the charterer. The aim of such actions may not be to recover money but to prevent the persons behind the legal entity from having the right to create such new entities.

8 What could be the effect of such modifications upon victims?

8.1 Such modifications do not change the normal functioning of the Conventions. The only change is that if a structural defect is proven the shipowner and his insurer may not be entitled to benefit from the limitation of liability.

8.2 In practice, it may require time to prove such a defect. However, this may not be a valid argument to delay the payment of compensation to victims by the shipowner/insurer, because what is at stake is not the limitation amount but 'extra' funding. If the limitation amount is exhausted, the 1992 Fund and, when it has entered into force, the Supplementary Fund would provide further compensation. That is to say that the question of proving the structural failure will ultimately be dealt with between the shipowner/insurer and the IOPC Funds, without prejudice to victims.

9 Action to be taken

The Working Group is invited:

(a) to take note of the information provided in this document; and

(b) to express its opinion upon the proposals set out in paragraphs 2, 3, 6 and 7.