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COMPENSATION
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INCREASE OF THE WORKING CAPITAL

Note by the Director

Introduction

1 Under Financial Regulation 5.1(a) and (c), the IOPC Fund shall have a general fund which shall be used:

(a) for the satisfaction of claims arising from "smaller" incidents, ie incidents where the aggregate amount to be paid by the IOPC Fund does not exceed 15 million (gold) francs (1 million SDR);
(b) for the payment of the first 15 million (gold) francs in respect of "larger" incidents;
(c) to meet the administrative costs and expenses of the IOPC Fund;
(d) to make provisional payments pursuant to Internal Regulation 8.6; and
(e) to make loans to a major claims fund for the satisfaction of claims to the extent that sufficient money is not available in that major claims fund.

2 The general fund shall be maintained at such a level as the Assembly may decide from time to time (Financial Regulation 5.1(b)).

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 IOPC Fund exceeds 15 million francs. Such a major claims fund shall be used for the payment of claims arising from the relevant incident, provided that the first 15 million francs in respect of each incident are to be paid from the general fund (Financial Regulation 5.2(a) and (d)).

4 In 1979, at is 2nd session, the Assembly decided that the IOPC Fund should maintain a working capital of £2 million. The working capital should include the initial contributions and annual contributions raised to meet claims in respect of "smaller" incidents, and it would be available to meet such claims and the necessary administrative expenses of the IOPC Fund. 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 of £2 million (document FUND/A.2/16/1, paragraph 9).

5 When the Assembly took its decision as to the level of the working capital, the IOPC Fund had 15 Member States. As at 1 November 1988, the IOPC Fund will have 40 Member States. It is likely that more States will soon join the IOPC Fund. The larger the number of Member States, the greater the risk that the IOPC Fund will be called upon to pay compensation for oil pollution incidents. Inflation has also eroded the value of the amount at which the working capital was fixed in 1979. The question has arisen whether the working capital should, therefore, be increased.

Experience Regarding the Payment of Claims

6 Since its establishment, it has been the policy of the IOPC Fund that victims of oil pollution incidents should be compensated as soon as possible. This policy has been underlying the decisions of the Assembly and the Executive Committee in respect of claims settlements and it has guided the Director in his negotiations with claimants. The IOPC Fund has also obtained a reputation of rapid payment of claims. In respect of minor and medium-sized incidents, payments are normally made within a short period of time, provided that claims are submitted rapidly and that they are accompanied by sufficient supporting documentation. However, rapid payments can only be ensured if the IOPC Fund's working capital is maintained at an appropriate level.

7 So far, the IOPC Fund has been able to make rapid payments in spite of the fact that the working capital has been as low as £2 million. This has been possible partly because an additional amount of £3-4 million has been available, since 1984, in the TANIO major claims fund. The Director has been able to use all the money available in the general fund for payments of accepted claims with the knowledge that the money in the TANIO major claims fund could be used for the payment of further claims in respect of incidents other than the TANIO, if the need were to arise (cf Financial Regulation 5.2(d)).

8 The total assets invested by the IOPC Fund in recent years has normally been in the region of £6 million. It has been possible, therefore, to spread the maturity dates of the investments over the year, thus ensuring that amounts of £500 000 to £1 million would always be available at short notice. This has considerably facilitated the settlement negotiations with claimants and the rapid payments of accepted claims.

9 Under Internal Regulation 8.4.1, the Director may make final settlement of any claim for compensation under Article 4 of the Fund Convention without the prior approval of the Executive Committee, if he estimates that the total cost to the IOPC Fund of satisfying all such claims arising out of the relevant incident is not likely to exceed 25 million francs (1.67 million SDR), which corresponds to approximately £1.25 million. The same limit applies in respect of the Director's authority to settle claims for indemnification of the

shipowner under Article 5 of the Fund Convention (Internal Regulation 9.5). The Executive Committee may authorize the Director to settle claims beyond this limit in respect of a particular incident (Internal Regulations 8.4.2 and 9.6, respectively).

10 Under agenda item 13, the Assembly will be invited to consider a proposal by the Director that the balance on the TANIO major claims fund should be distributed to contributors as at 1 February 1989, pursuant to Internal Regulation 4.4.1 (document FUND/A.11/10). If this proposal were to be adopted, thereafter only the working capital would be available as a reserve for the payment of claims which have not been taken into account in the assessment of the amount to be levied as annual contributions. This would apply to incidents which have not yet occurred when the Assembly decides on the levy of contributions. It would also apply to incidents which have occurred before that decision is taken but in respect of which it is not possible at that stage to estimate the amount that the IOPC Fund will eventually be called upon to pay, or in respect of which the amount actually to be paid by the IOPC Fund exceeds the estimate which forms the basis of the assessment of contributions. In the view of the Director, this could frequently lead to difficulties in carrying out the IOPC Fund's policy of paying compensation rapidly, if the working capital were to remain as low as £2 million.

11 It is obvious that there is a considerable uncertainty in the estimates that form the basis of the Assembly's decision to levy annual contributions. This is partly due to the comparatively long time period involved. It has been the policy of the Director to include in his estimates only those incidents in respect of which the IOPC Fund's payments can be assessed with a reasonable degree of accuracy. However, the decision to levy contributions is normally taken by the Assembly in October, say in October 1988. The contributions decided by the Assembly the following year (ie in October 1989) are not payable until 1 February 1990, ie more than 15 months after the decision on the 1988 contributions was taken.

12 It would be possible to keep the working capital at a low level if the above-mentioned estimates included figures based on a pessimistic evaluation of the amounts to be paid by the IOPC Fund in respect of incidents where there is a large degree of uncertainty as to the level at which the claims will finally be established. However, this would be at variance with the method of assessment applied so far, and the Director is not in favour of a change in this direction. As an illustration of this point, reference is made to the Director's estimates in respect of the THUNTANK 5, ANTONIO GRAMSCI, AKARI and AMAZZONE incidents in document FUND/A.11/12.

13 One possible solution would be for the IOPC Fund to rely on the possibility of taking loans. Under Internal Regulation 10.1, the Director may make arrangements to obtain short-term credit facilities or loans to meet the cash-flow requirements of the IOPC Fund, if the annual contributions determined by the Assembly do not in fact provide sufficient and timely funds for payments to be made for the satisfaction of claims, provisional payments or other expenses incurred in the operations of the IOPC Fund. However, bank loans are comparatively expensive. In addition, in the view of the Director it would not

be appropriate for the IOPC Fund to rely on the possibility of raising money by way of bank loans. The Director considers, therefore, that the working capital should be sufficiently large so that bank loans are not required for the rapid payment of accepted claims, at least not in normal circumstances.

The Director's Proposal

14 The Director considers that the working capital should be kept at a level which is sufficiently high so as to enable the IOPC Fund to make rapid payments of compensation and indemnification in respect of accepted claims without having to resort to taking bank loans. The existing level of £2 million may be insufficient if the Director wishes to make rapid settlements in respect of several incidents where the aggregate amount of compensation to be paid by the IOPC Fund is near the limit of his authority, ie 1.67 million SDR (approximately £1.25 million). The Director is of the opinion that the working capital should be kept at a level which would enable him to make payments rapidly up to approximately £1 million each in respect of at least three incidents which were not taken into account when annual contributions were assessed by the Assembly the previous year (either because the incident had not yet occurred or, in respect of incidents that had occurred, because it was not yet possible to make any accurate assessment of the amount to be paid by the IOPC Fund), as well as payments in respect of some new small incidents and some payments of indemnification to shipowners.

15 As mentioned in paragraph 8 above, in recent years the total assets of the IOPC Fund which could have been used for payments have been normally in the region of £6 million, in view of the reserve in the TANIO major claims fund. The Director considers that a working capital of £6 million would be reasonable. However, he acknowledges the desirability of limiting the financial burden on contributors and is of the opinion that it would be possible to operate the IOPC Fund in a satisfactory manner with a working capital of £4 million. For this reason, the Director proposes that the working capital of the IOPC Fund be increased from £2 million to £4 million.

16 If experience were to show that, as a result of the growing membership or other factors, a working capital of £4 million (or such other amount as the Assembly may determine) is insufficient, the Director would bring the matter to the attention of the Assembly.

Financial Consequences for Contributors of the Proposed Increase of the Working Capital

17 Any increase in the working capital decided at the 11th session of the Assembly would have to be financed by a levy of 1988 annual contributions to the general fund (payable by 1 February 1989) beyond the level which would normally be assessed for the payment of claims in 1989 and the administrative expenses for that year. This would lead to an increased financial burden on contributors. However, as mentioned above, the Assembly will also have to decide at its 11th session on the reimbursement to contributors of £13.7 million of the balance on the TANIO major claims fund (document FUND/A.11/10). In respect of those contributors who paid 1983 annual

contributions to the TANIO major claims fund, the 1988 annual contributions to the general fund would be set off against any reimbursement to which these contributors were entitled as a result of any such decision. Since the amount to be reimbursed will be much higher than the amount to be levied as 1988 annual contributions to the general fund as a result of the proposed increase in the working capital, these contributors would not actually be obliged to make any net payments to the IOPC Fund in respect of the 1988 annual contributions to the general fund.

18 At the time of the TANIO incident (7 March 1980), the following 18 States were Members of the IOPC Fund: Algeria, Bahamas, Denmark, France, Federal Republic of Germany, Ghana, Indonesia, Italy, Japan, Liberia, Monaco, Norway, Sweden, Syrian Arab Republic, Tunisia, Tuvalu, United Kingdom and Yugoslavia. Only very few contributors (approximately 25) in these States who will be under an obligation to pay 1988 annual contributions did not pay contributions to the TANIO major claims fund. With regard to the States which were Members of the IOPC Fund at the time of the TANIO incident, therefore, nearly all contributors would have no net payment to make as a result of the proposed increase in the working capital.

19 However, 22 of the present 40 Member States were not Members of the IOPC Fund at the time of the TANIO incident, and persons receiving contributing oil in these countries did not contribute to the TANIO major claims fund. Contributors in these countries would, therefore, not benefit from any set-off in respect of the 1988 annual contributions to the general fund. An increase in the working capital would thus impose a certain additional burden upon them. However, the amounts involved are comparatively low. An increase of the working capital from £2 million to £4 million would result in an extra contribution of approximately £1 250 for a contributor who received 500 000 tonnes of contributing oil in 1987, of £2 500 for a contributor who received 1 million tonnes and of £25 000 for a contributor who received 10 million tonnes.

20 It should be noted that an increase in the working capital would result in an increase in the yield in interest on the general fund. The interest from the investments of the IOPC Fund is taken into consideration when the annual contributions are assessed (cf document FUND/A.11/12, paragraph 3.6). A larger working capital and the consequent increase in the return on the IOPC Fund's investments would lead to a corresponding reduction in the need for annual contributions to the general fund in the future.

Action to be Taken by the Assembly

21 The Assembly is invited to consider the Director's proposal that the working capital of the IOPC Fund be increased from £2 million to £4 million.