



**INTERNATIONAL
OIL POLLUTION
COMPENSATION
FUNDS 1971 AND
1992**

EXECUTIVE COMMITTEE
18th session
Agenda item 3

92FUND/EXC.18/4
27 September 2002
Original: ENGLISH

ADMINISTRATIVE COUNCIL
9th session
Agenda item 15

71FUND/AC.9/13/5

INCIDENTS INVOLVING THE 1971/1992 FUNDS

NAKHODKA

Note by the Director

Summary:

Since the July 2002 sessions of the governing bodies the remaining claims, ie those by Japanese government agencies and the Japanese Maritime Disaster Prevention Centre (JMDPC), have been settled and paid.

Recourse proceedings had been brought by the IOPC Funds and others against the owner of the *Nakhodka*, his insurer, the parent company of the shipowner and the Russian Register of Shipping. The governing bodies approved a proposal for a global settlement of all outstanding issues at their April/May 2002 sessions. The agreement between the parties on the global settlement is being formalised.

The distribution between the 1971 Fund and the 1992 Fund of the financial benefits of the global settlement is discussed.

Action to be taken:

To decide on the distribution between the 1971 Fund and the 1992 Fund of the financial benefits of the global settlement and of the costs incurred as a result of the incident.

1 Claims for compensation

- 1.1 As at 25 September 2002, 458 claims totalling ¥36 045 million (£192 million^{<1>}) had been received. All claims had been settled for a total of ¥26 089 892 682 (£139 million).
- 1.2 At the July 2002 sessions of the governing bodies the only outstanding claims were those of 11 Japanese government agencies and the Japanese Maritime Disaster Prevention Centre (JMDPC).

<1> In this document, conversion of amounts in Yen has been made on the basis of the rate of exchange as at 4 September 2002, £1=¥187.40, except in respect of amounts paid where conversion has been made at the rate of the date of payment.

- 1.3 The claims by the JMDPC totalling ¥3 354 million (£18 million) in respect of the construction and removal of a causeway to facilitate the removal of oil from the bow section of the *Nakhodka* were approved by the governing bodies at their April/May 2002 sessions for a total of ¥2 043 million (£11 million) (documents 92FUND/EXC/16/6, paragraph 3.1.26 and 71FUND/AC.7/A/ES.9/14, paragraph 8.4.26).
- 1.4 The Japanese Government and JMDPC brought legal actions in the Tokyo District Court against the owner of the *Nakhodka* (Prisco Traffic Limited) and his insurer, the United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd (UK Club), in respect of the claims that had not yet been settled for the full amount claimed and in respect of the settled claims to recover the part of the settlement amounts which had not yet been paid.
- 1.5 At a hearing held on 30 August 2002, the Tokyo District Court made a formal recommendation for a settlement based on a proposal by the shipowner and the UK Club, which had been agreed by the IOPC Funds. This proposal was based on the amounts offered by the IOPC Funds and the UK Club. All parties accepted the Court's recommendation. The legal actions were therefore terminated.
- 1.6 The claims by government agencies in respect of clean-up operations were settled on 30 August 2002 for a total of ¥1 887 million (£10.1 million).
- 1.7 The claims by JMDPC relating to the causeway were also settled on 30 August 2002 at ¥2 048 million (£11 million), ie at the amount approved by the governing bodies at their April/May 2002 sessions plus interest (documents 92FUND/EXC/16/6, paragraph 3.1.26 and 71FUND/AC.7/A/ES.9/14, paragraph 8.4.26).
- 1.8 The settlement amounts were paid in full to the Japanese Government and the JMDPC on 10 September 2002, 80% by the 1992 Fund and 20% by the UK Club.
- 1.9 As at 25 September 2002, payments made to claimants by the Funds totalled ¥20 361 million (£111 million). The total payments made by the shipowner and his insurer, the United Kingdom Mutual Steamship Assurance Association (Bermuda) Ltd (UK Club), amounted to US\$5 million (£3.2 million) plus ¥2 867 million (£15 million).

2 Level of payments

- 2.1 As authorised by the governing bodies, the Director decided in January 2001 to increase the level of payments from 70% to 80% of the amount of the damage actually suffered by the individual claimants.
- 2.2 At their April/May 2002 sessions the governing bodies decided to authorise the Director to increase the level of payments, if and to the extent that he was satisfied that there was no risk that the Funds would face an overpayment situation (documents 92FUND/EXC.16/6, paragraph 3.1.12 and 71FUND/AC.7/A/ES.9/14, paragraph 8.4.12).
- 2.3 In accordance with a decision by the Assembly of the 1992 Fund the total amount available under the 1971 and 1992 Fund Conventions, ie 135 million Special Drawing Rights (SDR), equals ¥23 164 515 000 (£124 million).
- 2.4 At their July 2002 sessions the governing bodies noted that, after taking the unsettled claims by the Japanese government agencies and JMDPC into account, the total exposure of the IOPC Funds could be estimated at ¥27 021 696 000 (£144 million). It was also noted that the Director had therefore decided that he was unable to increase the level of payments over 80% at this stage.

- 2.5 As a result of the global settlement dealt with in section 4 below, the UK Club will pay the balance of 20% to all claimants. The question of an increase of the level of the IOPC Funds' payments is therefore no longer relevant.

3 Legal actions in the Japanese Courts

- 3.1 Pursuant to the governing bodies' decisions, in November 1999 the IOPC Funds brought legal actions in the Fukui District Court against the owner of the *Nakhodka* (Prisco Traffic Limited), Prisco's parent company (Primorsk Shipping Corporation), the UK Club and the Russian Maritime Register of Shipping, to recover any amounts paid by the Funds in compensation.
- 3.2 As mentioned above, the Japanese Government and the JMDPC brought legal actions in the Tokyo District Court against Prisco and the UK Club in respect of their claims that had not yet been settled for the full amount claimed and in respect of the settled claims to recover the part not yet paid.
- 3.3 Prisco and the UK Club brought legal actions in the Fukui District Court against the 1971 and 1992 Funds in December 1999 for ¥537 million (£2.9 million) in respect of their subrogated rights relating to the payments made by them.
- 3.4 For procedural reasons the IOPC Funds submitted a counter claim in the Fukui District Court against Prisco and the UK Club in respect of the Funds' payments to three prefectures totalling ¥2 913 million (£16 million).
- 3.5 The IOPC Funds also submitted defence pleadings to the Fukui District Court in January 2001 in respect of the actions taken by Prisco and the UK Club against the Funds. The Funds argued that these actions should be rejected on the grounds that Prisco should not be entitled to limit its liability as the incident resulted from its personal fault or privity and that in any event Prisco had not commenced limitation proceedings.
- 3.6 Under the global Settlement Agreement dealt with in section 4 below, the UK Club will pay the outstanding 20% balance of the settlement amounts to all claimants. All the claimants before the Fukui District Court will withdraw their claims after having received payments from the UK Club.

4 Global solution

- 4.1 At their April/May 2002 sessions, the governing bodies considered the following proposal for a global settlement made by the UK Club.
- 1 The compensation payments would be shared between the UK Club and the IOPC Funds on a 42:58 basis in respect of all settled claims.
 - 2 The IOPC Funds would continue to make payments at a level of 80% in respect of all settled claims.
 - 3 The UK Club would pay the 20% balance due to all claimants.
 - 4 The UK Club would reimburse the IOPC Funds approximately ¥5 200 million (£27.8 million), this being the amount payable by the Club to the Funds after payment by the Club of the 20% balance due to claimants.
 - 5 The joint costs incurred by the UK Club and the IOPC Funds would also be apportioned between them on a 42:58 basis.
 - 6 All legal actions arising from the incident would cease.

- 7 The IOPC Funds, Prisco Traffic Limited, Primorsk Shipping Corporation and the UK Club should each bear their own legal costs.
- 4.2 The governing bodies noted that the proposed global settlement would result in the IOPC Funds recovering approximately ¥5 203 million (£27.8 million) and making a saving of around ¥2 500 million (£13.3 million) as a result of not having to increase their payments over 80% of the settlement amounts, and that the Funds would get a contribution to joint costs of some £3.9 million.
- 4.3 The governing bodies approved the proposed global settlement and authorised the Director to conclude a Settlement Agreement provided it contained the elements set out in paragraph 4.1. They also authorised the Director to agree with the other parties on the details of such an agreement (documents 92FUND/EXC.16/6, paragraph 3.1.36 and 71FUND/AC.7/A/ES.9/14, paragraph 8.4.36).
- 4.4 The governing bodies further decided that the IOPC Funds should withdraw their actions against the Russian Register of Shipping.
- 4.5 The IOPC Funds, Prisco Traffic Limited and the UK Club will conclude a Settlement Agreement in the very near future.
- 4.6 Under the Settlement Agreement, the UK Club will pay the balance of 20% to all claimants except the Japanese government agencies and JMDPC which have already been paid in full (cf paragraph 1.8 above). It is envisaged that the UK Club's payment to the Funds will be made by 1 November 2002.
- 4.7 The IOPC Funds are discussing with Primorsk the conditions for the withdrawal of the Funds' actions against the company.

5 Conversion of the maximum amount payable by the 1971 Fund from SDR to Yen

- 5.1 The maximum amount payable by the 1971 Fund in compensation in respect of the *Nakhodka* incident under the 1971 Fund Convention is 60 million SDR minus the limitation amount applicable to the shipowner, ie 1 588 000 SDR, which gives 58 412 000 SDR. Under the 1971 Fund Convention, the conversion of the SDR into national currency should be made on the basis of the rate of exchange applicable on the date when the shipowner establishes his limitation fund (Article 1.4 of the 1971 Fund Convention as amended by the 1976 Protocol thereto read in conjunction with Article V.9 of the 1969 Civil Liability Convention as amended by the 1976 Protocol thereto). However, as a result of the global settlement approved by the governing bodies at their April/May 2002 sessions, the shipowner's limitation fund will not be constituted in the *Nakhodka* case.
- 5.2 The 1971 Fund Administrative Council considered at its July 2002 session which date should be used for the conversion of the amount payable by the 1971 Fund into Japanese Yen. The Council decided that the conversion should be made using the rate of exchange between the SDR and Japanese Yen on 19 February 1997, the date on which the 1971 Fund Executive Committee adopted the Record of Decisions of the session at which the Committee took the decision to authorise the Director to make final settlements of claims (cf document 71FUND/AC.8/6, paragraph 3.3.20). Using this conversion date, the amount payable by the 1971 Fund (58 412 000 SDR) equal ¥10 022 856 668.
- 5.3 At its 17th session held in July 2002, the 1992 Fund Executive Committee noted the 1971 Fund Administrative Council's decision (document 92FUND/EXC.17/10, paragraph 3.1.16).

- 6 **Distribution between the 1971 and 1992 Funds of any amount recovered on the basis of the global settlement**
- 6.1 **Previous consideration by the governing bodies**
- 6.1.1 At their July 2002 sessions the governing bodies considered the question as to the basis on which the financial benefits of the global settlement should be shared between the 1992 Fund and the 1971 Fund.
- 6.1.2 The Director had proposed that the financial benefits of the global settlement should be shared between the 1971 Fund and the 1992 Fund in proportion to their respective maximum liabilities under the 1971 Fund Convention and the 1992 Fund Convention, namely 58 412 000 SDR and 75 million SDR (135 million SDR-60 million SDR) respectively, ie the 1971 Fund would be liable for 43.783% and the 1992 Fund for 55.217%.
- 6.1.3 A number of delegations agreed with the Director's proposal, but expressed concern that the adoption of the proposal might set a precedent which could result in an inequitable distribution of recovered amounts in future cases. Some delegations expressed the view that the financial benefits should be shared on the basis of the actual payments made by the respective Funds rather than their maximum liabilities, although it was recognised that in the *Nakhodka* case both the 1971 Fund and the 1992 Fund would have paid up to their respective limits had it not been for the global settlement.
- 6.1.4 One delegation referred to the fact that the *Nakhodka* incident had occurred during the transitional period, ie between the date of the entry into force of the 1992 Fund Convention and the date on which the denunciations provided for in Article 31 of the 1992 Protocol to amend the 1971 Fund Convention took effect. That delegation drew attention to the provisions in Article 36 *bis* (b) and (c) of the 1992 Fund Convention whereby the 1992 Fund was only required to pay compensation to the extent that claims exceeded the maximum amounts available under the 1969 Civil Liability Convention, the 1971 Fund Convention and, if applicable, the 1992 Civil Liability Convention. In that delegation's view, as long as the relevant provisions existed in the 1992 Fund Convention, they should apply when determining the distribution between the two Funds and a natural interpretation of the provisions would lead to the conclusion that any amount recovered relating to an incident occurring during the transitional period should be reimbursed to the 1992 Fund first.
- 6.1.5 Another delegation made the point that Article 36 *bis* referred only to compensation payments as opposed to the distribution between the two Funds of any amount recovered as a result a successful recourse action. In that delegation's view, a more equitable distribution of amounts recovered would be on the basis of the respective payments made by each Fund.
- 6.1.6 A number of delegations expressed the view that it was premature for the governing bodies to make a decision on this important issue and proposed that the matter should be deferred pending a detailed analysis by the Director of the various options for distributing any recovered amounts.
- 6.1.7 One delegation expressed the view that any analysis undertaken by the Director should include a consideration of how any such distribution would be made in cases involving the 1992 Fund and the Supplementary Fund which would be set up under the proposed Protocol introducing a third tier of compensation.
- 6.1.8 At their July 2002 session, the governing bodies decided to postpone their decisions regarding the distribution of the amounts recovered as a result of the global settlement and instructed the Director to carry out a further study of the options available and their implications for the two Funds (documents 92FUND/EXC.A/10, paragraph 3.1.23 and 71FUND/AC.8/6, paragraph 3.3.27).

6.2 Director's analysis

- 6.2.1 The Director agrees with the delegation which stated at the July 2002 sessions that Article 36 *bis* referred only to compensation payments as opposed to the distribution between the two Funds of any amount recovered as a result a successful recourse action. In his view, there are no provisions in the Fund Conventions which are applicable to the question under consideration. For this reason he proposes that the decision should be such as to ensure a fair distribution between the Funds. It should be noted that, if the recourse actions had been unsuccessful and the IOPC Funds had been liable to pay legal costs incurred by the other parties, these costs should, in the Director's view, have been shared by the two Funds since they had taken the recourse actions together.
- 6.2.2 In the *Nakhodka* case, the IOPC Funds would, but for the global settlement, have paid up to the maximum amount available under the 1992 Conventions, ie 135 million SDR or ¥23 164 515 000. In this situation, the 1971 Fund would have paid ¥10 022 856 668 (43.268%) and the 1992 Fund ¥13 141 658 332 (56.732%). However, as a result of the global settlement, the IOPC Funds will pay only ¥20 288 915 844, out of which the 1971 Fund has paid ¥10 022 856 668 (49.401%) and the 1992 Fund ¥10 266 059 176 (50.599%).
- 6.2.3 The Director accepts that, as a matter of principle, the approach suggested by some delegations set out in paragraph 6.1.3 above is more appropriate than his original proposal. Indeed, if the total amount of the established claims arising from the incident were to fall well below 135 million SDR, that approach would clearly be more equitable than his original proposal. However, in the present case, for administrative simplicity the 1992 Fund and the UK Club agreed that the 1992 Fund should continue to pro-rate payments at 80% and that the Club would pay the 20% balance on all settled claims. Strictly speaking, on the basis of the total amount of settled claims, the 1992 Fund should have made pro-rated payments at 88.787% (ie up to the 1992 Fund limit) and the Club should have paid the balance of 11.213%, with the net result that the IOPC Funds would have been reimbursed a greater amount from the Club on the basis of the agreed distribution of liabilities between the UK Club and the Funds (42:58).
- 6.2.4 In the light of these considerations, the Director believes that both options set out above would be fair. He feels however that his original proposal is preferable in this case, ie that the financial benefits of the global settlement should be distributed in proportion to the respective liabilities of the two Funds, resulting in the 1971 Fund receiving 43.268% and the 1992 Fund 56.732% of these benefits.
- 6.2.5 The IOPC Funds have incurred significant costs as a result of the *Nakhodka* incident totalling some £8.9 million. These costs relate to the operation of the Claims Handling Office in Kobe, set up jointly by the IOPC Funds and the UK Club, and in general to the claims handling process. The UK Club has also incurred such costs. These costs are in general joint costs within the meaning of the Memorandum of Understanding signed by the IOPC Funds and the International Group of P&I Clubs, and should under the global Settlement Agreement be apportioned between the UK Club and the IOPC Funds on a 42:58 basis. This apportionment will be made once the global Settlement Agreement has been concluded and agreement has been reached between the Funds and the Club on the respective amounts of joint costs. The IOPC Funds and the shipowner/UK Club have also incurred considerable expenses in connection with the various legal actions, and under the global Settlement Agreement each party should bear its own legal costs.
- 6.2.6 The issue arises as to how the costs to be borne by the IOPC Funds should be apportioned between the two Organisations. In the Director's view, all costs to be borne by the Funds should be apportioned on the same basis as that which will be adopted by the governing bodies for the distribution between the two Funds of the financial benefits of the global settlement.
- 6.2.7 As regards the question of how the distribution of the financial benefits of joint recourse actions should be made in a similar case involving the 1992 Fund and the proposed Supplementary Fund,

the Director considers that the distribution should in principle be made on the basis of the total amount actually paid in compensation by each of them. However, he believes that the issue of the distribution of the benefits resulting from a joint recourse action taken by the 1992 Fund and the Supplementary Fund as well as the sharing of the financial burden if the action was unsuccessful could be considered by the respective governing bodies when they decide that recourse action should be taken, in the light of the particular circumstances of the case.

7 Action to be taken by the governing bodies

The governing bodies are invited:

- (a) to take note of the information contained in this document;
 - (b) to decide on the distribution between the 1971 Fund and the 1992 Fund of the financial benefits of the global settlement;
 - (c) to decide on the distribution between the Funds of costs incurred as a result of the incident;
and
 - (d) to give the Director such other instructions in respect of this incident as they may deem appropriate.
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