

Interim payments within the international regime established by the Civil Liability and Fund Conventions

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1 Scope of the study

1.1 We have been instructed by the Director of the International Oil Pollution Compensation Funds (IOPC Funds) and the International Group of P&I Clubs (“the International Group”) to address the following issues:

- A) The practice that has been followed by the P&I Clubs and the IOPC Funds in making interim payments under the 1992 Civil Liability Convention and the 1992 Fund Convention, and previously under the 1969 Civil Liability Convention and the 1971 Fund Convention;
- B) The problems faced by the P&I Clubs when making interim payments;
- C) The possible solutions to the problems identified in B) above.

1.2 It has also been suggested that it would be useful if our report addressed the following points when proposing solutions:

- 1) All efforts should be made to avoid a problem regarding overpayments;
- 2) The possibility that claimants have to pay back what they are not entitled to may work in some circumstances, but not in all and there may be political problems arising from such an approach;
- 3) If overpayment occurs, and claimants do not/cannot pay back the overpayment, it may have to be that the Fund and the P&I Club may have to share the liability for the “overpayment”.

1.3 A meeting was held on 24 January 2012 between ourselves and representatives of the IOPC Funds’ Secretariat and of the International Group of P&I Clubs at which the various issues involved were discussed.

2 Introductory remarks

2.1 During the discussions that have taken place in the governing bodies and the 6th Intersessional Working Group established by the 1992 Fund Administrative Council, there appears to have been a general consensus that the practice followed by the IOPC Funds and the P&I Clubs belonging to the International Group regarding interim payments should be maintained in the future.

2.2 The purpose of the present study is therefore to consider what options exist that could facilitate interim payments, in particular in cases where the aggregate amount of

the established claims will exceed the total amount available for compensation, or where there is a risk that this could occur.

2.3 The main issue that will have to be addressed is how to ensure that the present procedures where interim payments are made to claimants can be continued and at the same time ensure that the P & I Club involved and the 1992 Fund do not find themselves in a situation of overpayment, i.e. where one of them or both, when all claims have been settled and paid, have paid in excess of the maximum amount of their respective legal obligations under the Civil Liability Convention and the Fund Convention.

2.4 Overpayment can generally be avoided by “cautious” assessments of the claims presented and of the likely total of the admissible claims, with the addition of a reasonable safety margin, resulting in a prudent decision on the level of interim payments. This is the approach taken in the past by the Funds and the P&I Clubs. This approach has worked well in practice in incidents to which the Civil Liability and Fund Conventions have applied, with only very rare exceptions. It cannot be ruled out, however, that in spite of a very careful and prudent estimate of the total amount of all established claims it emerges later that that the estimate was too low and consequently the level of interim payments set by the governing body of the 1992 Fund was too high.

2.5 The Rules of the P&I Clubs in the International Group allow for a measure of discretion in the settlement of claims, whereas the IOPC Funds simply cannot act outside the terms of the applicable international conventions. The governing bodies of the 1992 Fund will however, as has been the case in the past, be called upon to interpret these Conventions in the light of their object and purpose (see Article 31(1) of the Vienna Convention on the Law of Treaties 1969).

2.6 In various documents that have been presented to the Working Group references have been made to the uncertainties of the decisions of national courts on the application and interpretation of the Civil Liability and Fund Conventions, in particular on questions regarding subrogation.

2.7 Our study has been based on the assumption that the Conventions have been correctly implemented into the law of the Contracting State in question and that the Conventions and the implementing legislation are interpreted and applied correctly by the competent national courts.

3 Provisions in the Conventions relating to interim payments

3.1 The 1969 and 1971 Civil Liability Conventions contain no provision relating to interim payment of claims. Article V paragraph 4 contains the bare statement:

“The [shipowner’s limitation] fund shall be distributed among the claimants in proportion to the amounts of their established claims.”

3.2 Of relevance to interim payments are also Article V, paragraphs 5 and 6 of the Civil Liability Conventions which provide:

“5. If before the [*limitation*] fund is distributed the owner or any of his servants or agents or any person providing him insurance or other financial security has as a result of the incident in question, paid compensation for pollution damage, such person shall, up to the amount he has paid, acquire by subrogation the rights which the person so compensated would have enjoyed under this Convention.

6. The right of subrogation provided for in paragraph 5 of this Article may also be exercised by a person other than those mentioned therein in respect of any amount of compensation for pollution damage which he may have paid but only to the extent that such subrogation is permitted under the applicable national law.”

The question of subrogation will be considered under section 9 below.

3.3 The only reference to interim payments in the 1992 Fund Convention is in Article 18 paragraph 7 which reads:

“The functions of the Assembly shall be:

7. to approve settlements of claims against the Fund, to take decisions in respect of the distribution among claimants of the available amount of compensation in accordance with Article 4, paragraph 5, *and to determine the terms and conditions according to which provisional payments in respect of claims shall be made with a view to ensuring that victims of pollution damage are compensated as promptly as possible;*” (emphasis added).

3.4 In this context reference should be made to Article 235, paragraph 2 of the United Nations Convention on the Law of the Sea 1982 which emphasizes the importance of prompt payment of compensation in respect of damage caused by pollution of the marine environment. That provision reads:

“States shall ensure that recourse is available in accordance with their legal systems for prompt and adequate compensation or other relief in respect of damage caused by pollution of the marine environment by natural or juridical persons under their jurisdiction.”

4 Previous consideration by the governing bodies of the issue of interim payments

4.1 The issue of the procedure for interim payments was raised by the International Group of P&I Clubs in February 1999. It was proposed that when there was a risk that the total amount of the established claims would exceed the maximum amount of compensation available under the applicable Civil Liability and Fund Conventions and the payments therefore had to be pro-rated, the Fund should from the outset participate in the payment to each claimant in proportion to the estimated respective ultimate liabilities of the Club and the Fund.

4.2 The Executive Committees of the 1971 Fund and 1992 Fund decided however that the existing practice and procedures did not require any change (documents 71FUND/EXC.60/17, paragraph 4.14 and 92FUND/EXC.2/10, paragraph 4.15.).

5 Practice followed by the P&I Clubs and the IOPC Funds in making interim payments

5.1 Despite the very limited support for interim payments in the text of the Civil Liability and Fund Conventions, the making of such payments has become an established practice, which has never been challenged by any Contracting State, and could therefore be considered a “*subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;*” as provided in Article 31 (3) (b) of the Vienna Convention on the Law of Treaties 1969. This practice could be summarized as follows.

5.2 The policy of the 1971 and the 1992 Funds has been to start paying compensation only after the shipowner’s insurer had made compensation payments up to the limitation amount applicable to the ship in question.

5.3 This procedure appears to have worked without any major complications in those cases where it was clear from the outset that the aggregate amount of the established claims would not exceed the total amount available under the applicable Civil Liability and Fund Conventions. In these cases, which constitute the great majority of the cases in which the IOPC Funds have been involved over the years, claimants have from the outset been paid the full amount of their established claim, first by the P&I Club involved and, after the aggregate of the Club’s payments has reached the limitation amount, by the 1971 Fund or the 1992 Fund, as the case may be.

5.4 A more difficult situation has arisen in those cases where the aggregate amount of the established claims was expected to exceed the total amount available for compensation under the applicable Civil Liability and Fund Conventions, or where there was a risk that this could occur. In such cases the governing body of the Fund involved has decided, after consultation with the P&I Club involved in the incident, to limit the Fund’s payments to a specific percentage of the established amount of each claim representing a conservative estimate of each claimant’s prospective share of the amount available for compensation. This percentage is customarily referred to as the “level of payments”. The estimate of the maximum of the established claims has been made on the basis of reports by technical experts engaged jointly by the Fund and the P&I Club.

5.5 The shipowner/P&I Club has normally agreed to pay claims at the same percentage as the one set by the Fund’s governing body¹ and has continued to make such payments until the shipowner’s limitation amount under the applicable Civil Liability Convention has been reached. The Fund’s pro-rated payments have commenced only when the shipowner’s payments have reached the applicable limit under that Convention.

¹In respect of some incidents the shipowner/P&I Club agreed to pay a number of small claims for the total established amount of their respective claims or made interim payments without pro-rating in order to mitigate financial hardship to vulnerable claimants.

5.6 In most cases where pro-rating has been applied, the percentage set by the governing body at an early stage of the incident has later been increased, sometimes in several stages, in the light of a more accurate assessment by the joint experts of the total amount of the admissible claims. All such decisions by the Fund's governing body have been taken after consultation with the P&I Club. When a decision on an increase of the payment level has been taken, the claimants who had received payments at the lower percentage have received an additional payment corresponding to the difference between the lower and the higher percentage without having to make a request for such payment.

5.7 The decisions as to whether claims are admissible and on the admissible quantum are taken by both the Fund and the shipowner/P&I Club. No payments are therefore made before both compensatory parties are in agreement on these points.

5.8 A reconciliation between the Fund and the P&I Club takes place when all claims have been settled (by agreement or final judgement) and paid, and a "balancing payment" is made by the Fund or the Club (as the case may be) to the other compensating party so that the total of the compensation payments by the Club equals the limitation amount.²

5.9 In the *Prestige* case however, the 1992 Fund Executive Committee decided that the 1992 Fund should, in view of the particular circumstances of that case, make payments to claimants from the outset, although the P&I Club involved would not be paying compensation directly to claimants. The reason for its position given by the P&I Club was that if the Club were to make payments to claimants in line with past practice it was, according to legal advice received, highly likely that these payments would not be taken into account by the Spanish courts when the limitation fund constituted by the shipowner was distributed, with the result that the Club could end up paying twice the limitation amount. The Club decided therefore to pay the limitation amount into the court (document 92FUND/EXC.21/5, paragraphs 3.2.19 and 3.2.34).

6 Concerns expressed by the P&I Clubs

6.1 The International Group has indicated that the issue which gives rise to concern on the part of the P&I Clubs is whether, if interim payments are made by the Club, it can rely on the competent court setting off the amounts paid against the limitation fund which has been constituted (or which may later have to be constituted). It has suggested that the proportion of an (interim or final) payment made by the Club but attributable to the Fund might be considered by the court as not relating to a legal liability of the shipowner/Club under the Civil Liability Convention and that that proportion of the payment would not therefore be set off against or be recoverable from the limitation fund.

²The costs incurred for the handling of the compensation claims (e.g. costs of operating claims offices and fees of surveyors and technical experts) are paid outside the maximum amount available for compensation. The distribution of such costs between the Fund and the Club is made in the context of the reconciliation, in accordance with the respective amounts of their ultimate liability for the incident, as set out in the Memorandum of Understanding between the International Group, on the one part, and the 1992 Fund and the Supplementary Fund, on the other part, signed on 19 April 2006 (document 92FUND/A/ES.11/6, Annex, paragraph 4B).

6.2 The International Group has further expressed concern that in some jurisdictions the subrogation rights taken from the recipient of an interim payment would not be recognised by the court administering a limitation fund constituted by the P&I Club by payment of the limitation amount into the court. The court might therefore not permit the Club to be reimbursed or credited for such interim payments however carefully the subrogation clause in the receipt and release document signed by the claimant has been drafted. The International Group has argued that in such cases the P&I Club involved might have to pay the limitation amount twice.

6.3 The International Group has mentioned that a variant of this question is whether, if these payments are made up to the limitation amount, the court will in due course return the limitation fund to the P&I Club/shipowner. The International Group has maintained that these questions arise particularly when it is proposed that the Club make payments for greater amounts than could safely be paid if the Civil Liability Convention alone applied.

6.4 The International Group has stated that this question has been of concern mainly in cases where there was considered to be a risk of the amount available for compensation being insufficient to pay admissible claims in full. Consequently the question should in the International Group's view be addressed on the assumption that the court would be asked to return the limitation fund in circumstances where the claimants had not been fully compensated. The International Group has stated that in these circumstances it was to be expected that the claimants would not have entered into final settlements (pending clarification of any final balance they may be entitled to receive), and that they would not necessarily agree to withdraw their claims, or consent to the release of the limitation fund. The issue is therefore in the International Group's view whether the court would make an order for release of the limitation fund despite any opposition from claimants.

6.5 The International Group has drawn attention to the fact that the risk of overpayment, which existed also in respect of incidents to which the 1969 Civil Liability Convention applied, has become a greater problem as a result of the entry into force of the 1992 Civil Liability Convention, since the shipowner's limitation amount is much higher under the 1992 Convention than under the 1969 Convention, for large tankers as high as 89 770 000 SDR (approximately US\$139 million). The International Group has also referred to the fact that a major part of the liability insurance for large tankers is reinsured in the insurance market, as set out below:

- (a) The P&I Club concerned provides the first US\$ 8 million;
- (b) The International Group (all 13 P&I Clubs Group Members) provides a further US\$52 million through a pooling arrangement.
- (c) The insurance market provides through a reinsurance policy the balance up to the shipowner's limitation amount, this balance amounting to US\$79 million for large tankers.

7 Proposals by the International Group of P&I Clubs

7.1 The International Group has proposed that the existing established practice in respect of interim payments be recognized in a formal manner which may be drawn to the attention of the competent court administering the shipowner's limitation fund. The International Group has submitted that when a P&I Club makes interim payments in accordance with the current practice, based on the estimated entitlements of claimants under the 1992 Civil Liability and Fund Conventions and the level of payments decided by the Fund's governing body, and continues to do so until the shipowner's limitation amount under the 1992 Civil Liability Convention is reached, it would do so on its own behalf to the extent of the proportion for which it is responsible and on behalf of the 1992 Fund for the remainder. Likewise once the shipowner's limitation amount has been reached, the 1992 Fund's payments would be made partly on its own behalf and partly on behalf of the Club.

7.2 The International Group has expressed the view that consequently the competent court should, in any distribution of the limitation fund, take into account not only the interim payments made by the P&I Club but all interim payments made under the compensation regime, including those made by the 1992 Fund. The International Group has recognized, however, that the suggested treatment of interim payments in the distribution of the limitation fund is not reflected in the Civil Liability Convention.

7.3 The International Group has also suggested that P&I Clubs' risk of overpayment would be reduced if the Fund were to participate in the compensation payments from the outset, i.e. that interim payments to each claimant were made separately by the 1992 Fund and the P&I Club involved.

7.4 The International Group has pointed out that the P&I Clubs are under no obligation under the 1992 Civil Liability Convention to make interim payments of compensation and that the risk of overpayment could be overcome by the Club involved simply following the procedures laid down in that Convention and establishing a limitation fund in the competent court. The Group has recognized that this could, however, result in the funds provided by the Club not being available to the claimants for a considerable period of time, and that in such circumstances interim payment of victims' claims would be more difficult to arrange.

8 Scenarios relevant to the issues under consideration

8.1 It is submitted that the issues involved only concern both the P&I Clubs and the 1992 Fund in cases where pollution damage is caused in a State party to both the 1992 Civil Liability Convention and the 1992 Fund Convention. In our view there are then two situations to be considered:

- (a) If it is clear from the outset that the aggregate amount of the established claims will stay within the total amount of compensation available under the 1992 Conventions the present practice does not give rise to any risk of overpayment for the P&I Club or the Fund. Although the Club would pay more than its share of the individual claims until it reaches the limitation amount

applicable to the shipowner under the Civil Liability Convention, and could therefore be considered having made an "overpayment", this "overpayment" would only be of a temporary nature. There would therefore be no real problem, since the Club and the Fund would make the necessary adjustment of the payments between them in the context of the reconciliation procedure referred to above. There could however be a problem for the Club to get the court to release any funds or bank guarantee deposited without undue delay.

(b) If the aggregate amount of the established claims exceeds the total amount available under the 1992 Conventions, or there is a risk of this happening, a P&I Club making interim payments could run the risk of overpayment if the percentage at which payments set by the Fund's governing body after consultation with the P&I Club were set at too high a level. It appears that this is the main case to be considered.

8.2 It should be noted that decisions on the distribution of the limitation fund are taken by the court (or other competent authority) with which the limitation fund was constituted. If that court considers that there is a risk, even very small, that the total of the established claims will exceed the amount of the limitation fund, the court may very well decide not to make any payments out of the limitation fund until the admissible amounts of all claims have been established and as a consequence thereof the total amount of the established claims is known. Only at that stage is it possible for the court to calculate the proportion of the limitation fund due to each claimant. In theory the court would be entitled to make interim payments to claimants on the basis of an estimate of the total amount of the established claims, but we consider that it is unlikely that any judge would be willing to exercise this power.

8.3 It has not been considered necessary to deal specifically in this study with the cases where also the Supplementary Fund Protocol applies to the incident, since the issues would be the same as those set out under (a) and (b) in paragraph 8.1 above. The only difference would be that the total amount available for compensation would be much higher than under the 1992 Conventions, and consequently the risk of the aggregate of the established claims exceeding the total amount available for compensation would be significantly smaller.

8.4 More complex problems could arise in cases where pollution damage is caused in more than one State and not all the affected States are parties to the same treaty instruments, but our study has been limited to incidents where pollution damage is caused in only one State.

9 Issues relating to subrogation

9.1 The area of the law which relates to subrogation appears simple in theory, but is difficult in application. Moreover the way in which it is applied appears to differ between common law and civil law jurisdictions. The important references to

subrogation appear in Article V, paragraphs 5 and 6 of Civil Liability Conventions,³ the text of which is set out in Section 3 above.

9.2 Most rights of subrogation arise when one party pays a claim and takes over the rights of the claimant against third parties. The classic example of this in the field of maritime law is in the case of a cargo insurance. When the cargo insurer settles and pays a claim under a cargo insurance policy, he takes over all the rights of the insured, including rights of action against a third party. Those rights are usually recorded in a standard form "letter of subrogation" signed by the cargo receiver.

9.3 In the provisions relating to subrogation in the Civil Liability Convention referred to above, the meaning is somewhat different. A shipowner who has paid a pollution damage claim acquires by subrogation the rights of the claimant under that Convention against his own limitation fund. The provisions do not specify the form required to give effect to that acquisition of rights. It is arguable that no formal document is required, but that the acquisition takes place by operation of law by virtue of the Convention and/or the statute incorporating it into the law of the State where the pollution damage occurred.

9.4 In practice the standard forms of receipt and release used by the P&I Clubs and Funds incorporate an express transfer of the claimants rights against the Funds and the shipowner/Club, respectively. The wording included in the forms used by the Clubs and the Funds in common law jurisdictions, which is standard in marine insurance practice, is well understood by judges in these jurisdictions. In incidents that have occurred in civil law jurisdictions the Clubs and the Funds have incorporated corresponding clauses prepared by their lawyers in the country concerned.

9.5 In view of the very different legal traditions in different jurisdictions concerning the wording of such clauses, it is considered that it would not be appropriate to prepare standard clauses in respect of subrogation. These clauses will have to be drafted by the P&I Club's and the Fund's lawyers on a case-by-case basis, but these lawyers will no doubt be inspired by clauses used previously by them, or used by the P&I Clubs and the Funds in other States with similar legal systems.

10 Analysis of various options

10.1 Amendments to the Conventions

10.1.1 The problems discussed above could be resolved by formal amendments to the 1992 Civil Liability and Fund Conventions, should there be a political will on the part of States to do so. Provisions could for instance be inserted in the Civil Liability Convention to the effect that interim payments should be taken into account in the constitution and distribution of the shipowner's limitation fund and that any amount or guarantee deposited by the shipowner/Club for the purpose of establishing the limitation fund should be reduced by the amount of the interim payments so made. The issue of who should bear the financial risk in an overpayment situation could also be

³ These provisions are similar in substance and wording to the corresponding provisions in the Convention relating to the Limitation of the Liability of Owners of Sea-going Ships 1957 (Article 3.3) and the Convention on Limitation of Liability for Maritime Claims 1976 (Article 12).

addressed in the revised Conventions as well as the question of whether claimants would be under an obligation to repay part of the amounts received in compensation if so required to ensure equal treatment of all claimants without the aggregate amount of the compensation payments exceeding the total amount available for compensation under the 1992 Conventions.

10.1.2 It is not likely, however, that the process for amendment of the Conventions will be reopened in the near future. We have therefore not considered this option further.

10.2 Assembly Resolution

10.2.1 Another option to be considered is whether the problems raised by the P&I Clubs, or some of them, could be solved or reduced by means of a Resolution adopted by the 1992 Fund Assembly.

10.2.2 An Assembly Resolution, even one adopted unanimously by all States parties to the 1992 Fund Convention, would not be binding on national courts, but would only constitute an element to be taken into account by the court for the purpose of the interpretation of the relevant provisions of the Conventions, on the basis that the Resolution would be evidence of a subsequent agreement between the States parties regarding the interpretation of the treaty and the application of its provisions (see Vienna Convention on the Law of Treaties 1969, Article. 31.3(b)).

10.2.3 The issues involved in this study mainly relate to provisions in the 1992 Civil Liability Convention, and a significant number of States parties to that Convention (at present 18) are not parties to the 1992 Fund Convention. These States would not therefore be entitled to participate in the 1992 Assembly's decision to adopt such a Resolution. The only fora in which all States parties to the 1992 Civil Liability Convention could take part in decisions relating to that Convention are the competent bodies of the International Maritime Organization (IMO), i.e. the IMO Legal Committee and the IMO Assembly. It would probably be very difficult to get consensus within IMO for the adoption of a Resolution on the interpretation and application of the provisions in the 1992 Civil Liability Convention dealing with issues discussed in this report

10.2.4 Notwithstanding the limited legal effects of a 1992 Fund Assembly Resolution, such a Resolution could be of value in setting out the position of the 1992 Fund and its Member States on specific issues of interpretation and application of the 1992 Conventions.

10.2.5 If the concerns of the P&I Clubs had related to a real or perceived incorrect application or interpretation by national courts of certain provisions of the 1992 Conventions, in particular those on subrogation and distribution of the limitation fund, these issues could have been addressed in the Resolution in the form of a recommendation by the States parties to national courts. This appears however not to be the Clubs' concern. The issue is rather that a correct interpretation and application of the provisions in the Civil Liability Convention on subrogation and on the distribution of the limitation fund may result in so-called "overpayment" by the Club concerned.

10.2.6 The problem is that a strict interpretation and application of the provisions in the Civil Liability Convention on distribution of the limitation fund would render the making

of interim payments to victims virtually impossible. Moreover the pragmatic approach to such payments which has been followed by the P&I Clubs and the Funds hitherto could result in the Clubs being unable to take credit for the full amount of such payments in the distribution of a limitation fund if such a fund has been constituted. This gives rise to the risk of “double payment” referred to by the Clubs.

10.2.7 We consider that there is no legally binding solution to this problem within the framework of the present text of the Conventions. An Assembly Resolution inviting the national courts to apply certain provisions in a manner that is contrary to their wording would not in our opinion be a viable option.

10.2.8 It would however in our view be of value if the 1992 Fund Assembly in a Resolution, after recalling the practice followed by the P&I Clubs and the IOPC Funds for interim payments, emphasized the importance for victims of oil pollution, and in particular for victims with limited financial resources, e.g. many claimants in the fisheries and tourism sectors, that interim payments should be made. Such an Assembly Resolution could also include an endorsement of a Memorandum of Understanding between the 1992 Fund and the International Group of P&I Clubs, to be attached to the Resolution, dealing with the issues discussed in section 10.3 below.

10.3 Memorandum of Understanding

10.3.1 The practice followed over the years by the P&I Clubs and the IOPC Funds in making interim payments has been described in section 5 above. Although this practice has been reported to the governing bodies on a number of occasions, it has not been set out in any formal document.⁴

10.3.2 It is suggested that the procedures followed by the P&I Clubs and the Funds be described in some detail in a Memorandum of Understanding to be approved by the 1992 Fund Assembly. The approval could be given in the form of an Assembly Resolution in order to give the Memorandum greater authority.

10.3.3 The Memorandum could also address another issue which has given rise to concern on the part of the P&I Clubs, namely the fact that there is no provision in the 1992 Fund Convention corresponding to Article V.5 in the 1992 Civil Liability Convention giving the shipowner/P&I Club subrogation rights against the 1992 Fund for compensation payments made in excess of their liability under the 1992 Civil Liability Convention. The absence of such a provision in the Fund Convention has not caused any difficulty in the past, since all claims are examined and approved by both the P&I Club and the Fund and no payments are made by the Club before such approval has been given by the Fund. In order to meet the concern of the P&I Club a statement could be inserted in the Memorandum to the effect that the 1992 Fund would accept the Club's right of subrogation against the Fund for such payments, provided that the

⁴The 2006 Memorandum of Understanding between the International Group and the Funds referred to in footnote 2 does not contain any provisions on interim payments. It is simply stated that the P&I Clubs and the Funds shall co-operate throughout with the aim of ensuring that, within the legal framework of the 1992 Civil Liability Convention, the 1992 Fund Convention and the Supplementary Fund Protocol, compensation is paid as promptly as possible.

assessment of the claims and the ensuing payments have been approved by the Fund.

10.3.4 Such a Memorandum of Understanding would only be a contractual arrangement between the Fund and the P&I Clubs and would not be binding on a court in the process of the distribution of the limitation fund, nor would it change the Club's subrogation rights against the 1992 Fund for amounts it has paid to claimants in excess of its liability under the 1992 Civil Liability Convention. The Memorandum could however be presented by the Club involved in an incident to the court in charge of the distribution of the limitation fund, if the Club considers it useful to do so, so as to make the court aware of the previous practice, and of the fact that interim payments will continue even after they have reached the limitation amount under the Civil Liability Convention.

10.3.5 The court could also be invited by the P&I Club involved to recognise that the arrangement set out in the Memorandum of Understanding has as its sole objective the recording of a practical arrangement between the Club and the Fund which renders possible the prompt payment of the claims of victims of pollution damage. The Club could draw the court's attention to Article 18.7 of the 1992 Fund Convention which refers to interim payments and inform the court that these arrangements constitute the "subsequent practice" of States parties referred to in Article 31.3(b) of the Vienna Convention on the Law of Treaties.

10.4 Approaches proposed by the International Group

10.4.1 As set out in section 7 above, the International Group has submitted that the current practice implies that when a P&I Club makes interim payments up to the shipowner's limitation amount, it does so on its own behalf to the extent of the proportion for which it is responsible under the Civil Liability Convention and on behalf of the 1992 Fund for the remainder. Likewise the International Group has maintained that once the shipowner's limitation amount has been reached and the Fund takes over the making of interim payments, these payments are made partly on its own behalf and partly on behalf of the Club. The International Group has also indicated the consequences that this approach in its view would have for the distribution of the limitation fund, namely that the court should take into account not only the interim payments made by the Club for the shipowner's/Club's account, but also interim payments made by the Fund, to the extent that these were made for the account of the shipowner/Club.

10.4.2 Although the International Group has on previous occasions made the 1992 Fund aware of its interpretation of the legal significance of interim payments as between the P&I Club involved and the 1992 Fund, the governing bodies of the IOPC Funds have not taken any position on this issue.

10.4.3 As the International Group has recognized, the suggested approach to the distribution of the limitation fund is not reflected in the text of the 1992 Civil Liability Convention. An acceptance of this approach by a governing body of the 1992 Fund governing would therefore not be binding on a court administering the limitation fund.

10.4.4 It would nevertheless be of interest to consider the consequences of an agreement between the International Group and the 1992 Fund along the lines proposed by the Group.

10.4.5 It should first be noted that such an agreement would not give the Club full protection against "overpayments". It would however reduce the financial consequences for the Club in an overpayment situation, since a proportion – and in many cases probably a major proportion – of the payments would from the outset have been made on behalf of the 1992 Fund. Conversely, the 1992 Fund would risk having to face an overpayment situation at an earlier stage than would otherwise be the case, since payments would from day one be considered having been made partly on behalf of the Fund.

10.4.6 An important question is whether an acceptance of the approach set out in paragraph 10.4.1 above could result in the 1992 Fund having to participate in the proceedings relating to the constitution and distribution of the limitation fund set up by the shipowner/P&I Club under Article V.3 of the 1992 Civil Liability Convention. The Funds have not in the past considered it appropriate to take part in these proceedings since they relate only to the Civil Liability Convention, except to the extent that the Funds have taken steps pursuant to Article V.2 to challenge the shipowner's right to limit his liability. It is difficult to predict how a court administering the limitation fund which has been informed of the approach set out in paragraph 10.4.1 would act in this regard.

10.4.7 If an agreement on the approach set out in paragraph 10.4.1 above were to be concluded between the International Group and the 1992 Fund, it should in our view only apply to payments of claims where the 1992 Fund has accepted their admissibility in principle under the 1992 Conventions and approved the admissible amounts. Furthermore, the payments must not exceed the percentage level of payments set by the 1992 Fund's governing body.

10.4.8 It would be important that the P&I Clubs would invoke such an agreement only in cases where it would be reasonable to expect that the aggregate amount of the established claims exceeded the shipowner's limitation amount. This is so because the 1992 Fund should not need to take part in the assessment and approval of claims in respect of incidents which would not be expected to require compensation payments by the Fund. Such an agreement could otherwise result in a significantly increased workload for the IOPC Funds' Secretariat.

10.4.9 As mentioned above, the International Group has submitted that the P&I Clubs' risk of overpayment would be reduced if the Fund were to participate in the compensation payments from the outset, i.e. that interim payments to each claimant were made separately by the 1992 Fund and the P&I Club involved. Such an approach might be easier to understand for the court administering the limitation fund. This approach would however necessitate an estimate from the outset of the proportion to be paid by the Club and the Fund respectively, and an adjustment would most likely have to be made once all claims have been settled and paid in the context of the reconciliation procedure between the Club and the Fund referred to above. A major drawback with this approach would be that each claimant would receive two payments,

one from the Club and another from the Fund, and would have to sign two receipt and release documents, and such a procedure could be difficult for claimants to understand. This approach would also result in a significant increase in the administrative work for both the 1992 Fund and the P&I Club, in particular in major incidents giving rise to thousands of claims, many for fairly modest amounts. For these reasons we consider that this approach would significantly complicate the procedure for interim payments and would be less efficient than the practice hitherto followed by the P&I Clubs and the IOPC Funds. The observations set out in paragraph 10.4.5 above are also relevant to this approach.

10.4.10 Another approach would be to provide in the Memorandum of Understanding between the Funds and the International Group that interim payments could be made in alternate tranches by the P&I Club and the 1992 Fund. For example, the Club would make interim payments up to say £10 million (first tranche), the 1992 Fund would then make payments totaling £10 million (second tranche), the Club would subsequently make payments for another £10 million (third tranche), and so on. The Club's payments would stop when the aggregate of its payments reached the shipowner's limitation amount, and the final distribution of the payments between the Club and the Fund would be adjusted by reconciliation when all claims have been settled.

10.4.11 The fundamental question is whether the approaches discussed in this section would be in conformity with the 1992 Civil Liability and Fund Conventions.

10.4.12 Under Article 4.1(c) of the Fund Conventions, the Fund shall pay compensation to those suffering pollution damage who are unable to obtain full compensation under the applicable Civil Liability Convention, because the damage exceeds the shipowner's limitation amount. As mentioned above, the policy of the Funds has been to start paying compensation only after the P&I Club concerned has paid up to the shipowner's limitation amount. We consider that the above provision does not prohibit payments by the Fund at an earlier stage, provided that it is reasonably clear that the aggregate amount of the established claims arising out of the incident will in fact exceed the shipowner's limitation amount. This was also recognized by the 1992 Fund Executive Committee in the *Prestige* case, where it decided that the Fund should make payments to claimants from the outset, although the P&I Club involved would not pay compensation directly to claimants (paragraph 5.9 above).

10.4.13 It is recognized that the three approaches to interim payments discussed in this section might not be consistent with the precise wording of the 1992 Civil Liability and Fund Conventions. However, in the interpretation of an international treaty account should be taken of its object and purpose, which in the case of the 1992 Conventions is to provide prompt compensation to victims of oil pollution. In our view an efficient system of interim payments is of great importance in this regard.

10.4.14. In the light of what is stated in paragraphs 10.4.12 and 10.4.13 above, we are of the view that all three approaches to interim payments discussed in this section would be compatible with the 1992 Civil Liability and Fund Conventions. It would be for the competent governing bodies of the IOPC Funds to decide whether any of these three approaches (or a combination of them) should be accepted, in the light of their

advantages and disadvantages for the IOPC Funds and the P&I Clubs and their benefits to claimants.

10.4.15 It would be for the International Group to decide whether the position taken by the governing bodies of the IOPC Funds is acceptable to the Group and for the individual Club to decide in each case, in the light of the position taken by the governing bodies, whether and, if so, to what extent it is prepared to make interim payments relating to a specific incident.

10.5 Steps taken by Member States to facilitate interim payments

10.5.1 It will be recalled that in a number of incidents, States where the oil pollution damage occurred have in various ways taken steps which have made interim payments by the P&I Club and the Fund possible, or have enabled the Club and the Fund to make interim payments at a higher percentage than otherwise would have been possible.

10.5.2 In a number of cases the State concerned has undertaken to “stand last in the queue”, i.e. undertaken not to pursue its claims for compensation against the Fund or against the shipowner/P&I Club/limitation fund if and to the extent that the presentation of such claims would result in the total amount of all claims arising out of the incident exceeding the maximum amount of compensation available under the 1992 Civil Liability and Fund Conventions.

10.5.3 Undertakings of this kind by the State involved have greatly facilitated the making of interim payments by the P&I Clubs and the IOPC Funds. Since the decision on whether to give such an undertaking and on its scope is taken by the State involved, this issue has not been considered further in this report.

10.6 Could claimants be required to repay part of the funds received in compensation?

10.6.1 It would from a legal point of view be possible to insert in each release and receipt document to be signed by the claimants a provision to the effect that he or she undertakes to repay the difference between the interim payment received and the sum finally calculated to be due to that claimant when the admissible amounts of all claims have been determined. That calculation would of course be based on the principle that all claimants should receive equal treatment and that the total payments to all claimants should not exceed the total amount available for compensation under the applicable Conventions. A similar clause is already included in the release and receipt documents used by the Funds and the Clubs, to the effect that that the claimant undertakes to repay any amount received which has been based on an incorrect or fraudulent claim.

10.6.2 It is suggested that this option could be considered in relation to States, public authorities and major companies. It would however in our view be politically and psychologically difficult to include such a provision in release and receipt documents regarding payments to other claimants. It is even conceivable that a national court would not enforce such a clause, considering it unreasonable to impose that clause on a claimant, for example a fisherman or a small business in the tourism industry, who at the time of signing the document may have been in a situation of severe financial hardship. It would also be very delicate for the Fund to enforce a judgment for recovery

against claimants belonging to these categories who have in good faith used the funds received. In many cases such claimants may not be able to reimburse the money received.

10.6.3 It appears therefore that this option would not be a solution to the problem of overpayments but could be considered in respect of certain major claimants to reduce the financial consequences of overpayments having been made.

10.7 Would the 1992 Fund Assembly be entitled to levy additional contributions in an overpayment situation?

10.7.1 The Funds' governing bodies have traditionally taken a very conservative approach when setting the level of payments in a situation where pro-rating of claims is found to be necessary. The estimate of the maximum aggregate of the established claims has always been made in such a way that there would be a considerable safety margin. It is nevertheless possible that, once the admissible amounts of all claims have been determined, it is established that the percentage was set at too high a level, and that consequently an equal treatment of all claimants would result in the total amount of compensation available under the relevant Conventions being exceeded. The Fund would then face two conflicting treaty obligations, namely on the one hand to ensure that all claimants are treated equally and receive the same percentage of their established claims (art. 4.5), and on the other hand that the total compensation payments should not exceed the maximum amount available for compensation under the 1992 Conventions, i.e. 203 million SDR (art. 4.4(a)).

10.7.2 The question is whether the 1992 Fund Assembly would be empowered to levy contributions to cover any excess payments that were to result from the competent governing body having, in spite of a very careful and prudent analysis of the level of the established claims and the addition of a reasonable safety margin, set the percentage of the compensation payments at a level which, with hindsight, i.e. when the established amounts of all claims had been determined, was too high.

10.7.3 Under Article 12.1(i)(b) and (c) of the 1992 Fund Convention the basis on which contributions are to be levied shall be an estimate of payments to be made by the Fund for the satisfaction of claims against the Fund due under Article 4. Pursuant to Article 4.4(a) (as amended) the aggregate amount payable by the 1992 Fund is limited to 203 million SDR minus the amount actually paid by the shipowner/insurer under the 1992 Civil Liability Convention.

10.7.4 In our opinion the 1992 Fund Assembly would not have the power to raise contributions to finance compensation payments over and above the maximum amount payable under the 1992 Fund Convention. It follows that, if interim payments have been made to claimants which later turn out to have been made at a higher percentage than the available funds would allow, claimants whose claims are paid towards the end of the payment procedures would not receive the same percentage of their established claims as those claimants who received their payments earlier.

11 Conclusions

11.1 There appears to be a general consensus as to the importance of the practice followed by the IOPC Funds and the P&I Clubs in making interim payments of compensation being maintained in the future. Such practice is in our view in line with the object and purpose of the international compensation regime, namely to ensure prompt and adequate compensation to victims of tanker oil spills. This objective has been repeatedly emphasized by the governing bodies of the IOPC Funds and by the P&I Clubs.

11.2 There is however no provision in the Civil Liability Conventions or the Fund Conventions which obliges the shipowner/P&I Club and/or the IOPC Funds to make interim payments to claimants. The only reference to interim payments in the Conventions is in Article 18, paragraph 7 of the Fund Conventions which empowers the Fund Assembly to determine the conditions according to which provisional payments to claimants shall be made. That paragraph indicates the objective of the Fund Convention that victims of pollution damage should be compensated as promptly as possible

11.3 The existing practice of the P&I Clubs and Funds in making interim payments, as set out in section 5 of this report, has been reported on a number of occasions to the Funds' governing bodies and no Contracting State has challenged this practice. This practice could therefore in our view be considered a "subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation", which should be taken into account in the interpretation of the Civil Liability and Fund Conventions, as provided in Article 31.3(b) of the Vienna Convention on the Law of Treaties.

11.4 The concerns expressed by the P&I Clubs as well as other issues discussed in this report could be resolved by formal amendments to the 1992 Civil Liability and Fund Conventions, but in our opinion it is not likely that the process for revising the Conventions will be reopened in the near future.

11.5 In this report three different approaches to interim payments have been discussed, namely:

- a) The International Group's contention that when a P&I Club makes interim payments, it does so partly on its own behalf and partly on behalf of the 1992 Fund, and that interim payments made by the Fund are partly made on the Fund's behalf and partly on behalf of the Club.
- b) Interim payments might be made in alternate tranches by the P&I Club and the 1992 Fund.
- c) Interim payments to each claimant might be made separately by the 1992 Fund and the P&I Club involved.

We consider that all these approaches would be compatible with the 1992 Fund Convention. It would be for the competent governing bodies of the IOPC Funds to decide whether any of these two approaches (or a combination of them) should be accepted, in the light of their advantages and disadvantages for the IOPC Funds and the P&I Clubs and the benefits to claimants.

11.6 It would be for the International Group to decide whether the position taken by the governing bodies of the IOPC Funds is acceptable to the Group and for the individual Club to decide in each case, in the light of the position taken by the governing bodies, whether and, if so, to what extent it is prepared to make interim payments relating to a specific incident.

11.7 With respect to the approach set out in paragraph 11.5.c) above under which interim payments to each claimant would be made separately by the P&I Club and the 1992 Fund, we consider that such an approach would significantly complicate the procedure for interim payments and would be less efficient than the practice hitherto followed by the P&I Clubs and the IOPC Funds as described in section 5.

11.8 Concerns have been expressed by the International Group as to the manner in which the existing practice for interim payments followed by the P&I Clubs and the Funds would be taken into account by the courts administering the limitation fund constituted under the Civil Liability Convention. In particular, it is feared that such a court may decline to give the shipowners/Clubs credit for interim payments made by them and specifically the proportions of the payments which in the Group's view are made on behalf of the 1992 Fund. We consider that there is no legally binding solution to this problem within the framework of the present text of the Conventions, but a measure of protection may be afforded if our recommendation in paragraph 11.8 is followed.

11.9 We recommend that the practice of the shipowners, P&I Clubs and Funds in making interim payments be recorded in Memorandum of Understanding to be approved by the 1992 Fund Assembly in an appropriately worded Resolution. This Memorandum could, if thought appropriate, be laid by the shipowner/P&I Club concerned before the court administering the limitation fund as authoritative evidence of the existing practice.

11.10 It would be possible from a legal point of view to insert in each release and receipt document to be signed by the claimants a provision to the effect that he or she undertakes to repay the difference between the payment received and the sum finally calculated to be due to that claimant when all claims have been settled. In our opinion this approach would not be a solution to the problem of overpayments, but could be considered in respect of certain major claimants to reduce the financial consequences of overpayments.

11.11 We consider that the 1992 Fund Assembly does not have the power to raise contributions to finance compensation payments over and above the maximum amount payable by the 1992 Fund under the 1992 Fund Convention.

Malmö and London on 8 February 2012

Måns Jacobsson

Richard Shaw

