

## **Conflict of the Contracts The Yacht Insurance Policy Vs. the Shipyard Contract**

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Reading a yacht insurance policy is often like an English-speaking person trying to read a Chinese storybook – it's impossible. However, understanding a yacht's insurance policy is essential to protect oneself from being denied coverage or breaching the insurance policy.

Upon signing a yacht insurance policy, the yacht owner and the insurer agree to a meeting of the minds concerning the terms of the policy. Thereafter, the yacht owner cannot unilaterally change the terms of the policy without the insurer's consent. The latest discord regarding yacht insurance policy coverage concerns conflicts with shipyard contracts and how shipyard contracts attempt to alter the terms of the yacht insurance policy without the insurer's consent.

A yacht insurance policy prohibits the policyholder from assigning additional liability onto the insurer without the insurer's consent. Breaching this condition of the yacht's insurance policy could possibly lead to denial of coverage. Even worse, many policyholders might not be aware of this potential conflict, since their representatives and crew are the ones entering into the shipyard contracts.

### **Problem clauses**

There are four common clauses which are found in many shipyard contracts, and if agreed to by the owner, could act against or violate the terms of the owner's yacht insurance policy and could ultimately void insurance coverage: 1) Hold Harmless, Defend and Indemnify, 2) Adding Shipyard as Additional Insured, 3) Waiver of Rights of Subrogation, and 4) Limitation of Liability.

In the "Hold Harmless, Defend, Indemnify" clause in a shipyard contract, the yacht owner agrees not to hold the shipyard responsible if the shipyard causes damage to the yacht. Further, the yacht owner agrees to compensate the shipyard for any loss the shipyard suffers, even if the yacht owner is not at fault. This is a voluntary assumption of additional responsibility. In the "Add shipyard as Additional Insured / Co-Insured / Named Insured" clause, the shipyard requires the yacht owner's insurer to add the shipyard to the yacht's policy for liability coverage. This gives the shipyard rights under the yacht owner's insurance policy. This creates numerous problems. First, the shipyard's request does not specify what exactly it wants to gain by being listed on the policy, and insurers may add the yard without further definition. The effect is that the yard may gain more coverage than it should have under the yacht owner's insurance policy. Second, insurers generally will not subrogate against a party with a named interest in the insurance policy. Adding the shipyard effectively removes the ability of the insurer to recover from the shipyard if the shipyard causes damage to the yacht. Third, all parties on an insurance policy share one limit of liability. Adding others to the policy dilutes the limit for the yacht owner in the event of a claim against the policy. Finally, yacht insurance policies are designed to cover the yacht owner for liability which arises out of the ownership, maintenance and use of the

yacht. When placing the yacht in the custody and control of a shipyard, the yacht's insurer expects the shipyard to be responsible for its acts and insure its operations.

In the "Waiver of Subrogation/Transfer of Rights" clause, the yacht owner agrees not to recover from another party damages the yacht owner sustains due to the negligence of that party. The shipyard requesting this waiver also expects that the yacht owner's insurer is bound by this agreement. Subrogation is a critical right under a yacht insurance policy. Under the insurance policy's terms, an insurer will cover a loss that is not the yacht owner's fault and then allows the insurer to step into the shoes of the yacht owner to pursue recovery from the party at fault. The Waiver of Subrogation clause takes this right away from the insurer without the consent of the insurer, which is a breach of the yacht insurance policy.

In the "Limitation of Liability" clause, the shipyard places a maximum dollar amount on its liability. This is similar to a waiver because it means the yacht owner waives his right to recover from the shipyard above this amount. The shipyard imposing this limitation within its contract expects the yacht owner's insurer to be bound by this agreement, even though the insurer did not consent to the agreement.

#### Out of pocket

What is the major impact of these clauses? Yacht insurance policies contain exclusions for additional liability that yacht owners assume when signing shipyard contracts (commonly called Contractual Liability Exclusion). This specifically addresses additional liability the yacht owner assumes, which he would not otherwise have. For example, when the yacht owner signs a shipyard contract containing these clauses, he is agreeing to pay another party for damages that party sustains, even if the yacht owner is not at fault. Due to the Contractual Liability Exclusion, the yacht owner is uninsured in this situation and would be paying out of pocket in the event of a claim.

Yacht Insurance policies may also contain a clause prohibiting yacht owners from waiving their rights of subrogation. When the yacht owner signs a shipyard contract that requires the yacht owner to waive such rights, the yacht's insurer is not bound by this contract. The impact is that the yacht owner agrees to waive his rights, but his insurer has not waived any rights. In this situation, if the shipyard is negligent and drops the yacht causing substantial hull damage, and the yacht owner's insurer pays to fix the damage then seeks to recover from the responsible shipyard, the shipyard could circle back to the yacht owner to recover its monetary losses because the yacht owner, not his insurer, agreed to waive rights to recover from the shipyard.

In both cases, insurers may agree to the indemnity and/or waiving rights, but they need to be notified with certain information in advance.. Also, additional premiums may apply since both types of activities translate into increased exposure to the yacht's insurance company. In addition to the negative effect that shipyard contracts might have on a yacht's insurance policy, many insurance policies use additional clauses to further limit or exclude coverage for yachts entering shipyards and/or undergoing refits. Insurance policies generally do not define "refit", so it is incumbent on the yacht owner to understand how his specific insurance policy would apply

in a given situation. Such clauses can take many forms within a yacht insurance policy. One might state, “exclusion for all claims arising while the yacht is undergoing work in a shipyard,” so even if the yacht owner’s claim was due to a lightning strike in the shipyard, the yacht’s insurer could still have grounds to deny the claim. Other language might state that, “before the yacht enters the shipyard, the yacht owner is required to notify his insurer who must agree to the shipyard period specifics.” If the yacht owner enters the shipyard without meeting this condition precedent, then he may have no insurance coverage at all.

#### Hot work

A clause might also state that, “there is no coverage for claims arising from hot work, unless the insurer agrees in advance.” Hot work involves welding, burning, cutting, soldering, grinding, using fire or spark-producing tools, or any work that produces a source of ignition. Initially, hot work might not be required, but as work progresses and more items are added to the repair list, hot work might become necessary. The yacht owner may not be aware that it is even taking place, yet he would have no insurance coverage if the yacht catches fire due to hot work. The situation is even worse if the yacht owner has signed a contract with the shipyard agreeing to waive his rights of recovery due to the shipyard’s negligence.

How does a yacht owner prevent these issues from arising and/or being denied coverage? One, the yacht owner can sign the shipyard contract “as is” and bear responsibility for all costs that are not covered by his yacht insurance policy. Two, the yacht owner can work with yacht’s insurer to modify coverage to address gaps. Lastly, the yacht owner may work with his insurer and the shipyard to include contract terms which are fair for both parties.

Remember, failing to read a yacht insurance policy is not a defense in court, so to prevent needless litigation, two rules of thumb are recommended: First, don’t just be concerned with the premium amount; read the entire insurance policy and contact your lawyer or insurance broker if you have any regarding the language. Lastly, make sure your representatives and captain understand the restrictions of the yacht’s insurance policy since they will most likely be making the daily decisions concerning the yacht, such as entering into shipyard contracts.

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