

Contractual Liability – An Underwriters Perspective

On all of our marine liability accounts, there is some element of contractual liability involved. The definition of Contractual Liability is “insurance that protects the Assured, in the event a loss occurs, for which he has assumed liability, express or implied, under a written contract.”

The Contract is normally a signed document, where the parties agree to take on the liabilities of a third party. The contract is usually for a specific period, and a specific job. The Contractual Liability is when both parties agree, to certain terms and conditions, for achieving their particular goals and interest. Some liabilities are assumed, when trying to achieve the contract requirement, for both parties.

The agreement signed by the parties create the Contractual Liability. Liability does not come into play if everything runs smoothly, but if anything goes wrong, then liabilities come into the picture.

There are three ways in which an Assured can become legally liable for damages:

1. Through their own negligence, i.e. failure to exercise the proper degree of care required by the circumstances
2. Through a Breach of Contract

3. Through assuming the liability of others

Contractual liability arises because of a contract, where parties agree, usually in writing, to take on the liability of someone else, or there would not have been a liability. The agreement, where one party takes on the liability of another, by contract, is commonly called a "Hold Harmless" agreement. An example would be a contract between an Assured and say the Long Island Railroad/The Metropolitan Transportation Authority or the City of New York for ferry operations.

Contractual Liability is the express liability assumed, in such things as a Charter Party, a Towage Agreement, Salvage Work, Bill of Lading and Charterer Agreements. The liability is documented, for the specific arrangement. The contract implies, that neither party to the contract, will unreasonably deprive the other of benefits under the policy.

Whether it is Charterers Legal Liability, Ship Repairers, Stevedores, Terminal Operators, Wharfingers Legal Liability, Protection & Indemnity, Marina Operators or more importantly Marine General Liability, there is a potential for contractual liability, if there is a contract signed between the Assured and a third party.

Typical Wharfingers, Terminal Operators, P&I and Stevedore Legal Liability policies, cover the legal liability of the Assured to third parties, but there are specific

exclusions for contractual liability. If coverage is granted, for any contractual liability, this should be done with an understanding of the types of coverage involved. If a CGL policy is attached to any of these policies, you would normally be picking up Contractual Liability. In a typical P&I policy, if left unendorsed, the policy excludes liability assumed under a contract .

Depending on the language of the contract, Underwriters are often asked to add a Blanket Additional Assured wording, and offer a Blanket Waiver of Subrogation, so that in the event that these contracts are signed during the policy period that there is protection for the Assured for these Contractual obligations. Contractual Liability can be provided on both a designated contract basis and on a blanket basis. This is typical in the River and Gulf business that we underwrite. An example would be when we add Additional Assureds to the various sections of our policies, say the Huey P. Long Bridge Fleet, Inc., when utilizing their facilities for crew changes.

By adding these Additional Assureds to our policies, they are offered the same protections in our policies, as the Named Assured. While most underwriters are very diligent in their craft of underwriting the Assured's business, we can be somewhat blinded by the contracts signed, when we are adding these Additional Assureds to our policies.

Generally, we are not asking for any real information on these third parties, we are adding to our policy, nor the 5 year loss record of these “blanket” companies we are adding to our policies. The worst part is, that we normally get no Additional Premium for the exposure. We are underwriting blindly. In the good “old days”, we would at least get an additional premium for each Additional Assured added to our policies, and would only, in rare cases, offer a Waiver of Subrogation. Underwriters would have the benefit of getting Underwriting information on each Additional Assured added to our policies. The contracts would be sent to the insurance company’s legal department for review. Generally, this is not the case today.

Things get even more complicated with contractual liability, as it relates to our Marine General Liability Policies, where we are providing coverage for our own workers via Action Over.

There is always confusion on, what is Action Over. Action Over is a type of action where an injured employee sues a third party, for causing or contributing to the employees injury. The employee sues a third party, and the third party seeks indemnity, from the injured workers employer (Assured) under the terms of the

contract. Therefore, through the contractual relationship, that liability is passed back to the injured workers' employer.

Action Over is one of the most widely misunderstood policy coverages, and the source of some of the industry's most difficult claims.

An example of Action Over could be in for a company involved in an offshore catering business. An employee reported that he injured his shoulder while moving milk containers, while on board a time chartered vessel. The Assured was working under a Master Service Agreement with the time charterer. The employee sued the time charterer, and the time charterer tendered to our Assured to provide their defense and indemnity.

The responsibility for damages stemming from the tort liability, is shifted from one party to the other. The right to indemnification, can arise pursuant to the terms of the written contract, or at common law.

Although all states with Anti-indemnity statutes prohibit indemnification, several states allow for procurement of insurance coverage, that indemnifies the other party, via Additional Assured coverage, for injuries to these employees. The way the risk is transferred is through:

1. Common law indemnification
2. Contractual Liability
3. Additional Assured coverage

There are three basic types of indemnity agreements:

1. Indemnification for liability, *arising* from the indemnitor's negligence
2. Indemnification for all liability, *except* liability arising from the indemnitee's own negligence
3. Indemnification for all liability, *including* liability arising from the Indemnitee's own negligence

Rules do vary from State to State. While under Marine General Liability and ISO CGL policies there is an exclusion for the Assured's employees, we are picking back up these exposures through the Contractual Liability coverage in the form. These employees get coverage under the Assured's Marine General Liability Policy, and are treated as third parties, even though there is a specific exclusion for employees under the Marine General Liability and CGL policies. Employees can have the Benefit of Workers Compensation, and then, also be entitled to sue their employer via this contractual liability arrangement. The Employees are considered a third party, per the terms of the contract, and the Contractual Liability coverage, in most Marine General Liability forms. ISO has over 35 endorsements for adding

Additional Assured coverage and each is tailored to a specific business relationship. The question is, whether these endorsements accurately reflect the parties' intention for coverage.

The other issue with contractual liability is, that we are offering our policy limit and offering defense to these third parties, of whom we have not generally received any underwriting information. Under an ISO CGL policy, defense is outside the limit but in most MGL policies defense is within the policy limit. Some companies offer a separate limit for defense coverage. In a typical P&I policy, defense is within the limit, and this can actually hurt the Assured, as this works fast in depleting the Assured's insurance coverage.

When these third parties cause a claim, we are on the hook for their actions. The Additional Assured also has no obligation to reimburse the Assured, for any deductible paid by the Assured. The actions of these third parties can have a significant impact on our Assured's loss record. The Assured can become legally liable, even though they have potentially done nothing wrong, and their record can be impacted by these third party contractual obligations.

Any breach of the contract, exposes both the insurance company and the underwriter, to extra Contractual liability or potentially “bad faith” liability. The benefits of being an Additional Insured in an Insurance policy, entitles them to:

1. Be named on payments
2. They are entitled to notice of cancellation
3. Anti-subrogation rules apply

The Additional Insured has no duty to pay premiums or deductibles. There are also more effects of the Additional Assured status:

1. They can dilute the policy limits
2. A Duty to defend may exist
3. There is an elimination of Subrogation Rights
4. They are usually afforded primary coverage, (or excess) unless already added as an Additional Assured to another policy.

Some commonly seen Marine Additional Assured endorsements:

1. They do not expressly limit the coverage to ongoing operations, so the coverage may include completed operations
2. They do not state that coverage will not extend beyond what is required under the contract or agreement

3. They do not limit the coverage to liability for claims caused “in whole or in part” but instead the the “arising out of” language.

The “arising out of” language has been construed by the courts, to mean “originating from”, “growing out of” and “flowing from” so the coverage can be quite broad.

Additional Assureds are generally entitled, to the same protection, as the Named Assured. Their scope of coverage is generally not greater, than the coverage afforded to the Named Assured. This naming and Waiving can affect the Assured’s insurance coverage, in many ways. The insurance company has a broad duty to defend it’s Assureds. The duty to defend is much broader, than the obligation to indemnify. The duty to defend terminates, only after the coverage issue has been resolved and the indemnity has been paid.

Under Maritime Law, courts require full disclosure and “ultimate good faith” by the insured, to the insurance underwriter, and if this standard is not satisfied, then both the Assured, and the Additional Assured, may lose their coverage under an insurance policy. Coverage for Additional Assureds may be available, even when coverage is excluded, for the Named Assured.

If there is nothing in the policy that limits Additional Assured coverage, to the coverage provided to the Named Assured, their coverage may exceed the coverage, of the Named Assured.

An example would be, if there was a crew exclusion on the P&I policy for the Named Assured. The Additional Assured coverage did not restrict coverage to the actual terms and conditions of the Named Assured's policy. We could arguably have to defend the Additional Assured for something not contemplated in the Named Assured's policy. We can also issue a policy with no Additional Assureds being added to the coverage, but still have to defend them because of a contractual obligation to that Additional Assured by the Named Assured.

The insurance policy is a contract. The Assured is referred to as a first party, to the contract. The insurance company, who issues the policy, is a second party. A stranger who makes a claim against the Assured, is known as a third party. The contract is an obligation, to compensate another person harmed, injured or suffered a loss, due to negligence or wrongful act of the first party. When the Assured causes a loss, then the insurance company assumes the Assured's liability up to the policy limit. Some examples of third party liabilities are: collision, third party injury or death, pollution liability, cargo claims, crew claims, etc. The claims

may also extend even to auto accidents, when an indemnity agreement is involved in, say, the moving of a crane to a work site. Some other claims that we have seen are injuries to caterers, while on board ships that claim to be seamen; and, in that case, we are seeking no seamen status, so we would look for indemnity from the cook's employer. There are also the employees that are injured on oil rigs. The employee would sue the rig's owner/operator, and we would get the Action Over as a result of the MSA in place.

In the Oilfield industry, operators usually enter into Master Service Agreements, or MSA'S, with various contractors, who supply services and materials needed in connection with varied oilfield operations. This agreement usually requires the contractor to indemnify the operator, against any claims arising out of or in connection with the services, and materials supplied by the Contractor, whether caused by the Contractor's, or operator's negligence. The Contractors are required to carry minimum amounts of insurance, and to include the operator as an Additional Insured, under their insurance policies.

One thing to note, is that if you are named as an Additional Insured, the coverage provided by the insurance company, is based on the terms, conditions and endorsements to the policy, and not the provisions of your contract. Some, of the

obligations, may be excluded from the insurance policy. Also, if you are named as an Additional Assured, there may be a number of Named Assureds, Additional Assureds and Loss Payees who have different interests in the policy. One further thing to think about is, when we add these Blanket Additional Assureds to our policies, is our intent to protect them under every section of our policy? If it is not the intent of the company to cover them under every section of the policy, we should be specific as to what sections these Additional Assureds are added to our policies. The Additional Assured doesn't even see the insurance policy to which they are added to the coverage.

Although you may be named as an Additional Assured, the question remains as to whether a claim against you, is within the scope of the Additional Assured coverage. The scope of coverage may be limited, by your contract with the Named Assured. The intent of Additional Assured provision is to protect you from losses arising out of the work, the named insured is doing for you. If there are no limitations, the Additional Insured provision would protect you, for losses in all your operations, even those unrelated to the Named Assured.

Another issue is Certificates of Insurance. Certificate holders are often noted to be included as Additional Assureds, on a Certificate of Insurance, and although you

may be added as an Additional Assured on the Certificate, most courts have found, that an insurer's obligations are determined by the terms of the policy, and not by the Certificate of Insurance, even though you may be named.

Regarding Contractual Liability, there are some things that can be controlled with Indemnification and Hold Harmless Agreements, and there are certain things we can do, as the underwriter, when we are looking at these contracts:

1. Avoid the use of broad language, when possible.
2. Make sure the insurance applies to only the Assured's liability (as interest may appear)
3. Will the insurance provide coverage for their negligence?
4. We shouldn't be defending/indemnifying for uninsured exposures like intentional acts
5. Try not to cover for the indemnity for the work of subcontractors
6. Is there vague statements regarding the contractual arrangements?
7. Should we be sub limiting our coverage for the Additional Assured coverage?

When underwriting Additional Insureds there are some things to consider:

1. Know the Additional Assured(s) you are covering
2. Know the interest in your policy and what we are insuring

3. If we are required to add them to a contract know:

- What type of contract
- What type of job
- Receipts generated from the job

4. Can you get the claims record of the Additional Assured?

5. Is this worth an Additional Premium to underwriters for this exposure

6. Is this a party we might want to subrogate against, if they are at fault for the loss or damage?

Lastly, when the claim comes in, the insurance company will need to determine:

- 1) Does the claim allege bodily injury or property damage; is it covered by the policy?
- 2) Was the injury caused by an occurrence?
- 3) Did the occurrence take place in the coverage territory?
- 4) Did the injury take place during the policy period?

As you all know we are in an extremely competitive market. Underwriters are sometimes forced to do things that they would not necessarily do in order to write

the business and keep the lights on. One word of advice is that with all the various companies, we are insuring, there are a lot contracts out there.

Most of which probably are being signed, and not being properly vetted to the right parties at their respective companies. If possible, ask for a copy of the normal contracts signed. The unknown can be scary, especially when we rate up an account and not knowing that in the event of a claim, even massive policy limits can be eroded by large legal bills, before indemnity can be paid. If there is any ambiguities contained within the policy and the endorsements, know that the law is not in our favor, for any uncertainty, and our policy will probably pay.

By Liz Nittolo – 5/10/2017

Special Thanks to:

- 1) The Law of Unintended Consequences: Legal Issues involving Additional Insured Endorsements
Jess B. Millikan – Bullivant/Houser Bailey – Pacific Admiralty Seminar – October 2002
- 2) Additional Insureds and the Anti-Subrogation Rule –John Nicoletti – October 29, 2001
and
- 3) Waiver of Subrogation/Impairment of Insurer’s Subrogation Rights – Nicoletti Hornig &
Sweeney – June 21, 2000
- 4) Best Practices to Minimize Action Over Claims – David Matthiessen – Everest National Insurance
Company – date unknown
- 5) Marine Engineering – Third Party Liability, Contractual Liability and Limitation of Liability dated
October 30th, 2012
- 6) Oilfield Anti-Indemnity and their Impact on Insurance Coverage – a Comparative Analysis by
Robert Redfearn, Jr. – August 22, 2005
- 7) Contractual Indemnity/Additional Assured Issues for Underwriters that arise from Master
Service Agreements and Charter Parties – Michael L. McAlpine and Richard A. Cozad – 122764
- 8) Additional Insureds and Marine Insurance – Joe Grasso and Michael Thompson – Marine
Insurance Day – October 5th, 2012
- 9) Underwriting Principles and Practices – Robert B. Holtom – 1981 – The National Underwriter
Company
- 10) Additional Insureds – Frank A. Piccolo & Caroline T. Webb – Preis dated January 19, 2015
- 11) Selected Legal Issues – James N. Hurley – Fowler White Burnett – November 3, 2014
- 12) Additional Insureds and Other Problems – Edward F. LeBreton, III – Fowler, Rodriguez dated
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