

# Legal And Insurance Issues Facing The Super Yacht Industry

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## The Six C's

It is a daunting task to address in but a few short minutes all of the relevant legal and insurance issues facing the superyacht industry. One of the main reasons is that so many issues are interrelated. Because this session is focused more on the operation of superyachts, I will focus on the issues other than those specific to new-builds.

Back in the early 80's, starting out as an environmental lawyer, a client came into the office with a number of problems concerning a 173 foot yacht which has been built by British royalty and given to the Emperor of Indochina as a gift. With no one in the firm having any experience with maritime matters, it essentially came down to, "OK, Eric. Fish. Water. Boats. You've got the case!"

Well, that case involved conflicts with a repair yard, the unconstitutional arrest of the yacht, a project manager who was negligent and bilked the client of substantial funds... and the concept of cleaning up those fiascos so that the yacht could be transformed into a timeshare or co-operative.

People tend to consider "contract", "construction", "certification", "crew", "charter" and "conflict" as separate specialties. In reality, people tend to address one of the Six "C's" at a time without considering the other five as sufficiently as necessary. Add in a contract of insurance (where you are betting you are going to have a loss and the carrier is betting you won't) and the interrelationship between these Six "C's" becomes self-evident... as is the need for multiple policies or endorsements.

## IS FILING AN INSURANCE CLAIM THE RIGHT THING TO DO?

A yacht has her engines serviced and partially rebuilt by a factory authorized repair facility and was approved by the classification surveyor. The yacht then travels to meet a charter and the engine fails... which resulted in other engine damage (in the ensuing rough seas) and the loss of a charter... which ultimately resulted in an arrested yacht, litigation in a third country claiming crew negligence, potential claims against the repairer... and the inability to timely obtain the necessary parts or factory authorized repairers.

You have a standard yacht policy with a commercial/charter endorsement and pollution coverage (which fortunately does not come into play). You are staring at a lawsuit claiming violation of the MYBA Charter Agreement for failure to deliver the yacht for the charter and that it was not force majeure because the major mechanical breakdown was not "beyond the crew's control and not caused by Owner's negligence". You are also considering who you are going to look to for the cost to rebuild your damaged engine. Meanwhile your yacht is tied up at a commercial facility with bulkheads intended for tankers, soot flying everywhere and a marshal who doesn't know the first thing about the needs of a superyacht.

Where do you start? Do you secure the yacht anticipating an extended stay? Do you post bond (wondering if you will ever see that money again)? Call your lawyer? Your insurance representative? The charter broker? The engine manufacturer or nearest authorized facility?

Your captain does his best to secure the yacht and protect it. Your attorney retains local counsel seeking to obtain the vessel's release by the posting of a bond, but there is a dispute as to the amount of the bond and a hearing must be held... delaying the release for weeks.

There may be issues associated obtaining an insurance-backed bond because you may well have a foreign flagged vessel arrested in a country which is not otherwise a party to the dispute and be subject to significant unsubstantiated claims with no reasonable expectation of a timeline for resolution and a system which may well be foreign to the underwriter. You may also be faced with a judicial system that does not recognize your insurance company or a local bonding agency which takes little comfort in your offshore corporation with no real assets other than the yacht. This can result in a lengthy delay, high premiums, etc. and, therefore, the need (or desire) to forego an insurance bond and, instead, the payment of a cash bond.

Meanwhile you are obligated to advise your insurance company that the yacht was arrested, but while believing there must be coverage for such an innocent loss, you wonder what type of coverage will be provided... and if it is worth making the claim versus the potential problems obtaining new coverage the following year. Notice is required, but generally a Proof of Loss is not required to be made for 180 days.

You read the policy and discover that there are exclusions for losses to motors whether it is be due to negligent repair or heavy weather. But, fortunately, you have secured an Institute Yacht Machinery Damage Extension Clause which covers such losses "excluding the making good any defect resulting from either negligence or breach of contract". You are looking fairly good at there being coverage for the engine damage... even if there was negligence by the crew which exacerbated the problem. In other words, your damaged engine will be a covered loss... except for the part that caused the failure. And that is where it gets interesting!

You do not know what cause the engine to fail. You do not know what damage was not caused by the initial failure, but from the resulting rough seas in heavy weather. The charterer claims your crew was negligent or there was a design defect. Your initial instinct is that the repair facility must have done something wrong. Could it have been, possibly neither: Bad fuel, perhaps? A failed purportedly non-serviceable high pressure fuel pump (properly not part of the partial rebuild)... which is later discovered (manufacturer misrepresentation aside) is actually easily serviced with the replacement of an inexpensive internal fuel filter?

But you are concerned because the charterer may claim that fuel pump is a possible latent (hidden) defect rendered your yacht unseaworthy on the date the charter agreement was executed... even with your service records and Classification Society surveys up to date, the concept of bad fuel seemingly still in play... and potential liability is staring at you.

Now, what do you do? Hold your cards close to your vest and fully evaluate whether that insurance policy - even if it pays - will be to your advantage.

That is a complex, but classic, reason why one must consider all of the "C's" when considering the legal and insurance issues. Here, obviously, "contract" "certification", "crew", "charter" and "conflict" all have come into play.

## **HOW DO I PROTECT MYSELF DURING A REFIT OR REPAIR?**

One area of great superyacht operational exposures is a visit to a shipyard. The best way to minimize the exposure to various forms of liability is to make sure all relevant parties have the appropriate insurance and that they enter into the appropriate contracts...with appropriate controls.

There is rarely an excuse for not negotiating an agreement and rate sheet prior to the yacht's arrival at the shipyard. In my opinion, one of the essential things to do is obtain the shipyard's written agreement that the Owner is not liable for any work which is not authorized in writing by the Owner's Representative or materials obtained by the crew over X dollars. This not only prevents an overly enthusiastic captain or runaway

engineer from committing the yacht to improvidently priced work or materials, it may well prevent unnecessary, ill-designed or untimely work from being performed on this multi-million dollar asset... possibly without the necessary coordination with the classification society. (There are many issues on what else should be included in such an agreement, but there is not sufficient time to go into this in detail.)

Part of that agreement must be a disclosure of the liability insurance of the repair facility as it relates not only to personal and property insurance, but also as to acts and omissions in relation to it work. A warranty without financial backing can, obviously, be worthless. Finally on this point, if possible the yacht and/or its Owner should be identified as an additional insured during the time the yacht is in the repair facility.

It is also essential that as to each individual work order that the specifications for that work be sufficiently spelled out. Terms such as "yacht finish" only lead to disputes. Be sure that if, for example, paint work is being performed or stainless steel is part of the task, it be specified in technical terms. Many times a simple hand drawn sketch can be attached to a work order to add clarity and avoid costly mistakes (both as to time and money).

One final point on insurance: While the Owner will require insurance of the repair facility and it will also have insurance to cover many errors or negligence of the captain and crew, many Owner's Representatives or Yacht Managers simply do not have professional liability insurance. Where, as here, the dollar figures are substantial and, therefore, the cost to the Owner of an error may be quite significant, I believe it is time for insurance to be required of them. The lack of a professional's ability to respond to an Owner as a result of his/her error has lagged behind the astronomical increase in cost and value of superyachts.

Here we have briefly looked at "contract", "construction", "certification", "crew", and avoidance of "conflict". Imagine if the focus was just on getting that bit of work done without consideration of the various pitfalls. Actually, for many Owners, it would not be "imagine" it would be "history".

## **HOW DO I LEGALLY OPERATE A SUPERYACHT IN U.S. WATERS?**

Let's look at another example; one recently discussed as being a source of utter frustration for a foreign flagged superyacht seeking to ply some of the more remote waters of the United States:

A foreign flagged yacht wants to enter the US and then travel directly from one U.S. port to another U.S. port. As we know, it is not a matter of showing up, clearing customs and cruising off.

First, the crew must obtain the appropriate Visas; either C-1/D or B-1; a C-1/D generally being more appropriate for charter yachts (as it is fashioned for transiting crew with a planned onward journey) and a B-1 for private yachts (where the crew may take some personal time off to travel in the US during the ship's stay in US waters).

Next, an environmental Certificate of Financial Responsibility must be obtained; including the posting of a bond insurance policy with a Coast Guard approved insurance company. As few superyachts are under 300 gross tons, it will apply to most yachts. It is of interest to note that regardless of whether the yacht charters (of course, chartering a foreign flagged vessel in the U.S. is essentially prohibited) it is still considered a pleasure craft - rather than a passenger vessel - if it does not carry more 12 "passengers for hire". This should be in place, hopefully, 60 days prior to the scheduled arrival.

The National Vessel Movement Center (NVMC) must be notified at least 96 hours prior to the foreign flagged yacht's arrival in U.S. waters. If, however, the voyage will take less than 96 hours (say, from the Bahamas to Miami), the notification must be given prior to departure, but no less than 24 hours before the expected arrival in the U.S. This notification, which must be done online, must include the crew manifest, crew effects declaration and ship's stores declaration. A Notice of Departure and a separate Notice of Arrival

may be required for each subsequent U.S. port visited outside of the then present local Coast Guard office's jurisdiction.

The U.S. Coast Guard's local office must also be contacted prior to the yacht's initial arrival as there are two possible requirements: (A) a Security Inspection; and, (B) a Pilot. Once the yacht enters U.S. waters it is theoretically (and in the Port of New York, for example, not so theoretically) monitored and is not permitted to proceed into the harbor without the inspection. It is, generally, at about the same location that a local pilot is required to board. The pilot is privately obtained through the local Pilot Association, who keeps in contact with the Coast Guard and the requirement for a pilot varies by port, so the local regulations must be checked in advance.

Finally, Customs and Border Protection must be contacted and coordinated. Upon arrival at the first port, the yacht and crew must be cleared by Customs and Border Protection. One point of concern can be where does the crew clear Customs? Hopefully Customs will come to the yacht, but if negotiations fail, you may well be bringing the crew to the local office. Upon clearance a Cruising License may issued which allows the foreign flagged yacht to cruise the U.S. waters from port to port provided the local Customs officer is so advised and there is a local pilot onboard when required.

The requirements are generally very easy to follow, assuming all of your crew can obtain the necessary visa. The one area of difficulty can be the requirements for a local pilot where there can be local or federally mandated pilot requirements. Complicating the matter can be how you get the pilot onboard and then back to port when you are traveling in more remote areas... or, if it is possible, for the pilot to remain onboard for an extended period.

A point to keep in mind, if you operate your yacht without a required pilot and sustain a loss you may well be without coverage.

So when addressing the Operation and Insurance of a superyacht, please remember to consider the interrelationship between "contract", "construction", "certification", "crew", "charter" and "conflict".