Offshore and Renewables Team – Contract Review Guide

The West recognises the unique nature of risks faced by Members operating in the Offshore sector and offers a tailor-made insurance solution to cover these additional risks which sits alongside and augments the Member's normal P&I Rules cover.

The West's services to Members under this product include:

- Reviewing contracts and charterparties
- Identifying contractual liabilities assumed under the contract
- Offering advice on amending the contract or failing that we will provide creative solutions in the form of additional cover.

1 Background: Mutual P&I Cover

Standard Mutual P&I covers the Member for legal liabilities arising out of their management and operation of a vessel entered in the Club. It responds to legal liabilities "at law", as opposed to liabilities assumed under a contract - known as "contractual liabilities". Legal liabilities may be incurred due to a Member's negligence i.e. tort, or by application of strict liability in law or statute, such as is often the case in incidences of pollution.

Legal liabilities covered by Mutual P&I Cover include

- Liability to seafarers
- Oil pollution from the vessel
- Loss of or Damage to third party property
- Wreck and debris removal of an entered vessel
- Collision and allision claims.

2 Contract Reviews

We look to advise our Members with regard to potential contractual exposures, providing creative solutions when additional covers are required.

The following are common issues we focus on and which may require additional cover.

a) Governing law and jurisdiction of the contract

Given that Club Rules are drafted in accordance with English law, it is the West's preference that the chosen law governing the contract should be the same. The Club would also prefer any disputes leading to judicial interpretation of the contract to be subject to the jurisdiction of the English courts. This is because, in some legal systems, there may exist certain statutes, rules or procedures which contradict Club cover. For example, the anti-indemnity laws of certain US states or certain legal system requirements of the Egyptian courts.

However, in many cases the Club concedes that in practice it may not be possible for the Member to dictate contractual terms.

b) Knock for Knock Liabilities

For the liabilities and indemnities provisions of a contract to fall under standard cover, it is a requirement that they be on a "Knock for Knock" (K4K) basis. This means that the provisions must stipulate that:

i) each party to a contract shall be similarly responsible for loss of or damage to, and/or death of or injury to, any of its own property or personnel, and/or the property or personnel of its contractors and/or of its and their sub-contractors and/or of other third parties, and that

ii) such responsibility shall be without recourse to the other party and arise notwithstanding any fault or neglect of any party and that

iii) each party shall, in respect of those losses, damages or other liabilities for which it has assumed responsibility, correspondingly indemnify the other against any liability that that party shall incur in relation thereto.

Essentially, the above means that the Member should be responsible for their own property and personnel and the other contracting party should be responsible for theirs, no matter who is at fault, and that they should protect each other from claims made by people outside the contract.

It is common in the Offshore industry for K4K regimes to be eroded by Operators keen to assert their dominant negotiating position. Therefore, it is highly advisable for all contractors to have Contractual Cover in place at least up to the required contractual limits stated in contracts.

i. Unbalanced Groups

An example of such an erosion is the now common practice for the contracting groups in Offshore contracts to be "unbalanced". Under a standard K4K regime, an Owner should take liability for the property and personnel of his own self, plus his contractors and subcontractors. A Charterer may only give the reciprocal indemnity in respect of his own self and exclude the property of his contractors and subcontractors usually by simply failing to mention them in the clause. Again, this would mean that the Member requires Contractual Cover to respond for claims made against him in relation to the property and personnel of his contractors and subcontractors or in respect of indemnities provided by him.

In contracts for Offshore and subsea construction and maintenance work, there is a higher probability that a Member will engage subcontractors than in a typically simple chartering scenario. In such circumstances, it is good practice and often a contractual requirement for an Offshore contractor to flow down the liability regime from his head contract into his subcontracts.

c) Third Party liabilities

It is not un-common to see contractual provisions concerning liabilities to third parties outside the contract in a clause separate from the K4K. Members should be cautious about the effect of such clauses because they may significantly increase their exposure and the resulting liabilities could potentially fall outside standard P&I Cover.

The preferred scenario for the Club is for the contract to remain silent on third party liability, thereby allowing such liabilities to lie where they fall. Normally, at law, liability will be negligence/fault-based or based on strict liability as often in the case of pollution. The Club takes this view because it avoids any potential confusion with the K4K liability and indemnity regime.

d) Limitation of Liability

It is fundamental to standard P&I Cover that Members should not expose themselves to liability greater than that which they find themselves under the prevailing law.

Members should be wary of agreeing to specific caps on liability in contract, as these could be greater than the ship's limitation under the law and could be interpreted as a waiver of right to limit. The Club's preference is therefore for a specific clause preserving the Member's right to limit liability, which is covered by standard P&I Cover. Anything in excess of this limit would require Contractual Cover.

e) Pollution from the entered vessel

A central tenet of standard P&I cover is to provide insurance for any loss/damage caused by pollution from the Member's vessel. This includes the costs of any clean-up operation. In some contracts, provisions may stipulate that the contracting party be in control of the clean-up operation and allow them to invoice the Member for such costs. It is essential for Mutual P&I cover that the Club deems such costs to be reasonable. If not, Contractual Cover may respond to the excess amount. Ultimately, it is important that the Member always retains control of the costs for which they may be billed and for which they may claim indemnity from the Club.

f) Cargo and property

Mutual P&I Cover is designed to insure merchant ships for liabilities to cargo according to international norms, namely the Hague/Hague Visby Rules. In the context of Offshore, however, such rules have little relevance and are not usually incorporated. Nevertheless, in determining any claim, it would fall on the Club to determine the extent of the Member's liability under the Hague/Hague Visby Rules. Such liability would be covered under standard P&I Cover - liability beyond that would require Contractual Cover.

g) Contractual Wreck Removal

Wreck removal is a legal liability insured by the Club under standard P&I Cover. Normally, for liability to attach, the wreck will be a hazard to navigation and/or the local authorities will issue a Wreck Removal Order. However, a common clause in the Offshore industry is for any wreck removal of the Member's vessel to be subject to the will of the contracting party. This means that a wreck must be removed according to contract and simply at the request of the Operator. Insurance for such a contractual commitment would require Contractual Cover.

h) Insurance provisions

Where the liability and indemnity terms of a contract are not clear, the courts will often turn to the contract's insurance provisions to shape their interpretation. Where the different provisions conflict, the courts regularly allocate liability to the party upon whom the contractual obligation of insuring the risk has been placed. Therefore, it is of paramount importance that the insurance provisions of any contract be reviewed to ensure they reflect the true position laid out in the liability and indemnity regime. Other commonplace issues with the insurance terms in a contract include:

i. Waiver of Subrogation

Subrogation is the right of an insurer, once it has made payment to its assured for a covered loss, to step into the shoes of the assured and to exercise any rights or remedies which the assured has against the person who caused the assured to suffer that loss. Normally, a provision waiving this right will mean that an insurer cannot sue the person at fault. In the context of a proper K4K liability regime in the contract, such a provision is included as a "belt and braces" measure, ensuring that an insurer cannot seek to challenge the validity of the K4K provisions by suing the contracting party; eg. for loss/damage/injury to the assured's property/personnel caused by the contracting party's negligence.

The language of these clauses needs to be precise or an Owner granting a waiver can give up his insurer's ability to recover the pay-out for the Owner's loss for a claim which falls outside the K4K liability regime, eg. a third party claim which was actually caused by the Charterer.

Such waivers should not therefore be defined in general terms in relation to "all claims" but qualified to apply, on one hand, only to those liabilities that are the responsibility of the Owner and, on the other hand, not applying to those liabilities that belong to the Charterer under the contract.

ii. Naming of Co-assureds

It is commonplace for a charterparty to include a provision requiring the Charterer to be named "co-assured" under the Owner/Member's Mutual P&I Cover. (Sometimes the phrase "additional assured" is used but understood to have the same meaning).[1] This means that the person named co-assured will have the ability to rely on the Member's Mutual P&I Cover for liabilities that would have been recoverable by the Member if the claim had been made against the Member rather than the person named co-assured. This is often described as the co-assured having the benefit of "mis-directed arrow cover", which will entitle him to rely on the Member's policy to defend himself against such a claim, but he cannot rely on the Member's Mutual P&I Cover for liabilities which properly belong to the co-assured according to their contract with the Member.

3 Specialist Operations

Specialist Operations are contracted works undertaken by the Member of such a nature that go beyond those generally carried out by traditional shipowners. Such activities are defined by Rule 17C of the Club's Class 1 Rules, which sets out a list of what are considered to qualify: "dredging, blasting, pile-driving, well-stimulation, cable or pipe laying, construction, installation or maintenance work, core sampling, depositing of spoil and power generation".[2]

The following examples, although not exhaustive, can therefore be covered under a Specialist Operations extension:

- Extended towage of offshore drilling rigs and other vessels
- Incidental salvage under an offshore contract
- Construction and maintenance projects
- Pipe and Cable laying operations
- Liability of use of ROVs for which the Member is responsible
- Liability of divers for which the Member is responsible
- Dredging operations.

Where required, under the West's Offshore and Renewables Cover, cover for Specialist Operations can also be integrated with the cover for Extended Contractual Liabilities. This Contractual Cover responds to liabilities that arise out of a P&I risk but for which the Member would not be liable "at law". For example, in a Wreck Removal case where the damaged vessel or equipment was not a hazard to navigation but where removal was required in contract simply at the behest of the other party. In this instance, the Member would be insured up to the agreed limit of Contractual Cover purchased.

It must be stressed, however, the such coverage is always subject to contract approval, so normally the Club will require sight of the contract prior to the operation taking place. It is during this process of contractual review that the Club ensures that the Members' liabilities are sufficiently covered and, if not, can propose solutions to bring the contract back in line.

i. Damage to Contract Works, CAR Deductible Buy-back

The property being constructed or positioned in Offshore projects, is normally insured by the Turnkey Operator under a Construction All Risks (CAR) policy. As liability for damage to such "Contract Works" is excluded from Mutual P&I Cover, it is not normally something which an Operator can pass on in contract to his contractor, even in the event of their negligence. However, some Operators deem it appropriate for their contractors to have "some skin in the game" by including a clause which passes liability for such damage to the contractor as a result of their negligence for a capped amount, usually the deductible under the CAR policy. This is often referred to as a Deductible Buy-down. In this instance, the Club is willing to insure such liability under its Contractual Cover subject to contract approval.

[1]Confusion often stems from opposite terminology being used in the Lloyd's market, where the term "co-assured" usually refers to a person being named assured under a policy for their contractual obligations in the context of a Joint Venture, and "additional assured" referring to a person merely having the benefit of mis-directed arrow cover under another's policy.

[2]Please note that liabilities incurred by vessels performing O&G drilling and/or production and certain accommodation units integral to such activities would not be covered under the West's Mutual or Extended Covers.

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