

Aviation Contracts Made Easy

What the underwriter looks for when reviewing a contract

By Thomas H. Chappell

I have written about the tricky nature of contracts. Yes, I know some of you are attorneys, but you must admit that there is easier reading than a contract, even the good ones, and some are just plain sneaky. You guys need to take a lesson from the insurance industry and include a definitions section and a section for exclusions. Well, maybe not. Insurance policies aren't exactly easy reading either.

All kidding aside, even the best contracts can be quite confusing to the layman, especially if he is not accustomed to reading legal documents. Some of the contracts we are asked to review on behalf of our clients are written for the purpose of communicating. They openly convey ideas and agreements between two or more parties. These are good documents. Unfortunately, the majority of the documents we see make absolutely no sense to many of our clients. In many situations, the average businessman will do his best to read and understand a contract himself, but will not seek the advice of an attorney for fear he will spend a little money. I often hear, "If you get the attorneys involved, you will spend a lot of money and the deal will never get done." This is a dangerous attitude. If you read a contract and don't have a clear understanding of the content, you need an attorney.

You must still be cautious. Make sure your legal advisor understands aviation and aviation insurance. The aviation industry has a vernacular all its own. In school and in most textbooks, attorneys learn insurance as it pertains to the general property and casualty world. Because of the unique language of the aviation industry, aviation insurance policies may vary greatly from property and casualty insurance in content and definition.

Often, the aircraft owner will send a copy of a proposed contract to the aviation insurance agent to review. Few insurance agents are attorneys and most don't want to be. We cannot give legal advice. What we can do is to advise whether the underwriter is likely to accept the contract and whether he will extend coverage. In the review process, our client will realize a lot about what he has been asked to sign. Obviously, if the contract is unfit for the underwriter to insure, it is also unfit for the client by exposing his--personal or business assets.

Note: In the general property and casualty industry, contractual liability is very broad and, in some circles, is referred to as "blanket contractual" liability. In aviation, contractual liability

In my agency, when we are asked to review a contract, one of my senior staff or I will discuss the document with the client and explain what we think the underwriter's concerns may be. This discussion will alert the client to potential exposure problems and allows time to renegotiate the contract provisions that affect the aviation insurance risk. These

changes can be made before submitting the document to the aviation underwriter for approval. This allows “fewer trips to the well.” I prefer to submit requests to the underwriter that will be approved on the first submission.

As mentioned above, most aviation insurance policies require underwriter approval before assuming any contractual liability. This approval process avoids any potential interruption of coverage because of difficult indemnification agreements or uncovered and unreasonable insurance requirements.

What is it we are looking for? Well, it isn't rocket science. In fact, reviewing and understanding a contract is easy, especially after you have read a few. Most fall into a pattern and often use the same words and phrases.

For insurance purposes, we are interested in just two sections. One is a section usually entitled INSURANCE. The other is a section entitled INDEMNIFICATION. Occasionally, some sneaky attorneys will incorporate indemnification wording within other sections in an attempt to hide or disguise variations on “hold harmless agreements.” Normally, you will find it under a plainly labeled section.

INSURANCE:

The section entitled insurance will list the various coverages and limits that the contract requires. It is important to the first party of the contract that the second party be financially responsible and insurance is the simplest way to accomplish this. In the insurance section, the author will specify the individual coverages, policy terms and conditions, and policy limitations that are acceptable to the first party. It is important to research the policies to be absolutely sure that before you sign the contract the coverage required is, in fact, in your policy or at least is available for a price you can justify. Skipping this step could mean agreeing to something in your contract that the underwriter will not confirm in the insurance certificate. Most contracts require that a certificate of insurance be issued confirming insurance coverage, terms, and limits.

If you sign a contract agreeing to provide certain insurance coverages that are not available, you may find yourself in a difficult situation if not in full default.

Frankly, a good insurance agent is the best person to confirm that the coverage required in the contract actually exists in the policy or can be obtained for a premium that is acceptable. The best time to do this is before the contract is signed. Many times the contract will require coverages that, in reality, are not pertinent to the situation or cannot be purchased.

Note: This is where the insurance section begins to interface with the indemnification section. Example: You are negotiating a hangar lease. The insurance section may require you to carry all risk hull insurance. It further requires a waiver of subrogation by the underwriter to the landlord. You are signing a simple hangar lease. Why should the landlord care if you insured your aircraft hull? Smell a rat? Just read on.

INDEMNIFICATION:

In the indemnification section, the contract states that you will hold the landlord harmless for any and all liability or damage to your own property regardless of negligence. Ah-Ha! They just tried to slip one by you. If the landlord damages your aircraft, through a hold harmless agreement, you may have forgiven him for his sins. Through the waiver of subrogation, your insurance company is required to repair your aircraft and cannot recover the cost of the damages from the negligent party, the landlord.

In this case, the solution is not to ask your underwriter to waive any right of recourse against the negligent party. The right thing to do is to insist that the contract be reworded to state “that you will hold the landlord harmless for any and all liability or damage, but only for acts arising out of the operations of the tenant (you) and only as the result of the tenant’s (your) negligence.

Just because the contract requires certain wording does not mean that the words cannot be changed. The thought from attorneys writing most contracts seems to be: “Let’s ask for it and sometimes they will sign.” Maybe they will just sign the contract and never read it. In reality, this frequently happens.

There is also the intimidation factor. “This is our contract. We are a big company and this is our policy.” The assumption that contract wording is carved in stone is incorrect. Even with large companies, manufacturers, and national fixed base operators, wording can be modified. Who gains the most from an agreement? That is the one who will guide the policy wording in the end.

POORLY WORDED PHRASES:

Look for poorly worded contract sections or phrases. There is no malice intended, but the outcome can be detrimental.

Many attorneys use canned wording when writing the insurance section of a contract. Frequently, they use wording that is designed for the general property and casualty industry. You can always tell, because in aviation, we use a different vocabulary than that used in the “real world.” Terms attorneys often use such as “public liability” and “personal injury” are nonspecific or totally archaic in the aviation world. It might be more specific if they referred to aircraft liability, passenger liability, or bodily injury and property damage.

To make my point: In the “old world” insurance vernacular, personal injury and bodily injury were considered to be synonymous. Personal injury was the broader of the two. Personal injury not only included bodily injury but also included coverage for libel, slander, defamation of character, false arrest, wrongful eviction, malicious prosecution, invasion of privacy, or withholding of civil rights. In today’s insurance world, a contract referring to personal injury would not include bodily injury. Personal injury has now been redefined to mean libel, slander, defamation of character, etc. In fact, personal injury is usually seen paired with advertiser’s injury.

I said all that to make the point that contract wording taken from “old school” textbooks may be completely wrong. In addition, standard contract templates are often built around generic businesses and general property and casualty policy forms. When used in the aviation insurance world, such agreements become misleading to both contract parties. Referring to our example of contractual liability, thinking that any contract would be covered could be dangerously misleading.

You can see how important it is for you to thoroughly review an aviation-related contract before signing. I would recommend having your attorney review the contract and forward a copy to your insurance agent for underwriter approval. You are the one signing on the line. It is your assets that are at stake. Ultimately, it is your responsibility to protect yourself. I hate to say it; you too must read the contract.

WHAT DOES THE UNDERWRITER LOOK FOR?

As mentioned above, the two sections most important to the underwriter are the Insurance section and the Indemnification section. Reading one without the other cannot offer a complete picture.

The insurance section simply lists the coverages the contract author believes to be important to the agreement. In most cases, they list an array of coverages (whatever they can find in the textbooks) for you to agree to buy. Beware, some of these coverages are very expensive and, in some cases, unavailable. In addition, many times the contract will ask for coverage that is of no importance to the agreement but will cost you money. The time to deal with this issue is before the agreement is signed.

We have seen products liability be required for an aircraft hangar tenant who simply is storing his aircraft. We have seen workers’ compensation required for a hangar tenant who has no employees. Some hangar agreements require “on premises” auto insurance where no cars are allowed. In short, the attorney just didn’t read his standard agreement or didn’t understand the exposure.

Your agent should be able to quickly review the coverage the contract requires and note the areas for which you have no protection. He will also be able to tell you any required coverage that does not apply to you or your situation. (We are assuming that your agent is an aviation insurance specialist.)

When the contract negotiations are finished and your underwriter signs off on the agreement, your insurance policy and the contract you are to sign must match. Otherwise, you have a gap through which your assets could be exposed. Remember, you have agreed to the contract and backed it with your assets whether the insurance company becomes a party to it or not. In the aviation insurance world, it only makes good sense for you to obtain your underwriter’s approval before signing the contract.

The indemnification section can be much more vicious than the insurance section. If you are willing to pay the premium, additional coverage can usually be added to your policy to meet the insurance requirements.

Assuming liability that you may otherwise not have could be catastrophic. In most cases, your underwriter will not extend coverage to assume someone else's liability. Dangerous phrases often found in contract indemnification sections are "to save and hold harmless for **any and all liability**" or the phrase "**regardless of negligence.**"

Does this happen? You bet it does. Just this week I was asked to review a classic example. I will let you read the indemnification section and see if you can pick out the "landmines."

***Indemnity Section:**

"Except for injury or damage caused by the willful misconduct or material breach of this Lease by Landlord, Tenant shall indemnify Landlord against, and hold Landlord harmless from, all claims for death, bodily injury, property damage or other loss or damage occurring on or about the Leased Premises, even if such damage or injury was caused or allegedly caused by Landlord's negligence. Tenant acknowledges and agrees that Tenant's use of the Leased Premises is at Tenant's sole risk. Tenant shall make no claim against Landlord for damage to Tenant's aircraft or any other property occurring on or about the Leased Premises or for any injury to any person occurring on or about the Leased Premises, even if such damage or injury was caused or allegedly caused by Landlord's negligence."

**This contract excerpt was taken from an actual lease that was presented to one of my clients to sign. I would have gladly given credit for authorship if the name had been disclosed.*

The attorney who wrote this was doing his job. He was simply passing as much as he could of his client's potential liability exposure off onto someone else and their insurance company. Well, it is worth a try.

In just one little paragraph, the author of this indemnification section contracted:

The tenant to pay on behalf of the landlord even if the landlord is the cause of the loss;

The tenant to occupy the premises at his sole risk;

The tenant to make no claim against the landlord for damage to his aircraft, or for injury to any person or property even if such damage is the landlord's fault (negligence).

Do you think your underwriter would extend coverage to include this landlord? Would you sign a contract containing this Indemnification clause? Does the phrase "all claims" seem a bit broad? If this was a hangar agreement with a fixed base operator, "all" could be construed to include products liability, damage from aircraft towing, hangar rash, and contaminated fuel. Judgments resulting from litigation could far exceed the liability limits of your insurance policy.

Don't let contracts confuse you. READ A CONTRACT THE EASY WAY by starting with the indemnification section. →