



## Insight Article

# Co-assurance

Rule 781 of the of the Association's Rules for Ships, sets out the different types of co-assurance available and the various categories of co-assureds. The first part of this article distinguishes co-assurance from two other types of cover with which it is sometimes associated, namely joint membership and cover for affiliates; the second part discusses co-assurance under the Rules for Ships.

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Although Rule 79 2 is entitled "Joint Members, Co-assureds and Affiliates", these are three entirely different entities. Joint membership arises where the vessel is entered in the names of two or more owners or operators. 3 All joint Members on an entry qualify for membership in the Association and enjoy all rights of Members of the Association, which are set out in the Association's Statutes. These rights include voting rights at the Association's General Meeting and eligibility for membership on the various committees. On the other hand, co-assureds are *not* Members of the Association, they are merely named insureds on a Member's Certificate of Entry. Their cover is restricted under the terms of the Member's entry and Gard's Rules 78 and 79. Co-assureds are not entitled to membership in the Association and therefore they do not have the same rights as Members. For example, they have no voting rights in the Association. The most important distinction between the co-assured and the affiliate is that, although neither can be Members of the Association (under Rule 78.2), the co-assured is expressly named in the certificate of entry whereas the affiliate is not (under Rule 78.1). Consequently, the co-assured is "an insured". He is a party to the contract of insurance, so he is entitled to the benefit of the contract of insurance as of right, pursuant to the terms and conditions agreed when he was named. On the other hand, the affiliate is not "an insured"; he is not a party to the insurance contract and therefore he is not automatically entitled to the benefit of the contract. After an incident has arisen, the Association, in its sole discretion, may agree to extend cover to an affiliate, but is under no obligation to do so. This in turn produces other distinctions between co-assureds and affiliates. One such distinction concerns liabilities under the insurance contract. Because the affiliate is not a party to the contract of insurance, he is never liable for payment of premium or calls (although the Association can set off any outstanding premium against compensation paid to an affiliate). In contrast, normally co-assureds, like joint Members and Members, are jointly and severally liable for all sums due to the Association under the Certificate of Entry in which they are named as co-assured, including supplementary and catastrophe calls. Co-assureds' liability for premiums and calls is discussed under the heading, "Liability for calls", on page 6 of this issue.

## B. CO-ASSURANCE UNDER GARD'S RULES

Rule 78 sets out the principles relating to co-assurance under the Rules for Ships, and also describes the bases upon which various entities may be named in the contract of insurance as co-assureds. There are three categories of co-assured cover, and they are defined in Rules 78.3, 78.4 and 78.5, which are: (1) Operators, crewing agents, mortgagees, etc. under Rule 78.3; (2) Associated Charterers under Rule 78.4; and (3) Misdirected arrow cover and protective co-assurance under Rule 78.5.

Under Rule 78.3: Operators, crewing agents, mortgagees, etc.

Cover under this Rule is meant to protect parties who may be carrying out, usually under contract, what is in effect part of the owner's tasks, and who are at risk of being sued because of their direct involvement in the operations of the entered ship. In order to be eligible for cover under Rule 78.3, the potential co-assured must bring himself within one of the three categories enumerated under that Rule. These potential co-assureds vary greatly in terms of degree of engagement in the operations of the vessel. On the one end of the scale, there are financial owners who

are more or less silent in the running of the ship. Slightly more involved but still at the low end of the scale in terms of operational involvement are crewing agents, who

*merely employ crew, or concessionaires on a cruise ship or passenger liner who operate only their particular business. On the other end of the scale there are fully fledged ship managers, who effectively take over the tasks of the owner.*

#### *Scope of Cover under Rule 78.3*

There are two limitations that apply to all categories of co-assureds under Rule 78.3. First, the cover extends only to liabilities arising out of operations or activities normally carried out by, or at the risk and responsibility of an owner (or charterer, under a charterers' entry). If a party co-assured under Rule 78.3 is acting only partially in one of the capacities described above, he is only partially protected by his co-assurance. The second limitation is that the co-assured is only insured for those risks for which the Member has cover.

#### *under Rule 78.4: Affiliated or Associated Charterers*

Where there is certain degree of unity of financial interest between the Member and the charterer, such that the charterer may be considered to be affiliated or associated with the owner, then the charterer may be eligible for co-assured cover under Rule 78.4. Cover under this provision is normally restricted to those cases where owners and charterers are owned by the same company or group of companies, or are engaged in a joint venture of some sort. Cover is also available under this provision where there is some pooling of expenses or profits between the Member and the charterer, even where there is no link in ownership. An example of this type of "borderline" affiliated charterer under the Rule is where a charterer and the entered owner share some expenses under a charterparty.

#### *Scope of Cover under Rule 78.4*

Assuming a potential co-assured meets the requirements that he is an affiliated or associated charterer, then he has cover under Rule 78.4 for all the risks, liabilities, losses, costs and expenses that he incurs in his capacity as charterer of the Ship, provided they are risks for which the Member has cover.

#### *under Rule 78.5: Misdirected Arrow Cover*

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Finally, there is the third category of co-assurance, which is available under Rule 78.5. Misdirected arrow cover applies to those cases where a co-assured is found liable to pay in the first instance for loss or damage which is properly the responsibility of the Member, and extends only to those amounts which would be recoverable from the Association had the claim in respect of such loss or damage been made or enforced against the Member. There may be cases where a claim should properly be brought against the Member, but is instead brought against the co-assured. It could be that the Member is insolvent, has no assets in the jurisdiction where the claim is brought, or for any other reason is difficult to sue, so a co-assured is sued instead. If the Member would have been covered had the claim been brought directly against him, then the co-assured is also entitled to cover on the basis of misdirected arrow cover. The only type of co-assurance available to independent charterers is protective co-assurance under Rule 78.5. Independent charterers are not eligible for co-assurance under Rule 78.3 and 78.4, nor misdirected arrow cover under Rule 78.5. Protective co-insurance is governed by strict rules in the Pooling Agreement of the International Group of P&I Clubs, and is only available in respect of offshore contractors. The Clubs in the International Group have restricted cover for independent charterers in this way because the risk that a Club may be forced to provide greater cover for a co-assured than what was agreed outweighs the benefits in offering cover for independent charterers.

#### Scope of Cover under Rule 78.5

Under this Rule, the cover is limited to what the co-assured may be found liable to pay in the first instance for loss or damage that is properly the responsibility of the Member. Nothing shall extend cover beyond what the Member could recover had the claim been made directly against him. To recover his losses under Rule 78.5 co-assurance, the co-assured must show that, had the claim been brought against the Member instead of the co-assured, the Member would have been held liable. This is the key feature of misdirected arrow cover, and the most important distinction between Rule 78.5 and Rules 78.3 and 78.4. Whereas Rule 78.5 cover protects the co-assured from liabilities for the Member's acts or defaults, Rules 78.3 and 78.4 cover the co-assured for their own acts or defaults.

#### C. THE THREE CATEGORIES OF CO-ASSURANCE COMPARED

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The nature of the risk covered and the extent of the cover under Rules 78.3 and 78.4 are entirely different from that under Rule 78.5. A co-assured under Rule 78.3 has full cover for liabilities and losses he incurs as a result of his own acts or omissions, but only to the extent that the liabilities or losses arise out of customary shipowners' activities (or customary charterer's activities, for a charterer's entry) and to the extent that the Member has cover. Likewise, a co-assured under Rule 78.4 has full cover for his own acts or omissions as a charterer, but only to the extent that the Member has cover. This may be a serious limitation if the owner has made any exclusions in his P&I cover. For example, if the Member has chosen to exclude cargo cover, then the co-assured cannot recover for cargo liability. Cover under Rule 78.5 protects the co-assured only from those losses which he incurs as a result of the Member's, not his own, acts or omissions. There is another distinction between the cover available under Rules 78.3 and 78.4 from the cover available under Rule 78.5, which arises by operation of Rule 78.7. This Rule provides that the Association's indemnity of a co-assured under Rules 78.3 and 78.4 does not reduce its obligations towards the Member on the same entry. There is a type of multiple liability in respect of the same entry (i.e. to the Member and to each and every co-assured). In contrast, under Rule 78.5, the Association's liability in respect of any claim is limited to its liability to either the Member or the co-assured. In other words, for Rule 78.5 cover, once indemnity limits have been reached, no more money is due to either the Member or co-assured or anyone else.

#### D. THE EFFECT OF RULE 79

There are several provisions in Rule 79 of an administrative nature that apply to all types of co-assurance. They are designed to facilitate the administration of the cover, and reflect the degree of mutuality between co-assureds, joint assureds and affiliates covered under a Certificate of Entry. Under Rule 79.1, co-assureds are jointly and severally liable for sums due to the Association, which is discussed below. Under Rule 79.2, payment from the Association to any one of the assureds (including co-assureds) or affiliates under the terms of entry shall discharge the Association's obligations in respect of such payment. Under Rule 79.3, communication from the Association to one of the co-assureds or joint Members shall be deemed communication to all. Finally, and most importantly, under Rule 79.4, the act or omission of one joint Member or co-assured which would constitute a breach of the Rules is deemed to be the act or omission of the other joint Members and co-assureds. In this way, the conduct of one co-assured can have the consequence of excluding cover for another co-assured under the same entry.

#### E. LIABILITY FOR CALLS

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Under Rule 79.1, all types of co-assureds are jointly and severally liable for all sums due to the Association in respect of any entry. This includes premiums, as well as supplementary calls and catastrophe contributions, deductibles and expenses. This does not always prevail in practice. Generally, if unlimited cover is available, then the co-assured is liable for calls. For example, a holding company co-assured under the owner's entry under Rule 78.3 is liable for calls because they are insured for their own risks as well as for owner's risks. This is the same for an affiliated company co-assured under Rule 78.4. They are insured for their own risks as a charterer, so they are liable for premiums. However, the Association may agree to waive Rule 79.1 in respect of a co-assured under Rule 78.5, so that he would not be liable for calls, deductibles, expenses, etc. The rationale is that under protective co-assurance and misdirected arrow cover there is only one risk covered, which is owner's risk. For all types of co-assurance there is only one retention per event, and no separate premium is usually charged to the co-assured, although the underwriters assess against the Member the additional exposure resulting from having additional assureds on the Certificate of Entry. In other words, although there is only one premium for the assured and all of the co-assureds named on one Certificate of Entry, the premium takes into account the additional risk exposure of having co-assured covered on the same entry.

#### F. IS CO-ASSURANCE ALWAYS A BENEFIT?

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Some potential co-assureds, such as mortgagees or ship managers, are eligible for co-assurance but do not want to be named as co-assureds on the Certificate of Entry. Sometimes this is because these parties do not want to be responsible for premiums and calls. In some cases, parties such as mortgagees and beneficial owners do not want to reveal their connection to the assured; the mere fact of being named on a Certificate of Entry may mean they are more likely to be named as co-defendants in an action against the primary assured. Some ship managers feel it is not necessary to be named as co-assureds on the owners' certificate of entry. Where the ship manager is functioning only as an agent of the shipowner, and has not taken over some or all of the owner's responsibilities in his own name, at his own risk and for his own account, then the ship manager may feel that he has sufficient protection because of the agency relationship between himself and the owner (i.e. any claims against the owner are properly brought against the principal, not his agent, so there is no need to arrange co-assured cover). Alternatively, the ship manager may feel that the terms of his contract with the owner place all risks with the owner, so there is no risk to cover. Even the manager functioning strictly as an agent of owners derives several important benefits from co-assurance under either Rule 78.3 or Rule 78.5. First of all, the manager is exposed to misdirected arrow claims even as an agent. Secondly, regardless of how favourable the contract with the shipowners is, if the shipowner goes bankrupt the manager is exposed. Finally, (and this benefit applies only in respect of co-assurance under Rule 78.3), if the manager decides to rely on cover under Rule 78.5, he has no cover for any liability in excess of the shipowners' limitation amount. When arranging co-assurance, parties should keep in mind the effect of Rule 79.4 (i.e., the act or omission of one joint Member or co-assured which would constitute a breach of the Rules is deemed to be the act or omission of the other joint Members and co-assureds). The Member should be careful about who is covered as a co-assured on his Certificate of Entry, since the conduct of the co-assured may prejudice his cover. To summarise, there may be some overriding reason why the party eligible for co-assurance does not want to be named on the Certificate of Entry. Otherwise, the prudent operator is better protected with co-assurance regardless of the nature of his activities or arrangement with the Member.

## Footnotes

### **1 Rule 78. Cover for Co-assureds and Affiliates**

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<sup>1</sup>. The Association may agree, subject to the provisions of this Rule 78 and to such other terms as may be required, to extend the cover afforded by the Association to the Member to:

any person who is affiliated to or associated with the Member (not being a Co-assured or other Affiliate), and who shall not be specifically named in the terms of entry; and  
any other named co-assured.

2. Affiliates and Co-assured shall not be entitled to Membership of the Association.

3. The cover afforded to a Co-assured in categories (a), (b) and (c) below shall extend only to liabilities, losses, costs and expenses (or, in respect of Defence cover, to costs incurred in connection with claims) arising out of operations and/or activities customarily carried on by or at the risk and responsibility of shipowners (or, in the case of a charterer's Entry, charterers):

any person interested in the operation, management or manning of the Ship;  
the holding company or the beneficial owner of the Member or of any Co-assured falling within category (a) above;  
any mortgagee of the Ship.

4. The cover afforded to a Co-assured who is a charterer of the Ship and who is affiliated to or associated with the Member (other than a Co-assured expressly given cover by the Association in accordance with Rule 78.5) shall extend only to the risks, liabilities, losses, costs and expenses in respect of which that Member has cover, and shall be limited in accordance with Rule 52.

5. The cover afforded to all other categories of Co-assured, other than those referred to in Rules 78.3 and 78.4, shall only extend insofar as such Co-assured may be found liable to pay in the first instance for loss or damage which is properly the responsibility of the Member (or, in the case of Defence cover, insofar as such Co-assured may be required to resist a claim arising from such a liability), and nothing herein contained shall be construed as extending cover in respect of any amount which would not have been recoverable from the Association by the Member had the claim in respect of such loss or damage been made or enforced against him.

6. The cover afforded to an Affiliate shall extend only, in the case of P&I cover, to claims made or enforced through the Affiliate in respect of any liabilities for which the Member has cover and, in the case of Defence cover, to costs incurred in resisting claims which, if brought against the Member, would be within his cover, and nothing herein contained shall be construed as entitling an Affiliate to recover any amount which would not have been recoverable from the Association by the Member had the claim been made or enforced against the Member.

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7. To the extent that the Association has indemnified a co-assured (other than a Co-assured in the categories referred to in Rules 78.3 and 78.4) or an Affiliate in respect of a claim, it shall not be under any further liability and shall not make any further payment to any person whatsoever, including the Member, in respect of that claim or of the loss or damage in respect of which that claim was brought.

## **2 Rule 79. Joint Members, Co-assureds and Affiliates**

1. Joint Members and Co-assureds insured on any one entry shall be jointly and severally liable for all sums due to the Association in respect of such entry.
2. Any payment by the Association to one of the Joint Members, Co-assureds or Affiliates shall fully discharge the obligations of the Association in respect of such payment.
3. Any communication by the Association to one Joint Member or Co-assured shall be deemed to be communication to all.
4. The conduct or omission of one Joint Member or Co-assured which under these Rules would constitute a breach of the contract of insurance, shall be deemed as the conduct or omission of all the Joint Members and Co-assureds.

3 A time or voyage charterer cannot be a joint Member because of the definition of "charterer's entry" under Rule 1. However, bareboat or demise charterers are not considered charterers for the purpose of the Rules so they may be joint Members.

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