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## Court expunges yacht mortgage and awards clear title to third-party purchaser

*Branch Banking & Trust Co. of Va. v. M/Y Beowulf*, 2012 WL 2064570 (S.D. Fla. June 7, 2012)

Citing irregularities in the loan papers and a bank's improvident decision to grant a workout to an insolvent borrower, the federal district court in Miami has awarded clear title to a third party who purchased a yacht without notice of the bank's mortgage.

The yacht was a custom sportfisherman built by Sculley Boatbuilders, Inc. and used as security for a personal loan to James Sculley, the president of Sculley Boatbuilders. The mortgage identified Mr. Sculley as the owner of the yacht, but the note and other loan documents identified Sculley Boatbuilders as the owner. As a further complication, the hull identification number was not affixed to the yacht. The bank was made aware of this through a marine survey report that it received before funding the loan.

Shortly after the mortgage was recorded by the Coast Guard, Sculley Boatbuilders assigned a different hull identification number to the yacht, obtained a different official number from the Coast Guard, and sold the yacht to a third party, all without notifying the bank. The issuance of the second identification number and official number resulted in two chains of title, so that when the yacht was later sold again, the chain of title did not reflect the mortgage recorded under the first hull identification number.

Several years later, Mr. Sculley defaulted on the loan. Although he was saddled with other delinquencies, the bank agreed to modify the loan. As part of the modification, the bank corrected the loan documents to show the owner of the yacht as Sculley Boatbuilders. But the bank did not correct the mortgage on record with the Coast Guard, nor did the bank demand to see the yacht or insist on proof of insurance as a condition of the workout.

Mr. Sculley died about a year later, the modified loan went into default, and the bank filed a foreclosure action in federal court. The yacht's current owner, who had purchased it without knowledge of the mortgage, contested the foreclosure and argued that the mortgage was invalid and should in any event be equitably subordinated. The bank moved for summary judgment, but the court denied that motion (as reported in Boating Briefs Vol. 21:1) and ordered a trial on the merits.

The first issue was whether Mr. Sculley owned the yacht when he granted the mortgage in his own name. Observing that the question of vessel ownership is a matter of state law, the court applied Florida law and found that the bank had not established Mr. Sculley's ownership of the yacht. Although Sculley Boatbuilders had issued a builder's certificate naming Mr. Sculley as the person for whom the yacht was built and the mortgage itself identified Mr. Sculley as the "sole owner," Mr. Sculley's status as owner was contradicted by all the other loan documents, which named Sculley Boatbuilders as the owner. In these circumstances, the court held that the bank could not properly rely on the builder's certificate as conclusive evidence of

*This newsletter summarizes the latest cases and other legal developments affecting the recreational-boating industry. Articles, case summaries, suggestions for topics, and requests to be added to the mailing list are welcome and should be addressed to the editor.*

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title. Given the discrepancies in the loan documents, the bank had not carried its burden of proving that Mr. Sculley owned the yacht when he granted the mortgage. Accordingly, the mortgage was invalid.

The court went on to consider whether the bank's actions—both in granting the loan and in later agreeing to the modification—warranted equitable subordination. The court found that the bank, having received at the outset a copy of a survey report noting the absence of the hull identification number, was grossly negligent by not insisting that the hull identification number be affixed to the yacht. Then, according to the court, the bank again acted unreasonably by granting a loan modification to a deeply insolvent borrower without inspecting the yacht or taking other steps to protect its interest in the collateral, all to the detriment of the subsequent purchaser. Therefore, even if it were valid, the bank's mortgage would be equitably subordinated to the subsequent purchaser's interest.

The bank has appealed this decision to the Eleventh Circuit. ■

### Mortgage lien perfected despite mortgagee misnomer

*In re Sherman*, 2012 WL 2132379 (D. Conn. Bankr. June 12, 2012)

A couple obtained a boat loan from Commerce Bank. In preparing the mortgage papers for signature, the documentation service hired by the bank mistakenly listed the mortgagee's name as "Commerce Bank/Shore, N.A.," an entity that had ceased to exist two years earlier as a result of a merger into Commerce Bank, N.A.

The borrowers later defaulted on their loan payments and filed a Chapter 7 bankruptcy petition. TD Bank, as successor to Commerce Bank, moved for relief from a bankruptcy stay, claiming it had a perfected security interest and should be permitted to exercise its rights as to the boat. The bankruptcy trustee objected, arguing that TD Bank's lien was not perfected because the mortgage did not show the mortgagee's correct name.

Rejecting the trustee's argument, the bankruptcy court held that a mortgage lien is perfected so long as the mortgage is filed in "substantial compliance" with the federal Commercial Instruments and Maritime Liens Act. Here, the error in the mortgagee's name did not render the mortgage lien unperfected. While "Commerce Bank/Shore, N.A." did not exist as a legal entity when the mortgage was signed, the actual mortgagee (Commerce Bank, N.A) did exist and its name was similar to that shown on the mortgage. Moreover, the mortgagee address printed on the mortgage was in fact a place of business occupied by Commerce Bank, N.A. In the circumstances, the mortgage provided sufficient notice of the mortgagee's identity, the mortgage lien was perfected, and TD Bank's motion for relief was granted. ■

### Low price did not make sale of repossessed yacht commercially unreasonable

*Provident Bank v. Bonnici*, 2012 WL 2283458 (N.J. App. Div. June 19, 2012) (unpublished)

In 2007 a man purchased a yacht partly with borrowed funds, signing a 20-year note and security agreement. Within one year, he defaulted on the loan payments. Following an unsuccessful attempt to sell the yacht himself, he surrendered the yacht to the bank. Having reviewed the results of a marine survey and consulted the National Automobile Dealers Association (NADA) valuation guide, a liquidator hired by the bank set the asking price at $95,000. Three offers and nine months later, the liquidator sold the yacht for $57,500—nearly $150,000 less than the borrower's original purchase price.

In response to the bank's suit for the loan deficiency, the borrower contended that the disparity between his purchase price and the price obtained by the liquidator rendered the sale commercially unreasonable and that a deficiency claim was therefore barred. According to the borrower, the liquidator also disregarded the yacht's customized features and relied too heavily on the NADA guide in setting the asking price.

The trial court granted summary judgment for the bank, ruling that the disposition of the yacht was commercially reasonable despite the seemingly low sale price. The borrower appealed.

According to the appellate court, a low sale price does not necessarily render a repossession sale

commercially unreasonable under New Jersey law. Here, the bank hired a liquidator in the business of selling repossessed boats; the liquidator set the asking price based on the condition of the yacht and the NADA valuation guide; and the liquidator passed all offers along to the bank, which made appropriate counteroffers in an attempt to obtain a higher sale price. According to the appellate court, "[t]he rejection of those counteroffers, and the fact that the handful of offers received approximated the price eventually obtained, demonstrates that the price for which the boat was sold was generated in a commercially reasonable manner." ■

# Insurance

### Owner's failure to disclose prior casualty voids policy

*St. Paul Fire and Marine Ins. Co. v. Matrix Posh, LLC*, 2012 WL 1530926 (E.D.N.Y. Apr. 30, 2012)

A yacht owner submitted a claim to his insurer, St. Paul, after the yacht allided with a submerged object in Long Island Sound. St. Paul brought an action for declaratory relief and moved for summary judgment on the basis that the policy was void due to misrepresentations and nondisclosures by the insured in the insurance application. In particular, St. Paul cited the insured's failure to disclose a prior incident in which an unmoored sailboat had drifted into the yacht—an incident which caused tens of thousands of dollars in damages to the yacht and which itself gave rise to an insurance claim.

The court held that, as a matter of law, the insured was obligated to disclose this prior incident to St. Paul. The prior incident had produced a crack in the yacht's hull, caused water ingress, and led the captain to put into port for what he described as "emergency" repairs. Moreover, St. Paul's insurance application specifically asked the insured to list any prior "insurance losses," yet the insured did not identify any such losses. The policy was therefore void at inception. ■

### In declaratory-judgment action, E.D.N.Y. denies jury trial on insured's counterclaims

*Markel American Ins. Co. v. Linhart*, 2012 WL 2930207 (E.D.N.Y. July 11, 2012)

Linhart, shortly after leaving the dock on his yacht, heard a loud bang and the yacht began taking on water. He submitted a claim to Markel for payment of the repair costs. After an investigation, Markel concluded that the incident was caused by a deteriorated shaft coupler and that the loss resulted from "wear and tear," "gradual deterioration," and "failure to maintain the insured vessel," which the policy excluded from coverage.

Markel filed a declaratory-judgment action in admiralty. Linhart counterclaimed for breach of contract and bad faith, sought punitive damages, and demanded a jury trial. Markel moved to dismiss the counterclaim for bad faith and to strike the jury demand.

The counterclaim alleged that Markel "'engaged in wrongful conduct and handling of his claim,' which was 'of morally reprehensible or wantonly dishonest nature.'" The court dismissed this counterclaim as conclusory and implausible. Markel had denied Linhart's claim after an investigation, and Linhart alleged no facts to suggest that the denial was in bad faith or that the investigation was improperly conducted.

Markel also moved to strike Linhart's demand for a jury trial on the surviving counterclaims. The court noted that the New York courts are split on the "issue of whether a defendant is entitled to a jury trial on a non-admiralty cause of action that is asserted as a counterclaim." In this case, the court decided that Linhart was not entitled to a jury trial given that his counterclaims and Markel's complaint implicated the same issues. A jury trial on the counterclaims would, in the court's view, "be wasteful, duplicative, and risk inconsistent results." ■

### Pollution exclusion bars coverage for carbon-monoxide poisoning

*Scottsdale Ins. Co. v. Pursley*, 2012 U.S. App. LEXIS 17437 (11th Cir. Aug. 20, 2012) (unpublished)

A boat mechanic allegedly failed to properly seal an engine exhaust system, which allowed carbon monoxide to enter the vessel's cabin, where it fatally

poisoned the vessel owner. The owner's widow sued the mechanic, whose Commercial General Liability insurer denied coverage and sought declaratory relief on the basis of the policy's pollution exclusion. The trial court ruled for the insurer, and the widow appealed to the Eleventh Circuit.

The pollution exclusion precluded coverage for "'[b]odily injury' or 'property damage' which would not have occurred in whole or part but for the actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape of 'pollutants' at any time." The policy defined the word "pollutants" as "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste."

Citing the Georgia Supreme Court's ruling in *Reed v. Auto-Owners Insurance Co.*, 667 S.E.2d 90 (Ga. 2008), which applied a similar exclusion when a tenant was poisoned by carbon monoxide and sued the landlord, the Eleventh Circuit held that the CGL policy's pollution exclusion was indeed broad enough to preclude coverage. This was so even though carbon monoxide might not be thought of as pollution in the traditional sense.

Alternatively, the widow attempted to rely on the policy's property-damage coverage, claiming that the death of her husband had diminished the value of the boat. The policy defined "property damage" as "[p]hysical injury to tangible property, including all resulting loss of use of that property. . . . or [l]oss of use of tangible property that is not physically injured." Because the widow alleged neither physical injury to nor loss of use of the boat, her claim for diminished value was not covered either. ■

### Citing Wikipedia, court holds "jet skis" exclusion inapplicable to Honda personal watercraft

*Fire Insurance Exchange v. Oltmanns*, 2012 WL 3510440 (Utah App. Aug. 16, 2012)

A homeowner's insurance policy excluded coverage for liability resulting from the use or ownership of "jet skis." The insured, while operating a Honda AquaTrax personal watercraft on a lake in southern Utah, was involved in an accident, and his passenger filed a lawsuit against him. Relying on the "jet skis" exclusion, the insurer argued that it had no duty to defend or indemnify the insured. The trial court agreed and granted summary judgment to the insurer.

The appellate court reversed, ruling that the term "jet skis" was ambiguous because it could reasonably be seen as a reference to a particular brand of personal watercraft manufactured by Kawasaki (which held the trademark on the term "Jet Ski"), rather than a general reference to all kinds of personal watercraft. Although the insurer probably did not intend to exclude coverage only as to Kawasaki brand "Jet Ski" models, someone reading the policy could reasonably interpret the term "jet skis" as encompassing only Kawasaki models. As support for this conclusion, the court turned to what it described as "that great repository of contemporary wisdom, Wikipedia," which, as of the time of the court's decision, had the following entry under "Jet Ski":

> Jet Ski is the brand name of a personal watercraft manufactured by Kawasaki Heavy Industries. The name is sometimes mistakenly used by those unfamiliar with the personal watercraft industry to refer to any type of personal watercraft; however, the name is a valid trademark registered with the United States Patent and Trademark Office, and in many other countries. The term "Jet Ski" (or JetSki, often shortened to "Ski") is often misapplied to all personal watercraft with pivoting handlepoles manipulated by a standing rider; these are properly known as Stand-up PWCs. The term is often mistakenly used when referring to WaveRunners, but WaveRunner is actually the name of the Yamaha line of sit-down PWCs, whereas "Jet Ski" refers to the Kawasaki line.

Because the term "jet skis" did not clearly encompass a Honda personal watercraft, the court held that the insurer could not rely on the exclusion to deny coverage.

Readers may be interested to know that Wikipedia's "jet ski" page was changed after this court's decision. The entry now (or at least as of November 20, 2012) states that "the term 'jet ski' is a popular term synonymous with 'personal watercraft.'" ■

# Salvage

### Contributing to successful salvage merits an award, even if salvor did not directly improve vessel's physical condition

*Esoteric, LLC v. M/V Star One*, 2012 WL 2105611 (11th Cir. June 12, 2012) (unpublished)

While underway near the Bahamas, the yacht *Esoteric* received an emergency report about a sinking vessel. The *Esoteric* arrived on the scene to find a large and mostly submerged yacht, the *Star One*. The captain of the *Esoteric* assessed the situation and determined that the *Star One* was a navigational hazard and was at risk of drifting into nearby coral reefs.

The *Esoteric* towed the *Star One* to the closest port, where Bahamian officials ordered the *Star One* to be anchored just outside the harbor entrance. The *Star One*'s insurer then arranged for a professional salvage company to pump the vessel dry and tow it to Miami, for which the insurer paid $93,000. A second salvage company was paid $2,800 to tow it to a boatyard. The *Esoteric*'s owner filed suit, seeking a salvage award from the *Star One* and its owner.

To succeed on a claim for pure salvage, a salvor must show that: (1) a marine peril existed, (2) the service was rendered voluntarily and not as part of an existing duty or contract, and (3) the service contributed to, or resulted in, the success of the salvage operation.

The district court found in favor of the *Esoteric* and rendered a salvage award of about $68,000, or 12 percent of the post-salvage value as determined by the court. Finding that the *Star One*'s defense to the salvage claim was frivolous, the court also ordered the *Star One* to pay about $73,000 toward the *Esoteric*'s legal fees.

The *Star One* appealed, arguing that the element of success was missing inasmuch as the *Esoteric* had simply moved the vessel to a new location and made no improvement to the vessel's physical condition. The *Star One* also challenged the award of legal fees.

Noting that the *Star One* was in a well-traveled sea lane where the water was more than 6,000 feet deep and that the vessel was drifting toward a stretch of coral reefs—and that the *Esoteric*'s efforts had brought the vessel to a location where professional salvors could complete the salvage process—the Eleventh Circuit affirmed the salvage award. The law of pure salvage requires that a salvor contribute to a successful salvage operation, not necessarily that it complete the operation entirely by itself.

The *Star One* also appealed the district court's award of legal fees to the *Esoteric*. The trial court had viewed as frivolous the *Star One*'s argument that a salvage claim requires proof of some physical improvement to the vessel. But the appellate court disagreed, finding that the *Star One*'s argument was reasonable, albeit ultimately unsuccessful. Accordingly, there was no basis to award legal fees. ■

### Boat owner with no defense to salvage claim ordered to pay salvor's legal fees

*Reliable Salvage and Towing, Inc., v. Bivona*, 2012 WL 1867166 (11th Cir. May 23, 2012) (unpublished)

On a calm Easter Sunday, a 35-foot Sea Ray ran into a shoal in Gasparilla Pass, near Boca Grande, Florida. Although neither the owner nor his boat was in immediate danger, a storm was expected that night and the following day. It would be several days before the tide was high enough for the boat to move under its own power.

The owner contacted a towing and salvage company, which used three vessels to free the boat from the strand. Before the operation began, the boat owner signed a form of contract as presented by the salvor, but the contract did not specify the rate that would be charged for the service.

After the operation was complete, the salvor sent a $7,500 invoice to the boat owner's insurer. But the owner's insurance policy had lapsed, and the insurer declined to pay the salvage bill. The owner did not pay the bill himself.

The salvor eventually filed suit against the Sea Ray and its owner, asserting claims for both contract salvage and pure salvage. After a bench trial, the district court dismissed the contract claim because the form of contract signed by the owner lacked material terms.

With respect to the claim for pure salvage, the Sea Ray owner argued that there was no marine peril because the weather was calm when the service was rendered. But the district court determined that the

coming storm was indeed a marine peril sufficient to support a salvage award. After evaluating the efforts and resources used in the salvage operation, the district court granted a salvage award of $14,000, nearly twice the salvor's original bill.

Moreover, based on the owner's concession at trial that the salvor had provided a service and was entitled to payment, the trial court concluded that the owner's defense to the pure-salvage claim was frivolous. Accordingly, the court awarded the salvor its legal fees and costs, which exceeded $36,500. (We reported on the trial court's decision in Boating Briefs Vol. 20:1.)

On appeal, the owner argued that his successful defense to the contract claim barred any award of legal fees. The Eleventh Circuit was not persuaded. It ruled that a meritorious defense to one claim does not mean that a defense to another claim cannot itself be frivolous. The trial court's award of fees was therefore affirmed. ■

### Landlocked lake entirely within one state is not a navigable waterway; hence no admiralty jurisdiction over salvage claim

*MacGowan v. Cox*, 2012 WL 3892645 (5th Cir. Sept. 7, 2012) (unpublished)

A canoeist discovered an unmanned personal watercraft adrift on Lake LBJ near Austin, Texas. He towed the craft to shore and later filed an admiralty action against its owner, seeking a salvage award of $3,000, half the craft's value. The district court dismissed the action for lack of subject-matter jurisdiction, and the would-be salvor appealed.

Due to its location in the middle of Texas, and with dams blocking passage at each end, the lake afforded no possibility of interstate travel. The lake was therefore not navigable for purposes of admiralty jurisdiction, and the Fifth Circuit affirmed the district court's dismissal order. ■

# Substitute Custodianship

### Court disallows fee to custodian who neglected vessel

*Horizon Shipbuilding, Inc. v. Blyn II Holding, LLC*, 2012 WL 2911918 (S.D. Tex. July 16, 2012)

A group of businessmen purchased a dilapidated 131-foot crewboat for $680,000 with the intent of converting it into a luxury yacht. They hired a naval architect to manage the project and signed a time-and-materials contract with an Alabama shipyard to carry out the conversion. Based on some preliminary specifications and drawings, the cost of the conversion was estimated at $4.5 million.

The architect's designs were not completed on time, which substantially delayed the project. Once the drawings were finally done, the shipyard reevaluated the project and informed the owners that the estimated cost of the project was now $9.4 million. The owners stopped paying the shipyard's invoices and issued a stop-work order.

The shipyard sued the owners and the vessel, seeking $1.15 million for the value of the work already done. The shipyard had the vessel arrested and was appointed as the substitute custodian. (As reported in Boating Briefs Vol. 19:1, the case came before the Eleventh Circuit, which held that, despite the extensive conversion, the craft remained a vessel subject to a maritime lien.) Later, the vessel owners entered bankruptcy.

Meanwhile, the shipyard was working on other projects and needed to use the drydock. So the shipyard launched the still-unfinished vessel into the water. Over the course of several months, water and moisture entered the vessel, various components became moldy or rusty, and the hull became fouled with barnacles. The owners then sued the shipyard in the bankruptcy court to recover for this damage.

The bankruptcy court determined that the shipyard's $1.15 million claim for the conversion work was well supported. But the bankruptcy court also held that the shipyard's poor performance as substitute custodian had caused $1 million in damages to the vessel. As a result, payment on the conversion work was almost entirely offset by the damage allegedly sustained during the custodianship. The

bankruptcy court also denied the shipyard's request for custodial fees.

The shipyard appealed this decision to the federal district court, which observed that the duty of a substitute custodian is "to keep the property in a safe and secure manner, so as to protect it from injuries so that its value to the parties will not be impaired by unnecessary deterioration or damage." While a custodian is not charged with preventing normal wear and tear or depreciation, and is generally not required to make improvements, the district court agreed with the bankruptcy court that leaving the vessel in the water without adequate protection was indeed a breach of the custodian's duty of care.

Next, the district court evaluated the bankruptcy court's conclusion that the shipyard's neglect caused $1 million in damages to the vessel. The district court noted that the owners had the burden of quantifying the damages. The bankruptcy court had based its finding on a "cost of repair" evaluation method, or in other words, by determining how much it would cost to return the vessel to the state it was in before it was launched into the water. However, that method did not account for the fact that the vessel would have experienced some degree of wear and tear in any event. Based on the evidence available, the district court found that the true damages to the vessel were just over $100,000.

Finally, the district court noted that the bankruptcy court's denial of custodia legis expenses could be reversed only for abuse of discretion. Given the shipyard's failure to take proper care of the vessel, the bankruptcy court did not abuse its discretion in declining to award the shipyard a custodial fee. ■

# Limitation of Liability

### Court grants limitation for sinking in extreme weather

*In re Anderson*, 2012 WL 1301162 (W.D. Wash. April 16, 2012)

A man purchased a catamaran from a builder in South Africa. The purchase price included delivery from South Africa to Port Townsend, Washington. Although the purchaser took title to the vessel when it departed South Africa, the delivery crew was employed by a third-party service. After several unplanned crew changes along the way, and when less than 10 miles off the Oregon coast, the vessel sank in 100 mile-per-hour winds with the loss of all three crewmembers.

One crewmember's widow sued the vessel owner, who filed a limitation action. The widow asserted claims under the Jones Act and the Death on the High Seas Act (DOHSA).

First, the court held that the Jones Act claim could not proceed because the vessel owner did not employ the crew. The yacht-delivery service had hired all of the crewmembers, paid them, and instructed them on the route to take and when and where to sail. The vessel owner had no contact with the crewmembers at all, and before the casualty did not even know their identities. As such, the owner was not an employer and therefore could have no Jones Act liability.

Second, the court held that the widow's claims for nonpecuniary losses and for punitive damages had to be dismissed, since such claims are unavailable under DOHSA.

Finally, the court considered whether the vessel owner was entitled to limit liability. Although the widow alleged various problems with the vessel, ranging from nonfunctional or missing items, to negligent navigation, to negligent selection of the master, there were no facts to indicate that any of these alleged problems actually caused the death of her husband. In the court's words, "the cause for the tragic events that underlie this case was a sudden 100-mile-per-hour-wind storm off the coast of Oregon—'an Act of God or peril of the sea.'" Any liability on the part of the owner was therefore limited to the vessel's value at the end of the voyage, presumably zero. ■

### Contribution claims against owner preclude return to state court

*In re Linton*, 2012 WL 2367604 (S.D. Miss. June 21, 2012)

Courtney Davis and Richard Allen Linton were travelling on Linton's 2000 Seafox when both were thrown from the vessel, which then began spinning rapidly in circles, striking Davis and Linton. Linton was killed, and Davis's leg was amputated.

Davis sued Linton's estate in Mississippi state court, and also asserted product-liability claims against the manufacturers, designers, assemblers, installers, distributors, and sellers of the vessel.

Two months later, Linton's estate filed a limitation action in federal court, claiming that the estate's liability should be capped at $7,000, the value of the vessel. The filing of the limitation action had the effect of staying the state-court litigation.

Davis stipulated that the federal court had exclusive jurisdiction over the limitation action and that she would not seek to enforce any damage award in the state court greater than the value of the vessel. On this basis, she sought to lift the limitation court's injunction so that she could resume her state-court action. Meanwhile, the product defendants appeared in the limitation action and filed indemnity and contribution claims against the Linton estate. The product defendants did not join in Davis's stipulation.

In ruling on Davis's motion, the court noted that there are two instances in which a state-court action should be allowed to proceed after a limitation action is filed: (1) when the total amount of claims does not exceed the value of the vessel or (2) when all claimants stipulate that the federal court has exclusive jurisdiction over the limitation proceeding and that the claimants will not seek to enforce any state-court judgment greater than the value of the vessel. Davis relied on Eleventh Circuit case law holding that state-court litigation may proceed even if the vessel owner is subject to contribution claims by parties who have not joined in the stipulation. But the court was unable to locate any Fifth Circuit cases endorsing that view and, given the pending claims for contribution, declined to allow Davis to resume her state-court action. ■

### Alleged negligence by a beneficial owner insufficient to deny limitation categorically, but state-court litigation will proceed first

*Sailing Shipps Ltd. v. Alconcel* 2012 WL 2884861 (D. Hawaii July 12, 2012)

During a ride on a Zodiac boat, Jason Alconcel fell into the water and was injured by the propeller. The Zodiac was being driven by Chimo Shipp, allegedly an employee and one-sixth owner of Sailing Shipps Ltd., the entity that owned the Zodiac. Alconcel sued Shipps in Hawaii state court, claiming that Shipps was liable for Chimo's allegedly negligent operation of the vessel. Shipps then filed a limitation action in Hawaii federal court, which issued the customary injunction restraining further proceedings in state court.

The Limitation of Liability Act permits a vessel owner to limit its liability to the value of the vessel if the owner had no knowledge of the negligence that caused the injuries and if the owner was not in privity with the actor who caused the injuries.

Alconcel moved for summary judgment, arguing that because he was injured due to the negligence of a part-owner of the company, the company necessarily had knowledge of that negligence such that the company could not possibly limit its liability. Alternatively, Alconcel asked that the state-court action be allowed to proceed, with the limitation action to be revisited if necessary after the state-court action ended.

The federal court first ruled that summary judgment was not appropriate on the question of the owner's right to limitation. Limitation issues are normally not decided until after the underlying liability has been established, and it was conceivable that Shipps could limit its liability even if Chimo were found to be negligent. In that regard, the court reviewed a series of cases holding that when a shareholder's negligence causes an injury, the corporation may be deemed to have knowledge of the negligence or be in privity with the negligent shareholder but only if the shareholder was a managing officer or a supervisory employee. Here, the record did not show that Chimo was a managing officer or supervisor. Therefore, the court could not presume that Shipps had knowledge of Chimo's alleged negligence or was in privity with him.

However, the court did agree to dissolve the injunction and allow the state-court action to continue. The court noted that it had discretion to dissolve the injunction so long as Shipps' right to pursue limitation was protected. Because only one person (Alconcel) was suing Shipps, the case would be relatively uncomplicated, and the court could dissolve the injunction so long as Alconcel stipu-

lated to three things: (1) that the value of the limitation fund would equal the value of vessel, (2) that Alconcel would waive any contention that a judgment in the underlying case prevented limitation of liability, and (3) that the federal court retained exclusive jurisdiction to determine limitation of liability.

Because Alconcel stipulated to these things, and because Shipps did not show that the limitation action would be somehow impaired by allowing Alconcel to proceed in state court, the federal court decided to dissolve the injunction. Shipps did argue that the evidence would overlap in the two cases and that this would invade the province of the federal court. But the court observed that in the state litigation Alconcel would be attempting to prove that Chimo was an employee of Shipps, but in the federal court case Alconcel would either have to impute to Shipps knowledge of Chimo's negligence or show privity between Chimo and the company. The court viewed these as very different questions and rejected Shipps' argument.

Shipps also asserted that the state-court case would create excessive delay and expense, but the court noted that these considerations did not outweigh Alconcel's right to pursue his claim in state court, as enshrined in the Saving to Suitors clause.

Accordingly, Alconcel would be permitted to pursue his claim in state court and the limitation action would be dismissed, but with leave to reopen after state-court case ended. ■

# Torts

### Coast Guard has no duty to search for overdue boaters

*Turner v. United States*, 2012 AMC 1607 (E.D.N.C. 2012)

A married couple got underway on their 25-foot boat after informing a relative of their intended itinerary. Late that evening, when the couple did not return as expected and could not be reached on their cell phones, the relative called 911, who in turn contacted the Coast Guard. Due to a shortage of assets in the area and a lack of specific information about the boat's possible location, the Coast Guard did not initiate an active search. A Coast Guard helicopter on its way back to refuel did keep a lookout for the boat but observed nothing unusual.

The next morning a family friend located the boat with no one on board. The wife washed ashore, alive, shortly thereafter. The husband's body was found dead two days later.

The wife sued the United States under the Suits in Admiralty Act, which waives the federal government's sovereign immunity in situations where the government, if it were a private actor, would be subject to liability for maritime negligence. But the government retains immunity from claims based on the exercise or performance of discretionary functions.

Although the Coast Guard is empowered by law to conduct search and rescue missions, it is not required to do so. Because the Coast Guard had discretion to conduct or not to conduct a search on the night the boat went missing, the court lacked subject-matter jurisdiction to pass on the reasonableness of the Coast Guard's conduct. The case was therefore dismissed. ■

### Court enforces indemnification agreement in boat-rental contract

*In re Aramark Sports & Entm't Servs., LLC*, 2012 U.S. Dist. LEXIS 123786 (D. Utah Aug. 29, 2012)

Before renting a powerboat for a trip on Lake Powell, a customer signed a rental contract with an indemnification clause requiring him to "indemnify and hold harmless [the rental company] from and against any claims, suits, penalties, obligations, costs and expenses (including reasonable attorney's fees), including claims by Customer or by third parties (which may include members of Customer's party) . . . resulting or arising from Customer's use of the [boat]." The five other people who were also to make the trip did not sign the contract, nor was there any evidence that they read it or were aware of its terms.

The next day, as the party of six was returning from their outing on the lake, the boat suddenly took on water and sank. Four people died, including the customer who signed the contract.

Based on the rental contract, the rental company argued that it was entitled to full indemnification

from the customer's estate in connection with the claims arising from the sinking. The death claimants countered that the indemnification clause was unenforceable.

Because Lake Powell was a navigable waterway, and in light of case law holding that recreational boating bears a substantial relationship to traditional maritime activity, the court ruled that the enforceability of the indemnification clause would be decided according to general maritime law.

Under maritime law, indemnity and exculpatory clauses are generally enforceable if they are (1) clear and unambiguous, (2) consistent with public policy, and (3) not part of a contract of adhesion or the product of overreaching, a monopoly, or significantly unequal bargaining power. Here, the claimants did not allege overreaching or a monopoly, and although the customer may not have been free to reject the indemnification clause, he was free—given the recreational nature of the activity—not to enter into the contract at all.

The main issue was whether the indemnification clause was clear enough to inform the customer that he was absolving the company of any liability for its own negligence. The claimants contended that the clause did not unambiguously relieve the company of such liability because the clause did not use the word "negligence," "fault," or the equivalent. But under maritime case law, an exculpatory clause does not need to use the term "negligence" to be clear and unambiguous. The phrase "all claims" had been previously held to include negligence claims, and it followed that the phrase "any claims" should likewise include any negligence claims against the rental company. Also, if "any claims" in the context of the indemnification provision did not include the company's own negligence, then in the court's view the provision would have had no real effect: unless it was negligent, the company would have no liability from which to be indemnified.

A related issue was whether the clause violated public policy. The court noted that prior cases distinguished between ordinary and gross negligence, with most cases holding that a party may contractually absolve itself from liability for negligence but not from liability for gross negligence. Enforcing the indemnification clause here would therefore be consistent with public policy, unless the rental company was ultimately proven to have been grossly negligent.

The upshot was that the estate of the customer who signed the contract could not proceed with a negligence claim against the company. The other claimants, however, could proceed with their claims, which the company would have to defend and resolve before seeking indemnification from the customer's estate. ■

### Injury turns sea trial into very expensive test drive

*Hines v. Triad Marine Center, Inc.*, 2012 WL 2688800 (4th Cir. July 9, 2012) (unpublished)

The Fourth Circuit Court of Appeals has upheld a judgment against a boat dealer in a suit brought by a doctor injured during a sea trial.

The plaintiff, a urologist, was boat shopping at the defendant's dealership. The defendant recommended a Triton model 2286. Despite a National Weather Service small-craft warning, a salesman took the plaintiff and a guest out for a sea trial. The plaintiff operated the vessel for a time but then turned over the controls to the salesman.

The salesman steered the boat into the oncoming waves and struck a wave head-on. The plaintiff bumped his head on the overhead and fell to the deck, fracturing one ankle and spraining the other. He underwent surgery for the broken ankle and suffered from residual pain, which required the use an opioid pain reliever. The medication caused cognitive impairment, which led the plaintiff to quit the practice of medicine. The plaintiff sued the dealership in admiralty.

After a bench trial, the court entered a $10.3 million judgment for the plaintiff. The court found that the salesman (a dealership employee) was negligent, and that the plaintiff's injury, resulting pain, and medication prevented him from working as a doctor. The court also awarded prejudgment interest at North Carolina's statutory rate of eight percent.

The dealership appealed, challenging the court's findings as to breach of the standard of care, the extent of plaintiff's damages, the admissibility of plaintiff's disability income, and the use of the state

prejudgment interest rate. The Fourth Circuit affirmed in all respects.

*Breach of Duty*

First, the defendant argued that the trial court erred in concluding that the salesman violated the standard of care. The plaintiff's expert had opined that the salesman was negligent by operating the boat too fast and by steering straight into an oncoming wave. The plaintiff's expert did concede, however, that had the plaintiff not been injured, his opinion of the operator's conduct may well have been different. Nevertheless, the Fourth Circuit decided that the expert's testimony, when combined with the other evidence, was sufficient to support a finding of negligence.

*Damages*

Next, the defendant argued that the trial court erred in its determination of damages. The trial court found that the plaintiff had a 20% permanent impairment in his ankle and that the pain would probably endure for the rest of his life. Although the defendant presented contrary expert testimony, the Fourth Circuit concluded that the trial court was within its discretion to give more weight to the plaintiff's expert. The Fourth Circuit also declined to reverse based on video surveillance footage, which seemed to show that the plaintiff was less than "totally disabled." Reversing on that ground would have amounted to re-weighing the evidence, which was not the appellate court's function.

As to damages for future injuries, the defendant argued that the award for future pain and suffering was not based on sufficient medical evidence and was excessive to the point of being punitive. The Fourth Circuit disagreed. After pointing out the evidence supporting the finding, it noted the district court had "great latitude" in assessing the amount.

The defendant also argued the plaintiff failed to mitigate his damages since he could have lost weight and used his cane in a different manner, which could have reduced his pain, which could have in turn obviated the need for the opioid that caused his cognitive impairment, which in turn caused him to quit his practice. The court dismissed this argument as "purely speculative."

*Admissibility of Plaintiff's Disability Payments*

Next, the defendant argued that it should have been able to cross-examine the plaintiff about his receipt of disability income. The defendant offered the evidence to "challenge his credibility, rather than to show that he was receiving income from other sources." The trial court permitted examination about the contents of plaintiff's applications for disability, but not the amounts the plaintiff was drawing, reasoning that evidence of such "collateral source payments" was inadmissible. The Fourth Circuit found no abuse of discretion in this decision.

*Prejudgment Interest*

Lastly, the defendant argued that the district court abused its discretion in awarding prejudgment interest at the North Carolina statutory interest rate of 8% rather than at the prevailing market rate. The Fourth Circuit noted that when "setting the proper rate of prejudgment interest, admiralty courts have broad discretion and may look to state law or other reasonable guideposts indicating a fair level of compensation." The district court had therefore not abused its discretion by using the North Carolina interest statute. ■

# Warranty

### *East River* no bar to owner's negligence claim against engine repairer

*Aviva, Ltd. v. Carter Machinery Co, Inc.*, 2012 WL 1970228 (W.D. Va. May 31, 2012)

The owner of the 153-foot yacht *Charade* paid an engine repairer $15,000 to overhaul the yacht's generator engines. Claiming that the workmanship was faulty, the owner sued the repairer for negligence and breach of contract. Among the alleged damages were travel expenses incurred in making follow-up repairs, the costs of dockage and electricity consumed during those repairs, the cost of replacing lube oil, monitoring costs, and cleaning costs.

The repairer moved to dismiss the negligence claim, arguing it was barred by the economic-loss doctrine as set forth in *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986). In that

case, the Supreme Court held that there is no maritime negligence claim against a product manufacturer, supplier, or installer if the only injury is to the product itself and the loss is purely economic. A plaintiff in that situation is limited to warranty or contract claims.

Here, the district court concluded that *East River* presented no obstacle to the plaintiff's negligence claim because the plaintiff was seeking recovery not for injury to the engines but rather for consequential losses arising from the need to remediate the repairer's allegedly faulty work. Moreover, the repairer had not manufactured or supplied the engines but rather was hired to overhaul them. A claim against the repairer for negligently performing that service therefore did not contravene *East River*. ■

# Regulatory Developments

### Coast Guard proposes changes to Inland Rules of the Road

The U.S. Coast Guard has proposed to amend the Inland Navigation Rules to bring them into greater conformity with the International Rules and to incorporate changes recommended by the Navigation Safety Advisory Council. Among the changes potentially pertinent to recreational vessels:

- A sentence would be added to Rule 1 in order to clarify that the Inland Navigation Rules "have preemptive effect over State or local regulation within the same field."
- Vessels 12 meters or more in length but less than 20 meters in length would no longer be required to carry both a bell and a whistle; a whistle alone would suffice.
- Sailing vessels less than 7 meters in length and vessels under oars would have the option of displaying an all-round white light in lieu of an electric torch or lighted lantern.
- Under Rule 7 (risk of collision), vessels equipped with working radar "and other electronic equipment" would be required to make proper use of that equipment in determining if a risk of collision exists. (The current version of Rule 7 mentions only radar.) The aim of the amendment is to require vessels with automatic identification systems (AIS) to make use of these systems in assessing the risk of collision.

Among the changes the Coast Guard considered but rejected was a proposal to require vessels 16 feet or more in length to carry a copy of the Inland Navigation Rules onboard. (Currently, only self-propelled vessel 12 meters or more in length are required to carry the Rules.) The Coast Guard decided that this proposal would have imposed a high regulatory burden without any quantifiable benefit. ■

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