FBO "HOLD HARMLESS" AGREEMENTS ARE NOT HARMLESS

Over the past several years, corporate general aviation has been confronted with what are commonly referred to as "FBO Hold Harmless Agreements." This type of agreement is designed to alleviate an FBO's responsibility for certain claims arising out of damage to customers' aircraft, including claims for consequential or incidental damages such as loss of use and diminution in value of the aircraft. By signing the agreement, the customer essentially gives up its rights of recovery against the FBO for such damages, regardless of fault.

Understandably, flight crews are faced with a dilemma when presented with these agreements for signature upon arrival at the FBO. Should they sign the agreements, thus waiving some of the aircraft owner or operator's rights of recourse against the FBO? Do they have the authority in the first place to sign them on behalf of the owner or operator? Would signing them present any insurance problems? Should they refuse to sign them and possibly be faced with the payment of higher parking and handling fees or, hopefully in rare cases, a denial of service by the FBO?

An example of these types of agreements is the ground services agreement used by the FBO at one popular winter resort destination, in which the customer agrees to hold harmless the FBO for "any damage incurred or consequential loss involved to the aircraft occurring during snow removal on or around the aircraft or deicing of the aircraft." The customer further agrees to hold harmless the FBO for "consequential loss, diminution of value, loss of use or other incidental loss but not actual physical damage to the aircraft, for other services offered by the FBO, including but not limited to towing or cleaning of the aircraft, lavatory services provided and fueling of the aircraft." Therefore, under the terms of the agreement, the customer has no recourse at all against the FBO for damages, direct or consequential, to the aircraft sustained during snow removal or deicing operations, and has recourse only for direct physical damage to the aircraft arising out of any other operations

Similarly to the agreement discussed above, the agreement used by a large national FBO chain provides that the customer "releases [the FBO] from any damages sustained to the customer's aircraft or other personal property as the result of high winds or other adverse weather conditions." In addition, the customer agrees that "under no circumstances shall [the FBO] be liable to the customer for indirect, incidental, consequential, special or exemplary damages, whether in contract or in tort (including strict liability and negligence), such as, but not limited to, loss of revenue, loss of use or anticipated profits, diminution or loss of value, or costs associated with substitution or replacement aircraft." Thus, as with the agreement discussed above, the customer has given up any right of recourse against the FBO for any damages, direct or consequential, as a result of adverse weather conditions and has waived its right of recovery from the FBO for anything other than direct damage to the aircraft as a result of other causes.

Another popular winter destination resort's service agreement states that, "Owner hereby agrees to indemnify and hold [the FBO] and [the Airport Owner], their respective agents, representatives, officers, directors, servants and employees harmless from and against any and all claims, demands, damages, liabilities, losses, actions or causes of action of any nature whatsoever (including, without limitation, reasonable attorneys' fees) sustained by the Aircraft . . ." Further, "Owner hereby waives its rights of subrogation and shall cause its insurer(s) to waive right of subrogation against [the FBO] and the [Airport Owner]." In addition, "[The FBO] assumes no liability for theft, collision, fire, vandalism or any other type or form of damage to Owner's property or the contents thereof while the same is located on [the FBO's] property." A literal reading of this language is that this FBO will not be responsible for <u>any</u> damage to the aircraft, whether direct or consequential.

These types of agreements arose as an effort to reduce the number and nature of claims against FBOs arising out of damage to aircraft during ground-handling operations. Given the current values of corporate aircraft, repair costs for even relatively minor "hangar rash" can be quite high. Further, depending on the aircraft involved, the reduction in the overall value of the aircraft because it has sustained damage can be a significant amount, even greater than the amount of the repair cost. The size of the claim against the FBO can further increase if the owner/operator has incurred expenses arising from the loss of use of the aircraft while it is being repaired.

While the FBO that uses this type of agreement may be enjoying a reduction in the premium for its insurance coverage, the customer who signs the agreement may be violating its own insurance policy, at least with respect to direct damage to the aircraft. (Most hull coverage will only pay for direct, and not consequential, damage.) It is common for aircraft hull coverage to contain a provision precluding the insured from waiving its rights of recovery against a wrongdoer, and thus the insurer's ability to subrogate against the wrongdoer for any loss it pays. For example, the policy issued by one major aviation insurer contains the following provision, "This insurance is for your benefit alone and not for any other person or organization. . . . [Y]ou promise not to do anything that will take away our right to collect for damages caused by others." An example from another policy is the provision, "In the event of any payment under this policy, the Company shall be subrogated to all the Insured's rights of recovery therefor against any person or organization . . . The Insured shall do nothing to prejudice such rights." Thus, theoretically, an insurer could consider the customer's agreement to waive its rights of recourse against the FBO a violation of a policy that contains such or similar language.

In addition to a potential insurance problem, the line "consequential" or "incidental" damage or loss versus "direct" or "actual" damage or loss can be gray, and is it is not uncommon for there to be significant disagreement over which is the appropriate

category. For example, if the aircraft has a propeller strike and the engine has to be disassembled to check for internal damage, is the cost to disassemble and reassemble the engine "consequential" or "direct" if no internal damage is found? What about the cost of certain internal parts required to be replaced simply because the engine was torn down if no damage was found?

The second hold harmless agreement described above encompasses more than just situations involving damage to the customer's aircraft by requiring that the customer represent that it "currently maintains policies of aircraft and commercial general liability insurance with respect to the aircraft, operations and maintenance, as well as 'all risk' type hull insurance on its aircraft and engines" and stating that, "In the event any third party claim is made against [the FBO], Customer's insurance coverage shall provide primary coverage." One problem with this language is that not all aircraft operators maintain commercial general liability (CGL) coverage. Further, the language implies that the FBO has been added as an additional insured on the customer's aircraft liability and CGL coverages and that those policies will provide primary coverage for the FBO for any claims made by third parties against it. It would be an uncommon situation where an aircraft owner/operator would want to provide liability coverage, either primary or excess, to an FBO to which it has brought its aircraft for service.

In addition, even if the customer wanted to add the FBO as an additional insured to those coverages, that would have to be done before signing the agreement. This is because it is typical for aviation liability policies to specifically exclude persons or entities engaged in the commercial aviation business as additional insureds. Thus, adding an FBO as an insured would involve a special advance request to, and agreement by, the insurer.

This agreement also requires that the customer agree to "indemnify, save and hold harmless" the FBO and the airport "from and against any and all claims, suits damages, fines and penalties including all expenses, reasonable attorneys' fees and costs incidental to the defense of any claims arising out of [the FBO's] acts or omissions . . . except to the extent such claims arise from the negligence or willful misconduct of [the FBO]." Not only is there no reciprocal provision requiring the FBO to indemnify the customer, but the indemnification obligations assumed by the customer may not be covered by its insurance.

Similarly, the third agreement discussed above provides that, "Owner hereby agrees to indemnify and hold [the FBO] and [the Airport Owner], their respective agents, representatives, officers, directors, servants and employees harmless from and against any and all claims, demands, damages, liabilities, losses, actions or causes of action of any nature whatsoever (including, without limitation, reasonable attorneys' fees) . . . arising out of or related to the Aircraft's use of [the Airport] or [the FBO's] property,

facilities or services." This agreement does not even exclude claims that arise from the FBO's negligence or willful misconduct.

Regardless of the desirability to the customer of accepting the provisions discussed above, the flight crew may not have the authority to enter into such agreements. For example, is the pilot an independent contractor with no such authority whatsoever? Does an employee-pilot's authority extend to waiving his or her employer's rights? Even if the pilot does not have authority to sign the agreement, might the customer still be bound by it under an "apparent agency" legal theory?

Another problematic scenario can arise if the customer operates, but does not own, the aircraft. If the customer is the lessee of the aircraft and is obligated under the lease agreement to reimburse the lessor for damage to or diminution in value of the aircraft, has it waived its right to recover such losses from the FBO while still remaining obligated to reimburse the lessor under the lease?

The use of these agreements by an FBO located at a federally-funded airport may constitute a violation of the airport owner's "grant assurances" to the federal government. The Airport and Airway Improvement Act of 1982 (AAIA) provides for the Airport Improvement Program (AIP), under which grants for airport improvement projects for public-use airports are made by the Secretary of Transportation from the Airport and Airways Trust Fund. Under the AAIA, an applicant for a project grant must submit an application containing a number of specific "grant assurances," one of which is that "the airport will be available for public use on reasonable conditions and without unjust discrimination." (Prior to being amended in 1994, the AAIA referred to "fair and reasonable" conditions, and predecessors to the AAIA such as the Airport and Airway Development Act of 1970 and the Federal Airport Act of 1946 contained substantially similar language.) Upon the applicant's acceptance of a grant offer by the government, a project grant agreement is formed, which is binding on the airport owner and the government.

The FAA is responsible for ensuring compliance of the airport owner's obligations under the grant agreements. According to FAA Order 5190.6A – Airport Compliance Requirements, "The owner of any airport developed with Federal grant assistance is required to operate it for the use and benefit of the public and to make it available to all types, kinds and classes of aeronautical activity on fair and reasonable terms and without unjust discrimination. . . . The terms imposed on those who use the airport and its services, including rates and charges, must be fair, reasonable and applied without unjust discrimination, whether by the owner <u>or by a licensee or tenant who has been granted rights to offer services or commodities</u> normally required at the airport." [Emphasis added.]

The Order further states, "The airport owner is obligated to the government to ensure that the facilities of the airport are made available to the public on fair and reasonable terms without unjust discrimination." With respect to services offered to the public, the Order recognizes that, "At most airports the provision of fuel, storage, aircraft service, etc. is best accomplished by a profit motivated private enterprise." However, "It is the responsibility of the airport owner, in negotiating the privilege to offer these services and commodities at the airport to retain sufficient control over the operation to guarantee that the patrons will be treated fairly." [Emphasis added.] According to the Order, the standard grant application requires that the airport owner will incorporate, and enforce, specific language in any contractual agreements into which it enters for the provision to the public of service or commodities essential to the operation of aircraft. The failure to include the required language in such agreements is a violation of the airport owner's grant agreement.

If the FAA determines that an airport owner has violated its grant assurances, the FAA may withhold the release of funds to the owner under a grant already approved and/or withhold approval of any future grant applications from the owner. Obviously, the airport owner that receives federal funds has a strong interest in ensuring that its grant assurances are not violated, whether by itself or those with whom it has contracted to provide services to the public.

When viewed against this background, it appears that an FBO's requirement that its customers sign hold-harmless agreements may very well mean that an airport owner that has received federal funding is violating the assurances incorporated into its grant agreement with the federal government, thus putting future funding in jeopardy. Whether a violation is occurring would depend upon the consistency and uniformity of its requests that the agreement be signed and the action it takes upon a customer's refusal to sign.

For example, it appears to be clear that an FBO is violating a grant assurance by being engaged in prohibited unjust discrimination if it refuses service altogether to a customer that declines to sign the hold harmless form. However, whether an FBO that charges higher service and parking fees to a customer that refuses to sign the form is violating an assurance would be determined on a case-by-case basis, with the test being whether or not those higher fees were "reasonable."

If an FBO is not requesting that all of its customers sign the form (for example, only requiring it of operators of turbine aircraft), it is most likely discriminating. In what is probably the more common situation, if an FBO charges higher fees to one customer that refuses to sign the waiver, but does not charge the higher fees to another customer that refuses to sign, the FBO would arguably be engaging in prohibited discrimination.

An individual citizen may not file a lawsuit against an airport owner for violating its federal grant assurances. As explained above, the FAA is responsible for ensuring

compliance, and an individual who has a grievance against an airport must file a complaint with the FAA under the procedures found in FAR Parts 13 and 16.

So what can an FBO customer which objects to these hold harmless agreements do? One obvious response is for the flight crew to refuse to sign them altogether. At least one major aviation insurance broker recommends that course of action to its clients. Another response is for the pilot (if he or she has the authority) to cross out and initial any provisions considered to be unacceptable before signing the agreement. The former approach is probably preferable, as it should avoid any ambiguity in the customer's intent.

Because the provisions of these FBO "hold harmless" agreements vary, an aircraft owner or operator asked to sign one should review the agreement's specific terms with its attorney and aviation insurance broker. Obviously, it is essential that owners and operators communicate with their flight crews regarding how these issues are to be addressed.