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Don't Overlook Warranties In Hull and P & I Policies

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A warranty in a marine insurance policy is a promise by the insured about something that will be done or something that will not be done. It may also be a promise about a particular condition that exists or will exist, or a condition that does not nor will not exist.

Two Types of Warranties

There are two types of warranties that may be found in hull and P & I policies: implied and express. An implied warranty of seaworthiness is a part of every time hull policy. It means when the coverage attaches, the vessel is fit for its intended purpose under the anticipated conditions. The implied warranty of seaworthiness does not mean the vessel can withstand all conditions. Thereafter, there is a continuing implied warranty that the insured will not knowingly send the insured vessel to sea in an unseaworthy condition.

Hull and P & I policies also frequently contain one or more express warranties. Express warranties might address the areas in which the vessel can operate, the type of operation the vessel can engage in, the particulars of the crew members, the equipment to be aboard the vessel or other factors material to the risk. This article focuses on the express warranties in hull and P & I policies.

The Consequences of a Breach of Warranty Depend on the Applicable Law

As discussed in a prior article, there are several instances in which federal and state law may lead to different results under the same set of facts or under the same contract. The effect of a breach of an express warranty in a hull or P & I policy is another of those instances. Sometimes the breach of a warranty in a hull or P & I policy results in the voiding of the policy. Other times, the breach has no effect on coverage. Whether the policy is void depends on what law applies. How the courts decide what law applies has its origin in the United States Supreme Court case of Wilburn Boat v. Fireman's Fund Ins. Co. 348 U.S. 310 (1955).

Wilburn Boat involved an insurance policy insuring a small houseboat against the risk of fire and other perils. The Wilburns bought the boat for the commercial carriage of passengers on an artificial inland lake between Texas and Oklahoma. While moored on the lake, the boat caught fire and was destroyed. The insurer, Fireman's Fund, denied coverage for the loss because of the breach of two express policy warranties: 1) the boat would not be transferred without the insurer's consent; and 2) the boat would be used only for pleasure purposes, i.e., not for commercial passenger-carrying purposes.

The Wilburns sued Fireman's Fund for coverage. The district court entered judgment for Fireman's Fund holding there was no coverage because of the unapproved transfer of the boat to the Wilburns and their use of the boat for commercial purposes. The district court applied the federal "literal performance" rule and held there was no coverage. That rule requires strict compliance with every warranty in the policy, and voids of coverage when a warranty is breached, whether or not the breach was causally connected to the loss. The court of appeals affirmed. The US Supreme Court reversed. It considered two questions: 1) whether there was an established federal admiralty law about the effect of the breach of the particular warranties in the Wilburns' policy; and if not, 2) whether it should fashion one. It answered both questions "no". It held if there is no well-established federal law on whether the breach of a particular policy warranty voids coverage, state law will govern. The Supreme Court then sent the case back to the district court to determine which state's law would apply.

Federal law is well established with respect to certain types of warranties such as a

trading/navigation warranty and requires strict compliance to prevent voiding of coverage. For example, Port Lynch, Inc. v. New England International Assurety of America, Inc. 754 F.Supp.816 (W.D.Wash. 1991) involved a hull policy on a commercial fishing vessel. The policy contained an express warranty that the insured vessel would be at anchor in southeast Alaska, processing shrimp. While the vessel was in the Bering Sea crabbing, a fire occurred causing the total loss of the vessel. The insured sued its insurer to recover for its loss. The court recognized the well-established federal admiralty law on the strict construction of navigation and trading warranties. It held there was no coverage because of the breach of those warranties when the vessel was in the Bering Sea crabbing instead of at anchor in southeast Alaska processing shrimp, even if compliance with the warranties would not have avoided the loss.

Other types of warranties are not so firmly entrenched in federal maritime law and the courts look to state law to determine the effect of their breach. The law in most states is consistent with the federal admiralty rule that a policy is void if a warranty is breached even if the breach was not causally related to the casualty. The reason for the rule is the practical difficulty faced by insurers in assessing a risk on a vessel. However, the law in a few states requires a connection between the breach of warranty and the loss, for coverage to be void.

For example, in Insurance Company of North America v. San Juan Excursions, Inc. 2006 AMC 2758 (W.D.Wash. 2006) the policy covered a whale-watching vessel and contained a lay-up warranty requiring the vessel to be laid up afloat from January 1 to April 14. In mid March the vessel sailed from its home berth of Friday Harbor to a shipyard in Port Angeles. Thereafter, a shipyard worker was injured aboard the vessel. The insurer filed a lawsuit against the vessel owner and the injured worker seeking a judgment of no coverage because of the breach of the policy's lay-up warranty. Following the Wilburn Boat decision, the district court first considered whether there was any well-established federal admiralty law about strict compliance with a lay-up warranty. The court noted: 1) very few courts had addressed whether a lay-up warranty requires strict compliance under federal admiralty law; and 2) no court had concluded there was an established federal admiralty rule on the issue. Because the court felt no need to fashion a federal admiralty rule about lay-up warranties, it held Washington state law applied to determine the effect of the breach of the lay-up warranty. Under Washington law, a breach of an express warranty in a policy does not void coverage unless the breach contributed to the loss or increased the risk of the type of loss sustained. In that case, there were disputed issues of fact on whether the breach of the lay-up warranty contributed to the loss or increased the risk of loss, which disputes precluded the court from deciding, without a trial, whether coverage was void.

Breach of Warranty Excused

There are circumstances under which a breach of an express policy warranty may be excused so that coverage is not void. The breach may be excused and not void coverage if it occurs to save a life. Also, if the breach of warranty is caused by a peril covered under the policy, the breach will not void coverage. For example, in US Fire Ins. Co. v. Cavanaugh 732 F.2d 832 (11th Cir. 1984), the captain of a fishing vessel took the vessel outside of the geographical limits in the policy contrary to the orders of the vessel owner. While outside the geographical limits, the vessel was lost due to stranding. The court held the efficient proximate cause of the loss was barratry by the captain, which caused the vessel to breach the navigation warranty in the policy. Under those circumstances, the policy was not void.

Breach of Warranty Endorsement

When the purchase of a vessel is financed, the financing agreement often requires the purchaser to obtain a hull policy with a breach of warranty endorsement in it. Under such endorsement, if the insured purchaser breaches a warranty and voids coverage for a loss, the bank or other financial institution is still entitled to payment under the policy to the extent of its interest.

Hull and P & I Policy Warranties Summarized

Hull and P & I policies frequently contain warranties. Under federal law and the law of most states, a breach of those warranties results in the voiding of coverage under the policy, even if the breach of warranty is not related to the casualty for which coverage is sought. Only a few states require a causal connection between the breach of a policy warranty and a loss, to void coverage. A vessel owner should not overlook warranties in a hull or P & I policy. Doing so may result in coverage not being available when it is needed.

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