Marilyn Raia
San Francisco,
Shareholder

Direct Dial: 415.352.2721
Fax: 415.352.2701
Email Attorney

Don't Lose Your Coverage Before You Need It Most

By Marilyn Raia

"Many would sooner walk the plank than engage in the risky business of interpreting maritime insurance policies." *Continental Oil Co. v. Bonanza Corp.*, 677 F.2nd 455 (5th Cir. 1982).

Unlike property and auto insurers, marine insurers are not required to insure against any particular risk. Many marine insurance policies are in non-standard manuscript form. The coverages and exclusions are as diverse as the number of insurers issuing the policies. Moreover, marine insurance policies are frequently subject to state law. Thus, each policy could be interpreted differently, depending on the state where it is issued, or the location where an accident happens.

It is very important for those in the maritime industry to assess their insurance needs before a loss occurs and then work with a knowledgeable marine insurance broker to make sure all of the exposures are "covered" as well as they can be. Many maritime insureds do not devote the effort needed to anticipate the risks posed by their business, and have been left with no coverage when they needed it the most. This article reviews a few recent cases in which courts have held that there was no coverage even though the insured might have expected otherwise.

Good Faith

The potential for the loss of coverage can arise before the marine insurance policy is even issued. Insurance on marine risks is governed by the doctrine of *uberrimae fidei*, or the doctrine of "utmost good faith." The insured under a marine policy has an obligation to deal with the insurer with the highest degree of good faith. That means that the insured must voluntarily disclose all known information that is material to the risk, even if the insurer does not ask for it. Material information is information that would have affected the decision to insure the risk, the terms of coverage, or the premium charged. Of course, the information provided must be accurate.

During the investigation of a claim, the insurer may learn that information given by the insured in the application was not correct. Inaccurate information on the application is commonly the basis for the denial of coverage and rescission of the insurance policy even if the inaccurate information was not related to the cause of the loss.

In *Commercial Union Insurance Company v. Franklin Lord, et al.*, 2005 A.M.C. 2925 (D. Conn. 2005), the insured applied for insurance on his vessel. In the application he stated that the vessel had been built in 2000 in Ontario, Canada and was purchased new for $450,000. He also stated that the vessel's engines were built by Perkins in 2000. There was a space on the application for additional "facts material to the risk" but the insured left it blank. Before the policy expired, the insured vessel sank, probably due to an engine room explosion. The remains of the vessel were never found. The insured made a claim for $450,000, the insured value of the vessel.

Misrepresentations

During its investigation of the claim, the insurer discovered that the insured had made several misrepresentations on his application. It discovered that the vessel's hull had been built in Ontario in 1984 but the insured has purchased it from someone in Virginia for $48,000. The insured finished constructing it himself in 2000 for what he alleged was a total of $450,000. The insurer also learned that the engines were built in 1996 and had been used several times by the

insured before he completed the insurance application.

The insurer denied the claim and contended that the insured's material misrepresentations rendered the policy void. The insured alleged that the answers were "essentially correct". The District Court held that the insured conveyed a "materially false" impression to the insurer and that the policy was void.

In *Commercial Union Insurance Company v. Pesante*, 459 F.3rd 34 (1st Cir. 2006) the insured was also left without coverage because of misstatements on the application. In that case, Mr. Pesante sought to insure the ***F/V OCEANA***, which he used for gill net fishing. Searching for a lower premium, his broker completed an application which described the boat as a lobster vessel. Mr. Pesante signed the application, apparently without noticing the misdescription. Eighteen months later, while returning to port from a fishing trip, the ***F/V OCEANA*** was in a collision and several occupants of the other boat were seriously injured. After the accident, Commercial Union learned it had been insuring a gill netter. It denied coverage and sought to rescind the policy. The lower court sided with Mr. Pesante, reasoning that because he was steaming home when the accident happened, he was not gill netting. The appellate court reversed and held that the misrepresentation on the application permitted Commercial Union to void the policy.

Review Advised

Once the marine policy is issued, the insured should carefully review it to determine whether it contains any warranties. A policy warranty is a promise by the insured that he will do, or refrain from doing, something that the insurer considers material to the risk that it is undertaking to insure. Marine policies contain various types of warranties; indeed a marine policy can have more than one warranty. Hull policies frequently contain warranties that require the lay-up of the vessel during a certain time of the year, limit the geographical area in which the vessel can navigate, and specify the number of crew members. A breach of a policy warranty can be the basis for the loss of coverage even if the breach is unrelated to the loss.

In *Cunningham v. Insurance Company of North America*, 2006 A.M.C. 1187 (E.D.N.Y. 2006), the insured obtained a hull policy on his fishing vessel. The policy had a warranty requiring the vessel to be laid up, i.e. winterized and out of service, from December 1 to April 1. On March 11, the vessel was destroyed by fire while tied up at the dock and winterized. Neighboring vessels were also damaged in the fire. The insured made a claim under his hull policy for the loss of the vessel and also sought assistance from his insurer in defending against the claims made by the other boat owners.

During its investigation, the insurer discovered that the insured had taken his boat out several times during the lay up period. It denied coverage on the basis of the breach of the lay-up warranty even though the boat was winterized and tied up at the dock at the time of the loss. The District Court upheld the denial of coverage and found the policy to be void even though the breach of the lay-up warranty was not related to the loss.

While many people believe that insurers look for ways to avoid paying claims, the opposite is likely true. Not only does a declination leave an insurer with an unhappy and often financially devastated customer, but also it may leave the insurer with legal fees and court costs. Busy adjusters would prefer to pay claims rather than attend court hearings and depositions. But, insurers can pay claims only when the risk has been underwritten on the basis of truthful and complete information, and the insured has complied with the requirements of his policy. A few

minutes spent making sure the application is complete and accurate, and reading the policy, perhaps with the assistance of experienced maritime counsel, to make sure that all warranties are understood and obeyed, will go far toward ensuring that claims are paid.