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A SEAWORTHINESS WARRANTY IN TIME POLICIES: A FIFTH CIRCUIT FALLACY  (formerly entitled ANOTHER CIRCUIT VIRUS...)

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The Infestation

The Court of Appeals for the Fifth Circuit was persuaded some years ago, and still believes, for aught we know, that there is an implied warranty of seaworthiness at the inception of a time policy, notwithstanding the lack of any logical explanation for such a usage and its authoritative disavowal from among those who might sometimes fortuitously benefit from it. The illegitimate conception of this warranty and its nurture in the Circuit have been exposed at some length in an earlier article and will be restated here to remind us again of its lack of foundation, with the aim of discouraging its spread.

Construction

The warranty in voyage policies, like most of our rules of marine insurance, appears in court by virtue of commercial usage, always a matter of fact rather than positive law. Those rules gained their status from recognition of the usages by the courts, as a result of which they are established usages but not positive law. The Marine Insurance Act 1906 (hereinafter “MIA”), which codified those rules, makes clear their nature by providing that they do not bind parties who agree differently or subject to a contrary usage. The main body of U.S. marine insurance law, including the seaworthiness warranty, is based on the same cases as the MIA.

The implied warranty of seaworthiness at inception of voyage policies was recognized as a general rule by the early English and American commentators, citing English and American cases and also earlier French authorities to support it. It was reasonable, and indeed highly plausible, to say that the seaworthiness of a vessel at the beginning of her voyage was impliedly agreed. It could not be supposed that the underwriter was willing to insure the safety at sea of a vessel known to be unfit to go there. Nor could it be accepted that the assured would claim that he expected the contrary. In recognition of the unreality of the warranty otherwise than at the outset of a specified voyage, it is not implied when the vessel is already at sea at the inception of the policy and in some analogous situations.

Sir M.D. Chalmers, draftsman of the MIA, in a book about it, pointed out that the warranty’s foundation was explained by one of the justices in a 1799 decision, who said: “The consideration of an insurance is paid, in order that the owner of a ship which is capable of performing her voyage, may be indemnified against certain contingencies; and it supposes the possibility of the underwriter gaining the premium [i.e. by not paying a loss]; but if the ship be incapable of performing her voyage, there is no possibility of the underwriter’s gaining the
premium and if the consideration fail, the obligation fails.”

This reasoning, of course, refers to a specified voyage.

The mischief began with a reading of the Union Insurance case, which concerned a time policy on a vessel admittedly seaworthy at inception of the policy. There was a charge of failure to make the vessel seaworthy before sailing from later ports and no issue of unseaworthiness at inception. The insurer relied in part on analogy to some of the earlier implied warranty cases which had dealt with the circumstance of a vessel’s being in a port where she could be made seaworthy. Its rather tentative argument based on those cases was summarized this way: “There seems to be, in time policies, an implied warranty of seaworthiness where the vessel, at the time of the taking out of insurance, is in a port where repairs can be made.” (Emphasis supplied.) In response, the court said that “[i]n the insurance of a vessel by a time policy, the warranty of seaworthiness is complied with if the vessel be seaworthy at the commencement of the risk,” as indeed the vessel there admittedly was. Thus the Court acknowledged that, if the assumption were true, the condition was met.

Deconstruction

Sensible warranties are not dropped from the clouds to attach to policies, or invented by courts as good ideas of how business should be done by commercial people. None of the business rationale of the warranty in a voyage policy applies to a time policy, when neither the underwriter nor the owner knows where and in what danger the vessel might be at the moment of inception of the policy. The distinction between voyage and time policies is therefore not a legal accident but the result of practical commercial differences. All authorities agree that what is seaworthiness is never fixed in law but varies with the operation in view. The requirement is less demanding of a vessel while in port than when putting to sea. So, too, it varies with the particular perils of a voyage, such as its length, the cargo to be carried, the seas to be navigated and ports of call and the season. At the inception of a voyage policy these perils are known or predictable to the assured from the description of the voyage insured, and he may be expected to prepare for them at the port of inception, and the underwriter to rate the risk accordingly. But a time policy is not written with that specificity of perils and may incept at any time, when the vessel may be at sea and beyond the owner’s power to know of her unseaworthiness or to do anything about it.

Voyage policies greatly predominated and time policies hardly appeared in the older texts and cases in which the rule was embraced. This accounts for the general statement of the rule in voyage policy cases and for the difficulty and qualification of its early application to time policies. As courts dealing only with voyage policies were used to saying that there was a warranty of seaworthiness at inception, that habitual assumption was sometimes made when they began to deal with time policies in the middle of the Nineteenth Century.
In 1853, however, the House of Lords in 1853 discarded the notion, recognizing that it could not be assumed that the ship-owner would know the condition of the vessel at inception, since she was not presumed to be in port and preparing for the start of a voyage. What the House would accept was that the insurance would be void if “the assured wilfully permits the ship to sail, or knows that it has sailed, on the voyage of which the time policy covers part, in an unseaworthy state”. In 1861, the Privy Council, speaking of the warranty, warned that “to time policies it does not apply”, and its explanation of how the nature of the voyage controls the nature of the warranty makes clear why the warranty can have no sensible application to the time policy.

In America in 1867, Phillips thought that “[t]he jurisprudence, both English and American, seems, at least, to converge to the doctrine that the risk may begin at sea or a distant port, though the requisite repairs cannot there be made,” which was actually to say that the risk in a time policy could incept without a warranty.

The rule stated by the House of Lords, after further refinement, evolved to this present statement in MIA § 39(5):

In a time policy there is no implied warranty that the ship shall be seaworthy at any stage of the adventure, but where, with the privity of the assured, the ship is sent to sea in an unseaworthy state, the insurer is not liable for any loss attributable to unseaworthiness.

The burden of this section is explicitly not a warranty. The reasons are not obscure: it has not the characteristics of a warranty; it states no fact that will be absolutely true as a condition of the policy; and a breach of it does not void the policy. This promissory condition is what would come to be curiously called by the Fifth Circuit a “negative, modified warranty” and a part of what the court has expansively called the “American Rule”.

The so-called “American Rule” is an extravagant misnomer, largely illusory, merely regional and seldom of practical consequence, as a distinction from the MIA and the general maritime law. It consists of two distinct parts:

[1] a warranty of seaworthiness as of the very moment of attachment of the insurance…[and]

[2] that the owner, from bad faith or neglect, will not knowingly permit the vessel to break ground in an unseaworthy condition…and the consequence of a violation of this “negative” burden is merely a denial of liability for loss or damage caused proximately by such unseaworthiness.

These are obviously two distinct rules, in no way dependent on one another. The second rule is not controversial and corresponds to MIA § 39(5), which uses the
word “privity” rather than “knowingly”. The Fifth Circuit, in Spot Pack, made clear that they meant the same thing, and it has continued to recognize privity as the test. The circuit itself has observed that, in most cases discussing the matter, only the second rule was in issue. Another court, in a review of the cases, has observed that “the great majority of the decided cases in this country are consistent with the English Rule”. We may therefore lay aside the second component of the “American Rule” and examine the plausibility of the first.

The Circuit finds itself embarrassed in explaining its embrace of the warranty at inception. Because good sense indicates that it is impractical and unfair in its generality, the Circuit has noted three possible qualifications or exceptions, potentially leaving little of its original generality:

There are at least three unresolved questions about the contours of this warranty. First, does the existence of an implied warranty of seaworthiness at the inception of a time hull policy depend on whether the vessel is at port or at sea when the policy attaches? Second, do principles of causation have any role in determining whether a condition of unseaworthiness at the inception of a time policy precludes recovery under the policy? And third, is the implied warranty of seaworthiness at the inception of a time hull policy absolute in nature—such that it is breached if the vessel is in fact unseaworthy at the time the policy attaches?

All this for a rule the court has described as “settled”! How should an insurer or an insured know whether his policy contained a warranty or not?

Implied terms, historically based on commercial realities and usage and the expectations of parties, exist because they are sensible. This one is not. Such implied rules were not enacted by legislatures and certainly not imposed by courts in flashes of regulatory inspiration. Patrick Griggs has reminded us that Lord Mansfield, whom we credit with articulating many of our rules of insurance and other commercial law, did so not by metaphysical invention but by learning commercial practice from those who knew it. This should be remembered when we find courts believing in a rule to favor insurers in which the insurers do not believe.

The crowning blow is that an executive of one of America’s leading marine underwriters in a well-known text on marine insurance has declared flatly that the supposed warranty, which would favor marine underwriters if it favored anyone, does not exist. Against such a denial, no case can be made for a national usage. A local usage is possible, but then it must be proved as a fact for the locality in question. And assuming it were proved for New Orleans, it would not apply to a policy issued elsewhere, most certainly not to one issued under the Marine Insurance Act 1906 and its replicas in other common law countries, the policies of which imply no such warranty.
Neither the Fifth Circuit nor any other that has repeated the "American Rule" has considered those factors or acknowledged their relevance. The allusion to the warranty in the Union Insurance case is not by any means a dictum because it is not a statement or declaration of such a rule. At very best, it rises to the level of intimation, and it is hardly credible that the Supreme Court, viewing its lack of foundation, would expect the lower courts to insist upon it to control the wills of the parties. What is the significance of the rule as an underwriting matter? Do underwriters fix lower premiums based on a probability that claims under the policy will be heard in the Fifth Circuit? Possibly, but it seems unlikely and, even if so, it may be doubted that the court confers a benefit on its vessel-owning constituents.

Action

The Fifth Circuit, with a wealth of good maritime doctrines to its credit; should graciously give up this false one and acknowledge that the American Rule is the same as the English rule of the MIA. Meanwhile other circuit and district courts should repudiate the hegemonic pretension of the epithet.

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5 See MIA § 87.
6 See, e.g., 1 JOHN DURI, THE LAW AND PRACTICE OF MARINE INSURANCE 2-7 (1845); New England Marine Ins. Co. v. Dunham, 78 U.S. (11 Wall.) 1, 31, 1870 AMC 2394, 2404 (1870); and citation of authorities in 1 and 2 DURI, supra; 1 and 2 W. PHILLIPS, LAW OF INSURANCE (5th ed. 1867); 1 and 2 THEOPHILUS PARSONS, LAW OF MARINE INSURANCE AND GENERAL AVERAGE (Boston 1868); 3 JAMES KENT, COMMENTS ON AMERICAN LAW (New York 1828).
7 See JAMES ALLAN POTHIER, A SYSTEM OF THE LAW OF MARINE INSURANCES 249-63 (citing Pothier and Emerigon) (Reprinted, Philadelphia 1789); 2 SAMUEL MARSHALL, LAW OF INSURANCE 364 (London 1802) (citing Valin, Pothier, Emerigon and the Ordonnance de la Marine, 1681); 3 JAMES KENT, supra 235.
8 See 1 W. PHILLIPS, supra note 8 §727.
9 CHALMERS AND ARCHIBALD, supra note 4, at 63.
12 Charles B. Anderson, in The Evolution of the Implied Warranty of Seaworthiness in Comparative Perspective, 17 J. Mar. L. & Com. 1, 4-7 (1986), found five cases before 1887 holding, with various conditions and qualifications, that time policies carried implied warranties of seaworthiness, and two holding that there was no such warranty.


13 Union Insurance Co. v. Smith, 31 L.Ed. at 498 (oral argument).
14 128 U.S. at 427.
16 M’Lanahan v. Universal Ins. Co., 26 U.S. (1 Pet.) 170, 184, 1998 AMC 285, 294 (1828) (“Seaworthiness in port...may be one thing...and seaworthiness for a whole voyage, quite another.”); 1 PHILLIPS, supra note 8 §§ 720, 721.
17 Hazard’s Adm’r, supra note 15, at 587.
18 See Gibson v. Small, 10 Eng. Rep. 500, 506-07 (H.L. 1853) (Baron Martin) (“both the contracting parties contemplated the state of the ship when the risk is to begin, that this state must be supposed to be known to the ship-owner, that he has it in his power to put the ship into good repair before the voyage begins”).
19 See cases cited supra note 12.
20 Gibson v. Small, supra note 18.
21 Id. at 521.
24 1 PHILLIPS, supra note 8 § 727.
25 See generally, Anderson, supra note 12, at 4-7.
26 Spot Pack, supra note 1, 242 F.2d at 388, 1957 AMC at 661.
27 Id.
28 242 F.2d at 390, 1957 AMC at 663-64.
F.2d at 1434, 1993 AMC at 1478 ("The second...looks very much like the second part of the English rule...").

30 Employers Insurance, supra note 1, 978 F.2d at 1435, 1993 AMC at 1480 n. 13.


32 Employers Insurance, supra note 1, 978 F.2d at 1435, 1993 AMC at 1480.

33 Id., 978 F.2d at 1434, 1993 AMC at 1478.


35 WILLIAM D. WINTER [Chairman of the Executive Committee Atlantic Mutual Insurance Company of New York], MARINE INSURANCE 217 (3d ed. 1952) (stating that the implied warranty of seaworthiness is not applicable to time hull risks).

36 See Insurance Co. of North America v. Hibernia Ins. Co., 140 U.S. 565 (1891) (usage is only valid where it is proved to prevail; usage claimed in New Orleans not valid in Philadelphia); Black’s Law Dictionary 1539 (7th ed. 1999) (trad usage: “such regularity of observance in a region, vocation or trade that it justifies an expectation that it will be observed in a given transaction; a customary practice or set of practices relied on by persons conversant in, or connected with, a trade or business”).

37 Insurance Co. of North America, supra.

38 MIA § 39(5).