

WARRANTIES IN MARINE INSURANCE

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INTRODUCTION

The law of warranties in relation to Marine Insurance at first glance appears to be extremely beneficial to insurers and, some might say, unfair to assureds. The black letter law is that a breach of a warranty entitles the insurer to avoid liability under the policy even if the breach of warranty had nothing to do with the loss and regardless of whether the warranty was material to the risk. This was often the result in many of the older cases. However, the more recent cases show a different inclination. In a modern marine insurance case it is more likely the insurer rather than the assured who will complain about the unfairness of it all.

DEFINITION

"Warranty is defined in section 32(1) of the Federal Marine Insurance Act (s.34(1) of the B.C. Act) as follows:

..."warranty" means a promissory warranty by which the insured

- (a) undertakes that some particular thing will or will not be done or that some condition will be fulfilled; or
- (b) affirms or negates the existence of particular facts.

The identifying characteristic of a true warranty is the consequence that flows from a breach of the warranty, namely that the insurer is discharged from liability. This is dealt with in s. 39 of the Federal Act (s. 34(2) & (3) of the B.C. Act):

- (1) Subject to this section, a warranty must be exactly complied with, whether or not it is material to the risk.
- (2) Subject to any express provision in the marine policy or any waiver by the insurer, where a warranty is not exactly complied with, the breach of the warranty discharges the insurer from liability for any loss occurring on or after the date of the breach, but does not affect any liability incurred by the insurer before that date.

These statutory provisions seem remarkably clear and unambiguous, however, as we shall see, the case law has had the effect of considerably narrowing the situations where an underwriter can avoid liability for breach of a warranty.

IMPLIED WARRANTIES

A warranty may be express or implied (s.32(2) Federal Act; 34(2) B.C. Act). The implied warranties are set out in the Act. They are:

- Warranty of legality (s.34 Federal Act; 42 B.C. Act);
- Warranty of neutrality (s.36 Federal Act; 37 B.C. Act); and
- Warranty of seaworthiness (s.37 Federal Act; 40 B.C. Act)

The warranty of neutrality is not really an implied warranty as it applies only when there is an express warranty of neutrality with respect to insurable property. It merely defines and delimits the express warranty of neutrality.

The implied warranties of seaworthiness and legality are, however, true implied warranties in that their existence is assumed at law and they will form part of any contract of marine insurance unless inconsistent with an express warranty. (s.33(3) Federal Act; 36(3) B.C. Act)

The implied warranties of seaworthiness and legality are things about which books can be and have been written. This paper does not attempt to canvass these subjects in any kind of detail but will give merely a very short introduction to the nature of these warranties.

SEAWORTHINESS

The implied warranty of seaworthiness applies with full effect only to voyage policies. The warranty is that the ship will be seaworthy "at the commencement of the voyage" for the particular adventure insured. A seaworthy ship is one that is "reasonably fit in all respects to encounter the ordinary perils of the adventure insured". In a time policy there is no warranty of seaworthiness 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". (s.37 Federal Act; s.40 B.C. Act) Thus, in a voyage policy the insurer needs to prove only one thing; that the ship was unseaworthy at the commencement of the voyage. In a time policy, on the other hand, the insurer needs to prove three things; that the ship was unseaworthy, that the unseaworthiness caused the loss, and that the assured was privy to the unseaworthy state of the ship.

The warranty of seaworthiness relates not only to the hull but also to the machinery and equipment, the crew, and the way in which a ship is loaded (or overloaded).

The implied warranty of seaworthiness often has to be interpreted together with an inchoate clause which provides coverage for any latent defect in hull or machinery. Whenever a loss is caused by any such latent defect it is almost certain that there would be coverage notwithstanding that the same defect could be a breach of the implied warranty of seaworthiness. (See Arnould, Law of Marine Insurance and Average, at para.710)

ILLEGALITY

The warranty of legality is one which is often expressly included in policies as well as implied. Where there is an express warranty of legality it will have precedence over the implied warranty to the extent the two are inconsistent.

There are three cases I would like to discuss in relation to the warranty of legality. The first is a decision by the New Zealand Supreme Court Harbour Inn Seafoods v Switzerland (1991) 6 ANZ Ins. 61-048. This case involved a fishing vessel which drifted upon a reef while "laying to" ie. drifting at sea at night with no watch. (This is not a practice which is unique to New Zealand, it is something that occurs on our coast as well, although it is rarely spoken of.) The insurer denied coverage on the basis of a clause in the policy which provided that the vessel was to be operated "in accordance with the regulations and bylaws and all other applicable laws". The Court held that the practice of "laying to" was a breach of the collision regulations and therefore a breach of the express provision and a breach of the implied warranty of legality.

Moving closer to home, James Yachts Ltd. v Thames and Mersey Marine Insurance Co. [1976] I.L.R. 1-751, was a case involving a boat builder who stored boats in his yard contrary to Municipal by-laws. A fire destroyed the boats and equipment so stored. The British Columbia Supreme Court agreed with the insurer that the assured's behavior was a breach of the implied warranty of legality and that the insurer was therefore discharged from liability.

The warranty of legality was also considered in Federal Business Development Bank v Reinsurance and Excess Managers Ltd. (1979) 13 BCLR 376. That case involved a tugboat that sank while towing a jet boat loaded with cedar shingles that had been illegally taken from the cutting site without being scaled. The Court declined to find that this technical breach of the Forestry Act discharged the insurer from liability as the assured was not deliberately acting in an unlawful manner and the failure to have the shingles scaled did not bear a direct relationship to the cause of the loss.

- EXPRESS WARRANTIES

Section 33(1) of the Federal Marine Insurance Act (s. 36(1) of the B.C. Act) stipulates how a warranty is created:

"An express warranty may be in any form of words from which the intention to warrant may be inferred."

This implies that creation of a warranty is a simple matter of choosing the appropriate policy wording. The real difficulty is, however, in choosing that policy wording. Further, in many cases even choosing the correct wording may not result in a warranty being created.

A review of earlier case law indicates that little more than a statement of fact was required to create a true warranty in a policy of marine insurance. For example, the following words were held to create warranties⁽¹⁾:

- "to sail on such a day";
- "declarations of interest to be made as soon as possible after sailing"; and
- "a Danish Brig".

In Yorkshire Insurance Company v Campbell 1917] A.C. 218, the issue was whether a description of the insured horse as "Bay gelding by Soult out of St. Paul (mare) 5 yrs" was a warranty in a policy insuring the horse on a sea voyage. In fact the pedigree of the horse insured was not "by Soult out of St. Paul mare". The Privy Council held the words were a true warranty and said:

"Prima facie, words qualifying the subject-matter of the insurance will be words of warranty, which in a policy of marine insurance operate as conditions."

The Law Commission of the United Kingdom published a report relating to warranties in 1980. Portions of this report are quoted in a very informative paper by Professor Cadwallader entitled "Instant Death (Breach of an Underwriters Warranty)" published as part of the Second International Maritime Law Seminar, 1981. Both the Law Reform Commission and Professor Cadwallader suggest that a warranty can be created by the use of the word "warranty" or a variant thereof such as "Warranted that..." or "the assured warrants that..." Professor Cadwallader says at p. 5 of his paper:

The most simple warranty to discover is obviously the one which declares itself unashamedly to be so. Two of the standard forms serve as examples: "Warranted that the vessel shall not be towed..."

In Arnould, Law of Marine Insurance and Average, at para. 679, the editors agree that the use of the word "warranted" is generally used to denote a warranty but they recognize this is not always conclusive. In the author's opinion even this more cautious statement by the editors of Arnould is no longer correct, at least in Canada. Recent Canadian case law is strongly against a finding of a warranty even when the policy uses words such as "warranted".

The leading case in this regard is undoubtedly the decision of the Supreme Court of Canada in Century Insurance Company of Canada v Case Existological Laboratories Ltd. (The "BAMCELL II") ([1984] 1 WWR 97. This case involved a ship that sank when a valve was negligently left open. The main issue in the case was whether the sinking was due to a peril of the sea. A secondary issue, however, concerned a clause in the policy which provided:

"Warranted that a watchman is stationed on board the BAMCELL II each night from 2200 hours to 0600 hours..."

It was admitted that no watchman had been on the vessel since the insurance came into effect. Hence, one would think that there had been an obvious breach of warranty and that the insurer would be entitled to a discharge from liability. However, both the British Columbia Court of Appeal and the Supreme Court of Canada had little difficulty in avoiding this result. The Court of Appeal read the policy *contra proferentem* and held that the clause was not a true warranty "having regard to the purpose of the clause". In the Supreme Court of Canada, Ritchie J., said at p. 104:

It is significant that, although there was no watchman stationed on board Bamcell II during the hours prescribed in that clause, this had absolutely no bearing whatever on the loss of the vessel which occurred in mid-afternoon. The clause would only have been effective if the loss had occurred between 2200 hours and 0600 hours, and it was proved that there was no watchman stationed aboard during those hours. To this extent the condition contained in the clause

constituted a limitation of the risk insured against but it was not a warranty.

This is the only paragraph in the judgment dealing with the warranty and it is more a conclusion than a statement of reasoning. The only reason given for rejecting the warranty is that the absence of a watchman "had absolutely no bearing on the loss". This, however, is a completely irrelevant consideration pursuant to the statute.⁽²⁾ In the author's opinion this seems to be a case where the Court disregarded the plain words of the policy of insurance and the statute to do what it perceived as fair.

The "BAMCELL II" has been considered and applied in numerous cases many of which appear on their face to contain true warranties. For example, in Federal Business Development Bank v Commonwealth Insurance (1983) 2 C.C.L.I. 200, the British Columbia Supreme Court refused to interpret a clause which expressly "Warranted vessel to be laid up at the north foot of Columbia Street..." as a warranty. The only reasoning given was that the Court concluded "the parties never intended that the warranty... be an undertaking or condition that must be strictly complied with".

In Federal Business Development Bank v Reinsurance and Excess Managers Ltd. (supra) the policy provided: "it is warranted that the vessel shall not otherwise tow or be towed". The Court held that this was not a true warranty as it was customary for vessels of the same type as the insured vessel to be used for towing. If this was the case, and the intention of the parties, one wonders why there was a warranty in the policy against towing.

Finally, in Britsky Building Movers Limited v The Dominion Insurance Corporation [1981] ILR 1-1420, the Court refused to find that a clause that provided "Warranted confined to the navigable waters of the Province of Manitoba.." was a true warranty the breach of which entitled the insurer to be discharged from liability. It is noteworthy that of all the cases that have considered this issue, this case from the Manitoba County Court is the best reasoned by far. The Court noted the use of the word "warranted" in the clause in issue and reviewed the case law on the effect of this. The court then reviewed the policy and concluded that the use of the term "warranted" had little significance as it was used in other sections of the policy where it clearly was not, or had been held to not be, a true "warranty". (This is an exercise all underwriters should likewise do.) The Court then concluded at p.438 as follows:

Turning back to the case at bar, did the parties intend that the clause in question should be construed as a promissory warranty? As I have mentioned, it is my view that little, or nothing, turns upon the use of the word "warranted". The parties might have put their intention beyond doubt simply by expressly stating that in the event the clause was breached by the navigation of the boat outside of the navigable waters in Manitoba and Northwestern Ontario, that breach would entitle the insurers to avoid the policy, and the coverage would be at an end.

These decisions illustrate that notwithstanding the use of relatively clear words courts are very reluctant to find that a particular clause is a warranty. Because of this tendency, the policy wording becomes much more important. It is incumbent on underwriters to ensure their policy wording clearly demonstrates that it is the intention of the parties that if a particular condition of the policy is breached then the insurer will be completely discharged from liability from the moment of the breach regardless of whether the condition is material or the breach has any bearing on the loss. Of course, even the best wording will not guarantee the desired result but it will make it more difficult for courts to ignore.

- TYPES OF EXPRESS WARRANTIES

The types of express warranties are limited only by the imagination and ingenuity of underwriters. Almost anything can be made to be an express warranty provided the proper words are used. Notwithstanding this total freedom to make almost anything a warranty most policies contain relatively few. Some of the more common express warranties that have been considered in recent cases are dealt with below.

NAVIGATION/TRADING WARRANTY

Two cases involving navigation warranties have already been referred to above: Federal Business Development Bank v Commonwealth Insurance and Britsky Building Movers Limited v The Dominion Insurance Corporation. In both of these cases the courts declined to give effect to navigation warranties although relatively clearly expressed in the policies. In Anderson v Dale & Company Ltd. (June 8, 1994) Reg. No.C927692 (B.C.S.C), in contrast, the Court denied coverage on the basis of a breach of a trading warranty. There was, however, an important factual distinction between Anderson v Dale & Company Ltd. and the other cases. In Anderson v Dale & Company Ltd. the insured vessel sank while being navigated in waters outside the trading area prescribed by the policy. Therefore, the Court did not have to consider whether the trading limits clause was a true warranty.

It is noteworthy that in Arnould, Law of Marine Insurance and General Average the editors say at para. 692:

In previous editions of this work, it was stated that provisions of this kind have generally been construed as warranties in the strict sense, rather than as exceptions to the cover granted by the policy. The question is of course one of construction of the particular policy, but the present editors consider that the marine insurance cases, which are relatively few in number, do not really support this proposition.

Recent Canadian case law in this area would tend to support the expressed opinion of those editors.

PRIVATE PLEASURE

Billings v Zurich Insurance Co. (1987) 27 CCLI 60 involved a claim made under a policy for theft of equipment from a boat. The policy contained a clause which provided: "Should you use or permit the use of your boat for any of the following purposes then the policy is declared null and void". One prohibited use was the carrying of passengers for payment. It was established at trial that the assured had, in fact taken people out fishing and charged them a fee. The assured argued that the charge was merely to cover expenses however the court disagreed and found he was carrying passengers for payment in contravention of the policy. The Court therefore enforced the warranty and dismissed the assured's claim.

TOWING WARRANTIES

A common warranty is one that prohibits a vessel from towing other vessels. Such a warranty was considered in the Federal Business Development Bank v Reinsurance and Excess Managers Ltd. case referred to above. The express warranty in that policy provided: "it is warranted that the vessel shall not otherwise tow or be towed". The Court held that the insurer could not rely on

the obvious breach of this warranty because it was customary for vessels of the type insured to engage in general commercial towing operations.

OTHER

Tulloch v The Queen (1988) 21 F.T.R. 72, Affirmed 26 F.T.R. 80, is an interesting case involving a warranty as the master of the insured vessel. The warranty provided:

"Warranted free from any claim for loss, damage or expense where anyone other than the Assured is Master of the insured vessel named in Clause 1 herein without prior approval of the Plan".

The rather unusual facts of the case were that the assured had to leave the vessel, which at the time was moored, but before doing so appointed a crew member as master. The newly appointed master subsequently also left the vessel leaving only one other crew member on the vessel. That sole remaining crew member was instructed to wait on the vessel until the assured returned. The remaining crew member did not wait but instead determined by himself to follow the rest of the fishing fleet to sea. The insured vessel was lost at sea. The Court held that the crew member in charge of the vessel when it sank was not a "master" within the meaning of the clause as he had not been appointed as master by the assured. Further, the Court held that appointment of the first crew member as master by the assured, although a breach of the warranty, had the effect of only suspending the coverage during the time he was master and his appointment concluded when he left the vessel.

The very recent case of Shearwater Marine Ltd. v Guardian Insurance Co. (February 28, 1997) No. C935887 (B.C.S.C.) is also illustrative of a restrictive approach to warranties. The policy in this case provided "Warranted vessel inspected daily basis and pumped as necessary". Although the court found that this condition had been complied with it did consider whether the condition was a true warranty or merely a suspensive condition and held that it was a suspensive condition.

- CONCLUSION

Recent developments in the law in relation to warranties in policies of marine insurance indicate that there has been a judicial amendment of, if not complete revocation of the Marine Insurance Acts. It is only in very rare circumstances that a Canadian court will find a policy to contain a true warranty. These circumstances will essentially be limited situations where the warranty is material to the risk and the breach has a bearing on the loss.

1. See Arnould, Law of Marine Insurance and General Average, para. 679, and the cases cited therein.

2. See Arnoulds, Law of Marine Insurance and General Average, para. 682, and the cases cited therein.