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Case Note

MARINE INSURANCE: The "literal compliance" rule applies to breaches of trading and navigational warranties. *Home Insurance Co. v. Vernon Holdings*, 1995 AMC 369 (S.D. Fla. 1994).

INTRODUCTION

For the past forty years, there has existed uncertainty regarding whether federal admiralty law or state insurance law applies to cases of breach of warranty. However, the recent decision of the Southern District of Florida in *Home Insurance Co. v. Vernon Holdings*[1] has clarified the situation, at least insofar as one particular area of marine insurance law is concerned. The court ruled that federal maritime law applies in cases in which an assured vessel owner has breached the trading and navigational limits warranty set forth in its policy.

The court pointed out that it had reached its conclusion based upon the existence of an established and generally acknowledged admiralty rule. This federal admiralty rule rendered inapplicable a provision in the statutory law of the State of Florida which would have furnished the basis for a contrary ruling. The federal maritime law precedent held to apply requires the assured's "literal compliance" with a warranty setting forth particular trading and navigation limits. As such, the insurance policy is automatically voided by proof of such a breach, irrespective of any state law that requires a causal relationship between the breach and the loss in order to void the policy.

THE *WILBURN BOAT* CASE

Litigation over the effects of an assured's breach of a warranty in a marine insurance policy has generated great confusion ever since the United States Supreme Court's decision in the famous case of *Wilburn Boat Co. v. Fireman's Fund Insurance Co.*[2] The Court surprised most scholars and commentators by holding that certain aspects of marine insurance law could

[1]1995 AMC 369 (S.D. Fla. 1994).

[2]348 U.S. 310, 1955 AMC 469 (1955).

be subject to state regulation. In any particular situation in which well-established federal maritime precedent did not exist, state law could furnish the applicable rule of decision in a marine insurance dispute. Thus, a breach of the policy's "private pleasure" warranty[3] did not void the policy. Texas state law, rather than federal maritime law, was allowed to function as the controlling authority for the issue of breach. While familiar federal maritime precedent would have required strict or literal compliance with this warranty and would have resulted in voiding the policy, Texas state law prevented the underwriters from even asserting the breach as a defense "unless such breach . . . contributed to bring[ing] about the destruction of the property."[4]

Maritime attorneys and underwriters long accustomed to viewing the assured's strict or literal compliance with all warranties as a condition precedent to recovery under any marine insurance policy were shocked by the *Wilburn Boat* decision.[5] Not only did the holding threaten the uniformity of American marine insurance law and practice, it represented a stunning departure from the equally time-honored policy of maintaining harmony between American and English marine insurance law. The Marine Insurance Act of 1906 and the cases decided under it had adhered rigidly to the rule requiring forfeiture of the policy where the assured failed to comply in strict or literal terms with a policy warranty.[6]

In the forty years since the *Wilburn Boat* decision, maritime attorneys in the United States have never been able to say with any degree of reliability, much less certainty, whether a federal admiralty rule or a state law provision will provide the rule of decision in any particular case involving a breach of warranty. Further complicating an already uncertain situation is the fact that statutory provisions pertaining to breach of warranty can vary widely from state to state. The New York State insurance code, for example, has continued to insist upon strict or literal compliance with marine warranties.[7] The statute in Texas, on the other hand, requires a causal connection between the breach and the incident in order for the breach to constitute a defense to coverage.[8] In Florida, the relevant statute requires a showing of exposure to an increased hazard as a result of the breach.[9]

Even within the confines of federal maritime law there exist differing precedents describing the effects of a breach of warranty. Some courts hold

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[3]A typical example of such a policy provision reads, "Warranted to be used solely for private pleasure purposes and not to be hired or chartered unless approved and permission endorsed hereon."

[4]Tex. Ins. Code Ann. art. 6.14 (West 1981).

[5]See, e.g., G. Gilmore & C. Black, The Law of Admiralty § 2–8, at 61–63 (1st ed. 1957).

[6]British Marine Insurance Act, 6 Edw. 7, c. 41, § 33 (1906). See also 2 Chorley, Arnould's Law of Marine Insurance and Average § 635 (13th ed. 1950).

[7]See N.Y. Ins. L. § 3106(c) (McKinney 1985).

[8]See supra note 4.

[9]Fla. Stat. Ann. § 627.409(2) (West 1984).

that federal law countenances a mere "suspension" of coverage during the time that a breach is in effect,[10] while others hold that literal compliance remains the established and controlling federal precedent.[11] Because the seamless web which ideally should be the federal maritime law of warranties has been torn apart, marine insurers do not know at the time they issue a policy whether there will be compliance with any given warranty.

THE "STRICT OR LITERAL COMPLIANCE" RULE REVIVED

In the case of *Home Insurance Co. v. Vernon Holdings*, the insurer issued a named perils policy to the assured on the latter's vessel, the M/V *Nina I.* Included was a navigational limits warranty limiting coverage to "trading between the Turks and Caicos Islands, Dominican Republic and the Bahama Islands." When the *Nina I* sank en route from Turks and Caicos to a port in Haiti, the insurer denied coverage on the basis of a breach of the navigational limits warranty. It then instituted a declaratory judgment action in the United States District Court for the Southern District of Florida pursuant to Rule 9(h) of the Federal Rules of Civil Procedure.

The assured contended that under *Wilburn Boat*, Florida state law applied and that pursuant to the applicable Florida statute, a breach of warranty would not void the policy "unless such breach or violation increased the hazard by any means within the control of the insured."[12] Sharply disagreeing with this position, District Judge Edward B. Davis distinguished or rejected all of the authorities cited by the assured. Instead, he chose to be guided by what had been, prior to *Wilburn Boat*, the well-established and accepted rule: marine warranties are to be strictly and literally complied with, upon pain of forfeiture of the policy.

Judge Davis began with *Wilburn Boat*'s premise that state insurance law applied *only* in the absence of some established federal admiralty rule. He stated that the question to be determined was "whether federal admiralty law applies to a navigational limits warranty in a marine insurance contract."[13] In answering this question Judge Davis made extensive reference to two cases that, in his view, made it clear that there already existed a well-established federal admiralty rule which required strict adherence to navigational limits warranties. Breach of this federal admiralty rule, Judge Davis held, served to void the policy.

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[10]See, e.g., Reliance Ins. Co. v. The Escapade, 280 F.2d 482 (5th Cir. 1960).

[11]See, e.g., Goodman v. Fireman's Fund, 600 F.2d 1040 (4th Cir. 1979).

[12]See supra note 9.

[13]1995 AMC at 372.

The first case looked to by Judge Davis was *Lexington Insurance Co. v. Cooke's Seafood.*[14] There, a navigational limits warranty had confined coverage to instances in which the insured vessel was traveling within 100 miles of the shoreline. The Eleventh Circuit ruled that "admiralty law requires the strict construction of express warranties in marine insurance contracts; breach of the express warranty by the insured releases the insurance company from liability even if compliance would not have avoided the loss."[15]

The second case referred to by Judge Davis was *New York Marine & General Insurance Co. v. Gulf Marine Towing, Inc.*[16] In that case, the Eastern District of Louisiana, following *Lexington Insurance*, had also found the existence of the well-established federal maritime precedent required by *Wilburn Boat.*

In rejecting application of Florida state law, Judge Davis noted that *Wilburn Boat* had involved the breach of a "private pleasure" warranty. That particular warranty was contrasted by Judge Davis with the trading and navigational limits warranty at issue in the case before him. Citing with warm approval the lower court opinion from the Southern District of Georgia which had preceded the Eleventh Circuit's decision in *Lexington Insurance*, Judge Davis explained that "navigation warranties are peculiarly maritime in nature, unlike the warranty at issue in *Wilburn Boat.*"[17] Judge Davis also noted the finding of the Southern District of Georgia that the rule of strict compliance with navigational warranties was "clearly established prior to the *Wilburn Boat* decision."[18]

Judge Davis then disposed of one last hurdle: the Eleventh Circuit's decision in *Windward Traders, Ltd. v. Fred S. James & Co. of New York, Inc.*[19] In that case the panel had seemingly approved reference to Florida state insurance statutes in order to decide a case involving a breach of a navigational limits warranty. Judge Davis noted that because the parties in *Windward* had *stipulated* that Florida substantive law would apply to their case, "the Eleventh Circuit did not have to evaluate whether the application of Florida law or federal admiralty law was appropriate, and *Lexington* and *Windward*, therefore, are not inconsistent."[20]

Judge Davis punctuated the return to a rule of strict or literal compliance with navigational warranties by taking note of a recent decision from a

[14]835 F.2d 1364, 1988 AMC 1238 (11th Cir. 1988).
[15]Id. at 1366, 1988 AMC at 1241.
[16]1994 AMC 976 (E.D. La. 1993).
[17]1995 AMC at 373.
[18]Id.
[19]855 F.2d 814 (11th Cir. 1988).
[20]1995 AMC at 373.

Florida state appellate court. In *Aetna Insurance Co. v. Dudney*,[21] the Fourth District Court of Appeal had reversed a lower court's application of state law to a case involving the breach of a navigational limits warranty after admitting that federal courts "have recognized for over forty years strict construction of navigational limit warranties has been an established rule of the federal judiciary."[22] Hence, said Judge Davis in awarding summary judgment to the insurer, "federal admiralty law applies to navigational limits warranties, and it does not matter whether the breach increased the hazard of loss; rather, a breach in itself precludes recovery."[23]

CONCLUSION

The decision of the United States District Court for the Southern District of Florida in *Home Insurance Co. v. Vernon Holdings* builds upon the foundation of the *Lexington Insurance* decision. One can only hope that it will have the salutary effect of returning uniformity and certainty, in one restricted but important area, to the law of breach of warranty in marine insurance. Attorneys in South Florida and throughout the Eleventh Circuit can now advise their clients with confidence that breach of a navigational limits warranty will void a marine insurance policy. The same is still not true as regards a private pleasure warranty, despite the fact that these two provisions quite frequently are included together and even complement each other in many policies.

It may be that we are witnessing the beginning of a slow but steady judicial process in which the holding of *Wilburn Boat* will be incrementally undone, and the law of breach of warranties in marine insurance returned to a state of uniformity and certainty. Judge Davis' decision certainly suggests that this is a possibility. It is certainly a consummation devoutly to be wished for by all who are concerned with uniformity in the operation of maritime law.

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[21]595 So. 2d 238 (Fla. 4th DCA 1992).
[22]Id. at 239.
[23]1995 AMC at 374.