SUN MOBILITY
Insurance and Claims Services Limited

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To: Transport Industry Operators

# Cargo insurance's warranty

The Hong Kong Court of Final Appeal ("the CFA") issued a Judgment on 10/9/2014 dismissing a cargo owner's ("the Assured") cargo insurance claim of US$1,555,209.00 against an insurance company ("the Insurer") on the ground that the Assured had breached an insurance warranty relating to the carrying vessel's deadweight capacity. [FACV No. 18 of 2013]

The Assured sought to overturn the decision of the Court of Appeal and restore the judgment given in its favour by the High Court enabling it to recover the sum of US$1,555,209.00 (together with interest and costs) under a contract of marine insurance ("the Contract") as against the Insurer. Liability had been disputed by the Insurer primarily on the basis of an insurance warranty in relation to the deadweight capacity of the vessel under the Contract. The essential question before the CFA was whether the Insurer could successfully do so.

By a Marine Cargo Insurance Application dated 2/1/2008 ("the Application"), the Assured applied to the Insurer for marine insurance coverage in respect of the shipment of a cargo of Malaysian round logs from "Malaysian Port" to Zhangjiagang in the PRC. The relevant carrying vessel was named as the "MV Ho Feng No. 7" ("the Vessel") and the amount sought to be insured was US$1,500,000.00. The application was accepted and a Marine Cover Note ("the Cover Note") was issued, confirming the insured interest as the logs valued at US$1,500,000.00. Three points were of note in relation to the Cover Note:-

(1) Against the side heading "Ship", there appeared the words "PER APPROVED VESSEL OR VESSELS TO BE DECLARED AND SUBJECT TO ANY ADDITIONAL SURCHARGE IF REQUIRED".
(2) Against the side heading "Conditions" was the clause "WARRANTED YEAR BUILT OF THE VESSEL NOT OVER 30 YEARS. WARRANTED DWT NOT LESS THAN 10,000" ("the Deadweight Warranty").
(3) The Cover Note also stated that the insurance cover would be subject to the terms, exceptions and conditions of the policy to be issued.

The policy replacing the Cover Note was dated 11/1/2008 ("the Policy"). The insured interest were the logs, but the value was stated to be US$1,555,209.00. Of note were the following on the face of the Policy:-

(1) In the box marked "Vessel" was typed "M.V. HO FENG No. 7 V.712S", in other words the Vessel and the identification of the relevant voyage.
(2) In the box to identify relevant clauses and conditions, there was typed out the Deadweight Warranty.

In or about mid-January 2008, in the course of the voyage from Kuala Baram Malaysia to Zhangjiagang in the PRC, the Vessel sank and the cargo of logs was totally lost. A claim under the Contract was made by the Assured to the Insurer for the insured value of US$1,555,209.00. The claim was rejected by the Insurer on the basis that the Assured was in breach of the Deadweight Warranty: the vessel's deadweight capacity was less than 10,000 tonnes.

The Marine Insurance Ordinance Cap 329 ("the MIO") was enacted in Hong Kong in 1961. The MIO contains a part specifically addressing the nature of marine insurance warranties: ss 33 to 41. Only s 33 was relevant:-

> "33. Nature of warranty
> (1) A warranty, in the following sections relating to warranties, means a promissory warranty, that is to say, a warranty by which the assured undertakes that some particular thing shall or shall not be done, or that some condition shall be fulfilled, or whereby he affirms or negatives the existence of a particular state of facts.
> (2) A warranty may be express or implied.
> (3) A warranty, as above defined, is a condition which must be exactly complied with, whether it be material to the risk or not. If it be not so complied with, then, subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without prejudice to any liability incurred by him before that date."

A number of points ought to be made in relation to this provision:-

(1) The provision defines warranties as promissory in nature and the definition of this term includes the affirmation of the existence of a particular state of facts: s 33(l).
(2) Although no particular form of words is required before a marine insurance warranty is created and the use of the word "warranted" does not conclusively mean that such a warranty exists, nevertheless the use of the word does raise a presumption that a warranty is intended.
(3) Where a marine insurance warranty is breached, the insurer is discharged from liability; there is an automatic discharge from liability: see *Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda) Limited (The Good Luck).* It provides a complete defence to any claim made under the policy. There need not be any causal connection between the breach of warranty and any loss suffered by an assured for which a claim is made: see *HIH Casualty and General Insurance Limited v New Hampshire Insurance Company*.

In the appeal in question, reliance was placed by the Assured on waiver. A warranty will be ineffective if it is waived: see s 34(3) of the MIO. In the context of a waiver under s 34(3) of the MIO, in the light of the principle that the breach of a marine insurance warranty results in the automatic discharge of an insurer's liability, the meaning of waiver is what has been termed waiver by estoppel: see *Argo Systems FZE v Liberty Insurance (Pte) (The Copa Casino)*. This type of waiver, the same as an equitable estoppel, requires three elements to be established by the party relying on it: first, a clear and unequivocal representation by the person said to have waived rights (ie the Insurer), whether by words or conduct, that the representor's legal rights will not be insisted upon; secondly, reliance by the representee (ie the Assured) on the representation; and thirdly, that it would be inequitable for the representor to go back on the representation.

The Assured accepted that the Deadweight Warranty was a marine insurance warranty and that s 33 of the Ordinance was therefore engaged. There was no doubt that the Deadweight Warranty was a marine insurance warranty. By this warranty, the Assured affirmed a particular state of facts, namely, that the carrying vessel of the cargo (the relevant interest insured under the Contract) would have a deadweight capacity of over 10,000 tonnes. The legal consequence of the Deadweight Warranty being a marine insurance warranty is that in the event of breach, an insurer will generally be discharged from liability under the relevant contract of marine insurance.

The Assured contended that the Insurer was prevented from relying on the Deadweight Warranty by reason of any one or more of the following: on a true construction of the Contract, rectification and waiver/estoppel.

**THE CONSTRUCTION OF THE CONTRACT**

It was apparent from the Assured's submissions that reliance was still placed on the High Court's reasoning that there was somehow an inherent inconsistency between naming a vessel in a contract of marine insurance and a warranty requirement regarding the deadweight capacity of that vessel (such as the Deadweight Warranty). In the CFA's view, it was unarguable. The mere fact that a vessel is named in a contract of marine insurance does not mean in any way that an insurer is somehow prevented from insisting by way of warranty on that vessel possessing certain characteristics. Nothing in the Ordinance remotely suggests otherwise. Indeed, the references to express warranties and the various other warranties in the MIO all suggest that they would exist even where the relevant carrying vessel is known to an insurer. Just to give one illustration: it cannot seriously be contended that just because an insurer is aware of the name and voyage of a relevant vessel that the insurer is somehow prevented from insisting on compliance with the warranty of seaworthiness contained in s 39 of the Ordinance. The CFA saw no inconsistency in the Contract between the identification of the Vessel and the existence of the Deadweight Warranty. Nor was the analysis any different by reason of the fact that the Vessel may have been an "APPROVED VESSEL".

Rather, the Assured's position was that by reason of the Insurer's knowledge of the Vessel's deadweight capacity, it was prevented from relying on the Deadweight Warranty. The Assured submitted that the High Court made an express finding that at all material times the Insurer knew of the Vessel's deadweight, that this finding should not be disturbed by the CFA and it should not have been disturbed by the Court of Appeal. As the Assured stated, this finding of knowledge "should form the basis of the adjudication of this appeal".

The CFA found it difficult to accept that the special knowledge of a party to a contract might affect what otherwise would be the true construction (as opposed to the effectiveness) of the terms of that contract.

Much less, in the exercise of construing a contract, could a party's knowledge result in a term of contract being 'red pencilled' into oblivion by its total deletion, as the Assured submitted (concerning the Deadweight Warranty). A party's knowledge may, however, result in some form of waiver on estoppel being applicable.

**THE STATE OF KNOWLEDGE OF THE INSURER**

The Assured contended first that the High Court made positive findings of primary fact to the effect that the Insurer did at all material times have knowledge of the Vessel's deadweight capacity.

But the CFA was of the view that the High Court did not identify any evidence to support such a finding at all, if indeed the High Court did make such a finding in the first place. The Court of Appeal was of the view that no such finding of actual knowledge had been made by the High Court. Nor was the Assured really able to identify any evidence to justify what it submitted were the High Court's findings of primary fact.

It was submitted, however, that the Assured having raised a *prima facie* case on the facts of actual knowledge, this *prima facie* position should be taken factually to be the established position in the absence of any contradictory evidence adduced by the Insurer. In other words, a *prima facie* case on the facts having been raised, adverse inferences could be drawn from the failure to adduce contradictory evidence, particularly where a party could be expected to provide such evidence; in such situations silence would be fatal.

However, before a *prima facie* factual situation can be said to exist, there must be evidence adduced of "sufficient cogency" to raise a *prima facie* case in the first place. The Assured did not reach this threshold. The Assured relied on the Statement of Claim in which there was a reference (without any particulars) to actual knowledge; reliance was also placed on the fact that the Vessel's deadweight capacity could be found on the internet. These were insufficient by a long way to make out a *prima facie* case on knowledge.

There being no evidence of actual knowledge, the Assured then tried to make out a case to suggest that some form of constructive knowledge was sufficient. The Assured's submissions amounted to this: since the exercise in contractual construction involved the Court taking into account the factual matrix of the relevant contract and the factual matrix included all facts which might be "reasonably available" to the parties, the Vessel's deadweight capacity being "reasonably available" to the parties meant that the Insurer was to be taken to have knowledge of the Vessel's deadweight capacity; the result then was that the Deadweight Warranty should be given no effect.

The CFA could not agree with this argument. The account that one takes of the factual matrix of a contract is to assist in arriving at the true construction of the contract and its terms. It does not have some separate life of its own to undermine or nullify the effect of a clear term of the contract. The meaning and effect of the Deadweight Warranty is clear and no assistance can be derived by reference to the factual matrix of the Contract.

The Assured's submissions on factual knowledge must fail, and insofar as some form of constructive or presumed knowledge was relied on, this did not advance the Assured's case at all. Any information to which the Insurer may have had access did not affect the operation of the Deadweight Warranty.

**RECTIFICATION**

The Assured submitted (and the CFA agreed) that the correct approach to rectification of a contract where it does not accurately reflect the parties' true agreement, is that set out in *Agip SpA v Navigazione Alta Italia SpA (The Nai Genova and Nai Superba)*:-

> "As the law stands, the conditions which must be satisfied if rectification is to be granted on the grounds of common mistake may, in my opinion, be summarized as follows:
> First, there must be a common intention in regard to the particular provisions of the agreement in question, together with some outward expression of accord. Secondly, this common intention must continue up to the time of execution of the instrument. Thirdly, there must be clear evidence that the instrument as executed does not accurately represent the true agreement of the parties at the time of its execution. Fourthly, it must be shown that the instrument, if rectified as claimed, would accurately represent the true agreement of the parties at that time: (see generally Snell's Equity, 28th ed. (1982) at pp. 612-614)."

In support of its case, the Assured referred to the High Court's judgment in which the High Court concluded that the insertion of the Deadweight Warranty must have been an error and did not represent

the parties' common intention. The High Court arrived at this conclusion by reference to two matters: the Deadweight Warranty had featured only rarely in the contracts of marine insurance previously entered into by the parties, and the view that the High Court took regarding what it saw as an inconsistency in the Contract between the naming of the Vessel and the Deadweight Warranty. The first reason, however, provided no basis at all for saying that the Deadweight Warranty was therefore somehow ineffective as a term of the Contract. This was notwithstanding even the fact that although previous policies may not have contained a deadweight warranty, the cover notes in relation to such policies did. The second reason was based on the High Court's construction of the Contract, and that construction was in error. Further, the High Court also seemed to place reliance on the fact that the Assured's employee (Ms Wong) was not sufficiently sophisticated to appreciate the significance of the Deadweight Warranty. This only had to be stated to be rejected as a ground for rectification.

The claim for rectification accordingly failed.

**WAIVER AND ESTOPPEL**

If the Deadweight Warranty was valid, the Assured contended that there had been waiver on the part of the Insurer. Reference was made to s 34(3) of the Ordinance. Under that provision, the meaning of waiver is waiver by estoppel or equitable estoppel. On the facts of the case in question, the Assured could not satisfy the requisite conditions for this form of waiver to apply:-

(1) It was the Assured's case that the Insurer made a representation to it that notwithstanding the Deadweight Warranty and notwithstanding the fact that the Vessel's deadweight capacity did not comply with that warranty, the Insurer would nevertheless accept the Vessel for the purposes of marine insurance cover under the Contract. According to the Assured, the representation arose by reason of the following matters: the Insurer's knowledge that the relevant vessel for the voyage was in fact the Vessel, the ease by which the Insurer could have found out about the Vessel's deadweight capacity (through the internet), the issuance of the Policy and the acceptance of the premium. The Assured is said to have relied on this representation by not taking out any other policy of marine insurance. It was submitted that, accordingly, it would be inequitable to allow the Insurer to rely on the Deadweight Warranty.
(2) This argument fell at the first hurdle. None of the matters relied on, whether singly or cumulatively, could possibly amount to the requisite clear and unequivocal representation contended for.

**NON-DISCLOSURE**

Both courts below dealt with the defence advanced by the Insurer that the Assured had breached the duty of disclosure under s 18 of the MIO. In its written Case, the Insurer maintained this defence.

The CFA did not see the relevance of non-disclosure, given the existence of the Deadweight Warranty. There is a certain illogicality in defending a marine insurance claim on the basis that a material fact should have been, but was not, disclosed by the assured to an insurer, when that very fact is the subject matter of a marine insurance warranty. Indeed, s 18(3)(d) of the Ordinance states that in the absence of inquiry, any circumstance which is superfluous to disclose by reason of an express warranty, need not be disclosed.

**CONCLUSION**

For the above reasons, the appeal was dismissed. Quite simply, the Deadweight Warranty was breached and there was no answer to that.

Please feel free to contact us if you have any questions or you would like to have a copy of the Judgment.

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