

**“HEAVY WEATHER
VS.
WASTAGE and CORROSION”**

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**October 5, 1994
Association of Average Adjusters of the United States**

On May 24, last, Bern Ustorf called and asked me whether or not I would do a small talk at this seminar. Foolishly, I replied in the affirmative before asking the nature of the topic. After inquiring as to the topic, I was then told that the title would be "Heavy Weather vs. Wastage and Corrosion". After swallowing several times, I then expressed a willingness to talk about "cancer" rather than the designated subject.

In any event, I did agree to express some thoughts. However, I intend to confine my observations and comments to those that I think are appropriate for a surveyor/consultant type to make. I also presume that the intent was to entice me further into making some comment as to how some combination of wear and tear (I will use wear and tear and wastage and corrosion synonymously) might relate to either the "Liner Negligence Clause" in the case of American policies or the "Additional Perils Clause" in the case of British policies. I will not read the clauses, but for the sake of continuity, and in expectation that someone might eventually read this short dissertation, the clauses are furnished as follows:

LINER NEGLIGENCE CLAUSE

"This insurance also specially to cover, subject to the Average Warranty:

- a. Breakdown of motor generators or other electrical machinery and electrical connections thereto; bursting of boilers; breakage of shafts; or any latent defect in the machinery or hull;**
- b. Loss of or damage to the subject matter insured directly caused by:**
 - 1. Accidents on shipboard or elsewhere, other than breakdown of or accidents to nuclear installations or reactors on board the insured Vessel;**
 - 2. Negligence, error of judgement or incompetence of any person; excluding under both a and b above only the cost of repairing, replacing or renewing any part condemned solely as a result of a latent defect, wear and tear, gradual deterioration or fault or error in design or construction;**

provided such loss or damage (either as described in said a or b or both) has not resulted from want of due diligence by the Assured(s), the Owner(s) or Manager(s) of the Vessel, or any of them. Masters, mates, engineers, pilots or crew not to be considered as part owners within the meaning of this clause should they hold shares in the Vessel."

INSTITUTE ADDITIONAL PERILS CLAUSES - HULLS

"(For use only with Institute Time Clauses - Hulls 1/10/83)

1. In consideration of an additional premium this insurance is extended to cover
 - 1.1 the cost of repairing or replacing
 - 1.1.1 any boiler which bursts or shaft which breaks
 - 1.1.2 any defective part which has caused loss or damage to the Vessel covered by Clause 6.2.2 of the Institute Time Clauses - Hulls 1/10/83.
 - 1.2 loss of or damage to the Vessel caused by any accident or by negligence, incompetence or error of judgement of any person whatsoever.
2. Except as provided in 1.1.1 and 1.1.2, nothing in these Additional Perils Clauses shall allow any claim for the cost of repairing or replacing any part found to be defective as a result of a fault or error in design or construction and which has not caused loss or damage to the Vessel.

1/10/83"

Before discussing a relationship between wear and tear, heavy weather and insurance coverage, let us attempt to generally define wear and tear and heavy weather at least from a surveyor's viewpoint.

In our office we have a rather comprehensive "marine" library and a diligent search failed to find a precise definition of "Heavy Weather".

Presumably, this is because there is no precise definition. Perhaps the complexities of determining what is and what is not heavy weather can be illustrated by the following example:

Wind forces at say Beaufort Scale 4, together with five (5) foot seas would be somewhat uncomfortable for a 60' shrimp boat. On the other hand, the Captain of the "QE2" might consider these conditions as likened to a "mill" pond.

The best definition that we could find for wear and tear or "wastage and corrosion," came from the "Dictionnaire de Marine" which was published in Paris in 1908. The definition is as follows:

"Wear and Tear: In nautical practice this term comprises all deterioration of the hull, ropes, sails, etc., or of a steamer's machinery, through use or time, not attributable to accident."

I, personally, think that this is not only a short but also a very precise definition which can be accepted by all who are involved in the marine business in general and certainly in marine insurance matters in particular.

In any event, and in going through our not inconsiderable library, we have found absolutely no reference to "heavy weather" per se, or to an attempt at a specific definition. We did find, in the Maritime Dictionary published in Paris in the year 1908, reference to the term "wind". A man by the name of Augustin Challamel edited the dictionary and due credit was given to five (5) others who translated the book from French into English, German, Spanish and Italian.

The term "wind" was defined thusly:

"Wind: Is the term given to the greater or lesser movement of the atmosphere arising from various causes. The effects in velocity pressure on surfaces, etc., as tabulated by "Beaufort" are as follows:

0	Calm
1	Light airs
2	Light breeze
3	Gentle breeze
4	Moderate breeze
5	Fresh breeze
6	Strong breeze
7	Moderate gale
8	Fresh gale
9	Strong gale
10	Whole gale
11	Storm
12	Hurricane "

Thus we can see that the "Beaufort" scale upon which we all, to this date, rely on, was an accepted standard some eighty-six (86) years ago.

In short, however, I think that no one has been able to accurately define the words "heavy weather." Thus we can assume that a precise characterization is not available and apparently for some good reasons. Then, can we not assume that the literal substance of what is or what is not "heavy weather" must be left for decision to those who have "gone down to the sea in ships" and have literally experienced 20' to 40' waves or larger?

Damages involving combinations of "heavy weather" and various stages of "wear and tear" are probably the most controversial kinds of claims with which surveyors, representing both Underwriters and Owners, must deal. Certainly 10 or 15 minutes is not nearly enough time to scratch the surface of this topic, never mind trying to adequately deal with the complexities involved, or to offer meaningful suggestions.

I think that everyone in this room will agree that Underwriters, over at least the last decade, have taken a severe financial beating. The reasons for this are myriad and complex. However, one has only to consider the "pollution" and "asbestiosis" claims that have arisen through the courts in our country to get some feel for the plight of Underwriters, not to mention the unexplained sinkings and disappearances of questionably maintained or designed or constructed bulk carriers.

I think many people on a worldwide basis, but especially here in the United States, look upon Underwriters as a large company with inexhaustible funding. As we all know, this, sadly, is not the case.

It is a fact that Underwriters, in order to stay in business, must collect a greater amount in premiums than is paid out in claims. This premise does not require "rocket scientist" thinking. Understandably, Underwriters are now scrutinizing potential claims and are increasingly reluctant to respond to claims until all the "T's" are crossed and the "I's" are completely dotted. We have no quarrel with this type of thinking. As a matter of fact, we think that this type of thinking should apply not only in a bad market for Underwriters, but should also apply in a good market as well.

Underwriters are raising premiums not only for standard coverage but also for the more comprehensive coverage (liner and additional perils). They are apparently also becoming extremely more discriminating as well with regard to whom they offer the more comprehensive coverage. Again, we have no quarrel with this path of recovery. Certainly, discrimination in offering liner negligence and additional perils coverage again should be, in our opinion, standard procedure regardless of whether the market, from the Underwriters' point of view, is good or bad. In short, we, and we assume almost every one in our business, is not without some sort of sympathy with regard to the plight in which Underwriters' have now found themselves.

It is now the time for the "however's" and "but's." It seems to us that Underwriters in the last few years, and in what at least from our point of view appears to be in some desperation, have ridden rather rough-shod over some very basic principles under which the industry has been operating, at least going back through the confines of my memory which (as you can plainly see) is not inconsiderable. As an aside, I have painfully learned that the individual who coined the phrase "golden years" had not yet reached the age of forty (40).

Now then, and having said that, we feel that this subject - "heavy weather vs. wear and tear" - is probably one of the most common areas in which some long standing general principles or guidelines have become extinct almost overnight, as if they were kindred with the dinosaur.

Consider the subject of "wear and tear" by itself. From our point of view and over the last few years, we have been given the impression, rightly or wrongly, that Underwriters will not pay for what is loosely termed as "wear and tear". It has only recently become practice for Underwriter's Surveyors to either deny or adjust claims made by Owners. This denial or adjustment then becomes actually part of the survey report and in turn is considered "Gospel" until some argument is put forward through the adjuster to obtain a reversal or mitigation. All of this could take years before the Underwriter's client, the ship owner, receives compensation for what was a legitimate claim at the outset.

There are, in our opinion, several long-standing principles regarding the treatment of wear and tear that have recently become history with regard to claims presentation and Underwriters' response. Among others, here are a few:

1. There will be no "new for old" adjustment for damage due to a peril or other coverage insured for.
2. The "death blow" theory.
3. Under the "liner negligence" clause the only exclusion that we can recognize is the phraseology "...replacing or renewing any part condemned solely as a result of a latent defect, wear and tear, gradual deterioration or fault or error in design or construction..."
4. Under the "additional perils" clause, we note that there is not even an exclusion of parts condemned solely as a result of wear and tear.

Leslie Buglass, with whom many of the older people in this audience including myself, were privileged to have known and to have had the opportunity to work with, had the following to say with regard to these subjects. Following are quotes from the third edition of his book entitled, "Marine Insurance and General Average in the United States." This third edition was published in 1991.

In the interest of conserving time, I will not read these quotes. Copies of this short presentation containing the text of the quotes will be available at the conclusion of this meeting.

"...while the underwriter is not answerable for wear and tear and decay from ordinary causes, he is answerable for the risks insured against, though they may be enhanced by the ordinary effects of the elements (Subsect. 1546). This is sometimes called the "death blow" theory (see Integrated Container Service v. British Traders Insurance Co., supra) but it is really a question of proximate cause; the question to be asked is: 'Would this damage have occurred but for the operation of an insured peril?' Thus, if a vessel is classed with a reputable classification society and has been properly maintained in accordance with the requirements of that society and her plating fails in heavy weather, there is a prima facie claim under the policy even though her plating may have been subject to thinning or 'aging' and even though it might have been necessary to effect maintenance repairs very soon. In arriving at the reasonable cost of repairs, no deduction is made for any enhanced cost arising out the vessel's age and condition, for the policies will invariably contain a clause stipulating that there shall be no deduction for the substitution of new material for used or old material. In one English case, the court was satisfied that as the loss was proximately caused by a period of the sea (heavy weather), it was recoverable, although it might not have occurred but for the concurrent action of some other cause not within the policy, namely, unseaworthiness. (Frangos v. Sun Ins. Co. Ltd., L.L.R., Vol. 49, p. 354; see also yacht Duet discussed earlier.)"

"For example, take the case of a vessel which, while very old and decayed, is nonetheless seaworthy and capable of fulfilling its assigned tasks. If, as a result of the operation of an insured peril, the vessel is damaged to such an extent that the cost of repairing it would exceed the insured value, there is, of course, a constructive total loss. The fact that the vessel was particularly old and decayed would not defeat the claim if she was serviceable before the encounter with the insured peril."

"Under this clause (liner negligence), as long as there has been an accident and damage has resulted, it is not necessary for the assured to point to a specific peril. If the claim is to be avoided, the underwriters must rely on the exclusions part of the clause. This reads:

excluding...only the cost of repairing, replacing or renewing any part condemned solely as a result of a latent defect, wear and tear, gradual deterioration or fault or error in design or construction.

This part of the clause appears to have caused some difficulty to the uninitiated but it means only that the mere discovery of a latent defect, a wear and tear condition, or a fault or error in design or construction during a routine examination in port does not provide grounds for a claim under the clause. The exclusion would also apply even if, at a routine examination, the defect had manifested itself. This for the reason that, in those circumstances, there has been

no accident, no actual failure in operation, but merely the condemnation of a part owing to the presence of a latent defect, wear and tear, gradual deterioration, or fault or error in design or construction. Thus underwriters do not respond when a part is merely condemned on inspection or survey and has not been damaged due to a previous accident in operation. Conversely, underwriters are liable if the defective part failed in operation; in those circumstances the defective part has reached the breaking point and there has been an accident within the meaning of the clause.

A somewhat similar exclusion was interpreted recently by the English courts. The exclusion read as follows:

No claim shall be allowed in respect of...any loss or expenditure incurred solely in remedying a fault in design...or for the cost and expense of replacing or repairing any part condemned solely in consequence of a latent defect or fault or error in design or construction.

The decision reached was that the exclusion applied only where a part was condemned solely in consequence of a latent defect or error in design or construction. The word "solely" means "without the intervention of any peril" (the Miss Jay Jay - J.J. Lloyd Instruments v. Northern Star Insurance Co., 1985 1 L.R. 264, 1987 1 L.R. 32). The thrust of this decision is that, if an insured peril intervenes between the original flaw and the resultant damage, the insurers are not entitled to rely on the exclusion.

In summary, in determining whether the exclusion in the liner negligence clause is applicable in any particular case, the questions to be asked are:

- a) Has there been an accident in operation--that is to say, a failure in service? (an accident is an insured peril); or**
- b) Has any other insured peril operated in conjunction with any of the defects (latent defect, wear and tear, gradual deterioration, or fault or error in design or construction) enumerated in the exclusion and, if so, was it this combination which resulted in the defective part in question being condemned?**

If the answer to either of these questions is in the affirmative, the exclusion does not operate, because there has been no part condemned solely as a result of a latent defect, etc. However, the exclusion is not restricted to the condemnation of an apparently sound part whose defects have not yet been manifested. For example, if on opening up machinery at a routine survey it is found that a latent defect has become patent (as when cracks are discovered in a part formerly thought to be sound) and there has been no intervention of an insured peril, the

exclusion is applicable. In particular it cannot be argued that the exclusion does not apply because there has been an accident in operation resulting in the cracks discovered on opening up. The clause requires that the damage be caused by an external accidental event. If the sole cause of the damage giving rise to the condemnation of the defective part was an inherent defect (that is, latent defects, wear and tear, and design defects, etc.), any claim for repairing or replacing the part is caught by the exclusion in the clause. To suggest otherwise would be to construe the clause as providing a permanent guarantee or the shipbuilder's or designer's work and entitle an assured to improve his vessel at underwriter's expenses. This is certainly not the intent of the clause.

Before leaving the subject of the exclusions, it should be pointed out that this part of the clause simply restates the position under common law; the exclusions are precautionary and operate when no accident has occurred. Furthermore, as is the cause in every 'all risks' insurance, once a prima facie claim has been presented to underwriters, the onus of proof lies with them should they wish to reject the claim."

These quotes are, however, rife with language proclaiming that liability rests with Underwriters where wear and tear exists and the failure is accompanied by an intervening peril, i.e. heavy weather. The only valid exclusion is lack of diligence on the part of the Owners and the burden of proof of lack of diligence is on the Underwriters.

We have seen formal surveys presented by those representing Underwriters where the surveyor completely denies the claim where "heavy weather" is accompanied by "wear and tear." We have seen cases where the surveyor representing Underwriters apportions or adjusts the claim in his report based upon a percentage to be applied to "wear and tear", hence Owners' account, and a percentage to be applied to heavy weather and thereby to damage or Underwriters' account. In so doing, all common costs must be apportioned, as well, in accordance with the surveyor's original separation. We presume that in so doing, the surveyor is acting or performing under instructions issued either by or certainly with the blessing of Underwriters.

With regard to this rather recent procedural change, we would make the following comments:

- 1) In the case of either "Liner negligence" or "additional perils" coverage, this procedure seems rather contradictory to traditional interpretation.
- 2) It apparently gives no consideration to the "death blow" doctrine.

- 3) The new procedure gives rise to the proposition that both Underwriters and their clients, the ship owner, will have to rely on the interpretations of each individual surveyor. If Underwriters employ or use 2,000 surveyors world-wide, then we can expect 2,000 different interpretations.
- 4) Are not Underwriters, through their representatives, usurping the traditional role of the Average Adjuster?
- 5) Does not allocation, apportionment or separation by underwriter's surveyors take settlement opportunities out of the Underwriters' hands?

I think we could explore these ramifications indefinitely but one thing, in my opinion, is patently clear. Recent changes in claims reporting have made a shambles of the interpretations with which all in the industry have grown accustomed to and as so eloquently put forth in Mr. Buglass' book.

Consider a situation such as this:

- 1) A vessel undergoes special survey, say in 1989.
- 2) During the survey some steel plating or internals are found variously wasted to as much as 21%.
- 3) The limit of wastage permitted before renewal is 25%.
- 4) The vessel is issued a new Load Line certificate and Special Survey is credited without making steel renewals.
- 5) The vessel encounters severe heavy weather just prior to the expiration of the Load Line and Special Survey certificates. The plates and internals previously described are found damaged.
- 6) During survey, measurements taken show the percentage of wastage to be at generally 26%.
- 7) The vessel's Owners have warranted "Class maintained" and have documentation to show that the warranty has been satisfied.

What happens in a case like this?

- 1) Are Classification Surveyors obliged to foresee wastage beyond limits and make recommendations before the limit is reached?

- 2) Does the Owner become partially self-insured on a progressive basis between special surveys?

Note: One might ask, and not without considerable justification, "what are the responsibilities of either the Classification Society or the Owner during this 4 - 5 year period between surveys?" This is in our opinion a very legitimate question and I recommend that the Association consider this as a possible topic for a future seminar.

Incidentally, and before leaving "Classification Societies" and "Owners", I would like to make a comment regarding the JH 115, 115A and 722 surveys now being made by The Salvage Association. In our opinion, they have provided, and hopefully will continue to furnish, a means for helping to rid our industry of some of the more poorly maintained tonnage. The presence of Underwriters' surveyors acting in this phase of the business will, no doubt, get some attention from the Classification Societies and thereby, over a period of time, raise the industry standard of maintenance to a higher level than now exists.

In the meantime and for the purpose of this illustration, we will assume or consider that the wastage was not as a result of lack of diligence on the part of the Owner.

- 3) Are these damages recoverable without an adjustment for "new for old"?

It would seem to us and based upon Mr. Buglass' book and our own experience, that the answers to questions 1 and 2 are "No," while question 3 should be replied to in the affirmative.

Before coming to a close, I would like to quote three (3) paragraphs from the general section of the now defunct U.S. Salvage Association's instructions to surveyors:

"Marine underwriters and adjustors must make their evaluations of damage circumstances on the basis of coverage of policies of insurance. The conditions of insurance are of fundamental importance and interest to underwriters and adjustors; they do have some significance to surveyors, but only to the extent that such knowledge leads the surveyor to inquire and obtain facts and costs when attending a survey which will permit preparation of a survey report which will supply the information needed by underwriters and adjustors to treat with the circumstances in accordance with insuring conditions."

.....

"At a damage survey an Association surveyor acting for underwriters, when in doubt as to the treatment of any item or service, should make no dogmatic overtures, but rather, should gather at the survey full descriptive and price information on the items which to him are questionable, in order that this information can addendively be set forth in his report, to be treated by adjustors and underwriters as they see fit.

At no time is the surveyor to act in an adjusting capacity, which in plain terms means that the surveyor is in no position to "apportion" any item or items between or among damages or principals, and accordingly, damage survey reports for underwriters are to be concluded with a phrase indicating that the report is subject to adjustment."

I might add, and as I understand it, these instructions were not the product of the senior officers of U.S. Salvage Association, but rather were promulgated by members of the U.S. Hull Syndicate, claims examiners, Underwriters and also their attorneys.

Apparently, the thrust of all of this was to make every effort to provide information to allow the adjustors and the Underwriters to agree on what is claimable within the policy conditions.

It seems now that Underwriters have delegated at least part of the adjustors functions to their surveyors. In our opinion, this is regrettable but we certainly hope not irreversible.