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Admiralty law: LOLA litigation and a long overdue small-passenger-vessel exception

FOR INJURIES ON A SMALL VESSEL, SUCH AS A SUNSET HARBOR CRUISE, THE LIMITATION OF LIABILITY ACT (LOLA) CAN BE YOUR ENEMY, BUT NOW THERE'S HOPE

Imagine your client was seriously injured during a sunset harbor cruise on a small boat carrying about 50 passengers. Your client is undergoing medical treatment, and as usual, you've identified an insurer and sent your letter of representation to an adjuster. You've also discovered the boat owner carries a $2 million liability policy.

Within a few months, while waiting for your client to complete treatment before sending out a policy limit demand letter, you unexpectedly receive a "Notice of Complaint." After examining this unusual pleading, you realize your client is being sued in federal court by the boat owner who seeks to be exonerated from liability, or alternatively, to have its liability limited to the value of the vessel and its freight which is declared to be $300,000. You also realize that the federal judge issued an order enjoining you from filing a lawsuit in state court and requiring you to respond to the federal complaint within 30 days or else be defaulted and forever barred from any recovery. Could all this be true, you may ask in disbelief? The answer is, yes.

The boat owner's right to hale your injured client into federal court and to seek to limit its liability stems from an antiquated law originating in 1851. (The Limitation of Liability Act ("LOLA") 46 U.S.C. sections 30501 et seq., of which sections 30503 through 30512 are now redesignated as sections 30521 through 30530, respectively, James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, PL 117-263, December 23, 2022, 136 Stat 2395, Section 11503.)

The LOLA history

One hundred seventy-two-years ago, LOLA was enacted to encourage investment in the then-growing international maritime industry, protect the shipbuilding industry in the United States and place American shipowners on the same competitive ground as their foreign counterparts. (*Lewis v. Lewis & Clark Marine, Inc.* (2001) 531 U.S. 438, 446-447 [121 S.Ct. 993, 1000, 148 L. Ed.2d 931].) It allows a vessel owner to seek exoneration from liability, or alternatively, if liability is found, to limit damages to the value of the vessel and its freight *after* the damage-causing incident.

Limitation of liability is allowed when the damages are "done, occasioned, or incurred, without the privity or knowledge of the owner." (46 U.S.C. 30505 redesignated to 30523.) In the 1800s, vessel owners sending a ship to sea on an international voyage was quite risky. Vessel owners had no means of communicating with the ship in real time, no means to monitor the vessel's operations or its movement at sea and had to hope that their ship and its cargo or passengers safely arrived at its intended destination.

Under these circumstances, in an effort to incentivize ongoing maritime activities, vessel owners were provided with protection against liability in excess of any remaining value in the vessel, if they had no knowledge of negligent acts or conditions of unseaworthiness of the vessel that ultimately caused the casualty and resulting damages. Under this limitation-of-liability scheme, the vessel owner was able to protect other business assets and only put at risk the seagoing vessel itself.

LOLA has lost its purpose

While the LOLA may have had some justifiable origins, its reasoning has not held water for a long time. In today's modern maritime industry, with the advent of advanced marine technology, instant communication systems, radars, and satellite systems, as well as ample insurance protection (usually as Protection and Indemnity insurance offered by a P&I Club), the LOLA has lost it purpose and usefulness. Yet, the LOLA is routinely used by vessel owners who are well protected with substantial insurance coverage, to limit their liability and avoid paying victims just compensation. P&I Club contracts contain a standard clause called "pay to be paid rule" which obligates the insured to first pay the injured claimant before seeking indemnity from the P&I Club. As such, P&I Club benefits from encouraging vessel owners to file LOLA actions that could be used as leverage in the litigation.

This outdated law has been highly criticized as archaic, especially because it is being unjustly used in cases involving small vessels, pleasure boats, and even jet skis. (See e.g., *Matter of Hechinger* (9th Cir. 1989) 890 F.2d 202, 206 [applying LOLA to non-commercial pleasure boat]; *Keys /Jet Ski, Inc. v. Kays* (11th Cir. 1990) 893 F.2d 1225 [applying LOLA to a jet ski accident].)

While LOLA was never intended to benefit recreational or small-vessel operators who are not involved in international commerce, most vessels were swept into the Act by its expansive definition. Section 30502 of title 46 of the United States Code defined the Act to apply to "seagoing vessels and vessels used on lakes or rivers or in inland navigation, including canal boats, barges, and lighters." Thankfully, recent, long overdue legislative changes have brought some much-needed relief.

A new exception for small passenger vessels

In 1989, the Ninth Circuit recognized that "The Liability Act provides shipowners a generous measure of protection not available to any other enterprise in our society. Many have suggested that the Act, a relic of an earlier era, provides protections that are neither warranted nor consistent with current

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reality. . . .With the availability of incorporation, insurance and other devices to protect shipowners against major disasters, the Liability Act seems oddly out of place in the modern economy; its application could well lead to wholly unexpected and harsh results. . . Congress might be well advised to examine other approaches or to consider whether the rationale underlying the Liability Act continues to have vitality as we enter the last decade of the twentieth century." (*Esta Later Charters, Inc. v. Ignacio* (9th Cir. 1989) 875 F.2d 234, 239.)

Thirty-three years later, after several failed efforts to change the LOLA, Congress finally acted in the face of public outcry stemming from the horrific and tragic loss of life in the M/V Conception dive boat incident. On September 2, 2019, the 75-foot, 97 gross ton vessel with 99 (or 49 overnight) passenger capacity, caught fire, killing all 33 passengers and one of its six crewmembers and sank off the coast of Santa Cruz Island, California. (NTSB Marine Accident Report NTSB/MAR-20/03 available at https://www.ntsb.gov/investigations/Pages/DCA19MM047.aspx.)

The vessel owner filed a LOLA action seeking to limit the recovery of all victims to the value of the vessel after the incident, which effectively was zero. This unjust and cruel prospect led Congress to amend LOLA to exempt a limited segment of maritime casualties involving small passenger vessels from its application. Unfortunately, the amendments to LOLA are not retroactive, and will be of no help to the M/V Conception victims.

Under the amendments, signed by President Biden as part of the James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, "covered small passenger vessels" are excluded from the application of LOLA (46 U.S.C. § 30502.) The exempted vessels are small passenger vessels as defined in section 2101of title 46 of the United States Code, which includes vessels of less than 100 gross tons carrying more than six passengers, and as provided in the new amendment to section 30501 of title 46 of the United States Code, limiting the exemption to vessels carrying no more than 49 passengers on an overnight domestic voyage and not more than 150 passengers on any voyage that is not an overnight domestic voyage. The definition also includes any wooden vessel constructed prior to March 11, 1996, and carrying at least one passenger for hire. (PL 117-263, December 23, 2022, 136 Stat 2395, Section 11503.)

The new legislation also amends section 30508 of title 46 of the United States Code (redesignated as 30526) which now prohibits owners of covered small passenger vessels from contractually limiting the time to give notice of a claim or to file a lawsuit involving a personal injury or death to less than two years after the date of injury or death.

While the new amendments to the LOLA are welcomed, they are not retroactive and do not apply to vessels that do not qualify as "covered small passenger vessels." As such, if a LOLA action has been filed, it is very important to act quickly in response.

LOLA litigation – what you must know

Initiating the action

The procedures for a limitation action are governed by section 30511 of title 46 of the United States Code (redesignated 30529) and the Supplemental Admiralty and Maritime Claims Rule F of the Federal Rules of Civil Procedure. A vessel owner or an owner pro hac vice (the party chartering and operating the vessel at its own expense) (46 U.S.C. § 30501) can initiate a LOLA action by filing a complaint for exoneration or limitation of liability in federal court.

The action must be filed in the district where a state court case is pending, or if no state action has been filed, where the vessel can be found. (FRCP SUPP AMC Rule F(9).) The filing is done concurrently with providing a declaration as to the value of the vessel from a marine surveyor or an insurance adjuster and depositing with the court the value of the owner's interest in the vessel and pending freight or an alternative approved security.

This security creates the "limitation fund" from which prevailing claimants can be paid pro rata. Most commonly, vessel owners provide a letter of undertaking from their insurer or an Ad Interim Stipulation as to the value of the vessel providing an assurance that the vessel's insurer will pay up to the value of the vessel in the action should the court find payment is due. The vessel owner will also submit proposed orders to the court to approve the value of the vessel, a proposed notice of the complaint and a proposed order enjoining all suits arising out of the subject incident.

If the complaint follows the requirements of Rule F and proper security is provided, the court will issue an injunction that stays all pending claims and enjoin the further prosecution against the vessel owner or its property with respect to the claims. The court will set a "monition" period which provides the time period for all claimants to file their claims in the limitation action or be defaulted. This process, called a "concursus," is similar to bankruptcy proceedings, in that all claimants are forced to come into the federal limitation action and file their claims, so that if limitation is ultimately allowed, the court sitting without a jury then adjudicates the claims and distributes the funds among the claimants. The court will also issue an approved notice to claimants, which the vessel owner must publish and provide to known claimants regarding the details of making a claim.

Time limitations on filings

Notably, the limitation action must be brought within six months after a claimant gives the owner written notice of a claim. (46 U.S.C. § 30511 (redesignated 30529) and FRCP SUPP AMC Rule F(1).) This is an important requirement that has been the subject of numerous cases and can be used to defeat an untimely

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limitation action. Some federal courts have held the six-month period is jurisdictional and will oust the court's jurisdiction to decide an untimely action. The Ninth Circuit, in a case of first impression in the circuit, however, has recently held that the time limit is an ordinary statute of limitations and is not jurisdictional, and therefore, a claimant may raise the issue as an affirmative defense to be decided on a motion for summary judgment. (*Martz v. Horazdovsky* (9th Cir. 2022) 33 F.4th 1157.)

The written notice does not require any formality and can simply be a letter to the vessel owner, or a series of letters or communications. (*Id.* at 1164.) However, the communication must: a) convey that a demand for compensation is being made against the owner of the vessel, i.e., an actual intent to initiate a claim, not simply imply it or hint at a possibility of asserting a claim, and b) assert the type of claim for which the owner may seek limitation such as one exceeding the value of the vessel. (*Id*. at 1165.) The *Martz* case departed from other Circuit decisions where notice of a "potential" claim was deemed sufficient. It held that a letter that did not state an intent to seek recovery from the vessel owner, even though it outlined a theory of liability was insufficient to start the statute of limitation period, as was a preservation of evidence letter that noted investigation was ongoing. (*Id.* at 1167-68.) This case illustrates the importance of drafting a proper notice of claim letter, and not merely sending a typical letter of representation. If a proper notice letter is sent to the vessel owner or its authorized agent (such as an insurance adjuster, see e.g., *Doxsee Sea Clam Co., Inc. v. Brown* (2d Cir. 1994) 13 F.3d 550, 554), an untimely LOLA action can be defeated.

Claimant's response

Any claimant seeking to recover against the limitation fund must file a claim with the federal court within the time prescribed by the court's order. (FRCP SUPP AMC Rule F(5).) A claim is similar to filing a complaint with appropriate counts or causes of action against the vessel owner and the facts supporting the claim for damages. Filing a claim alone, simply seeks recovery from the limitation fund.

However, if one wishes to contest the vessel owner's right to exoneration or limitation of liability, an answer must also be filed responding to the allegations in the vessel owner's complaint and asserting appropriate affirmative defenses. Claimants usually file a single pleading containing the claim and answer, and if appropriate, also a third-party complaint against other third-party defendants.

The vessel owner thereafter files an answer to the claims filed and the matter proceeds as any other federal action, with the caveat, that the action is tried by the judge without a jury. A LOLA action is considered an admiralty proceeding and therefore a jury is unavailable, unless an advisory jury is allowed under rule 39(c) of the Federal Rules of Civil Procedure.

Returning to state court

In a LOLA action, a claimant can proceed with the case in the federal court, or seek to return to state court based on a few limited exceptions. The unavailability of a jury trial and federal procedures often make litigating the claims in federal courts less desirable.

Courts have recognized that there is a conflict between the vessel owner's rights under the LOLA to bring an action to determine limitation of its liability exclusively in federal court on the one hand, and the Saving to Suitors Clause (28 U.S.C. § 1333) preserving to claimants the rights to proceed with claims in state court before a jury on the other. (*Lewis*, *supra* 531 U.S. at 452.) To balance these opposing interests, courts have created exceptions that allow claimants to adjudicate claims in state court before a jury while preserving the vessel owner's right to seek limitation of liability in federal court.

Three recognized exceptions are: 1) the multiple claimant sufficient fund, 2) the single-claimant insufficient fund, and 3) the multiple-claimants insufficient fund. (See e.g., *Newton v. Shipman* (9th Cir. 1983) 718 F.2d 959, 962; *Beiswenger Enterprises Corp. v. Carletta* (11th Cir. 1996) 86 F.3d 1032, 1038-39.) With the multiple claimants sufficient funds situation, the limitation fund exceeds the value of all claims, and therefore a pro rata distribution is not necessary and claimants are therefore allowed to proceed with their individual claims in their chosen forum with a jury.

The single-claimant insufficient fund exception is based on the rationale that no other claimants will be competing for the same limitation fund. Therefore, a court can dissolve the injunction and permit the claimant to proceed in state court to adjudicate his or her claims and obtain a jury verdict, as long as the claimant agrees to protect the vessel owner's interests that must be exclusively decided by the federal court.

This is accomplished by the claimant providing certain stipulations, including that: 1) the value of the limitation fund equals the value of the vessel and its freight (cargo or passenger fares), 2) the claimant waives the right to claim res judicata based on any judgment rendered against the vessel owner outside of the limitation proceedings; and 3) the district court will have exclusive jurisdiction to determine limitation of liability issues. (*Newton*, *supra* 718 F.2d at 962.) If the claimant offers these stipulations, the court must dissolve the injunction, unless the vessel owner shows that its right to limit liability will be prejudiced. (*In re Williams Sports Rentals, Inc.* (9th Cir. 2019) 770 Fed.Appx. 391, 392.)

The third exception arises where there are multiple claimants whose claims exceed the value of the limitation fund; however, with proper stipulations they effectively convert their claims to a single claimant exception. This is accomplished by an agreement of all claimants as to the priority of their claims and entering stipulations similar to the one a single claimant would offer. By setting forth the priority of claims, if limitation of liability is appropriate, the court can distribute

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funds according to the agreed priorities and thereby eliminate the need for a concursus proceeding.

Where proper stipulations are offered that protect the vessel owner's interests in the limitation action, the court has the discretion to stay or dismiss the LOLA action. (*Lewis*, *supra*, 531 U.S. at 454.) The Ninth Circuit has noted that most often, "it has been found expedient to stay the limitation proceeding and try the liability issue first, thus preserving the possibility that a jury will find no liability or award less than the limitation fund and thereby moot the limitation proceeding." (*Newton*, *supra* 718 F.2d at 963.)

Limitation proceedings in federal court

From a practical standpoint, when cases are litigated in state court pursuant to one of the noted exceptions, they are often resolved in the state court proceeding. However, if the claims remained in federal court in the first instance or were litigated in state court with a finding of liability and damages exceeding the limitation fund, then the federal court must make final determinations as to the vessel owner's right to exoneration or limitation of liability. The state court's finding will not be binding based on the agreement to waive the res judicata defense in order to protect the vessel owner's rights.

If a claimant establishes negligence on the vessel owner's part, the burden shifts to the vessel owner to show there was no privity or knowledge of the negligent acts or unseaworthy conditions at issue. Passengers on vessel are not entitled to the warranty of seaworthiness, however, a showing of unseaworthiness can be used to shift the burden of proof to the vessel owner, even though any recovery of damages would have to be based on a negligence theory. (*In re Hyatt Corp.* (D. Hawaii 2009) 262 F.R.D. 538, 546.)

Privity or knowledge includes actual or constructive knowledge; therefore, courts have held that the owner must prove more than just the lack of actual knowledge but that it availed itself to information that was reasonably available to prevent the claimed losses. (*Washington State Dept. of Transp. v. Sea Coast Towing Inc.* (9th Cir. 2005) 148 Fed.Appx. 612, 613-614.) A vessel owner therefore must establish that it did not participate in the negligent act and did not know or should not have known of any negligent act or unseaworthy condition causing the claimed losses.

If the vessel owner is successful in showing the absence of privity and knowledge, the owner may limit its liability to the value of the vessel and the court will distribute funds pro rata among the claimants. (*Newton*, *supra* 718 F.2d at 961.) If the vessel owner is unsuccessful, limitation of liability will be denied, and claimants may recover their full damages.

If claimant cannot establish negligence in the first instance, the vessel owner would be entitled to complete exoneration of liability.

Conclusion

Limitation of liability actions are harsh and unnecessary in today's maritime industry. They are used primarily as a leverage against legitimate claims and often create needless proceedings in instances that clearly would not entitle a vessel owner to limitation. Given the short time period to respond to a LOLA complaint, attorneys need to take any notice of such action seriously and file timely claims to avoid default, or if needed, seek the assistance of a maritime practitioner familiar with such actions.

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