

2005

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Recommended Citation

Guy H. Riddle, *Aviation Insurance Coverage Issues Beware the Renter Pilot*, 70 J. AIR L. & COM. 407 (2005)
<https://scholar.smu.edu/jalc/vol70/iss3/3>

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AVIATION INSURANCE COVERAGE ISSUES “BEWARE THE RENTER PILOT”

GUY H. RIDDLE

I. INTRODUCTION

ASIDE FROM THE many obvious pitfalls that owners of light aircraft face—i.e. the expenses associated with operation and maintenance, violations of unknown FAA regulations, and operational and mechanical failures while in flight—they also face less obvious, or quite frequently ignored, pitfalls pertaining to the insurance coverage provided by the aviation policies covering their aircraft. One frequently ignored, or unsuspected, pitfall deals with whether the aircraft owner’s aviation policy will cover claims for hull loss and/or liability arising out of the crash of the owner’s aircraft while being rented, chartered and/or used without authorization. This paper will address some of the issues and case law associated with light aircraft owners renting and/or chartering their aircraft in violation of their insurance policies, as well as coverage for unauthorized use.

II. INSURANCE COVERAGE DEFENSES

Many aircraft owners who have “Pleasure and Business Use” policies, also known as “Non-Commercial Use” policies, rent their aircraft to friends, acquaintances, and strangers to deflect some of the indirect costs of owning and maintaining their aircraft. However, unless the insurance policy covers such rentals, the owners and their renter-pilots may find themselves without coverage for the loss of the aircraft and/or liability (defense and indemnity) coverage when the aircraft is involved in an accident. In light of the catastrophic nature of aviation accidents, this could have serious financial consequences for the insured owner, the renter-pilot, and/or their respective estates.

In connection with excluded use for rental and/or charter of aircraft under Pleasure and Business policies, insurance carriers have several defenses to providing coverage, including: (i)

fraud/misrepresentation in the insurance application; (ii) "commercial use" exclusion; (iii) renter-pilot exclusion; and (iv) conversion exclusion.¹

A. FRAUD / MATERIAL MISREPRESENTATION IN APPLICATION

Like most insurance policies, aviation policies require insureds to provide truthful information in their insurance applications.² Most policies explicitly void the coverage in the case of fraud, attempted fraud, false swearing, or misrepresentation of any material fact or circumstance in connection with the insurance policy.³ Each insurance carrier has its own application form that should clearly describe that the policy is for pleasure and business use (non-commercial)⁴ or request information regarding the prospective insured's intent to charter or rent the aircraft.

Although most insureds complete policy applications truthfully, many, either knowingly or unwittingly, do not provide accurate information regarding the intended use of the aircraft. In the case of the unwitting prospective insured, a mistaken material misrepresentation, *at least under Texas law*, will not void the policy.⁵ However, in the case of an insured who knowingly provides inaccurate information to avoid paying higher insurance premiums associated with renting or chartering his or her aircraft, the policy is likely void *ab initio*.

The claim investigation may reveal that the insured intended all along to use the aircraft outside the parameters of a Pleasure and Business Use policy. Typical evidence of such intent may

¹ See, e.g., 45 C.J.S. *Insurance* § 777 (2005).

² 45 C.J.S. *Insurance* § 770 (2005).

³ *Id.*

⁴ Non Commercial Business Use typically does not provide coverage for Flights that result in a "charge."

⁵ It is well established Texas law that an insurer may invalidate a policy of insurance on the basis of the insured's misrepresentations in the insurance application *only* if the insurer can successfully plead and prove the following five elements: (1) the making of the representation; (2) the falsity of the representation; (3) reliance thereon by the insurer; (4) the intent to deceive on the part of the insured in making same; and (5) the materiality of the representation. *Albany Ins. Co. v. Anh Thi Kiev*, 927 F.2d 822, 891 (5th Cir. 1991) (citing *Mayes v. Mass. Mut. Life Ins. Co.*, 608 S.W.2d 612, 616 (Tex. 1980); *S. Life & Health Ins. Co. v. Medrano*, 698 S.W.2d 457, 461 (Tex. App.—Corpus Christi 1985, writ ref'd n.r.e.)). The insurer must prove that the insured made some material misrepresentation, willfully and with design to deceive or defraud the insurer. *Id.* (citing *Soto v. S. Life & Health Ins. Co.*, 776 S.W.2d 752, 756 (Tex. App.—Corpus Christi 1989, no writ)).

include ownership in a Part 135 operation, previous rental or charter of the subject aircraft, and/or correspondence detailing intended uses of the aircraft that predates the completion of the insurance application. If such evidence is adduced during the claim investigation, an insurance carrier may rely on the avoidance language in the policy to deny coverage of any claim, including hull loss and liability, arising out of an aviation accident. Although an insured's fraud or misrepresentation may be a viable defense to coverage when the aircraft is rented or chartered in violation of the policy, the theory is often not effective because the insurer is required to show the insured's subjective intent to deceive.

B. "COMMERCIAL USE" EXCLUSION

The more common method for excluding coverage to an insured who rents or charters an aircraft in violation of a Pleasure and Business policy is to rely on the stated use of the aircraft as set forth in the policy's declarations, along with the policy's definition of "non-commercial" or "pleasure and business."⁶ The typical Pleasure and Business policy will provide coverage for use in the insured's business, including personal and pleasure uses, but it will exclude coverage for hire or reward.⁷ Today, most Pleasure and Business policies extend coverage where payments are made to cover the direct cost of a flight, including, fuel, oil, and insurance and hangar expenses involved with the particular flight.⁸ However, if a payment includes indirect operating expenses, it is likely that the flight will not be covered.⁹

Texas, as well as other jurisdictions, has long embraced the exclusion of rental use in aircraft policies.¹⁰ Any charge exceed-

⁶ *Pac. Indem. Co. v. ACEL Delivery Serv. Inc.*, 485 F.2d 1169, 1172 (5th Cir. 1973).

⁷ *Id.*

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.* at 1169 (Finding that a \$10.00 an hour assesment for use of aircraft over and above cost of fuel constituted a charge, and as such, accident was not within coverage of the policy) (emphasis added); *Monarch Ins. Co. v. Siegel*, 625 F. Supp. 693 (N.D. Ind. 1986) (holding payment including amount beyond operating costs were charges constituting "rental use" which fell outside of the "Pleasure and Business" limitation of the policy); *Kohler v. Proprietors Ins. Co.*, 394 So. 2d 463 (Fla. Dist. Ct. App. 1981) (holding that insured could not recover for aircraft hull and liability policy that excluded from coverage any operation of aircraft for which a charge was made even though the required charge was being paid to third party charitable organization); *Flagstaff Mortuary, Inc. v. Gamble*, 662 P.2d 149, 151 (Ariz. Ct. App. 1988); *Avemco Ins. Co. v. Auburn Flying Serv. Inc.*, 242

ing the direct operating cost of the aircraft constitutes a flight for which a charge was made.¹¹ In *Pacific Indemnity Co. v. ACEL Delivery Service, Inc.*, the insureds sought a declaratory judgment that coverage existed for liability claims filed by the estates of two passengers who died when the insured's aircraft crashed.¹² The policy's stated use was for "pleasure and business," which it defined as "[p]ersonal, pleasure, family and business uses excluding an operation for which a charge is made."¹³ The issue before the Fifth Circuit was whether a \$10.00-per hour charge, in addition to the cost of fuel and storage, constituted a "charge" within the policy exclusion.¹⁴ The appellees (the insureds) argued that the term "charge" meant "profit" and that the reimbursement of expenses was not a "charge" as defined by the meaning of the policy.¹⁵ The insureds introduced evidence that the \$10.00-per hour assessment would barely cover the aircraft's expenses, and that the average rental of a similar aircraft was \$25.00- to \$35.00- per hour.¹⁶ Despite the evidence that the charge would not make the value "profitable," the court held that the appropriate standard for determining whether a charge was made depended on the motivation for making the flight.¹⁷ The pilot also gave an \$84.00 check to the owner and operator of the flying service for the use of the aircraft.¹⁸ The court found the payment of \$84.00 was not a voluntary gesture, but was a motivating factor and prerequisite to the flight taking place, and thus, the charge fell within the meaning of the policy.¹⁹ The Fifth Circuit also upheld the district court's findings based on its determination that the \$10.00-per hour charge was beyond those allowed under the narrowly defined charges in the policy.²⁰

In *Monarch Insurance Co. of Ohio v. Siegel*, the United States District Court for the Northern District of Indiana granted a mo-

F.3d 819, 825 (8th Cir. 2001) (charging a \$10.00 fee for a ride in an airplane during a "fly-in" was a quid pro quo exchange for which a charge was made, and as such, was not covered by the policy).

¹¹ *Pac. Indem. Co.*, 485 F.2d at 1169.

¹² *Id.* at 1170.

¹³ *Id.* at 1172.

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.*

tion for summary judgment in favor of Monarch.²¹ The court held that the aviation insurance policy did not provide liability or hull loss coverage where the pilot agreed to pay the owner of the aircraft \$46.00-per hour to use the aircraft, in addition to direct operating costs of gas and oil.²² In *Monarch*, the policy was issued for "pleasure and business."²³ The policy defined pleasure and business as "personal and pleasure use in direct connection with the insured's business, excluding any operation for which a charge is made."²⁴ The owner of the aircraft admitted in his deposition that the \$46.00-per hour charge was designed to cover the maintenance reserve for the plane and the cost of annual inspections.²⁵ The court found that the expenses were not "direct" operating expenses.²⁶

In *Kohler v. Proprietors Insurance Co.*, the Third District Florida Court of Appeals upheld a summary judgment in favor of Proprietor's Insurance Co. ("Proprietor's"), finding that it did not owe its insured for a hull loss claim when the aircraft was seized by Colombian authorities.²⁷ The court held that the \$125.00-per hour payment for use of the plane was a charge because the payment was a prerequisite to the use of the plane, not a gratuitous reimbursement of flight expenses.²⁸ The court further noted that, even though the charge was to be paid to a third-party charitable organization, the status of the payee did not have any effect on the decision-calculus of whether the payment constituted a charge under the policy.²⁹

In *Avemco Insurance Co. v. Auburn Flying Service, Inc.*, an insurer of a non-commercial aviation liability policy sought a declaratory judgment against the personal representative of the deceased pilot after an accident.³⁰ Avemco alleged that the commercial purpose exclusion applied to the crash, because it occurred while the pilot was giving rides in exchange for a fee.³¹ The passengers paid \$10.00 for a ten- to fifteen-minute airplane

²¹ 625 F. Supp. 693.

²² *Id.* at 699-700.

²³ *Id.* at 696.

²⁴ *Id.* at 699.

²⁵ *Id.*

²⁶ *Id.*

²⁷ 394 So. 2d 463, 464 (Fla. Dist. Ct. App. 1981).

²⁸ *Id.*

²⁹ *Id.*

³⁰ 242 F.3d 819.

³¹ *Id.* at 821.

ride.³² On the ninth trip of the day, while attempting to land, the plane struck a passing truck and crashed.³³ Everyone on the plane died in the crash.³⁴ The Eighth Circuit affirmed the district court's summary judgment on the ground that there was no coverage for the fatal flight.³⁵

The insurance policy contained the following exclusion of coverage: "This policy does not cover bodily injury, property damage, or loss . . . [w]hen your insured aircraft is . . . used for a commercial purpose." The policy also contained the following definition: "'Commercial purpose' means any use of your insured aircraft for which an insured person receives, or intends to receive, money or other benefits. It does not include: the equal sharing among occupants of the operating cost of the flight."³⁶

The Eighth Circuit, after distinguishing other "for a charge" cases, held that the policy language was not ambiguous.³⁷ In reaching its conclusion, the court considered the general purpose for the exclusionary clause.³⁸ The court found that the exclusionary language of the policy limited risk by removing the motivation to make flights because the policy holder received payment.³⁹ The court analyzed four factors in determining whether the fee was a shared expense or a simple receipt of money: (i) the relationship of the amount paid to the expenses of a flight; (ii) the existence of a community of interest in taking the flight, other than the flight itself; (iii) the voluntariness of the payment; and (4) any indication of a *quid pro quo*.⁴⁰

Even though the \$10.00 payment was not enough to cover all expenses of the flight, the court found that the exchange constituted a payment rather than equally shared expenses.⁴¹ In arriving at this conclusion, the court looked at the depositions of the other passengers.⁴² The deposition testimony showed the lack of an agreement to share expenses.⁴³ The deposition testimony

³² *Id.*

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.* at 826.

³⁶ *Id.* at 821.

³⁷ *Id.* at 822.

³⁸ *Id.* at 823.

³⁹ *Id.*

⁴⁰ *Id.* at 824.

⁴¹ *Id.* at 825.

⁴² *Id.* at 825-26.

⁴³ *Id.* at 825.

also showed that at no time did the agreement state that the \$10.00 amount was only for expenses.⁴⁴ The court held that the pilot and his passengers “possessed no community of interest other than just taking the flight itself.”⁴⁵ The court also found that by advertising flights for \$10.00 and providing the flights in conjunction with the event, the pilot was providing a flight service to the general public.⁴⁶ The court then distinguished the conduct in the case from taking family or friends on joy rides.⁴⁷ In concluding, the court stated “[b]y offering flights to anyone willing to pay the fee, [the pilot] increased the number of flights he would make with the plane, and increased the risk to the insurer beyond that contemplated in the insurance contract. Consequently, the flight in question was for the receipt of money and was not an equal sharing of expenses.”⁴⁸

In *General Insurance Co. (SAFECO) v. Flanco Leasing, Inc.*, the Arkansas Court of Appeals reversed and remanded a summary judgment in favor of the insureds, Flanco and CCT, against the insurer, General Insurance (“SAFECO”), for the agreed value of the hull of an aircraft plus a twelve-percent penalty and attorneys’ fees.⁴⁹ In the case, SAFECO denied the insured’s claim for the value of the hull.⁵⁰ SAFECO argued that, at the time of the crash, the aircraft was not being used for its stated purpose of “industrial aid.”⁵¹ The policy defined “industrial aid” as “personal, pleasure, family and business uses and transportation of executives, employees, guests and customers, excluding any operation for which a charge is made other than the sharing or reimbursement of direct operating expenses incurred for the flight.”⁵² In reversing the summary judgment, the court noted that a \$75.00-per hour fee was generally assessed against passengers who used the aircraft.⁵³ The court also noted that the pilot acknowledged receiving payment from the deceased passenger on previous flights and that he had been censured by the FAA for doing so.⁵⁴ Additionally, the owner of the plane acknowl-

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.* at 826.

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ No. CA 95-775, 1996 WL 494650 (Ark. App. Aug. 28, 1996).

⁵⁰ *Id.* at *2.

⁵¹ *Id.*

⁵² *Id.*

⁵³ *Id.* at *3-4.

⁵⁴ *Id.* at *2-4.

edged under oath that he engaged in conversations about the use of the aircraft for charter purposes and provided invoices that showed that the aircraft had been used for profit on previous occasions.⁵⁵ The court found this evidence enough to raise a question of fact sufficient to overcome the motion for summary judgment.⁵⁶

In *Flagstaff Mortuary, Inc. v. Gamble*, the appellee sued his insurance agent for failing to provide a new insurance policy identical to a second policy.⁵⁷ The trial court granted the insurance agency's motion for summary judgment.⁵⁸ The court found that an agent is not liable for failing to procure a second identical policy where coverage would be excluded under the original policy.⁵⁹ The suit arose from a crash of a Flagstaff Mortuary aircraft.⁶⁰ Before the accident, the pilot promised to pay \$100.00 to use the aircraft.⁶¹ On the second leg of a round-trip flight between Flagstaff and Phoenix, the aircraft crashed and sustained severe hull damage.⁶² The Arizona Court of Appeals upheld summary judgment in the insurer's favor, because the payment was a charge within the meaning of the policy exclusion.⁶³ The appellate court held, as a matter of law, that the policy exclusion applied because the payment was for more than the direct operating cost of the flight.⁶⁴ In fact, the evidence showed that the \$100.00 payment for the flight far exceeded the anticipated costs and nearly matched the hourly rate for the commercial rental of the aircraft.⁶⁵ The court concluded that the \$100.00 payment was intended to reimburse the plaintiff for indirect costs of operation, including maintenance.⁶⁶

In *Ferro Corp. v. Aviation Insurance Managers, Inc.*, the Tennessee Court of Appeals affirmed the trial court's ruling that Ferro,

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ 662 P.2d 149 (Ariz. Ct. App. 1983).

⁵⁸ *Id.* at 150.

⁵⁹ *Id.* at 152.

⁶⁰ *Id.* at 150.

⁶¹ *Id.*

⁶² *Id.* at 151.

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ *Id.* at 152. The evidence further showed that a round-trip flight between Flagstaff and Phoenix takes approximately one hour and twenty-four minutes and that the cost of fuel for this flight was approximately \$20. *Id.* The evidence also showed that an identical plane would have rented out for \$75 an hour plus fuel. *Id.*

⁶⁶ *Id.*

a previous lessee and a named insured under an aviation liability policy, was not entitled to avoid liability arising out of the crash of an aircraft and death of its occupants.⁶⁷ At the time of the crash, Abernathy Auto Parts ("Abernathy") owned the plane but Ferro controlled the plane under an oral rental agreement.⁶⁸ Ferro was permitted to rent the aircraft at any time for a \$35.00-per hour charge.⁶⁹ Originally, Ferro and Abernathy had a written lease agreement that listed Ferro as an additional named insured under Abernathy's aviation insurance policy.⁷⁰ However, prior to the flight, Ferro requested to be removed from the insurance policy and sought reimbursement for the unused premium.⁷¹ Even though Ferro never received a premium reimbursement, the trial court held that, at the time of the crash, Ferro was no longer an insured under the policy.⁷² The court further found that because Ferro paid \$35.00-per hour for the use of the aircraft, the plane was not used for "industrial aid" by an insured.⁷³ Thus, the defendant owed no duty to defend or provide coverage to Ferro under the policy.⁷⁴

In *Smith v. Ranger Insurance Co.*, the Third Circuit Louisiana Court of Appeals affirmed a judgment against Ranger on an action for liability and hull loss coverage arising out of the crash of an insured's airplane.⁷⁵ Ranger denied coverage on the ground that the flight was a "charter" flight and not covered under the limited commercial use policy.⁷⁶ The policy defined "Limited Commercial use" as including pleasure and business, industrial aid, student instruction and rental to pilots, but excluding passenger, carrying for hire or reward.⁷⁷ The Court of Appeals affirmed, due to conflicting evidence as to whether the price terms were certain and determinant, as required by the Louisiana Civil Codes.⁷⁸

In *United States Fire Insurance Co. v. Cowley & Associates*, an insurer brought a declaratory judgment action, seeking to avoid

⁶⁷ 462 S.W.2d 523 (Tenn. Ct. App. 1970).

⁶⁸ *Id.* at 525.

⁶⁹ *Id.*

⁷⁰ *Id.* at 524.

⁷¹ *Id.* at 525.

⁷² *Id.* at 529.

⁷³ *Id.* at 532.

⁷⁴ *Id.*

⁷⁵ 301 So. 2d 673 (La. Ct. App. 1974).

⁷⁶ *Id.* at 674-75.

⁷⁷ *Id.* at 674.

⁷⁸ *Id.* at 676.

liability claims filed under the policy.⁷⁹ The policy provided for personal and pleasure use, as well as use in direct connection with the insured's business, but excluded coverage for any flight operation for which a charge was made.⁸⁰ The owner allowed the independent contractor pilot to fly the plane for business endeavors.⁸¹ Because the flight was for the pilot's business, the insurer alleged the flight was part of a "charter."⁸² The Georgia Court of Appeals affirmed the finding against the insurer and stated:

[s]ince all of the passengers died in the crash, none was available to testify whether or not arrangements had been made for payment for the flight. There were no invoices, memos, bills, pre-flight charges, or other documents or testimony evidencing a charge made by McConnell for the flight or the intention of the passengers to pay any amount to McConnell for the flight. In his deposition Cowley testified that he did not make and has not made a charge relative to the operation of his plane on the fatal flight; that using the plane as a charter for profit was strictly prohibited; and that it was never used in that way as far as he knew. Cowley further testified that McConnell had his own construction management company and was an architect with a substantial engineering background, and that he allowed McConnell to use the plane for McConnell's architectural, engineering, draftsman, and construction management work. Cowley said he did not receive cash reimbursements for allowing McConnell to use the plane; instead, McConnell repaid him by piloting him free of charge.⁸³

The Court further held that the insurer's only evidence was an implication that McConnell would charge for the flight because he had done so in the past.⁸⁴ The court concluded that U.S. Fire did not meet its burden to affirmatively show that a charge was made for the flight, and as such, summary judgment was appropriate.⁸⁵

In *Houston Fire & Casualty Insurance Co. v. Ivens*, the Fifth Circuit Court of Appeals affirmed summary judgment in favor of an insured against Houston Fire in its declaratory judgment ac-

⁷⁹ 359 S.E.2d 160, 161 (Ga. Ct. App. 1987).

⁸⁰ *Id.*

⁸¹ *Id.*

⁸² *Id.*

⁸³ *Id.* at 162.

⁸⁴ *Id.* at 163.

⁸⁵ *Id.*

tion.⁸⁶ Houston Fire sought determination that it was not liable under its policy for the deaths of the passengers on the aircraft.⁸⁷ The policy in question was classified as a Pleasure and Business Use policy.⁸⁸ The Court evaluated a charge as “the price demanded for a thing or service,” and held that the \$60.00 contribution was not a charge but a gratuitous offer to defray gas costs.⁸⁹ The Court stated:

It is clear on the record that Ivens and Fletcher had planned the flight independently and before Ulsch knew anything about it, and that Ulsch had nothing to say about when or how the flight would to be made. The agreement of Ulsch to contribute \$60.00 toward payment of the cost of gasoline was a voluntary gesture on his part, based upon his feeling that this was the fair thing for the Company to do . . . There was no obligation on the part of Ulsch or on the part of the Company to provide Fletcher with transportation to Knoxville to pick up the equipment.⁹⁰

C. RENTER PILOT EXCLUDED AS “INSURED”

Another concern that arises with aircraft rental is the coverage provided to the renter-pilot. “Limited Commercial” policies permit rental pilot use of the aircraft; however, this does not always mean that the renter pilot will be an “insured” for purposes of liability coverage.⁹¹ Several policies that provide coverage for the owner of the aircraft for rental use do not provide coverage for the renter-pilot.⁹² Renter-pilots should beware of this defense to coverage before assuming that they will be covered in the event of an accident.

In *Ranger Insurance Co. v. Silverthorne*, the Missouri Court of Appeals held that Ranger was not obligated to defend a pilot in a suit for injuries sustained by passengers in an accident, where the insured’s limited commercial use policy permitted rental of the aircraft, but expressly stated that any person operating the aircraft under a rental agreement was not an insured under the policy.⁹³ In *Ranger*, the injured passengers brought suit against

⁸⁶ 338 F.2d 452 (5th Cir. 1964).

⁸⁷ *Id.* at 453.

⁸⁸ *Id.* at 453-54. Pleasure and business use was defined by the policy as “personal, pleasure, family and business use, excluding any operation for which a charge was made.” *Id.*

⁸⁹ *Id.* at 455.

⁹⁰ *Id.*

⁹¹ 553 S.W. 2d 530, 533 (Mo. App. 1977).

⁹² *Id.*

⁹³ *Id.*

the pilot and the owner of the aircraft.⁹⁴ The pilot and owner then tendered their defense to Ranger Insurance under the policy.⁹⁵ Ranger first denied the policy covered the pilot and sought a declaratory judgment that the policy did not cover the pilot.⁹⁶ The pilot argued that ambiguities plagued the policy, such as the intended use provision (which covered rental pilots) and the definition of insured (excluding rental pilots).⁹⁷ The Court held that no ambiguity existed between the definition of insured and the purposes of use provisions and that:

[t]he 'Purpose(s) of Use, which includes rental to pilots provides coverage to the named insured for liability which might be imposed upon it arising out of such use of the aircraft. The parties to the contract of insurance were under no obligation to provide coverage for the rental pilots and by the terms of the policy elected not to do so. There can be no question as to their right so to contract.⁹⁸

In contrast, the court in *Martin v. Ohio Casualty Insurance* concluded that a rental pilot was insured under a policy that excluded rental pilots in the printed definition of "Insured" but allowed rental of the aircraft to pilots as a purpose of use in the declaration of "Commercial."⁹⁹ In so concluding, the Court stated:

[t]he policy is to be considered as a whole and should be construed liberally in favor of the insured. This is in line with the Michigan rule as to construction of insurance policies generally. Where the policy contains both typewritten and printed provisions, the latter must yield to the former because of the rule that typed provisions are deemed special conditions modifying the printed portions. It was this latter rule that the trial court invoked, and properly so, in ruling that item 6 of the 'declarations' modified that definition of 'insured' and extended coverage to a renter pilot. An 'X' was typed into the box in the front of subsection (e) of item 6, and this is the provision that authorized the use of the insured aircraft for rental to pilots. We hold that the

⁹⁴ *Id.* at 531.

⁹⁵ *Id.*

⁹⁶ *Id.*

⁹⁷ *Id.* at 534.

⁹⁸ *Id.*; see also *Melton v. Ranger Ins. Co.*, 515 S.W.2d 371 (Tex. Civ. App.—Fort Worth 1974, writ ref'd n.r.e.) (holding that Purposes of Use provision in the policy, which allowed for rental to pilots, did not modify the definition of "insured" which expressly excluded renter pilot); but see *Martin v. Ohio Cas. Ins.*, 157 N.W.2d 827 (Mich. Ct. App. 1968).

⁹⁹ 157 N.W.2d at 829.

court correctly ruled that this provision modified the definition of 'insured' and extended coverage to plaintiffs. 'To hold otherwise would be to permit the . . . insurance company to "blow hot and cold" in one breath, or, to give coverage in one part of the policy and take it away in another.'¹⁰⁰

D. CONVERSION EXCLUSION

In the event a renter-pilot or lessee decides to use an insured's aircraft for unlawful purposes, a conversion exclusion may exclude coverage for loss of the aircraft or for liability claims. Under aviation insurance policies, the conversion exclusion has most often been applied to hull loss claims arising out of insured aircraft being confiscated by governments for drug smuggling.¹⁰¹

In *General Electric Credit Corp. of Tennessee v. Kelly & Dearing Aviation*, the court held that a lienholder was not entitled to coverage under the lienholder's endorsement for a loss sustained as a result of the insured airplane being confiscated.¹⁰² The lienholder sought to be paid under the breach of warranty endorsement after the Colombian government confiscated the plane.¹⁰³ Kelly & Dearing ("K&D"), the insured, purchased the aircraft and executed a promissory note in favor of the lienholder, GE Credit Corporation ("GECC").¹⁰⁴ Thereafter, K&D leased the aircraft to Ownby, who obtained an aviation insurance policy from Aetna.¹⁰⁵ The Aetna policy included a lienholder endorsement in favor of GECC.¹⁰⁶ The aircraft was later confiscated by the Colombian government for Ownby's illegal transportation of drugs into Columbia.¹⁰⁷ After being notified of the confiscation, GECC contacted Aetna and sought

¹⁰⁰ *Id.*; see also *Wzontek v. Zurich Ins. Co.*, 208 A.2d 861 (Pa. 1965) (citations omitted).

¹⁰¹ *Nat'l Union Fire Ins. Co. v. Care Flight Air Ambulance Serv., Inc.*, 18 F.3d 323 (5th Cir. 1994); *Gen. Elec. Credit Corp. v. Kelly & Dearing Aviation* 765 S.W.2d 750 (Tenn. Ct. App. 1988); *Nat'l Union Fire Ins. Co. v. Carib Aviation, Inc.*, 759 F.2d 873 (11th Cir. 1985); *Gelder v. Puritan Ins. Co.*, 668 P.2d 1117 (N.M. Ct. App. 1983); *Swish Mfg. Se. v. Manhattan Fire & Marine Ins. Co.*, 675 F.2d 1218 (11th Cir. 1982).

¹⁰² 765 S.W.2d at 750.

¹⁰³ *Id.* at 751.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.* The policy covered Ownby as lessee and K&D as lessor of the plane. *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

coverage under the lienholder's endorsement.¹⁰⁸ Aetna denied coverage, citing that Ownby had converted the airplane when he used it for illegal purposes, an exclusion to the lienholder endorsement.¹⁰⁹ The court agreed and held that Aetna was not liable for payment to GECC under the lienholder endorsement because the plane had been converted.¹¹⁰ The court reasoned:

In the case at bar, Ownby had legal possession of the airplane pursuant to his lease from K&D. The lease contained no territorial or other limitations on his use of the aircraft, however, K&D had the right to assume that Ownby would use it for legal purposes. Ownby's actions in his use of this leased airplane was in reckless disregard for K&D's right, as owner of the airplane, to repossession of the property. His action clearly exceeded K&D's implied consent for his operation of the plane and has completely deprived them of their property for an indefinite period of time. The intentional act of Ownby constituted conversion.¹¹¹

In *Gelder v. Puritan Insurance Co.*, the aviation insurer, Puritan, moved for summary judgment, claiming that it did not have an obligation to pay its insured under the hull loss coverage of its policy for a crash that occurred immediately after the insured's lessee unloaded a delivery of 28 pounds of marijuana.¹¹² Puritan argued that the loss was excluded under the conversion exclusion.¹¹³ The appellate court upheld the trial court's summary judgment grant in favor of Puritan. The court found the loss was excluded because, at the time of the accident, the lessee had converted the insured's aircraft.¹¹⁴ The court noted that the "lease agreement made it clear that the plane was not to be used 'for any violation of federal or state controlled substance laws'" and, thus, found the lessee had exceeded the authorized use of the aircraft.¹¹⁵

In *Swish Manufacturing Southeast v. Mahattan Fire & Marine Insurance Co.*, the Eleventh Circuit reversed a summary judgment action in favor of the insured under an aviation policy.¹¹⁶ In that case, Swish Manufacturing ("Swish") leased a plane to a

¹⁰⁸ *Id.* at 752.

¹⁰⁹ *Id.* at 754.

¹¹⁰ *Id.*

¹¹¹ *Id.*

¹¹² 668 P.2d 1117, 1118 (N.M. Ct. App. 1983).

¹¹³ *Id.*

¹¹⁴ *Id.* at 1119.

¹¹⁵ *Id.* at 1118.

¹¹⁶ 675 F.2d 1218, 1221 (11th Cir. 1982).

lessee who agreed not to use the plane for unlawful purposes.¹¹⁷ Swish carried insurance on the plane, but the policy contained an exclusion for conversion.¹¹⁸ The lessee then flew the plane to the Bahamas.¹¹⁹ Once it was in the Bahamas, the police confiscated the plane and its cargo of marijuana.¹²⁰ While in police custody, the plane was damaged and electronic equipment was removed.¹²¹ Swish then demanded payment from the insurance company; the insurance company refused, relying on the conversion exclusion of the policy.¹²² As a result, Swish sued in district court and was granted a partial summary judgment on the issue of liability.¹²³ However, on appeal, the Eleventh Circuit held that there was a conversion by Swish's lessee that precluded payment under the policy.¹²⁴ Consequently, the court reversed and rendered partial summary judgment for the insurance company.¹²⁵

In *National Union Fire Insurance Co. of Pittsburgh v. Care Flight Air Ambulance Service, Inc.*, ("General Electric Capital Corporation") ECC leased an aircraft to Care Flight.¹²⁶ The lease prohibited subleasing of the aircraft without GECC's consent, and further required Care Flight to obtain insurance coverage for the aircraft.¹²⁷ National Union Fire Insurance Co. ("National Union") provided Care Flight insurance coverage.¹²⁸ The policy contained a breach of warranty endorsement that named GECC and Care Flight as beneficiaries.¹²⁹ Care Flight, without GECC's consent, subleased the aircraft to a third party who then subleased it to a subsequent lessee, Contraras.¹³⁰ The Colombian government seized the aircraft while under Contraras' control for violations of air traffic laws.¹³¹

GECC's insurance carrier, under its subrogation rights, sought payment from National Union under its policy with Care

¹¹⁷ *Id.* at 1219.

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *Id.*

¹²² *Id.* at 1218.

¹²³ *Id.*

¹²⁴ *Id.* at 1221.

¹²⁵ *Id.*

¹²⁶ 18 F.3d 323, 324 (5th Cir. 1994).

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ *Id.*

¹³¹ *Id.*

Flight.¹³² National Union filed a request for declaratory judgment and moved for summary judgment on the grounds that coverage was precluded because Care Flight had converted the plane.¹³³ The district court "granted summary judgment in favor of National Union ruling that Care Flight had converted the aircraft as a matter of law and that the conversion limitation in the breach of warranty endorsement precluded coverage."¹³⁴ The Fifth Circuit held that Care Flight converted the aircraft when it breached its lease agreement with GECC by entering into an unauthorized sublease.¹³⁵ In reaching its conclusion, the Fifth Circuit analyzed the Second Restatement of Torts as follows:

'One who is authorized to make a particular use of chattel, and uses it in a manner exceeding the authorization, is subject to liability for conversion to another whose right to control the use of the chattel is thereby seriously violated.' *Restatement (Second) of Torts* §28 (1965)). Texas generally follows the elements of conversion as stated in the *Restatement*, which provides that '[t]he limits of permitted use ordinarily are determined by the terms, expressed or reasonably implied, of the contract or other agreement between the parties, and the question becomes one of whether there is a material breach of the agreement.' *Id.* at Cmt. C.

The district court correctly determined that the unauthorized sublease of the aircraft was a material breach. Texas law recognizes the distinction between serious violations of another's right of control, which constitute conversion, and minor or technical violations insufficient in degree of interference to constitute conversion.¹³⁶

E. CAUSAL CONNECTION REQUIREMENT

Depending on the jurisdiction, insureds *may* be able to argue that, in order to use the above-cited exclusions, there must be a causal connection between the renting and/or conversion of the aircraft, and the accident for which coverage is sought. For example, the Fifth Circuit's opinion in *Fireman's Fund Insurance Co. v. Wilburn Boat Co.* may support an argument that a causal

¹³² *Id.*

¹³³ *Id.*

¹³⁴ *Id.*

¹³⁵ *Id.* at 328.

¹³⁶ *Id.*

connection must exist.¹³⁷ In *Wilburn Boat*, the Fifth Circuit, interpreting a marine insurance policy, held that a breach of a “private pleasure use” warranty by carrying passengers for hire was not a defense to coverage unless the breach caused or contributed to the destruction of the insured property.¹³⁸ The Fifth Circuit based its decision on the Texas anti-technicality statute Article 6.14 of the Texas Insurance Code, which reads:

No breach or violation by the insured of any warranty, condition or provision of any fire insurance policy, contract of insurance, or applications therefore, upon personal property, shall render void the policy or contract, or constitute a defense to a suit for loss thereon unless such breach or violation contributed to bring about the destruction of the property.¹³⁹

III. DECLARATORY JUDGMENT ACTIONS AND THE EIGHT CORNERS RULE

The typical vehicle for determining the rights of the parties to an insurance contract, including the applicability of the above-referenced exclusions, is through a declaratory judgment action. In the context of hull loss claims, the rules of evidence and discovery are comparable to a typical breach of contract action, and there is no limitation on the evidence that will be considered by the court outside the applicable evidentiary rules. However, in the context of a liability claim, Texas courts follow the “Eight Corners Rules” to determine specifically whether an insurer has a “duty to defend” its named insured owner or renter-pilot on claims brought by injured third-parties.¹⁴⁰ Under the Eight Corners Rule, the courts look *only* to the pleadings and the insurance policy to determine whether or not the duty to defend exists.¹⁴¹ However, in many instances the court is required to examine facts outside the pleadings. Crafty plaintiffs’ attorneys do not plead the insured’s rental or charter of the aircraft in an attempt to keep the insurer liable for defense

¹³⁷ 300 F.2d 631, 646 (5th Cir. 1962).

¹³⁸ *Id.*

¹³⁹ TEX. INS. CODE ANN. § 6.14 (Vernon 2003); *but see* *Electron Mach. Corp. v. Am. Mercury Ins. Co.*, 297 F.2d 212 (5th Cir. 1961) (finding that at the time of the crash the aircraft was being used to instruct a pilot not named for instruction purposes, and therefore, the insurance was not in force even though excluded use was not a cause of the loss).

¹⁴⁰ *Cluett v. Med. Protective Co.*, 829 S.W.2d 822, 829 (Tex. App.—Dallas 1992, writ denied).

¹⁴¹ *Id.*

costs. This is done in order to negotiate a possible settlement of noncovered claims. In such instances, Texas courts have created an exception to the Eight Corners Rule for extrinsic evidence.¹⁴²

At least one court has suggested that extrinsic evidence may be used to resolve coverage questions that the complaint itself is insufficient to resolve.¹⁴³ Specifically, "if the underlying complaint, however, does not allege facts, if taken as true, that sufficiently state a cause of action under the policy, evidence induced in the declaratory judgment action may also be considered."¹⁴⁴ When extrinsic facts are "insurance facts" that do not deal with the underlying liability case, they should be admitted in the declaratory judgment to determine coverage.¹⁴⁵ *Cook v. Ohio Casualty Insurance Co.* involved an auto insurance policy that covered household drivers in some cars, but not others.¹⁴⁶ In that case, the petition failed to state which member of the household or which car struck and injured the plaintiff.¹⁴⁷ Extrinsic evidence was allowed to prove several facts necessary to resolve the coverage question: (1) which member struck the plaintiff, and (2) which automobile struck the plaintiff.¹⁴⁸ The evidence was allowed because the identity of the driver and the specific car are not facts that would affect the merits of the tort claim.¹⁴⁹

Many courts follow this rule and allow the introduction of extrinsic facts.¹⁵⁰ In *State Farm Fire & Casualty Co. v. Wade*, the petition was silent as to whether a boat was used for personal or business purposes at the time it was involved in an accident.¹⁵¹ The insurance policy covered pleasure use but not business

¹⁴² *Matagordo Ventures, Inc. v. Travelers Lloyds Ins. Co.*, 203 F. Supp. 2d 704, 714 (S.D. Tex. 2001).

¹⁴³ *John Deere Ins. Co. v. Truckin' U.S.A.*, 122 F.3d 270 (5th Cir. 1997).

¹⁴⁴ *Id.* at 272.

¹⁴⁵ *Cook v. Ohio Cas. Ins. Co.*, 418 S.W.2d 712 (Tex. Civ. App.—Texarkana 1967, no writ).

¹⁴⁶ *Id.* at 714-15.

¹⁴⁷ *Id.* at 713-14.

¹⁴⁸ *Id.* at 714.

¹⁴⁹ *Id.* at 716.

¹⁵⁰ See, e.g., *Int'l Serv. Ins. Co. v. Boll*, 392 S.W.2d 158, 160 (Tex. Civ. App.—Houston [1st Dist.] 1965, writ ref'd n.r.e.); *Gonzales v. Am. States Ins. Co.*, 628 S.W.2d 184 (Tex. App.—Corpus Christi 1982, no writ); *State Farm Fire and Cas. Co. v. Wade*, 827 S.W.2d 448 (Tex. App.—Corpus Christi 1992, no writ).

¹⁵¹ 827 S.W.2d at 450.

use.¹⁵² The court held that the insurer could offer evidence that the boat was being used for the excluded business purposes.¹⁵³

IV. INSURERS' RIGHT OF SUBROGATION

Another issue that arises frequently after the crash of an aircraft during a rental flight is whether the insurance company that pays its named insured for the value of the damaged or destroyed aircraft has a right to bring a subrogation action against the renter-pilot who caused the accident. Such a right would be based upon several factors, including the terms of the specific policy, and whether the named insured would have a valid claim against the renter-pilot (i.e., whether an agreement entered before or after the accident between the named insured and the renter-pilot limited or extinguished liability for the renter-pilot).¹⁵⁴

It is well settled in the area of insurance law that because subrogation may arise only against third persons, an insurer does not have a right of subrogation against its insured to recover for sums paid out.¹⁵⁵ This doctrine is commonly referred to as the "anti-subrogation rule."¹⁵⁶ An insurer who subrogates itself to its insured "stands in the shoes" of the insured and cannot recover by subrogation except to the extent of the rights of the insured.¹⁵⁷ To permit subrogation "would permit an insurer, in effect, to pass the incident of the loss, either partially or totally, from itself to its own insured and thus avoid the coverage that its insured purchased."¹⁵⁸ This anti-subrogation rule also applies to additional insureds.¹⁵⁹ However, the applicability of the anti-subrogation rule to an additional insured who is only an insured under the liability coverage of a policy (i.e., not covered under the collision or hull coverage) is not so clear.

In *Aviation Employees Insurance Co. v. Barclay*, the pilot rented an aircraft that was subsequently crashed on takeoff.¹⁶⁰ The

¹⁵² *Id.*

¹⁵³ *Id.* at 453.

¹⁵⁴ *Aviation Employees Ins. Co. v. Barclay*, 206 A.2d 119, 121-124 (Md. 1965).

¹⁵⁵ *Taylor v. Bunge Corp.*, 845 F.2d 1323, 1329 (5th Cir. 1998).

¹⁵⁶ 44 A.A.M. JUR. 2D Insurance § 1770 (2005).

¹⁵⁷ *AGIP Petroleum Co., Inc. v. Gulf Island Fabrication, Inc.*, 920 F. Supp. 1318, 1326 (S.D. Tex 1996).

¹⁵⁸ *Taylor*, 845 F.2d at 1329 (quoting *St. Paul Fire & Marine Ins. Co. v. Murray Plumbing & Heating Corp.*, 135 Cal. Rptr. 120, 126 (Cal. Ct. App. 1976)).

¹⁵⁹ *Tri-State Ins. Co. of Mian. V. Commercial Group West LLC*, 698 N.W. 2d 483, 487 (N.D. 2005).

¹⁶⁰ 206 A.2d 119 (Md. 1965).

owner's insurer paid for those repairs and then sued the pilot, as subrogee, to recover all costs except for the deductible.¹⁶¹ The trial court granted the defendant's motion for summary judgment.¹⁶² On appeal, the court held that when the pilot rented the airplane from the airport facility, he was not an additional insured as to the hull loss coverage and, as such, the facility's insurer did have a right of subrogation against him.¹⁶³ In reaching its conclusion, the court acknowledged the two different types of coverage under the policy—liability coverage and hull loss coverage.¹⁶⁴ The court examined the definition of insured under the policy and noted that a permissive user was an insured for the purposes of liability coverage only.¹⁶⁵ The court held that the definition of insured did not extend to the hull coverage.¹⁶⁶ In reaching its conclusion, the court relied heavily on the fact that, under the hull loss coverage, there was a condition that provided the "policy would not inure, directly or indirectly, to the benefit of any bailee."¹⁶⁷

In *Pacific Indemnity Co. v. United States*, the Ninth Circuit found that insurance coverage for hull damage did not inure to a "permissive user."¹⁶⁸ Here, the insured was obliged to protect a permissive user against liability to third parties and their property, but the hull coverage provisions did not use the same unqualified terms as other provisions.¹⁶⁹ The court further held that a cooperation clause did not create any ambiguity in the extension of coverage under the hull coverage.¹⁷⁰

In *Rushing v. International Aviation Underwriters, Inc.*, the lessee of an aircraft appealed from an adverse judgment brought by subrogee insurance company for damages to a covered aircraft.¹⁷¹ The lessee had leased the plane from the named insured and, upon landing, improperly caused severe damage to

¹⁶¹ *Id.*

¹⁶² *Id.* at 121.

¹⁶³ *Id.* at 121-22.

¹⁶⁴ *Id.* at 122.

¹⁶⁵ *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ *Id.* at 124.

¹⁶⁸ 463 F.2d 1213 (9th Cir. 1972).

¹⁶⁹ *Id.* at 1214.

¹⁷⁰ *Id.*; see also *Graham v. Rockman*, 504 P.2d 1351, 1356-57 (Ala. 1972) (holding that where "insured" not defined in policy, named insured's reasonable expectation considered in determining whether subrogation allowable).

¹⁷¹ 604 S.W.2d 239, 240-41 (Tex. Civ. App.—Dallas 1980 writ ref'd n.r.e.).

the plane.¹⁷² The insurer paid for the damage under the hull loss coverage of the lessor's policy and brought a subrogation claim against the lessee.¹⁷³ The appellee argued that the insurer's claim was barred due to the named insured's forfeiture of its corporate charter post filing of the subrogation action.¹⁷⁴ Additionally, the appellee argued that the lease agreement limited his liability to the deductible under the insurance policy and that the insurer could not recover attorney's fees.¹⁷⁵ The appellate court rejected both arguments, upheld the judgment in favor of the subrogee insurance company and sustained the award of attorneys' fees to the insurer.¹⁷⁶

In *Insurance Co. v. Crippen*, the Dallas Court of Appeals held that the hull loss coverage of an aviation policy *did* extend to cover a lessee of the airplane and that the lessee was therefore entitled to be reimbursed under the hull loss coverage for monies it had paid to repair an airplane damaged while under the lessee's control.¹⁷⁷ The court reasoned that the lessee became a co-insured under the hull loss coverage of the policy by reason of the lessor/named insured's "request that coverage be extended to include the lessee followed by the insurer's acquiescence and ratification."¹⁷⁸ Although this case is not a subrogation action, it can be used to argue by negative inference that simply being an insured under an aviation policy for liability does not automatically extend hull loss coverage to the permissive user. If not for the "acquiescence" by the insurer, the permissive user would arguably not have been considered covered under the hull loss provision.

In *Rocky Mountain Helicopters, Inc. v. Bell Helicopters Textron*, the Tenth Circuit, applying Texas law, held that a "lien holder payee under an endorsement extending breach of warranty coverage was not an insured party for purposes of immunity from subrogation."¹⁷⁹ In *Rocky Mountain Helicopters*, the insured and its insurer filed suit against the manufacturer/lien holder payee of a helicopter seeking damages arising out of a helicopter acci-

¹⁷² *Id.* at 240.

¹⁷³ *Id.* at 241.

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ 223 S.W.2d 297, 301 (Tex. Civ. App.—Dallas 1949).

¹⁷⁸ *Id.*

¹⁷⁹ 805 F.2d 907 (10th Cir. 1986).

dent.¹⁸⁰ The lien holder payee asserted that it was immune from a subrogation claim because it was an insured under its loss payee endorsement.¹⁸¹ The court held that the lien holder payee was, in fact, not an insured under the breach of warranty endorsement.¹⁸² More importantly, the court found that even if the lien holder was an insured party, it would still be subject to suit for liability and negligence and, in that event, the lien holder's status "would be limited to its property or breach of warranty."¹⁸³

V. CONCLUSION

Prior to renting, leasing or chartering aircraft, owners, as well as pilots, would be well advised to understand how the policies of insurance covering their subject aircraft will treat such uses in the event of an accident. Failure to abide by the stated uses in an aviation insurance policy could result in non-coverage and have serious financial consequences for the uninformed aircraft owner.

¹⁸⁰ *Id.* at 909.

¹⁸¹ *Id.* at 910.

¹⁸² *Id.* at 914.

¹⁸³ *Id.*