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Recent Case Summaries**Second Circuit Breathes Life Into Manifest Disregard of the Law**

Stolt-Nielsen Transpt. Group Ltd. v. Animalfeeds Intern'l Corp., No. 06-3474-cv, 2008 WL 4779582 (2d Cir. Nov. 4, 2008).

In a non-reinsurance case, the Second Circuit Court of Appeals joined the Seventh Circuit in holding that the manifest disregard doctrine has survived the United States Supreme Court's decision in *Hall Street Associates, L.L.C., v. Mattel, Inc.*, 128 S. Ct. 1396 (2008). This case has implications for reinsurance arbitrations and for those who will attempt to vacate reinsurance arbitration awards using this doctrine.

The issue in dispute concerned the permissibility of class arbitration under international maritime contracts, which incorporated certain rules of the American Arbitration Association's ("AAA") Supplemental Rules for Class Arbitrations. The arbitration panel issued a clause construction award finding that silence in the arbitration clause did not preclude class arbitration and, therefore, permitted class arbitration under the relevant contracts. The losing party sought to vacate the award based on manifest disregard of the law and the district court agreed. The Second Circuit reversed and very carefully set forth how parties must now view the very narrow ground of manifest disregard of the law when seeking to vacate an arbitration award.

In reversing the vacatur by the district court, the circuit court reminded the parties that the courts must grant an arbitra-

tion panel's decision great deference. After setting forth the limited grounds for vacatur in the Federal Arbitration Act ("FAA"), the court reiterated that the district court may vacate an award that is in manifest disregard of the law. In describing the legal standard for manifest disregard, however, the court outlined the heavy burden and severe limitation associated with the rarely granted relief based on manifest disregard of the law. The court provided an updated laundry-list of cases construing the doctrine, all of which demonstrate how exceedingly rare relief is granted on this ground. The circuit court pointed out that manifest disregard means more than error or misunderstanding of the law, more than misconstruction of the contract, and more than the court's serious reservations about the soundness of the arbitrator's reading of the contract.

In what is a helpful reiteration of the doctrine, the court set forth the three components for the application of the manifest disregard standard: (1) whether the law allegedly ignored by the arbitrator was clear and, in fact, explicitly applicable to the dispute; (2) if the law is clearly and plainly applicable, whether the law in fact was improperly applied leading to an erroneous outcome; and (3) if the first two inquires are satisfied, whether the arbitrator actually knew of the law's existence and its applicability to the dispute.

In addressing the effect of *Hall Street*, the circuit court agreed with other courts that have found the manifest disregard doctrine to be a reconceptualized judicial gloss on the specific grounds for vacatur under section 10 of the FAA. While recognizing

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that the Supreme Court's holding in *Hall Street* that the FAA sets forth the exclusive grounds for vacating an arbitration award is inconsistent with some statements made by the Second Circuit in construing manifest disregard, that holding did not, according to the Second Circuit, abrogate manifest disregard altogether.

Thus, the Second Circuit views the manifest disregard doctrine and the FAA as mechanisms to enforce the parties' agreements to arbitrate rather than as judicial review of the arbitrators' decision. The circuit court stated that it must continue to bear responsibility to vacate awards in those rare instances in which the arbitrator knew of an applicable law, appreciated that the law controlled the case, and nonetheless willfully flouted the governing law by refusing to apply it. When arbitrators are found to have done all of that, the arbitrators have failed to interpret the contract and have exceeded their powers or so imperfectly executed them that a final and definite award on the matters submitted had not been made.

The court went on to determine if the district court's finding of manifest disregard was correct under these principles and held that it was not. The errors identified – the failure to make a meaningful choice-of-law analysis and ignoring federal maritime law and its custom and usage – did not rise to the level of manifest disregard of the law. Because no federal maritime law or state law established a rule of construction prohibiting class arbitration where the arbitration clause is silent, the arbitrator's decision to construe the language to permit class arbitration was not in manifest disregard of the law.

This decision demonstrates the severely limited circumstances where a court will

vacate an arbitration award as being beyond the power of the arbitrators because of manifest disregard of law. It is rare in reinsurance cases that there is a specific law that applies without question to the subject matter of the dispute. Thus, the manifest disregard doctrine, which was limited even before *Hall Street*, clearly has been limited further and will rarely apply in reinsurance arbitration disputes.

Eighth Circuit Affirms Arbitration Award as Not Exceeding the Arbitration Panel's Authority

Crawford Group, Inc. v. Holecamp, 543 F.3d 971 (8th Cir. 2008).

In a non-reinsurance case, the Eighth Circuit Court of Appeals affirmed a decision by the Eastern District of Missouri, which upheld an arbitration award in favor of a former corporate executive over a stock repurchase by the employee's former employer on a finding that the AAA properly decided that an arbitrator was qualified to hear a valuation dispute and that the arbitrators acted within the scope of their authority in reaching their conclusion and in setting the price of the stock.

The dispute arose after the company announced its intention in 2004 to repurchase stock from the employee who had retired in 2000. The company paid the employee \$11.4 million, which was based on a price of \$25.32 per share. When the employee demanded arbitration, the company responded with a lawsuit in state court. Ultimately, the parties went to arbitration on the sole issue of the value of the employee's shares. In a 2-1 vote, the arbitration panel awarded the employee \$20.7 million, based on a price of \$45.90 per share. The company sought to vacate

the award, but the district court affirmed the award.

The company's primary argument on appeal was that the appointment of the employee's arbitrator was not in accordance with the agreement, with the result that the arbitration panel exceeded its power to issue the award. During the arbitration, the company objected twice to the appointment of the employee's arbitrator on the basis that he did not possess the qualifications required by the agreement. The parties submitted their arguments and supporting documentation to the AAA, and the AAA each time determined that the employee's arbitrator was qualified to serve as an arbitrator.

Under the terms of the agreement, the parties designated the AAA to conclusively decide the issue of the arbitrators' qualifications. The court held that the parties' method of appointment was arguably followed because the AAA's decision that the employee's arbitrator was qualified to serve was an arguable interpretation of the provision that "[e]ach arbitrator shall have experience in arbitrating matter substantially similar to the matter being arbitrated." Therefore, the AAA's resolution of the company's challenges to the employee's arbitrator did not present a basis for vacatur of the arbitration award.

The company also argued that an agreement between the employee and the company deprived the arbitrators of the authority to determine the value of the employee's shares. The company relied on a provision of the agreement stating that "the Administrator's determination of the Purchase Price shall be final and binding on all parties," but the court noted that another provision required the administra-

tor to act in good faith and follow a certain procedure.

Specifically, the administrator was required to "apply valuation principals substantially the same as those which applied to valuing the Award on the Award date." The employee presented evidence showing that the valuation principles employed in 2000 and in 2004 differed, but the company presented evidence that the principals were essentially the same. In light of the conflicting evidence, the court left it up to the arbitrators, and not the court, to weigh the parties' conflicting evidence.

Fifth Circuit Upholds Arbitration Against McCarran-Ferguson Preemption

Safety Nat'l Cas. Corp. v. Certain Underwriters at Lloyd's, London, 543 F.3d 744 (5th Cir. 2008).

The Fifth Circuit Court of Appeals has reversed a district court order denying the reinsurers' motion to compel arbitration based on a Louisiana anti-arbitration statute aimed at insurers. A Louisiana self-insurance fund entered into a reinsurance agreement with London reinsurers. The reinsurance agreement contained an arbitration clause. Another insurer claimed that the fund had assigned the rights under the reinsurance agreement to it in a loss portfolio transfer agreement; however, the reinsurers' did not recognize the assignment.

The purported cedent sued the reinsurers in federal court to determine whether the rights under the reinsurance agreement were assignable. The reinsurers moved to stay the action and compel arbitration with both the purported cedent and the fund based on the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. The fund opposed and the court

agreed with the fund, finding that the arbitration agreement was unenforceable under Louisiana law. The court held that a provision of the Louisiana insurance law voids, for certain insurance contracts issued or delivered in Louisiana and covering Louisiana risks, any condition, stipulation or agreement that "depriv[es] the courts of this state of the jurisdiction of action against the insurer." The court concluded that the Louisiana statute reverse preempted the Convention under the McCarran-Ferguson Act because (i) the Convention does not relate to the business of insurance, (ii) the Louisiana statute was enacted to regulate the business of insurance, and (iii) the Convention would invalidate, impair or supersede the Louisiana statute.

In reversing the district court, the Fifth Circuit commented that the Convention as a treaty was outside the scope of an "Act of Congress" as the term is used in the McCarran-Ferguson Act, even though the Convention was implemented by an Act of Congress. A treaty, the court wrote, is much more than an Act of Congress because a treaty is (i) negotiated by the executive branch and (ii) ratified only by the Senate. The court stated that it was unlikely that when Congress crafted the McCarran-Ferguson Act, it intended any future treaty implemented by an act of Congress to be abrogated to the extent that treaty conflicted in some way with a state law regulating the business of insurance if Congress' implementing legislation did not expressly save the treaty from reverse preemption by state law. The Fifth Circuit also noted that provisions in the Convention ameliorate concerns that a state's regulatory policies regarding contracts would not be recognized in international arbitration. Given the commonly understood meaning of the term "Act of Congress," the court concluded that

the Convention was not reverse preempted by the McCarran-Ferguson Act.

Florida Federal Court Clarifies the Applicability of Arbitration Provisions Present in Some, But Not All Agreements Between Reinsurer and Cedent

Northbrook Indem. Co. v. First Auto. Serv. Corp., No. 3:07-cv-683-J-32JRK, 2008 WL 3009899 (M.D. Fla. Aug. 01, 2008).

A Florida federal court ordered a cedent and its reinsurer to participate in arbitration of the underlying claim based upon a lack of a showing of "positive assurance" that the arbitration provision was not applicable.

The cedent and the reinsurer commenced their relationship by signing an initial placement slip, which eventually ripened into a reinsurance agreement between them. The initial placement slip purported to cover all vehicle service contracts insured by the cedent and contained a broad arbitration clause covering "any differences ... between the contracting parties with reference to the interpretation of [the agreement] or their rights with respect to any transaction involved." After the initial placement slip became effective, but before it ripened into the reinsurance agreement, the cedent and the reinsurer also signed a separate slip that did not contain an arbitration clause, and under the terms of which the reinsurer agreed to reinsure cedent's potential obligations related to a particular vehicle service company. In subsequent years, the parties signed three additional slips effectively renewing the separate slip for three additional annual terms - while the reinsurance agreement between them also remained in effect.

Following a dispute between the parties concerning the reinsurer's obligation to

cover repair costs of the vehicle service company, the reinsurer brought an action in the Florida federal court seeking an order requiring arbitration of the dispute under the reinsurance agreement signed by the parties. The cedent challenged the reinsurer's request for arbitration, noting that the terms of the four separate slips did not contain an arbitration provision.

In its order compelling arbitration, the court held that the arbitration provision of the reinsurance agreement reached "differences" between the parties over the interpretation of the agreement "with respect to any transaction involved." The court distinguished contrary case law cited by the cedent, noting that some of the cited cases involved claims generated from a separate agreement for different services and different purposes from the one containing the arbitration clause. Another cited case involved an arbitration clause present in a "secondary" document, but absent from the "central" agreement between the parties. Unlike those agreements, the set of agreements between the cedent and the reinsurer here governed "the same ongoing relationship between the same parties concerning the same subject matter and for overlapping time periods." Moreover, the four separate slips signed by the parties served as a mere "modification" or "upgrade" of the existing initial placement slip agreement and reinsurance agreement between them because the reinsurer would have been obligated under the reinsurance agreement to cover repair costs of the vehicle service company even if the four slips did not exist. Thus, nothing more than "doubt" existed as to how the agreements between the cedent and the reinsurer were related, and this doubt was resolved in favor of arbitration. The court noted that the arbitration provision

would not have been applicable only upon a showing of "positive assurance" that it did not cover the asserted dispute.

Pennsylvania Federal Court Grants Motion to Compel Arbitration and Confirm Arbitrator

Lincoln Gen. Ins. Co. v. Clarendon Nat'l Ins. Co., No. 4:08-cv-0583 (M.D. Pa. Aug. 15, 2008).

A Pennsylvania federal court compelled arbitration of a dispute regarding obligations under a quota reinsurance treaty that was alleged to have been cancelled over a year earlier and confirmed the delayed appointment of an arbitrator. According to the court, this was a case "where otherwise good lawyering has, at least as to the selection of an arbitrator, lapsed into unseemly gamesmanship."

The dispute arose out of a quota reinsurance treaty that the parties signed in 2004 regarding the reinsurance of certain automobile policies. The treaty required the reinsurer to post collateral if its A.M. Best rating fell to B++ or below. Two years after the cedent gave its notice to terminate the treaty, and 18 months after the termination became effective, the reinsurer's A.M. Best rating was downgraded from A- to B++. Despite the purported termination of the treaty, the cedent demanded that the reinsurer post collateral. When the reinsurer refused, arguing that its obligations under the treaty had long ended, the cedent demanded arbitration.

In response, the reinsurer promptly filed an action in state court seeking a declaration that it had no further obligations under the treaty. The cedent responded by removing the action to federal court and making a motion to compel arbitration under the

FAA. In granting the cedent's motion, the court found that arbitration was appropriate because the reinsurer neither specifically challenged the validity of the arbitration provision nor the validity of the contract. The court was not persuaded by the reinsurer's argument that no valid agreement existed because the arbitration clause contained in the treaty ended when the treaty was cancelled.

While the court action was pending, the reinsurer chose not to comply with a deadline contained in the treaty regarding the selection of arbitrators. The treaty provided that each side was to pick its own arbitrator 30 days after being requested to do so by the other party, and once selected, these two arbitrators would pick a third who would preside. But if one party failed to pick an arbitrator within this time period, the treaty allowed the other side to select both arbitrators after notice and a ten day grace period. After the reinsurer declined to select an arbitrator, citing its pending declaratory action, the cedent selected both arbitrators.

Not surprisingly, the reinsurer rejected the arbitrator that the cedent chose and purported to reserve its right to select an arbitrator of its choosing. The reinsurer then nominated its own arbitrator, which the cedent contested. When the disputed arbitrator informed the cedent that he would cease all activity in the matter until the status of his appointment was clarified by the court, the cedent offered to advance the arbitrator's retainer on the reinsurer's behalf and to indemnify and defend the arbitrator against any effort to prevent him from serving in the matter. The court found this conduct problematic.

In resolving the conflicting appointments, the court confirmed the appointment of the reinsurer's desired arbitrator. While there was no controlling precedent on this issue, the court followed a line of cases developed in other jurisdictions, which hold that a relatively short, non-prejudicial and good faith delay in the appointment of an arbitrator does not deprive that party of its bargained-for right to choose its own arbitrator. The court expressly declined to follow cases that strictly enforced the unambiguous terms of an arbitration provision, and also declined to order that this issue be decided in arbitration.

New York Federal Court Vacates Award Provision for Continued Panel Jurisdiction

KX Reins. Co. v. Gen. Reins. Corp., No. 08 CIV. 7807 (SAS), 2008 WL 4904882 (S.D.N.Y. Nov. 14, 2008).

A New York federal court confirmed an arbitration panel's award in favor of two retrocedents, but vacated that part of the award that provided for the arbitration panel to remain in effect until all parties expressly requested the panel to disband.

The retrocedents entered into a series of excess-of-loss treaties with the retrocessionaire and brought separate arbitration proceedings to collect reinsurance recoverables under the treaties. The retrocedents agreed to a consolidated arbitration proceeding and the retrocessionaire obtained an interim award for pre-award security. After hearing, the panel issued an award, which incorporated the interim award for security on the retrocessionaire's obligation to post a letter of credit, and determined in the retrocessionaire's favor all the specific claims raised at the hearing (along with interest, attorneys' fees and costs). The award also provided that the panel would

remain constituted until all parties request the panel to disband.

After the retrocessionaire paid the full amount of the balances due under the award and posted additional security, it asked the panel to disband, but the retrocedents opposed the request and the panel rejected the request. The retrocessionaire then petitioned the court to confirm the arbitration award in all respects, except for that part of the award where the panel retained jurisdiction.

In confirming the substantive portion of the award, the court concluded that although the panel did not denominate the award as a "final" award, it was in fact a final award susceptible to confirmation. The court also noted that its power to vacate an award was very limited. In vacating that portion of the award in which the panel retained jurisdiction, the court explained that the powers granted to arbitrators is determined and circumscribed by the issues submitted for their determination. It noted that once the panel decides the submitted issues, it becomes *functus officio* and lacks further power to act. The court found that while it may have been prudent and economical for the panel to remain in place to deal with claims that had not been the subject of the arbitration and future issues concerning the letter of credit, it was not legally permissible according to the scope of authority granted to the panel by the parties. The court rejected the notion that an arbitration panel could retain unlimited authority and the power to exist indefinitely. Because the specific issues submitted to the panel define and delineate its powers, the court held, by definition, the panel had no jurisdiction over any potential future disputes.

New York Federal Court Denies Remand to Arbitration Panel Where Arbitration Award Is Not Ambiguous

Hartford Fire Ins. Co. v. Evergreen Org., Inc., No. 07 Civ. 7977 (RJS), 2008 WL 4185731 (S.D.N.Y. 2008).

In a non-reinsurance case, a New York federal court denied an insurer's motion to remand an arbitration award to the arbitration panel and instead granted the insurance agent's motion to confirm the award stating that remand was inappropriate because the award was not ambiguous or unclear.

The insurer had entered into an agreement with the agent whereby the agent acted as program manager and claims servicer for the insurance program. The contract was subsequently terminated, but the agent still owed a duty to the insurer for certain continuing obligations including premium collection. The insurer claimed that the agent breached its fiduciary duty on proper premium remittance and both parties agreed to arbitrate the dispute. The arbitration panel found for the insurer and issued an award for damages.

Both parties moved to confirm the award, but had differing interpretations of the award. The insurer argued that the arbitration panel had pierced the corporate veil and thus the individual shareholders of the agent should be jointly and severally liable for the amount of the award. The agent disputed this claim, arguing that the corporate veil had not been pierced and thus individual shareholders should not be liable. The district court remanded the award to the arbitration panel, which clarified that no individual shareholders were liable. The insurer then made another motion for remand claiming that the panel's award was

ambiguous because the panel had refused to hold the shareholders personally liable even though its decision found the shareholders had disregarded the agent's corporate form.

The court refused to remand holding that the award was clear and unambiguous and that there was ample basis for the panel's findings. The court emphasized the extreme amount of deference that must be shown to arbitration awards, noting that a court must confirm an award as long as "a ground for the decision can be inferred from the facts of the case." The court held that remand is only appropriate where the award is "indefinite, incomplete or ambiguous" and that the insurer could not ask for a second remand simply because it did not like the result of the first. The insurer also argued that under New York law it should be allowed to seek a clarification from the arbitration panel without a remand order from the court. The court held that New York law did not apply in this situation because the contract specifically indicated that it was governed by the Federal Arbitration Act. The court noted that the insurer could have made a motion to vacate the award if it thought the arbitration panel had made a mistake of law.

New York Federal Court Grants Default Judgment Against Retrocessionaire Confirming Arbitration Award for Retrocedent

North Star Reins. Corp. v. Harel Ins. Co., No. 08-cv-02380 (S.D.N.Y. Sept. 5, 2008).

A New York federal court granted a default judgment against a retrocessionaire that did not comply with an arbitration award for unpaid claims and failed to post security for the retrocessionaire's portion of the retrocedent's reserves for losses.

The dispute arose out of two retrocessional contracts between the retrocedent and the retrocessionaire, both of which provided for all contractual disputes to be subject to arbitration. In response to alleged non-payment by the retrocessionaire for past billings, the retrocedent demanded arbitration for 39 separate claims for which the retrocedent claimed that the retrocessionaire was responsible under the contracts. In April 2007, after discovery and an arbitration hearing, the arbitrator issued a final award for the retrocedent.

In March 2008, arguing that the retrocessionaire had not complied with the arbitration award, the retrocedent filed a motion to confirm the arbitration award in New York federal court. The retrocedent contended that the retrocessionaire had failed to pay the outstanding balance on past claims, pay post-arbitration claims within a 30 day notice period, or post security for the retrocessionaire's share of the retrocedent's reserves for losses. In June, citing the retrocessionaire's failure to submit an answer, the court clerk certified the retrocessionaire's default. In turn, the retrocedent filed a motion for default judgment against the retrocessionaire in July.

In granting the motion, the court concluded the litigation by entering default judgment against the retrocessionaire as per the retrocedent's proposed default judgment included with its motion. The default judgment comprised damages for unpaid claims awarded in arbitration plus interest, as well as post-arbitration claims. In addition, the court ordered the retrocessionaire to post security for the retrocedent's reserves for losses. The court also held the retrocessionaire liable for the retrocedent's attorney's fees. Now all the retrocedent

has to do is enforce the default judgment. A task often easier said than done.

Colorado Federal Court Holds Federal Statutory Interest Rate Applies to Post-Judgment Arbitration Award

Newmont U.S.A. Ltd. v. Ins. Co. of N.A., No. 06-cv-01178-ZLW-BNB, 2008 WL 4378777 (D. Colo., Sept. 19, 2007).

A Colorado federal court has ordered that the post-judgment interest rate on an arbitration award be calculated according to the federal post-judgment interest statute, as opposed to the interest rate contained in the arbitration agreement.

In an arbitration arising from three reinsurance agreements, the cedent was ordered to pay to the insured over \$1.2 million. At dispute in the federal court's review of the award was the interest rate applied to the award. The claims arose under reinsurance agreements from over 20 years ago and the interest rate applied by the arbitrator was determined by language in the reinsurance agreements. The agreements stated that either party would pay to the other an interest charge at a monthly rate of 1.5 percent on any amount not paid within the time required by the agreements, the charge to commence at the time any payment was required by the agreements. The court determined, however, that the 1.5 percent rate should only be applied to the months prior to entry of judgment; the post-judgment interest statutory rate would then apply to those months following entry of judgment.

In modifying that part of the arbitration award, the court noted that the Tenth Circuit has an extremely strict standard for altering the statutory rate and that anything short of an explicit statement that the contractual

rate is meant to control subsequent to entry of a federal judgment is inadequate.

New York State Court Denies a Motion to Stay Arbitration Because Arbitrators Must Determine Issues of Arbitrability

Life Receivables Trust v. Goshawk Syndicate 102, No. 601244/08, 2008 N.Y. Misc. LEXIS 6032 (N.Y. Sup. Ct., Sept. 9, 2008).

In a non-reinsurance case, a New York state trial court has denied a motion to stay arbitration because the arbitration agreement at issue and the FAA require an arbitration panel to determine issues of arbitrability.

The movant is a special purpose business trust that owns a portfolio of life insurance policies and the respondent is an insurance syndicate that issues contingency cost insurance ("CCI"), which is a financial guarantee against the risk that the seller of a life insurance policy would live beyond a specified period. The movant alleged that the respondent had not paid claims under CCI agreements to date. The CCI agreements contained an arbitration provision that gave the parties the right to appeal an error of law to the courts. The movant filed an action in state court after a dismissal from federal court for lack of subject matter jurisdiction.

The movant filed a motion to stay arbitration for two reasons. First, the movant relied on the CCI agreements' recourse provision. The recourse provision contained an absolute obligation to pay claims, thus the movant argued the issue was not subject to arbitration. Second, the movant challenged the validity of the arbitration agreement, relying on *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 128 US 1396 (2008), in which the U.S. Supreme Court held that parties to an arbitration agreement could not expand

the grounds for vacatur and modification by contract.

Disagreeing with the movant's reasoning, the court denied the motion to stay arbitration because the arbitration agreement provided that arbitrators would determine issues of arbitrability and that *Hall Street* was inapplicable. The FAA applies to the determination of whether the parties made a valid agreement to arbitrate disputes. The arbitration agreement establishes that the parties agreed to arbitrate their disputes arising out of the CCI agreement. The arbitration agreement also incorporated the American Arbitration Association rules, which states that arbitrators, not the courts, decide the "existence, scope or validity" of an arbitration agreement. Even though the movant challenged the arbitration agreement based on *Hall Street*, the scope and validity of the arbitration agreement is to be determined by arbitrators. *Hall Street* was distinguishable because the issue was whether the exclusive grounds for vacatur and modification were expanded. The court remanded the case in *Hall Street* for determination of the grounds for judicial enforcement of arbitration awards.

New York State Court Reaffirms "Render Academic" Standard for Determining Whether to Stay an Action Pending a Related Arbitration

Global Reins. Corp.-U.S. Branch v. Equitas Ltd., No. 600815-2007, 2008 N.Y. Misc. LEXIS 4970 (N.Y. County, Jul. 3, 2008).

A New York State trial court has reaffirmed the long-established standard for determining whether to stay an action pending the resolution of a related action or arbitration by expressly rejecting the argument that an intermediate appellate court recently overruled that standard.

Before 1993, the retrocedent entered into retrocessional reinsurance treaties with certain underwriters at Lloyd's. In 1996, in response to a flood of asbestos- and environmental-related claims, Lloyd's implemented a Reconstruction and Renewal Plan ("R&R Plan") under which Equitas Limited and Equitas Reinsurance Limited were created to reinsure and handle claims related to some of Lloyd's underwriters' pre-1993 liabilities. After paying asbestos-related claims to various cedents, the retrocedent sought payment from the Lloyd's underwriters under the retrocessional treaties. Equitas, which handled those claims, did not immediately pay and allegedly made demands that were not contemplated in the retrocessional treaties.

The retrocedent initiated arbitration against the Lloyd's underwriters for breaching the retrocessional treaties and, shortly thereafter, filed an action against Equitas for tortious interference with contract and state antitrust law violations. Equitas moved to stay the action pending the arbitration on the ground that resolution of the arbitration may dispose of or limit the issues raised by the action. Equitas based its position on *Belopolsky v. Renew Data Corp.*, 41 A.D.3d 322 (N.Y. App. Div. 1st Dep't 2007), an intermediate appellate court decision in which the court affirmed the stay of an action pending the resolution of a related action because "there were overlapping issues and common questions of law and fact, and 'the determination of the prior action may dispose of or limit issues which are involved in the subsequent action.'" *Belopolsky*, 41 A.D.3d at 322-23 (quoting *Buzzell v. Mills*, 32 A.D.2d 897 (N.Y. App. Div. 1st Dep't 1969)). Equitas argued that *Belopolsky* overruled the existing standard for determining whether to stay an action pending a related action or arbitration,

which looked to whether the determination of the related action or arbitration would “render academic” the issues raised in the subsequent action.

The court disagreed. It held that the *Belopolsky* court did not overrule the “render academic” standard for two reasons: first, despite the *Belopolsky* court’s use of different language, its reasoning is consistent with “render academic” precedent; and second, the decision is three sentences in length and does not distinguish or even cite the long line of “render academic” cases. In applying the “render academic” standard, the court concluded that the anti-trust claims raised in the action were independent of the breach of contract claims raised at arbitration such that resolution of the latter would not render academic the issues raised by the former. Thus, the court denied Equitas’ motion to stay the action.

The court did, however, grant Equitas’ motion to dismiss the retrocedent’s tortious interference with contract claim on the ground that the retrocedent failed to allege, among other things, that Equitas acted outside the scope of their agency or for personal profit or gain. Notably, the court did not go so far as to hold that, as a matter of law, Equitas is the agent of the Lloyd’s underwriters such that they would not be subject to similar tortious interference claims.

Texas Federal Court Retains Jurisdiction Where Third Party Has a Separate Dispute With Defendant and Federal Question Jurisdiction Exists

Huntsman Corp. v. Int’l Risk Ins. Co., No. 08-1542, 2008 U.S. Dist. LEXIS 74397 (S.D. Tex. Sept. 26, 2008).

A Texas federal court has denied an insured plaintiff’s request that its case

be remanded to state court. The insured wholly owns the cedent, which it created as a captive in order to obtain reinsurance in the international market. Reinsurance was obtained from various reinsurers, including the reinsurers in this case. The insured is covered 100 percent by the cedent, who is 100 percent reinsured by the reinsurers.

The insured’s plant was damaged in a fire during the policy term. The reinsurers paid some damages directly to the insured, but not all. The reinsurers refused to make further payments without more evaluation, and subsequently sued the insured and the cedent in federal court. The insured then filed a separate suit against the cedent in state court; the cedent attempted to tender the defense to the reinsurers, but upon rejection petitioned to bring in the reinsurers as third parties. The cedent sought judgment that the reinsurers must accept the cedent’s tender of the defense to the insured’s claims, and that if the reinsurers did not accept then they would be liable for the cedent’s damages in the litigation, or that the reinsurers accept arbitration of the dispute. Certain reinsurers removed the action to federal court, asserting federal question jurisdiction, and also claiming that there would be diversity jurisdiction if the parties were realigned to reflect their true interests. The insured moved to remand to state court.

The reinsurers argued that federal diversity jurisdiction would be created if the parties were realigned according to their ultimate interests in the lawsuit. They argued that both the insured’s and the cedent’s true purposes were to obtain payment from the reinsurers, and that the reinsurers should be realigned to be defendants against the insured and the cedent, thus gaining the right to keep the case in federal court based

on diversity jurisdiction. In rejecting the reinsurer's arguments on diversity jurisdiction, the court considered recent case law disapproving of removal from state court based on realignment of a non-defendant. The court also held that realignment was inappropriate because the plaintiff's primary purpose was to recover under the cedent's policy. Therefore, the court held that it lacked diversity jurisdiction over the case.

The court, however, sustained jurisdiction and determined that the case was properly removed because the reinsurance certificates were an indemnity that was entirely independent of the policy contract between the insured and the insurer. Therefore, the dispute between the cedent and the reinsurers was a separate matter, which could be removed if the federal court had jurisdiction.

The court held that there was federal question jurisdiction over the case because the claims included arguments governed by the Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the Inter-American Convention on International Commercial Arbitration. The federal courts consider these Conventions a matter of interest and are interpreted based on federal case law. Because the arbitration issues involved in the case triggered the Conventions, federal question jurisdiction was available and this separate dispute was properly removed to the federal court. Thus the removal of the entire case was proper in light of considerations such as fairness and convenience.

New Jersey Federal Court Dismisses Economic Duress Counterclaim Raised by Guarantors of Reinsurance Agreement

Everest Nat'l Ins. Co. v. Sutton, No. 07-722(JAP), 2008 U.S. Dist. LEXIS 62081 (D.N.J. Aug. 11, 2008).

A New Jersey federal court held that the guarantors of a reinsurance agreement must post security in the amount of \$70 million as ordered by an arbitration panel.

The guarantors, who underwrote and serviced subprime automobile loans, were engaged in negotiations with a cedent to provide default protection insurance to lenders. To encourage the cedent to enter into an insurance agreement, the guarantors executed guaranties in favor of the cedent, securing the obligations of a reinsurer under a reinsurance agreement. The cedent's motion for partial summary judgment to order the guarantors to post the security set forth in a prior arbitration award was granted. The cedent's motion to dismiss the guarantors' counterclaims was granted in part and denied in part.

The guarantors argued that the guaranties had been executed under conditions of economic duress, and, therefore, were unenforceable. The guarantors claimed that the cedent created the condition of economic duress by springing a non-negotiable demand for the guaranties at the last minute. The court disagreed, noting that the "case law is clear that 'driving a hard bargain' and 'taking advantage of another's financial difficulty' are not duress." More importantly, the court found that the duress that the guarantors may have been facing was not caused by the cedent, but rather by the guarantors themselves when they chose to negotiate only with the cedent. Furthermore, the court found that the

guarantors had failed to submit evidence that they had been subjected to economic duress in their role as guarantors of the reinsurance agreement, as distinct from their role in negotiating the original insurance agreement.

The guarantors' argument that they had been fraudulently induced to enter the agreement and to execute the guaranties failed because of the parol evidence rule. The guarantors' claim that the cedent had orally assured them that the guaranties would never be enforced contradicts the express language of the guaranties, and therefore the parol evidence rule precluded proof of these allegations.

The court, however, denied the cedent's motion to dismiss the guarantors' counterclaim that the cedent had knowingly and voluntarily elected to pay claims on loans that did not meet the cedent's underwriting standards. The cedent argued that these losses could only be raised as defense to payment under the guaranties, and had been improperly pled as affirmative claims. The court ruled that while the guaranties provide that the guarantor "may claim as a defense" that the reinsurer is not liable for, the language of the guaranties did not bar the guarantors from asserting the claim as a counterclaim.

Connecticut State Court Compels Reinsurer to Pay Pre-pleading Security

Hartford Accident & Indem. Co. v. Ace Am. Reins. Co., Cons. (X02)CV030178122S, (X02)CV030179514S, 2008 Conn. Super. LEXIS 2470 (Conn. Super. Ct. Sept. 19, 2008).

A Connecticut Superior Court granted a motion compelling reinsurers, who are not licensed to engage in the business of insur-

ance in Connecticut, to post a pre-pleading security with the court despite the reinsurers' due process objections. The cedents and reinsurers had entered into a number of excess-of-loss reinsurance treaties. When presented with claims on certain losses, the reinsurers denied their liability and refused to pay a "substantial portion" of the billed amounts. The cedents then filed suit to recoup their losses and subsequently moved the court to compel the reinsurers to post a pre-pleading security.

The cedents' motion to compel pre-pleading security was made pursuant to Connecticut General Statutes § 38a-27, which requires, as a condition precedent to entering a responsive pleading in an action, an unlicensed insurer or reinsurer to either (i) provide a security "sufficient to secure the payment of any final judgment which may be rendered in the action or proceeding" or (ii) become authorized in the state to conduct the business of insurance. A hearing was held to determine the amount owed under the pre-pleading statute. During the hearing, both sides were given the right to present evidence of the amount in dispute and the reinsurers were permitted to cross-examine the cedents' witnesses. The reinsurers objected to the scope of the hearing, claiming that it did not comport with their due process rights because the court prevented them from presenting defenses to the claims asserted, which, if successful, would have eliminated the need for or reduced the amount of any required security.

Drawing on both persuasive and binding authority, the court explained that the strictures of due process were not offended in a pre-pleading security hearing when, as here, the reinsurers received an opportunity to be heard on the amount owing. Due process, the court held, was satisfied when

– after the cedents' submitted "some proof that contracts existed," and proof that "billings were made under the auspices of those contracts, and the bills remain unpaid" – the reinsurers were able to "cross-examine the presented witnesses and offer [their own] proof that the bills were paid or that the amounts were incorrect." Moreover, the court made plain that the scope of a pre-pleading security hearing was never intended to be so broad as to include all of the reinsurers' defenses. In fact, the court said that the fundamental policy behind the statute was simply to ensure that an unlicensed insurer or reinsurer has "sufficient assets [in Connecticut] to satisfy *any* judgment" (emphasis added) rendered against it as a result of the litigation. Thus, a pre-pleading security hearing need only establish the potential amount owed and need not "resolve the dispute on the merits or predict the outcome of the case."

In addition to the due process argument, the reinsurers argued that because the litigation would advance in stages – trying issues specific to certain reinsurers at different times – they should be permitted to pay any pre-pleading security incrementally and simultaneously with their involvement in the dispute. This argument failed as well. The court held that "the security must be filed before any pleading" and stated that "[t]he defendants do not get to choose the time for posting pre-pleading security just because the case may be long and complex."

Missouri Federal Court Rules Reinsurer Must Follow the Settlements of Cedent
Employers Reins. Corp. v. Mass. Mut. Life Ins. Co., No. 06-0188-CV-W-FJG, 2008 U.S. Dist. LEXIS 63420 (W.D. Mo. Aug. 19, 2008).

In a dispute over individual disability income policies, a reinsurer brought a breach of contract claim against its cedent alleging that the cedent had mishandled a wide number of claims. The reinsurer and cedent had disputes about the cedent's claims adjudication procedure since 1997 or 1998 and had entered several Claims Review Agreements that provided for an outside consultant to review the cedent's claims handling procedures. These Claims Review Agreements both contained provisions for the cedent to "be the final decision maker in all benefit determinations." The cedent counterclaimed against the reinsurer for improperly offsetting the amounts that the reinsurer had paid in the past on claims it was disputing against the amounts currently due to the cedent for undisputed claims.

The reinsurer sought summary judgment that it was not required to follow the cedent's settlement decisions, arguing that there was no "follow-the-settlements" or "follow-the-fortunes" provision in the contract. In ruling against the reinsurer, the court found that "follow-the-settlements" is a widely recognized doctrine in the reinsurance industry. The court noted that under the doctrine, the cedent's decisions in adjusting and settling claims were binding on the reinsurer, and the reinsurer could only challenge claims by the cedent on the grounds that they were fraudulent or made in bad faith or, alternatively, that they were outside the contract of reinsurance. The court held that the language in the contract, which provided that the cedent would investigate, pay, settle or defend policies, constituted a follow-the-settlements clause and found for the cedent. The reinsurer asked the court to reconsider or certify the question of whether the contract contained a follow-the-settlements clause for interlocutory

appeal. In denying the request, the court held that there was no reason present for reconsideration and that the presence of a follow-the-settlements clause was a question of applying law to facts and not a pure question of law.

California Federal Court Grants Default Judgment in Favor of Cedent Against a Captive Reinsurer

Frontier Ins. Co. in Rehabilitation v. Ramona Tire, Inc., No. 07-CV-0052-H (S.D. Cal. Sept. 23, 2008).

A California federal court recently granted a motion for default judgment and a default judgment for damages against a captive reinsurer.

The cedent was approached by the insured to obtain a workers' compensation insurance policy. An agreement was reached, and as part of the deal the insured created a "captive" insurance company to reinsure the cedent. The reinsurer agreed to reimburse the cedent for the first \$250,000 of any single claim made by the insured under the policy. The cedent paid all of the claims under the policy, but the reinsurer failed to reimburse the cedent for the bulk of the payments owed.

The court found that the cedent had adequately alleged both an enforceable contract and breach of that contract. The court accepted these allegations as true for the purposes of the request for default judgment, and also found that there was little chance of a dispute over these facts because the reinsurer had actually informed the cedent that it "will allow judgment to be entered by default and pay all the available funds to [the cedent]."

The court found the compensatory damages requested by the cedent to be ade-

quately supported by the evidence, and thus awarded damages equal to those demanded in the pleadings. Prejudgment interest of ten percent was also granted.

Mississippi Federal Court Grants Partial Summary Judgment to Reinsurer on Claims of Cedent's Agents as Third-Party Beneficiaries Under Reinsurance Agreement

Mike Robinson v. Guarantee TrustLife Ins. Co., Case No. 2:00-CV-243-B-B, 2008 U.S. Dist. LEXIS 72255 (N.D. Miss. Sept. 22, 2008).

A Mississippi federal court has granted partial summary judgment to a reinsurer on claims of tortuous and fraudulent conspiracy and concealment arising via the cedent's selling agents' possible third-party beneficiary status in the reinsurance agreement.

The plaintiffs are selling agents of the cedent whose claims arose from an Assumption Reinsurance Agreement entered into between the reinsurer and the cedent. Under the agreement, the reinsurer assumed the cedent's obligation to pay continuing commissions on assumed policies to the agents who originally sold them. The selling agents had previously settled with the cedent in Mississippi state court on allegations that the cedent engaged in improper practices related to inactive or replaced insurance policies in an effort to cut the original selling agents out of commissions by directly offering replacement insurance to insureds. The agents alleged that the reinsurer acted in the same manner as the cedent had previously done in order to convert the cedent's existing policies to policies under the reinsurer thereby cutting the agents out of more commissions.

The reinsurer removed the cases to federal court in October 2000, where the magistrate judge overseeing the pretrial process entered an order consolidating the cases for trial. The district court had previously granted the reinsurer partial summary judgment finding "no evidence that [the reinsurer] was obligated to pay plaintiffs commissions on [cedent's] inactive or replaced policies or on replacement policies" and further finding "no evidence that [the reinsurer] was contractually restricted from offering replacement coverage to its insureds." On appeal, the Fifth Circuit affirmed that there was no novation of the plaintiffs' agency contracts under the cedent with the reinsurer, but found genuine issues of material fact concerning whether the agents were third-party beneficiaries of the reinsurance agreement. The Fifth Circuit further stated that derivative claims such as breach of contract, fraud, and negligence survived summary judgment at that stage.

In granting the reinsurer's motion for partial summary judgment on claims arising from the cedent's conversions via the plaintiffs' possible third-party beneficiary status in the reinsurance agreement, the district court found that the agents had failed to carry the burden of directing the court to evidence that the reinsurer "was involved in a conspiracy with [the cedent] prior to the reinsurance agreement or engaged in fraudulent acts against the plaintiffs prior to the reinsurance agreement." The court denied the reinsurer's motion for summary judgment on the issue of punitive damages and carried that matter forward to trial, but granted the reinsurer's motion to vacate the consolidation order.

Pennsylvania Federal Court Dismisses Insured's Breach of Contract Action Against Reinsurer and Third-Party Administrator

Samuel W. Brand v. AXA Equitable Life Ins. Co., No.08-2859, 2008 U.S. Dist. LEXIS 69661 (E.D. Pa. Sept. 16, 2008).

A Pennsylvania federal court has granted a motion to dismiss brought by a reinsurer and a third-party administrator for failure to state a claim upon which relief can be granted. The motion sought dismissal of the cedent's action for breach of contract and bad faith.

The insured purchased a disability insurance policy from the cedent. The cedent entered into a contract with the reinsurer under which the cedent would be reimbursed the entirety of its losses under its disability insurance policies. Together, the cedent and reinsurer contracted with a third-party administrator for a number of disability policies, including that purchased by the insured.

After being injured in a motor vehicle accident, the insured filed a claim for total disability benefits. Over two years later, the third-party administrator advised the insured that he was entitled to only residual disability benefits under his policy. The insured brought this diversity action against the cedent, reinsurer, and third-party administrator alleging bad faith conduct in the handling of his claim and breach of contract for denial of total disability benefits.

In granting the motion to dismiss, the court examined the contractual relationship between the cedent and the reinsurer and determined that the insured did not constitute a third-party beneficiary of the con-

tract. The intention that the insured benefit from the reinsurance agreement was not expressly stated in the contract, and no surrounding circumstances existed that would indicate such an intention. Additionally, the insured failed to demonstrate any compelling circumstances, such as insolvency of the cedent, that would entitle him to status as a third-party beneficiary.

The same result followed for the third-party administrator. The court found no express intention or other circumstances indicating that the insured be permitted to obtain satisfaction directly from the third-party administrator as a third-party beneficiary.

The insured's claim for bad faith arose out of Pennsylvania's bad faith statute, 42 Pa. Cons. Ann. § 8371. Under the statute, relief is permitted only for bad faith conduct by the insurer towards the insured. The court considered to what extent the non-cedent defendants acted as the "insurer." The court was unable to find that the reinsurer constituted an "insurer" under the circumstances, as it had not been assigned the policy and had no other direct relationship with the insured. Further, a third-party administrator engaged by a cedent is not deemed to be an "insurer" under Pennsylvania law.

Managing General Underwriter's Claims for Interference With and Breach of Reinsurance Contract Are Dismissed

TIG Ins. Co. v. Titan Underwriting Managers, LLC, No. M2007-01977-COA-R3-CV (Tenn. Ct. of App. Nov. 7, 2008).

A Tennessee appeals court affirmed the dismissal of various claims by a managing general underwriter against its principle, including a claim for tortious interference with the reinsurance contract that the MGU

put in place between the cedent and the reinsurer. The underlying business was health and life stop-loss insurance for self-insured employer groups, which was produced and written by the MGU on behalf of the cedent. As part of the MGU's responsibilities, it arranged for reinsurance covering the stop-loss policies. Ultimately, the cedent terminated the stop-loss program, directed the MGU to stop its activities, and cancelled the reinsurance contract. The cedent sued the MGU for a declaratory judgment and the MGU counterclaimed based on tortious interference and related claims. The trial court granted the cedent's motion to dismiss the counterclaims and this appeal ensued (eventually).

In affirming the dismissal of the counterclaims, the appeals court reiterated the basic principle that a party to a contract cannot be liable for tortious interference with that contract. On that basis, the MGU's claim that the cedent interfered with the reinsurance contract failed. The MGU's claim for breach of that contract also failed because there was no evidence that the MGU was considered a third-party beneficiary to the reinsurance contract.

New York Federal Court Denies Attorney-Client Privilege and Work Product Protection to Documents Pertaining to Claims Investigation By a Reinsurer

AIU Ins. Co. v. TIG Ins. Co., No. 07 Civ. 7052, 2008 U.S. Dist. LEXIS 66370 (S.D.N.Y. Aug. 28, 2008).

In response to a motion to compel production of documents contained in the reinsurer's privilege and redaction logs, a New York federal court ordered many of the withheld documents to be produced. The cedent brought an action based on the reinsurer's failure to pay amounts due under

reinsurance contracts. Under the reinsurance contracts, the cedent was required to provide the reinsurer with prompt notice of any occurrence likely to involve the reinsurance contract, and the reinsurer was permitted to inspect the cedent's records pertaining to any reinsured policies. The reinsurer asserted lack of prompt notice as a defense to the cedent's action.

In granting the cedent's motion to compel production of certain documents, the court agreed with the cedent that many of the documents were not subject to attorney-client privilege. The court noted that even documents created by an attorney are not subject to attorney-client privilege when created in the course of investigating a claim, and that in-house counsel often gives business advice, rather than legal advice, and that these documents are not protected.

The cedent claimed that the documents to which the reinsurer claimed attorney work product privilege were created as part of the reinsurer's investigation of the cedent's claim for coverage in the ordinary course of business. The cedent argued that the reinsurer never denied the claim for coverage and that the reinsurer had audited the cedent's records under the access-to-records clause in the reinsurance contract. The court agreed with the cedent's position on most of the documents, noting that "[a]pplication of the work-product doctrine to an insurance company's claims files has been particularly troublesome because it is the routine business of insurance companies to investigate and evaluate claims," and that documents contained in a claims file that are a part of the ordinary course of the insurer's business are not afforded work-product protection. In reaching this

decision, the court relied on a presumption that documents prepared prior to a coverage decision are prepared in the ordinary course of an insurer's business. The presumption may be rebutted if the insurer can demonstrate that it possessed a "resolve to litigate" when the documents were created; however, neither the reinsurer's retention of outside counsel nor its explicit reservation of rights in communications with the cedent was sufficient to demonstrate such a "resolve to litigate" because the reinsurer continued to investigate the claim without denying it. The court also noted that some courts have followed a more flexible, case-by-case approach.

Mississippi Federal Court Orders Discovery on Interpretation and Investigation of Insurer Liability and Denies Discovery of Reinsurance Documents

Bituminous Cas. Corp. v. Smith Bros., Inc., No. 2:07-cv-354-KS-MTP, 2008 U.S. Dist. LEXIS 81915 (S.D. Miss. Sept. 22, 2008).

An insurer sought a declaratory judgment that it had no duty to defend in an underlying action arising from an automobile accident. The insurer joined the underlying plaintiffs in the action. The underlying plaintiffs sought discovery of various documents, including: (1) other policies not related to the insurance policy at issue, (2) documents relating to other policyholders not involved in the litigation, (3) information about the insurer's reinsurance agreements, and (4) the establishment of reserves.

The insurer resisted discovery on the ground that the information requested had no relevance to the action. The court held that the insurer must disclose: (1) its reservation of rights in regard to the underlying action, (2) information about the negotiation and formation of the policy at issue,

and (3) information related to the insurer's investigation of the accident at issue in the underlying litigation. The court stated that the insurer opened the door to the disclosures by suing the underlying plaintiffs and by making their investigations and interpretations of the policy an issue in their amended complaint. The court found the remaining requested documents, including reinsurance information, to be irrelevant to the current action and therefore not discoverable.

Connecticut Appellate Court Reverses Decision to Grant Insured Discovery Against Reinsurer

H & L Chevrolet, Inc. v. Berkley Ins. Co., 955 A.2d 565 (Conn. App. Ct. 2008).

A Connecticut appellate court reversed the judgment of a trial court granting a bill of discovery against a reinsurer. The court held that an insured had not met its burden in demonstrating that it had a potential cause of action against a reinsurer and could not compel discovery of information relating to a reinsurance agreement.

The insured had issued a number of extended warranty contracts to its customers and purchased insurance to cover those warranties, believing the policy to be backed by reinsurance. Although the cedent did have reinsurance at the time it sold the insurance policy, the reinsurance only covered losses from warranties that occurred during the coverage period, which was set to expire within a month of the insurance policy's issuance. The cedent did not inform the insured that its reinsurance was about to lapse and would not be renewed. The insured continued to issue warranties and the cedent honored its obligations under the insurance policy. Nearly

two and half years later, however, the cedent filed for bankruptcy and was declared insolvent. The insured then sought reimbursement for claims paid under the warranty contracts directly from the reinsurer.

When the reinsurer refused to pay, the insured petitioned the court for a bill of discovery in order to determine whether it had a cause of action against the reinsurer for breach of contract, fraud or unfair practices. Under Connecticut law, a party seeking a bill of discovery must demonstrate that probable cause exists to bring an action and that the information sought is necessary to the prosecution of the action.

The court held that there was no probable cause to believe that the reinsurer breached its contract with the cedent, noting that the reinsurance agreement, which the reinsurer voluntarily disclosed, unambiguously stated the terms and the period of coverage. Moreover, the agreement demonstrated that the cedent declined to purchase run-off coverage, which would have covered all warranties that were written, but unexpired at the time the reinsurance agreement lapsed. The court noted also that the reinsurer was not obligated by the agreement or by statute to notify the insured or the insurance commissioner that the reinsurance would not be renewed. In rejecting the insured's allegation of fraud, the court found that the only representation on which the insured relied – that the cedent had reinsurance – was true at the time it was made and was made by the agent who brokered the insurance policy, not by the reinsurer. Finally, the court ruled that the reinsurer did nothing to violate Connecticut's unfair trade practices statute.

**Pennsylvania Federal Court Admits
Previously Excluded Evidence**

United Nat'l Ins. Co. v. Aon Ltd., No. 04-539,
2008 U.S. Dist. LEXIS 81825 (E.D.P.A. Oct.
15, 2008).

In a complex litigation involving various reinsurance agreements, a Pennsylvania federal court admitted five pieces of evidence it had previously excluded, finding that the cedent had cured the defects in the evidence and had met the "slight burden" required to overcome the authentication hurdle.

The parties had been battling over the admissibility of documentary evidence and deposition testimony in advance of their trial. The court had previously excluded a fax for lack of authentication, ruling that it needed "markings plus more" – some additional circumstances or testimony that supported its reliability. The fax was sent by an employee of the broker on a company fax sheet. The cedent presented a sworn affidavit by the individual at the broker stating that she recognized the communication, that she wrote it, and that the exhibit was authentic. The court noted that the burden of authentication is light, and that a proponent can authenticate evidence in a variety of ways, including testimony by a witness with direct knowledge of the evidence's authenticity or by pointing to "distinctive characteristics" that, under the circumstances, suggest reliability. Therefore, the court admitted the fax as evidence, basing its decision on both the affidavit and the fax's distinctive markings.

The court also admitted three exhibits that were or relied on financial data generated by the cedent's computer system. In support of its motion to admit this evidence, the plaintiffs included a detailed affidavit from its Chief Financial Officer describing the computer system and his knowledge and oversight of its operation. The court found that because the CFO managed the computer system and was familiar with the activities recorded by the computer system and with the computer system itself, he was a "qualified witness." The court also found that the documents were trustworthy because the cedent's business appeared to "hinge substantially on the regular use and proper working of the computer system," and because the CFO attested that the information contained in the exhibits was: 1) recorded contemporaneously with the activities described; 2) logged at the instruction of plaintiffs' staff with direct knowledge of the information and activities; and 3) kept and maintained as a regular part of the plaintiffs' business activities.

This case gives us a peek behind the curtain of admissibility of evidence in a complex reinsurance dispute. Of course, all these issues of authenticity would not be an issue if the parties were not fighting over what appears to be every scrap of evidence. The lesson is to make sure that important documents are authenticated in the deposition process or by other means to avoid spending time and money fighting over authenticity issues on the eve of trial.

Recent English Case Summaries:**Interpretation of a Claims Cooperation Clause – No Summary Judgment for the Reinsurer**

Markel Capital Ltd v Gothaer Allgemeine Versicherung AG and others [2008] EWHC 2517 (Comm).

In this case the reinsurer refused to pay a claim under the reinsurance of a D&O policy and applied for summary judgment against the cedents on the basis that the claims cooperation clause (CCC) in the reinsurance had not been satisfied. The judge refused to grant the reinsurer's application in finding that the cedents had a reasonable prospect of defeating the case as: (i) it was not clear whether the CCC had been incorporated into the reinsurance, and (ii) the reinsurer was relying on knowledge of persons other than the defendants to trigger it.

The cedents were two German insurers and members of a pool that wrote D&O liability business. Although it was outside of pool guidelines and the pool declined the business, the cedents wrote a D&O policy for a German bank, which they reinsured with the reinsurer.

A claim was made against the bank arising from alleged liabilities of the members of the bank's management board. The lead underwriter settled the claim for €14.75 million plus costs. The cedents paid their share of the settlement and sought payment under their reinsurance. In response, the reinsurer issued proceedings seeking a declaration that it was not liable under the reinsurance because a condition precedent to its liability had not been satisfied. The cedents disputed this and counterclaimed. They also issued Part

20 proceedings against the Lloyd's broker who brokered the reinsurance on their behalf. The reinsurer applied for summary judgment alleging that the cedents had no reasonable prospect of defeating the case.

The reinsurer argued that it was not liable under the reinsurance because the contract contained a CCC providing it was a condition precedent to liability that if the cedents knew of any circumstances that may give rise to a claim against them, they should advise the reinsurer within 30 days. The live issues before the court were: (i) whether the CCC was agreed as a term of the reinsurance and (ii) whether the knowledge of the pool manager amounted to knowledge of the cedents. (It was established that there was a delay between the pool manager learning of the circumstances and notice being given by the cedents to the reinsurer).

Relating to (i), the CCC was not agreed at the time that the reinsurer subscribed to a slip presented by the broker on June 16, 2000. The reinsurer argued that it was agreed later in January 2001, when a copy was scratched by a deputy underwriter. A copy of this CCC was included in the reinsurance contract processed by the LPSO in November 2002. The cedents cast doubt on the agreement because the quality of the CCC that was bound with the slip was not of the brokers' usual quality. They also argued that the CCC that was processed by the LPSO was not in relation to the bank's risk, but another risk entirely.

The judge disagreed that there should be summary judgment on (i) relying, among other things, on the fact that the reinsurance contract presented to the LPSO was not drawn up in accordance with the broker's usual practice. This prompted the

question whether the broker might have made some mistake in its procedures that led to the CCC being included in the reinsurance contract. The judge also identified that there was no obvious reason for the parties to agree the wording of a CCC for the reinsurance during the busy renewal period.

On (ii), the issue was whether the knowledge of the pool manager was enough to trigger the CCC. This involved analysis of the contractual description of “the Reinsured” (who upon knowledge of circumstances shall advise the Reinsurers) in the CCC. The reinsurer relied upon the definition of the cedents in the slip policy as “as per” VOV (VOV being the pool manager) to mean that the cedents were acting by the pool manager for all purposes connected with the reinsurance. Knowledge of the pool manager could therefore trigger the CCC.

The judge rejected the reinsurer’s argument because it did not fit some of the uses of “the Reinsured” in the slip policy. The judge said that it would not be unnatural for a slip contract of this kind to specify that “the Reinsured” was entering into it through an agent. The pool manager’s knowledge could not start time running under the CCC for advising the reinsurer of relevant circumstances. The judge, therefore, declined to give summary judgment on the reinsurer’s claim or on any of the issues before it.

The Court of Appeal Decides What Is a Misrepresentation to Reinsurers and What Is Not

Limit No 2 Ltd v Axa Versicherung AG [2008] All ER (D) 115 (Nov) - 12 November 2008.

The Court of Appeal in this case dismissed part of the appeal in agreeing with the deputy judge that it was a misrepresentation for the reinsured’s broker to say in a fax that the reinsured would not normally write certain risks unless the original deductible was at a certain level or preferably at a higher level. This applied to the first treaty and its extension by endorsement. But the appeal was allowed in part to the extent that the representation of intention in the fax did not apply to a second treaty because such a representation cannot last forever.

The appellant managed two Lloyd’s syndicates (the reinsured) whose reinsurance brokers approached the respondent reinsurers proposing a fac/oblig reinsurance treaty relating to construction and operating risks of oil rigs. On July 4, 1996, the broker sent a fax to the reinsurer comprising a draft slip and information sheet provided by the syndicates to which it attached a front sheet saying “*As a matter of principle [the syndicates] maintain high standards and would not normally write construction unless the original deductible were at least £500,000 and preferably £1,000,000.*” The reinsurers entered into the treaty for 12 months from July 1, 1996. It was extended by endorsement to January 31, 1998. A second treaty was written for 12 months up to January 31, 1999.

Reinsurers procured an audit in 2005 and found that most of the relevant risks ceded by the syndicates had deductibles lower than £500,000 let alone £1 million. Reinsurers sought to avoid on the grounds that the broker’s statement in the fax was a representation that (i) on July 4, 1996 and earlier the syndicates had a practice of writing risks with the stated deductibles; or (ii) on July 4 the syndicates had the intention to write risks in the future with the stated

deductibles; or (iii) this practice or their intention could be relied upon as an indication or guide as to future underwriting practice. It was alleged that one or more of the representations had been false, material to the risk, intended to be acted upon and induced reinsurers to write the treaties. On this basis the treaties could be avoided.

At first instance the deputy judge held (i) the sentence in the fax relied on as a representation was a statement of the syndicates' current policy as regards deductibles; (ii) in 1996 it was not the syndicates' policy to write construction risks unless the deductible was at least £500,000 or preferably £1 million which was a misrepresentation; (iii) the syndicates acted in good faith because their underwriter had not seen the broker's fax cover sheet; (iv) the misrepresentation was material; (v) it had induced the 1996 treaty, which could be avoided and the endorsement could also be avoided because it was an extension to the treaty or the representation was effective in July 1997; and (vi) the representation was also effective in February 1998 and the second treaty could also be avoided.

The syndicates appealed on four grounds:

- (i) The conclusion that it was not the syndicates' policy in July 1996 to write with the stated deductibles had been reached on an unfair basis (current practice had not been investigated at trial) and was wrong. Judgment should be entered for the syndicates or the case remitted to the deputy judge to determine what the policy was in 1996 after discovery and evidence.
- (ii) Even if the broker's fax had been a statement of the syndicates' intention in July 1996 to write business with those deductibles it was no more

than a statement of expectation or belief and it had been a statement by the syndicates' broker and not by the syndicates' themselves.

- (iii) The endorsement was a separate contract and the same arguments applied to it as to the 1998 treaty.
- (iv) The judge was wrong to hold in both June 1997 and January 1998 that the representations of the syndicates' current policy from July 1996 were continuing representations or that there was any obligation on the syndicates to disclose that their policy had changed.

In deciding the case, the Court of Appeal dealt with the four bullet points above:

- (i) Longmore LJ found that the deputy judge had not made any incorrect findings about the syndicates' pre-July 1996 practice. He had said correctly that the policy and therefore the practice was maintained. What did not exist was the intention to continue that practice. In addition, on the basis of the evidence of the syndicates' underwriter, the deputy judge was entitled to come to the view that the syndicates had no policy – or intention – to write construction risks with the stated deductibles.
- (ii) Longmore held that the statement in the fax was a statement of intention, which was a representation of existing fact. Once it had been decided that the fax cover sheet did contain a representation that the syndicates intended to write business with the stated deductibles it was not seriously arguable that it was a statement of opinion or expectation or belief. It was not relevant that the statement was made by the brokers who could have had no more than an expectation of what the underwriter would do in the future. The brokers were the agents of

the syndicates to present the risk and therefore it amounted to a statement of the syndicates of their intention.

- (iii) Longmore said that it would be artificial to regard the endorsement as a new contract. It was an extension or variation of the existing contract. It was avoidable for misrepresentation.
- (iv) Two questions arose: Did the representation of July 1996 of the syndicates' intention continue to be effective? Was there any obligation on the syndicates to disclose that their policy had changed? Longmore held that any statement of intention would be intended to operate when the risk began and would continue up until that time. It did not follow that it would operate on renewal and the 1998 treaty was, without doubt, a new contract. The time when a representation of intention was spent was well before 19 months. Whatever the syndicates' intention was as to deductibles in July 1996 had become irrelevant by February 1998. It put "too much weight" on a representation of intention relating to deductibles to say that it must be taken to still be operative after a lapse of 19 months. Longmore did not think that a court should struggle to hold that everything said at inception should be impliedly repeated on renewal. Finally, the argument that the syndicates should have disclosed their intention had changed

also failed. It just repeated the same argument a different way.

Therefore the deputy judge's decision on the 1996 year and 1997 endorsement was upheld, but the order on 1998 was set aside. Longmore noted that the litigation may not be finished because the deputy judge was unable to reach a final conclusion on the 1998 year if he was wrong on the points he decided (which he was).

Follow-the-Settlements – the House of Lords Will Decide

Wasa Intern'l Ins. Co. v Lexington Ins. Co. [2008] EWCA Civ 150.

We reported on the Court of Appeal's decision in this case in the Dewey & LeBoeuf June 2008 *Reinsurance Newsletter*. It challenged the English courts' approach that reinsurers do not have to follow the settlements where there is a difference between the insurance and reinsurance contracts. The finding that the insurance and reinsurance were back-to-back, and that the policy period clause was one of the "as original terms" would mean that reinsurers must pay for decades of pollution clean-up falling outside of the three-year reinsurance period. These complex issues will now be decided by the House of Lords on May 5, 2009

Recent Regulatory Developments

Contract Certainty Comes to New York

On October 16, 2008, the New York Insurance Department issued Circular Letter No. 20 (2008). This Circular Letter set forth the Department's position and expectations concerning contract certainty for property/casualty insurance policies and "all reinsurance contracts." Insurers and producers doing business in New York have no more than 12 months to develop and implement practices to assure that policy documentation is delivered to insureds before or promptly after inception of the contract.

The Circular Letter defines contract certainty as "the complete and final agreement of all terms to an insurance policy or reinsurance contract by the date of inception, and the issuance and delivery of the policy or contract before, at, or promptly after inception." The Department set forth its expectations that the insurance industry in New York would adhere to a set of reasoned principles and practices to enhance contract certainty. "Promptly," as defined by the Circular Letter, generally means within 30 days, with any extensions carefully documented. The Department has asked the industry to strive for contract certainty in at least 90 percent of contracts not already subject to a more stringent requirement.

Recent Speeches and Publications:

Hugh McCormick will be speaking on the "Decline of the Capital Markets: Obtaining Financing and Reducing Risk in the Wake of the Credit Crunch," at the American Conference Institute's Third Annual Legal and Strategic Forum on Life Reinsurance, on January 26-27, 2009, in New York City.

Larry Schiffer will be speaking on "E-Discovery in Reinsurance Arbitrations," at the Harris Martin Reinsurance Conference, on March 26, 2009, in Miami, Florida.

Deirdre Johnson will be speaking on "Reinsurance Principles," at PLI's Understanding Insurance Law 2009 conference, on April 6, 2009 at the PLI Center in New York City.

Deirdre Johnson will be speaking at the American Conference Institute's Contract Wording Seminar, in late April 2009.

John Nonna will be participating as a panelist at a "Bonus Session: Mediation with a Fact Pattern," at the Mealey's 16th Annual Insurance Insolvency & Reinsurance Roundtable, on April 23, 2009, in Scottsdale, Arizona. Dewey & LeBoeuf will be sponsoring the Keynote Speaker breakfast on Thursday, April 23, 2009, at the Roundtable.

Larry Schiffer spoke on depositions and document discovery in reinsurance arbitrations at the ARIAS-U.S. Arbitrator Training Seminar, "The Powers of Arbitrators: Discovery Legal Standards," on November 5, 2008, in New York City.

Larry Schiffer moderated a panel on the "Purchase and Sale of Reinsurance Recoverables," at the AIRROC/Cavell Commutations and Networking Event Educational Sessions Developed by LexisNexis Mealey's, on October 20, 2008, at the Meadowlands, New Jersey.

Larry Schiffer spoke on "Minimizing Disputes between Cedents and Reinsurers: Dispute Hotspots and Resolution Strategies," at the American Conference Institute's Forum on Reinsurance Claims & Arbitration, on September 24-25, 2008, in New York City.

Bill Marcoux spoke on "Selecting the Right Classification for Long-Term Success of Your Reinsurance Operations," at the American Conference Institute's ReAct Brazil International Forum on Positioning for Success in the Brazilian Reinsurance Market, on September 24, 2008, in Miami, Florida.

John Nonna spoke on a panel entitled "The Board Room – Emergency Meeting: Interactive Crisis Management Hypothetical," at the Practising Law Institute's Reinsurance Law 2008 program on September 17, 2008, in New York City.

Larry Schiffer's article, "You Too Can File an Electronic Brief," was published as a Tech Tips in the ARIAS-U.S. Quarterly, Third Quarter 2008, p. 20.

Larry Schiffer's article, "Arbitration in Run-off – The Receivership Anomaly – Part 2," was published in *AIRROC Matters*, the magazine of the Association of Insurance and Reinsurance Run Off Companies, in its Fall 2008 issue.

The Reinsurance Newsletter is a publication of Dewey & LeBoeuf LLP, and is not intended as legal advice regarding specific transactions or matters. Authors contributing to this newsletter are: Larry P. Schiffer, Editor, Jo Marshall, Catherine J. Archibald, Rachel Berk, Michael J. Davis, John T. DiNapoli, Brendan H. Jordan, Brian J. LaClair, Adam L. Lounsbury, Ryan W. Lang, Evan T. Lee, Melissa S. Geller, Alan Maguire, Mahbod Moghadam, Yevgeniy Markov, Sabrina A. Miesowitz, Erin J. Reichenbach, Jeremy D. Scholem, Carla Small, Timothy Stapleton, Jennifer M. Stewart, and Travis M. Tatko. For further information, please contact your responsible Dewey & LeBoeuf lawyer at:

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