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Since its founding in 1901, Hunton & Williams has prided itself on excellence and hard work. Over the course of the last 100 years, the firm has experienced tremendous growth and currently consists of more than 850 attorneys in 17 offices in the United States, Europe, and Asia.

**Reasonable Discovery in Reinsurance Arbitrations**

Too little. Too much. Just right. Like Goldilocks' search for the right porridge, there is an ongoing search for the right balance of discovery in reinsurance arbitrations. Some critics have complained that arbitration has grown too expensive and lengthy, and have pointed to severely limiting discovery as a means to expedite the arbitration process and control costs. In response to these concerns, arbitration panels regularly curtail pre-hearing discovery by refusing to allow interrogatories and requests for admission. Disallowing these methods of discovery outright, however, may go too far, particularly where a dispute may have been ripe for summary disposition had reasonable interrogatories and requests for admission been permitted.

Unlike court proceedings, where the scope of discovery is reasonably well defined, in reinsurance arbitrations, the panel, guided by the parties, has to establish the discovery rules for each dispute. While some advocate very broad discovery rules based on the Federal Rules of Civil Procedure or analogous state rules, these rules generally allow for very broad discovery based on potential relevance, instead of admissibility. This distinction can lead to extremely broad and expensive discovery requests. Panels with specialized expertise, however, may reject overbroad discovery, such as deposition and document discovery, that seeks largely tangential information.

The desire to expedite the process and cut the expense, however, may backfire

when discovery is too limited. Often a number of the benefits of discovery are overlooked. Perhaps most significantly, discovery helps parties narrow their dispute. Frequently, some part of a reinsurance dispute may revolve around a limited set of facts and people. Discovery specially tailored to these issues can allow them to be brought to the panel for summary disposition in advance of an all-encompassing hearing.

Allowing a summary disposition of certain issues can benefit both parties. Hearings can be extraordinarily expensive. It is not uncommon to have more than half-a-dozen lawyers and the arbitration panel all billing at the same time, in addition to travel expenses and client time. If a panel, otherwise trying to control overbroad discovery, is amenable to allowing reasonable discovery on dispositive issues, it may save the parties and the panel time and money by permitting the summary resolution of certain issues, which may allow the parties to settle the overall dispute.

Permitting the parties reasonable discovery, including a reasonable number of interrogatories and requests for admission, also prevents unfair surprise at the hearing. No cedent or reinsurer enters into an arbitration provision expecting that there will be "trial by ambush." When key discovery devices are eliminated in their entirety, the fairness of the process becomes suspect. In some cases an extreme deprivation of discovery may

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raise due process concerns or support vacating the award under the Federal Arbitration Act (“FAA”). See *Home Indem. Co. v. Affiliated Food Distribs.*, 1997 U.S. Dist. LEXIS 19741 (D.N.Y. 1997) (holding that the FAA requires “fundamental fairness”).

In particular, the FAA allows federal courts to vacate arbitration awards where panels refuse “to postpone the hearing, upon sufficient cause shown.” 9 U.S.C. 10. If the parties have not been able to narrow the issues through discovery, a party may be unfairly surprised at the hearing and need a continuance to assemble and present evidence to rebut the surprise. If the panel refuses to grant a continuance, this may be cause for vacating the panel’s award. See *Local Union No. 251 v. Narragansett Improv. Co.*, 503 F.2d 309, 312 (1st Cir. 1974) (indicating that unfair surprise may be a ground-requiring postponement); cf. *Tempo Shain Corp. v. Bertek, Inc.*, 120 F.3d

16, 21 (2d Cir. 1997) (vacating award where a panel refused to continue the hearing to allow an individual to testify); but see *Burton v. Bush*, 614 F.2d 389,



390 (4th Cir. 1980) (holding there is no general right to pre-hearing discovery in arbitration).

Another often overlooked benefit of pre-hearing discovery is the preservation

of evidence that may inadvertently be destroyed. While ten or fifteen years ago it was uncommon to see emails as evidence in a reinsurance arbitration, today they are ubiquitous, but the preservation of them is not. Companies routinely delete emails that may be the subject of a dispute simply because no one takes the time to safeguard them from pre-scheduled computer housekeeping. Allowing reasonable pre-hearing discovery may preserve evidence that is later determined to be critical.

While most courts have heavy dockets, arbitration panels employed by the parties are in a better position to actively manage the discovery process. A relatively small effort by panels and the parties early on in the arbitration process to define the scope of reasonable and tailored discovery will, in most cases, promote a fair and efficient arbitration. Without reasonable discovery, a fair resolution on the merits is undermined, and costs may actually be increased in some arbitrations.

## Arbitration Panel Exceeded Its Powers In Concluding Cedent’s Agent Entitled To Indemnification

A Texas federal court held that an arbitration panel exceeded its authority when it determined, contrary to a prior court ruling, an agent of a cedent was entitled to indemnification for negligent claims handling. See *HCC Aviation Ins. Group, Inc. v. Universal Loss Mgmt., Inc.*, No. 3:05CV744M, 2005 U.S. Dist. LEXIS 19992 (N.D. Tex. Sept. 13, 2005). Employers Reinsurance Corporation (“Employers”) reinsured Ranger Insurance Company (“Ranger”) and HCC Aviation Insurance Group, Inc. (“HCC”), which was a “claims handling facility” for Ranger. Employers and Ranger sued HCC and HCC’s agent Universal Loss Management, Inc.

(“ULM”), another claims handling facility, for negligent claims handling. HCC and ULM moved to dismiss the claims asserting, among other things, that HCC was entitled to indemnification from Employers under a reinsurance treaty, as was ULM as HCC’s agent.

The trial court refused to dismiss the claims reasoning that ULM was not entitled to indemnification from Employers, and that while HCC was potentially indemnified under the treaty for its own actions, it would not be entitled for indemnification for acts ULM committed as its agent. The court then ordered that the remaining disputes between the parties be arbi-

trated under an arbitration provision contained in the treaty.

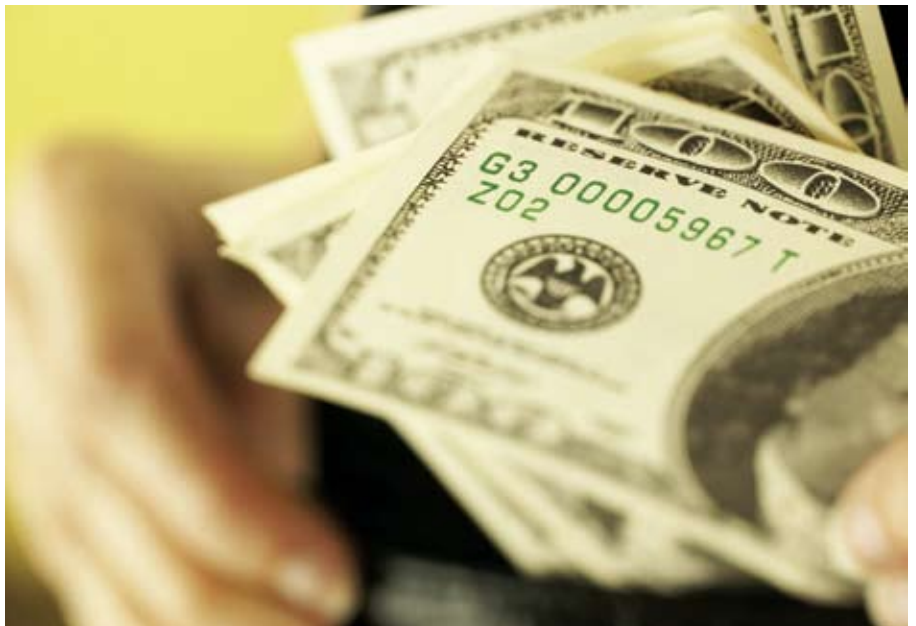
The arbitration panel determined that Employers and HCC had intended the reinsurance treaty to apply to ULM. Therefore, it concluded that Employers was precluded from recovering against either HCC or ULM. HCC and ULM moved to have the award confirmed by the court. The Northern District of Texas, however, vacated the award. It held that under the law of the case doctrine, the arbitration panel was precluded from revisiting an issue already decided by necessary implication through an earlier court decision.

## Reinsurer Is Bound By Cedent's Post-Settlement Single Occurrence Allocation

A reinsurer is bound under the follow-the-fortunes doctrine to the good faith post-settlement allocation of its cedent. See *Travelers Cas. & Sur. Co. v. Gerling Global Reinsurance Corp. of Am.*, No. 03-9220-cv, 2005 U.S. App. LEXIS (2d Cir. Aug. 18, 2005). A cedent provided coverage to Owens Corning Fiberglass ("OCF") that provided both products and completed-operations coverage as well as premises and operations coverage. Both coverages had per-occurrence limits, but the operations coverage had no aggregate limit. OCF distributed and/or manufactured an asbestos product and operated a division that installed, maintained and removed its asbestos product. In connection with thousands of bodily injury claims, OCF exhausted all of the available product limits. OCF then submitted asbestos claims under the premises and operations coverage arguing that the claims arose out of their contracting operations. The cedent argued that it owed no additional coverage because, among other things, all the asbestos claims were a single occurrence and it had already paid one ULM set of occurrence limits. The dispute was eventually submitted to an arbitration panel, but the parties settled before the panel issued its decision.

The cedent's settlement with OCF "explicitly disclaimed any particular theory of coverage," and the parties never agreed on the number of occurrences. After the settlement, the cedent allocated the settlement amount among the triggered policies on a one-occurrence basis, using a "rising bathtub" methodology, allocating equal amounts to each triggered year. This allocation quickly exhausted the primary policies, and additional amounts were allocated to the excess policies in the same manner. The cedent had reinsurance for the

excess policies, but apparently not for the primary policies. The reinsurer for specific portions of the 1975-77 excess policies refused to pay the portion of the OCF settlement allocated to its five facultative certificates based on the allocation method used by the cedent. Specifically, the reinsurer argued that in agreeing to settle with OCF the cedent had implicitly agreed to OCF's multiple occurrence position.



The Second Circuit rejected the reinsurer's argument and ruled that the follow-the-fortunes doctrine applied to the allocation decision. The reinsurer, therefore, was bound by that allocation so long as it was made in good faith, was reasonable and was within the applicable policies. The court's decision was based in large part on *North River Insurance Co. v. ACE American Reinsurance Co.*, 361 F.3d 134 (2d Cir. 2004), whose facts were so similar as to be "striking and ultimately decisive."

North River also involved a cedent's post-settlement allocation of OCF non-products asbestos claims and the reinsurer's denial based on the one occurrence, rising bathtub allocation. There, the court applied the follow-the-fortunes doctrine to a cedent's post-settlement allocation decisions. Applying *North River*, the court ruled that they would not "authorize an inquiry into the propriety of a cedent's

method of allocating a settlement if the settlement itself was in good faith, reasonable, and within the terms of the policies."

The reinsurer tried to avoid this result by arguing that the allocation was made in bad faith, did not fall within the terms of the policy and was unreasonable. The court rejected all these arguments and held that the reinsurer was required to pay its allocated portion of the cedent's settlement with OCF.

## Certificates Requiring Arbitration Supercede Binders Not Requiring Arbitration

A federal court in Washington State has ruled that reinsurance certificates containing an arbitration provision supercede reinsurance binders that do not contain an arbitration provision. See *King County v. Swiss Reinsurance Am.*, No. C05-783Z (W.D. Wash. Aug. 31, 2005). Two reinsurers had issued binders to King County for the county's self-insurance program. The binders contained a number of specific terms, but did not include any provisions requiring disputes to be arbitrated. Subsequently, reinsurance certificates containing additional provisions, including arbitration provisions, were sent by both reinsurers to the county. The county contended that when it received the certificates, it did not read them and the arbitration provisions were not binding because it never agreed to them. The court rejected the county's argument. It held that binders are not intended to include all the contract terms and that the cedent "must always look to the formal policy subsequently issued for a complete statement of the agreement."

## Federal Court Refuses To Convert Declaratory Judgment Awarded By Arbitration Panel Into Damages Award

An Illinois federal district court refused to modify a declaratory judgment award, made by an arbitration panel, to specify the amount of damages. See *Continental Cas. Co. v. Scandinavian Reinsurance Co.*, No. 05C2349, 2005 U.S. Dist. LEXIS 18995 (N.D. Ill. Aug. 30, 2005). Continental Casualty, the cedent, arbitrated a dispute with its reinsurer, Scandinavian Reinsurance Company, Inc., and the arbitration panel found in favor of Continental Casualty, awarding it declaratory judgment. But the panel held that the specific amount of damages should be determined by the parties based on the award and in consideration of a methodology used by Continental to recast amounts due from Scandinavian. Continental asked the arbitration panel to clarify the award and confirm the amounts specifically due. The panel refused, holding that to do so would modify and not clarify its previous award. Subsequently, Continental brought suit to confirm the arbitration award and moved the court for a monetary judgment. The Northern District of Illinois refused to enter a specific monetary award, holding that to do so would be to improperly modify the arbitration panel's award, which required the parties to make the determination.

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